

18 Feb 2020

Buy

Price
 RM1.69

Target Price
 RM2.25 (from RM1.98)

Market Data

Bloomberg Code	RCE MK
No. of shares (m)	351.8
Market cap (RMm)	594.5
52-week high/low (RM)	1.81 / 1.52
Avg daily turnover (RMm)	0.5
KLCI (pts)	1,537.1

Source: Bloomberg, KAF

Major Shareholder (%)

Cempaka Empayar	(60.7%)
EPF	(2.9%)
Cheam Heng Ming	(1.1%)
Free Float	101.0

Source: Bloomberg, KAF

Performance

	3M	6M	12M
Absolute (%)	(3.4)	5.6	4.3
Rel Market (%)	0.8	9.9	14.9



Source: Bloomberg, KAF

RCE Capital

3Q20 results above expectations

We maintain our Buy rating on RCE Capital (RCE) and boost our target price to RM2.25, based on our GGM valuation. 9M20 results exceeded expectations. We have raised our earnings estimate on stronger receivables growth, lower funding cost, and a lower provision charge. RCE trades at a PBR of 0.9x FY20F, which is below its five-year average PBR of 1.0x. Our GGM-derived TP of RM2.25 implies a PBR of 1.2x (+1SD of five-year mean). We think this is justified by decent earnings growth (8-15%), improvement in ROE (16-17%), and high dividend yield (6-7%).

Financial Highlights

FYE Mar	2017	2018	2019	2020F	2021F
Operating income	171.7	188.3	200.0	219.8	234.6
Net profit	78.9	88.7	95.5	109.5	117.8
EPS (sen)	22.4	25.2	27.2	31.1	33.5
EPS growth (%)	99.5	12.3	7.7	14.6	7.6
Net DPS (sen)	3.0	7.0	8.7	10.0	10.8
Net yield (%)	1.8	4.1	5.2	5.9	6.4
PER (x)	7.5	6.7	6.2	5.4	5.0
PBR (x)	1.3	1.1	1.0	0.9	0.8
ROE (%)	17.6	18.5	17.3	17.6	16.8

Source: Company, KAF

Ahead of expectations. RCE recorded net profit of RM82m in 9M20 (84% of our and the consensus forecast), +15% yoy on the back of higher operating income. The group reported 10% yoy operating income growth in 9M20, exceeding 6% full-year growth in FY19. The double-digit income growth stemmed mainly from higher disbursement of consumer financing product, i.e., +5.4% yoy (FY19: +4.8% yoy).

Slight improvement in NPL. RCE's NPL ratio was 4.3% in 3Q20, slightly better than 4.4% in 2Q20 on improved asset quality. Receivables grew c.1.9% yoy, while NPLs fell by c.1.8% yoy.

Lower provision charge. 9M20 earnings were also supported by a lower provision charge, -15% yoy, despite the growth in receivables and operating income. However, its coverage ratio is still high, at 167%. 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.

Lower funding cost from sukuk issuance. To support its receivables growth, RCE issued an additional RM120m Sukuk Zamarad in 3Q20. The total issuance of said sukuk in 9M20 was RM220m. The expected effective yield for the overall RM2.0b sukuk programme is c.5.0%. Overall, at the group level, the average funding cost was c.5.4% in FY19. Therefore, with a lower effective yield, we expect the overall average funding cost to improve every year. We estimate the funding cost to be 5.0-5.1% in FY20-21F.

Raising earnings forecast. Overall, we raise our earnings forecast for FY20F by 11%, mainly to reflect: 1) higher receivables growth at 5.4% (from 5.0%); 2) a lower average funding cost, at 5.1% (from 5.3%); and 3) 20% lower provision charge. Overall, we arrive at net profit forecasts of RM109m for FY20F and RM118m for FY20F, implying a two-year CAGR of 11%. Correspondingly, RCE's sustainable ROE is now at 16.9% (from 15.5%).

Generous dividend. No dividend was declared in 3Q20. RCE has a dividend payout policy of 20-40% of net profit. A dividend per share of 5.0 sen was declared in 2Q20. We expect a DPS of 10.0 sen in FY20F. Our estimate is based on the same payout ratio as FY19, i.e., 32%. At the current price, this implies a 6-7% yield.

Valuation. RCE trades at a PBR 0.9x FY20F – below its five-year average PBR of 1.0x, which we find attractive. Our GGM-derived TP of RM2.25 implies a PBR of 1.2x (+1SD of five-year mean). We think a valuation at +1SD is justified by decent earnings growth, improved ROE, and high dividend yield.

Analyst

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Table 1: Quarterly trends (before revision)

Year to 31 March	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	% chg		Cumulative			KAF	
RM m	2Q19	3Q19	4Q19	1Q20	2Q20	3Q20	qoq	yoy	9M19	9M20	% chg	2020F	9M/F
Interest and fee income	65	67	67	67	70	73	3%	8%	195	210	7%	276	76%
Interest expense	(19)	(20)	(20)	(20)	(20)	(20)	0%	1%	-58	-61	5%	-85	71%
Net interest and fee income	46	47	47	47	50	52	4%	11%	137	149	8%	190	78%
Non-interest income	4	4	4	5	5	5	0%	26%	12	15	30%	16	93%
Operating income	49	51	51	51	55	57	4%	12%	149	164	10%	207	79%
Operating expenses	(11)	(12)	(12)	(14)	(13)	(12)	-8%	0%	-33	-38	13%	-47	81%
Underlying profit	39	39	39	38	42	46	8%	16%	115	126	9%	160	79%
Provisions	(7)	(4)	(6)	(5)	(6)	(5)	-17%	21%	-18	-15	-15%	-25	60%
Exceptional	0	0	0	0	0	0	nm	nm	0	0	nm	na	nm
Pre-tax profit	31	35	33	33	37	41	11%	16%	98	111	14%	135	82%
Taxation	(8)	(10)	(10)	(9)	(10)	(10)	4%	-3%	-26	-29	11%	-37	79%
Net profit	23	25	24	24	27	31	14%	23%	72	82	15%	98	84%

Source: Company, KAF

Table 2: Quarterly trends (after revision)

Year to 31 March	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	% chg		Cumulative			KAF	
RM m	2Q19	3Q19	4Q19	1Q20	2Q20	3Q20	qoq	yoy	9M19	9M20	% chg	2020F	9M/F
Interest and fee income	65	67	67	67	70	73	3%	8%	195	210	7%	277	76%
Interest expense	(19)	(20)	(20)	(20)	(20)	(20)	0%	1%	-58	-61	5%	-82	74%
Net interest and fee income	46	47	47	47	50	52	4%	11%	137	149	8%	195	76%
Non-interest income	4	4	4	5	5	5	0%	26%	12	15	30%	25	60%
Operating income	49	51	51	51	55	57	4%	12%	149	164	10%	220	75%
Operating expenses	(11)	(12)	(12)	(14)	(13)	(12)	-8%	0%	-33	-38	13%	-50	76%
Underlying profit	39	39	39	38	42	46	8%	16%	115	126	9%	170	74%
Provisions	(7)	(4)	(6)	(5)	(6)	(5)	-17%	21%	-18	-15	-15%	-20	75%
Exceptional	0	0	0	0	0	0	nm	nm	0	0	nm	na	nm
Pre-tax profit	31	35	33	33	37	41	11%	16%	98	111	14%	150	74%
Taxation	(8)	(10)	(10)	(9)	(10)	(10)	4%	-3%	-26	-29	11%	-41	71%
Net profit	23	25	24	24	27	31	14%	23%	72	82	15%	109	75%

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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