Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Max Financial Services

Strong performance, robust outlook

Banks & Finance	Sharekhan code: MFSL	Result Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 738**	
Price Target: **Rs. 1000**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

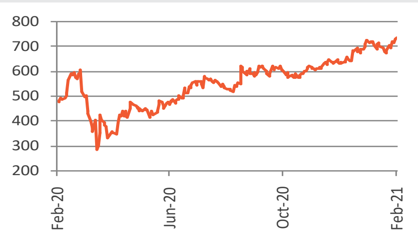
Company details

Market cap:	Rs. 25,464 cr
52-week high/low:	Rs. 752/280
NSE volume: (No of shares)	16.1 lakh
BSE code:	500271
NSE code:	MFSL
Free float: (No of shares)	28.5 cr

Shareholding (%)

Promoters	17.3
FII	20.3
DII	54.7
Others	7.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	0.3	17.7	37.8	52.4
Relative to Sensex	-5.0	-2.9	3.4	27.1

Sharekhan Research, Bloomberg

Summary

- Q3FY21 results were strong; Max Life Insurance (MLI) clocked robust 37% growth in VNB, driven by strong 22% growth in APE, and a robust 270 bps expansion in VNB margin to 26.5%.
- We see operating leverage benefits kicking in going ahead, as improving business mix would support VNB margins; we believe Indian insurance market has attractive growth opportunities
- Stock available at 2.1x / 1.8x FY2022E / FY2023E EVPS; valuations are reasonable and are still at a discount to some bank-owned life insurance companies.
- Deal with Axis positive and will provide re-rating boost; we maintain a Buy rating with a revised price target (PT) of Rs. 1,000.

Q3FY21 results were strong with subsidiary Max Life Insurance (MLI) reporting strong 37% growth in VNB, driven by a strong 22% growth in APE, significant reduction in over-runs and a robust 270 bps expansion in VNB margin to 26.5%. Moreover, a shift in product mix towards non-par savings (forms 36% from 19%) was the key driver behind the strong margin performance. Subsidiary Max Life Insurance (MLI) reported individual adjusted sales growth of 21% and the company maintained its private market share of 11% and VNB growth of 37% in 9MFY21. Max Life Insurance reported gross written premium of Rs. 4,629 crore, which was up 19% YoY while the Shareholders' PAT of Rs. 220 crore, which was up 43% YOY, due to higher investment income and reserve release due to hedging of in-force Protection business. Strong Individual adjusted sales were recorded at Rs. 1210 crore in Q3FY21, being 21% higher than last year, spurred by a 27% growth in bancassurance channel sales, which in turn was a result of a 32% increase in Axis Bank sales. Overall bancassurance contribution has increased from 65% in FY20 to 70% in 9MFY21 mainly as the agency channel was subdued due to pandemic during 9M FY21. Hence, while proprietary channel sales grew by 9%, led by a better show in the agency channel. The E-Commerce channel grew by 54% year-on-year due to protection tailwinds, leading claims paid ratio and a competitive price.

VNB margins beat expectations, expanding to 25.9% in 9MFY21, posting strong growth, as against from 21.6% in FY20, driven by an increase in protection and non-PAR savings mix. Max Life has been consistently delivering APE growth throughout the pandemic and that coupled with the sharp VNB expansion has led to 37% y-o-y VNB growth in 9MFY21. Going forward, we see operating leverage benefits kicking in, helped by improving business mix which will help support VNB margins. 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 gain market share and growth. We believe that strong business fundamentals and current valuations (at a significant discount to peers) make risk-return favourable for MFS. We have revised our estimates and target multiples. We maintain a Buy rating on the stock with a revised price target (PT) of Rs. 1,000.

Key positives

- VNB stood at Rs. 788 crore; up 37% y-o-y. The New Business Margin (NBM) expanded by 490 bps to 25.9%.
- EV grew 18% to Rs 11,723 crore driven by growth in VNB and quality of in-force business.

Key negatives

- RoEV at 18% for 9M FY2021, lower than 18.4% a year ago primarily due to lower unwind.

Our Call

At CMP, the stock is available at 2.1x / 1.8x FY2022E / FY2023E EVPS (value per share for Max Financial). Valuations appear reasonable and are still at a discount as compared to some bank-owned life insurance companies. However, Max's VNB margins and RoEV are now best-in-class in the industry, with high solvency ratios and completion of the Axis Bank deal (IRDA approval pending), we believe will likely drive a big re-rating boost for Max Financials (as it removes overhang on the relationship with its dominant bancassurance partner). MLI's strong agency force is a key advantage against competition as it allows for closer and more complex product sales. We have revised our earnings estimates and the target multiples for Max Financial. We have maintained our Buy rating on the stock with revised price target of Rs. 1,000.

Key Risks

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
Net Earned Premium	14,418	15,968	18,375	21,236	24,527
Net Profit	555.2	539.6	540.9	685.1	851.3
EPS (Rs)	2.9	2.8	2.8	3.6	4.5
ROA (%)	0.9	1.0	0.6	0.7	0.8
ROE (%)	20.3	20.2	18.0	19.3	20.5
EV / Share (Rs)	48	52	62	74	87
NBV / Share (Rs)	4.3	4.7	6.2	7.3	8.4
P / EV (x)	16.2	15.0	12.5	10.5	8.9
Dividend Yield (%)	0.3	0.3	0	0.1	0.1

Source: Company; Sharekhan estimates

Deal with Axis Bank progressing well, final approval awaited

Our interaction with the management indicated that the MLIC's deal with Axis Bank is progressed well (new structure proposes 9% stake sale to Axis Bank, 3% stake sale to Axis Bank's subsidiaries and further 7% stake sale to these subs) and may be expected in the near term, which we believe will be positive. Even though the deal is likely to be long ended, the company is awaiting final regulatory approval for the transaction from IRDAI, which will be the final approval required. The deal stabilises the relationship. The Axis Bank channel provides a significant 50-60% of the new business sales for MLI and is an important part. Hence the formalising of the relationship removes the overhang and therefore will be positive for valuations re-rating potential for the stock.

Margins perform well, expected to sustain

Max Life Insurance (MLI) reported strong 65% growth in Q3FY21 post-overrun VNB, which was driven by strong 22% growth in APE, significant reduction in over-runs, and a robust 270 bps pre-overrun VNB margin expansion to 26.5%. Also, shifting product mix towards non-par savings (at 36% versus 19% earlier) was the key driver behind strong margin performance.

The management indicated that owing to operating leverage and improving business mix, VNB margins are likely to hold at present levels, for the long term. During the year, there was some drag on the ULIP offtake, due to market movements and also issues with bancassurance partner (internal issues of Yes Bank), which are now over. Currently, the ULIP traction is improving (generally at a lag of six months to market performance).

Hence going forward, the 13th month persistency is also expected to improve in FY22E. Going froward, the management indicated a balanced mix of business with Non PAR at 30-35% of APE, while protection is at 35-40% of the APE.

Agency channel to improve contribution as business normalises

Strong individual adjusted sales were recorded at Rs. 1210.6 crore in Q3FY21, being 21% higher than last year, spurred by a 27% growth in bancassurance channel sales, which in turn was a result of a 32% increase in Axis Bank sales. Overall bancassurance contribution has increased from 65% in FY20 to 70% in 9MFY21 mainly as Agency channel was subdued due to pandemic during 9MFY21. Hence, while proprietary channels sales grew by 9% in Q3FY21, led by the agency channel's performance. The e-Commerce channel grew by 54% year-on-year due to protection tailwinds, higher claims paid ratio and competitive pricing.

Results Rs cr

Particulars	Q3FY21	Q3FY20	y-o-y (%)	Q2FY21	q-o-q (%)
Total Revenue from Operations	8,989.7	5,365.7	67.5	7,020.1	28.1
Other Income	0.6	0.1	866.7	0.3	123.1
Total Income	8,990.3	5,365.7	67.5	7,020.4	28.1
Expenses					
Finance Cost	0.1	0.1	33.3	0.1	60.0
Impairment of Financial Instruments	(1.2)	2.1	NA	(56.2)	NA
Employee expenses	13.2	15.5	(14.6)	13.2	-
Depreciation and Amortization	1.4	2.0	(31.5)	1.2	15.1
Legal & Professional expenses	4.3	9.4	(54.4)	5.1	(16.6)
Policyholder's expenses of Life Insurance Ops	8,686.3	5,152.8	68.6	6,954.5	24.9
Other Expenses	6.7	6.7	(0.3)	6.7	(0.1)
Total Expenses	8,710.7	5,188.5	67.9	6,924.6	25.8
Profit before Tax	279.5	177.3	57.7	95.5	192.7
Total Tax	52.4	29.7	76.6	14.5	262.7
PAT (for the period)	227.1	147.6	53.9	81.1	180.2

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 ~~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 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 as 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 private players armed with the right mix of products, services, and distribution mix, backed by strong and stable bancassurance partnerships are likely 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. Going froward, the management indicated a balanced mix of business with Non PAR at 30-35% of APE, while protection at 35-40% of APE. 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. Despite challenges, sales growth for Max Life 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 near formalisation of deal with Axis Bank), appears well placed on most parameters.

■ Valuation - Maintain Buy with a PT of Rs. 1,000

At CMP, the stock is available at 2.1x / 1.8x FY2022E / FY2023E EVPS (value per share for Max Financial). Valuations appear reasonable and are still at a discount as compared to some bank-owned life insurance companies. However, Max's VNB margins and RoEV are now best-in-class in the industry, with high solvency ratios and completion of the Axis Bank deal (IRDA approval pending), we believe will likely drive a big re-rating boost for Max Financials (as it removes overhang on the relationship with its dominant bancassurance partner). MLI's strong agency force is a key advantage against competition as it allows for closer and more complex product sales. We have revised our earnings estimates and the target multiples for Max Financial. We have maintained our Buy rating on the stock with revised price target of Rs. 1,000.

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 Dilbagh S Narang	Dir:Taxation
Mr Patnam Dwarakanath	Head: Human Capital

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Mirae Asset Global Investments Co	5.42
2	ICICI Prudential Asset Management	3.87
3	MONEYLINE PORT INV LTD	3.49
4	Nippon Life India Asset Management	3.42
5	HDFC Asset Management Co Ltd	3.22
6	WF ASIAN SMALLER CO FUND	3.12
7	Kotak Mahindra Asset Management Co	2.85
8	New York Life Insurance Co	2.79
9	Baron Capital Inc	2.74
10	BARON EMERGING MRKTS FUND	2.53

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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