# Easing of FDI norms boosts deals in insurance space

After Max India, Reliance Capital sheds stake in insurance biz; will help firms unlock value

**COMMENT**

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There have been plenty of deals in the insurance space recently, thanks to the government increasing the foreign direct investment cap to 49 per cent from 26 per cent.

On Tuesday, Nippon Life bought 23 per cent stake in Reliance Life Insurance (part of Reliance Capital) pushing up its holding in the company to 49 per cent. The deal comes close on the heels of Max India's sale of 23 per cent in Max Bupa — its health insurance business to its foreign JV partner Bupa Plc on Monday.

Max India and Reliance Capital's stake sale in their insurance businesses is one of the many deals that have taken place in the last one year. Like many conglomerates in the financial services space, this will help both Max India and Reliance Capital unlock value in their insurance subsidiaries by transferring shares in favour of their foreign partners.

## Undervalued

Insurance subsidiaries of companies in the financial services space have been undervalued for two main reasons. One, until recently only a few insurance players were profitable. And, two, there has been a lack of investor interest in the space due to absence of valuation benchmarks in the listed space.

But now many players, both in the life and general insurance space, have turned profitable. The hike in FDI limit in insurance has now paved the way for unlocking value in insurance subsidiaries by opening up avenues for listing or transferring shares in favour of their foreign partners.

Also, for players such as Max India and Reliance Capital, the value unlocking will be substantial. This is because the contribution of the insurance busines to the companies' overall business is substantial.

For instance, 55-80 per cent of these companies' fair value (calculated on the basis of sum-of-the-parts value) comes from their insurance businesses. Other banking stocks such as SBI, HDFC and ICICI Bank derive a lesser share from their insurance business — 8-14 per cent of their SOTP value.

## Deal consideration

Reliance Life is a joint venture between Nippon Life Insurance and Reliance Capital in which the latter directly and indirectly held 74 per cent stake. Following the 23 per cent stake sale to Nippon Life, Reliance Capital will hold 51 per cent in Reliance Life.

Nippon Life will pay ₹2,265 crore for the 23 per cent stake, which pegs the valuation of the insurance business at about ₹10,000 crore. According to the company, this is over three times the implied embedded value (a measure used to value a life insurance business which, among other parameters, takes into account the future earnings of the company) of the life insurance business.

In the past, deals in the life insurance space have taken place at one to three times the embedded value of the life insurance business. While the valuation *vis-à-vis* industry norm is attractive, it is a tad lower than the implied value based on Nippon Life's earlier stake purchase in 2011.

In 2011, Nippon Life had bought 26 per cent stake in Reliance Life for ₹3,062 crore, pegging the valuation of the business at about ₹11,500 crore.

ICICI Bank's recent stake sale in ICICI Prudential Life Insurance Company, valued the company at ₹32,500 crore, which is about 2.4 times the embedded value of the life insurance business (as on March 2015).

In the general insurance space, the implied valuation of the companies are at about 14-16 times their estimated one-year forward earnings or at one to two times their one-year forward gross written premiums.

Max India's 23 per cent stake sale in Max Bupa will fetch ₹191 crore and values the health insurance business at ₹830 crore. This is close to 1.5-1.9 times its one-year forward gross written premium.

Recently, Sundaram Finance acquired an additional 26 per cent stake in Royal Sundaram, its non-life insurance joint venture with RSA Group, UK. The deal pegged the enterprise value of the insurance business at about ₹1,800 crore, which was about 1.1 times Royal Sundaram's current year gross written premium.

ICICI Bank's stake sale in the general insurance business about a month back valued the insurance company at ₹17,225 crore, which is over two times the FY15 gross premium.