

28 June 2024

India | Equity Research | Company Update

Star Health and Allied Insurance

General Insurance

Earnings outlook gets lifted with COR improvement outlook; compliments strong industry position

We attended Star Health's (Star) 'Investor and Analyst Day' on 27 Jun'24 in Chennai. Star is building well on its vantage in the retail segment via a well-concerted strategy encompassing distribution, product innovation, superior claims processing and enhanced underwriting. It envisions doubling premiums over the next four years; thus, enabling PAT of ~INR 25bn under IFRS by FY28. Star's premium/distribution scale, cost leadership and intense in-house claim servicing capabilities are business moats that give Star an edge, as the industry ultimately seeks profits alongside adherence to EOM guidelines while customer service regulations only get tougher. We remain constructive on Star – retain **BUY** with a TP of INR 728 (35x FY26E EPS of INR 20.8). In an earlier report, we studied recent sectoral trends – read it here ([Link](#)).

Robust organisation structure; to double premiums in 4 years

Star has more than 880 branch offices, 1,150+ STAR Gramin Bima Kendra, 8,500+ sales managers, 700k+ agents and 2,000+ tele-agents for sales and distribution. Along with this, the company partners with 572 direct brokers, 44 banks, 58 corporate agents and 14 NBFCs/HFCs CAs. Star services its customers through 15k+ employees, 30k+ healthcare provider network footprint, more than 550 qualified medical professionals and 400+ customer service agents. For Star, 43% of retail health GWP originates from semi-urban and rural. The company sees agency, banca, corporate and digital growth – its four channels – as growth engines. It envisions GWP/PAT (IFRS) of INR 300bn/25bn by FY28 via doubling of premium, implying ~ retail market share to reach 35% with COR of ~95%. Star also guides for a 100bps COR improvement in FY25.

IFRS will likely augment profitability

On the P&L front, IFRS will likely see a major impact from deferred expenses on procurement costs and unrealised gain/(loss) on investments. This can be gathered from the fact that with the IFRS implementation, Star's FY24 earnings gets an upward revision of 28%, from INR 8.5bn to 10.8bn; consequently, FY24 RoE improves 330bps to 17.7%, from 14.4%. IFRS also enhances transparency and global compatibility, leading to increased public listing, investor confidence and better risk management.

Financial Summary

Y/E March (INR mn)	FY23A	FY24A	FY25E	FY26E
NEP (INR mn)	1,12,616	1,29,383	1,50,499	1,80,798
PAT (INR mn)	6,186	8,450	10,141	12,096
EPS (INR)	10.6	14.5	17.4	20.8
% Chg. YoY	n.m.	36.6	20.0	19.3
P/E (x) (fully diluted)	49.7	36.4	30.3	25.4
P/BV (x)	5.7	4.8	4.2	3.6
Combined Ratio (%)	95.2	96.7	96.0	96.1
Dividend Yield (%)	-	-	-	-
Return on Inv(%)	6.7	7.5	7.5	7.5
RoE (%)	11.4	13.3	13.8	14.1

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Market Data

Market Cap (INR)	310bn
Market Cap (USD)	3,711mn
Bloomberg Code	STARHEAL IN
Reuters Code	STAU BO
52-week Range (INR)	675 /455
Free Float (%)	32.0
ADTV-3M (mn) (USD)	4.5

Price Performance (%)	3m	6m	12m
Absolute	(4.2)	(1.4)	(5.5)
Relative to Sensex	(12.7)	(11.4)	(30.5)

Previous Reports

03-05-2024: [Q4FY24 results review](#)

01-02-2024: [Q3FY24 results review](#)

Composite license could be an opportunity for Star

The life risk segment is a strong adjacency to health. Additionally, Star will likely scale faster by leveraging its proprietary distribution to cross/up-sell to existing customers. Post composite license, Star may also aim at greater activation and engagement of agents through a broader product portfolio, which should bring in better productivity and hence will likely be profit accretive. Greater monetisation of assets – brand/branches/website – with broader offerings on digital channels may potentially increase traffic and business. There will also be a strong potential to innovate on integrated products, which could accelerate business growth.

Enhanced underwriting processes, improved risk pricing

The company has developed a risk scoring model to bucket proposals into high, medium and low risk. Risk scoring and categorisation is based on several factors such as sum insured, products, pin-code, PED, age, channel codes. Based on these factors the proposals are divided into three categories – red, amber and green; this influences the underwriting flow and decision.

Star also has a loss ratio prediction model, which seeks to predict expected ULR of the business underwritten. This helps in monitoring the quality of the portfolio being underwritten proactively, and helps provide a strategy for portfolio optimisation, including underwriting and commission management.

Key risk: High competitive intensity impacting profitability

Below, we share key exhibits from Star Health’s analyst day presentation to highlight some of the salient elements of the company’s strategy and initiatives ahead

Exhibit 1: Customer centricity the core of strategy; key initiatives detailed below



Source: I-Sec research, Company data

Exhibit 2: Product innovations to provide coverage for all



Source: I-Sec research, Company data

Illness to wellness journey – this is an active customer engagement initiative to ultimately ensure profitable growth

Exhibit 3: Illness to wellness journey

Engagement with customers with pre-existing health conditions has increased 3x while tele-medicine customers have increased 1.45x in FY24



Source: I-Sec research, Company data

Exhibit 4: Claims – digital transformation initiatives



Source: I-Sec research, Company data

IRDAI (Insurance Products) Regulations, 2024: Star ready to adapt

Exhibit 5: Key changes in product and Star's readiness

Key Changes – Product		STAR's Readiness	Impact on Existing Business	Opportunity to improve Customer exp
1	CIS to be provided to every policy holder of Individual Insurance policies as well as members of Group Insurance policy	✓	●	Opportunity to have the member data / customer details of the group customers and we can send CIS to mitigate mis-selling
2	Free look Period: Enhanced to 30 days from the existing 15 days from the date of receipt of the policy	✓	●	Our Free look cancellation is negligible.
3	Cancellation by Policy Holder: Notice period by policyholder reduced to 7 days from existing 15 days Refund on pro rata basis as against the existing short period basis	✓	●	Beneficial to customer Receives refund for the period where coverage is not yet started
4	Nomination of the policy: Mandatory at the time of proposal for fresh policies and for existing policies at the time of renewal	✓	●	Beneficial to customer's family

Ready to be implemented by mandated timeline
 To be evaluated
 No Major impact on Business
 Favorable impact on business.

Key Changes – Product		STAR's Readiness	Impact on Existing Business	Opportunity to improve Customer exp
5	Grace Period Cancellations: 15 days for monthly instalment payments and 30 days for quarterly, half yearly and annual payments. Cover to be provided during the grace period	✓	●	We have already initiated auto payment of premiums via ECH / NACH.
6	Moratorium period: Reduced to 50 months (5 years) from the existing period of 8 years	✓	●	Current trends do not reflect major impact. Future behavior changes might require pricing interventions.
7	No Claim Bonus: The Insurer <u>may</u> reward the policyholders who do not make claim in the form of No Claim Bonus (NCB) and / or Discount. Such NCB shall be paid as per the choice/ express consent of the policyholder at the time of every renewal	✓	●	Gives more flexibility to customer for discount or SI enhancement
8	Cashless Approval: Cashless Authorization to be provided immediately but not more than one hour	✓	●	Plans in place to comply by Jul-24 end. This will improve customer experience positively

Ready to be implemented by mandated timeline
 To be evaluated
 No Major impact on Business
 Favorable impact on business.

Key Changes – Product		STAR's Readiness	Impact on Existing Business	Opportunity to improve Customer exp
9	Final Approval: Final authorization to be provided within Three hours of the receipt of discharge authorization request	✓	●	Plans in place to comply by Jul-24 end. This will improve customer experience positively
10	Short term and long-term products: Insurers can offer short term (less than 1 year) and long term (more than 1 year) policies.	✓	●	It gives flexibility to STAR to design short term and long-term policies.
11	Products for All ages/ medical conditions / types of treatment etc	✓	●	STAR has various products catering to all the requirements of regulations.

Ready to be implemented by mandated timeline
 To be evaluated
 No Major impact on Business
 Favorable impact on business.

Source: I-Sec research, Company data

Exhibit 6: Building digital capabilities with the help of cloud, data and API

Star is enhancing its digital capabilities with the help of cloud, data and API. Cohesively, these capabilities will likely drive its next level of business agility and growth.



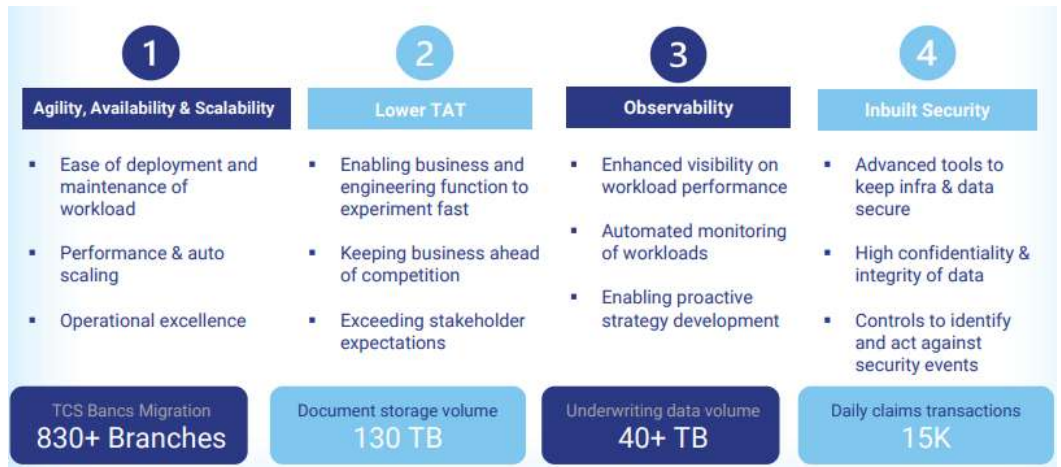
Source: I-Sec research, Company data

Exhibit 7: Cloud and SaaS journey since FY18



Source: I-Sec research, Company data

Exhibit 8: The journey has resulted into unprecedented business benefits



Source: I-Sec research, Company data

Exhibit 9: 'Star Customer App' – integral part of D2C strategy

'Star Customer App' includes face scan, telemedicine consultations, health record management, health risk management, wellness program delivery and ABHA ID generation.

To measure vital health parameters for users and gamify app usage

Configuration settings to limit the usage of Face-scan for customer and non-customer.

Biomarkers include blood pressure, heart rate, oxygen saturation, breathing rate, sympathetic stress, parasympathetic activity, pulse-respiration quotient (PRQ), and Wellness Score.

Monthly Scan **40K+** Total Scan **1.25 Lac**

Source: I-Sec research, Company data

Exhibit 10: Shareholding pattern

%	Sep'23	Dec'23	Mar'24
Promoters	58.0	57.9	57.9
Institutional investors	36.8	37.1	37.7
MFs and other	3.8	3.6	8.1
FIs/ Banks	0.0	0.0	0.0
Insurance Cos.	1.5	2.0	2.7
FIIIs	31.5	31.5	26.9
Others	5.2	5.0	4.4

Source: Bloomberg, I-Sec research

Exhibit 11: Price chart



Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 12: Profit & Loss

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Gross Direct Premium Income (GDPI)	1,29,509	1,52,511	1,79,963	2,15,955
Add: Reinsurance Accepted	15	34	-	-
Gross Written Premium (GWP)	1,29,525	1,52,545	1,79,963	2,15,955
Less: Reinsurance ceded	5,728	11,871	14,397	17,276
Net Written Premium (NWP)	1,23,796	1,40,674	1,65,566	1,98,679
Less: Adjustment for unexpired risk reserve	11,181	11,291	15,066	17,881
Net Earned Premium (NEP)	1,12,616	1,29,383	1,50,499	1,80,798
Incurring Claims (Net)	73,204	86,000	1,00,835	1,21,135
Commission expense	16,828	18,537	22,848	27,557
Operating expenses related to Insurance	-	-	-	-
Underwriting profit/losses	2,047	903	1,651	1,907
Total Investment Income (Policyholder)	-	-	-	-
Operating Profit/Loss	2,047	903	1,651	1,907
Total Investment Income (Shareholder)	5,014	6,407	7,480	8,867
Other expenses (including provisions)	2,185	496	750	740
PBT	8,264	11,289	13,558	16,172
Tax	2,078	2,838	3,417	4,075
PAT	6,186	8,450	10,141	12,096

Source Company data, I-Sec research

Exhibit 13: Balance sheet

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Share Capital	5,817	5,853	5,853	5,853
Reserves & Surplus	59,839	60,429	67,705	79,801
Shareholders' Funds	54,339	63,416	73,557	85,654
Share Application Money	-	-	-	-
Fair Value Change Account	234	1,036	-	-
Borrowings	4,700	4,700	4,700	4,700
Total Sources of Funds	70,589	72,018	78,257	90,354
Investments	1,33,921	1,54,909	1,82,612	2,17,503
Fixed Assets	1,113	1,751	1,951	2,151
Deferred tax Assets	5,689	3,582	3,582	3,582
Current Assets (Inc. Cash)	11,538	17,435	18,158	18,891
Claims Outstanding including IBNR & IBNER	20,301	24,779	29,232	35,079
Provision for unexpired risk reserve	72,687	83,747	98,813	1,16,695
Other liabilities	-	-	-	-
Total Application of funds	70,589	72,018	78,257	90,354

Source Company data, I-Sec research

Exhibit 14: Key ratios

(Year ending March)

	FY23A	FY24A	FY25E	FY26E
Growth ratios (%)				
GDPI Growth	13.0	17.8	18.0	20.0
GWP Growth	13.0	17.8	18.0	20.0
NWP Growth	14.5	13.6	17.7	20.0
NEP Growth	14.8	14.9	16.3	20.1
Shareholders' funds growth	20.0	16.7	16.0	16.4
Investment growth	17.7	15.7	17.9	19.1
PBT growth	(159.2)	36.6	20.1	19.3
PAT growth	(159.4)	36.6	20.0	19.3
Profitability Ratios				
Loss ratio (%)	65.0	66.5	67.0	67.0
Operational expenses ratio (%)	16.6	17.0	15.2	15.2
Commission Ratio (%)	13.6	13.2	13.8	13.9
Combined Ratio (%)	95.2	96.7	96.0	96.1
Underwriting Profit/Loss Ratio (%)	1.8	0.7	1.1	1.1
Investment Returns as a % of NEP	445.3	495.2	497.0	490.4
Other Opex as a % of NEP	1.9	0.4	0.5	0.4
PBT as a % of NEP	4.3	5.3	5.6	5.6
Taxes as a % of NEP	1.8	2.2	2.3	2.3
PAT as a % of NEP	2.5	3.1	3.3	3.3
NEP to Average Net Worth (x times)	2.1	2.0	2.0	2.1
Return on Equity (%)	11.4	13.3	13.8	14.1
Analytical Ratios				
Net Retention Ratio (%)	95.6	92.2	92.0	92.0
GDPI to Net Worth ratio (x)	2.4	2.4	2.4	2.5
Operating profit ratio (%)	3.3	1.1	1.6	1.6
Capital Structure				
Investment Leverage (net of borrowings)	2.4	2.4	2.4	2.5
Solvency Ratio (%)	-	-	-	-
Return ratios				
RoAE (%)	12.4	14.4	14.8	15.2
RoAE (%) - including fair value change	12.3	15.5	13.2	15.2
Payout Ratio (%)	-	-	-	-
Return on avg Investments (%)	6.7	7.5	7.5	7.5
Valuation Ratios				
No. Of Shares (mn)	-	-	-	-
Basic EPS	10.6	14.5	17.4	20.8
Diluted EPS	10.6	14.5	17.4	20.8
Price to Earnings	49.7	36.4	30.3	25.4
Price to Earnings (fully diluted)	49.7	36.4	30.3	25.4
Book Value/share (Rs)	93.4	109.0	126.4	147.2
Book Value/share (Rs) - including fair value change	93.8	110.8	126.4	147.2
Price to Book	5.7	4.8	4.2	3.6
Price to Book - including fair value change	5.6	4.8	4.2	3.6
DPS	-	-	-	-
Dividend yield (%)	-	-	-	-

Source Company data, I-Sec research

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