

February 3, 2023

## New tax proposal drags life insurance....

**Announcement:** The government has proposed to lift tax exemption on income from life insurance policies with premium over and above ₹ 5 lakh in a year (only non-linked i.e. par and non-par policies). Notably, annuities and unit linked (annual premium of ₹ 2.5 lakh) are already been taxed.

The new proposal aims to bring traditional policies under the tax net with proceeds pertaining to incremental aggregate contributions above threshold. Under the proposal, payouts related to contribution in excess of threshold will be taxed. However, tax exemption of section 10(10D) is proposed to be continued for proceeds upon death. The new taxation is considering aggregate contribution including all non-linked insurance policies, thus removing any escape through splitting across low ticket policies.

### Management commentary:

- According to media reports, HDFC Life is likely to witness an impact of 10-12% on topline and 5% on profits due to changes proposed in Budget
- As per exchange filing, SBI Life said that annualised premium equivalent (APE) product mix was well diversified at 56.4% unit linked, 27.4% non-unit linked, 10.1% protection, 2.8% annuity and 3.3% group funds. Share of business of non-unit linked policies with annual premium of above ₹ 5 lakh is < 2% of total APE for 9MFY23
- As per exchange filing, ICICI Pru said that APE product mix was well diversified at 41.4% unit linked, 19.7% protection, 6.3% annuity, 4.0% group funds and 28.6%. Share of business of non-unit linked policies with annual premium of above ₹ 5 lakh is ~6% of total APE for 9MFY23
- As per exchange filing, Max Life indicated a well-diversified product mix across products and customer segments with share of non-unit linked policies with annual premium of above ₹ 5 lakh at ~9% of individual APE for 9MFY23 and ~6% for FY22 with impact on VNB anticipated to be lower

### Factors not in favour:

- Removal of tax exemption on high contribution on traditional plans is seen impacting the wallet share of HNI customer
- Further, steps towards new tax regime without exemptions remain an overhang for long term growth prospects

### Factors in favour:

- Large population base with lower insurance penetration and density, which enables to sustain long term growth
- Bringing large ticket traditional insurance policies under tax net remains a drag. However, from a customer's perspective other investment avenues are taxable, thus providing no differential benefit
- Large product suite with innovation and product along with strategy restructuring to minimise the adverse impact

**Impact:** In our view, on an industry basis, the new proposal will impact non-linked saving segment (par, non-par products), which contributes ~30-60% of APE and value of new business (VNB). An assumption of ~20% lower than estimate premium accretion is seen impacting APE by ~6-14%, though the impact is varied across players. A higher impact is expected for players with higher contribution of non-linked business (HDFC Life and Max Financial) followed by SBI Life and ICICI Prudential Life insurance. Though steps undertaken by insurers are to be seen ahead, the recent correction in stocks seems to have factored in the negatives and offer an investment opportunity.

### Target revision

Companies	CMP	Target Price	Rating
HDFC Life	483	540	HOLD
SBI Life	1,105	1,300	BUY

### Key highlights

- *New proposal to be applicable for policies issued on or after April 1, 2023*
- *HDFC Life is likely to witness an impact of 10-12% on topline and 5% on profits*
- *ICICI Pru's share of non-unit linked policies with annual premium of above ₹ 5 lakh is ~6% of total APE*
- *SBI Life's share of non-unit linked policies with annual premium of above ₹ 5 lakh is < 2% of total APE for 9MFY23*

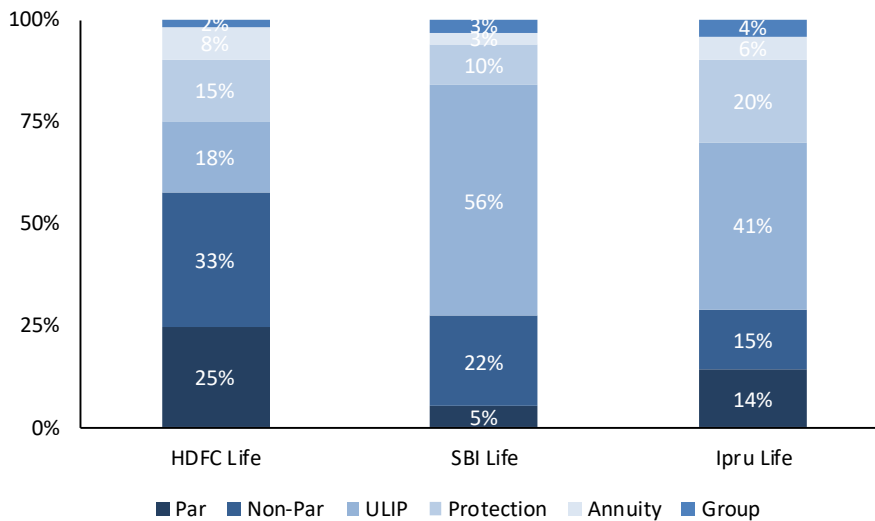
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Exhibit 1: Player wise product mix based on APE (as of December 2022)



Source: Company, ICICI Direct Research

## HDFC Life

### Near term challenges:

- Impact of proposed change in Budget to bring proceeds from maturity of traditional insurance policies of an assess with aggregate annual premium contribution of ₹ 5 lakh and above under tax net. According to media reports, HDFC Life is likely to witness an impact of 10-12% on topline and 5% on profits due to changes proposed in Budget
- Moderation seen in protection business in recent quarters with a gradual pick-up anticipated ahead
- Clarity with regards to parent's stake post-merger
- Gradual pick-up in acquired business (Exide) with integration undertaken

### Long term benefit:

- Large population base with lower insurance penetration and density, which enables to sustain long term growth
- Historically proven ability in terms of faster adaptability and large product suite and strong distribution strength

Factoring in near term challenges and anticipated reduction in APE and VNB, we downgrade our rating from BUY to HOLD and revise our target price from ₹ 690 to ₹ 540, valuing the stock at 2.2x FY25E EV.

Exhibit 2: Change in estimates

(₹ Crore)	FY23E			FY24E			FY25E		
	Old	New	% Change	Old	New	% Change	Old	New	% Change
Premiums earned - Net	54,661	54,661	0.0	65,528	62,406	-4.8	78,721	73,999	-6.0
EV	38,376	38,376	0.0	46,046	44,702	-2.9	56,047	53,086	-5.3
EV/Share	182	182	-0.2	218	212	-2.9	265	251	-5.1
P/IEV	3.2	2.7	-15.2	2.7	2.3	-13.7	2.2	2.0	-10.8

Source: Company, ICICI Direct Research

## SBI Life Insurance

### Near term challenges:

- Impact of proposed change in Budget to bring proceeds from maturity of traditional insurance policies of an assessee with aggregate annual premium contribution of ₹ 5 lakh and above under tax net
- Steps towards new tax regime without exemptions remain an overhang for long term growth prospects

### Long term benefit:

- Large population base with lower insurance penetration and density, which enables to sustain long term growth
- Higher proportion of unit linked and lower ticket size business provides relative advantage
- Continued traction in non-par business and gradual pick up in protection premium coupled with strong physical and digital distribution

Factoring in near term challenges we revise our target price from ₹ 1500 to ₹ 1300, valuing the stock at 2.2x FY25E EV. However, SBI Life seems to be relatively better placed with valuation comfort given recent correction in the stock. Thus, we remain positive on the stock and maintain our BUY rating on the stock.

### Exhibit 3: Change in estimates

(₹ Crore)	FY23E			FY24E			FY25E		
	Old	New	% Change	Old	New	% Change	Old	New	% Change
Premiums earned - Net	69,536	69,536	0.0	82,679	81,182	-1.8	98,666	96,182	-2.5
EV	45,194	45,194	0.0	52,162	51,711	-0.9	60,368	59,340	-1.7
EV/Share	452	452	0.0	522	517	-0.9	604	593	-1.8
P/IEV	2.9	2.9	-1.2	2.5	2.5	0.2	2.1	2.2	3.9

Source: Company, ICICI Direct Research

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Buy: > 15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: < -15%



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