

16 February 2023

Financial Services | Banks

RCE Capital (RCE MK)

Neutral (Maintained)

3QFY23: No Major Surprises

Target Price (Return): MYR1.95 (+5%)
 Price (Market Cap): MYR1.85 (USD309m)
 ESG score: 3.10 (out of 4)
 Avg Daily Turnover (MYR/USD) 0.95m/0.21m

- **Keep NEUTRAL and GGM-derived TP of MYR1.95, 5% upside and c.4% yield.** RCE Capital's 9MFY23 (Mar) results met our and consensus estimates, with stronger fee income and sequentially improving impairment allowances being the key standouts. While financing growth has been strong YTD, the expected upward normalisation of credit costs led to flattish bottomline growth on a 9M basis. We deem the counter to be fairly valued at the current juncture given it is trading near +2SD from its 5-year mean forward P/BV.
- **9MFY23 earnings within expectations.** 9MFY23 net earnings of MYR103.9m met our and Street forecasts. Earnings growth of 2.3% YoY was largely due to higher non-II (+42% YoY) on higher customer refinancing activities, while NII remained flattish. The higher operating income base and lower opex (-1% YoY) led to a PIOP of MYR158m (+12% YoY). Impairment allowances of MYR20.5m were up three-fold YoY, although this mainly arose from the low base effect as credit costs were exceptionally low between FY21-22. At the 9-month mark, the group's ROE stood at 16.9% (9MFY22: 16.8%).
- **Financing growth still robust.** Gross financing as at 31 Dec 2022 stood at MYR1.98bn – up 6% YoY and 5% YTD. Discussions with management suggest that financing demand among civil servants is still being sustained, despite the rising cost of living and upward repricing of assets. Management is hopeful that the company's financing growth can track the wider banking industry's, which we expect to grow at a mid-single digit rate.
- **Asset quality continues to improve.** RCE recorded impairment allowances of MYR5.5m in 3QFY23 – down 20% QoQ, but tripled YoY. This does not immediately concern us as credit costs were exceptionally low during the pandemic and are now returning to pre-pandemic levels of 100-200bps (3QFY23 credit cost: 111bps). Despite this, management is observing stable repayment trends, leading us to believe that the group's asset quality remains solid.
- **Forecasts and valuation.** Our forecasts remain relatively unchanged as lower asset yields are offset by higher non-II. Our TP is kept at MYR1.95, and includes a 2% ESG premium, which is in line with our in-house methodology. The counter is currently trading at a forward P/BV of 1.4x, near +2SD from its 5-year mean. We believe RCE's defensive attributes – namely its resilient salary deduction scheme and prudent asset quality controls – have been well priced in by the market, and thus, we stick to our NEUTRAL call.
- **Key risks** include higher-than-expected credit costs and weaker-than-expected financing growth. The converse, including favourable regulatory developments concerning civil servants, present upside risks.

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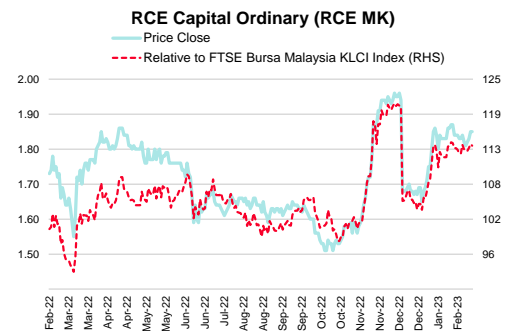


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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	9.5	(0.5)	11.4	12.8	6.9
Relative	10.0	0.0	8.8	13.9	13.9
52-wk Price low/high (MYR)	1.51 – 1.96				



Source: Bloomberg

Overall ESG Score: 3.10 (out of 4)

E: GOOD

The group maintains transparent and detailed disclosures of its Scope 1 and Scope 2 emissions, which has recorded a decent reduction of 3% between FY22 (Mar) and FY20. Fosters a culture of green volunteerism through its Green Warriorz Team, and has designated e-waste containers on office floors to encourage proper disposal of e-waste such as unused gadgets and batteries.

S: GOOD

RCE outsources auditing of its IT systems to ensure competency standards are met. The group, in collaboration with Yayasan Azman Hashim, also provides study grants and scholarships to deserving underprivileged students to pursue Chartered Accountancy certifications. To date, MYR524,000 has been distributed under the programme.

G: EXCELLENT

The Board comprises of nine non-executive directors, five of whom are independent directors. Board members have a maximum allowed tenure of nine years, to facilitate Board refreshment. However, in FY22, there was a one-off incident of non-compliance in relation to a late payment of service tax due to administrative delay, but that has since been resolved.

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD0.5bn.

Forecasts and Valuation	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
Reported net profit (MYRm)	125	133	135	139	148
Net profit growth (%)	12.7	6.9	1.4	3.2	5.9
Recurring net profit (MYRm)	125	133	135	139	148
Recurring EPS (MYR)	0.18	0.18	0.18	0.19	0.20
BVPS (MYR)	1.13	1.19	1.14	1.30	1.45
DPS (MYR)	0.07	0.07	0.08	0.08	0.09
Recurring P/E (x)	10.18	10.17	10.03	9.72	9.18
P/B (x)	1.64	1.55	1.62	1.42	1.27
Dividend Yield (%)	3.8	4.1	4.3	4.3	4.6
Return on average equity (%)	17.2	16.2	15.8	15.6	14.6

Source: Company data, RHB

See important disclosures at the end of this report

Market Dateline / PP 19489/05/2019 (035080)

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Financial Services | Banks

Financial Exhibits

Asia	Financial summary (MYR)	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
Malaysia	EPS	0.18	0.18	0.18	0.19	0.20
Financial Services	Recurring EPS	0.18	0.18	0.18	0.19	0.20
RCE Capital	DPS	0.07	0.07	0.08	0.08	0.09
RCE MK	BVPS	1.13	1.19	1.14	1.30	1.45
Neutral						
	Valuation metrics	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
	Recurring P/E (x)	10.18	10.17	10.03	9.72	9.18
	P/B (x)	1.6	1.6	1.6	1.4	1.3
	Dividend Yield (%)	3.8	4.1	4.3	4.3	4.6
	Income statement (MYRm)	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
	Interest income	273	275	275	286	300
	Interest expense	(81)	(80)	(86)	(94)	(97)
	Net interest income	192	194	189	192	203
	Non interest income	39	45	68	71	73
	Total operating income	232	239	257	262	277
	Overheads	(49)	(51)	(51)	(53)	(56)
	Pre-provision operating profit	183	189	206	209	221
	Loan impairment allowances	(16)	(12)	(26)	(24)	(24)
	Pre-tax profit	167	177	180	186	197
	Taxation	(43)	(44)	(45)	(46)	(49)
	Reported net profit	125	133	135	139	148
	Recurring net profit	125	133	135	139	148
	Profitability ratios	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
	Return on average assets (%)	5.1	5.1	4.8	4.7	4.7
	Return on average equity (%)	17.2	16.2	15.8	15.6	14.6
	Return on IEAs (%)	11.7	10.9	10.6	10.7	10.7
	Cost of funds (%)	4.8	4.6	4.5	4.7	4.7
	Net interest spread (%)	7.0	6.2	6.1	6.0	6.0
	Net interest margin (%)	8.3	7.7	7.3	7.2	7.2
	Non-interest income / total income (%)	17.0	18.9	26.5	26.9	26.5
	Cost to income ratio (%)	21.1	21.1	19.8	20.2	20.2
	Credit cost (bps)	85.1	62.0	133.1	114.9	111.3
	Balance sheet (MYRm)	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
	Total gross loans	1,845	1,879	2,011	2,111	2,217
	Other interest earning assets	625	702	604	631	660
	Total gross IEAs	2,471	2,581	2,615	2,743	2,877
	Total provisions	(124)	(115)	(129)	(141)	(153)
	Net loans to customers	1,721	1,764	1,882	1,970	2,063
	Total net IEAs	2,346	2,466	2,485	2,602	2,724
	Total non-IEAs	144	260	415	433	467
	Total assets	2,491	2,725	2,901	3,035	3,191
	Other interest-bearing liabilities	1,671	1,804	2,015	2,035	2,075
	Total IBLs	1,671	1,804	2,015	2,035	2,075
	Total non-IBLs	46	49	49	50	50
	Total liabilities	1,717	1,853	2,063	2,084	2,126
	Share capital	188	201	213	226	239
	Shareholders' equity	774	872	837	951	1,065
	Asset quality and capital	Mar-21	Mar-22	Mar-23F	Mar-24F	Mar-25F
	Reported NPLs / gross cust loans (%)	4.0	3.8	3.8	3.8	3.8
	Total provisions / reported NPLs (%)	168.4	162.8	169.1	175.9	182.1

Source: Company data, RHB

Results At a Glance

Figure 1: RCE – Summary of 3QFY23 and 9MFY23 results

FYE Mar (MYRm)	3QFY22	2QFY23	3QFY23	QoQ (%)	YoY (%)	9MFY22	9MFY23	YoY (%)	Comments – 9MFY23 vs 9MFY22
Net Interest Income	49.0	49.3	47.2	(4.3)	(3.6)	143.9	145.4	1.0	
Interest income	69.0	71.0	70.1	(1.3)	1.5	204.3	210.2	2.9	Driven by robust receivables growth (+6% YoY), but offset slightly on lower yields (-77bps).
Interest expense	(20.0)	(21.6)	(22.8)	5.6	14.2	(60.4)	(64.9)	7.4	In line with increased <i>sukuk</i> funding (+19% YoY).
Non-Interest Income	13.4	17.2	18.8	9.7	40.3	35.2	50.0	42.3	Higher fee income on increased refinancing activities by customers.
<i>Non-IT/Total income (%)</i>	21.5	25.8	28.5			19.6	25.6		
Operating Income	62.4	66.5	66.0	(0.7)	5.8	179.0	195.4	9.1	
Overhead expenses	(14.2)	(11.0)	(14.5)	31.4	2.3	(37.6)	(37.3)	(0.5)	
<i>CIR (%)</i>	22.7	16.6	22.0			21.0	19.1		
PIOP	48.2	55.4	51.5	(7.0)	6.9	141.5	158.0	11.7	
Impairment on financing	(1.9)	(6.9)	(5.5)	(20.3)	>100	(5.7)	(20.5)	>100	Hefty pre-emptive provisions made in 1QFY23 for civil servants that retired early or have left the service. Credit costs are normalising to pre-pandemic levels of 100-200bps.
<i>Ann. credit costs (bps)</i>	40	142	111			44	151		
PBT	46.4	48.6	46.1	(5.2)	(0.6)	135.8	137.5	1.3	
Taxation	(11.7)	(12.0)	(10.9)			(34.2)	(33.6)		
<i>ETR (%)</i>	25.1	24.8	23.6			25.2	24.4		
Net Earnings	34.7	36.5	35.2	(3.7)	1.4	101.6	103.9	2.3	In line with our and Street forecasts.
Other key data and ratios									
Gross financing	1,862.1	1,957.6	1,978.5	1.1	6.3				Management guided for financing growth to track growth of the banking industry (RHB forecast: +5.4% YoY in CY23).
Total borrowings	1,751.9	1,844.3	2,086.1	13.1	19.1				
Total assets	2,637.3	2,807.4	2,908.7	3.6	10.3				
Shareholders' funds	840.6	911.7	771.8	(15.4)	(8.2)				
ROAA (%)	5.3%	5.2%	4.9%			5.3%	4.9%		
ROAE (%)	16.7%	16.4%	16.7%			16.8%	16.9%		

Source: Company data, RHB

Figure 2: Revisions in full-year earnings forecasts

FYE Mar	Net profit (MYR m)			EPS (MYR)			DPS (MYR)		
	Previous	Revised	% Chg	Previous	Revised	% Chg	Previous	Revised	% Chg
2023F	136.3	135.0	-0.5	0.19	0.18	-0.5	0.26*	0.26*	0.0
2024F	139.8	139.3	-0.3	0.19	0.19	-0.3	0.08	0.08	0.0
2025F	147.3	147.5	0.1	0.20	0.20	0.1	0.09	0.09	0.0

Note: *Comprises 8 sen core DPS and 18 sen special DPS
Source: Company data, RHB

Valuation and TP

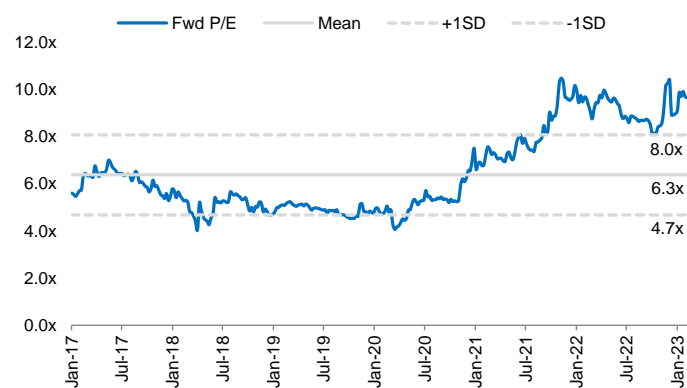
Our TP of MYR1.95 (maintained) is based on a GGM-derived fair value P/BV of 1.48x on RCE's 12-month blended forward BVPS. This compares against the other non-bank lenders' P/BV multiples of around 1-1.2x. We believe the stock is fairly valued, given that it is trading at near +2SD from its 5-year mean, with RCE's defensive attributes already priced in. We keep our NEUTRAL call on the counter.

Figure 3: RCE – GGM valuation summary

Cost of equity (COE) computation:		Sustainable ROE (%)	15.3
Risk free rate (%)	4.0	COE (%)	11.5
Equity premium (%)	6.5	Long-term growth (g)	3.5
Beta (x)	1.2	Implied P/BV (x)	1.48
Cost of equity - CAPM (%)	11.5	BVPS – 12-month forward	MYR1.29
		Intrinsic value	MYR1.91
ESG premium/(discount) (%)	2.0	ESG premium/(discount)	MYR0.04
		TP (rounded)	MYR1.95

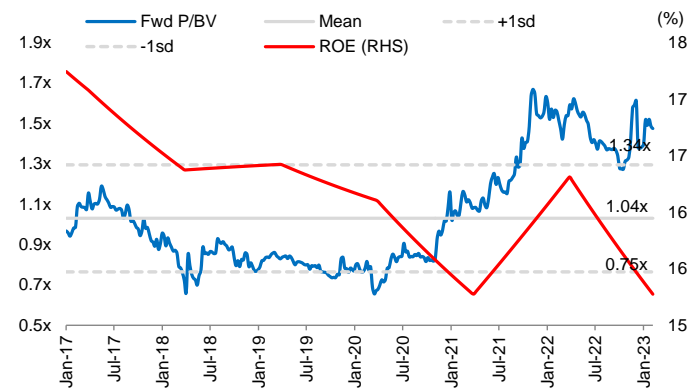
Source: Company data, RHB

Figure 4: RCE's 12-month forward P/E



Source: Bloomberg, RHB

Figure 5: RCE's 12-month forward P/BV vs ROE



Source: Bloomberg, RHB

Recommendation Chart

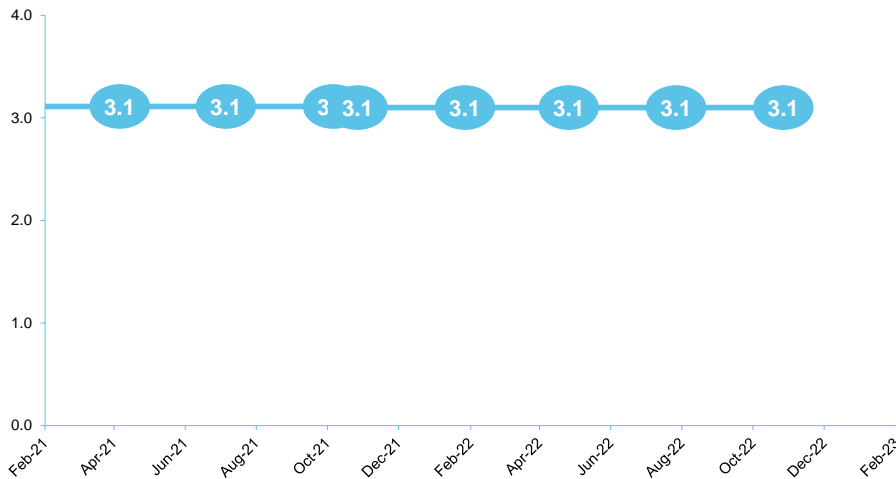


Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2022-11-22	Neutral	1.95	1.87
2022-08-12	Buy	1.92	1.64
2022-05-31	Buy	2.00	1.76
2022-02-25	Buy	1.90	1.69
2021-11-10	Neutral	3.90	2.02
2021-08-12	Buy	3.20	1.43
2021-05-26	Buy	3.20	1.43
2021-02-09	Buy	3.00	1.32
2020-12-08	Buy	2.80	1.29
2020-08-18	Buy	2.50	1.02
2020-07-06	Buy	2.50	1.01
2020-06-16	Buy	2.20	0.95
2020-03-15	Buy	2.10	0.79
2020-02-19	Buy	2.20	0.93
2020-02-19	Buy	2.20	0.93

Source: RHB, Bloomberg

ESG Rating History



Source: RHB

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