

16 Jun 2020

Buy

Price
 RM1.81

Target Price
 RM2.30 (from RM2.25)

Market Data

	RCE MK
Bloomberg Code	RCE MK
No. of shares (m)	353.2
Market cap (RMm)	614.6
52-week high/low (RM)	1.97 / 1.22
Avg daily turnover (RMm)	1.1
KLCI (pts)	1,498.8

Source: Bloomberg, KAF

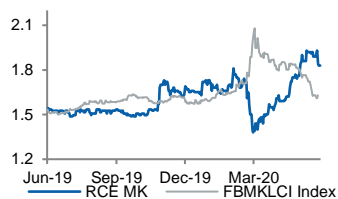
Major Shareholder (%)

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

Source: Bloomberg, KAF

Performance

	3M	6M	12M
Absolute (%)	16.0	7.4	6.1
Rel Market (%)	4.1	12.6	16.0



Source: Bloomberg, KAF

Analyst

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RCE Capital

Results in line

We maintain our Buy rating on RCE Capital (RCE) with a slightly higher target price at RM2.30, based on our GGM valuation. FY20 results broadly in line with expectations. Despite a potential contraction of the broad economy this year, we expect RCE to be less impacted as majority of its customers are civil servants with auto salary deduction repayment mechanism in place. However, we do expect higher provisions this year as GDP is one of the forward-looking variables in arriving to its expected credit loss (ECL). RCE trades at a PBR of 0.8x FY21F, which is below its five-year average PBR of 1.0x.

Financial Highlights

FYE Mar	2018	2019	2020	2021F	2022F
Operating income (RMm)	188.3	200.0	221.3	228.1	245.0
Net profit	88.7	95.5	110.6	110.0	119.4
EPS (sen)	25.1	27.0	31.3	31.1	33.8
EPS growth (%)	12.3	7.7	15.8	(0.5)	8.5
Net DPS (sen)	7.0	8.7	10.9	10.8	11.8
Net yield (%)	3.9	4.8	6.0	6.0	6.5
PER (x)	7.2	6.7	5.8	5.8	5.4
PB (x)	1.2	1.1	0.9	0.8	0.7
ROE (%)	18.5	17.3	17.6	15.2	14.6

Source: Company, KAF

FY20 results in line. RCE recorded net profit of RM111m in FY20, +16% yoy. This is broadly in line with our net profit forecast of RM109m or c.1% variance (consensus: 3%). The growth was supported by higher operating income, +11% yoy, stemmed mainly from higher disbursement of consumer financing product, i.e., +6% yoy.

Slight improvement in NPL. RCE's NPL ratio was 4.1% in FY20, slightly better than 4.4% in FY19 on improved asset quality. Receivables grew c.5% yoy, while NPLs fell by c.1% yoy. RCE's coverage ratio remained high at 173% in FY20. This was expected as management has adopted stringent risk management and a prudent provisioning policy. We think this is justified as consumer financing is unsecured in nature.

Less vulnerable due to auto salary deduction mechanism. We believe RCE would be less impacted relative to other personal lenders as its customers are largely government's civil servants. As the government had been very supportive with its stimulus packages to protect the well-being of its citizens during Covid-19 pandemic, it's unlikely there would be major cutback from the government side. In addition, the auto salary deduction repayment mechanism is in place and applicable to all civil servants. This shall cushion the impact of loan non-repayment.

Higher provision from ECL model. Despite registering a lower provision in FY20, its 4Q20 provision has surged by 33% yoy and 75% qoq. This is due to the forward-looking variable (real GDP) in its current expected credit loss (ECL) model. In view of this trend, we expect the group to register a higher provision in FY21F by 31% yoy or c.13% of its total operating income (FY20: c.10%).

1% receivables growth target. RCE's receivables grew by 5% in FY20. However, looking over FY21F, the management are unable to provide any guidance on the receivables growth. Taking a cautious stance, we only expect the group to register a marginal receivables growth at 1% in FY21F. Minimal receivables growth along with higher provision, would likely translate into a flattish-year for the group.

Hefty distributable reserve. Despite paying a regular dividend, RCE has a hefty distributable reserve. This is made possible from its profitable and low-Capex business model. Within our forecast periods, we believe another special dividend is possible.

Assuming that RCE is able to maintain its performance as per our forecasts, while maintaining its retention rate, we estimate that its reserves will replenish to its pre-special dividend level by FY22F. Our DPS estimate for FY21F-22F of 11-12 sen excludes any special dividend.

Generous dividend. A DPS of 6 sen was declared in 4Q20. This brings a total DPS of 11 sen in FY20 or c.35% payout ratio. RCE has a dividend payout policy of 20-40% of net profit. We expect a DPS of 10.8 sen in FY21F. Our estimate is based on the same payout ratio as FY20, i.e., 35%. At the current price, this implies a 6-7% yield.

Valuation. RCE trades at a PBR 0.8x FY21F – below its five-year average PBR of 1.0x, which we find attractive. Also, RCE is trading at a discount to the banks (avg PBR: 0.9x). Although RCE's assets quality is lower than the banks, this is offset by higher NIM (7-8%) and high coverage ratio (173%) to manage the risk. Our GGM-derived TP of RM2.30 implies a PBR of 1.1x. Maintain Buy.

Table 1: Quarterly trends

Year to 31 March	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	% chg		Cumulative			KAF	
	3Q19	4Q19	1Q20	2Q20	3Q20	4Q20	qoq	yoy	FY19	FY20	% chg	2020F	12M /F
Interest and fee income	67	67	67	70	73	73	1%	8%	263	283	8%	277	102%
Interest expense	(20)	-20	(20)	(20)	-20	(21)	2%	4%	(78)	(82)	5%	(82)	99%
Net interest and fee income	47	47	47	50	52	52	0%	10%	185	201	9%	195	103%
Non-interest income	4	4	5	5	5	5	2%	35%	15	20	32%	25	81%
Operating income	51	51	51	55	57	57	0%	12%	200	221	11%	220	101%
Operating expenses	(12)	(12)	(14)	(13)	-12	(11)	-2%	-3%	(45)	(49)	9%	(50)	99%
Underlying profit	39	39	38	42	46	46	1%	17%	155	172	11%	170	101%
Provisions	(4)	(6)	(5)	(6)	-5	(8)	75%	33%	(24)	(23)	-3%	(20)	116%
Exceptional	0	0	0	0	0	0	nm	nm	0	0	na	na	na
Pre-tax profit	35	33	33	37	41	38	-8%	14%	131	149	14%	150	99%
Taxation	(10)	(10)	(9)	(10)	-10	(10)	-5%	0%	(36)	(38)	8%	(41)	94%
Net profit	25	24	24	27	31	28	-9%	19%	96	111	16%	109	101%

Source: Company, KAF

Exhibit 1: Income Statement

FYE March (RM m)	2018	2019	2020	2021F	2022F
Net interest income	149.2	156.2	175.1	181.0	195.6
Non-interest income	39.1	43.8	46.2	47.1	49.5
Total income	188.3	200.0	221.3	228.1	245.0
Operating costs	(41.3)	(45.2)	(49.3)	(50.8)	(54.6)
Pre-prov operating profit	147.0	154.8	172.0	177.3	190.4
Provision charges	(29.5)	(23.7)	(23.1)	(30.2)	(31.7)
Pre-tax profit	117.4	131.0	148.9	148.1	160.8
Taxation	(28.7)	(35.6)	(38.3)	(38.1)	(41.4)
Net Profit	88.7	95.5	110.6	110.0	119.4

Source: Company, KAF

Exhibit 2: Balance Sheet

FYE March (RM m)	2018	2019	2020	2021F	2022F
Consumer financing	1,689.9	1,598.7	1,689.9	1,723.7	1,809.9
Factoring and confirming	3.8	3.7	3.0	2.5	2.0
Deposits with financial institutiona	169.6	275.8	360.7	360.0	384.2
Plant and equipment	6.2	4.5	13.1	13.1	14.0
Investment in properties	0.0	0.0	0.0	0.0	0.0
Goodwill on consolidation	47.3	47.3	47.3	47.2	50.4
Other investments	0.0	0.0	0.0	0.0	0.0
AFS financial assets	0.0	0.0	0.0	0.0	0.0
Deferred tax assets	39.5	42.0	45.4	45.3	48.4
Other receivables and deposits	40.0	37.5	12.0	12.0	12.0
Asset held for sale	0.0	0.0	0.0	0.0	0.0
Cash and bank balances	27.6	216.6	259.5	222.2	268.2
Total Assets	2,024.0	2,226.1	2,431.0	2,426.1	2,589.1
Borrowings	1,298.5	1,604.9	1,714.4	1,637.5	1,719.4
Payables and accruals	33.0	27.0	31.0	30.9	33.0
Hire purchase	1.3	1.1	0.7	1.0	1.4
Deferred tax liabilities	0.3	0.0	5.2	5.2	5.5
Tax liabilities	6.4	9.7	6.4	6.4	6.8
Total Liabilities	1,339.5	1,642.6	1,757.7	1,681.0	1,766.1
Share capital	31.3	134.5	146.3	146.3	146.3
Redeemable convertible preference shares	0.0	0.0	0.0	0.0	0.0
Reserves	487.9	449.0	527.0	598.8	676.7
Total Shareholders' Equity	519.3	583.5	674.0	746.0	823.0
Total Liabilities & Equity	1,858.8	2,226.1	2,431.0	2,426.1	2,589.1

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.

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