

The Scoop: Company Reports Strong Q4

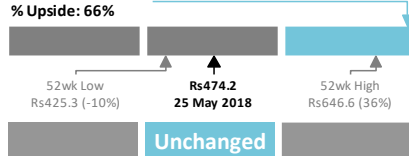
Insurance

India

25 May 2018

BUY

Target: Rs785.0
% Upside: 66%



Basic Share Information

Market cap	Rs127.3b / US\$1.88b
Daily traded value (3mth)	US\$4.52m
Shares outstanding	268.4m
Free float	55%
Foreign Shareholding	30%
1 yr high	Rs646.6
1 yr low	Rs425.3

Price/Volume



Source: Bloomberg

	1mth	3mth	12mth
Absolute	-5.7%	-4.8%	-15.8%
Absolute USD	-6.9%	-9.1%	-19.8%
Relative to SENSEX	-6.9%	-7.1%	-29.4%



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What event has happened?

Max Financial Services reported its Q4 FY3/18 results on 25 May 2018, which were strong and in line with our expectations.

Why is it significant?

The stock has underperformed the index as well as its peers and is down around 16% over last one year, whereas the Sensex is up around 11% over the same period. This underperformance was based on the view that the tie-up with Axis Bank (AXSB IN) would break and Axis Bank would start its own life insurance company. However, in line with our argument, both Axis Bank and Max Life (unlisted) have clarified that the tie-up stays as it is. Hence we expect the focus to now shift to the fundamentals of the company, where the company has reported one of the strongest results in the sector, with annualized premium equivalent (APE) growing 22% YoY in FY3/18, value of new business (VNB) profits growing 31% YoY in FY3/18 with a VNB margin of 20.2% in FY3/18 (second only to HDFC Standard Life Insurance (HDFCLIFE IN) amongst the top four life insurance companies in India). The company has also reported operating RoEV of 20.6% (on opening embedded value, EV), which is currently one of the highest in the sector in India.

Implications for our earnings forecast?

If the management decides to go ahead with its intention of investing in its proprietary channels, then we think APE growth will pick up from 17% in FY3/19 and to 30% in FY3/20, but we expect VNB margins to decline in FY3/19 to 19% and then recover in FY3/20 to 22%. Hence we raise our target price for Max Financial Services from Rs725 to Rs785. Our valuation is derived using an appraisal value methodology, where we add the value generated from new business using discounted cashflow (DCF) analysis of the merged entity's pre-dividend EV. The main risk to our rating and to the attainment of our target price is the risk of regulatory regulations on traditional products.

How do valuations look now?

The stock is trading at 1.6x FY3/20 P/EV (pre-dividend) which we estimate is at around a 35% discount to its peer group. This is despite the fact that we believe the company's RoEV of 20.6% on opening EV is one of the highest in the sector and it has a FY3/18 VNB margin of 20.2%.

What is distinctive about our stock view?

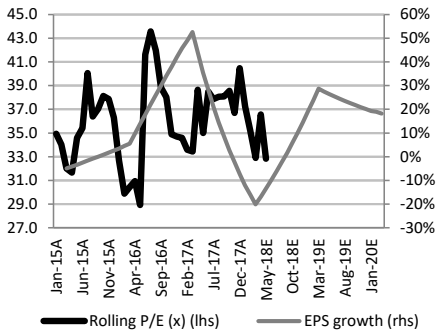
We believe that the market is ignoring the fundamentals of the stock. We expect Max Life's EV to grow at around 20% pre dividend and VNB to grow at around 30% p.a. over the next two years. In FY3/18, Max Life reported operating RoEV of 20.6% (on opening EV) and VNB growth was 31% YoY, which, in our view, shows business has picked up.

	Mar-16A	Mar-17A	Mar-18A	Mar-19E	Mar-20E	Trend
Gross premiums written (Rsm)	92,160	107,804	125,010	133,990	154,687	▬ ▬ ▬ ▬ ▬
Total turnover (Rsm)	106,473	151,999	167,408	184,014	213,332	▬ ▬ ▬ ▬ ▬
Pre-tax profit (Rsm)	5,091	7,682	6,160	7,757	9,123	▬ ▬ ▬ ▬ ▬
Net income to ord equity (Rsm)	3,017	4,619	3,699	4,760	5,628	▬ ▬ ▬ ▬ ▬
Net profit growth	5.5%	53.1%	(19.9%)	28.7%	18.2%	▬ ▬ ▬ ▬ ▬
P/EV (x)	2.99	2.63	2.30	1.94	1.60	▬ ▬ ▬ ▬ ▬
P/B (x)	6.44	5.45	4.45	3.59	2.93	▬ ▬ ▬ ▬ ▬
P/E (x)	41.93	27.48	34.40	26.74	22.61	▬ ▬ ▬ ▬ ▬
ROE	11.5%	21.5%	14.2%	14.9%	14.3%	▬ ▬ ▬ ▬ ▬
EVPS (Rs)	158.8	180.1	206.1	244.9	296.1	▬ ▬ ▬ ▬ ▬
EPS HTI old (Rs)	11.31	17.26	15.32	19.05	23.72	▬ ▬ ▬ ▬ ▬
EPS HTI New (Rs)	11.31	17.26	13.78	17.74	20.97	▬ ▬ ▬ ▬ ▬
Consensus EPS (Rs)	13.93	12.19	11.44	14.01	16.11	▬ ▬ ▬ ▬ ▬
HTI EPS vs Consensus	(18.8%)	41.6%	20.5%	26.6%	30.2%	▬ ▬ ▬ ▬ ▬

Source: Company data, Bloomberg, HTI estimates

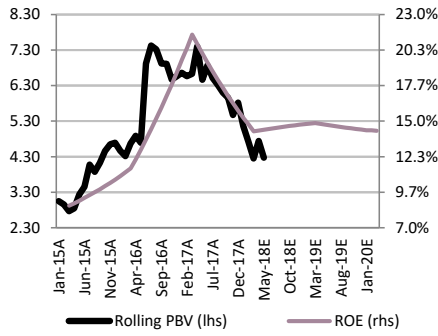
Click [here](#) to download the working model

P/E (x) vs EPS Growth (%)



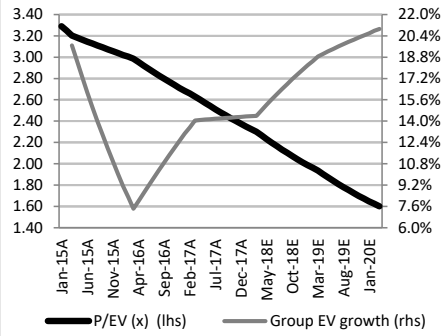
Source: Company data, Bloomberg, HTI estimates

P/B (x) vs ROE



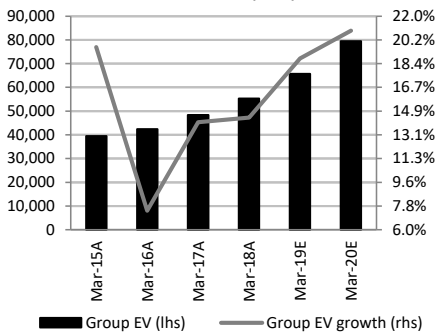
Source: Company data, Bloomberg, HTI estimates

P/EV (x) vs Embedded value growth (%)



Source: Company data, Bloomberg, HTI estimates

Embedded Value and Growth (Rsm)



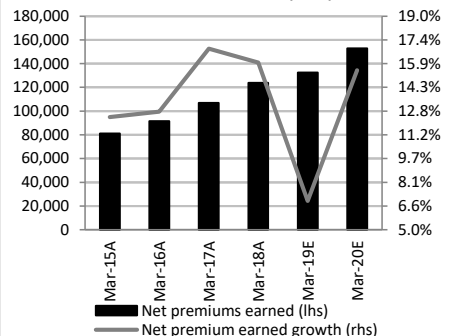
Source: Company data, Bloomberg, HTI estimates

ROA (%) vs Asset Turnover (x)



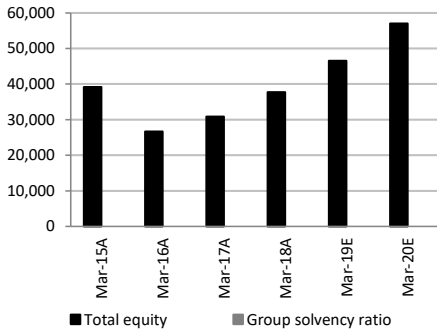
Source: Company data, Bloomberg, HTI estimates

Net Premium Earned and Growth (Rsm)



Source: Company data, Bloomberg, HTI estimates

Total Equity vs Solvency Ratio (Rsm)



Source: Company data, Bloomberg, HTI estimates

APPENDIX

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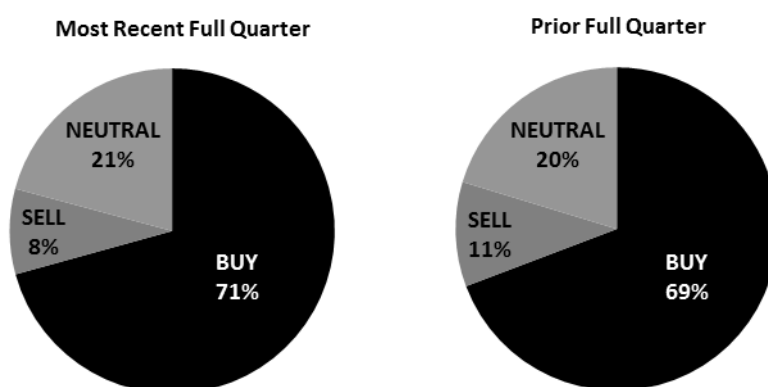
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Recommendation Chart



Date	Recommendation	Target (Rs)	Price (Rs)
2018-04-25	Buy	725.0	502.7
2018-02-14	Buy	775.0	518.1
2017-11-24	Buy	797.3	562.5
2017-05-01	Buy	756.0	656.1
2017-03-16	Buy	644.0	565.3
2017-03-10	Buy	635.0	536.1
2017-01-12	Buy	637.0	554.2
2016-12-21	Buy	626.0	536.4

Source: Company data Bloomberg, HTI estimates

Definitions for Key Investment Metrics

Business Growth

This is the metric which matches the top line in our report.

Business profit

This is the metric which best represents operating profit in our report

Shareholder Returns

Return on Equity

Balance Sheet Risk

Net Debt to Equity