

HDFC Life Insurance Company Ltd.



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HDFC Life to acquire Exide Life

Event highlights

- HDFC Life to acquire 100% stake in Exide Life Insurance from Exide Industries via issuance of 8,70,22,222 shares at an issue price of INR 685 per share and a cash payout of INR 726 Cr, aggregating to INR 6,687 Cr.
- Issuance of 8,70,22,222 equity shares of face value of INR 10/- each of the Company, on a preferential allotment basis at a price of INR 685/- per equity share (including a premium of INR 675/- per equity share) to Exide Industries Limited as part consideration for acquisition of 100% of the shareholding of Exide Life Insurance Company Limited ("Proposed Issue").
- The process for merger of Exide Life into HDFC Life will be initiated on completion of the acquisition.
- The entire process, including the acquisition and subsequent merger, is subject to obtaining the relevant regulatory and other approvals.
- Exide Life's total premium in FY21 stood at INR 3,325 Cr with an AUM of INR 18,780 Cr as of 30th June 2021. The Embedded value of the Company is INR 2,711 Cr as of 30th June 2021.
- The acquisition is expected to be completed before June 30, 2022.

Transaction Rationale for HDFC Life

- HDFC Life has been looking for an acquisition with a decent distribution mix, a strong agency channel, a presence in Tier 2-3 towns, a strong book and a healthy business.
- The transaction will help to accelerate its proprietary channel growth. It will add ~40% to the topline of HDFC Life Agency. As of 30th June 2021, the agent base for HDFC Life is ~36,700. This merger will also improve the APE by ~38% on its base of FY21.
- The proposed transaction will not only boost its agency business growth but will also strengthen other distribution channels such as Broker, Direct, and Co-operative Banks.
- The acquired company will benefit from HDFC Life's scale, market-leading digital and product innovation capabilities, and prudent risk management strategy, which will help to optimise costs and achieve higher margins over time.
- Exide Life's good-quality business, mostly traditional and protection products, will add about 10% to HDFC Life's existing embedded value.
- Exide life complements HDFC life's geographical footprint. The company anticipates that Exide Life's strong presence in South India, particularly in Tier 2 and Tier 3 towns, will enable access to a wider market.
- Customers of HDFC Life will benefit from a more comprehensive product portfolio, a broader distribution network, and more service touch points.
- Synergies are expected to boost shareholder value, with the potential to improve new business margins through operating leverage and product mix optimization.
- It would help the company achieve its goal of providing financial protection to a wider customer base by increasing insurance penetration.

Conference call highlights:

- HDFC Life has been growing agency force at about 40% recently and at a 20% CAGR, which will be sustained for HDFC Life from an organic perspective, but the Exide Life acquisition will be equivalent to 2-3 years' worth of agency force augmentation.
- The synergies will be realized over a period of 18-24 months post the transaction.
- The acquisition will improve the new business margins as there will be a change in the product mix as well as improvement in the operating leverage for HDFC Life. The Company has a scope to improve its persistency.
- HDFC Life plans to start selling its products via Exide Life distribution.
- Exide Life will contribute approximately 10% to the HDFC Life's business.
- The Exide Life product mix includes 11% protection, ~70% par, 13% Non-Par and 5% ULIPs.
- Exide Life's cost to revenue is about 20% compared to 12-13% for HDFC Life. Thus, it is expected that Exide Life's ratio will normalize closer to that of HDFC Life's in near future.
- The cash transaction is because Exide Life wants to be tax-Neutral as it will have a large tax outgo due to this transaction.
- This transaction will bring about 15% incremental growth in the southern market for HDFC Life post the transaction.
- Exide Life will own 4.1% stake in merged entity while stake of HDFC Ltd will go down to 47.9% from 49% in HDFC Life.
- Exide Life retains lesser risks on its books in protection and re-insure business than HDFC Life.
- Exide Life has a market share of 1.3% in the overall industry which is steady for last few years.
- The transaction will take roughly 6 months to get the relevant regulatory approvals. As a result, HDFC Life has estimated that it will take 12-15 months to align the operations and the high expense ratio with HDFC Life.

Valuation and outlook:

This transaction is beneficial to HDFC Life in terms of ramping up its distribution mix and product mix in order to achieve a healthier margin expansion. We believe the Company's premium valuation relative to peers will be sustained due to the Company's significant growth opportunity and strong prospects. **Currently, the shares of HDFC Life is trading at a P/EV of 4.7x/4.0x on FY22E/23E. We are working on the acquisition synergies and building them into our estimates till then we continue to assign a 4.35x P/EV on FY23E EVPS of INR 181.4 and VNB multiple of 42x and maintain the weighted average Target Price of INR 790 per share for HDFC Life (50:50 weights on the P-EV and appraisal value methodology); implying an upside potential of 7.6% over CMP. Accordingly, we maintain the rating on the shares of HDFC Life Insurance to an "ACCUMULATE".**

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Rating Legend (Expected over a 12-month period)	
Our Rating	Upside
Buy	More than 15%
Accumulate	5% – 15%
Hold	0 – 5%
Reduce	-5% – 0
Sell	Less than – 5%

ANALYST CERTIFICATION:

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