



3R MATRIX

	+	=	-
Right Sector (RS)	✓	■	■
Right Quality (RQ)	✓	■	■
Right Valuation (RV)	✓	■	■

+ Positive = Neutral - Negative

Reco/View

Reco/View	Change
Reco: Buy	↔
CMP: Rs. 5,899	
Price Target: Rs. 7,500	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

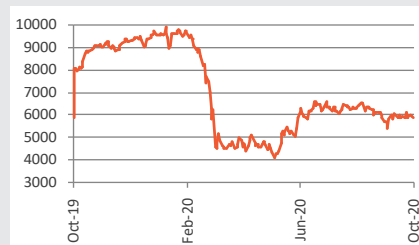
Company details

Market cap:	Rs. 93,758 cr
52-week high/low:	Rs. 10297/3985
NSE volume: (No of shares)	9.7 lakh
BSE code:	532978
NSE code:	BAJAJFINSV
Free float: (No of shares)	6.2 cr

Shareholding (%)

Promoters	60.8
FII	8.5
DII	6.8
Others	23.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	4.3	-7.5	24.8	-26.9
Relative to Sensex	-3.3	-13.9	-2.5	-30.7

Sharekhan Research, Bloomberg

Summary

- ♦ Bajaj Finserv's (BFS; holding company) results for Q2FY2021 were mixed; Income from operations came above estimates, but PAT declined by 19.9% y-o-y (below estimates).
- ♦ Lending business, Bajaj Finance Limited's (BFL) Q2FY2021 results were mixed. Operational numbers were in-line with estimates and asset quality improved sequentially. However, higher provisions (taken on prudent basis for Stage 1 and 2 loans) due to upfronting of provisions impacted PAT.
- ♦ Insurance subsidiary, BAGIC posted strong results, (helped by lower claims) in motor OD; BALIC's PAT declined (due to higher new business strain; absence of capital gains seen in Q2FY2020); but healthy APE growth is encouraging.
- ♦ The ~40% holding company discount to Bajaj Finserv's valuations make risk return attractive. We maintain our Buy rating with an unchanged SOTP-based PT of Rs. 7,500.

Bajaj Finserv's (BFS; holding company) results for Q2FY2021 were mixed. Income from operations grew by 5.8% y-o-y and 6% q-o-q to Rs. 15,052 crore (above estimates). However, net profit declined to Rs. 1,618 crore, down 19.9% y-o-y (below estimates). Lending business, Bajaj Finance Limited's (BFL) Q2FY2021 results were mixed. Operational numbers came in line with estimates and asset quality improved on a sequential basis, which were positives. However, higher provisions (taken on prudent basis for Stage 1 and 2 loans) due to upfronting of provisions resulted in PAT impact. For the insurance subsidiaries, Bajaj Allianz General Insurance (BAGIC) posted strong performance, and saw its PAT rising by 13% y-o-y, mainly due to lower costs. The claim ratio was at ~74% (down 80bps YoY), helped by lower claims in motor-OD segment. Consequently, the combined ratio fell to 97.4% from 102.8% in Q2FY2020. Bajaj Allianz Life Insurance (BALIC) saw its PAT decline by 53% y-o-y to Rs. 97.7 crore, mainly due to higher new business strain and lower capital gains (Rs. 46.8 crore in Q2FY2021 versus Rs. 102.1 crore in Q2FY2020). It recorded healthy APE growth of 17% during Q2FY2021, outperforming the industry (4%). In the individual rated mix, focus remained on non-PAR (i.e. high-margin business) with share increasing to 41% in Q2FY2021 (17% in Q2FY2020). With the upfronting of provisions in FY2021E, we expect BFL to enter FY2022E with a clean slate, high capitalisation, and strong balance sheet to be the growth facilitators. While near-term headwinds are present, sound fundamentals of BFL's business franchise are likely to sustain during present times as well. Bajaj Finance Limited (BFL) is well capitalised with a conservative leverage, and both BALIC and BAGIC have healthy solvency ratios and strong operating metrics, and have structural tailwinds to benefit them for the long term. We maintain our Buy recommendation on Bajaj Finserv with an unchanged SOTP-based price target (PT) of Rs. 7,500.

Key Positives

- ♦ Strong capital metrics across all subsidiaries, with BAGIC's solvency ratio robust at 307% and BALIC's solvency ratio at healthy 730%, with BFL Tier-1 capital at 26.64%.
- ♦ A lower claim ratio was seen in motor, crop, and health segments, which partly were benefitted by the pandemic.

Key Negatives

- ♦ There was tepid business traction for BFL during Q2; however, some recovery was seen in September in segments such as urban consumer business (B2B), which was at 72%, rural consumption business (B2B) at 91%, credit card originations at 73%, and E-Com at 75%. Auto business, however, continues to lag with only 54% of last year's volumes.

Our Call

Valuation: With the upfronting of provisions in FY2021E, we expect BFL to enter FY2022E with a clean slate, high capitalisation, and strong balance sheet as growth facilitators going forward. Notwithstanding the near-term headwinds, sound fundamentals of BFL's business franchise are likely to sustain during present times as well. BFL is well capitalised with conservative leverage and both BALIC and BAGIC have healthy solvency ratios and strong operating metrics, along with strong structural tailwinds to provide growth opportunities for them for the long term. At present, the ~40% holding company discount to Bajaj Finserv's valuations make risk return attractive. We maintain our Buy rating on the stock with an unchanged SOTP-based PT of Rs. 7,500.

Key Risks

Slowdown in consumer finance growth and worsening of economic parameters may pose risk to earnings growth and profitability.

SOTP Valuation

Particulars	Holding	Value per share (Rs.)	Rationale
Life Insurance	74.0%	1,301	1.6x FY23E EV
General Insurance	74.0%	1,117	16.5x FY23E PAT
Bajaj Finance	52.8%	7,600	4.3x FY23E BVPS
Less: Holding Co Discount	25%	2,519	
Total		7,500	

Source: Company; Sharekhan estimates

Key Concall Highlights

- ◆ **Business update:** Even though the lockdown has been lifted and economic activity has started to recover, risk levels remain elevated across businesses.
- ◆ **BAGIC:** BAGIC has gained ground in motor but is less active in high-end cars as pricing is lower. BAGIC is cautious on the group's general insurance due to high competitive intensity and less profitability in the segment. It is instead focusing on the retail segment.
- ◆ **BALIC:** BALIC continues to see slow group protection business traction. It is slow as banks and NBFCs have still seen lower disbursement. However, it is augmenting capacity and has hired 2,228 new agents during Q2.
- ◆ **Digital push:** Customers are still avoiding branch visit and, hence, are looking to increase sales via digital channels.
- ◆ **Provisions:** Provisions made in Q4FY2020 due to MTM losses have been recovered in H1FY2021.
- ◆ **BFL Subsidiary:** BFL has doubled its new loans book since Q1 helped by improved market conditions.
- ◆ **BAGIC Subsidiary:** Claims ratio declined to 74% from 75% in Q2FY2020. Claims experience was mixed with higher claims in health due to COVID and property (due to heavy rains), which were compensated by lower claims in the motor OD segment.
- ◆ **BALIC's new tie-up:** Started Karur Vysya banca relationship.
- ◆ **BAGIC crop insurance:** Has maintained its stance for some time and has been doing crop portfolio and will look to maintain the proportion.
- ◆ **BAGIC Health** – The company expects the claim ratio for COVID to drop and then rise; same is expected with motors. TP claims settlement is now low but will rise going forward. BAGIC has already provided sufficient for the COVID claims. Health market share is 4%, and COVID is difficult to estimate, but is expected to remain as per the market share.
- ◆ **BAGIC combined ratio:** Total health insurance claims paid higher. COVID claims are rising exponentially, but non COVID claims were down. However, they are moving up as patients are now going back to hospitals. Going forward, the combined ratio will again rise in line with industry COR reversal.
- ◆ **BALIC update:** Banca distribution and persistency etc. are shaping up well.
- ◆ **Micro insurance/pocket insurance:** The product is suited for uninsured people; or those who do not have adequate insurance cover.
- ◆ **Opex outlook for BAGIC:** BAGIC expenses in Q1 were lower due to travel etc. expenses not happening. Moreover, there were other aspects too. Manpower, they were adding people, but since H2FY2020 last year, BAGIC were rationalising their manpower, so were already in a lean shape. Also have introduced quarterly bonus structure versus annual bonus, which has created a high-performance culture. Moreover, office infrastructure too being rationalized in cities with multiple branches, also size of offices. In addition, Co have also re-negotiated rentals costs, due to these measures, costs have come down.
- ◆ **BALIC Opex:** Similar strategy to reduce structural costs. Started new channels such as Axis Bank, RBL Bank etc., which saw some cost impact.
- ◆ **Credit Life business:** The credit life business has come down. But as credit offtake is picking up, this should start improving.
- ◆ **Agency:** Growth and performance in agency channel was hit across the sector. The core reason behind this was that new advisors were not onboard due to people not taking the IRDAI exam.
- ◆ **Reserve for COVID claims:** The company has created extra reserve of Rs. 21 crore to meet the claims from COVID claims.
- ◆ **Protection demand:** Think by Q3, growth would normalise, but it will be still better than Q2. BALIC saw strong Q1 demand due to pent-up demand.
- ◆ **Axis Bank:** Bancassurance partnership with Axis Bank continues and is good for long-term products.
- ◆ **Persistency:** Life insurance persistency has dipped, which was as per expectations in UILPs segment.
- ◆ **New Investments:** New health platform has earmarked Rs. 100 crore investment. Trying to cover the entire healthcare requirements. By this platform, customers can get services such as doctor advice along with insurance coverage. Demand is strong for the platform.
- ◆ **Bajaj Financial Securities:** Reported profit for Q2. Clients have started to come, want to provide diversified services, but it is still at early stages.
- ◆ **BAGIC claims:** Trends in claims ratio are lower in motor OD, but frequency is returning to 80%-90% earlier levels. Once it resumes, one may see higher claims compared to pre-COVID levels in the initial period.

Results						Rs cr
Particulars	Q2FY21	Q2FY20	YoY (%)	Q1FY21	QoQ (%)	
Income from operations	15,049.6	14,221.9	5.8	14,190.1	6.1	
Other income	2.0	2.4	-14.8	2.0	-0.5	
Total Income from operations	15,051.6	14,224.2	5.8	14,192.1	6.1	
Expenses	12,894.9	11,597.2	11.2	11,623.7	10.9	
Employee Expenses	1,013.9	1,201.6	-15.6	993.6	2.0	
Finance Costs	2,340.2	2,313.2	1.2	2,395.2	-2.3	
Fees and commission expense	613.9	509.3	20.5	441.2	39.1	
Claims paid	2,802.9	2,965.6	-5.5	2,105.8	33.1	
Reinsurance ceded	1,715.2	1,598.7	7.3	773.0	121.9	
Net Change in Insurance / Investment Liabilities	1,884.7	1,352.5	39.3	2,457.4	-23.3	
Depreciation & Amtzn.	114.0	116.0	-1.7	125.4	-9.1	
Other Expenses	750.0	980.7	-23.5	650.3	15.3	
Provisions	1,660.1	559.7	196.6	1,681.8	-1.3	
Profit before tax	2,156.7	2,627.0	-17.9	2,568.4	-16.0	
Share in PAT of invst in associates	-0.1	-0.6	-85.5	-0.3	-64.0	
Tax	538.3	605.1	-11.0	645.9	-16.6	
PAT	1,618.3	2,021.2	-19.9	1,922.3	-15.8	

Source: Company; Sharekhan Research

Bajaj Finance (Consolidated)						Rs cr
Particulars	Q2FY21	Q2FY20	YoY %	Q1FY21	QoQ %	
Interest Income & Fees	6516.6	6321.5	3.1	6648.2	-2.0	
Interest and Other Charges	2358.1	2323.4	1.5	2497.6	-5.6	
Net Interest Income	4158.4	3998.0	4.0	4150.6	0.2	
Other Income	6.7	1.1	512.7	1.5	337.7	
Total Operating Income	4165.2	3999.1	4.2	4152.1	0.3	
Employee Expense	514.4	628.3	-18.1	537.5	-4.3	
Depreciation & Amortisation Expenses	71.5	70.7	1.1	84.2	-15.1	
Other Expenses	573.4	683.5	-16.1	535.0	7.2	
PPoP	3005.9	2616.7	14.9	2995.4	0.3	
Provisions and Loan losses	1700.4	594.2	186.2	1685.7	0.9	
PBT	1305.5	2022.4	-35.5	1309.7	-0.3	
Tax Expense	340.6	516.1	-34.0	347.4	-2.0	
Profit After Tax	964.9	1506.3	-35.9	962.3	0.3	

Source: Company; Sharekhan Research

Bajaj Allianz Life Insurance						Rs cr
Particulars	Q2FY21	Q2FY20	YoY %	Q1FY21	QoQ %	
Gross written premium	2,677.0	2,235.0	19.8	1,700.0	57.5	
New business premium	1,372.0	1,235.0	11.1	2,432.0	-43.6	
Renewal premium	1,305.0	1,000.0	30.5	958.0	36.2	
Shareholders Profit	131.0	208.0	-37.0	182.0	-28.0	
Transfer from policyholder account	-33.0	-1.0	3,200.0	-52.0	-36.5	
Profit / (Loss) after tax	98.0	207.0	-52.7	130.0	-24.6	

Source: Company; Sharekhan Research

Bajaj Allianz General Insurance						Rs cr
Particulars	Q2FY21	Q2FY20	YoY %	Q1FY21	QoQ %	
Gross Written Premium	4,156.0	4,279.0	-2.9	2,289.0	81.6	
Net Earned Premium	1,986.0	2,131.0	-6.8	1,818.0	9.2	
Underwriting Result	29.0	-91.0	NA	175.0	NA	
Investment & other Income	414.0	462.0	-10.4	352.0	17.6	
Profit before tax	443.0	371.0	19.4	527.0	-15.9	
Profit after tax	332.0	294.0	12.9	395.0	-15.9	

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector view - Green shoots in the economy are encouraging

Retail players have a large market to grow post the unlocking of the economy. Banks are reporting incremental pickup in credit demand, especially in retail and consumer segments. Leading indicators indicate recovery in economic activity, which will be a positive. Credit Bureau information is expected to be fully onstream by November, which should further aid volume momentum for lenders such as BFL. We believe the retail and consumer lending segments have a long structural growth runway available to them as India's credit delivery diversifies and penetration increases. We believe the insurance sector has a huge growth potential in India with a large protection gap, expanding per capita income, retiral needs, as well as greater awareness/acceptance of financial security products (accelerated by the pandemic) etc., which are key long-term growth drivers for the sector. In this backdrop, we believe strong players such as BALIC and BAGIC, armed with the right mix of products, services, and distribution (augmented by stable Bancassurance partnerships) are likely to gain disproportionately from the opportunity.

■ Company outlook - Subsidiaries' sound fundamentals will allow play on long-term opportunities

Notwithstanding the near-term challenges, all of BFS subsidiaries are well placed. BFL stands out with its strong balance sheet, comfortable liquidity, high credit ratings, and well-matched asset-liability management position. It is also well-capitalised as well and has a strong provision buffer that will help it cushion the impact on its balance sheet and profitability. BFL has modularity built across various cost items, including salary costs, which will provide BFL a reasonable control over costs. We believe insurance companies are sensitive to bond downgrades (for corporate bonds, etc.), for their investment portfolios and investment earnings. However, pickup on month-on-month basis in premiums is encouraging, reflecting a rapid normalisation aided by operational tweaks and agility in technology adoption. While near-term headwinds persist, the sound fundamentals of business franchises are likely to sustain during these tough times.

■ Valuation - Risk reward favourable, Maintain Buy with a PT of Rs. 7,500

Bajaj Finance Limited (BFL) is well capitalised with a conservative leverage and both BALIC and BAGIC have healthy solvency ratios and strong operating metrics, along with strong structural tailwinds to provide growth opportunities for them for the long term. At present, the holding company discount to the Bajaj Finserv's valuations is at ~40%, which we believe makes risk return attractive. We maintain our Buy rating on the stock with an unchanged SOTP-based PT of Rs. 7,500.

About company

Bajaj Finserv (BFS) is a diversified financial services group with a pan-India presence in life insurance, general insurance, and lending. It is the holding company for Bajaj Finance Ltd (BFL) and BFS' shareholding in BFL (Bajaj Finance Ltd.) was 54.81%. It also holds 74% each in Bajaj Allianz General Insurance (BAGIC, amongst top 5 private general insurer in India in terms of Gross Premium) and Bajaj Allianz Life Insurance (BALIC, is among top 5 Pvt sector Life insurers in India on new business basis).

Investment theme

Bajaj Finserv is a financial conglomerate having presence in the financing business (vehicle finance, consumer finance and distribution) via Bajaj Finance (BFL) and is among the top players in the life insurance (BALIC) and general insurance (BAGIC) segments. We expect BFL to maintain its loan book trajectory in the long term as and when business environment normalises. Near term challenges are mostly related to disruption of normal business due to the pandemic which have impacted business across the economy. However, for BAGIC and BALIC, we find their healthy operating metrics and profitability positive. The insurance arms are focusing on strengthening distribution channel and profitability and are likely to emerge as attractive businesses over time.

Key Risks

Slowdown in consumer finance growth and worsening of economic parameters may pose risk to earnings growth and profitability.

Additional Data

Key management personnel

Mr. Sanjiv Bajaj	Managing Director & CEO
S Sreenivasan	CFO
V. Rajagopalan	President - Legal
Mr. Ganesh Mohan	Group Head – Strategy
Mr. Ajay Sathe	Head – Group Risk Management
Rajeev Jain	Managing Director – Bajaj Finance Limited

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Jamnallal Sons Pvt Ltd	9.64
2	Jaya Hind Industries Ltd	3.85
3	Maharashtra Scooters Ltd	2.34
4	Bajaj Niraj Ramkrishna	1.72
5	Bajaj Sevashram Pvt Ltd	1.5
6	Life Insurance Corp of India	1.42
7	Bachhraj & Co Pvt Ltd	1.27
8	Axis Asset Management Co Ltd/India	1.17
9	SBI Funds Management Pvt Ltd	0.88
10	Vanguard Group Inc/The	0.87

Source: Bloomberg

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Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and deteriorating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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