Max Financial Services

Q2 results beat COVID odds

Banks & Finance | Sharekhan code: MFSL | Result Update

3R MATRIX + = -

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

\+ Positive = Neutral - Negative

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 600**	
Price Target: **Rs. 750**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Company details

Market cap:	Rs. 16,183 cr
52-week high/low:	Rs. 645/280
NSE volume: (No of shares)	14.9 lakh
BSE code:	500271
NSE code:	MFSL
Free float: (No of shares)	20.9 cr

Shareholding (%)

Promoters	22.3
FII	33.1
DII	30.4
Others	14.2

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-2.0	6.7	27.8	45.8
Relative to Sensex	-6.4	1.3	9.9	46.6

Sharekhan Research, Bloomberg

Summary

- Max Financial Services (MFS) posted strong numbers for Q2FY2021, with strong Individual APE growth, encouraging growth in embedded value (EV) with market share gains (despite challenges due to COVID-19)
- Value of New Business (VNB) written during H1FY21 grew by 20% y-o-y, while New Business Margin (NBM) expanded by 320 bps y-o-y to 24.2%, helped by a shift in product mix towards NPAR- Savings and Protection products. EV was at Rs 11,047 Cr., with RoEV at 17.5%.
- We believe the Indian insurance sector has a long growth runway; and Max Life, with strong metrics, stable bancassurance partnership with Axis Bank, etc is well-placed to benefit from growth opportunities.
- Max Financial is available a reasonable valuation of 1.7x / 1.5x FY2022E / FY2023E MCap / EV; We maintain Buy with a revised PT of Rs. 750.

Despite challenges in collections due to COVID-19, Max Financial Services (MFS) posted strong results for Q2FY2021, with strong individual growth of 11% y-o-y in APE and encouraging growth in embedded value (EV). It also gained market share. Max Life Insurance (MLIC, where MFS has a 72.5% shareholding) gain 162 bps to reach a 10-year high market share of 11% in the private segment in H1FY21. Max Life reported a market consistent embedded value (MCEV) of Rs. 11,047 crore, in H1FY21, with an Operating Return on Embedded Value (RoEV) of 17.5%. The Value of New Business (VNB) written during H1 FY21 stood Rs. 438 crore, growing by 20% year-on-year, while new business margin (NBM) stood at 24.2%, expanded by 320 bps over last year, arising from shift in product mix towards NPAR- Savings and protection products. Individual protection grew by 78% year-on-year and penetration increased to 12% in H1FY21 as compared to 7% in H1FY20. Renewal premium grew by 16% to Rs. 4,789 crore. In this period, Max Life's assets under management (AUM) stood at Rs. 77,764 crore, growing 19% y-o-y. New business premiums (on an APE basis) amounted to Rs 1815 crore, up 5% y-o-y which indicates improving traction. Moreover, the individual sum assured of new business clocked grew by 40% due to strong growth in protection business. MLIC's relation with its bancassurance partner Axis Bank now seems more stable; and the recent approval from regulator (albeit with tweaks) further clears the way and will be seen as a positive. Going forward, as operating leverage benefits kick in, and lesser pressure on investing in own channels will support margins, which will help in present times of impacted sales and volatile markets. We believe that the Indian insurance market has significant growth opportunities; and MLIC, with its strong brand and stable bancassurance partnership, is well-placed to ride over medium term challenges. We believe strong business fundamentals and current valuations (at a significant discount to peers) make risk-return favourable for MFS. We have fine-tuned FY2021E and FY2022E and introduce FY2023E estimates with this note. We maintain our Buy rating on the stock with a revised price target (PT) of Rs. 750.

Key positives

- The 13th-month persistency ratio for Q2 FY2021 was unchanged at 83% from FY2020 levels, which indicates good customer retention and effective client communications.
- EV grew 12% driven by growth in VNB and quality of in-force business.
- New Business Margins (actual cost) increased to 24.2%, up 320 bps y-o-y and also from 21.6% in FY20. NBMs improved due to a higher share of protection products in the mix.

Key negatives

- RoEV at 17.5% was lower y-o-y primarily due to management expectations of lower unwinding driven by a fall in interest rates.

Our Call

Valuations: At CMP, Max Financial is available at 1.7x / 1.5x FY2022E / FY2023E MCap / EV (considering MFS' present stake in Max Life). Valuations appear reasonable and are still at a discount as compared to some bank-owned life insurance companies. The approval by the RBI for deal with Axis Bank is will help pave the way for achieve the very likely fruition of the deal. On a performance basis, the insurance sector has been progressing well, with a consistent 13-15% growth on the normal rate and improving recovery post the lockdown opening up. Max has strengths on protection (20% of APE as on H1 FY21) and Non-PAR (31% of APE as on H1 FY21) segments which we believe are likely to see customer preference in the medium term, which augurs well for MLI. Max Life generates healthy ROEV (17.5% in H1 FY21) and has sufficient capital (solvency ratio of 207%; no need for dilution in near term) and hence its strong fundamentals make it a strong candidate for potential re-rating as outlook improves further. We have fine-tuned FY2021E and FY2022E and introduce FY2023E estimates with this note. We maintain our Buy rating on the stock with a revised price target (PT) of Rs. 750.

Key risk

A slowdown in business operations and higher slippages/bond downgrades due to the economic weakness may impact earnings outlook.

Valuation Rs cr

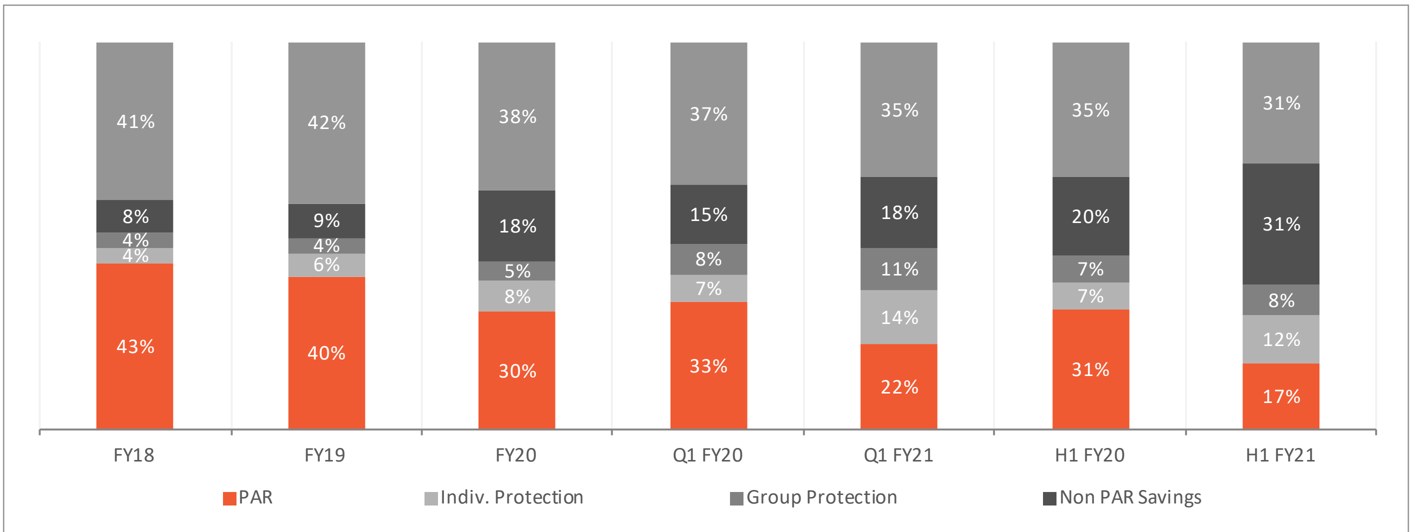
Particulars	FY19	FY20	FY21E	FY22E	FY23E
Total Premium	14,575	16,183	18,523	21,270	24,429
New Business Premium	3,950	4,345	5,171	6,179	7,384
VNB Margin (%)	21.7	21.6	19.0	20.0	20.0
Embedded Value	9,257	9,977	11,450	13,088	14,929
EV / Share (Rs)	248	267	308	352	402
MCap / Prop EV (x)	2.5	2.3	2.0	1.7	1.5

Source: Company; Sharekhan estimates

Robust operating performance; non-PAR and protection products growing strongly

Consolidated revenues grew by 45% y-o-y, while Consolidated PAT stood at Rs. 263 crore, up 121% y-o-y. Profit growth was aided by higher investment income, lower claims and tax refunds. Max Life recorded the highest H1 market share of 11% in last 10 years, which grew by 4% against Private Players' de-growth of 11% y-o-y. Max Life's growth was driven by e-Commerce and Bancassurance sales growth of 49% and 8% respectively. New business sum assured written by Max Life is among the highest in the industry with growth of 40%.

Balanced Product mix



Source: Sharekhan Research

Max Life has increasingly built balanced product and channel mix and the business is majorly shifting towards protection and savings products where Max Life is strong, which makes the company well placed going forward as well. The Increase in NPAR savings owing to launch of new non par product

Axis deal progressing well, RBI nod received

The Reserve Bank of India (RBI) has advised Axis Bank to acquire up to a 9% stake directly in Max Life and up to a 3% stake through its subsidiaries. It has also given the lender the right to acquire an additional stake of up to 7% stake in one or more tranches in Max Life. Post the RBI's nod, the IRDAI application is under progress. So far, shareholders, the Competition Commission of India (CCI) and stock exchanges have given their approval; and approvals from the DEA & IRDAI are underway.

We believe that regulatory approval is important, and although the deal structure is altered, in effect the Axis Bank along with its subsidiary can hold up to a 19% stake in Max. The bancassurance relationship is important to both partners, and a regulatory clearance to the deal is expected to be viewed positive for Max Financial.

The proposed joint venture will help Max Life compete with other leading bank-backed insurers that have stable bancassurance tie-ups with top banks to cross-sell policies at branches.

Results Rs cr

Particulars	Q2 FY21	Q2 FY20	YOY (%)	Q1 FY21	QoQ (%)
Total Revenue from Operations	7,020.1	4,685.9	49.8	5,517.3	27.2
Other Income	0.3	0.1	188.9	12.7	(98.0)
Total Income	7,020.4	4,686.0	49.8	5,530.0	26.9
Finance Cost	0.1	0.1	(37.5)	0.1	(37.5)
Impairment of Financial Instruments	(56.2)	4.1	NA	2.0	NA
Employee expenses	13.2	10.6	25.4	9.3	41.8
Depreciation and Amortization	1.2	0.1	750.0	1.3	(9.2)
Legal & Professional expenses	5.1	12.3	(58.3)	5.2	(1.2)
Policyholder's expenses of Life Insurance Ops	6,954.5	4,578.7	51.9	5,342.3	30.2
Other Expenses	6.7	8.5	(21.3)	6.4	4.5
Total Expenses	6,924.6	4,615.1	50.0	5,366.6	29.0
Profit before Tax	**95.5**	**70.8**	**34.9**	**150.7**	**(36.6)**
Total Tax	**14.5**	**6.5**	**124.0**	**(30.8)**	**NA**
PAT (for the period)	81.1	64.4	25.9	181.5	(55.3)

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Long runway for growth for Insurance in India, opportunity for strong players to gain

We believe that the Indian insurance sector has a huge growth potential with facilitating factors like a large gap in protection products (under-insured), expanding per capita income, etc (savings products), increasing life expectancy (retirement products) being key structural long-term growth drivers. India has high under-insurance in life insurance premiums at about ~2.8% of GDP in 2020, as compared to the world average of over 3%. India has only ~92% of the protection gap (addressable population, which doesn't have insurance coverage), which is estimated to be at $8.56 trillion. Even though the share of life insurance funds in household financial savings has increased from 20.3% in FY2017 to 23.3% in FY2018, we believe it has long way to go when compared to International peers. We believe that the Indian life insurance industry to have strong growth potential due to above-mentioned factors. In this backdrop, we believe strong players such as Max Life Insurance, armed with the right mix of products, services, and distribution mix, backed by strong and stable bancassurance partnerships and stable persistency levels are well placed to gain disproportionally from the opportunity.

■ Company Outlook – Strong metrics; sustainable growth business

MFS is effectively building an attractive insurance franchise, characterised by a multi-channel distribution network built upon a conservatively underwritten insurance business. We believe that the company's strategy to achieve a balanced product mix and focus on non-PAR savings with the protection segment will be margin-accretive and is achievable. We view that cost management, re-balancing of product mix, and further diversification of distribution channels are key levers for profitability improvement and also add to business sustainability. Going forward, as operating leverage benefits kick in, due to lesser pressure on investing in own channels, there will be positive support for margins, which will help in the ongoing times of impacted sales and volatile markets. Though the lockdown affected premium recovery and incremental sales growth for insurers, including Max Life, companies, especially private players are seeing impressive bounce-back in revenues, which is encouraging. MLIC, with its strong brand image and riding on stable bancassurance partnership (further strengthened with the gradual formalisation of deal with Axis Bank), appears well placed on most parameters to ride over medium-term challenges.

■ Valuation – We recommend a Buy with a Price Target of Rs 750

At CMP, Max Financial is available at 1.7x / 1.5x FY2022E / FY2023E MCap / EV (considering MFS' present stake in Max Life). Valuations appear reasonable and are still at a discount as compared to some bank-owned life insurance companies. The approval by the RBI is significant and will help pave the way for achieve the very likely fruition of the deal and removes any overhang. On a performance basis, the insurance sector has been progressing well, with a consistent 13-15% growth on the normal rate and improving recovery post the lockdown opening up. Max has strengths on protection (20% of APE as on H1 FY21) and Non-PAR (31% of APE as on H1 FY21) segments which we believe are likely to see customer preference in the medium term, which augurs well for MLI. Max Life generates healthy ROEV (17.5% in H1 FY21) and has sufficient capital (solvency ratio of 207%; no need for dilution in near term) and hence its strong fundamentals make it a strong candidate for potential re-rating as outlook improves further. We have fine-tuned FY2021E and FY2022E and introduce FY2023E estimates with this note. We maintain our Buy rating on the stock with a revised price target (PT) of Rs. 750.

About company

MFS is the holding company (holds ~72.5% share) of Max Life Insurance (MLI), a private life insurance company. MLI is a joint venture with a Japanese insurance partner, which holds 25.5% share of MLI, and is a global leader in life insurance. MLI offers comprehensive long-term savings, protection, and retirement solutions through its high-quality agency distribution and multichannel distribution partners. The company has a strong customer centric approach focused on advice-based sales and quality service delivered through its superior human capital. It is the fourth largest private life insurance player in India with ~11% Private market share.

Investment theme

MFS holds MLI, which is among the leading private sector insurers. It has gained critical mass and enjoys strong operating parameters in the industry. MLI had delivered strong performance on both new and renewal business over the years. As the insurance sector is showing signs of sustained growth potential, the company's well-diversified product mix and a strong distribution channel augur well and will help sustain healthy growth in premiums and profits. Strong focus towards customer measures has helped to deliver superior performance across parameters and will continue to remain an important differentiator.

Key Risks

A slowdown in business operations and higher slippages/bond downgrades due to the economic weakness may impact earnings outlook.

Additional Data

Key management personnel

Mr Mohit Talwar	Managing Director
Mr V Krishnan	Company Secretary
Mr Jatin Khanna	Chief Financial Officer
Mr Archana Pandey	Senior Director - Corporate Affairs

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	MONEYLINE PORT INV LTD	6.7
2	Mirae Asset Global Investments Co	6.1
3	HDFC Asset Management Co Ltd	4.1
4	Reliance Capital Trustee Co Ltd	3.7
5	ICICI Prudential Asset Management	3.5
6	New York Life Insurance Co	3.4
7	Baron Capital Inc	3.4
8	BARON EMERGING MRKTS FUND	3.3
9	Kotak Mahindra Asset Management Co	3.1
10	WF ASIAN SMALLER CO FUND	3.1

Source: Bloomberg

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 detoriating 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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