

## ICICI Bank

ICICI Pru Life management speaks: entering a tough stage - ALERT

## Overweight

ICBK.BO, ICICIBC IN

Price: Rs1,142.10

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### Banks

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- *We met with management at ICICI Prudential. They expect to contain volume contraction within a few months, but remain cautious on margin guidance. ICICI Pru has restructured costs with relatively less pain, and this will be key to margins going forward. We maintain our cautious view on insurance, given risk to margins and growth.*
- **Pressure on margins:** Management maintained their guidance of 15-16% NBP margins (from ~19% currently) – there are downside risks from expenses and persistency. DTC implementation (implying 30% tax rate for insurance vs. the existing 14%) would further impact margins by 3-4 bps. We reckon the negative impact on EV at 10-15%, but that could be offset by a change in the tax calculation method.
- **Growth – could bounce back:** ICICI Pru expects flat to low single digit new business premium growth in FY11E, implying ~15% contraction in 2H11. The top end of the market is seeing some traction for single premium policies, offsetting pressure on regular pay products. Management expects share of conventional products to increase but LIC has a clear advantage in conventional products, given higher bonuses and the ability to mine the historic portfolio.
- **Expense management very important:** ICICI Pru has not resorted to any mass restructuring which they believe would be counter productive over the long term. Management aims for ~30-40% reduction in expense ratio from current levels and believes that containing expenses would be very important to deliver on the margin guidance.
- **Clear product segmentation, ICICI Bank branches will help:** Under the new ULIP guidelines, management is trying to align product offerings with customer needs. Conventional products would focus on smaller ticket premiums, single premiums to the top end, and ULIPs to the middle market. Management also sees its linkage to ICICI's 2500-strong branch distribution network as a clear competitive advantage.
- *We maintain our cautious stance on the sector as we believe the industry would face significant challenges in maintaining NBAP margins at >13-14%. Also news of internal restructuring would continue to impact sentiment. Our valuation of ICICI Pru stays at Rs 160bn (~11.0x FY11E NBP multiple) and it contributes 7% to ICICI's SOTP valuation of Rs1350. Key risks to our PT include a slowdown in the economy and a spike in interest rates as ICICI continues to be dependent on wholesale deposits (albeit on a lower scale than earlier).*
- *We retain our OW rating on ICICI despite the negative view on insurance because: a) its contribution to SOTP is now small, b) the negative view is quite consensus now, and c) the credit cost improvement in the parent bank could surprise consensus and drive outperformance.*

See page 3 for analyst certification and important disclosures, including non-US analyst disclosures.

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Figure 1: ICICI Pru Life Valuations

	ICICI Pru
Value of business (Rs bn)	161.2
EV (Rs bn)	78.2
PV of NBAP (Rs bn)	83.0
P/NBAP	20.4
P/NBAP (ex-EV)	10.51
P/EV	1.90
P/AUM	31.3%
NBAP Margins - Long term	13.5%
Cost of Equity	17.5%
Contribution to parent (Rs/share)	91
% of PT	7.0%

Source: J.P.Morgan estimates.

Figure 2: ICICI Bank: Subsidiary valuation

	Method	Value of sub - [A]	ICICI/BC's share [B]	ICICI share (Rs mn)	Per share of parent
Life Insurance	Appraisal value	161,200	74%	119288	107
Asset Management	4% of AUM	36,080	51%	18401	17
ICICI Securities	PE of 15x Sep-12	22,753	100%	22753	20
ICICI Home Finance	PE of 12x Sep-12	23,826	100%	23826	21
General Insurance	Combined ratio	14,811	74%	10960	10
Foreign subsidiaries	1.0x Sep-12 book	92,493	100%	92493	83
Total Subsidiary value				287721	258
Value post holding discount (15%)				244,563	219

Source: J.P.Morgan estimates.

Figure 3: ICICI Bank: SOP Valuation

FY12-13 EPS	63.8
Target PE Multiple	17.3
Value for banking business	1,104
Subsidiary valuation at 15% holding discount	219
Total Value	1,324
Sep-11 PT	1350
Implied Sep-12 P/B (Lending book)	2.55

Source: Company data, J.P. Morgan estimates.

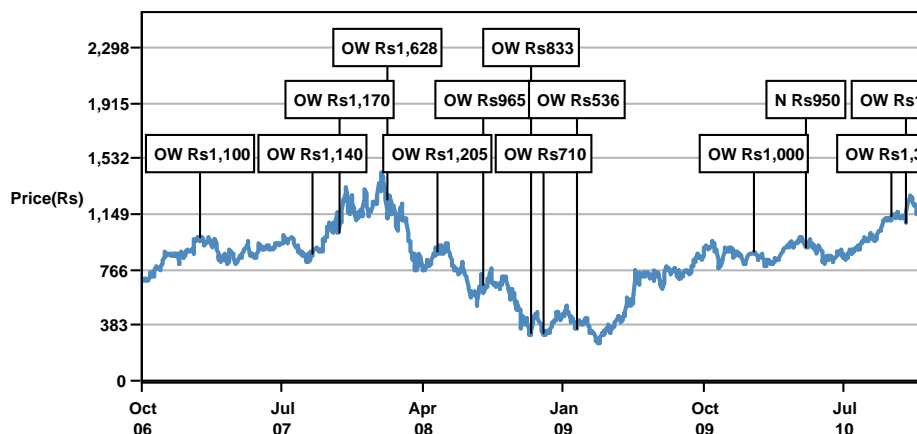
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ICICI Bank (ICBK.BO) Price Chart



Date	Rating	Share Price (Rs)	Price Target (Rs)
20-Jan-07	OW	985.55	1100.00
31-Aug-07	OW	872.05	1140.00
21-Oct-07	OW	1024.05	1170.00
21-Jan-08	OW	1245.45	1628.00
28-Apr-08	OW	894.95	1205.00
27-Jul-08	OW	663.45	965.00
28-Oct-08	OW	335.40	833.00
22-Nov-08	OW	335.55	710.00
26-Jan-09	OW	364.30	536.00
06-Jan-10	OW	888.05	1000.00
15-Apr-10	N	918.00	950.00
02-Oct-10	OW	1135.20	1300.00
30-Oct-10	OW	1089.05	1350.00

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends.  
Break in coverage Mar 07, 2004 - Jun 22, 2004. This chart shows J.P. Morgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period.  
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#### ICICI Bank (IBN) Price Chart



Date	Rating	Share Price (\$)	Price Target (\$)
15-Apr-10	N	42.84	-
02-Oct-10	OW	49.85	-

Source: Bloomberg and J.P. Morgan; price data adjusted for stock splits and dividends.  
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