

Star Health & Allied Insurance Co

| Recommendation | Subscribe | BACKGROUND |
|---|---|---|
| Price Band | Rs. 870 – Rs. 900 | STAR (Star Health and Allied Insurance Co) is one of the largest private health insurers in India with overall market share of 15.8% and retail share of 31.3%. The company primarily focuses on retail health insurance segment (89% mix). Its network distribution includes 779 health insurance branches across 25 states and 5 union territories in India. STAR has also built one of the largest health insurance hospital networks in India with more than 11,778 hospitals. Details and Objects of the Issue The public issue is of Rs. 7239 Cr consisting of – (i) Offer for sale of Rs. 5,239 Cr by investors and (ii) Fresh issue of Rs. 2,000 Cr to augment its capital base and maintain the solvency levels. Investment Rationale <ul style="list-style-type: none">Retail health insurance industry to grow at 23% CAGR till FY25Industry leading growth with focus on profitable retail segmentLargest private health insurance company in IndiaLargest and well spread distribution networkFocus on innovative and specialized productsStrong risk management focus with domain expertise Valuation and Recommendation STAR being the leader in fast growing retail health insurance segment with a market share of 31.3%, offers an attractive opportunity to participate in this granular (retail health mix at 89%), high growth business (FY18-21 GWP CAGR of 31%). In comparison, ICICI Lombard’s growth has lagged at just 4% CAGR owing to a downturn in the motor business (50% mix). STAR and ICICI Lombard both share equally impressive operating metrics, except for the years FY21/22 which are an aberration (due to covid) for STAR, being focused only on the health segment. We view STAR’s valuations at 8.2x Sep 2021 BV favorably in comparison to similar levels for ICICI Lombard, as we expect STAR to continue to grow at much higher growth rates while maintaining decent ROE in the post covid era. We recommend subscribing to the issue from a long term perspective. |
| Bidding Date | 30 Nov - 02 Dec | |
| Book Running Lead Manager | Axis, Ambit, BOA, Citi, SBI Caps, DAM, CLSA, Credit Suisse, I-Sec, IIFL, Jefferies, Kotak | |
| Registrar | K-Fintech | |
| Sector | Health Insurance | |
| Minimum Retail Application- Detail At Cut off Price | | |
| Number of Shares (bid lot) | 16 | |
| Minimum Application Money | Rs. 14,400 | |
| Payment Mode | ASBA | |
| Post Issue Shareholding Pattern | | |
| Promoters | 58.3% | |
| Public | 41.7% | |
| Offer structure for different categories | | |
| QIB (Including Mutual Fund) | 75% | |
| Non-Institutional Investors | 15% | |
| Retail | 10% | |
| Post Issue Equity (Rs Cr) | 575.5 | |
| Issue Size (Rs Cr) | 7,239 | |
| Market Cap (Rs Cr) | 51,796 | |
| Face Value (Rs) | 10 | |
| Jehan Bhadha (+91 22 6273 8174) Sr. Research Analyst jehankersi.bhadha@nirmalbang.com Mahima Mehta (+91 22 6273 8186) Research Analyst mahima.mehta@nirmalbang.com | | |

| Financial Snapshot | FY19 | FY20 | FY21 | H1FY22 |
|-----------------------|-------|-------|--------|--------|
| Gross Written Premium | 5,415 | 6,891 | 9,349 | 5,070 |
| Growth | 30% | 27% | 36% | 28% |
| Net Earned Premium | 3,580 | 4,693 | 5,023 | 4,660 |
| Growth | 31% | 31% | 7% | 72% |
| PAT | 128 | 268 | -826 | -380 |
| Growth | -25% | 109% | NA | NA |
| Combined Ratio | 94.3% | 93.2% | 114.8% | 119.2% |
| ROE * | 13.1% | 18.8% | -32.3% | -15.1% |
| BVPS * | 23 | 34 | 108* | 110* |
| EPS * | 2.2 | 4.7 | -14.3 | -6.6 |
| P/E * | 404 | 193 | NA | NA |
| P/BV * | 39.3 | 26.9 | 8.3* | 8.2* |

Source: Company, NBRR
* = Calculated on post IPO basis

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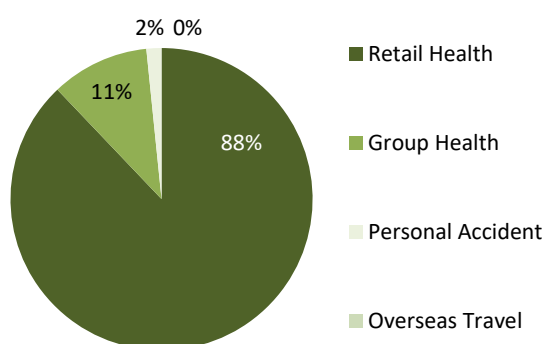
Company Background

STAR (Star Health & Allied Insurance) is the **largest private health insurer in India with a market share of 15.8%** in the Indian health insurance market (retail + group) in FY21 with a total GWP of Rs. 9349 Cr. **Market share was higher at 31.3% with respect to the retail health insurance market in FY21.** From being the first standalone health insurance company established in India in 2006, it has grown into the largest standalone health insurance company in the overall health insurance market in India. **Its comprehensive health insurance product suite insured 2.05 crore lives in FY21 in retail health and group health, which accounted for 89.3% and 10.7%, respectively, of its total health GWP in FY21.** STAR is strategically focused on the retail health market segment. It has been consistently ranked first in the retail health insurance market in India based on retail health GWP over the last three years. The retail health segment is expected to emerge as a key growth driver for the overall health insurance industry in India after the COVID-19 crisis due to low penetration of health insurance, high out-of-pocket expenses for healthcare costs and since only 10% of the population has insurance policies outside of government plans. In FY21, **STAR's retail health GWP was over three times the retail health GWP of the next highest retail health insurance market participant.**

STAR distributes health insurance policies primarily through individual agents, which accounted for 79% of its GWP in FY21. Its total number of individual agents grew at a CAGR of 27% from 0.29 million in FY19 to 0.46 million in FY21. As of September 30, 2021 STAR's distribution network has grown to 779 health insurance branches spread across 25 states and 5 union territories in India. The existing branches are also supplemented by an extensive network of over 562 Sales Managers Stations, which are small individual service centres, and over 6,892 in-house sales managers. STAR has successfully built one of the largest health insurance hospital networks in India, with 11,778 hospitals as of September 30, 2021.

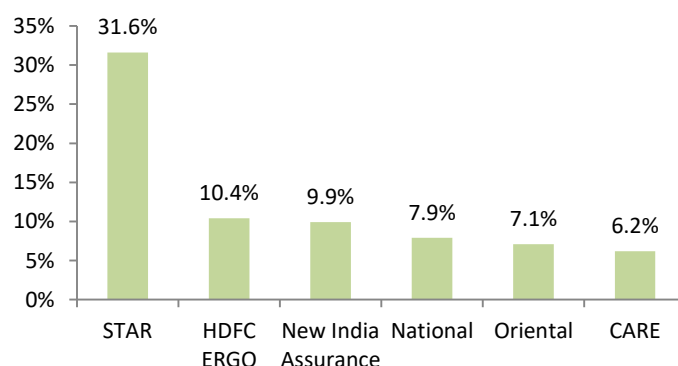
The claims process being the most sensitive part of a customer's experience with health insurance, STAR's entirely in-house claims management capabilities are a key part of its customer service proposition. Controlling the claims process enables it to make the process more customer friendly, deliver a quality service experience and control the costs associated with the claims process. It also enables to reduce the costs associated with claims process, improve the accuracy and cost-efficiency of the actual claim amounts and better detect fraudulent claims.

GWP Mix dominated by Retail



Source: Company, NBRR

Market share of 3x its nearest competitor in Retail Health Ins.



Source: Company, NBRR

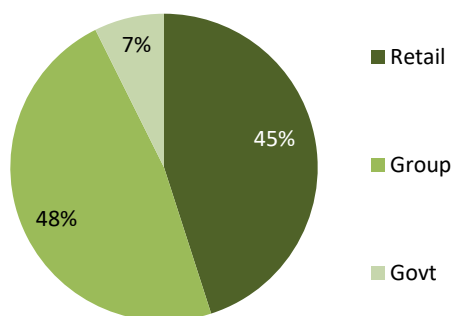
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Investment Rationale

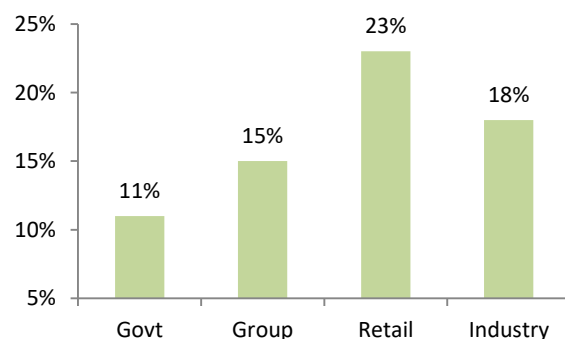
Strong Industry Tailwind – Retail health insurance industry to grow at 23% CAGR till FY25E

The Indian health insurance market continues to be underpenetrated, with a health insurance penetration of only 0.36% of GDP in 2019, compared to the global average of approximately 2.0% of GDP. India has one of the lowest health insurance densities globally, based on per capita premium, at just US \$5 in 2019. The retail health insurance segment contributed 45% of the total health GWP generated in the overall health insurance market in FY21. Profitability in the retail health insurance segment is being driven by (i) higher pricing, (ii) customer loyalty, which is higher than other health insurance segments, as well as (iii) lower claims ratios, which were 73% in retail health, compared to 99% in group health and 92% in government sponsored health schemes in FY20. In addition, standalone health insurers only had a claims ratio of 66% in FY20, compared to 82% and 102% for private sector and public sector insurers, respectively.

Health insurance industry – segmental mix (GWP FY21)

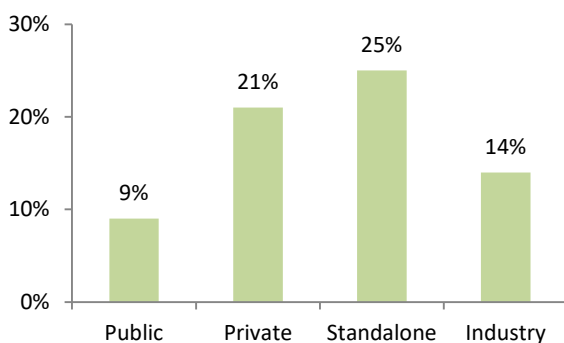


4 year CAGR in GWP (FY21-25E)

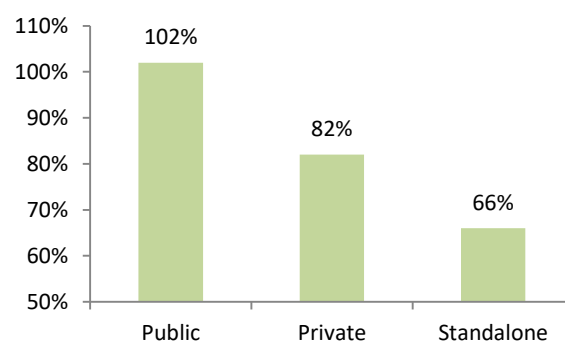


Source: Companies, NBRR

3 year CAGR in GWP (FY18-21) within retail health



Standalone health insurers have lowest claims ratio



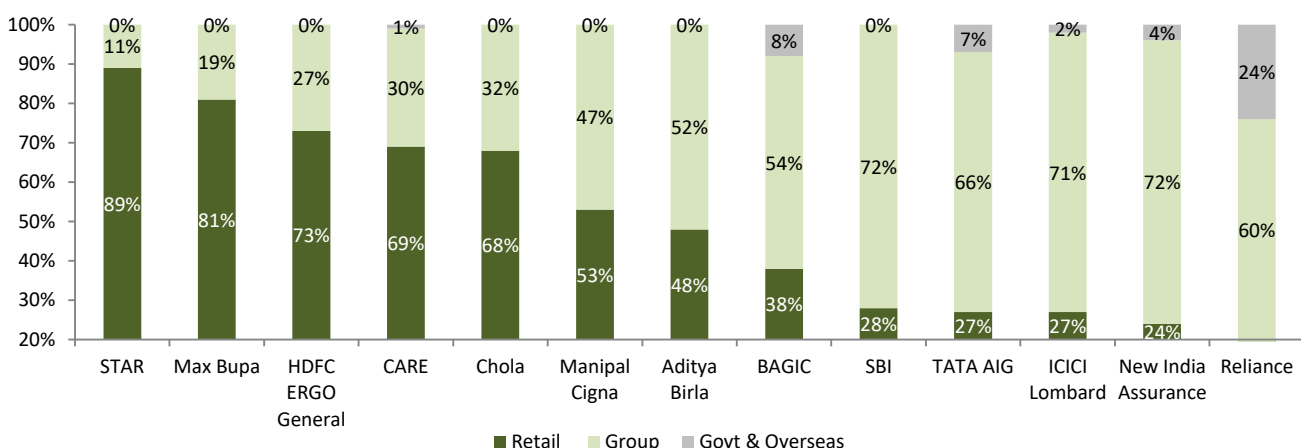
Source: Companies, NBRR

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Industry leading growth with focus on profitable retail segment

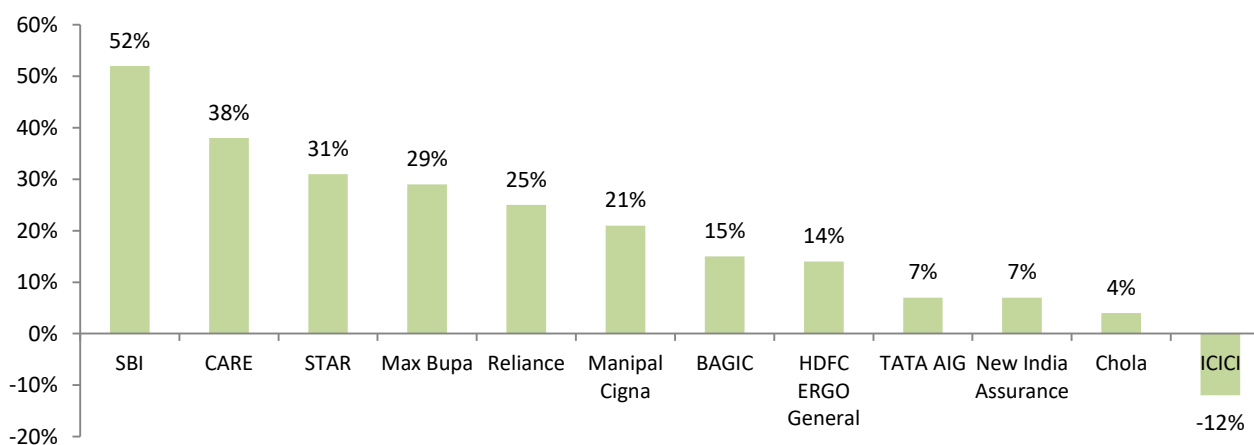
STAR stands out among all competitors for its focus on the profitable retail segment. **STAR has capitalised on the inherent higher growth in the retail health insurance segment and grew at a CAGR of 31% over FY18-21 compared to standalone retail health insurance segment growth of 25% CAGR and overall retail health insurance segment growth of 14%.**

Product Mix - FY21 GWP



Source: Companies, NBRR

Retail health insurance premium CAGR over FY18-21



Source: Companies, NBRR

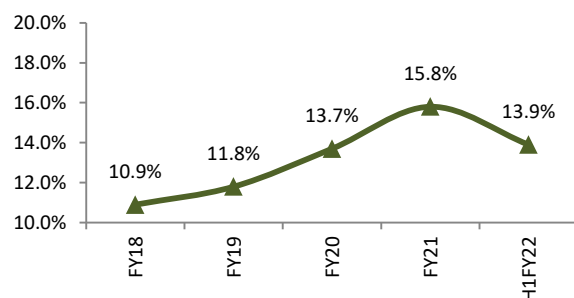
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Largest private health insurance company in India with leadership in the attractive retail health segment

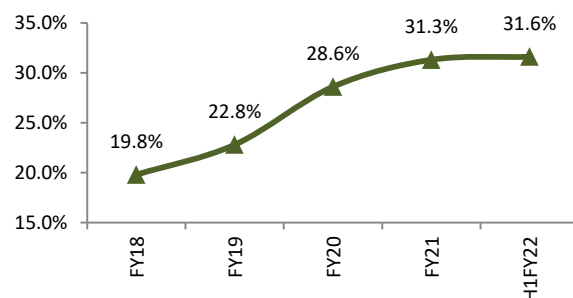
STAR is the largest private health insurance company in India by health GWP, with a 15.8% overall health insurance market share and a 31.3% retail health insurance market share in FY21. **The retail health segment in India is expected to emerge as a key growth driver for the overall health insurance market due to its lower claims ratio of 73%, as compared to government health and group health with claims ratios of 92% and 99%, respectively, in FY20, making the retail health segment more attractive from a profitability perspective.**

STAR's size and established market share positions it well to continue to capitalize on these ongoing market dynamics in the retail health insurance sector. In addition STAR also had **97.9% renewals** by GWP value for retail health business in FY21, as well as approximately 63.4% higher inward portability compared to FY20, which reflects the increase in retail health GWP from new customers choosing to change to STAR insurance plans from other health insurance providers. **Average retail health sum insured for STAR grew at a CAGR of 11.7% over FY19-21**, which can be considered an indication of the company selling new policies with higher sum insured, as well as customers choosing to upgrade their insurance coverage to higher sum insured products when they renew. As a result, the **retail health insurance market share by GWP, increased increased for STAR.**

Market share of STAR in TOTAL health insurance



Market share of STAR in RETAIL health insurance



Source: Companies, NBRR

Largest and well spread distribution network in the health insurance industry

STAR's distribution network includes the largest branch network among non-public health insurance providers in India, which as of September 30, 2021 included **779 health insurance branches spread across 25 states and 5 union territories** in India. Its branch network is supplemented by an extensive network of over 562 Sales Managers Stations and over 6,892 in-house sales managers as of September 30, 2021. Its branches act as a hub to its Sales Managers Stations and agents, which enable it to access a geographically and demographically broad Indian customer base, facilitating future expansion.

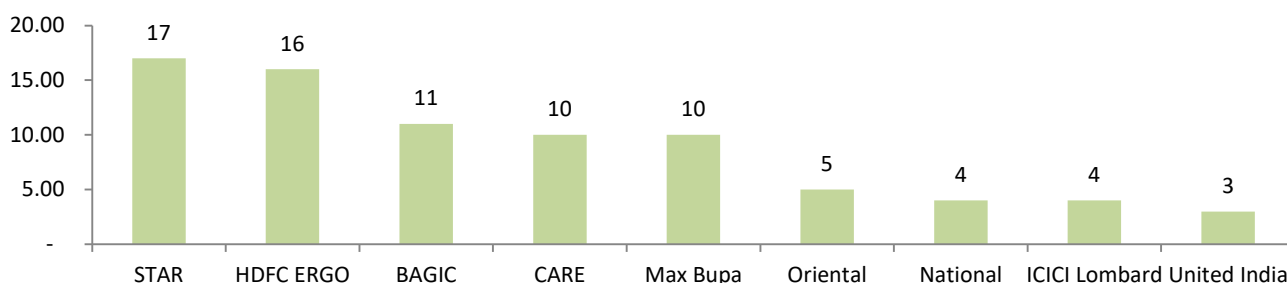
As on FY21, STAR had the largest number of individual agents among standalone health insurers, at approximately three times that of the company with the next highest number of agents. **STAR's total number of individual agents grew at a CAGR of 27% from 0.29 million as of FY19 to 0.46 million as of FY21 and was 0.51 million as of September 30, 2021.** In addition, as of September 30, 2021, 0.07 million of its agents were engaged directly to sell health insurance policies. The number of its agents engaged directly grew at a CAGR of 45% over FY19-21. **Its agency network accounted for 80.4% of its GWP.**

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Focus on innovative and specialized products

STAR develops products through innovation-driven product development process, which includes extensive market research in which it analyses market demand and coverage gaps, and profitability analyses. **As a part of the product development process, STAR involves members of its marketing, products, claims, actuarial and underwriting teams, which include in-house medical professionals, in the various stages of the product development process in order to meet the needs of different customer profiles.** Its products include family floater products (58% mix in retail), individual products (29% mix in retail) and specialized products based on the age of its customers, such as Senior Citizens (13% mix in retail). STAR has also developed premium products, which have additional coverage and higher sum insured than its traditional products. STAR also introduced other innovative products tailored to specific geographies, such as Star Micro Rural and Farmers Care.

Player wise number of retail health insurance products

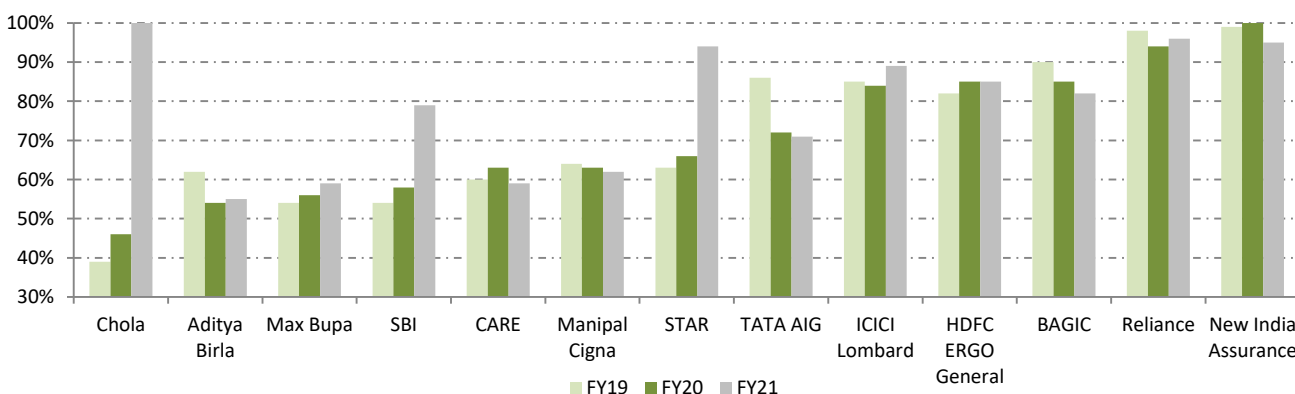


Source: Companies, NBRR

Strong risk management focus with domain expertise

Claims process is the most sensitive part of a customer's experience with health insurance, and an insurer's approach to claims management is a key part of its customer service proposition. To reduce the costs associated with claims, STAR engages with customers through in-house tele-medicine service, TALK TO STAR, which provides customers with access to experienced doctors that can give second opinions and alternative medical solutions over the telephone or internet. STAR believes that controlling the claims process enables it to make the claims process more customer friendly and to deliver a better quality customer service. It also enables it to reduce the costs associated with the claims process, ensure the accuracy and cost-efficiency of the actual claim amounts and better detect fraudulent claims.

Claim ratio for health insurance



Source: Companies, NBRR; *FY21 claim ratio is an aberration due to covid

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Key Risks

Catastrophic events, such as natural disasters, could materially increase the claims liabilities by policyholders, resulting in losses

Health insurance business is exposed to the risk of catastrophes such as pandemics or other catastrophic events which could lead to losses in the investment portfolio of STAR due to the failure of counterparties to perform their obligations or significant volatility or disruption in the financial markets, and could in turn have a material adverse effect on the business.

Adverse movement in investment yields could impact investment income

As of September 30, 2021, almost all investment assets were invested in fixed income assets and mutual funds. Changes in prevailing interest rates including parallel and non-parallel shifts in yield curve could materially affect investment returns, which in turn could have a material effect on the investment income.

Prolonged existence of covid and emergence of subsequent waves

Many countries the world over are witnessing repeated covid waves resulting in higher hospitalization. STAR's business is directly impacted by covid as witnessed in FY21 & H1FY22 when the company posted losses. Emergence of subsequent covid waves in India shall again impact STAR and delay the recovery in earnings.

Outstanding legal proceedings

There are outstanding legal proceedings (civil – Rs. 462 Cr & taxation – Rs. 105 Cr) involving STAR, its directors, promoters and group companies. These proceedings are pending at different levels of adjudication before various courts and tribunals. Such proceedings could divert management time and attention and consume financial resources in their defence. Further, an adverse judgment in some of these proceedings could have an adverse impact on the financial condition of the company.

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Valuation and Recommendation

STAR being the leader in fast growing retail health insurance segment with a market share of 31.3% offers an attractive opportunity to participate in this granular (retail health mix at 88%), high growth business (FY18-21 GWP CAGR of 31%). In comparison, ICICI Lombard's growth has lagged at just 4% CAGR owing to a downturn in the motor business (50% mix). STAR and ICICI Lombard both share equally impressive operating metrics, except for the years FY21/22 which are an aberration (due to covid) for STAR, being focused only on the health segment. We view STAR's valuations at 8.2x Sep 2021 BV favorably in comparison to similar levels for ICICI Lombard, as we expect STAR to continue to grow at much higher growth rates while maintaining decent ROE in the post covid era. **We recommend subscribing to the issue from a long term perspective.**

Peer Comparison

| Parameters as on FY21 | ICICI Lom. | STAR |
|------------------------|------------|--------|
| <u>Growth</u> | | |
| GWP | 14,320 | 9,349 |
| CAGR (FY18-21) | 4% | 31% |
| <u>Product Mix</u> | | |
| Motor | 50% | 0% |
| Health, Travel, PA | 22% | 100% |
| Fire | 16% | 0% |
| Marine | 3% | 0% |
| Others | 9% | 0% |
| <u>Combined Ratio</u> | | |
| FY19 | 99% | 94% |
| FY20 | 100% | 93% |
| FY21 | 100% | 115% |
| <u>Claims Ratio</u> | | |
| FY19 | 85% | 63% |
| FY20 | 84% | 66% |
| FY21 | 89% | 94% |
| Expense Ratio | 29% | 28% |
| Solvency Ratio (x) | 2.9 | 1.5 |
| <u>ROE</u> | | |
| FY19 | 21.3% | 13.1% |
| FY20 | 20.8% | 18.8% |
| FY21 (one off year) | 21.7% | -32.3% |
| P/E FY21 (Post IPO) | 45.9 | NA |
| P/BV Sep'21 (Post IPO) | 8.4 | 8.2 |

Source: NBRR

Star Health & Allied Insurance Co

Financials

| P&L (Rs. Crs) | FY19 | FY20 | FY21 | H1FY22 | Bal. Sheet (Rs. Crs) | FY19 | FY20 | FY21 | H1FY22 |
|-----------------------------|-------------|-------------|---------------|---------------|------------------------------|--------------|--------------|---------------|---------------|
| Gross Written Premium | 5,415 | 6,891 | 9,349 | 5,070 | Equity capital | 456 | 491 | 548 | 553 |
| <i>Growth</i> | 30% | 27% | 36% | 28% | Reserves & surplus | 587 | 1,153 | 3,676 | 3,765 |
| Net Written Premium | 4,141 | 5,261 | 7,145 | 4,779 | Net worth | 1,043 | 1,644 | 4,224 | 4,318 |
| <i>Growth</i> | 30% | 27% | 36% | 62% | Share Application Money | 350 | 0 | 0 | 0 |
| Net Earned Premium | 3,580 | 4,693 | 5,023 | 4,660 | Borrowings | 250 | 250 | 250 | 650 |
| <i>Growth</i> | 31% | 31% | 7% | 72% | Fair Value change Account | 0 | 3 | -7 | 6 |
| Claims Incurred | 2,298 | 3,087 | 4,369 | 4,111 | Current Liabilities | 902 | 1,179 | 1,564 | 1,567 |
| <i>Net Claims Ratio</i> | 64% | 66% | 87% | 88% | Provisions | 2,492 | 3,051 | 5,195 | 5,325 |
| Commission exp. (a) | 264 | 341 | 584 | 626 | Debit Balance from P&L | 164 | 0 | 725 | 1,105 |
| Operating exp (b) | 983 | 1,102 | 1,401 | 854 | Total liab and equity | 4,872 | 6,127 | 10,501 | 10,762 |
| Opex exp (a+b) | 1,246 | 1,443 | 1,985 | 1,481 | Investments-Shareholders | 952 | 1,478 | 2,632 | 3,200 |
| <i>Net Expense Ratio</i> | 30.1% | 27.4% | 27.8% | 31.0% | Investments-Policyholders | 2,078 | 2,812 | 4,205 | 5,403 |
| Underwriting Profit | 35 | 163 | -1,332 | -932 | Fixed Assets | 98 | 102 | 99 | 116 |
| Investment Income | 196 | 294 | 424 | 437 | Deferred Tax Asset | 142 | 147 | 421 | 549 |
| <i>Investment Yield</i> | 6.5% | 8.0% | 7.6% | 11.3% | Cash & Bank Balances | 893 | 611 | 1,879 | 878 |
| Provisions | 4 | -3 | 34 | 0 | Advances & Other Asset | 709 | 977 | 1,265 | 616 |
| Other exp | 45 | 46 | 104 | 18 | Total assets | 4,872 | 6,127 | 10,501 | 10,762 |
| Operating Profit/PBT | 182 | 413 | -1,046 | -513 | Key Ratios | FY19 | FY20 | FY21 | H1FY22 |
| Tax | 54 | 145 | -220 | -132 | Combined Ratio | 94.3% | 93.2% | 114.8% | 119.2% |
| <i>Tax Rate</i> | 30% | 35% | 21% | 26% | ROE (Reported) | 13.1% | 18.8% | -32.3% | -15.1% |
| PAT | 128 | 268 | -826 | -380 | Solvency | 1.53 | 1.50 | 2.23 | 1.52 |
| <i>Growth</i> | -25% | 109% | NA | NA | Valuation Ratios | FY19 | FY20 | FY21 | H1FY22 |
| Per Share Data | FY19 | FY20 | FY21 | H1FY22 | P/E | 403.9 | 193.3 | - | - |
| EPS (Post IPO) | 2.2 | 4.7 | -14.3 | -6.6 | P/BV (Pre IPO) | 39.3 | 26.9 | 11.7 | 11.5 |
| BVPS (Pre IPO) | 23 | 34 | 77 | 78 | P/BV (Post IPO) | - | - | 8.3 | 8.2 |
| BV (Post IPO) | - | - | 108 | 110 | | | | | |

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