ICICI Prudential Life Insurance Company

Earnings conference call – Quarter ended December 31, 2018

(9M-FY2019)

January 22, 2018

NS Kannan:

Good evening and welcome to the results call of ICICI Prudential Life Insurance Company for 9M-FY2019.

I have with me here: Puneet Nanda, Deputy Managing Director and Satyan Jambunathan, CFO. We will walk you through the developments during the quarter as well as the presentation on the performance for 9M-FY2019. We have put up the results presentation on our website. You can refer to it as we walk you through the performance.

At the outset, as we had informed the stock exchanges, Ms. Vibha Paul Rishi has been appointed as an Independent director of the Company from January 1, 2019. She is a marketing expert and her competencies includes product rebranding and launch, entering new international markets, strategic planning and human resources. She has been in leadership roles across areas of marketing, with entities such as PepsiCo for 17 years and Tata Administrative Service - as a part of its start-up team of Titan Watches. She currently serves on the boards of various companies including Asian Paints, Tata Chemicals, Indian Hotels, Philips Lighting India and Escorts Limited and has been a director of PNB Metlife Insurance. She has also been an executive director of Max India in the past.

I will now highlight our performance for 9M-FY2019 along with our key strategic imperatives. Thereafter, Satyan will discuss the performance in greater detail. At the end, Puneet, Satyan and I will be happy to take any questions you may have.

Strategy & performance

Our primary focus continues to be to grow the absolute Value of New Business (VNB) while ensuring that our customer is at the core of everything we do. We have previously highlighted the strategic elements in the form of 4P's, namely, premium growth, protection, persistency and productivity improvement; and we believe that these 4 P's continue to be core to the path of delivering our objective of VNB growth.

The first "P" of "Premium growth"

Before we discuss our growth during the quarter, I would like to give you some context. The average annual premium of our business for FY2018 was ~ ₹ 90 thousand and for the unit linked segment it was ~₹180 thousand. On the back of our customer centric product portfolio, simplified on-boarding process and macro factors, we were able to penetrate the affluent segment quite well and establish our strength in that segment.

During the quarter, there were multiple concerns around macro factors both on the international and the domestic front such as high prices of crude oil, tariff wars, certain corporates and the Indian NBFC sector. All of these created conditions for weak sentiments and volatility in the capital markets, particularly in the equity market. This impact was seen in the behaviour of affluent customers who seem to have deferred investment decisions during the period.

At the same time, we identified the need to also focus on pools of opportunity in the form of customer segments other than just the affluent segment. During this quarter, we took significant steps to extend our distribution into these other customer segments while simultaneously working on protecting our strength in the affluent segment. We believe that broadening the customer base is necessary for long term sustainable growth.

Our Annualized premium equivalent (APE) for Q3-FY2019 declined by ~2% year on year, as against the H1-FY2019 decline of ~5%. For 9M-FY2019, the APE declined by ~4% year on year. While we began the quarter with a decline of ~12% for October, the month of December saw a growth of 3% year on year. As we go into the seasonally peak quarter, it would be important for us to carry this momentum forward.

For 9M-FY2019, we had a market share of 10.8% based on retail weighted received premium (RWRP).

The second "P" of "Protection focus"

While we saw some challenges on the growth of the savings business, the protection business continued to grow during the quarter. For 9M-FY2019, our protection APE grew ~100% year on year. This growth was led by both retail and group protection business. The growth of group protection business is an outcome of our focus on building partnerships over the past two years.

As a part of our protection strategy, we have also partnered with CNBC-TV18 in the Mission Insure India campaign, which is a thought leadership initiative to highlight the need of insurance cover for consumers.

The third "P" of "Persistency improvement"

We believe customer retention is probably the most effective indicator of the quality of sale and is a barometer of customer experience. During this year, we continued our efforts in this direction which resulted in ~13% growth of total premium and ~19% growth of retail renewal premium on a year on year basis. With the exception of the 13th month, persistency at other durations has improved compared to the same time last year. During 9M-FY2019 our retail linked surrenders have reduced by ~30% as compared to the corresponding period last year. I would like to re-iterate that our persistency and surrender experience continues to be well within the assumptions in our VNB and Embedded Value calculations.

The fourth "P" of "Productivity gains reflecting in reduced cost ratios"

Technology and process re-engineering have been at the centre of our efforts to improve expense ratios. Continuing this journey, we are the first life insurance company in India to have direct integration with WhatsApp for a verified business account. We have also launched an Artificial Intelligence powered instant Optical Character Reader for instant classification and verification of documents.

While our overall expense ratios for the savings business was flat on account of the robust renewal premium growth, the decline in our new business has meant that our new business cost ratios have somewhat worsened this year.

VNB growth: Outcome of strategic elements

The outcome of our focus on these 4 Ps has resulted in our Value of New Business for 9M-FY2019 of ₹ 9.10 billion, compared to ₹ 7.67 billion for the same period last year.

The VNB margin for 9M-FY2019 is 17.0% as compared to 16.5% for FY2018 and 17.5% for H1-FY2019. The current margin is lower than the margin declared in H1-FY2019 of 17.5%, only on account of revised forecast of new business expense ratio keeping in mind the lower growth seen in Q3.

I would like to conclude with my view for the coming quarter.

With respect to our savings line of business, we will look to protect our strong position in the affluent segment while continuing to extend our distribution into other segments to improve the long term sustainability of the business. As we enter the seasonally peak quarter, our performance will determine the full year growth as well.

At the same time, we will continue the thrust on building the protection proposition and to deliver growth in that segment.

With this, I thank you for your attention and now hand over to Satyan to discuss the results in greater detail.

Satyan Jambunathan: Thank you Kannan. Good evening. I will now go into greater detail on the elements of the Company's performance.

As mentioned earlier, our focus is to grow the absolute Value of New Business (VNB) while ensuring that our customer is at the core of everything we do. In doing so, we believe in a long term strategy focused on retail business through our multi-channel distribution, customer centric products and relentless effort to deliver superior business quality; with technology as a business enabler in each of these aspects.

Premium growth

The retail segment contribution continues to be significant at ~ 95% of new business APE for 9M-FY2019. Out of the overall AUM of ~ ₹ 1.50 trillion, the retail AUM of ₹ 1.34 trillion constitutes more than 89% and this share has continued to be strong during the year.

As Kannan mentioned, within the retail business, our immediate focus is to broaden our customer base in other segments while protecting our strength in the affluent customer segment. One of the initiatives we took during the quarter was to encourage regular monthly savings, similar to what is seen in other savings instruments. The monthly premium option allows customers to pay premiums through the year. The relatively higher mix of monthly premium business in our portfolio has resulted in some difference between the retail weighted received premium (RWRP), and annualised premium equivalent (APE). As you can see on slide 14, the difference is evident from the month-wise APE numbers already disclosed.

Customer centric products

Customer centricity continues to be at the core of our product strategy. In the savings segment, unit linked products offer transparency, lower cost and minimal persistency risk to the customer. They can compete effectively across the wider financial savings space in both offline and online environments. In protection products, benefits are paid only on mortality/morbidity events and typically there is no maturity or surrender value. For 9M-FY2019, unit linked products continued to be our mainstay category in savings and the protection mix stood at 8.6% of APE.

Multi-channel distribution

We have invested across various distribution channels such as agency, bancassurance partnerships, proprietary sales force, corporate agents and brokers including web aggregators. For 9M-FY2019, non-promoter channels have contributed ~47% of our APE, providing us with diversification in the distribution mix. During Q3-FY2019, bancassurance APE grew by ~4%. The growth in group business APE has been driven by protection products.

Protection

With rising affluence of Indian families and their aspirations for a better standard of living, the need to protect their dependents from losing their family income is on the rise. This need is further accentuated by the trend of nuclear families becoming the norm. Further, to fuel the aspirations, people are taking more loans and liabilities, thereby exposing themselves and their families to financial risks. It is in this context that our approach of providing products and solutions to meet this need of the customer sharpens our focus on this business segment.

During 9M-FY2019, our protection APE grew ~100%, with the mix of protection at 8.6% of APE. When we look at number of policies, ~43% of retail new business policies came from protection products for 9M-FY2019. New business sum assured for 9M-FY2019 grew by ~39% over the corresponding period last year. We continue to focus on the three segments of protection i.e. Individual life/health, Credit cover and Group life. All protection segments including retail protection have witnessed significant growth during 9M-FY2019.

Persistency

While sales effort is normally directed towards acquisition of customers, it is the retention of these customers that delivers the full intended benefit to the customer and profitability to the Company.

To reiterate, we continue to exclude group premium and single premium in the calculation of persistency. 13th month persistency of 84.1% for 8M-FY2019 is lower as compared to 9M-FY2018. This decline is more in the higher premium segment. In the recent past, with weak sentiments dominating the market and institutional fund managers' performance lagging the market, confidence of the affluent customers has been somewhat impacted, as can be observed from the persistency trend for that segment. Persistency at other durations has improved compared to the same time last year. We would like to highlight that our persistency rates continues to be one of the best in industry and are better than the assumptions used in the VNB and EV.

As on date, the 13th month persistency for the same group of policies has improved from 84.1% to 84.8% with the current month also being used to drive renewal collection. We continue to focus on building the confidence of our policyholders and encourage them to pay the renewal premiums.

Beyond the premium payment term, containing surrenders are key and retail linked surrenders have reduced by 30% as compared to the corresponding period last year.

Our retail renewal premium grew by ~19%, with ~64% of renewal premium received through electronic mediums.

Productivity

Improving productivity of all parts of the organisation from sales to service to support has resulted in our cost ratios coming down over the years. As we redouble our focus on protection, we are also conscious that we will have to invest in this segment resulting in some increase in cost ratios.

Our cost to TWRP ratio was 15.4% for the nine months as compared to 14.0% for corresponding period last year. The increase in ratios is also on account of investments made in growing the protection business. We have discussed before that cost ratio for protection products is significantly higher than saving products while it is margin accretive.

As mentioned by Kannan, the improvement in expense ratio is a result of growth in retail renewal premium while there has been increase in the new business expense ratio.

As you are aware, during the year, each quarter we compute the VNB based on projected costs for the year, which at the end of the year are the actual costs for the year. As we progress during the year, we have a greater visibility of both the projected costs and the expected new business for the year. Now that we are 9 months into the year, we have revised the cost assumptions upwards to reflect the weakness in new business growth during the last quarter.

The commission ratio continues to be stable on a sequential basis at 5.5%.

Financial update

Overall, Value of New Business for 9M-FY2019 was at ₹ 9.10 billion at a margin of 17.0% compared to the margin of 16.5% for FY2018. The change from the half year margin is on account of the revised forecast of the new business expense ratio. We would like to once again emphasize that the change in margin is not on account of any other parameter but only on account of expense ratio.

The profit after tax for 9M-FY2019 was ₹ 8.79 billion as compared to ₹ 12.79 billion during the same period last year. The drop in PAT is primarily on account of the new business strain arising from the increased protection and annuity business that we have written during the period. Amongst the expense items, you will notice that the most significant increase in expenses has been with respect to advertisement and publicity on a year-on-year basis. This is consistent with what we are seeking to do for protection. Looking at the profit across segments, the drop in profit is explained by a reduction of surplus mainly in the non-par life and annuity segment. Surplus of non-par life and annuity declined on account of higher new business strain resulting from strong growth in both the protection and the annuity business.

Solvency ratio continues to be strong at 224%.

To summarize, we monitor ourselves on the 4P framework of "Premium growth", "Protection business growth", "Persistency improvement" and "Productivity improvement to improve expense ratios". Our performance on these dimensions is what we expect to feed into our VNB growth over time. Value of New Business for the nine months was ₹ 9.10 billion as compared to ₹ 7.67 billion in the same period last year.

Thank you and we are now happy to take any questions that you may have.

Hitesh Gulati: You have mentioned that operating expenses has been revised upwards. So if we look at P&L, which line item should we look at? Is it advertisement and publicity expenses as an indicator, if not the actual number?

Satyan Jambunathan: It is not about a line item of expense, expense growth has not been out of line. The challenge has been that the new business APE has not grown. Therefore, as an outcome, the ratio is expected to worsen this year, which is what we have reflected into the margin forecast.

Hitesh Gulati: : So, if you are saying VNB margin of 17% versus 17.5%, so we are in a way saying that acquisition costs are going to be higher, is that correct?

Satyan Jambunathan: That is correct. So if I were to give you an example, if you look at the employee cost line in the financial statements, you will find that for the nine months of the last year employee cost to new business APE was about 12.8%. While employee cost itself has only grown at about 5% or 6% for this nine months, the employee cost for new business APE for the current nine months actually stands at closer to 14%. So what I am trying to say here is that the cost increase has been in line with normal inflation of wage cost. However, because the new business APE has not grown the ratio has deteriorated. Now that we are nine months into the year we are more able to reflect our forecast of both expenses and APE resulting in the cost ratio being revised upwards for the margin.

NS Kannan: So just to reiterate, we are talking more about upward revision of the cost ratio rather than the cost itself.

Nidhesh Jain: I assume you would have forecast certain growth at end of H1 and end of Q1, and that growth has not played out in Q3, because of which your margin has declined in this quarter. So, had we envisaged growth slowdown at the end of H1 itself, what would have been the H1 like-to-like margin?

Satyan Jambunathan: It will be of a similar order of magnitude. The challenge for us when we were at the end of H1 was, while we had a big decline in Q1, Q2 was starting to show an upward trend, and that is what went into our own expectation of what the year would look like. Q2 for us grew at 6%, Q3 was negative in the context of the 6% growth that we saw in Q2, and that is what has resulted in us revising our estimate. The order of magnitude would have been similar whether we had done it at H1 or we have done it now.

Nidhesh Jain: So probably the margins would have been similar to what we have seen?

Satyan Jambunathan: That is correct.

Nidhesh Jain: Going forward, what is the strategy to revive the growth to 15% as we have been seeing some pressure for last three to four months? In the month of November we focused on monthly SIP’s, but the share of monthly SIP's seems to have reduced in the month of December and 3% growth is not a very good number that we have reported in December.

Puneet Nanda: To give you a context of this, as Kannan mentioned, Q3 has been a pretty challenging quarter from two or three perspectives. One, the overall market environment for a number of reasons has been pretty weak. Compounded by the fact that we have had a significantly disproportionate focus on the more affluent customer segment. The affluent customer segment once they get a little nervous or rattled by the market environment or let's say lack of returns and also advised by their own relationship advisors are choosing to defer investments. We are seeing that across all categories, not just in our business. That is what actually is really hurting us. We are trying to engage as much as possible with the customers, with the distributors who serve the customers to try and explain to them how it is good to stay invested, how it is good to take longer-term calls because our product by definition is longer-term. But while we are doing that, we are also trying to expand the width of both the customer segments as well as the distribution segments in order to actually de-risk ourselves a bit. So, from a scenario where we were very largely focused on the affluent segment, we continue to try and engage them, we are also expanding the reach to more mass and mass affluent segments of customers. Once you go to that segment, obviously the wallet size is smaller, and of that smaller wallet size we hope to get some share. So, as a consequence of that, one of the strategies that we have applied is to look at monthly premium option. We have seen that strategy work well in other savings instruments, so we feel that is something that we can also try. It is something in addition to what we have been doing in order to try and expand and we have seen some early signs of success. I think it has been only two months and it is not enough for us to take a call on whether it is sustainable or not. But what we are very clear is that we will continue to try and diversify both the customer segment as well as distribution segment, in the bargain we have seen a slight month-on-month improvement. But if the strategy plays out, we should hopefully do well, not just in Q4 but from longer-term perspective as well.

Nidhesh Jain: What are we doing in terms of expansion of distribution, both in agency or direct channel, or more penetration in bancassurance?

Puneet Nanda: That is a continuous effort. We have been actively trying to hire more agents. But as you all know, our focus has never been to increase just the number of agents, because our number of agents is already good. Our focus has been on more quality agents, so we continue with that, we continue to work very closely with a number of potential bank partners to try and expand the partnership, we work with a lot of other entities, corporate agents, brokers to try and expand partnerships. So that is a continuous effort, and every quarter we are getting more and more partners which will hopefully expand the distribution mix.

Nidhesh Jain: Can you give some sense on the margin of the newly launched limited pay protection product as compared to the earlier protection product of 20 year tenure? What could be the order of magnitude in terms of margins difference between these two products?

Satyan Jambunathan: As mentioned in our previous call, the limited pay in margin terms will be lower. But in absolute VNB for a like-to-like it will not be a loss of VNB; that is how we have constructed the product. Also from the positioning/selling perspective, there is a segment of regular pay protection that continues to be there, the limited pay protection segment we are actually trying to create as an incremental segment and not as a replacement of the regular pay protection that we have been doing.

Puneet Nanda: And just to supplement, we are seeing good growth even in the regular pay protection segment. In addition, this is the new segment of limited pay which we are seeing opening up.

Nidhesh Jain: So, just to conclude, the VNB per sum assured would broadly be similar or better in limited pay protection?

Satyan Jambunathan: That is correct.

Anirban Sarkar: I understand on the savings side that the moderation in growth we are seeing here is partly because of equity market volatility, but that holds for all life insurance companies, and yet we are seeing our peers perform better in this segment. What could be the reason for that? What kind of traction we are seeing in the new monthly premium paying ULIP policies? And what is the value proposition there compared to something like mutual fund SIPs?

NS Kannan: On the first question, you talked about why there is a possible disproportionate impact on us, we can only make a hypothesis and assessment based on our conversations with the distribution as well as with our customers, and the data which is available to us. So, one of the possibilities could be that if we look at our average premiums as I mentioned in my opening remarks, we are at about ₹ 180,000 for ULIP products which could be probably much higher compared to some of the others you talked about. So, given the environment which Puneet talked about in terms of the cause for concern for certain segments, given the market volatility, and also the affluent segments being impacted by a general institutional fund performance across the institutional managers. And also if I triangulate and see that the bulk flows to the mutual funds have also been under stress during the third quarter. If I put all that I could sort of conclude to say that one of the possible reasons for impact could be the skew in terms of the average premium in respect of ULIP products. So that is the hypothesis, we can only make a hypothesis based on all the information which is available to us. But what is more important from my perspective is what has been our response. As Puneet articulated, we have focused on expanding the distribution and simultaneously on protection products which is growing at a very rapid pace. So those are the things which we have tried to do. And to look at specifically a monthly strategy, which not only meets the customer’s requirement who has a regular income coming on a monthly basis, it will be easier for him to buy a policy. And more importantly, activating the distribution also so that they have a proper conversation to have with the customers, I think those have been the responses. And we believe that some of that has played out in terms of our APE decline being arrested in the month of November on a year-on-year basis and actually APE growing somewhat in the month of December. As I said, it is important for us to take the momentum forward. And as one of you mentioned on the call, the good outcome of all this strategy has been decent growth in the number of policies during this period, so that is something which we are very happy about. So this is the way we are trying to respond and we believe that given our franchise and our diversification of distribution, we should be able to pursue this kind of strategy going forward, that is the way I would like to assess Q3 in our own context and the market volatility during this period.

Puneet Nanda: Regarding our monthly pay product versus the mutual fund SIPs, our opinion is, there is such a wide market that it is up to us to offer more and more options to customers. The way we have always said, ULIP offers one more option to customers, given that it is a convenience product which gives you access to market linked instrument while also giving you adequate cover. Our monthly pay options also give one more option to the customers where there is a monthly pay investment while in the same product still giving you 10 times cover. So, just on that perspective we believe it opens up one more segment of customer that we are trying to target. And as Kannan mentioned, it also helps us to engage distributors when they are struggling to sell the big ticket annual pay, and they may be able to continue to do something via this strategy.

NS Kannan: Maybe in this kind of market environment, the customer's ability to predict a monthly cash flow maybe a bit better and he may be prepared to invest much more compared to a more lumpy annual cash flow. So that is what we try to do. But as Puneet said, it is an additional investment option which is available to the customer, but we make no bones about the fact that ours is a long-term option. So, we don't offer liquidity or a short term investment option; clearly the hypothesis for sale is the long-term which makes sense to be investing in a life insurance product.

Avinash Singh: On your employee expenses where you said that nine months employee expenses has grown by 5% to 6%, if I recall correctly, you have added close to 1,000 employees towards the beginning of FY19. So that would be roughly ~ 9% of your workforce and still your employee expense is just going 5% or 6%. So what am I missing? Secondly, VNB growth of 18% is also partly due to different way to calculate VNB in the previous year nine months. But if we go for full year, even if we assume that APE growth coming back and margin staying where they are, FY19 absolute VNB is going to be somewhat flat at FY18 level. What kind of a VNB growth for FY20 you would be looking because FY19 for whatever reason is going to be flat at FY18?

Satyan Jambunathan: You are right Avinash. Towards the end of last year we did expand our manpower and that was visible. You would also have noticed and we have discussed that the expansion of manpower was more at the sales staff frontline where the costs are not that high. Through the year also natural attrition brings down the number of people, so what is the cost over the period is the average headcount. So that roughly, as we speak, is now starting to normalize and that is why you do not see an expense of much more than 5% or 6%. With respect to the comparable period of last year, the 13.7% margin for nine months of FY2018 was not on the same basis as full year last year. It is more appropriate to compare 17% margin this year with 16.5% margin of full year last year. Where we will end up the year in terms of absolute VNB will really depend upon how well we are able to do from a new business

APE perspective in the last quarter. Looking at next year, quite clearly, giving a one year view of VNB growth and top-line growth is something that we have never been comfortable with. Nothing that has happened in the last nine months changes our view of the opportunity and potential to the various business segments over the medium-term to long-term. And I see no reason why over the medium-term to long-term we should not come back to the trajectory of growth that we see from a potential in the country.

Harshit Toshniwal: When I look at the monthly pay ULIP which you have started, how much in terms of number of policies of ULIP which has been sold would be the monthly pay ULIP over the last quarter? Even a broad number would help, is it somewhere around 5% to 10% in terms of mix?

Satyan Jambunathan: We have not given out the specific number of how much monthlies we did. But the way we look at is, in the month of November it was an initiative that we started. The objective, as Kannan and Puneet also explained was to make sure that our distribution was still continuing to stay interested. And as we go along, it is not as if monthly premiums are going to start to dominate our business, it will still be one additional option the way Puneet described it.

Harshit Toshniwal: So in that context what I really fail to understand is that broadly high ticket size savings business what we saw, how should we gain confidence that even in medium-term they will return back? Because that was a phase which we saw in a particular period of demonetization and 2014-2015 run. You think that we can again go back to those ticket size or those customers could again come back? And if they are moving out, just want to understand that why is it specific to IPru and not for the industry as a whole?

Puneet Nanda: I think we will have to look at it on a long-term basis, and we will also have to look at the past long-term trend. Maybe even if you take out demonetization, look at last five year trends, and I have used that to extrapolate to the next five years. Our whole affluent strategy has been playing out for five years, it is not just a demonetization thing. If you look at normalized growth, if you look at our five year CAGR and compare it to the industry, you will find that it is pretty encouraging. That gives us a confidence that it will play out. Number two, all the standard macroeconomic parameters that we look at in terms of high savings rate, how the average income levels of the country are increasing, how people are moving more towards financial savings instruments, etc., I think all those are very much intact. We are currently perhaps in a period over a quarter and it may last for two or three quarters we do not know; there is a lot of uncertainty in the market and it will play out. I think in a business like ours we will have to look at it from a long-term perspective where all the fundamentals, not just remain intact but we genuinely feel that those are actually improving. And I still want to reiterate, the monthly strategy, honestly, we feel is giving us access to newer segment of customers, maybe newer segment of distributor. It is not something that is going to replace what our existing strength is, our existing strength will remain as is, and we will continue to focus very hard on that. We are very confident it will work well over the long-term. But maybe this was a good time for us, may be in a bit of a hard way we have learned that is very good for us to diversify, which is what we are attempting to do.

Harshit Toshniwal: In an annuity business you are having new business strain, but my understanding is that it's a single premium in most of the cases. We receive entire premium upfront and it is not that operating expenses are very high in that business, typically in terms of single premium the operating expenses should not look very high, why are we still having a new business strain in that line?

Satyan Jambunathan: That's correct. There are two reasons for new business strain, one, operating expenses which is a cash flow issue, and the second is reserving. Given that we receive all of the premiums upfront and given that the liability is a conservative valuation, that is what creates a new business strain.

Harshit Toshniwal: Even if I assume conservatism in the liability, is it that embedded that in the first year also we make losses? So the reason I understand of new business strain in ULIP is because of the regular premium nature of the business itself. But when I receive entire amount upfront in an annuity and I don't think annuity growth has been very high for us in this particular quarter. Has annuities as a business has been very good for us?

Satyan Jambunathan: You can find the annuity segment in our financial statements. The single premium has roughly doubled. To go back to your earlier question, on unit linked the strain is driven by charge less expense, which is correct, so operating expenses dominates it. If I were to take a very simple example on any guaranteed benefit product and say that I expect to earn 8% per annum, it is quite likely that I may have to reserve assuming I will earn 6% per annum. The difference between the 8% and 6% is what results in the new business strain. So, on any product where the benefit is guaranteed, you will find that the reserving strain actually dominates over the expense strain, especially in the single premium.

Harshit Toshniwal: When I look at the VNB margin, have we benefitted from the fall in interest rate? Because when I compare the rates between December and September, they were around 60 basis point down on an average 10 year rates.

Satyan Jambunathan: Yes, reported margins are at the current yield curve, so there will be some benefit. It may not be the entire 60 basis point that you described, because reality is we are using the entire yield curve depending on the cash flows at various points of time, so the impact could be different from the 10 year point that you quantified. But yes, that is already there. If you see the pack, it sets out the reference rates on page #54 which is updated for the December 31st yield curve.

Harshit Toshniwal: So, when I look at that, 50 basis points is the optical difference or a fall in the margin on a sequential basis, but when I add that 20, 30 basis points by the sensitivity table, so the fall sequentially has actually been 60, 70 basis points on a core basis?

Satyan Jambunathan: I do not know the exact quantification of the yield curve at this point of time, but you are right, the core base would have been more than the 0.5% that you see between H1 and 9M.

Madhukar Laddha: Have we launched the deferred annuity product?

Satyan Jambunathan: No, we haven't.

Madhukar Laddha: Do we plan to do it? Why are we not doing it, because obviously competition is doing very well in that product?

Satyan Jambunathan: We have said this before as well, when it comes to guaranteed returns product, our preference is to do when we are more comfortable with the ability to hedge it properly.

Madhukar Laddha: So, for lack of hedging options that would be the main thing?

Satyan Jambunathan: That is correct.

Madhukar Laddha: Because of this change in upfront commission for mutual funds, do you see that impacting the life insurance/ULIP business in any way?

Satyan Jambunathan: You should also context it with the relative size of the premiums. Having said that, these are two different product categories with very different liquidity and considerations. Even when the tax law changed at the start of the year it wasn't as if we saw any wholesale migration. So we don't think the answer is as straight as saying that commission alone determines what the distributor is going to do, eventually the customer also has different requirements of liquidity and tenure from an investment horizon. And some of those will also become very important determinants of buying decision.

Madhukar Laddha: But do you think this will tilt the scales in your favor?

Satyan Jambunathan: Not really.

Madhukar Laddha: Can you talk a little bit about what steps you are taking to improve protection share in the business mix?

Puneet Nanda: We have articulated that in protection basically there are three categories, first is the retail protection part which is just the term life which you and I buy. Second is the group credit life, and the third is group term. There are different dynamics at play for each, though of course all of them come under the overall protection umbrella. In the retail protection side, of course the biggest play is clearly the fact that it is the most under penetrated segment in the country, overall insurance penetration we know but within that the protection penetration part is very low. So, clearly that is the biggest opportunity. Of course, many of us started on that and have done well, as we go along, we are realizing that within that there are different sub-opportunities, for example, limited pay as we have launched. And like that there are several more opportunities, so we will keep trying to do different variations of that. But all of them will be under the umbrella of retail protection. And retail protection also, there are certain kinds of distributors who can be engaged primarily from this perspective, so we are trying to do that. Second big player is the credit life side, which is largely driven by the retail credit growth in the country. In spite of whatever short-term hiccups, that certainly remains a good opportunity. There our job is more to tie-up with the entities that give loan, they could be banks, NBFCs, HFCs and microfinance institutions, obviously with the right proposition for the customer. So that is a continuous effort and we will keep doing that. The third is the group term insurance, or the group protection market where whether formal or informal groups can be convinced to take, similar to retail term but on a group basis. And obviously there are economies of scale that happen over there. So, again, that is a category which is growing for us. So, clearly there are different segments, but our focus is to grow each and every one of these segments, and we are seeing very good traction in all in terms of our overall mix. Because credit life within that does tend to have a bit of a wholesale flavour, because there we have managed to tie-up with quite a few partners, within the overall mix, growth rate of credit life is more, but all segments are growing quite well.

Madhukar Laddha: Considering most of our business comes from bancassurance channel, can we see some conversion happening over there towards protection?

Puneet Nanda: It is happening, bancassurance is as good a channel as any other in terms of retail protection. In terms of credit life, anyway it is the biggest channel.

Madhukar Laddha: It is still quite low with ULIPs dominating it?

Puneet Nanda: These are two different opportunities, ULIP is a savings opportunity. For banks both retail protection as well as the credit life opportunity exists. So there is a lot of focus on both sides. And if you feel it is low, it is actually very good because that tells us how much opportunity there still is.

Abhishek Saraf: On the ULIP side you said average ticket size is ₹ 180,000 but in terms of this affluent segment, what is the range of ticket size? And what proportion of the overall ULIP pool it would have formed over past one year and how it has declined now? Since you are not able to generate new business premium on the affluent side, are you also witnessing some surrenders in the earlier policies which have been booked earlier or is persistency falling off?

Satyan Jambunathan: With respect to our own mix of business across premium categories, the numbers are available. What we spoke about from an affluent perspective was, if we take annual premium in excess of 125,000 as a proxy, you will see from there what our share is. With respect to your question on impact on surrenders, as we spoke during our opening remarks, the premium persistency for 13th month to some extent has been affected in that segment, but surrender rates have not really been affected in that segment. Surrender rate continues to hold up, in fact surrender still continues to be so far well below what seen in the last year.

Abhishek Saraf: Are you saying that the older policies are still sticking with the general trend that we have witnessed over the years?

Satyan Jambunathan: That is what we have seen so far.

Abhishek Saraf: Like Puneet earlier mentioned during the call that you expect that for the next two, three quarters this segment will stay away from the market as well. So, effectively then are we actually looking at similar kind of growth for next two, three quarters or you think the other segments would be able to pull up the growth from the current low single-digit levels?

Puneet Nanda: I never said we will not see growth for the next two, three quarters. I said the market environment can remain volatile. As a consequence of it, we are not sure what will happen. We are not giving up, we genuinely feel that given the kind of long-term product we have, this volatile environment is the right time to do more. That's why I said we are actually engaging more and more with the affluent customers, and with those kinds of distributors to do more. But the results currently we are seeing is that they are taking more time to get convinced or they are deferring their investment, which is why we are trying to widen and increase the width of whole distribution as well as the customer segment that we want to target. I think that effort has started about two months back and we will continue on that effort. And as I mentioned earlier, I think we are now convinced that effort will be a long-term effort because clearly there is a very mass affluent segment in the Indian market, which still want some of the propositions that we have and maybe we were missing out. So, clearly it is an opportunity that we will pursue.

Abhishek Saraf: On our bancassurance business, effectively over past few years we have struck partnership with other banks also. Given that credit life is driving this and my sense is that your newer partnerships would also be bringing to fruition, how has the share of ICICI Bank in your overall pie evolved in this period?

Satyan Jambunathan: Just as a context, since credit life partnerships are single premium, in APE terms it will not contribute much. From a share of APE, it is not moving the needle too much. Also, ICICI Bank compared to any of the other bank partnerships that we have is much larger. And therefore, within the bancassurance, ICICI Bank still continues to dominate share for us.

Sudhir Kedia: Why the commission rates for the first year premium has gone up both YoY and QoQ?

Satyan Jambunathan: Two factors are driving the commission rate change. First is mix of protection has increased, protection has a higher commission. The second is, within the savings business, commission structures are also a function of productivity of the distributor. If you see share of bancassurance and other corporate distribution in this nine months has been more than what it was in the same period last year. So the channel mix along with the product mix is what is driving it, there is no other change to the commission structure.

Sudhir Kedia: While there is change on product mix on a QoQ basis, you are suggesting that in the same way is channel mix as well?

Satyan Jambunathan: That is correct.

Abhijeet Tibrewal: Can you please breakdown your protection APE into individual protection and group protection?

Satyan Jambunathan: We have not disclosed that breakup at this time.

Abhijeet Tibrewal: Can you give us some more qualitative colour on your credit life book, like what were the attachment rates like and what proportion of our credit life book comes from ICICI Bank?

Puneet Nanda: A large part of our credit life book is actually mortgage, firstly, because within credit life there are three or four segments. Given that most of our partnerships are in the sense last one or two years, of the entire credit life book ICICI Bank is absolutely the biggest and dominant player.

Vinod Rajamani: Now that you are looking also at the mass affluent customer base along with the regular affluent customer base, how are you segmenting your distribution? Is it the same bank trying to sell to both segments of customers, in terms of agency network how are you segregating as to how they will be targeting these two segments of customers?

Puneet Nanda: Within each channel there is a segmented strategy by customer segment. So, for example, ICICI Bank which is the biggest, within that as you know like in any other bank there is a wealth channel, there is a private banking channel, there is a normal mass channel, there is a salary segment, so automatically that segmentation happens. When we come to a channel like agency, there of course we try to segment it in a similar way, obviously it is not so logical but clearly there are certain agents from a certain background who are more focused on the affluent which has been our strength. We are now trying to bring in agents who will have more mass and mass affluent customers. And actually it is not just bringing in more, even in our current base of 1.5 lakh agents there are large number of agents who are perhaps not as active in the mass affluent segment as they could have been. So we are trying to activate them as much as possible.

Nishchint Chawathe: Can you share the contribution of the protection LOB to total VNB?

Satyan Jambunathan: We have not shared that.

Nishchint Chawathe: Can you share persistency on number of policies?

Satyan Jambunathan: It would not be very different, if you look at our persistency for nine months. We have not put out by channel and segment but when we look at it it's still broadly similar. In fact, the weakening trend of persistency, like we described, seems to be more on the higher premium side this year.

Nishchint Chawathe: Which is the reason I thought if you can share that, maybe it gives a slightly better colour in terms of what is happening.

Satyan Jambunathan: I think it is there in the public disclosures.

Nishchint Chawathe: On the solvency part, what are your thoughts? At what point of time will you really want to kind of draw a line and really start thinking about fresh capitalization?

Satyan Jambunathan: We already have. If you notice in the first half of this year on dividend distribution, the special dividend dropped off. So we have already started thinking about it, we will have a discussion again at about the end of the year to see if we need to revisit our dividend policy.

Nishant Shah: How equity market volatility is going to affect your affluent customers? We have not really seen persistency ratios go down much, even in the ULIPs. So would it be fair to assume, probably as like the five year lock-ins come to fruition you might just see a lot of surrenders coming through from these high ticket policies as well?

Puneet Nanda: As mentioned, our 13th month persistency is impacted a bit currently. And within that the larger impact is from the affluent or the high ticket policies, so we are seeing that impact. As far as surrender is concerned, I think we covered that earlier, even those who have completed five years, the current trend seems to be that it is well contained, people seem to be understanding the importance of staying long. So we are not seeing any stress over there, at least.

Nishant Shah: In ULIP I think you have three or five fund switches, so in a year what percentage of your customers actually utilize that instead of letting the policies go into discontinuance and something like?

Satyan Jambunathan: Very negligible, in fact not just three or five, some of our current products have indefinite number of switches, yet we do not see that happening.

Puneet Nanda: I think customers want the flexibility to switch, and once that flexibility is available, it is not necessary that they switch. Our current experience, as Satyan said, is negligible on the number of people who actually use the switch option. Having said that, there is a decent number of customers who do have automatic asset allocation plans, so their automated switches happen.

Nishant Shah: Since we have relatively large portion of debt in the AUM, our thesis was that these policies start off as 100% equity allocation and then maybe switch over to debt as market volatilities improve or something like that. Is that not the case?

Puneet Nanda: There are two kinds of customers. There is one kind who determine the asset allocation upfront, and in their asset allocation they will chose upfront whether to take balanced or equity or debt. Our current experience is that upfront itself the mix is purely well balanced. The second kind of customers are the ones who are passive and who do automatic asset allocation. So actually it is the other way around. A large number of people start with a certain amount in a debt or a short term fund and automatically keep switching into equity over long-term.

Nishant Shah: If it is starting off pretty well balanced why should equity market volatility really impact our new growth or something like that so much?

Puneet Nanda: Because of the upfront premium a large amount still goes into equity on an absolute basis. They do get impacted.

Satyan Jambunathan: We have said this before, we roughly get about 55% to 60% or thereabouts of fresh money which goes into equity, so it is not a small proportion.

Manish Shukla: Would ULIP ticket size in Q3 be materially different than the FY18 number of ₹ 180,000?

Satyan Jambunathan: In Q3 it will be.

Manish Shukla: Could you quantify the order of magnitude, approximately how different it would have been?

Satyan Jambunathan: It is available in the life council disclosures, I can send exact numbers to you.

Manish Shukla: And we are specifically looking only at the ULIP product and not overall ticket size.

Satyan Jambunathan: Yes, we will send it across to you.

Manish Shukla: As you try and go more mass and mass affluent, it obviously will have some kind of cost implications. So what are your assumptions around that? And overall in terms of profitability in general, be it persistency or otherwise by VNB margin, do you believe that it will be different than what you have experienced with the affluent segment?

Satyan Jambunathan: I think to start with, the product choices will be made by the customer, so I do not quite know where it can end up, but it will be really choices made by the customer. With respect to cost associated with going in that segment, again, just to highlight, it is not as if we are going to the extreme mass or low income segment, we are still talking about a premium segment which is Rs 50,000 per annum or more. And that really we do not think should result in any meaningful increase in our cost ratios.

Puneet Nanda: And a large part of the distribution cost is actually just variable, so it does not have that much impact.

Manish Shukla: As Satyan earlier mentioned, the monthly premium is just the start and it may not be a large part of your overall business today, obviously the affluent segment has to be the mainstay for foreseeable future. While market conditions will have its impact on business, is there anything which you can drive from your end either via distribution strategy or otherwise to let's say either try or arrest the fall in that segment or ensure that the segment grows?

Puneet Nanda: Of course, I think that effort is very much on. So, as I mentioned earlier, the effort is on multiple parameters, one of course is directly interact and communicate with the customers on the benefit of long-term, on the benefit of staying invested, on the benefit of volatile market and taking advantage of that, because by definition our product is long-term. Second is communication with the distributors and give them the confidence and some of these are constant conversations. And while we are doing that, create options for monthly. And honestly, everybody needs protection, we also continue to try and engage more and more with the same customer using protection policies so that at least if they stay engaged, once they have confidence then they come back. So it is a combination of all of these things.

Manish Shukla: I know you do not break your protection into individual and group, over the last year would the mix have shifted in favor of group versus individual? Which segment is growing faster?

Satyan Jambunathan: Shifted in favor of group. Because of the multiple partnerships that we have got, the share of retail relative to the same period last year will be lesser now.

NS Kannan: Thank you all of you for your time. If you have any further questions, my team is there to answer your questions. Thank you very much.