

CMP: ₹600

Target: ₹ 700 (17%)

Target Period: 12 months

BUY

May 2, 2023

Steady Q4; strong guidance remains encouraging...

About the stock: Star Health is the largest standalone insurer engaged in the health insurance segment with relatively superior market share, operating performance.

- Star Health is a market leader in the retail health insurance segment with ~34% market share as of March 2023
- Star Health has 835 branches and 14200+ network hospitals, with a presence in 25 states and five union territories

Q4FY23 Results: Premium growth remains healthy.

- GWP up 13.8% YoY to ₹ 4199 crore, NWP up 15.0% & NEP up 11.1% YoY
- Incurred claims flat YoY, QoQ. Claims ratio was at 65%
- Combined ratio within guidance at 95.3%; underwriting loss at ₹ 65 crore
- Net profit was at ₹ 102 crore vs. a loss of ₹ 122 crore YoY

What should investors do? Star Health is expected to maintain its leadership in the retail health segment with sustainable long term growth opportunity. Higher than industry growth and targeted improvement in combined ratio provides confidence.

- We maintain **BUY** rating on the stock

Target Price and Valuation: Given levers for improvement in RoE – strengthening of distribution channels through banca tie-up, focus on profitable growth, elevated yields and issuance of Esop at market price, we remain positive on the fundamental strength. Thus, we assign a multiple of 2x on FY25E GDPI and arrive at a revised target price of ₹ 700 from ₹ 650 earlier.

Key triggers for future price performance:

- Price hikes, increasing proportion of specialised products to keep premium growth ahead of industry thereby enabling market share leadership
- Improving footprints in rural India, increase in bancassurance tie-up along with strengthening of own agency channel to propel business momentum
- Strong distribution (agency and banca tie-up), hospital network and claim management to act as moats aiding profitable growth momentum
- Expansion of hospital tie-ups, faster claim settlement to keep claim ratio at 62-65%. Focus on efficiency to further improve combined ratio ahead
- Elevated yields and issuance of new Esop at market price to further aid RoE

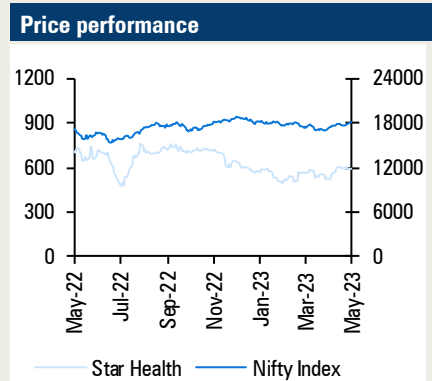
Alternate Stock Idea: Apart from Star Health, we like SBI Life Insurance.

- It is among the most dominant players in the Indian life insurance industry
- BUY with a target price of ₹ 1350



Particulars	
Particulars	Amount
Market Capitalisation	₹ 35408 crore
52 week H/L	780/451
Net Worth	₹ 5430 crore
Face Value	₹ 10

Shareholding Pattern					
(in %)	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Promoter	58.9	58.8	58.6	58.3	58.3
FII	9.8	9.6	10.3	35.5	35.2
DII	27.3	27.2	1.5	1.3	1.4
Others	4.02	4.34	29.60	4.94	5.03



- ### Key Highlights
- Combined ratio healthy at 91.3% in Q4FY23
 - Key risk:** i) Anticipated introduction of composite license remains an overhang ii) Uptick in claim ratio

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Key Financial Summary

	FY20	FY21	FY22	FY23	3 year CAGR (FY20-FY23)	FY24E	FY25E	2 year CAGR (FY23-FY25E)
Gross written premium (GWP)	6890.7	9388.5	11462.3	12950.9	23.4	16052.3	19262.8	22.0
Net Incurred Claims	3087.4	4369.5	8540.0	7320.4	33.3	9352.0	10970.6	22.4
Underwriting Profit/Loss	168.4	(1331.8)	(2061.6)	204.7		529.4	677.5	
Profit after Tax	272.0	(825.6)	(1040.7)	618.6		841.1	1038.0	
NWP/Net Worth (x)	3.2	1.7	1.7	1.9		1.5	1.6	
Price/Float (x)	0.8	0.5	3.3	2.6		1.9	1.7	
P/GWP (x)	5.1	3.7	3.0	2.7		2.2	1.8	
P/E (x)	128.0	(42.2)	(28.9)	48.4		42.6	34.6	

Key takeaways of recent quarter & conference call highlights

Q4FY23 Results: Mixed set of numbers; premium growth remains healthy. market share remains buoyant

- Star Health reported mixed numbers on the business growth front. Gross written premium (GWP) registered healthy growth of 13.8% YoY, 35.6% QoQ at ₹ 4199 crore
- Continued focus on retail health segment led to 100 bps YoY improvement in market share (FY23) to 34%
- Net written premium (NWP) was up 15% YoY while earned premium growth was at 11% YoY to ₹ 2912 crore
- Incurred claims were largely steady at ₹ 1805 crore but claims ratio (adjusted) in FY23 were at 64.6% vs. 65.8% in FY22. Net commission expense was up 10.6% YoY while other operating expenses grew higher at 11.8% YoY. The management expense ratio declined from 30.3% in Q4FY22 to 29.3% in Q4FY23
- Combined ratio witnessed an improvement at 95.3% (remain in the guided range) vs. 117.9% a year ago. Despite that, the company reported, underwriting loss of ₹ 64.8 crore. On account of lower net earned premium and lower investment income, it posted net profit of ₹ 102 crore (lower than our estimate) vs. ₹ 241 crore in Q3FY23 (vs. loss of ₹ 82 crore in Q4FY22)

Q4FY23 Earnings Conference Call highlights

- In Q4FY23, health insurance industry premium (including PA) grew 25.4%, driven largely by 28% growth in Group Health and 16% growth in Retail Health
- Star Health recorded ~25% growth in premium in April 2023 with claim ratio being lower YoY. Growth is heterogeneous from all lines of business – retail as well as group
- For FY23, Star Health's retail health premium grew at ~18% vs. industry's retail health growth of 15.3%. Market share in the retail health segment increased from 33% in FY22 to 34% in FY23
- The management aims to grow premium at a higher than industry rate thereby further increasing retail health market share. Growth in FY24E could be driven by value (55-60%) and volume (40-45%). Share of the group segment to increase to 10% of overall premium. Focus on profitable growth to keep loss ratios in the guidance range
- Average sum assured of new policies has increased by 13% to ~₹ 9 lakh per policy. Policies with ₹ 5 lakh sum insured and above constitute 70% of portfolio vs. 64% in FY22
- Premium from benefit products has grown by 53% in FY23 with proportion in overall GWP increasing by 62 bps YoY to 2.3% in FY23
- Launched two new products in Q4FY23 - Star Special Care Gold and Star Group Health Benefit Plus. Special Care Gold is a product tailored specifically for individuals with disabilities and those who are HIV-positive. Star Group Health Benefit plan offers critical illness cover up to 54 critical illnesses, personal accident cover, hospital cash cover an EMI protect due to hospitalisation. It also covers health indemnity & health indemnity top-up
- Contribution from the agency channel was at 82% with net addition of 76000 agents in FY23 (total agent count at 625860). Tie up with corporates and banca channel picking up with contribution growing at 43% in FY23
- Digital sourcing from web and tele sales models has grown 28% YoY in FY23 to ₹ 625 crore
- Tie up achieved with leading banks - Standard Chartered Bank, India Post Bank and ESAF Small Finance Banks for distribution of Star Health products through their platforms
- Cashless claim settlement for 73% of claims by volume (63% in FY22) and 80% by value (71% in FY22)
- Anti-fraud digital initiatives are operational and provided ~1.3% benefit in claim ratio in FY23, which is well in-line with guidance of ~1% benefit to be achieved
- Expense ratio fell to 30.3% in FY23 vs. 30.8% in FY22 on account of efficient cost control and management. Claims ratio improved from 87.1% in FY22

to 65% in FY23 (includes 0.4% impact of Covid claims). Thus, combined ratio improved from 117.9% in FY22 to 95.3% in FY23. For Q4FY23, the opex ratio has improved to 29.4% vs. 30.3% in Q4FY22 despite lower group business

- Currently, 4.1% of portfolio is invested in ETFs, which is planned to increase up to 7%. With a rise in interest rates and deployment of fresh investments at higher yield, portfolio yield increased from 6.71% in Q4FY22 to 7.34% in Q4FY23
- The management aims to continue improvement in combined ratio in FY24E
- New Esop will be issued at market price with no substantial impact on P&L
- Growth in retail health business at 18% in FY23 - split equally between volume and value
- Total ~2.5% of policies are long term plans i.e. plans for more than one year. Star Health aims to focus on increasing proportion of long term policies ahead
- Management is targeting RoE at 15-16% in FY23 driven by price hike, growth and end to Esop expense. RoE in FY22 at 12.5% includes impact of Esop expense
- With implementation of IFRS, wherein cost is deferred over the policy period, positive impact of 300-400 bps could be seen on RoE

Peer comparison

Exhibit 1: ICICI Direct coverage universe (BFSI)

Sector / Company	CMP		M Cap	EPS (₹)				P/E (x)				P/EV (x)			RoE (%)					
	(₹)	TP(₹)		Rating	(₹ bn)	FY22	FY23	FY24E	FY25E	FY22	FY23	FY24E	FY25E	FY22	FY23	FY24E	FY25E			
SBI Life Insurance	1149	1350	Buy	114	15.1	17.2	18.6	21.3	76.3	66.8	61.8	54.1	2.9	2.5	2.2	2.0	8.5	10.8	16.2	15.9
HDFC Life	543	570	Hold	116	5.7	6.4	7.3	8.7	95.0	84.7	74.4	62.2	3.8	3.0	2.5	2.1	18.0	18.1	18.2	18.2
Star Health	600	700	Buy	354	-21.0	12.6	14.3	17.6	-28.6	47.8	42.1	34.1	7.9	4.7	3.4	3.0	-27.8	9.9	8.1	8.9
ICICI Lombard	1086	1250	Hold	533	38.4	38.4	38.4	47.0	28.3	28.3	28.3	23.1	4.4	4.4	4.4	3.8	15.5	15.5	15.5	16.4

Source: Company, ICICI Direct Research

Exhibit 2: Variance Analysis

Policyholder's Account	Q4FY23	Q4FY23E	Q4FY22	YoY%	Q3FY23	QoQ%	
Gross Premium Written	4199.2	3263.3	3689.2	13.8	3096.7	35.6	Retail health market share remained buoyant at 34%
(-) Reinsurance ceded	206.0	195.8	215.4	(4.3)	153.3	34.4	
Net written premium (NWP)	3993.2	3067.5	3473.8	15.0	2943.4	35.7	
Net earned premium (NEP)	2912.5	2914.2	2621.2	11.1	2867.2	1.6	
(-) Net Incurred Claims	1805.4	1865.7	1784.8	1.2	1827.8	(1.2)	Claim ratio improved at 62%
(-) Net Commission Expense	561.2	507.6	507.2	10.6	402.6	39.4	Commission ratio up at 14.1%
(-) Operating expenses related to insurance business	610.7	662.0	546.4	11.8	511.0	19.5	
(-) Total expense	2977.3	2697.7	3105.7	(4.1)	3072.0	(3.1)	
Underwriting Profit/Loss	(64.8)	(26.2)	(217.2)	(70.2)	125.8	NA	Combined ratio improved at 91.4%
Investment Income	115.7	11.9	4.0	2791.1	13.6	753.4	Higher yield benefited investment income
Operating Profit/Loss	75.7	153.8	(156.6)	(148.3)	331.2	(77.1)	
Transfer to Shareholder's Account	75.7	153.8	(156.6)	(148.3)	331.2	(77.1)	

Shareholder's Account	Q4FY23	Q4FY23E	Q4FY22	YoY%	Q3FY23	QoQ%	
Operating Profit/Loss	75.7	153.8	(156.6)	(148.3)	331.2	(77.1)	
Investment Income	77.7	61.2	20.6	276.9	69.8	11.2	
Other Income	1.33	1.50	1.17	13.7	1.73	(23.1)	
Profit before tax	136.7	155.3	(155.4)	(187.9)	332.9	(58.9)	
(-) Provision for Taxation	34.3	39.6	33.7	1.6	(71.3)	(148.1)	
Profit after Tax	102.4	115.7	(121.7)	(184.2)	261.6	(60.9)	High opex partially offset premium accretion

Source: Company, ICICI Direct Research

Exhibit 3: Change in estimates

	FY24E			FY25E		
	Old	New	% change	Old	New	% change
Gross written premium (GWP)	16052.3	16052.3	0.0%	19262.8	19262.8	0.0%
Net earned premium (NEP)	13958.3	13958.3	0.0%	16622.2	16622.2	0.0%
Net Incurred Claims	9352.0	9352.0	0.0%	10970.6	10970.6	0.0%
Underwriting Profit/Loss	529.4	529.4	0.0%	677.5	677.5	0.0%
Operating Profit/Loss	1194.8	1194.8	0.0%	1584.8	1584.8	0.0%
Profit after Tax	841.1	841.1	0.0%	1038.0	1038.0	0.0%

Source: Company, ICICI Direct Research

Exhibit 4: Assumption

	Current		Earlier	
	FY24E	FY25E	FY24E	FY25E
NWP growth (%)	22.5	20.0	22.5	20.0
NEP growth (%)	19.9	19.1	19.9	19.1
Claims ratio (%)	67.0	66.0	67.0	66.0
Commission ratio (%)	12.5	12.5	12.5	12.5
Expenses ratio (%)	16.7	18.0	16.7	18.0
Combined ratio (%)	96.2	96.5	96.2	96.5
Underwriting Profit (%)	0.8	0.1	0.8	0.1
EBIT/NEP (%)	8.1	8.3	8.1	8.3

Source: Company, ICICI Direct Research

Financial summary

Exhibit 5: Policy holder's Account				
	₹ crore			
Policyholder's Account	FY22	FY23	FY24E	FY25E
Gross written premium (GWP)	11462.3	12950.9	16052.3	19262.8
(-) Reinsurance ceded	1.1	-	802.6	963.1
Net written premium (NWP)	10809.5	12319.6	15249.7	18299.7
Net earned premium (NEP)	9809.2	11261.6	13958.3	16622.2
(-) Net Incurred Claims	8540.0	7320.4	9352.0	10970.6
(-) Net Commission Expense	1492.2	1682.8	1906.2	2287.5
(-) Operating expense	1838.5	2053.8	2170.7	2686.6
(-) Other expense	0.0	0.0	0.0	0.0
(-) Total expense	3330.7	3736.6	13428.9	15944.7
Underwriting Profit/Loss	(2061.6)	204.7	529.4	677.5
Investment Income	479.6	501.4	665.4	907.3
Operating Profit/Loss	(1582.0)	706.1	1194.8	1584.8
Transfer to Shareholder's Account	(1582.0)	706.1	1194.8	1584.8

Source: Company, ICICI Direct Research

Exhibit 6: Balance sheet				
	₹ crore			
Balance Sheet	FY22	FY23	FY24E	FY25E
Source of Funds				
Share Capital	575.5	581.7	575.9	575.9
Reserves and Surplus	5793.7	5983.9	9814.7	11064.1
Net Worth	6369.3	6565.6	10390.6	11640.0
Fair value gains	26.7	23.4	36.8	65.3
Borrowings	7200.0	4700.0	470.0	470.0
Deferred Tax Liability	0.0	0.0	0.0	0.0
Total	7115.9	7057.9	10897.4	12175.3
Application of Funds				
Shareholder Investments	4493.9	5345.9	6373.8	7422.1
Policyholder Investments	6879.6	8046.2	11837.0	13783.9
Total Investments	11373.4	13392.1	18210.8	21206.1
Deferred Tax Assets	776.7	568.9	299.9	95.0
Fixed Assets	117.1	111.3	258.3	218.2
Cash and Bank balance	563.6	309.4	1535.4	1828.4
Other current assets	683.2	844.4	933.3	1148.2
Total Current Assets	2140.6	1834.0	2468.7	2976.6
Current Liabilities	1961.2	2030.1	1930.8	2233.7
Provision	6202.2	7268.7	8409.5	10086.9
Total Current Liabilities	8163.3	9298.8	10340.3	12320.6
Net Current Assets	(6916.5)	(8145.1)	(7871.5)	(9344.0)
Total	7115.9	7057.9	10897.4	12175.3

Source: Company, ICICI Direct Research

Exhibit 7: Shareholder's Account				
	₹ crore			
Shareholder's Account	FY22	FY23	FY24E	FY25E
Operating Profit (from Policyholder's a/c)	(1582.0)	706.1	1194.8	1584.8
Investment Income	313.3	338.8	358.3	488.6
Other Income	0.8	0.0	0.4	0.4
(-) Expense and Provision	1336.0	218.5	429.4	686.7
Profit before tax	(1396.7)	826.4	1124.1	1387.1
Provision for Taxation	(356.0)	207.8	(282.9)	(349.1)
Profit after Tax	(1040.7)	618.6	841.1	1038.0

Source: Company, ICICI Direct Research

Exhibit 8: Key Ratios				
Key Ratios	FY22	FY23	FY24E	FY25E
Incurred Claims ratio (%)	88.0	66.4	67.0	66.0
Commission Ratio (%)	13.3	13.0	12.5	12.5
Expense Ratio (%)	17.3	16.5	16.7	18.0
Combined ratio (%)	118.6	95.9	96.2	96.5
Investment yield (%)	9.6	7.5	7.8	7.9
Investment Income / NEP (%)	6.4	6.3	7.2	8.3
PAT margin (%)	(12.1)	6.2	6.0	6.2
RoE (%)	(27.8)	9.9	8.1	8.9
ROCE (%)	(23.9)	9.3	7.7	8.5
NWP/Net Worth (x)	1.7	1.9	1.5	1.6
Debt/EBIT (x)	(0.5)	0.5	0.4	0.3
Debt/Equity (x)	0.12	0.06	0.05	0.04
ABV (₹)	75.5	126.5	176.6	198.1
Valuation				
Price/Float (x)	3.3	2.6	1.9	1.7
P/GWP (x)	3.0	2.7	2.2	1.8
P/E (x)	(28.9)	48.4	42.6	34.6
P/ABV (x)	8.1	4.8	3.4	3.1

Source: Company, ICICI Direct Research

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