Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

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 Oct 08, 2022

Medium Risk

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

Source: Morningstar

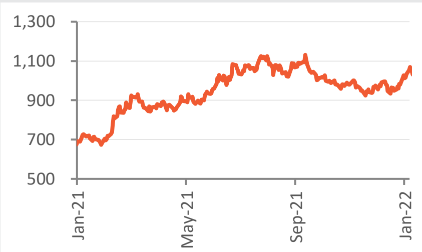
Company details

Market cap:	Rs. 27,395 cr
52-week high/low:	Rs. 1081 / 628
NSE volume: (No of shares)	8.9 lakh
BSE code:	500271
NSE code:	MFSL
Free float: (No of shares)	21.7 cr

Shareholding (%)

Promoters	13.0
FII	45.8
DII	31.7
Others	9.5

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	13.9	4.7	-5.4	-24.7
Relative to Sensex	17.3	1.1	-15.7	-24.2

Sharekhan Research, Bloomberg

Stock Update

Company Update

Max Financial Services Ltd

Uncertainty uplifted on partnership with Axis Bank

Insurance	Sharekhan code: MFSL

Reco/View: Buy	↔	CMP: Rs. 794	Price Target: Rs. 1,020	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- Axis Bank has announced that it will buy the balance ~7% stake in Max Life from Max Financial at fair market value using discounted cash flows (DCF) instead of valuation as per Rule 11UA of the Income Tax Rules, 1962.
- The revision in valuation has been done consequent to the guidance received from IRDAI (Insurance Regulator). With this announcement, uncertainty over the Axis Bank Bancassurance tie-up with Max also goes away.
- The bank has not disclosed the revised valuation; however, we expect the revised valuation for the balance 7% stake should be atleast ~ Rs. 22 billion (i.e Rs.166/- per share of Max Life because as per the annual report 2022, Max Financial acquired 0.74% stake of Max Life from Axis Bank at Rs.166 per share during March 2021), which would be higher by Rs. 18 billion compared to the earlier transfer price.
- We believe now the key catalyst would be the reverse merger of Max Financials with Max Life Insurance along with the listing of Max Life Insurance. Valuations are inexpensive, factoring some uncertainty about the event. We maintain our Buy rating on the stock with an unchanged PT of Rs. 1,020.

Axis Bank announced that it will buy the balance ~7% stake in Max Life from Max Financial at a fair market value using discounted cash flows (DCF) instead of valuation as per Rule 11UA of the Income Tax Rules, 1962. The revision in valuation has been done consequent to the guidance received from IRDAI (Insurance Regulator). Axis Bank is now set to own a 20% stake in Max Life, uplifting the uncertainty on the transaction. Max Financial will get more money for its stake in Max Life. The promoter recently reduced the stake in Max Financial, down to ~13% from 14.7%. Now higher dividend could help promoters reduce debt.

- **Background:** The deal was first announced in 2020, under which Axis Bank proposed to acquire a 29% stake in Max Life Insurance and consequently got the approval for acquisition of a 20% stake. The bank then acquired a 12.99% stake in Max Life at Rs. 35 per share with the right to acquire an additional 7% stake in the company. This was based on valuation as envisaged under Rule 11UA of Income Tax Rules. In October 2022, last year, the Insurance Regulatory and Development Authority (IRDAI) had imposed a penalty of Rs 3 crore on Max Life and Rs. 2 crore on Axis Bank due to violations of valuation rules in the proposed deal, as IRDA noted that the promoters of Max were engaging in the transfer of shares of the insurer to Axis Bank at a price, which is substantially lower than the fair market value. Consequently, IRDA asked the bank and Max Life to revise their valuation methodology for getting approval. Thus, Axis Bank entered into a revised agreement to buy the balance 7% stake at FMV using DCF vs. earlier valuation rule as per Income Tax.
- **Transaction value expected to be higher and closer to the Fair Value:** The bank has not disclosed the revised valuation. However, we expect the revised valuation for the balance 7% stake should be atleast ~Rs.22 billion (i.e Rs.166/- per share of Max Life because as per the annual report 2022, Max Financial acquired 0.74% stake of Max Life from Axis Bank at Rs.166 per share during March 2021), which would be higher by ~Rs. 18 billion compared to the earlier transfer price.

Our Call

Valuation – Maintain Buy with an unchanged PT of Rs. 1,020: Max Life has increased its focus on the non-PAR segment along with the protection segment, which currently forms ~51% of total APE (vs. ~16% in FY2017). Growth in non-par savings continues to witness strong momentum, led by the annuity business. Group protection is seeing a decline due to pricing pressure in GTL policies, while individual protection is expected to do better. The company is increasing its focus on annuity and protection, which would support the overall growth momentum. It 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 sectoral tailwinds may result in providing a positive trigger for improving growth metrics going forward. MLI generated stable operating RoEV (of 15.7% in H1FY2023) and has sufficient capital (solvency ratio of 196%). We believe now the key catalyst would be the reverse merger of Max Financials with Max Life Insurance along with the listing of Max Life. Valuations are inexpensive, factoring some uncertainty about the event.

Key Risks

Muted demand. Any adverse regulatory policies/guidelines may affect its profitability.

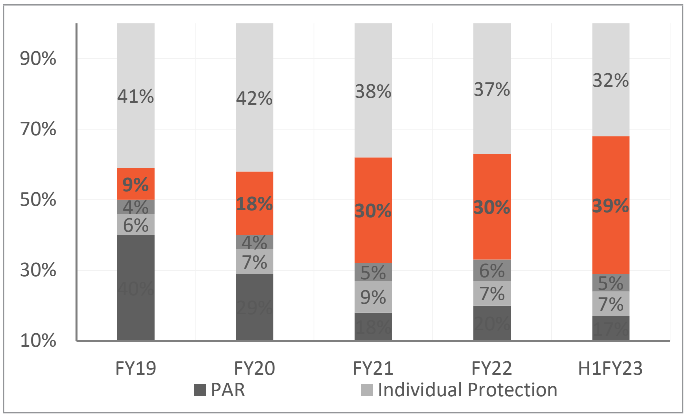
Valuation Rs cr

Particulars	FY22	FY23E	FY24E	FY25E
APE	5,590	6,330	7,290	8,390
VNB	1,530	1,770	2,060	2,360
VNB Margin (%)	27.4	28.0	28.3	28.1
EV	14,170	16,940	20,230	24,010
ROEV (%)	19.2	21.9	21.5	20.7
P/EV (x)	2.4	2.0	1.7	1.4
P/VNB (x)	22.4	19.3	16.6	14.5

Source: Company; Sharekhan estimates

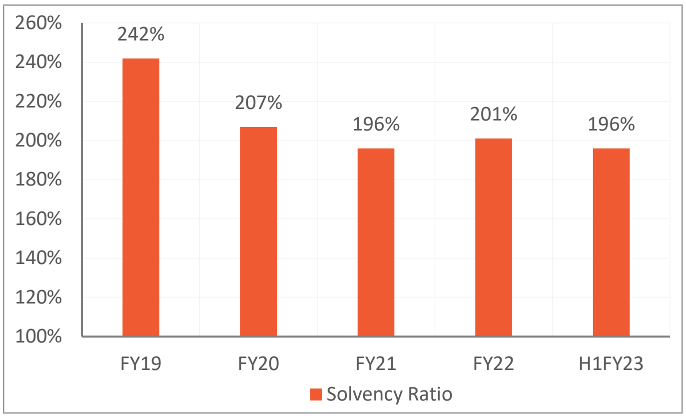
Financials in charts

Trend in Product mix improving towards Non PAR



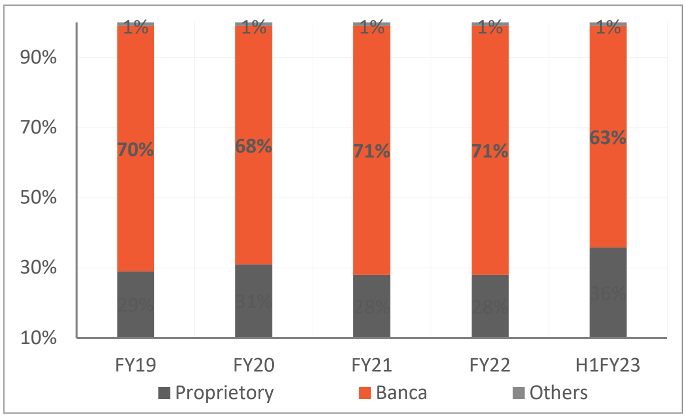
Source: Company, Sharekhan Research

Trend in Solvency Ratio



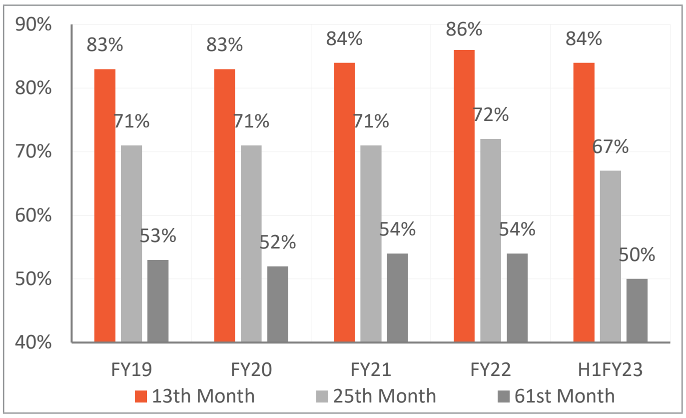
Source: Company, Sharekhan Research

Trend in Sourcing



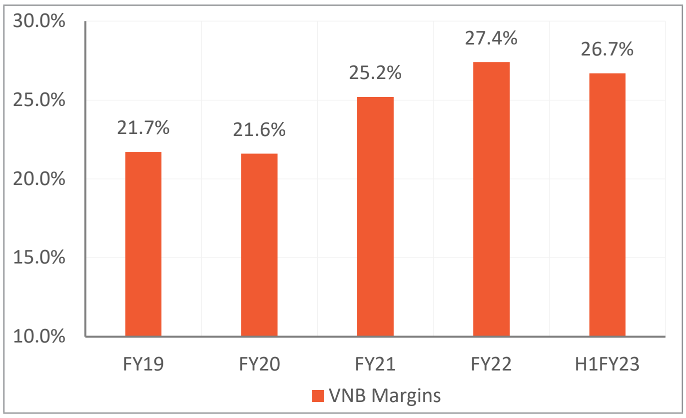
Source: Company, Sharekhan Research

Trend in Persistency



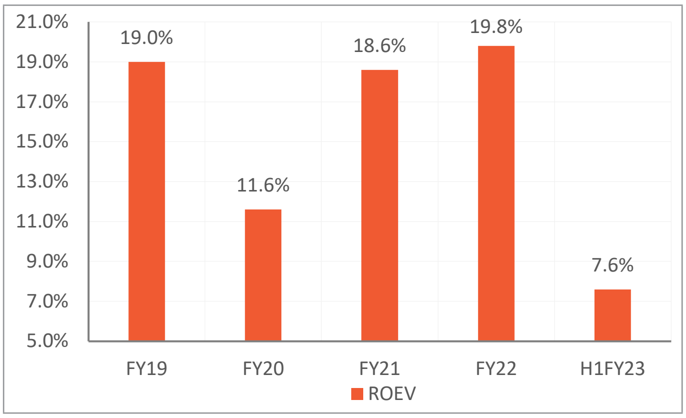
Source: Company, Sharekhan Research

Trend In VNB Margins



Source: Company, Sharekhan Research

Trend in Return Ratio



Source: Company, Sharekhan Research

Outlook and Valuation

■ **Sector View – Strong growth outlook**

Factors such as a large protection gap and expanding per capita income are key long-term growth drivers for the insurance sector in India. India has a high protection gap and credit protection product is still at an early stage and has the potential to grow multifold as the 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 – Moving towards a balanced product mix**

MFS is building a strong franchise, characterised by a multi-channel distribution network built upon a balanced product mix. 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. Going forward, management has indicated a balanced mix of business with non-PAR at 34-37% of APE, while protection 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, growth, and add value to the business franchise.

■ **Valuation – Maintain Buy with an unchanged PT of Rs. 1,020:** Max Life has increased its focus on the non-PAR segment along with the protection segment, which currently forms ~51% of total APE (vs. ~16% in FY2017). Growth in non-par savings continues to witness strong momentum, led by the annuity business. Group protection is seeing a decline due to pricing pressure in GTL policies, while individual protection is expected to do better. The company is increasing its focus on annuity and protection, which would support the overall growth momentum. It 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 sectoral tailwinds may result in providing a positive trigger for improving growth metrics going forward. MLI generated stable operating RoEV (of 15.7% in H1FY2023) and has sufficient capital (solvency ratio of 196%). We believe now the key catalyst would be the reverse merger of Max Financials with Max Life Insurance along with the listing of Max Life. Valuations are inexpensive, factoring some uncertainty about the event.

About company

Max Financial Services Limited (MFSL) is part of India's leading business conglomerate – Max Group. Focused on life insurance, MSFL currently owns a ~87% 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.

Investment theme

MFS holds a majority stake in 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 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 business. Strong focus towards customer measures has helped to deliver superior performance across parameters and will continue to remain an important differentiator. Key catalyst is reverse merger of Max Financials with MLI.

Key Risks

Muted demand. Any adverse regulatory policies/guidelines may affect its profitability.

Additional Data

Key management personnel

Mr. Mohit Talwar	MD of Max Financial Services
Mr. Prashant Tripathy	MD and CEO of Max Life Insurance
Mr. Amrit Singh	CFO of Max Financial and Life Insurance

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	MS&AD INSURANCE GROUP HOLDINGS INC.	21.86
2	MAX VENTURES INVESTMENT HOLDINGS PVT. LTD.	14.60
3	MIRAE ASSET GLOBAL INVESTMENT CO. LTD.	5.63
4	ICICI PRUDENTIAL ASSET MANAGEMENT CO. LTD.	3.79
5	HDFC ASSET MANAGEMENT CO. LTD.	3.78
6	MONEYLINE PORT INV LTD.	3.49
7	NIPPON LIFE INDIA ASSET MANAGEMENT LTD.	3.03
8	NEW YORK LIFE INSURANCE CO.	2.90
9	WF ASIAN SMALLER CO FUND	2.84
10	KOTAK MAHINDRA ASSET MANAGEMENT CO. LTD.	2.80

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

Sharekhan
by BNP PARIBAS

Know more about our products and services

For Private Circulation only

Disclaimer: This document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This Document is subject to changes without prior notice. This document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved) and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusions from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst has not dealt or traded directly or indirectly in securities of the company and that all of the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst and SHAREKHAN further certifies that neither he or his relatives or Sharekhan associates has any direct or indirect financial interest nor have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report nor have any material conflict of interest nor has served as officer, director or employee or engaged in market making activity of the company. Further, the analyst has also not been a part of the team which has managed or co-managed the public offerings of the company and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Limited or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either, SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Compliance Officer: Ms. Binkle Oza; Tel: 022-61150000; email id: complianceofficer@sharekhan.com;

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

Registered Office: Sharekhan Limited, The Ruby, 18th Floor, 29 Senapati Bapat Marg, Dadar (West), Mumbai – 400 028, Maharashtra, INDIA, Tel: 022 - 67502000/ Fax: 022 - 24327343. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O/ CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183.