Equity | Malaysia | Non-Bank Financials

24 May 2023

RCE Capital

FY23 Finished In-line

Hold

Price
RM1.92

Target Price
RM2.00

FY23 results were within expectations, accounting for ~101% of FY23 projection. Net profit was supported by higher fee and early settlement income, cushioning the impact of higher impairments during the period. On a separate note, management announced a new dividend policy of 60% to 80% payout. All in all, we maintain a Hold rating for RCE Capital (RCE) with an unchanged GGM-derived valuation of RM2.00. While RCE is expected to register stable earnings growth in a range of 3% - 5% supported by sustainable loan growth of around 5%, we reckon that potential downside risk remains given the challenging environment, which could demand higher provision. Valuation-wise, RCE currently trading at P/B valuation of 1.5x, which is above +2SD.

Market Data

Bloomberg Code	RCE MK
No. of shares (m)	353.2
Market cap (RMm)	667.5
52-week high/low (RM)	1.93 / 1.37
Avg daily turnover (RMm)	0.4
KLCI (pts)	1,428.5

Source: Bloomberg, KAF

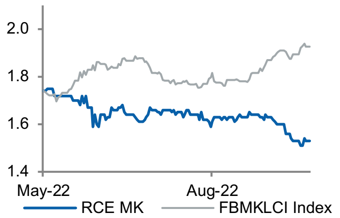
Major Shareholder (%)

Cempaka Empayar	(55.0%)
EPF	(2.4%)
Cheam Heng Ming	(1.1%)
Free Float	121.2

Source: Bloomberg, KAF

Performance

	3M	6M	12M
Absolute (%)	4.4	21.5	16.1
Rel Market (%)	7.0	22.5	25.8



Source: Bloomberg, KAF

Financial Highlights

FYE Mar	2022	2023	2024F	2026F	2026F
Operating income	239.6	261.6	261.9	274.5	287.7
Net profit	133.2	138.8	144.6	151.1	159.3
EPS (sen)	18.2	18.8	19.8	20.6	21.8
EPS growth (%)	6.9	3.6	5.5	4.5	5.5
DPS (sen)	10.4	30.0	11.9	12.4	13.1
Div yield (%)	5.4	15.6	6.2	6.5	6.8
PER (x)	10.5	10.2	9.7	9.3	8.8
PBR (x)	1.6	1.7	1.4	1.3	1.2
ROE (%)	16.2	17.2	14.7	14.5	14.4

Source: Company, KAF

FY23 results finished inline.

RCE reported a net profit of RM34.8m in 4Q23 (+10.5% YoY), driven by higher fee income (+180.8% YoY) as disbursements were higher on certain products arising from sales campaigns as well as an increase in other income (+52.8% YoY) due to income earned from deposits placed.

4Q23 net profit was lower by 1.0% QoQ nonetheless attributable to a 49.0% increase in impairment loss.

Cumulatively, RCE reported an improvement of 4.2% YoY in net profit to RM138.8m on the back of higher fee and early settlement income. Overall, results were in line with our and consensus expectations, meeting ~101% of full-year FY23 earnings estimates.

Higher impairment loss in the 4Q23.

FY23 reported a higher impairment loss by 148.5% YoY due to changes in employment trend, i.e., higher retirement and shift in employment status. We observe that the trend has normalised however, with impairments falling in 2Q23 and 3Q23, after the peak in 1Q23.

Nevertheless, a 49.0% surge in impairment loss in the 4Q23 has caught us by surprise, though we argued that was mainly due to the change in key macroeconomic variables, in reflection of slower GDP growth in 2023. The non-performing financing remains at RM77m (9M23: RM77.8m), supporting further this argument.

Asset quality position remains solid.

We observe a stable repayment trend for the Group, demonstrating its receivables quality position is solid. This is also supported by management's stringent risk and prudent provisioning policy. Thus far, RCE maintained its NPL ratio at a 4% level since 2016 while credit cost remains low at 6% (pre-pandemic: 7% - 8% range). This translates to a coverage ratio of 157.8%. To note, the current coverage ratio was lower as compared to >170% before

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FY20, explaining that the quality of its receivables has improved, by means of a lower provision.

Healthy financing growth.

RCE's financing receivables growth expanded by 7.7% YoY in FY23, showing that the demand for financing among civil servants remains strong despite the higher interest rate environment. For the coming year, management's impression is that demand will be remaining strong, in order to face the current pressure on the cost of living. This is also supported by salary increments and the fund needs for the festive season. We foresee the mid-single digit growth is justifiable given the management's resilience on quality financing.

A more lavish dividend.

The Group announced a second interim dividend of 7sen per share. This sums its dividend per share (DPS) for FY23 of 30sen (with a dividend payout of 159%), including a special dividend of 18sen. Excluding a special dividend, a 12sen DPS translates to a dividend payout of 64%.

Given the generous dividend payments in FY23, management has made another important announcement, indicating a more lavish dividend policy moving forward. Commencing FY24, RCE will adopt a new dividend guidance with a dividend payout ratio ranging from 60% to 80%. To recap, the Group previously adopted a dividend payout of 20% - 40% since 2019 and consistently paying >30% payout since.

View & valuation.

We view that the RCE business model is generally healthy as it is sheltered by the auto-deduction payment scheme. However, given the slower economic growth and challenging environment (i.e., higher interest rate and cost of living) this year, potential downside risk remains should there be any need for higher provision.

We maintain our TP of RM2.00 based on a sustainable ROE of 14.5%, cost of equity of 10.5% and long-term growth of 3%, implying a P/B of 1.5x. While RCE is expected to register stable earnings growth in a range of 3% - 5% supported by sustainable loan growth of around 5%, we view that it has reflected in its current P/B valuation of 1.5x, which is above +2SD. As such, we maintain our Hold call.

Table 1: Quarterly trends

Year to 31 March	Dec-21	Mar-22	Jun-22	Mar-22	Dec-22	Mar-23	% chg		Cumulative			KAF	
RM m	3Q22	4Q22	1Q23	2Q23	3Q23	4Q23	QoQ	YoY	FY22	FY23	**% chg**	**2022F**	**12M/F**
Interest and fee income	76.9	74.7	77.7	81.8	81.6	82.6	1.3	10.6	299.5	323.6	8.1	313.9	103.1%
Interest expense	(19.9)	(20.1)	(20.3)	(21.6)	(22.8)	(25.4)	11.3	26.5	(80.2)	(90.1)	12.2	(85.4)	105.5%
Net interest and fee income	**56.9**	**54.7**	**57.3**	**60.2**	**58.8**	**57.3**	**-2.5**	**4.8**	**219.2**	**233.6**	**6.5**	**228.6**	**102.2%**
Non-interest income	5.5	5.7	5.6	6.3	7.3	8.8	19.9	52.8	20.4	28.0	37.4	21.4	131.0%
Operating income	**62.5**	**60.4**	**62.9**	**66.5**	**66.1**	**66.1**	**-0.1**	**9.4**	**239.6**	**261.6**	**9.2**	**250.0**	**104.7%**
Operating expenses	(14.3)	(13.1)	(11.8)	(11.1)	(14.6)	(11.5)	-21.3	-12.5	(50.9)	(49.0)	-3.7	(53.1)	92.3%
Underlying profit	**48.2**	**47.3**	**51.1**	**55.4**	**51.5**	**54.6**	**5.9**	**15.4**	**188.8**	**212.6**	**12.6**	**196.9**	**108.0%**
Allowance for impairment	(1.9)	(5.9)	(8.2)	(6.9)	(5.5)	(8.2)	49.0	39.2	(11.5)	(28.7)	148.5	(14.4)	198.9%
Exceptional	0.0	0.0	0.0	0.0	0.0	0.0	n.a.	n.a.	0.0	0.0	n.a.	n.a.	na
Pre-tax profit	**46.4**	**41.4**	**42.9**	**48.6**	**46.1**	**46.4**	**0.8**	**12.1**	**177.2**	**183.9**	**3.8**	**182.5**	**100.8%**
Taxation	(11.7)	(9.9)	(10.7)	(12.0)	(10.9)	(11.6)	6.6	17.3	(44.1)	(45.2)	2.5	(45.4)	99.5%
Net profit	**34.7**	**31.5**	**32.2**	**36.5**	**35.2**	**34.8**	**-1.0**	**10.5**	**133.2**	**138.8**	**4.2**	**137.1**	**101.2%**

Source: Company, KAF

Disclosure Appendix

Recommendation structure

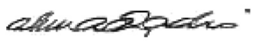
Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

Disclaimer



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