

9 December 2020

Financial Services | Banks

RCE Capital (RCE MK)

Buy (Maintained)

Steady As It Goes; Keep BUY

Target Price (Return): MYR2.80 (+14%)
Price: MYR2.45
Market Cap: USD215m
Avg Daily Turnover (MYR/USD) 0.76m/0.18m

- **Keep BUY, with new TP MYR2.80 from MYR2.50, 14% upside and c.5% yield.** RCE Capital's share price saw a strong rally (+25%) since mid-November. We believe the market is finally beginning to recognise its consistent delivery in earnings and dividends. Despite the handsome share price performance, valuation is still attractive a mere 1.0x FY22F (Mar) P/BV, against ROE of c.15% and 5% yield. Operations remain largely business-as-usual with no imminent concerns of either asset quality or demand for credit.
- **Latest update: All is well.** Based on our latest channel check, RCE Capital's operations are mostly business-as-usual. Underlying demand for credit remains robust while the salary-deduction collection scheme is still running smoothly. Although the disbursement process has slightly slowed at the employer-verification section due to most civil servants working from home, we see this as a minor inconvenience and hardly a concern to the company's operations, if at all.
- **3QFY21F results preview.** While there are about three weeks before Dec 2020 ends, we believe RCE Capital's 3QFY21F results will remain resilient given its niche business model. That said, PATAMI is likely to see a QoQ normalisation from 2QFY21; 2QFY21 PATAMI was partially lifted by the delayed recognition of an early settlement fee income due to the Movement Control Order (MCO) during 1QFY21. The biggest swing factor is still the changes in macroeconomic variables used in the Expected Credit Loss (ECL) model, which could result in higher provisions. However, we reiterate that these extra provisions are purely model-related and do not always reflect the company's true asset quality, which has shown tremendous resilience amidst the challenging 2020.
- **Earnings and TP.** We make no changes to our forecasts. Our GGM-derived TP is raised to MYR2.80 as we lower our risk premium assumption. In our opinion, RCE Capital has repeatedly demonstrated consistent delivery in earnings and dividends that resulted in the YTD share price uplift. Even after the YTD rally, the stock still looks attractive at the current valuation of 1.0x FY22F P/BV.

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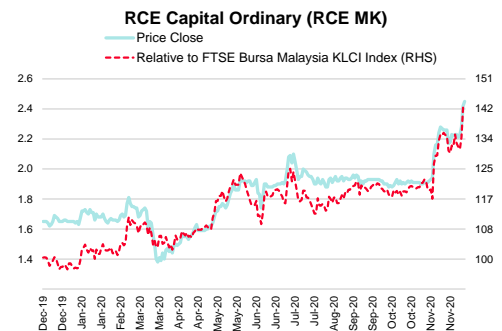


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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	48.5	27.6	28.9	29.6	47.6
Relative	46.4	20.8	22.1	25.3	44.1
52-wk Price low/high (MYR)				1.38	2.45



Source: Bloomberg

Forecasts and Valuation	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
Reported net profit (MYRm)	96	111	110	119	125
Net profit growth (%)	7.7	15.8	(0.2)	7.9	4.9
Recurring net profit (MYRm)	96	111	110	119	125
Recurring EPS (MYR)	0.28	0.32	0.32	0.34	0.36
BVPS (MYR)	1.71	1.94	2.16	2.42	2.70
DPS (MYR)	0.09	0.11	0.12	0.12	0.12
Recurring P/E (x)	8.74	7.70	7.78	7.21	6.87
P/B (x)	1.43	1.26	1.13	1.01	0.91
Dividend Yield (%)	3.7	4.5	4.9	4.7	4.9
Return on average equity (%)	17.3	17.6	15.4	14.8	13.9

Source: Company data, RHB

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD1bn.

Financial Exhibits

Asia	Financial summary (MYR)	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
Malaysia	EPS	0.28	0.32	0.32	0.34	0.36
Financial Services	Recurring EPS	0.28	0.32	0.32	0.34	0.36
RCE Capital	DPS	0.09	0.11	0.12	0.12	0.12
RCE MK	BVPS	1.71	1.94	2.16	2.42	2.70
Buy						
	Valuation metrics	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
Valuation basis	Recurring P/E (x)	8.74	7.70	7.78	7.21	6.87
Our GGM assumptions are:	P/B (x)	1.4	1.3	1.1	1.0	0.9
i. CoE of 13.2%;	Dividend Yield (%)	3.7	4.5	4.9	4.7	4.9
ii. ROE of 14.7%;						
iii. 2% long-term growth rate						
Key drivers	Income statement (MYRm)	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
Our FY21 forecasts are most sensitive to changes in:	Interest income	234	257	268	279	287
i. Financing margins;	Interest expense	(78)	(82)	(87)	(91)	(91)
ii. Impairment allowances;	Net interest income	156	175	181	188	196
iii. Growth in receivables.	Non interest income	39	46	48	49	52
	Total operating income	195	221	229	238	248
	Overheads	(45)	(49)	(53)	(55)	(57)
	Pre-provision operating profit	150	172	176	183	190
	Loan impairment allowances	(18)	(23)	(27)	(23)	(22)
	Pre-tax profit	131	149	149	160	168
	Taxation	(36)	(38)	(38)	(41)	(43)
	Reported net profit	96	111	110	119	125
	Recurring net profit	96	111	110	119	125
Key risks	Profitability ratios	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
i. Higher credit cost;	Return on average assets (%)	4.7	4.7	4.3	4.3	4.4
ii. Weaker net financing margins;	Return on average equity (%)	17.3	17.6	15.4	14.8	13.9
iii. Weaker growth in receivables.	Return on IEAs (%)	12.2	12.2	11.9	11.8	11.7
	Cost of funds (%)	5.4	4.9	4.8	4.8	4.7
	Net interest spread (%)	6.9	7.3	7.1	7.1	7.0
	Net interest margin (%)	8.2	8.3	8.1	8.0	8.0
	Non-interest income / total income (%)	19.8	20.9	20.9	20.8	20.8
	Cost to income ratio (%)	23.2	22.2	23.2	23.1	23.2
	Credit cost (bps)	110	130	149	119	110
Company Profile	Balance sheet (MYRm)	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
RCE Capital provides general financing services to civil servants - repayments are done via direct salary deductions. Its wholly-owned EXP Payment unit offers payroll collection management services for government departments under the purview of the Accountant General's Department.	Total gross loans	1,729	1,820	1,866	1,965	2,049
	Other interest earning assets	279	364	444	438	438
	Total gross IEAs	2,009	2,184	2,309	2,403	2,487
	Total provisions	(130)	(130)	(142)	(151)	(159)
	Net loans to customers	1,599	1,690	1,724	1,814	1,890
	Total net IEAs	1,878	2,054	2,168	2,253	2,328
	Total non-IEAs	348	377	517	541	599
	Total assets	2,226	2,431	2,685	2,794	2,928
	Other interest-bearing liabilities	1,605	1,714	1,893	1,913	1,949
	Total IBLs	1,605	1,714	1,893	1,913	1,949
	Total non-IBLs	38	43	35	32	32
	Total liabilities	1,643	1,758	1,928	1,945	1,982
	Share capital	154	172	179	185	191
	Shareholders' equity	584	673	756	849	946
	Asset quality and capital	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
	Reported NPLs / gross cust loans (%)	4.4	4.1	4.7	4.6	4.6
	Total provisions / reported NPLs (%)	172.1	173.0	163.3	166.5	168.3

Source: Company data, RHB

Valuation

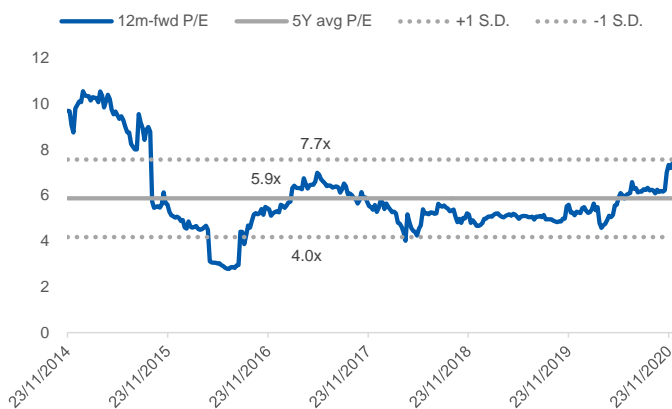
Our GGM-derived TP is raised to MYR2.80 from MYR2.50 and values RCE Capital at 1.14x FY22F P/BV, which is above +1SD from its historical mean. Although already trading at +1SD, we believe the company’s historical P/BV is not properly reflected as the market is only beginning to recognise its consistent delivery in earnings and dividend. It remains our Top Pick among non-bank lenders on its resilient asset quality.

Figure 1: RCE Capital’s GGM valuation

Cost of equity (COE) computation:		Sustainable ROE (%)	14.7
Risk free rate (%)	2.9	COE (%)	13.2
Equity premium (%)	7.4	Long-term growth (g)	2.0
Beta (x)	1.4	Implied P/BV (x)	1.14
Cost of equity - CAPM (%)	13.2	BVPS – FY22F	MYR 2.42
		Target price	MYR 2.76
		TP (rounded)	MYR 2.80

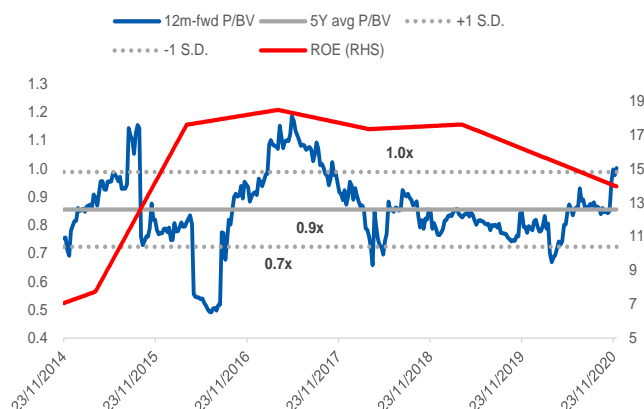
Source: Company data, RHB

Figure 2: RCE Capital’s 12-month forward P/E



Source: Bloomberg, RHB

Figure 3: RCE Capital’s 12-month forward P/BV



Source: Bloomberg, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-07-06	Buy	2.50	1.92
2020-06-16	Buy	2.20	1.81
2020-03-15	Buy	2.10	1.50
2020-02-19	Buy	2.20	1.77
2020-01-10	Buy	2.10	1.72
2019-08-16	Not Rated	na	1.60

Source: RHB, Bloomberg

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Analyst	Company
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