"Bajaj Finserv Q3 FY18 Results Conference Call"

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MODERATOR: **MR. KARAN SINGH-JM FINANCIAL**

Moderator: Ladies and gentlemen good day and welcome to Bajaj Finserv Q3 FY18 Results Conference Call hosted by JM Financial. As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference to Mr. Karan Singh from JM Financial. Thank you and over to you sir.

Karan Singh: Thank you. Good afternoon everybody and welcome to Bajaj Finserv's Earnings Call to discuss the third quarter results. To discuss the results, we have on the call Mr. S. Sreenivasan-CFO, Bajaj Finserv, Mr. Ramandeep Singh Sahni-CFO, Bajaj Allianz Life & Mr. Milind Choudhari-CFO, Bajaj Allianz General. May I request the management to take us through the financial highlights subsequent to which we can open the floor for Q&A session? Over to you Sir!

S. Sreenivasan: Thank you Karan. Welcome everybody to this conference call. Today we will be discussing the results of Bajaj Finserv Limited for the quarter ended 31st December 2017. In this call we will largely be concentrating on the consolidated results of Bajaj Finserv as well as the results of our insurance operations through Bajaj Allianz General Insurance and Bajaj Allianz Life Insurance companies. Bajaj Finance which is another major subsidiary of ours has already had its conference call today. However, if there are any high-level questions we would be glad to take that as well. We will not be taking any questions on the status of Allianz's stake in our Insurance Companies. The status has remained the same as of the end of the previous quarter and there is no change there. Just as a matter of hygiene any statements that may look like forward-looking statements are just estimates and do not constitute an assurance or indication of any future performance.

Let me now take you all through the highlights of the quarter ended 31st of December 2017. For Q3 Bajaj Finserv has had a very satisfactory quarter, we recorded the 21% increase in total revenue and a 22% increase in consolidated profit after tax. Bajaj Finance continues its stellar growth and it has been another record quarter for them with the 31% growth in revenues and 38% growth in profit after tax.

Our general insurance company BAGIC recorded 10% growth in gross premium and 33% growth in PAT, excluding the crop insurance business the growth in gross premium was 23%. In terms of profitability BAGIC continued a sustained performance in General Insurance with a combined operating ratio for Q3 FY18 at 92.1%. BALIC too has continued its focus towards selling more individual regular premium, BALIC's rated individual new business premium grew by 28% and in this quarter, we saw all round growth across rated individual business, renewal premium and gross written premium. It is the highest ever quarterly profit after tax reported by both Bajaj Finance and Bajaj Allianz General. Bajaj Finance continues to have high level of capital adequacy and solvency respectively.

I will now hand it over to Karan to moderate the questions.

Moderator: Thank you very much Sir. Ladies and gentlemen, we will now begin with the question and answer session. We take the first question from the line of Mayur Parkeria from Wealth Managers. Please go ahead.

Mayur Parkeria: Little broader question on the Life side, actually just before I make a question just a small disclaimer. We have been invested for five years at a stretch, so it's not a quarterly number which I'm trying to understand. But the question may look like on a quarterly but it's a broader one. It is 19 straight quarters where we are seeing profitability under stress for Life Insurance now. Whichever way we approach, 2012-13 we had profit of almost around 1300 crores in Life. This time we will reach 700 crores odd or not is also a question, so it's a half of the profit whereas the gross return premium if we look at that was almost around in the same region now, 7000 crores plus minus. So where do we see this going forward firstly? And secondly the one that now renewal premium and the individual rated premium has started gaining traction. We were given to understand that the surrender issues, those are also behind us, so why is it that the Life continues to see profitability issue?

S. Sreenivasan: I will just give a brief answer then I will hand it over to Raman. In Life business unfortunately, the PAT always comes from the back-book, so irrespective of how well you do on your new business the PAT is determined by what you did some years ago and it's a fairly long cycle. The parameters by which Life companies therefore are looked at are largely based on the growth in embedded value, value of new business etc. Our value of new business has been growing in the last couple of years; we do not do a quarterly assessment of value of new business. We will do it by end of the year and it is our hope that the value of new business will be higher. There are couple of reasons why this year the profits are lower; one is we did have one seasonal claim which Raman will explain which did dent the profits a bit. Otherwise it might have been at least flat if not slightly better. And secondly, we are still running expense overruns by choice, as the market is heavily towards ULIP. Although in this quarter if you see we have done remarkably well in terms of balancing the product mix. We have actually sacrificed a bit of growth we otherwise would have got for the sake of getting better balance, because with the way the equity markets have moved we do see the risks in having excessive exposure to unit linked insurance. So now I will hand it over to Raman, he will give you a better flavor on the profit after tax.

Ramandeep Singh Sahni: Thanks Sreeni. I think Sreeni touched upon the fact that if you look at the company for several years until last year and probably a little over that also, we had seen significant amount of de-growth in our individual business and we have essentially become a group driven company and largely focused only on agency which we know is a very high cost model. What that had led to was fall in profits which you rightly spoke about and company went through that spiral of de-growth and we were at a stage where the expenses were just too high compared to whatever we could afford. So we went through a cycle of revamping the company and I think that investment has been going on for the last 18 months, where we slightly try to rejig the entire company. So what we discussed internally is we've like completely revamp the company and it's at a stage where a new insurance company would be because you are at a size of individual business which was two years back very similar to a very small volume company and now we've scaled up significantly, you see the growth. And what happens with this growth is the strain and this is the situation we are in we are seeing a significant amount of strain so even if you see renewals growing but the new business is growing at a much faster pace. For nine months you know that the growth is close to 50% and that is causing a lot of strain on our profitability and we believe that this will continue to be there for a next few years, because, our aspirations to grow individual business is really high. So, to answer your first question I think the strain will continue and I think the profits growth expectation which you are envisaging will not be there for the next few quarters as well, because, of the high strain which we'll envisage. In specific to this year's profit what Sreeni really spoke about was we got some bit of high claims from one of our large MFI partners and that gave a big dent on the profitability in the current year. But that is one off thing which was there, it is now behind us and we are hopeful that will not arise in the future. So that one dent which is there I can't quantify the same but that's a big dent in our profits for this year. But will the profits improve now; it is still going to take some time because we are still investing in high-growth. In addition, we're also investing a lot, you would have seen on technology you've been hearing lot of things which we've been doing on technology whether it's BOTS or revamping our website. So anything on digital, we are really trying to transform the company so that we get the benefit of that in the long run. But I think it's a phase of investment for us and you will have to wait for another few quarters for profits to really take up.

S. Sreenivasan: Just to summarize before you take on; if we cut our growth by half we could have actually reported a better profit because new business strain is always there.

Mayur Parkeria: On the individual side?

S. Sreenivasan: Yeah.

Mayur Parkeria: When we say we don't see profitability improving and profitability strain to continue for few years, are we saying that the….?

Ramandeep Singh Sahni: We said few quarters.

Mayur Parkeria: Couple of questions on the number side; the combined ratio for this quarter is not there in the General. We have only Q2 FY18 numbers …

S. Sreenivasan: It is there in the press release in the stock exchange.

Milind Choudhari: In the presentation the combined ratio has been shown in comparison with top 5 players also. So published results are available….

S. Sreenivasan: But that is only up to second quarter**.** But Q3 won't have competition numbers. I can tell you what exactly it is. Underwriting profit for the quarter Q3 was 113 crores, our combined ratio was 92.1% in Q3 FY18, for the corresponding period in FY17 it was 99.6%.

Mayur Parkeria: How much was the claim ratio?

S. Sreenivasan: 62.4%, last year was 70.8%, so pretty much the combined ratio improvement is from a reduction in the claim ratio.

Mayur Parkeria: One observation was this time along with gross written premium you have given net earned premium.

S. Sreenivasan: Yes.

Mayur Parkeria: But earlier you used to have net written premium.

S. Sreenivasan: Ultimately net earned premium is the premium that you, get in your books on which you pay the claims, expenses and commission and report an underwriting profit or a loss. Net written premium is something in between gross and net earned premium.

When you look at General Insurance with the business of selection, there is quite a lot of business which BAGIC may not compete in because of issues of profitability or sustained profitability. If you look at BAGIC's relative position in the market in gross premium and net earned premium you will find a remarkable difference. The difference between BAGIC and the leader in the private sector would not be more than 15% in net earned premium. Perhaps it may be as high as 30% in gross return premiums.

Mayur Parkeria: Last question on the crop side; if you look at industry premium growths they are pretty much better but our total gross return premium was lower because of I think crop insurance.

S. Sreenivasan: Yes, because crop insurance it is reported through the financing bank and the cycle of reporting is through a variety of banks. So timing wise it could on year-to-year have a lot of variations. So last year, if you look at the nine-month figures it pretty much shows the correct number. But some extra business booked in Q3 of last year, this year it got shifted to Q2 in this year, last year it was booked more in Q3.

Mayur Parkeria: But business wise there is no change in terms of…

S. Sreenivasan: No, roughly our target is to do as much as our overall market share which is roughly 7% of the crop business.

Moderator: We take the next question from the line of Adarsh Parasrampuria from Nomura. Please go ahead.

Adarsh Parasrampuria: Can you just walk through the claim ratio excluding the crop business, how it's been, what's the improvement and the key businesses where you've seen that improvement?

Milind Choudhari: When we look at the current year excluding crop—if you were talking about the overall YTD results as such—the overall loss ratio it is around 64.7% was around 70.5% excluding crop last year nine months. So I think the major savings in terms of the claims as well as improvement in the combined ratio is coming on account of the core insurance business which the company writes other than crop. So it's not something that it is a big impact of crop or lower loss ratio in crop insurance which is offsetting this and improving this.

S. Sreenivasan: Predominantly if you remember last year in Q1 and Q2, we had set upon a task of repairing or getting out of some of our loss making relationships because we found the claim ratio was increasing in areas like motor and group health. In both those areas we have reported significantly improved loss ratios. Our motor OD and TP loss ratios were much lower than last year and overall in group health also it is lower than last year.

Adarsh Parasrampuria: The group health what has been the pricing change in the market that you would have seen?

Milind Choudhari: What I would like to state here is, that I think pricing has become little better. This was on the wake of listing of a few companies, so I think pricing was better and more rational. I think you would have also heard about the yesterday's announcement in terms of merger of all three unlisted PSU companies together, so I think this is going to lead to more underwriting discipline in the market. So that is what is reflecting in terms of improved loss ratios in this segment of group health.

Adarsh Parasrampuria: So just on the perspective of you are seeing a combined ratio significantly better off than what you have seen in the last few years and now interest rates are headed up, so would you think that this translates into significantly higher ROEs for the business or you will likely see some competition somewhere else?

Milind Choudhari: Of course, there is the competition coming in because I think if we look at the stance taken by RBI right now it is a kind of a pause. It’s still time in terms of witnessing the increase in terms of rates of interest. But I think as it starts moving up over the next 2 or 3years, newer areas of competition where I think on one front the regulator has actually prevailed well in terms of controlling the overall commission cost particularly the new motor insurance service provider guidelines which came in, which actually capped all the motor related commissions also. So on that front we are looking at in terms of better portfolios and overall combined ratios we think that as the market has more sanity I think they will start moving lower. Because, the combined ratios which was around 118% for the industry have already dropped around 113-114 for the current year. I think as this starts consolidating and more and more avenues start coming up in terms of business growth I think this will balance out very well. Of course, there will not be able to see whether it will really translate into a very high return on equity, but our ROE will continue to be one of the top most within the industry.

Moderator: We take the next question from the line of Hitesh Gulati from Haitong Securities. Please go ahead.

Hitesh Gulati: You stated that you have 5% share in GTL health and 9% in group health so do you have any proportion of government health schemes also? What will be your take on the yesterday's announcement where Finance Minister basically said that 10 crores families would get sum insured up to 5 lakh, so what do you make up for…

S. Sreenivasan: You're talking about Life or non-Life because GTL is mostly in the life side?

Hitesh Gulati: No, the announcement was on the health insurance.

S. Sreenivasan: Health insurance if you look at the market, there is already a scheme called Rashtriya Swasthya Bima Yojana that is roughly 15% to 20% of the market. Then there is the Corporate Health Insurance which is probably about 45% of the market or so and about 40% of the market is retail health. The three segments behave differently, and the government scheme typically has been 15% or so of the market. Regarding yesterday's announcement we cannot comment anything because we have to wait for the scheme to roll out. Typically, if it is a government-subsidized scheme like crop insurance it will only be given to people of minimum / below a certain income level. And in that we believe there is a significant population below that level who do not have access to health care, leave alone health insurance. So, we will have to wait for the fine print and the actual scheme to be rolled out to see what are the eligibility conditions, who will come, what is the level of government subsidies, whether the central government and state government both involved and what is the budgetary allocation because that is the most critical thing which will drive that. So we think that is important, but most of the private companies now are in a segment which is much higher than those levels in terms of sum insured or in terms of ticket size or customer segment. Mostly it is salaried income and above.

Moderator: We take the follow up question from the line of Mayur Parkeria from Wealth Managers. Please go ahead.

Mayur Parkeria: Within group how much would be term?

S. Sreenivasan: In Life or non-Life?

Mayur Parkeria: In Life

Ramandeep Singh Sahni: I will just tell you the exact numbers, so our total group business for the nine-month period was about 2000 crores of which the funds business which is the employee-employee thing is about 1300 crores and the balance is your credit protection and GTL which is about 600 crores. This will be divided in GTL and credit protection almost close to each other in equal terms. That's how this split is now.

Mayur Parkeria: That's it from my side. Thank you.

Moderator: We will take the next question from the line of Kunal Shah from Edelweiss. Please go ahead.

Prakhar: Couple of questions, first on General Insurance; when we talk about this scheme which is RSBY, how has been the pricing on this and what is the profitability of this segment if at all?

S. Sreenivasan: I won't have a specific answer to that question because BAGIC has not been a very active participant. I think we do little bit of the business just to be in it.

Milind Choudhari: Actually, we just did some small amount of business of around 50 - 100 crores and we are just trying to gain experience, because, we knew that this kind of a universal coverage is likely to come, of course this is coming in phases. But just to actually be ready in terms of when the actually launch comes which is getting ready now, so pricing has not been very good as far as the current pricing is concerned, because, one thing the pie was very small and there were lot of companies which were willing to write it. But once now the pie becomes bigger then there is enough for all the players to be in and therefore the pricing should improve.

S. Sreenivasan: There are two ways, if it is like the crop insurance where the pricing is left to the market that is one thing. If the pricing is going to be fixed, then it is going to be another case altogether.

Milind Choudhari: It is going to be tender based, so it will behave in similar pattern to crop insurance. But we are looking at it as this particular area also may become as big as crop insurance over the next few years.

Prakhar: In terms of your combined ratio ex-crop insurance what will be the comparable numbers this quarter and last quarter?

Milind Choudhari: This quarter our combined ratio excluding crop is around 90% as against 100% last year.

Prakhar: And last quarter it was?

S. Sreenivasan: If I remember right it was 93% or 94%.

Prakhar: On the Life Insurance when we talk about the let-go off some of the opportunities because we wanted to have a balance mix, what sort of mix that we are targeting over next couple of years?

S. Sreenivasan: We don't have a specific target ideally there is no magic number there. Nevertheless, excessive dependence on ULIP like for example 80% or more on ULIP, we have found in the past especially when the market goes down and financial savings get affected or due to regulatory changes as we saw between 2008 and 2012 can cause significant disruption in the distribution channel because the people who sell unit linked are not the people who are good at selling traditional policies. So in order to compensate that in this quarter at least we started pushing for a higher proportion of traditional business. I think for this quarter Raman you have the number?

Ramandeep Singh Sahni: The quarter we have moved up, so for YTD the concentration was higher about 78% ULIP but we got it down to 72% in the quarter. So just to take on from what Sreeni said rightly, so we don't want to force on our product mix. But the way we are driving this now is there are smaller cities where we are good in terms of presence, the C and D category towns then there we realized that the customers really prefer traditional. So these are the markets where we are trying to push more of traditional to have a more balance mix. And rightly so the mix is as we see is skewing toward the 70-30 kind of a ratio now.

Prakhar: But how has been pricing on crop insurance as in we have any improvement?

Milind Choudhari: Basically, in response to your earlier question, in Q2 also we had a combined ratio of around 90% against 99.6%. So both the quarters we have combined ratio of 90% but Q3 it was against 100.1% and in Q2 it was against 99.6%. As far as crop insurance pricing is concerned, I think pricing is slightly coming down as the crop insurance market is maturing and governments are also coming to know in terms of how to float the tenders and what kind of outlay they have in terms of the overall budgetary sanctions. Our strategy continues to get into some profitable clusters, profitable states and to bid only those places where we can strategically play-sit in terms of the concentration risk as well as the profitability. Our effort continues in that direction. Overall loss ratios seem to be better this year as compared to the last year and the Rabi season is just getting started so we are still getting premiums in our accounts and the farmers. Ones that is frozen I think more business will flow in the month of January and February because last year this was little early, it depends on the closing deadlines which are given, so 15th January was the deadline in terms of collection of farmers premium. So that we will get into our account by 31st January as well as the remittance will happen in the first week of February. So February and March will be having the rest of the booking and we are expecting to touch around 1800 crores this year.

Moderator: We take the next question from the line of Thomas Wang from Goldman Sachs. Please go ahead.

Thomas Wang: You talked about net earned premium and that will close much faster than your gross written-premium in this quarter. Is it something that's one-off or is it something because of improved profitability that will continue?

S. Sreenivasan: I think it is due to the mix of crop and non-crop, because, the crop insurance is heavily reinsured relative to other businesses and that can affect the earning pattern. Earning is after reinsurance.

Thomas Wang: Second is on Life side, you talked about that there was little bit lower scale, do you see any inorganic growth opportunities?

S. Sreenivasan: As and when things come we do have a look at all the opportunities but currently we are not participating in any on Life insurance

Moderator: We take the follow up question from the line of Mayur Parkeria from Wealth Managers. Please go ahead.

Mayur Parkeria: Pending the Allianz issue, is there any strategy on the dividend side because solvency ratio on the Life.

S. Sreenivasan: Currently no.

Mayur Parkeria: Because it's 600% now.

S. Sreenivasan: Yeah it is. But currently it is something we review every year but as of now we are not taking a decision on that.

Moderator: We take the next question from the line of Megha Hariramani from Pi-square Investments. Please go ahead.

Megha Hariramani: I just wanted to understand what challenges are we facing in the Life Insurance business because this quarter as well we don't have good numbers on that front?

S. Sreenivasan: We were explaining earlier, in Life Insurance now our growth has been quite strong for several quarters. This quarter the growth has been little bit lower than previous quarters lastly because we were focusing on a balance product mix to more traditional business and slightly less unit linked business. So on an YTD basis we have been able to bring down our ULIP from 78% to 72% only in this quarter. Having said that the Life business as we grow we will continue to have new business strain because the new business does come at a cost for everyone. And till we get that balance between new and renewable it may take us another couple of years, we will have this strain. As far as the P&L is concerned we had one off death claim this year which has affected the P&L. But apart from that as the new business grows we think over the next few more quarters we would have effect on the statutory P&L as they call it. I'm not talking about value of new business or embedded value. I'm talking about the statutory profit after tax that is reported in the financials.

Megha Hariramani: So is there any other strategy that we have outlined, how do we…?

S. Sreenivasan: We don't need to put in any strategy. We grow much slower than what we are doing now, we could actually improve our profit but that is not what we want to do. We have a lot more room to go in terms of scale and we need to be significantly higher scale before the slowdown on the expensive side, so it will take us some time. Otherwise the quality parameters are doing exceptionally well. This quarter I think our persistency as of November has touched 76% which is 11% improvement and we are in sight of 80% by end of the year. It may fall short slightly if at all and by next year we have a fair chance of being among the top 3-4 companies in terms of persistency as well. So these were some of the issues which were bugging us in the past. The only downside risk as I see is because the older book. Some part of it will mature over the next two years that is true not only for us but all companies which were strong at the time and B. as the equity market moves higher there is a tendency to surrender. All the company to couple of years ago the surrender levels are much lower, compared to last year they are higher.

Ramandeep Singh Sahni: They are almost flat Sreeni despite the market going up significantly.

Megha Hariramani: But I think the market seeing a correction after the LTCG law.

S. Sreenivasan: That we don't know yet, we have to rethink. It may be positive for Life Insurance but we will have to wait and see.

Moderator: Thank you. As there are no further questions from the participants on the half of JM Financial we would like to thank the management for giving is the time for this call. Ladies and gentlemen with that we conclude today's conference. Thank you for joining us and you may now disconnect your lines.