

# Life Insurance: A Business of Risk Management

Motilal Oswal CEO track | Aug 24, 2020

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# What are life insurance companies supposed to do for their customers?

Competition reduces as we approach the core



Banks (>2100)



AMCs (>45)



Life Insurers (24)



Gold

.....and many more!

Risk of inflation & interest rate movements



Health / General Insurers (34)



Life Insurers (24)

Risk of falling ill



Life Insurers (24)

Risk of living too long

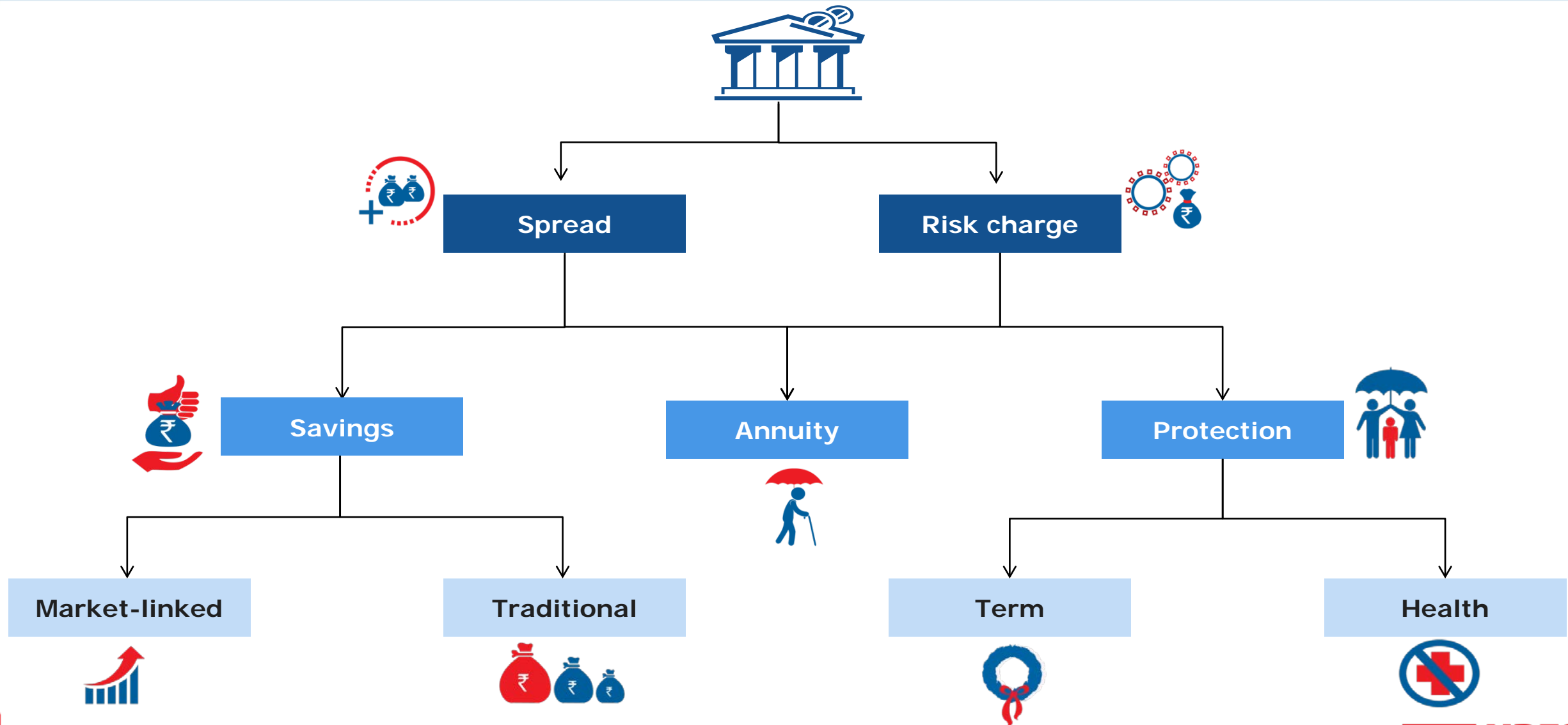


Risk of dying too early

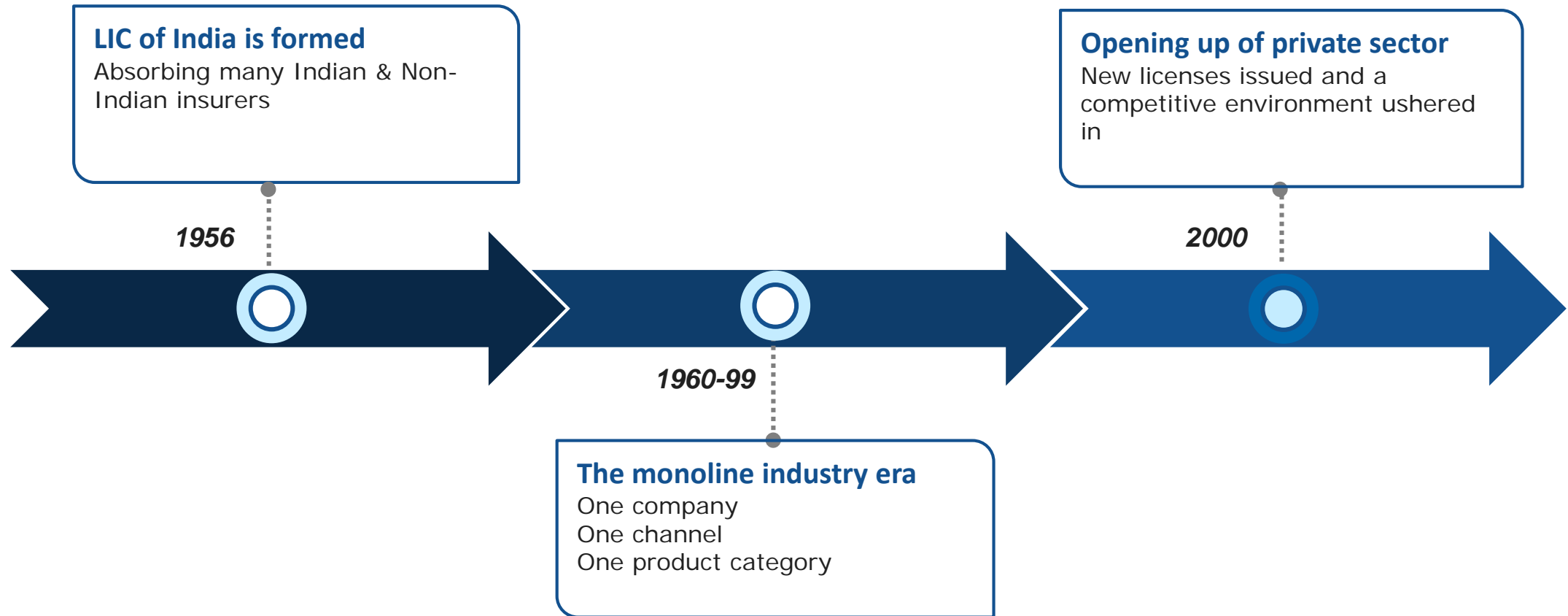


Cover a variety of risks that customers are exposed to

# And how are they expected to generate value?

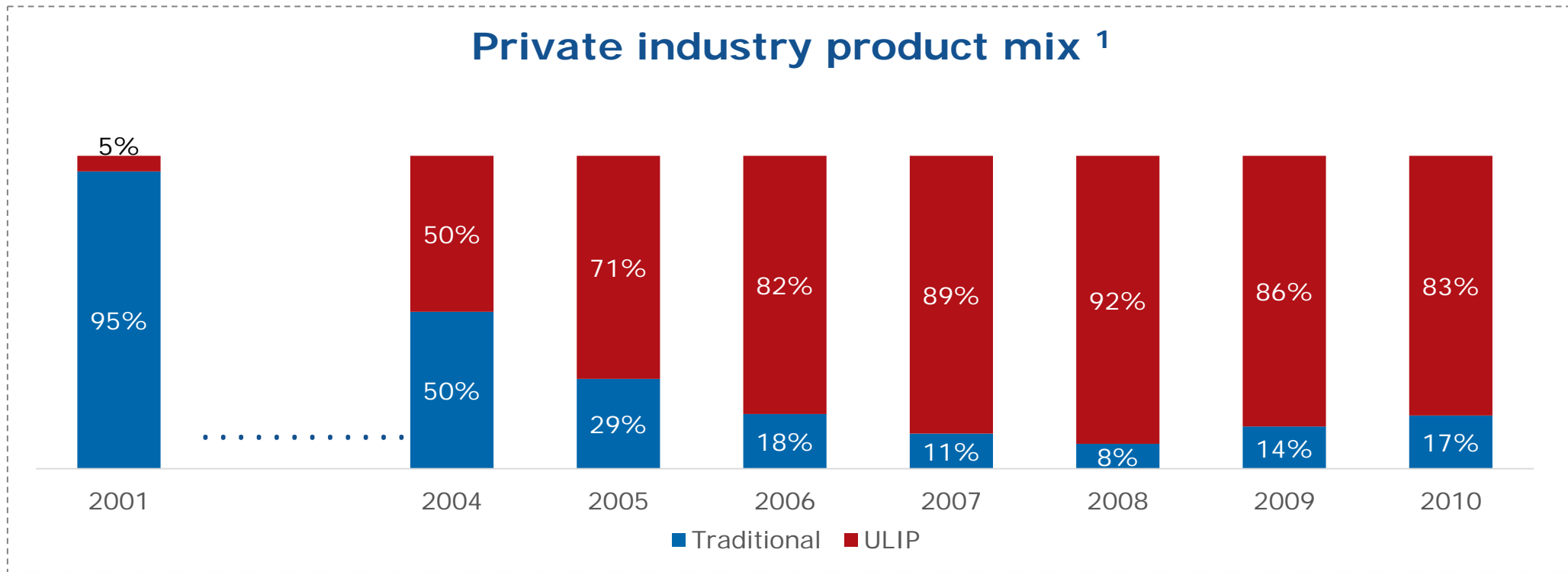


However, what we've seen in India till the early 2000s was mainly focused on mobilising savings



The end result being that a lot of savings were mobilised, but **without adequate risk transfer!**

# After trying to emulate LIC for a while, private insurers decided to find their own path... with ULIP



The new product category mobilised even more savings, while continuing to compete with other financial and non-financial products...

**But with no material risk transfer yet!**

*(While Total premium grew at a CAGR of ~26%, In-force sum assured grew slower by ~21% between FY06 and FY10)*

# At HDFC Life, we charted our independent, unique path introducing innovative products that helped address customer concerns



**Retirement** ✓  
Early commitment to the category

2006

2011-14

2015

2017-18

2019

2020



**Online sale of protection** ✓  
Popularized with our flagship *Click2Protect*



**Low charge ULIP** ✓  
Pioneered with *Click2Invest* \*



**Niche health concerns** ✓  
Addressed with products like *Cancer Care* \*



**Credit Life** ✓  
Leveraged a prominent white space



**Children's plans** ✓  
Expanded the category with our *Youngstar* brand  
**Women as a category** ✓  
Introduced concept with *Smart Woman* \*



**Long term solution with cash payouts** ✓  
Creatively structured via *Sanchay Par Advantage*



**Annuity deferment** ✓  
Introduced concept with *Pension Guaranteed Plan* \*



**Long term guarantees** ✓  
Advanced risk management with *Sanchay Plus* \*



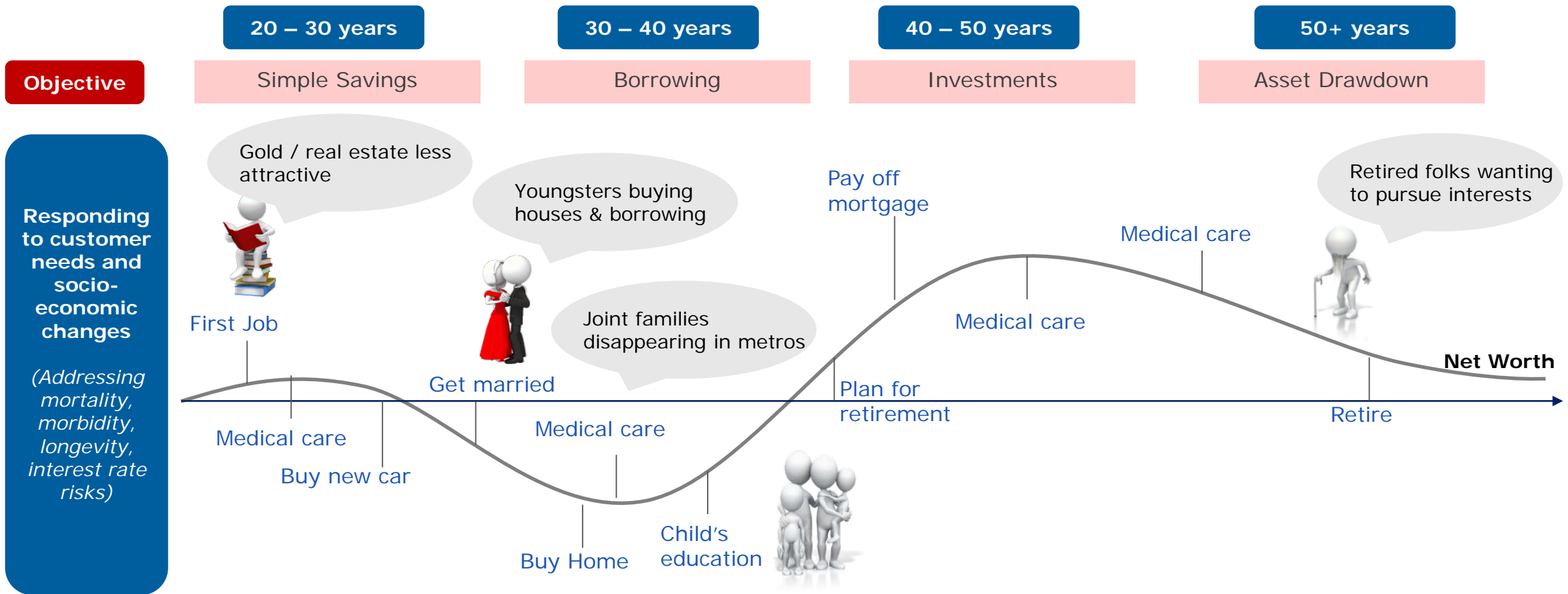
**Cost effective ULIP, even at higher ages** ✓  
Joint life concept innovatively used in *Classic One* \*



Risk transfer solutions

\* Industry firsts

# These propositions were directed at real customer needs across their lifespans



**Responding to customer needs and socio-economic changes**  
*(Addressing mortality, morbidity, longevity, interest rate risks)*

And our approach was validated with a number of our propositions becoming the industry norm!

# Our propositions over the years were all centered around the core of risk management



**Mortality**  
(Risk of dying early)

**Longevity**  
(Risk of living too long)



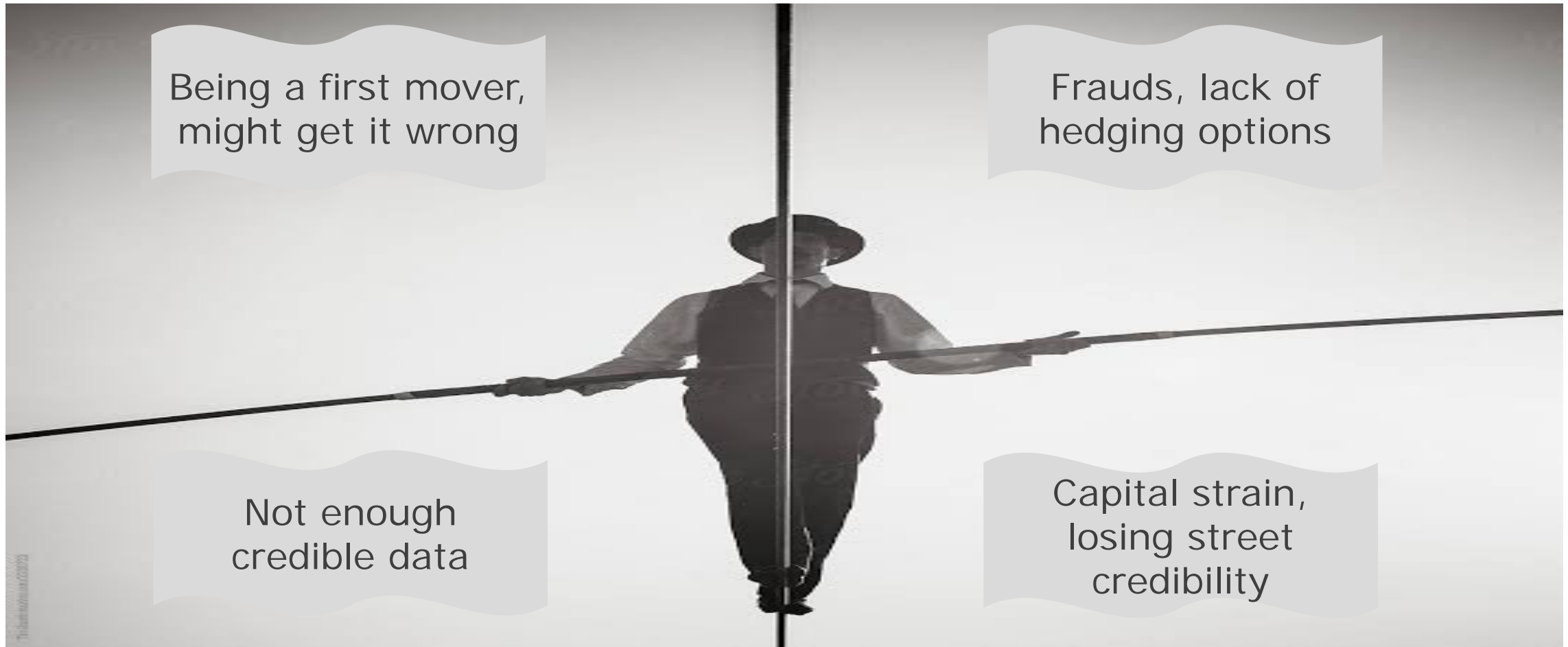
**Morbidity**  
(Related to illness / disease)

**Interest rate**  
(Related to investments,  
managing guarantees)



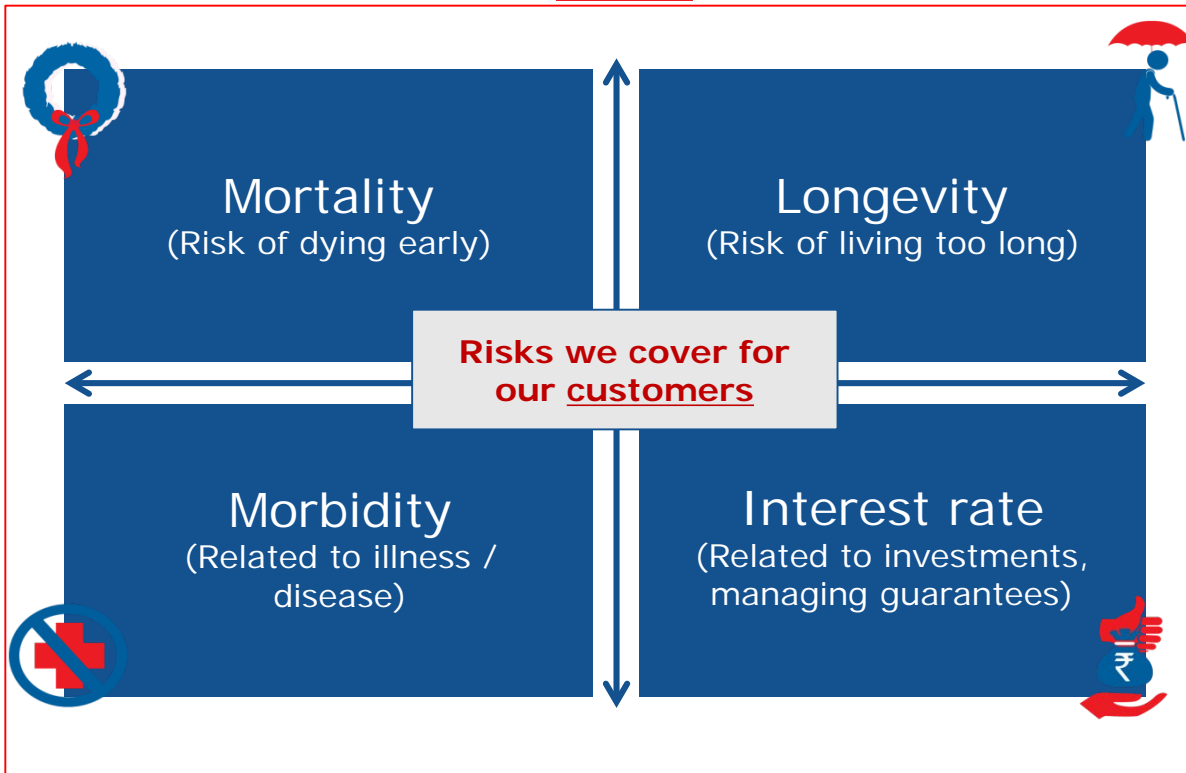


# But risk management can be tricky...

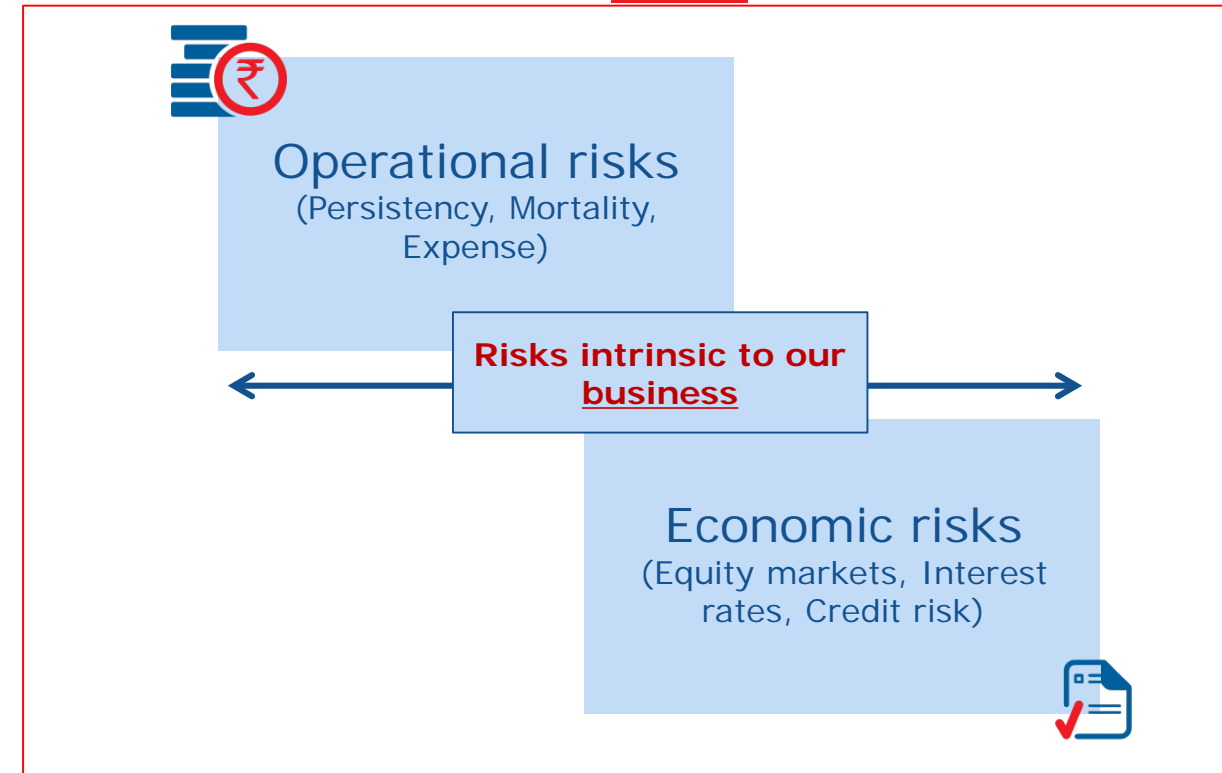


# So, what is the science behind our risk management that helps HDFC Life stay balanced on the rope?

1



2



# Risk management measures: Mortality & Morbidity

## 1 Reducing incidence of fraud & early claims

### Analytics and Data Enrichment

#### Risk+

AI-ML based risk models, rule engines, credit bureaus etc.

### No 'one size fits all' underwriting



Dynamic classification depending on profile, detailed medical & financial underwriting

### Regular portfolio review



To identify emerging trends, outliers and take corrective actions

### Industry collaboration



Mitigation from organised cartels

## 2 Limiting impact on profitability & solvency

### Reinsurance



Optimized reinsurance strategies for risk transfer

### Catastrophe agreement



To protect excess loss

### Proactive reserving



Well provisioned to prevent sudden shocks from current pandemic

## 3 Balancing price and risk

### Active re-pricing



Ongoing wherever required (mostly applies for Group schemes)

### Product boundary conditions



Gate criteria depending upon customer profile and sourcing channel

### Product design



Exclusions - pre-existing conditions, age limitations, suicide clause etc

## 4 Strong governance & audits @Partners

### TPAs & medical centers



Ensure process & quality adherence

### Distribution partners



Adherence to best practices and continuous monitoring of risk



# Risk management measures: Longevity & Interest rate

## 1 Natural hedges & Residual strategy

### Naturally hedged product lines



Protection and longevity; Unit linked and Non-par savings

### Limit quantum of AUM



Quantum of retail guaranteed products  
14% of AUM

### External hedging



Instruments such as FRAs, IRFs, Swaps, amongst others

### Reinsurance



Natural offset to mortality risk exposure

## 2 Product design & mix monitoring

### Prudent pricing assumptions



Interest rate and risk margins assumptions

### High Annuity ROPP business



Return of premium annuity products  
(>95% of annuity)

### Regular monitoring & repricing



Monitoring of interest rates and business mix;  
repricing to align benefits with prevailing rates

## 3 Prudent ALM approach

### Target cash flow matching



For Non-par savings + Group protection portfolio to manage non-parallel shifts & convexity

### Duration matching



Immunise overall portfolio to manage parallel shifts in yield curve

## 4 Validation

### Stress test scenarios

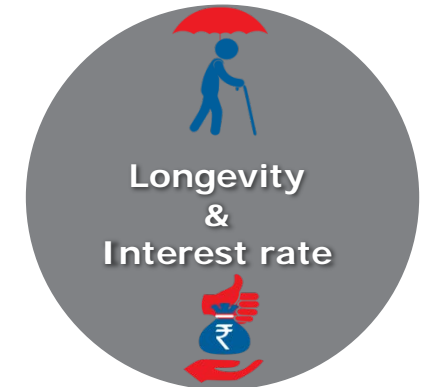


W.r.t. interest rates and persistency to identify impact on net asset-liability position

### External validation (by Milliman)



ALM strategy appropriate to meet policyholder liability cash flows & protect net asset-liability position



# Risk management measures: Operational and Economic

## 1 Operational risks

### Balanced product mix



To manage risk emerging from market volatility

### Mortality assumptions



Regular, granular review of experience vs assumptions, with corrective actions

### Digital renewals



~90% of renewal payments made digitally

### Cost control measures



Continuous measures to reduce variable and discretionary costs

### Conservative assumptions



To factor adverse market impact

### Continue to invest in Tech



To stay ahead of the curve & invest in future cost-saving technologies

## 2 Economic risks

### Conservative investment strategy



GSecs or AAA rated securities (~97%);  
Exposure to below AA assets 0.3% of AUM

### Regular monitoring



Ongoing investment portfolio review

### Calibrated approach to shareholders funds



Risk averse approach for investment in shareholders funds (~25% equity)

Business Risks



# In conclusion

Sensitivity of key risk factors (FY20)	Scenario	Change in VNB Margin	% Change in EV
Reference rate	▲ 1%	-0.7%	-1.2%
	▼ 1%	0.2%	0.6%
Equity Market movement	▼ 10%	-0.1%	-1.1%
Persistency (Lapse rates)	▲ 10%	-0.5%	-0.7%
	▼ 10%	0.6%	0.8%
Acquisition Expenses	▲ 10%	-3.9%	NA
	▼ 10%	3.9%	NA
Mortality / Morbidity	▲ 5%	-0.6%	-0.9%
	▼ 5%	0.6%	0.9%

Non par

VNB Margin	EV
-2.0%	-1.3%
1.7%	0.0%

## Key takeaways:

- We are in the business of risk transfer, which implies the need for strong risk management measures
- These measures, if executed in a calibrated manner, have the potential to generate significant value, while also meeting varied customer needs
- At HDFC Life, we follow a prudent approach along with regular assessment of assumptions vs actual experience
- As seen, this has resulted in lower sensitivity to EV and VNB, which is also validated by external agencies

Thank You

