

# RCE Capital Bhd (RCE MK) In good shape

# Maintain BUY and MYR1.80 TP

2QFY20 earnings/dividends were within/above our expectations. Average lending yields continued to climb while average cost of funds continued to ease, expanding margins. We maintain our earnings and dividend estimates and MYR1.80 TP. Our TP is premised on 0.87x end-CY20E P/BV, which is close to the five-year average 12-month forward P/BV of 0.86x. We continue to favour RCE for its cheap valuations, high ROEs and high dividend yields.

# Earnings in-line but dividends pleasantly surprised

2QFY20 net profit of MYR27.2m (+16% YoY, +13% QoQ) brought 6MFY20 net profit to MYR51.3m (+10% YoY), which was within our/consensus expectations at 52%/52% of FY estimates. 6MFY20 revenue of MYR137.1m (+7% YoY) was also within our expectation at 49% of our FY estimate. That said, the first interim DPS of 5.0sen (+25% YoY) was above our expectation at 56% of our FY estimate. This is because the 6MFY20 DPR employed was 34% or up 5ppts YoY.

# Generally good operating metrics

2QFY20 gross NPL ratio was flat QoQ at 4.4% while 2QFY20 credit cost as a percentage of gross loans ticked up only slightly to 1.3% (1QFY20: 1.0%, 4FY19: 1.4%). Note that AEON Credit Services (M) (ACSM MK, Not Rated) and Malaysia Building Society (MBS MK, Not Rated) have been struggling with credit costs of late. 2QFY20 gross loans also continued to grow 5% YoY (1QFY20: +5% YoY) while 2QFY20 estimated average lending yield hit 14.3% (2QFY19: 13.7%, 1QFY20: 14.1%).

# Profit spreads still on expansion mode

Our earnings and dividends estimates are unchanged for now. That said, we note that the 2QFY20 estimated average lending yield of 14.3% is already higher than our FY20-FY22 forecast of 14.2%. Yet, average cost of funds has been trending downwards. The Zamarad sukuk third tranche was priced at 4.51% or 41bps lower than the first one, which was issued less than eight months ago. We forecast profit spreads to expand to 8.8% this year from -8.5% last year.

FYE Mar (MYR m)	FY18A	FY19A	FY20E	FY21E	FY22E
Operating income	188	200	210	224	236
Pre-provision profit	147	155	163	174	184
Core net profit	89	96	100	106	113
Core FDEPS (MYR)	0.26	0.28	0.28	0.30	0.32
Core FDEPS growth(%)	9.0	7.6	0.7	6.9	6.3
Net DPS (MYR)	0.07	0.09	0.09	0.09	0.09
Core FD P/E (x)	4.7	5.8	5.6	5.2	4.9
P/BV (x)	0.8	1.0	0.8	0.7	0.7
Net dividend yield (%)	5.7	5.5	5.7	5.7	5.7
Book value (MYR)	1.52	1.71	1.90	2.12	2.36
ROAE (%)	18.5	17.3	16.1	15.3	14.7
ROAA (%)	5.0	4.7	4.4	4.4	4.5
Consensus net profit	-	-	100	106	112
MKE vs. Consensus (%)	-	-	(0.0)	0.3	0.8

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# **BUY**

Share Price MYR 1.57

12m Price Target MYR 1.80 (+23%)

Previous Price Target MYR 1.80

#### **Company Description**

RCE Capital is principally involved in the provision of general loan financing services.

#### **Statistics**

52w high/low (MYR)	1.68/1.44
3m avg turnover (USDm)	0.1
Free float (%)	27.7
Issued shares (m)	369
3m avg turnover (USDm) Free float (%) Issued shares (m) Market capitalisation	MYR579.2M
	USD140M

Major shareholders:
Cempaka Empayar Sdn. Bhd. 56.3%
RCE Capital Bhd. 5.5%
Employees Provident Fund 2.3%

#### **Price Performance**



 -1M
 -3M
 -12M

 Absolute (%)
 3
 (4)
 2

 Relative to index (%)
 (1)
 (3)
 8

-RCE Capital Bhd / Kuala Lumpur Composite Index - (RHS, %)

Source: FactSet

Figure 1: Results summary

FY Mar (MYRm)	2QFY3/20	2QFY3/19	% YoY	1QFY3/20	% QoQ	6MFY3/20	6MFY3/19	% YoY
Interest income	63.2	57.6	9.7	61.6	2.6	124.7	114.0	9.4
Other revenue	7.0	7.4	(4.8)	5.4	30.8	12.4	14.2	(12.6)
Revenue	70.2	65.0	8.0	66.9	4.8	137.1	128.2	7.0
Other income	5.2	3.9	33.6	4.8	7.1	10.0	7.5	33.1
Interest expense applicable to revenue	-20.2	-19.4	4.4	-20.4	(0.6)	-40.6	-37.9	7.1
Directors' remuneration and staff costs	-5.6	-5.8	(3.3)	-7.5	(25.5)	-13.1	-10.8	21.2
Allowances for impairment loss on receivables, net	-5.7	-7.4	(23.1)	-4.5	25.4	-10.2	-13.7	(25.5)
Depreciation of plant and equipment and right-of-use asset	-0.4	-0.7	(41.1)	-0.4	5.5	-0.9	-1.5	(42.2)
Other expenses	-6.6	-4.3	54.4	-5.7	16.5	-12.3	-9.4	30.1
Finance costs	-0.0	-0.0	(20.0)	-0.0	(7.7)	-0.0	-0.0	(13.8)
Profit before tax	36.8	31.3	17.7	33.3	10.5	70.1	62.4	12.4
Taxation	-9.6	-7.8	23.5	-9.2	5.1	-18.8	-15.7	19.7
Net profit	27.2	23.5	15.8	24.1	12.6	51.3	46.7	9.9
FD EPS (sen)	7.8	6.9	13.6	7.0	11.3	14.8	13.7	8.1
Net DPS (sen)	5.0	4.0	25.0	=	N/M	5.0	4.0	25.0
Loans & receivables, gross	1,778.8	1,701.2	4.6	1,752.6	2.6	1,778.8	1,701.2	4.6
(Allowance for impairment)	-132.5	-132.1	0.3	-130.1	2.6	-132.5	-132.1	0.3
Loans & receivables, net	1,646.2	1,569.1	4.9	1,622.5	2.6	1,646.2	1,569.1	4.9
	2QFY3/20	2QFY3/19	+/- ppt	1QFY3/20	+/- ppt	6MFY3/20	6MFY3/19	+/- ppt
Tax rate (%)	26.2	25.0	1.2	27.5	(1.3)	26.8	25.2	1.6
Gross NPL ratio (%)	4.4	4.3	0.2	4.4	0.0	4.4	4.3	0.2
Loan loss coverage ratio (%)	167.7	182.6	(14.9)	168.3	(0.6)	167.7	182.6	(14.9)
Net gearing (%)	177.6	201.9	(24.3)	181.0	(3.4)	177.6	201.9	(24.3)

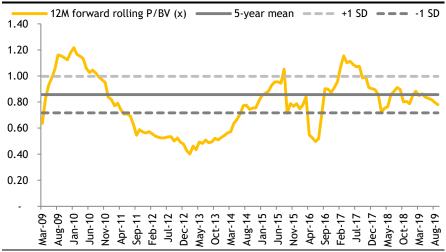
Source: Company

# Results analysis

2QFY20 net profit grew 16% YoY, driven by: (i) loans growth of 5% YoY; (ii) higher estimated average lending yield of 14.3% (2QFY19: 13.7%); and (iii) net impairment loss on receivables easing 23% YoY.

2QFY20 net profit grew 13% QoQ, driven by: (i) loans growth of 3% QoQ; (ii) higher estimated average lending yield of 14.3% (1QFY20: 14.1%); and (iii) directors' remuneration & staff costs easing 26% QoQ (share options were granted in 1QFY20), partially offset by net impairment loss on receivables growing 25% QoQ.

Figure 2: RCE Capital 12M forward rolling P/BV (x)

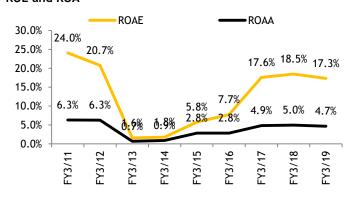


Source: Company, Maybank Kim Eng, Bloomberg

# Value Proposition

- RCE Capital provides personal financing, the ultimate borrowers being civil servants.
- With a gross loans balance of just MYR1.8b, we estimate that its market share is only 2%.
- Non-performing loans kept in check thanks to nondiscretionary direct salary deductions.
- Competitive advantage lies in fast loan processing turnaround time of 48 hours.
- ROE generation surpasses that of the average for the overall banking industry.

#### **ROE and ROA**

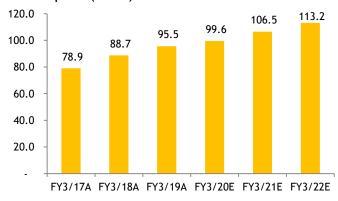


Source: Company, Maybank Kim Eng

# **Financial Metrics**

- Introduced a better credit scoring model in 2013. Forecast gross loans growth of 4-5% p.a. over the next three years.
- Average lending yields may be peaking at 14% but average cost of funds is falling.
- Asset quality better than before. New loans are smaller in size (<MYR20k) and their NPL ratios are low (<2%).</li>
- Forecast stable three-year forward core net profit CAGR of 6% p.a.
- There is room for dividends to surprise to the upside as its DPR policy is only 20-40%.

#### Core net profit (MYRm)



Source: Company, Maybank Kim Eng estimates

# **Price Drivers**



Source: Company, FactSet, Maybank Kim Eng

- 1. Proposed special interim DPS of 10.5 sen. Still paid a final DPS of 3.5sen.
- Proposed capital repayment of MYR0.075/shr and 4-into-1 share consolidation.
- 1QFY17 net profit surged 86% YoY as FY17 revenue grew 39% YoY.
- FY17 net profit surged 98% YoY as FY17 revenue grew 38% YoY.
- 5. Concerns arise that the government may reduce the size of the civil service.

# **Swing Factors**

# Upside

- Easing competition competitors have been reducing their exposure to personal financing.
- Lower interest rates we estimate that every 25bps reduction in cost of funds will accrete 3% to earnings.
- Access to CCRIS if RCE Capital gains access to CCRIS, it can better assess borrowers' total indebtedness.

# **Downside**

- High household debt Household debt to GDP is elevated at >80% and may crimp borrowers' repayment ability.
- Need to leverage RCE Capital cannot take deposits and thus, has to assume debt to finance its loans.
- Asset-liability duration mismatch borrowers' repayment may not match RCE Capital's debt repayment.

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November 12, 2019

FYE 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Key Metrics					
Core P/E (x)	4.7	5.8	5.4	5.1	4.8
Core FD P/E (x)	4.7	5.8	5.6	5.2	4.9
P/BV (x)	0.8	1.0	0.8	0.7	0.7
P/NTA (x)	0.9	1.0	0.9	0.8	0.7
Net dividend yield (%)	5.7	5.5	5.7	5.7	5.7
INCOME STATEMENT (MYR m)					
Interest income	218.5	242.2	259.7	272.6	284.9
Interest expense	(69.4)	(78.1)	(87.5)	(89.3)	(90.7)
Net interest income	149.2	164.2	172.1	183.3	194.1
Islamic banking income	na	na	na	na	na
Other income	39.1	35.8	38.3	40.2	42.0
Total non-interest income	39.1	35.8	38.3	40.2	42.0
Operating income	188.3	200.0	210.4	223.5	236.1
Staff costs	(22.4)	(21.4)	(22.9)	(24.1)	(25.2)
Other operating expenses	(18.9)	(23.8)	(24.3)	(25.4)	(26.5)
Operating expenses	(41.3)	(45.2)	(47.2)	(49.5)	(51.7)
Pre-provision profit	147.0	154.8	163.2	174.0	184.5
Loan impairment allowances	(29.6)	(23.7)	(26.6)	(27.9)	(29.2)
Associates & JV income	0.0	0.0	0.0	0.0	0.0
Pretax profit	117.4	131.1	136.6	146.1	155.3
Income tax	(28.7)	(35.6)	(37.1)	(39.6)	(42.1)
Reported net profit	88.7	95.5	99.6	106.5	113.2
Core net profit	88.7	95.5	99.6	106.5	113.2
BALANCE SHEET (MYR m)					
Cash & deposits with banks	197.2	492.4	532.7	572.3	617.9
Sec. under resale agreements	0.0	0.0	0.0	0.0	0.0
Derivatives financial assets	0.0	0.0	0.0	0.0	0.0
Dealing securities	0.0	0.0	0.0	0.0	0.0
Available-for-sale securities	0.0	0.0	0.0	0.0	0.0
Investment securities	0.0	0.0	0.0	0.0	0.0
Loans & advances	1,528.5	1,602.4	1,680.2	1,760.4	1,826.8
Fixed assets	6.2	4.5	4.5	4.5	4.5
Intangible assets	47.3	47.3	47.3	47.3	47.3
Other assets	79.5	79.5	79.5	79.5	79.5
Total assets	1,858.8	2,226.1	2,344.3	2,464.1	2,576.1
Derivatives financial instruments	0.0	0.0	0.0	0.0	0.0
Subordinated debt	0.0	0.0	0.0	0.0	0.0
Other securities in issue	766.9	1,005.2	1,225.2	1,325.2	1,425.2
Other borrowings	230.4	280.8	106.1	49.7	(21.1)
Other liabilities	342.2	356.6	357.0	357.7	358.4
Total liabilities	1,339.5	1,642.6	1,688.3	1,732.7	1,762.5
Share capital	44.7	154.5	160.0	160.0	160.0
Reserves	474.6	429.1	496.0	571.4	653.6
Shareholders' funds	519.3	583.5	656.0	731.4	813.6
Preference shares	0.0	0.0	0.0	0.0	0.0
Minority interest	0.0	0.0	0.0	0.0	0.0
-	519.3	583.5	656.0	731.4	813.6
Total equity					

FYE 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Key Ratios					
Growth (%)					
Net interest income	14.5	10.1	4.8	6.5	5.9
Non-interest income	(5.6)	(8.3)	6.9	5.0	4.4
Operating expenses	(4.1)	9.4	4.6	4.8	4.3
Pre-provision profit	14.3	5.3	5.4	6.6	6.0
Core net profit	12.3	7.7	4.2	6.9	6.3
Gross loans	8.0	5.2	5.0	5.0	4.0
Customer deposits	na	na	na	na	na
Total assets	9.2	19.8	5.3	5.1	4.5
Profitability (%)					
Non-int. income/Total income	20.8	17.9	18.2	18.0	17.8
Cost/income	21.9	22.6	22.4	22.2	21.9
Liquidity (%)					
Loans/customer deposits	na	na	na	na	na
Asset quality (%)					
Gross NPL	4.1	4.4	4.5	4.7	4.9
Loan loss coverage	178.0	172.1	170.1	167.0	164.1
Capital adequacy (%)					
CET1	na	na	na	na	na
Tier 1 capital	na	na	na	na	na
Risk-weighted capital	na	na	na	na	na
Returns (%)					
ROAE	18.5	17.3	16.1	15.3	14.7
ROAA	5.0	4.7	4.4	4.4	4.5
Shareholders equity/assets	27.9	26.2	28.0	29.7	31.6

Source: Company; Maybank

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#### APPENDIX I: TERMS FOR PROVISION OF REPORT, DISCLAIMERS AND DISCLOSURES

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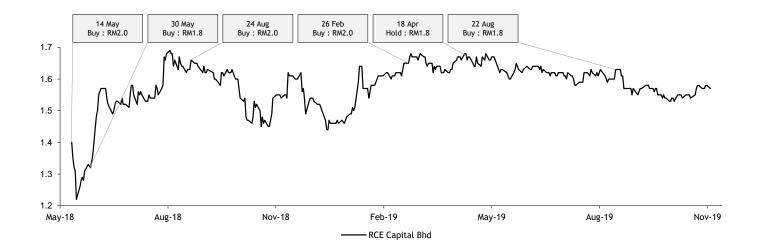
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# Historical recommendations and target price: RCE Capital Bhd (RCE MK)



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November 12, 2019

10