

## RCE Capital Bhd (RCE MK)

# Set to cross MYR100m net profit mark this financial year?

### Maintain BUY - tweak TP upwards by 2% to MYR1.94

3QFY20/9MFY20 earnings handily beat our expectations. Gross loans continue to grow while profit spreads continue to expand. We raise our EPS estimates by 6-7%. That said, we do not discount the possibility that there maybe more earnings upside going forward as cost of funds continue to fall. Ascribing an unchanged target end-CY20 P/BV of 0.93x (0.5x above the five year average 12-month forward P/BV), we arrive at a higher TP of MYR1.94 (MYR1.91 previously).

### Earnings outperformed our expectations again

3QFY20 net profit of MYR31m (+23% YoY, +14% YoY) brought 9MFY20 net profit to MYR82.3m (+15% YoY), which was above our expectations at 83% of our FY estimate. That said, 9MFY20 revenue of MYR209.6m (+7% YoY) was within our expectations at 74% of our FY estimate. The net profit outperformance was due to: (i) lower than expected interest expense (MYR60.9m or 70% of our FY estimate); and (ii) lower than expected credit cost (MYR14.9m or 56% of our FY estimate).

### Operating metrics generally good still

3QFY20 gross loans continued to grow 5% YoY (2QFY20: +5% YoY) while 3QFY20 estimated average lending yield hit another record high of 14.5% (2QFY20: 14.3%). 3QFY20 gross NPL ratio eased ~10bps QoQ to 4.3% and 3QFY20 trailing four quarters moving average credit cost ratio remained well contained at 1.2%. While 3QFY20 loan loss coverage ratio was down 13ppts YoY and ~30bps QoQ, we opine that it is still sufficiently adequate at 167%.

### Raise EPS estimates but more maybe in store

We raise our FY20/FY21/FY22 EPS estimates by 6%/7%/7% to reflect lower interest expense on less borrowings and lower credit cost ratios (Fig. 2). We remain positive on RCE's earnings outlook as lending yields continue to rise while cost of funds continues to fall. Bank Negara cut the Overnight Policy Rate by 25bps to 2.75% on 22 Jan 2020. This implies to us that the next Zamarad sukuk may be priced even lower than the last tranche which was issued on 19 Nov 2019 at 4.26% profit rate.

FYE Mar (MYR m)	FY18A	FY19A	FY20E	FY21E	FY22E
Operating income	188	200	214	229	242
Pre-provision profit	147	155	167	179	190
Core net profit	89	96	106	114	121
Core FDEPS (MYR)	0.26	0.28	0.30	0.32	0.34
Core FDEPS growth(%)	9.0	7.6	7.2	7.6	6.3
Net DPS (MYR)	0.07	0.09	0.10	0.11	0.11
Core FD P/E (x)	4.7	5.8	5.6	5.2	4.9
P/BV (x)	0.8	1.0	0.9	0.8	0.7
Net dividend yield (%)	5.7	5.5	5.9	6.2	6.5
Book value (MYR)	1.52	1.71	1.91	2.14	2.38
ROAE (%)	18.5	17.3	17.1	16.3	15.6
ROAA (%)	5.0	4.7	4.7	4.8	4.9
Consensus net profit	-	-	100	106	112
MKE vs. Consensus (%)	-	-	6.4	7.4	8.0

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# BUY

Share Price	MYR 1.69
12m Price Target	MYR 1.94 (+21%)
Previous Price Target	MYR 1.91

### Company Description

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

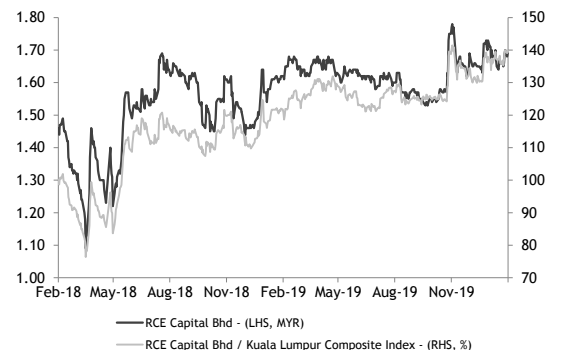
### Statistics

52w high/low (MYR)	1.78/1.53
3m avg turnover (USDm)	0.1
Free float (%)	32.5
Issued shares (m)	371
Market capitalisation	MYR626.4M USD151M

### Major shareholders:

Cempaka Empayar Sdn. Bhd.	51.4%
RCE Capital Bhd.	5.5%
Employees Provident Fund	2.3%

### Price Performance



	-1M	-3M	-12M
Absolute (%)	(2)	(3)	4
Relative to index (%)	1	1	15

Source: FactSet

Figure 1: Summary Results Table

FY Mar (MYRm)	3QFY3/20	3QFY3/19	% YoY	2QFY3/20	% QoQ	9MFY3/20	9MFY3/19	% YoY
Interest income	65.2	60.0	8.7	63.2	3.3	190.0	174.1	9.1
Other revenue	7.3	6.9	4.5	7.0	3.3	19.7	21.1	(6.9)
<b>Revenue</b>	<b>72.5</b>	<b>67.0</b>	<b>8.3</b>	<b>70.2</b>	<b>3.3</b>	<b>209.6</b>	<b>195.2</b>	<b>7.4</b>
Other income	5.2	4.1	25.6	5.2	(0.5)	15.2	11.6	30.4
Interest expense applicable to revenue	-20.3	-20.0	1.4	-20.2	0.4	-60.9	-58.0	5.1
Directors' remuneration and staff costs	-5.4	-5.5	(2.8)	-5.6	(3.9)	-18.5	-16.4	13.1
Allowances for impairment loss on receivables, net	-4.7	-3.9	21.2	-5.7	(17.0)	-14.9	-17.5	(15.2)
Depreciation of plant and equipment & right-of-use asset	-0.5	-0.7	(22.9)	-0.4	19.1	-1.4	-2.2	(36.1)
Other expenses	-5.7	-5.5	4.9	-6.6	(13.3)	-18.0	-14.9	20.8
Finance costs	-0.0	-0.0	71.4	-0.0	100.0	-0.0	-0.0	14.0
<b>Profit before tax</b>	<b>41.0</b>	<b>35.5</b>	<b>15.5</b>	<b>36.8</b>	<b>11.4</b>	<b>111.1</b>	<b>97.8</b>	<b>13.5</b>
Taxation	-10.0	-10.3	(3.1)	-9.6	3.7	-28.8	-26.0	10.6
<b>Net profit</b>	<b>31.0</b>	<b>25.2</b>	<b>23.2</b>	<b>27.2</b>	<b>14.1</b>	<b>82.3</b>	<b>71.8</b>	<b>14.6</b>
FD EPS (sen)	8.8	7.4	20.3	7.8	13.5	23.7	21.0	12.5
Net DPS (sen)	-	-	N/M	5.0	(100.0)	5.0	4.0	25.0
Loans & receivables, gross	1,807.4	1,720.3	5.1	1,778.8	2.6	1,807.4	1,720.3	5.1
(Allowance for impairment)	-129.9	-128.4	1.2	-132.5	2.6	-129.9	-128.4	1.2
<b>Loans &amp; receivables, net</b>	<b>1,677.5</b>	<b>1,591.9</b>	<b>5.4</b>	<b>1,646.2</b>	<b>2.6</b>	<b>1,677.5</b>	<b>1,591.9</b>	<b>5.4</b>
	3QFY3/20	3QFY3/19	+/- ppt	2QFY3/20	+/- ppt	9MFY3/20	9MFY3/19	+/- ppt
Tax rate (%)	24.4	29.1	(4.7)	26.2	(1.8)	25.9	26.6	(0.7)
Gross NPL ratio (%)	4.3	4.1	0.2	4.4	(0.2)	4.3	4.1	0.2
Loan loss coverage ratio (%)	167.4	180.4	(12.9)	167.7	(0.3)	167.4	180.4	(12.9)
Net gearing (%)	177.1	202.4	(25.3)	177.6	(0.4)	177.1	202.4	(25.3)

Source: Company

## Results analysis

3QFY20 net profit grew 23% YoY, driven by: (i) loans growth of 5% YoY; and (ii) higher estimated average lending yield of 14.5% (3QFY19: 14.0%).

3QFY20 net profit grew 14% QoQ, driven by: (i) loans growth of 3% QoQ; (ii) higher estimated average lending yield of 14.5% (2QFY20: 14.3%); and (iii) credit cost easing 17% QoQ.

Figure 2: Revised assumptions

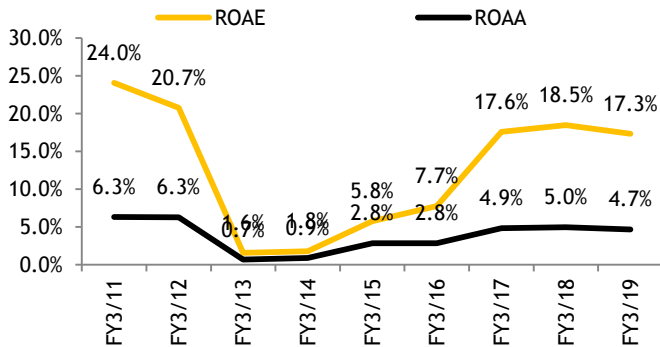
	FY3/19A	FY3/20E	FY3/21E	FY3/22E
<b>Previous</b>				
FYE borrowings (MYRm)	1,604.9	1,650.5	1,694.5	1,724.0
Credit cost ratio	1.4%	1.5%	1.5%	1.5%
<b>Revised</b>				
FYE borrowings (MYRm)	1,604.9	1,613.8	1,657.7	1,687.3
Credit cost ratio	1.4%	1.2%	1.2%	1.2%

Source: Company (historical), Maybank Kim Eng (forecasts)

## 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 non-discretionary 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.

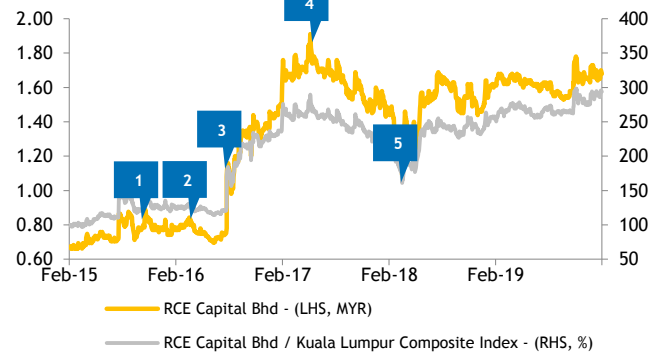
### ROE and ROA



Source: Company, Maybank Kim Eng

## Price Drivers

### Historical share price trend



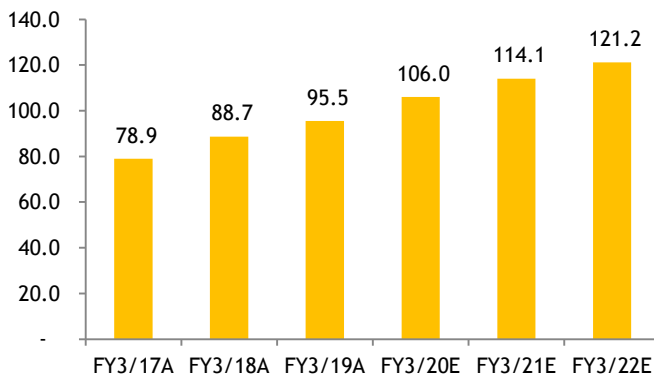
Source: Company, Maybank Kim Eng

1. Proposed special interim DPS of 10.5 sen. Still paid a final DPS of 3.5sen.
2. Proposed capital repayment of MYR0.075/shr and 4-into-1 share consolidation.
3. 1QFY17 net profit surged 86% YoY as FY17 revenue grew 39% YoY.
4. 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.

## 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%).
- Forecast stable three-year forward core net profit CAGR of 8% 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

## 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.

FYE 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Key Metrics</b>					
Core P/E (x)	4.7	5.8	5.5	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	0.9	0.8	0.7
P/NTA (x)	0.9	1.0	1.0	0.8	0.8
Net dividend yield (%)	5.7	5.5	5.9	6.2	6.5
<b>INCOME STATEMENT (MYR m)</b>					
Interest income	218.5	242.2	262.3	275.4	287.8
Interest expense	(69.4)	(78.1)	(86.5)	(87.1)	(88.3)
<b>Net interest income</b>	<b>149.2</b>	<b>164.2</b>	<b>175.8</b>	<b>188.3</b>	<b>199.5</b>
Islamic banking income	na	na	na	na	na
Other income	39.1	35.8	38.6	40.6	42.4
<b>Total non-interest income</b>	<b>39.1</b>	<b>35.8</b>	<b>38.6</b>	<b>40.6</b>	<b>42.4</b>
<b>Operating income</b>	<b>188.3</b>	<b>200.0</b>	<b>214.4</b>	<b>228.9</b>	<b>241.9</b>
Staff costs	(22.4)	(21.4)	(23.2)	(24.3)	(25.4)
Other operating expenses	(18.9)	(23.8)	(24.5)	(25.7)	(26.8)
<b>Operating expenses</b>	<b>(41.3)</b>	<b>(45.2)</b>	<b>(47.7)</b>	<b>(50.0)</b>	<b>(52.2)</b>
<b>Pre-provision profit</b>	<b>147.0</b>	<b>154.8</b>	<b>166.7</b>	<b>178.9</b>	<b>189.7</b>
Loan impairment allowances	(29.6)	(23.7)	(21.3)	(22.3)	(23.3)
Associates & JV income	0.0	0.0	0.0	0.0	0.0
<b>Pretax profit</b>	<b>117.4</b>	<b>131.1</b>	<b>145.4</b>	<b>156.5</b>	<b>166.4</b>
Income tax	(28.7)	(35.6)	(39.4)	(42.5)	(45.1)
<b>Reported net profit</b>	<b>88.7</b>	<b>95.5</b>	<b>106.0</b>	<b>114.1</b>	<b>121.2</b>
<b>Core net profit</b>	<b>88.7</b>	<b>95.5</b>	<b>106.0</b>	<b>114.1</b>	<b>121.2</b>
<b>BALANCE SHEET (MYR m)</b>					
Cash & deposits with banks	197.2	492.4	499.6	541.7	588.6
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
<b>Total assets</b>	<b>1,858.8</b>	<b>2,226.1</b>	<b>2,311.3</b>	<b>2,433.4</b>	<b>2,546.8</b>
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	69.4	12.9	(57.8)
Other liabilities	342.2	356.6	357.7	358.5	359.2
<b>Total liabilities</b>	<b>1,339.5</b>	<b>1,642.6</b>	<b>1,652.3</b>	<b>1,696.6</b>	<b>1,726.7</b>
Share capital	44.7	154.5	160.0	160.0	160.0
Reserves	474.6	429.1	499.0	576.8	660.1
Shareholders' funds	519.3	583.5	659.0	736.9	820.2
Preference shares	0.0	0.0	0.0	0.0	0.0
Minority interest	0.0	0.0	0.0	0.0	0.0
Total equity	519.3	583.5	659.0	736.9	820.2
<b>Total liabilities &amp; equity</b>	<b>1,858.8</b>	<b>2,226.1</b>	<b>2,311.3</b>	<b>2,433.4</b>	<b>2,546.8</b>

FYE 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Key Ratios</b>					
<b>Growth (%)</b>					
Net interest income	14.5	10.1	7.1	7.1	6.0
Non-interest income	(5.6)	(8.3)	7.9	5.0	4.4
Operating expenses	(4.1)	9.4	5.6	4.8	4.3
Pre-provision profit	14.3	5.3	7.7	7.3	6.1
Core net profit	12.3	7.7	10.9	7.6	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	3.8	5.3	4.7
<b>Profitability (%)</b>					
Non-int. income/Total income	20.8	17.9	18.0	17.7	17.5
Cost/income	21.9	22.6	22.3	21.9	21.6
<b>Liquidity (%)</b>					
Loans/customer deposits	na	na	na	na	na
<b>Asset quality (%)</b>					
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
<b>Capital adequacy (%)</b>					
CET1	na	na	na	na	na
Tier 1 capital	na	na	na	na	na
Risk-weighted capital	na	na	na	na	na
<b>Returns (%)</b>					
ROAE	18.5	17.3	17.1	16.3	15.6
ROAA	5.0	4.7	4.7	4.8	4.9
Shareholders equity/assets	27.9	26.2	28.5	30.3	32.2

Source: Company; Maybank

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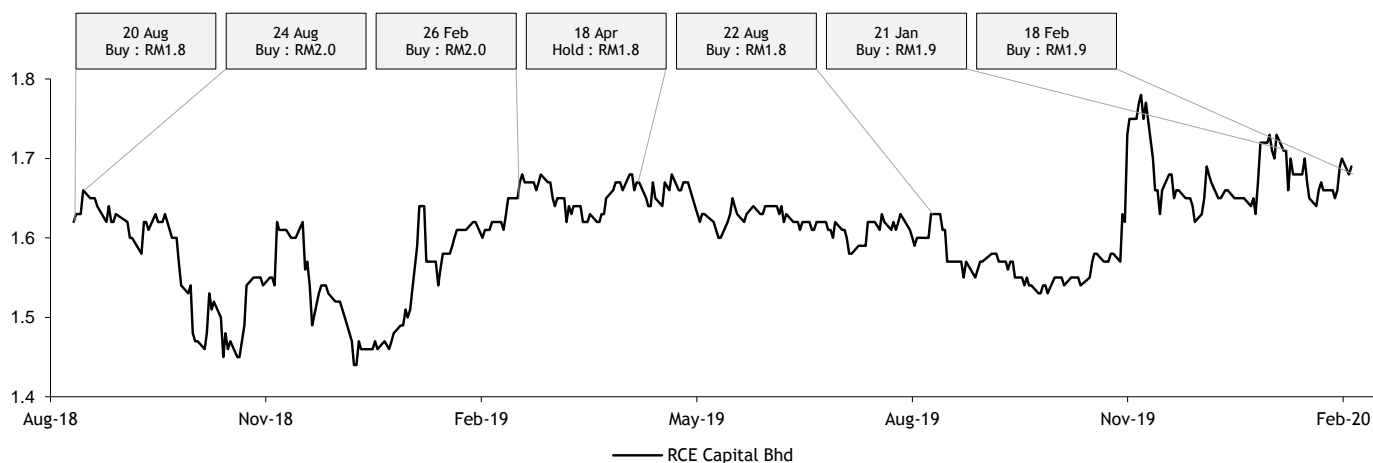
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