Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Max Financial Services Ltd

Healthy Q1; Better product mix drives VNB margins

NBFC	Sharekhan code: MFSL
Reco/View: Buy ↔	CMP: Rs. 849
	Price Target: Rs. 1,020 ↓

↑ Upgrade ↔ Maintain ↓ Downgrade

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING	29.85
Updated July 08, 2022	

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

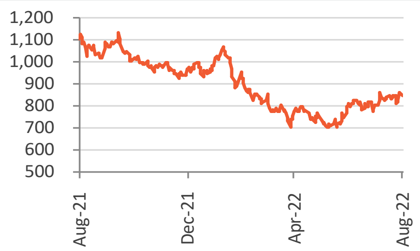
Company details

Market cap:	Rs. 29,223 cr
52-week high/low:	Rs. 1,140/697
NSE volume: (No of shares)	5.5 lakh
BSE code:	500271
NSE code:	MFSL
Free float: (No of shares)	29.4 cr

Shareholding (%)

Promoters	14.7
FII	23.8
DII	53.3
Others	8.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.0	18.2	-6.4	-23.1
Relative to Sensex	-4.2	13.8	-5.3	-19.9

Sharekhan Research, Bloomberg

Summary

- Max Life Insurance reported strong new business premiums (on APE basis) growth of 15% y-o-y and down by 45% q-o-q to Rs. 1,009 crore, driven by strong growth in PAR and ULIP sales. Protection business grew by a moderate 7% y-o-y.
- VNB grew by ~24% y-o-y to Rs.213 crore. VNB margin stood at 21.1%, up by 140 bps y-o-y, aided by better margins of new products across categories.
- Company reiterated its strategy to focus on annuity segment (was up by 125% y-o-y in Q1FY23) going ahead. It reiterated VNB margin guidance at 25-26% by FY23.
- We maintain a Buy on the stock with a revised price target (PT) of Rs. 1,020.

Max Financials Services' (MFS') consolidated PAT grew by 90% y-o-y (but down by ~53% q-o-q) to Rs. 68 crore in Q1FY22. Max Life Insurance (MLI, subsidiary of MFS) reported a gross premium growth of ~18% y-o-y (down by ~49% q-o-q) to Rs. 4,103 crore versus our expectation of Rs. 4,198 crore. This was primarily led by growth in single premium (up by ~30% y-o-y) and renewal premium (up by ~17% y-o-y). It reported new business APE sales of Rs. 1,009 crore, up 15% y-o-y (declined by 45% y-o-y) with a market share of ~9.9% in Q1FY23, on account strong growth across channels. Value of new business (VNB) stood at Rs. 213 crore, increased by ~24% y-o-y (down by ~64% q-o-q). VNB margin stood at 21.1%, up by 140 bps y-o-y, on account of better margins of new products across categories. The company's operating expenses (policyholders) to net premium ratio improved to 16.9% versus 17.4% in Q1FY22, aided by higher growth and effective cost management efforts. The company holds reserves of Rs. 500 crore as pandemic reserves and it do not intend to draw down going ahead.

Key positives

- Value of new business grew by ~24% y-o-y with VNB margin at 21.1%, an increase of 140 bps y-o-y.
- Operating expenses (policyholders) to net premium ratio improved by 50 bps y-o-y to 16.9%.
- Total protection business grew by 7% y-o-y.

Key negatives

- While overall protection business witnessed a healthy growth, its retail protection business declined by 19% y-o-y. .

Management Commentary

- Management guided for 25-26% VNB margin by FY23, instead of 26-27% VNB margin guided earlier, which would be driven by share of high margin products and balanced product mix.
- Company maintained that it would increase manpower for distribution which would see some impact on prospective margins.
- ULIPs witnessed a strong growth of 21% y-o-y. However, the company foresees the demand for ULIPs to moderate going ahead due to volatile markets.

Our Call

Valuation - MLI's business has evolved over the years with improving VNB margins, private market share at 9.9% and a diversified product portfolio. It is an attractive player with strong capabilities and business mix in the insurance space. Axis Bank continues to be the MLI's strongest distribution partner, with ~67% contribution to APE and, hence, is a crucial partner. Moreover, MLI has been on-boarding newer bancassurance partners and new-age digital players, which would not only help diversify the mix but also provide higher sales capacity for it. Hence, we believe business tailwinds may result in providing a positive trigger for improving metrics going forward. MLI generates healthy RoEV (of 13.5% in Q1FY23) and has sufficient capital (solvency ratio of 196%) and hence it is likely to benefit from the improving outlook for the insurance sector going ahead. We maintain our Buy rating on the stock with a revised price target (PT) of Rs. 1,020.

Key Risks

Slowdown in business operations and any adverse change of regulations by IRDA

Valuation Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Net Earned Premium	18,739	22,189	26,183	30,896
EPS (Rs.)	2.7	2.9	3.7	4.0
ROE (%)	18.7	17.5	19.7	18.7
P/EV (x)	3.4	2.5	2.1	1.7
BVPS	14.6	16.6	18.9	21.7

Source: Company; Sharekhan estimates

Key Concall Highlights:

Current headwinds to continue in the near term: Domestic financial markets have remained volatile on the back of recession concerns coupled with relentless selling by foreign investors. This is likely to impact on consumer demand in certain product categories.

Growth across segments: The company reiterated its strategy to focus on annuity segment going forward. Its annuity business grew by 125% y-o-y in Q1FY23. Non-PAR savings rose by 20% y-o-y. Total protection business grew by 7% y-o-y, aided by growth in group protection business while retail segment fell by 19% y-o-y, primarily because of a higher base for retail last year where retail protection demand was high in Q1FY22. Management expects demand for retail protection products to improve in the coming quarters. ULIP was up by 21%, primarily driven by sales in the new product - Flexi Plus Advantage Plan.

Balanced product mix: The product mix stood at Par, Non Par savings, ULIPs and Protection at 17%, 27%, 38% and 18%, respectively. The management intends to retain its product mix as that of FY22 levels.

Distribution channel growth: Proprietary and bancassurance channels witnessed growth of 32% y-o-y and 8% y-o-y respectively. Offline channels grew by34% and online channels grew by 24%. The share of online channel in the new business stood at 6%.

VNB guidance: The management guided for 25-26% VNB margin by FY23, instead of 26-27% VNB margin guided earlier, which would be driven by share of high-margin products and balanced product mix. The company maintained that it would increase manpower for distribution which would see some impact on the prospective margin. With respect to non-PAR products, margin have remained steady sequentially while it was higher y-o-y.

Solvency ratio: Solvency ratio stood at 196% in Q1FY23 versus 197% in Q1FY22. The management opined that it would not require capital raise for one to two years and are comfortably placed in terms of capital position.

Results Rs cr

Particulars	Q1FY23	Q1FY22	y-o-y (%)	Q4FY22	q-o-q (%)
First year premium	918	804	14.2	1,743	-47.3
Renewal premium	2,619	2,244	16.7	5,381	-51.3
Single premium	566	435	30.1	876	-35.4
Gross Written Premium	4,103	3,484	17.8	8,000	-48.7
Profit After Tax	77	80	-3.8	154	-50.0
New Business APE	1,009	875	15.3	1,836	-45.0
VNB	213	172	23.8	586	-63.7
VNB Margins (%)	21.1	19.7	140	31.9	-1,080
Solvency Ratio (%)	196.0	197.0	-100	201.0	-500
Embedded value	14,153	12,290	15.2	14,170	-0.1

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Insurance industry has long-term positive growth prospects

Factors such as a large protection gap and expanding per capita income are key long-term growth drivers for the sector. India has a high protection gap and credit protection product is still at an early stage and has the potential to grow multifold as penetration of retail loans improves in the country. Hence, we believe the insurance sector has a huge growth potential in India. In this backdrop, we believe strong players armed with the right mix of products, services, and distribution are likely to gain disproportionally from the opportunity. Industry growth even during the pandemic shows a promising future for India's life insurance sector and the pandemic has highlighted the protection gap in India.

■ Company outlook - Strong metrics; Sustainable growth business

Max Financial Services (MFS) is effectively building an attractive insurance franchise, characterised by a multi-channel distribution network built upon a conservatively underwritten insurance business. We believe 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 forward, the management has indicated a balanced mix of business with non-PAR at 32-35% of APE, while protection is at 35-40% of APE. We view cost management, re-balancing of product mix, and further diversification of distribution channels are key levers for profitability improvement and add to business sustainability.

■ Valuation

MLI's business has evolved over the years with improving VNB margins, private market share at 9.9% and a diversified product portfolio. It is an attractive player with strong capabilities and business mix in the insurance space. Axis Bank continues to be the MLI's strongest distribution partner, with ~67% contribution to APE and, hence, is a crucial partner. Moreover, MLI has been on-boarding newer bancassurance partners and new-age digital players, which would not only help diversify the mix but also provide higher sales capacity for it. Hence, we believe business tailwinds may result in providing a positive trigger for improving metrics going forward. MLI generates healthy RoEV (of 13.5% in Q1FY23) and has sufficient capital (solvency ratio of 196%) and hence it is likely to benefit from the improving outlook for the insurance sector going ahead. We maintain our Buy rating on the stock with a revised price target (PT) of Rs. 1,020.

About company

Max Financial Services Limited (MFSL) is part of India's leading business conglomerate - Max Group. Focused on life insurance, MSFL owns and actively manages an 81.83% majority stake in MLI, which is the sole operating subsidiary of MFSL. Max Life is India's largest nonbank private life insurer and the fourth largest private life insurance company. MLI offers comprehensive long-term savings, protection, and retirement solutions through its high-quality agency distribution and multi-channel 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 has 358 branch units across India as of March 31, 2022.

Investment theme

MFS holds MLI, which is among the leading private sector insurers. The company 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 any adverse change of regulations by IRDA

Additional Data

Key management personnel

Mr. Mohit Talwar	Managing Director
Mr. V Krishnan	Company Secretary
Mr. Jatin Khanna	Chief Financial Officer
Mr. Patnam Dwarakanath	Head Human Capital

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Mirae Asset Global Investments Co	5.6
2	ICICI Prudential Asset Management	3.9
3	Moneyline Port Inv	3.5
4	HDFC Asset Management Co Ltd	3.4
5	Nippon Life India Asset Management	3.1
6	New York Life Insurance Co	2.9
7	WF ASIAN SMALLER CO FUND	2.8
8	Vanguard Group Inc	2.5
9	Kotak Mahindra Asset Management Co. Ltd	2.5
10	Baron Capital Inc	2.3

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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by BNP PARIBAS

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For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com

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