ICICI Prudential Life Insurance Company
Earnings Conference call- Quarter ended September 30, 2016 (Q2-2017)
October 25, 2016

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Sandeep Batra: Good afternoon and welcome to the results call of ICICI Prudential Life Insurance Co for H1 2017. I have Satyan Jambunathan, CFO and Vikas Gupta, Head IR with me and we will walk you through the developments during the quarter as well as the presentation on the performance for H1 2017.

We have put up the results presentation on our website. You could access it as we walk through the performance presentation.

As you are aware, our stock was listed on September 29, 2016 pursuant to an IPO of the company through an offer for sale by ICICI Bank, one of the promoter shareholders. As part of the offer document, we had articulated our key strategies as

- Continue to focus on growth through strengthening our multi-channel distribution architecture keeping customer centric product propositions at the core
- Focus on growing the significantly underpenetrated protection opportunity by providing suitable solutions to customers
- Continue to maintain the quality of the business as measured through persistency, expense efficiency, customer grievances and quality of the balance sheet and capital position
- Build the profitability of the business through
    - growing the protection business faster than the rest of the business
    - continuing to improve the persistency of the business
    - Stay focused on cost management

We will update you on the progress on each of these elements as we go through the presentation.

As you are also aware, we have a dividend policy of 40% of PAT as the payout ratio and have over the past quarters been declaring special dividends over and above this keeping in mind the comfortable capital position. The Board today has approved an interim dividend payout of 60% of the PAT for Q2 2017 which included a special dividend of about 20% of PAT for Q2 2017. Going forward the Board will consider dividend proposals on a half-yearly basis.

Performance presentation

I will start with a bit of the background before I get into the performance. As you may be aware, the Indian life insurance market is predominantly a savings oriented market with protection just being a nascent part of it. In that context, we see the savings opportunity being driven by the underlying demographic and economic factors and protection opportunity being driven by the significant potential and evolving delivery ecosystem. Consistent with the opportunity, we look at our business in these two parts of savings and protection. In the savings space, we believe that the competitiveness of our products with other financial products and the convenience of the delivery process will be a key determinant of being able to capitalize on the underlying savings opportunity.

The industry performance for the half year has been quite encouraging. Fiscal 2016 saw the industry growing by 8.1% after a number of years. H1 2017 has seen this growth momentum continuing with the industry growing 17.9% on Retail Weighted Received premium. We are also seeing bancassurance continue to be a significant channel for the private sector. On the product mix front, we have over the past 3 years seen unit linked business becoming a larger share of new business.

As we have articulated earlier, our key strategies are around

- Leveraging market opportunity through delivering customer value propositions
- Strengthening our multi-channel distribution platforms through deepening existing relationships as well as building new relationships
- Focus on growing Value of New business through growth in protection business, improvement of persistency and focus on efficiency
- Using technology as a key driver of profitable growth through process efficiency and opportunity mining

Leveraging Market opportunity

Our RWRP for H1 was Rs 24.80 bn, a growth of 17.1%, largely in line with the industry growth of 17.9%. Within this growth, the savings products APE grew by 14.4% and protection APE grew by 132.7%.

For Q2 2017 our growth was 21.0% compared to industry growth of 19.5 %. For the half year, our market share was 12.4% and we continue to be the market leader in the private sector.

For the half year, our product mix was 80.1% unit linked, 12.0% participating, 4.4% protection and 3.4% for the other products. Our protection mix has increased from 2.7% in FY 2016.

Distribution

All our channels have continued to grow during the half year with agency and direct business continuing to have robust growth. For H1 2017, we had 56.1% of our APE coming from Bancassurance, 23.4% from agency, 12.4% from direct and 8.2% from other channels.

Quality

We continue our focus on persistency. Our persistency across most durations has improved with the 13th month persistency being 82.1% for 5m 2017 versus 81% for H1 2016. The 49th month persistency for 5m-2017 was 61.1% as compared to 77.8% for H1-2016. This was on account of higher Single premium mix in new business for H2-2011 after new linked product regulation came into effect in September 2010. Excluding single premium 49th persistency was 59.7% for 5M-FY2017 compared to 57.7% for H1FY2016.

Our cost to TWRP stood at 17.1% for H1 2017 versus 16.7% for H1 2016. Both commission and non-commission cost ratio have increased marginally from 3.5% to 3.7% and from 13.2% to 13.4% respectively. The marginal increase in cost ratio was due to increased emphasis on protection business and continued focus on building distribution.

Our fund performance continues to be robust vis-à-vis the benchmarks and our quality of fixed income investments continues to be robust.

Profitability

Our PAT for the half year stood at Rs 8.24 bn compared to the Rs 8.12 bn for H1 2016.

Our VNB for H1 2017 stood at Rs 2.44 bn, a VNB margin of 9.4% compared to the FY2016 margin of 8%. The growth in the VNB has come from the growth of the overall business as well as the protection business which grew at 132.7% for the half year. The costs ratios for the half year have been marginally higher than the same period last year.

The embedded value as at 30th September 2016 was Rs 148.38 bn as compared Rs 139.39 bn as at 31st march 2016.

Summary

In summary, we continue to stay focused on growth, especially of the protection business with a continued emphasis on the quality of the business with a view to improving profitability. That's my opening statement. I do hope you are able to access the presentations now and I am happy to take on any questions you might have.

Question and Answer Session

Moderator: Thank you sir. Ladies and gentlemen, we will now begin the question and answer session. If you have a question, please press * and 1 on your telephone keypad and wait for your turn to ask the question. If you would like to withdraw your request, you may do so by pressing * and 1 again. Sir our first question comes from Mr. Sameer from Macquarie. Please go ahead sir.

Suresh: Yeah hi. Sir this is Suresh here from Macquarie. Quickly your new business margin is 9.4%. it is post cost overrun. Can you share with us what would be pre cost overrun your business margin?

Sandeep Batra: Suresh we explained this as part of the RHP, pursuant to the new Indian embedded value coming into force, there is no concept of pre and post cost overrun margin. 9.4% is the margins we have declared which compares with 8%. This is based on actual cost but I would like to add a clarification over here that given the seasonality of cost we have taken the forecast of the cost for FY2017 while disclosing the margin.

Moderator: The next question comes from Mr. Avinash Singh from Jeffries. Please go ahead.

Avinash Singh: Two questions on this your new business margin. Can you provide some sort of targets or guidance do you have and on embedded value, what is your operating return for the first half if annualized. Those are my two questions thank you.

Sandeep Batra: We have grown our margin essentially on the back of protection as well as focus on persistency. We will continue to be focused on these. Our strategies as I have been articulating for over a year is increasing the margins through higher protection mix, improved persistency and lower expenses. We continue to remain focused on each of these items. On the embedded value, we will disclose ROEV only on an annual basis. This is in line with the international practice.

Satyan Jambunathan: Avinash the reason again from an ROEV perspective is that because of the seasonality of the business in the Indian market, we cannot quite annualize what you get from the first half. And therefore it makes more sense if you do it on a full year basis.

Avinash Singh: Okay. On new business margin again one follow up, yes Indian markets work differently so you have sort of a different margin but how does your margin compare with the other large Asian peers. Do you think catching up with them on the margins?

Satyan Jambunathan: Avinash, the Asian markets are quite different; be it the nature of product, be it the nature of distribution even in terms of the product mix.. Most Asian markets tend to have a higher level of protection in their business. In the Indian market the protection business is just about getting started and that is really the big opportunity we have been focused on. If you look at our own trajectory of the way our margins have progressed over the past year and a half, fiscal 2015 we had a margin of 5.7% which grew to a margin of 8% in fiscal 2016 which now is at 9.4% for H1 fiscal 2017and that is largely coming on the back of working on leveraging the protection opportunity and growing the protection business much faster. So I am not so sure it may be quite so straight forward to compare the margins across market but clearly the way we see it, the opportunity in the Indian market from the profitability perspective comes from the protection opportunity.

Moderator: Thank you sir. The next question comes from Mr. Nidhesh Jain from Investec.

Nidhesh Jain: Thanks for the opportunity sir. My first question is that just to understand this VNB margin, since the costs are broadly same and for H1 is relatively slow on the business side, so actual margins may be lower but we have smoothened the cost and hence at 9.4%. Is that understanding right?

Satyan Jambunathan: Can you just repeat the last line of the question?

Nidhesh Jain: So because the costs are broadly the same in H1 and H2, but the business mostly comes in H2. So if one looks at the margin from actual cost, maybe lower than this number but you have smoothened the cost and business in H1 and H2 and hence the margins are 9.4%.

Satyan Jambunathan: The margins factor in a full year forecast of our cost. Broadly you will find that only 40%-45% of our business comes in in H1 and 55%-60% comes in H2 as seen from the historical trend. So given the fact that the value of new business emerges more towards the second half in line with the business. So our margin expansion during this half year is largely a result of further improvement in the protection business. Our protection mix as I mentioned was about 4.4% for this H1FY2017 versus about 2.7% in FY2016.

Nidhesh Jain: So if I look at the H2 margins normally for other life insurance companies, the H1 margins and H2 margins are very different. Normally we see a higher margin in H2 which are significantly higher than the H1 number but in your case the H2 number will be similar to this number or there will be a significant jump.

Sandeep Batra: There are two parts to this. One is in terms of the protection story; we will continue to drive protection. However in the Indian context seasonality is more on the savings side so while the absolute numbers for H2 would be higher, the protection part of it as a percentage may be a little lower because the savings element in H2 seems to grow at a much faster pace. So you will see an absolute number growth and the rest of the margin growth will largely be a function of protection mix and how much we are able to improve persistency.

Satyan Jambunathan: The other thing to keep in mind is typically review our experience on the various parameters towards the end of the year. So what you would see at the end of the year would reflect the actual experience that comes through this year on each of these parameters such as persistency and mortality as well.

Nidhesh Jain: And can you share the amount of dividend which has been paid in H1 just to calculate the pre-dividend embedded value?

Sandeep Batra: Dividend in terms of accounting point of view is now accounted for in EV at the time of payment and not at the time of declaration. So what has got factored in is the dividend that we paid in Q1 which was Rs.2.1 per share aggregating to about Rs 3 Billion plus dividend distribution tax

Satyan Jambunathan: Plus there was an outflow on account of the dividend and DDT of a little under Rs 4 billion in the current year.

Nidhesh Jain: Okay so post dividend embedded value will be around 152 billion? Pre-dividend sorry.

Satyan Jambunathan: That's correct.

Nidhesh Jain: Can you share unwind and any other operating numbers?

Satyan Jambunathan: As described earlier, we expect to do that at the end of the year because due to the seasonality of business what you tend to see in the shorter period tends to be quite distorted. It would be more meaningful to look at it on a full year basis.

Nidhesh Jain: Lastly on the investment variance can you share that number?

Satyan Jambunathan: Like I said all the individual variances and splits we expect to be sharing only on a full year basis.

Nidhesh Jain: Okay sir thank you that's it from my side.

Moderator: The next question comes from Mr. Seshadri Sen from JP Morgan. Please go ahead sir.

Seshadri Sen: Good afternoon Sandeep, Satyan congratulations on the listing and strong numbers. I have three, or four questions so while I go through, the first is you are at 306% solvency and you are at 60% dividend payout ratio. What is your comfort as to what is the level of solvency that the management and the board would be comfortable with and how do you therefore see your payout ratio going forward? Also are you going to continue to pay quarterly dividends because that's not usually the practice of listed companies?

Satyan Jambunathan: Thank you Seshadri, we have decided to move to dividend payout on half yearly basis. You are right most insurance companies actually declare on an annual basis but given the stability in our earning we are expect to declare it half yearly.. So the next dividend we will be declaring is the final dividend for March. Our dividend paying policy as you are aware is 40% payout and considering that we are having a solvency ratio of about 300%, the Board has decided to give an extra dividend of approx. 20% in terms of special dividend. This will be a call taken on a half yearly basis by the Board, keeping in mind the growth, solvency and capital requirement. Just to keep the things in perspective, as we keep on expanding our business and specially the protection business we would consume capital. About two years back if you recall, the solvency ratio was about 370%.

Seshadri Sen: Okay, so is there a minimum floor for the solvency ratio or it is just depending on where you see your future growth?

Sandeep Batra: At this point of time we are pretty comfortable at 300%. Secondly the solvency ratio, the way it is calculated in India it is still on solvency I, we have not moved to the risk-based solvency II as yet and that is the point of time when most companies start assessing solvency ratio. Given that we are above than the regulatory position and from an economic capital point of view given the significant unit-link portfolio we do not see an increase in solvency requirement based on economic capital our solvency ratio may improve.

Seshadri Sen: Okay. The second question is line 16 in your release, the actuarial liability change, that's on a year-on-year basis increased quite significantly, quarter-to-quarter it is down. I know it is not good to look at it on a quarterly basis, but if you could give some of the underlying drivers, is it growth, is the new business train, is it, the underlying macro changes, and how exactly is this panning out?

Satyan Jambunathan: Seshadri, the actuarial liability typically tends to move in line with the premium income and investment income, net of the claims and what we're seeing as the change in liability is actually reflecting the premium income in this period as well as the investment income in this period. There is nothing different from that in the way it is progressing.

Seshadri Sen: Okay. And, okay, so the seasonality does impact it a little bit, am I right in…?

Satyan Jambunathan: Seasonality to the extent that the premium income flow across the four quarters are not uniform, yes it does.

Seshadri Sen: Okay. I see your persistency ratios have moved up a little and thanks for the clarification on the 49-month one, but your renewal ratios are also starting to improve, is that a function of the your book is improving and should we expect it to continuously improve, just the premium renewal rate?

Satyan Jambunathan: Are you talking about the growth in renewal premium, Seshadri?

Seshadri Sen: Yeah, renewal to last year's full total premium.

Satyan Jambunathan: Okay. That is happening because at this point of time my renewal premium is growing in excess of 20%, my new business was growing at about 17 odd percent. Given the strong growth that they have had in the new business over the past few years we have now starting to see that come through into the renewal premium growth as well, so that is showing up as ratio of the renewal premium being slightly higher than the past period.

Seshadri Sen: Okay. And it should continue to improve because in recent years you've done better quality business; it's also a function of the persistency.

Satyan Jambunathan: That is correct.

Moderator: Thank you, sir. The next question comes from Mr. Pankaj Agarwal from Ambit Capital.

Pankaj Agarwal: Hello, sir. Sir, the share of bank assurance has gone down for the industry as well as you for first half of this year versus last year. Any particular reason?

Sandeep Batra: This is more an outcome. We let our customers decide what product they want and from which channel that they want to buy. We are happy to note that our agency channel as well as our proprietary sales force channel has been doing well. The proportion of a channel is not so relevant. I am glad that all the channels are actually growing and they have been growing for the last few years.

Pankaj Agarwal: Okay. And, sir, second, in terms of….you said that your overall growth would be dependent on protection growth as well as savings growth, but, like, the industry already has around 18-19% market share in financial savings. Do you think it can further go up; it can remain constant or go down…what has been the experience in other countries on this matrix?

Sandeep Batra: we believe that the financial savings space will increase and in the financial saving space we are competing with other financial instruments, which includes mutual funds, bank deposits, provident fund, etc. So our growth in this segment will largely be a function of how competitive our products are going to be. So if you recall in 2010 the life insurance business had a share of about 26%, and then it went down and has slowly started to move up again. The way we see it the savings business will largely be growing in line with GDP and within GDP how the financial savings map out. The protection is a big opportunity, which we believe is very, very nascent. For us, we have improved this number from 2.7% last year to about 4.4% of our APE in the first half. It has grown about 130 percent. We believe that is where a larger gap is in terms of opportunity to grow and improve profitability.

Pankaj Agarwal: So, sir, let's say if industry starts losing market share on investments and savings, can protection compensate for that market share loss given that…

Sandeep Batra: Not on top line terms, but on profitability, yes.

Pankaj Agarwal: Okay. Thank you, sir. Thank you very much.

Moderator: Thank you, sir. We have the next question from Mr. Manish Shukla from Deutsche Bank. Please go ahead, sir.

Manish Shukla: Good afternoon and thank you for the opportunity. Of the 4.4% protection, what is the split between individual and group?

Satyan Jambunathan: It's largely individual at this point of time. We have not put out the split between individual and group for protection, but we still operate mainly in the individual space so far.

Manish Shukla: Okay. Just understanding the cash dividend impact on embedded value, so the embedded value that you reported for first half, it is still gross of the dividends of 2Q, so 2Q dividend will take the embedded value lower.

Satyan Jambunathan: That is correct.

Manish Shukla: Right. So now when you announced the FY17 embedded value at the end of the year you would have declared a dividend, but the dividend would not have been paid out, so this basically will be a roll forward, right, I mean, so FY17 embedded – yeah, fine.

Satyan Jambunathan: That is correct.

Sandeep Batra: It will factor in dividends of Q1 and Q2. It will not factor in dividend of H2.

Manish Shukla: Right. Okay. That was one. Second, the increasing share of protection also is coming along with decreasing share of mix of banca. Now, I know you said that you're happy as long as the channel grows, but is it that the other channels are contributing more to protection as compared to banca?

Satyan Jambunathan: Manish, it's not as if one channel is contributing more or less. The way we look at it is that every channel is playing its role in the protection journey. The target opportunity from each channel tends to be a little different. For example, on the bank distribution, the target opportunity is selling term product along with a loan product and that is working quite well for us in the bancassurance space. In the retail space it tends to be one of adding an additional layer of protection to a savings product that's working well. We also sell a fair amount of stand-alone term insurance along with a critical illness cover, which is working well for us. So no matter which channel you look at, the opportunities there are quite distinct and there are some areas, which are common in terms of opportunities. So we are seeing all channels contributing in the protection growth.

Manish Shukla: Okay. My last question, your views on non-participatory savings product, would you not be pursing that as a product and focusing only on ULIP and par?

Sandeep Batra: As we do not think we have the ability to forecast interest rates in a long-term basis the non-participatory savings business can pose balance sheet risk. Secondly, given the high lapsation which can happen on this product it may not be the suitable for large customer segments. So product in our portfolio is very, small portion and it is not going to be an area of our focus.

Manish Shukla: Got it. Thank you, sir. Those were all the questions.

Moderator: Thank you, sir. The next question comes from Mr. Avinash Singh from Jefferies.

Avinash Singh: Hi. One follow-up. Can you provide your new business margin breakup between different products or, I mean, if not for the half-year, do you have any intension to provide this breakup with the full year results?

Satyan Jambunathan: No, Avinash. We have not disclosed product category level margins. We don't expect to do that in the near term.

Avinash Singh: Okay. Thank you.

Moderator: The next question comes from Mr. Sumit Kariwala from Morgan Stanley.

Sumit Kariwala: Hi, Sandeep and Satyan. A quick question from me, that's on cost growth. So just wanted to have some outlook over there, how much of cost growth is actually driven by our expansion and protection and what kind of cost ratios improvement can we see in the savings business, potential distribution expansion plan, some color on that, please?

Satyan Jambunathan: Sumit, when you look at cost and the way it is playing out, we're seeing quite a dramatic fall in our cost ratios over the past two years and where we are at this point of time is one of the best cost ratios in the industry. We believe that it's important for us to stay focused and not losing sight of opportunity, but it in terms of protection, which tends to be a little bit more expensive to sell given the smaller premium prices as well as in terms of building of distribution to make sure that the growth continues. So from that perspective in the near term we don't really expect to see any significant cost improvements come through from what we saw in the last year. If at all we would expect in the near term that the ratios would increase a little bit keeping in mind the growth that we are working on, but going forward clearly the focus is to make sure in the savings business we do stay focused on productivity so that the cost ratio for that portion of the business continues to improve.

Sumit Kariwala: Got it. And distribution expansion, can you give some numbers as to what kind of branch expansion, etc., are you looking at?

Satyan Jambunathan: Our distribution expansion is less about branch. An important part of where our growth has been coming from in the past few years is reducing the dependence on physical infrastructure and working through the digital mode that we have been setting up over the past few years. So in that context it's not a branch expansion, which is coming through, but we are seeking to put in place new partnerships in place from a distribution perspective, which will over a period of time start to yield business potential.

Sumit Kariwala: Got it. Thank you.

Moderator: Thank you, sir. The next question comes from Mr. Vinod Raja Mani from HSBC. Please go ahead, sir.

Vinod Raja Mani: Good afternoon. This is Vinod. . Is there any RoEV guidance for the full year?

Satyan Jambunathan: Vinod, we had an RoEV of about 15.3% for the last year and clearly where we see the opportunities from an RoEV perspective are exactly the same drivers that we have articulated from an improvement of profitability. So the protection business growth is a very important driver, improving persistency is a very important driver and really what we will be able to achieve and deliver on the ground on this as we go through this year will become a key determinant of our RoEV.

Vinod Raja Mani: Thanks.

Moderator: The next question comes from Mr. Nidhesh Jain from Investec.

Nidhesh Jain: Thank you, sir. So on persistency side in H1 have we changed our –our assumption while calculating the margins on persistency or that will happen only at the end of the year?

Satyan Jambunathan: We typically review our assumptions at the end of the year and reflect – if there are any changes we reflect it in the full year. So in the first half year there has been no change in the persistency assumptions.

Nidhesh Jain: Because as I understand last year also there was no change in persistency assumption because of the requirement of APS.

Satyan Jambunathan: Last year there was some change in persistency assumption, but because we had a public report out for the first time we had restated the opening embedded value on the same assumptions that we use for closing, that's why you did not see a separate line of change in assumptions.

Moderator: The next question comes from Mr. Nishchint Chawate from Kotak Securities.

Nshchint Jawate: Yeah, hi, this is Nishchint. I just wanted to understand the growth in protection now is this driven by higher ticket or higher volumes and if you could, kind of, give a broad share as to how the tickets would have gone up?

Satyan Jambunathan: Nishchint, for the half year the ticket sizes in protection haven't changed any significant fashion, so this has really been about growth of volume.

Nshchint Jawate: You're comparing half year to half year?

Satyan Jambunathan: That's right.

Moderator: The next question comes from Mr. Arun from City National Rockdale.

Arun: Yeah. Sir, just wanted to quickly understand how do the commission on single premium flow in right now into the P&L, I mean considering that premium income has fallen for this quarter, but the commission seems to have moved completely differently.

Satyan Jambunathan: The commission is always accounted as it is incurred, so for single premium also it will be exactly the same. There is not too much of single premium that we have done in the current period. Most of our single premium will be with respect to annuities, so there is no change in any fashion in the way single premium is – and commissions have been accounted.

Arun: Right. So if I see, let's say last year, it would have been around, you got 88 number, but now it's flown down to 41, but your commissions there have more than doubled. So that's why I was….

Satyan Jambunathan: You're right. The mix of products in single premium has changed between last year the same period and this year. Earlier we used to sell much more of annuities in the single premium. This year I've been selling some amount of single premium protection as well, so a lot of the annuities didn't even carry a commission or carry the lower commission, whereas the single premium protection come products carry a commission of 2% and that is what is showing up as a different trend that you're seeing.

Arun: All right. Okay. Sir, and secondly on the bank insurance channel, has the growth been similarly consistent across the parent bank, let's say Stan C or the other banks or has any one….has there been a de-scaling in any one bank in terms of growth?

Satyan Jambunathan: No, there has been no de-scaling. If you look at it today out of our bancassurance, a bulk of it still comes from ICICI Bank and Standard Chartered is still a small contributor yet. That's a new relationship with a small base, therefore the growth on that would be faster than what you would have on the large base of what we are delivering on the ICICI Bank relationship, but in aggregate we are seeing all of our channels growing at a healthy pace.

Moderator: Ladies and gentlemen, this concludes your conference call for today. Thank you for your participation and for using Door Sabha's conference call service. You may all disconnect your lines now. Thank you and have good day everyone.

Note: 1.This document has been edited to improve readability.

2. Blanks in this transcript represent inaudible or incomprehensible words.