

9 Feb 2021

Hold

Price
 RM2.51

Target Price
 RM2.55 (from RM2.30)

Market Data

	RCE MK
Bloomberg Code	RCE MK
No. of shares (m)	357.7
Market cap (RMm)	897.8
52-week high/low (RM)	2.83 / 1.22
Avg daily turnover (RMm)	1.1
KLCI (pts)	1,586.1

Source: Bloomberg, KAF

Major Shareholder (%)

Cempaka Empayar	(55.0%)
EPF	(2.4%)
Cheam Heng Ming	(1.1%)
Free Float	121.2

Source: Bloomberg, KAF

Performance

	3M	6M	12M
Absolute (%)	30.1	33.5	51.2
Rel Market (%)	26.0	32.6	48.4

Source: Bloomberg, KAF

Analyst

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RCE Capital

Stretched valuation; Downgrade to Hold

We downgrade RCE Capital (RCE) from a Buy to a Hold but raise our target price to RM2.55 (from RM2.30), based on our GGM valuation. 9MFY21 results are above expectations from lower than expected IL provision in 3QFY21. From 1) potential recovery in the broad economy in 2021F and 2) high collection ratio from its auto salary deduction repayment mechanism, we expect its IL provision to normalise in the following quarters. Despite of factoring 1) higher receivables growth, 2) lower IL provision, 3) stronger earnings, and 4) roll-forward our valuation to CY21F, we believe that the upside potential to its share price is capped. At forward PBR of 1.1x, RCE is trading at 2SD above 5-year mean of 0.8x.

Financial Highlights

FYE Mar	2018	2019	2020	2021F	2022F
Operating income (RMm)	188.3	200.0	221.3	228.1	245.0
Net profit	88.7	95.5	110.6	114.9	124.6
EPS (sen)	24.8	26.7	30.9	32.1	34.8
EPS growth (%)	12.3	7.7	15.8	3.9	8.4
Net DPS (sen)	7.0	8.6	10.8	11.2	12.1
Net yield (%)	2.8	3.4	4.3	4.5	4.8
PER (x)	10.1	9.4	8.1	7.8	7.2
PB (x)	1.7	1.5	1.3	1.2	1.1
ROE (%)	18.5	17.3	17.6	16.1	15.6

Source: Company, KAF

9MFY21 results above expectations. RCE recorded net profit of RM91m in 9MFY21, +10% yoy, ahead of ours and market expectations. 9MFY21's earnings made up c.82% of our initial net profit forecast of RM110m in FY21F. Stronger than expected earnings was due to lower than expected impairment loss (IL) provision in 3QFY21.

Lower provision from ECL model. RCE's IL provision in 3QFY21 has declined by 56% yoy and 64% qoq. This is due to the forward-looking variable (real GDP) in its current expected credit loss (ECL) model which expect a potential recovery in the broad economy in 2021F. In view of this trend, we expect the group's IL provision to normalise to pre-Covid level in FY21-22F to c.10% (previous forecast: c.13%) of its total operating income.

Improvement in NPL. RCE's NPL ratio was 4.0% in 3QFY21, a slight improvement than 4.2% in the previous quarter. This is the combination of a 2% qoq contraction in its NPL and a 2% qoq growth of its receivables. RCE's coverage ratio remained high at 174% in 3QFY21. High coverage ratio is justified as consumer financing is unsecured in nature.

Revised earnings and TP. Due to the above-mentioned reasons, we have cut our IL provision numbers by 22% in FY21-22F. This has resulted to a higher earnings by 4% in the same period. Subsequently, sustainable ROE is higher at 15.5% (previously: 15.1%). We have also roll forward our valuation to CY2021. As a result, our TP is higher at RM2.55 (from RM2.30).

No dividend declared. No dividend declared in 3QFY21. Normally, the group would only declare a dividend in 2Q and 4Q. RCE has a dividend payout policy of 20-40% of net profit. We expect a DPS of 11.0-12.00 sen in FY21-22F. Our estimate is based on the same payout ratio as FY20, i.e., 35%. At the current price, this implies a 4-5% yield.

Stretched valuation. Despite of factoring 1) higher receivables growth, 2) lower IL provision, 3) stronger earnings, and 4) roll-forward our valuation to CY21F, we believe that the upside potential to its share price is capped.

Post-the steep run up in its share price, RCE is now trading at 1.1x CY21F PBR. Our GGM-derived TP of RM2.55 implies a CY21F PBR of 1.1x, which is at 2SD above its 5-year mean. We think valuation at 2SD above mean is more than sufficient to price in the potential earnings growth of c.6-8% in CY21-22F. As current valuation is at 2SD above its 5-year

mean, we think that the valuation is somewhat stretched. Downgrade to Hold.

Table 1: Quarterly trends (before revision)

Year to 31 March	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	% chg		Cumulative			KAF	
RM m	2Q20	3Q20	4Q20	1Q21	2Q21	3Q21	qoq	yoy	9M20	9M21	% chg	2021F	9M/F
Interest and fee income	70	73	73	65	76	78	3%	7%	210	218	4%	288	76%
Interest expense	(20)	-20	(21)	(21)	(20)	(20)	1%	-2%	(61)	(60)	-1%	(81)	75%
Net interest and fee income	50	52	52	44	56	58	3%	11%	149	158	6%	207	76%
Non-interest income	5	5	5	6	5	4	-10%	-16%	15	15	-3%	21	71%
Operating income	55	57	57	49	61	62	2%	9%	164	173	5%	228	76%
Operating expenses	(13)	-12	(11)	(12)	(11)	(14)	20%	16%	(38)	(36)	-4%	(51)	72%
Underlying profit	42	46	46	38	50	49	-2%	7%	126	136	8%	177	77%
Provisions	(6)	-5	(8)	(7)	(6)	(2)	-64%	-56%	(15)	(15)	0%	(30)	50%
Exceptional	0	0	0	0	0	0	nm	nm	0	0	na	na	na
Pre-tax profit	37	41	38	31	44	47	6%	14%	111	121	9%	147	83%
Taxation	(10)	-10	(10)	(8)	(11)	(12)	7%	19%	(29)	(31)	7%	(38)	81%
Net profit	27	31	28	23	33	35	5%	12%	82	91	10%	110	82%

Source: Company, KAF

Table 2: Quarterly trends (after revision)

Year to 31 March	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	% chg		Cumulative			KAF	
RM m	2Q20	3Q20	4Q20	1Q21	2Q21	3Q21	qoq	yoy	9M20	9M21	% chg	2021F	9M/F
Interest and fee income	70	73	73	65	76	78	3%	7%	210	218	4%	288	76%
Interest expense	(20)	-20	(21)	(21)	(20)	(20)	1%	-2%	(61)	(60)	-1%	(81)	75%
Net interest and fee income	50	52	52	44	56	58	3%	11%	149	158	6%	207	76%
Non-interest income	5	5	5	6	5	4	-10%	-16%	15	15	-3%	21	71%
Operating income	55	57	57	49	61	62	2%	9%	164	173	5%	228	76%
Operating expenses	(13)	-12	(11)	(12)	(11)	(14)	20%	16%	(38)	(36)	-4%	(51)	72%
Underlying profit	42	46	46	38	50	49	-2%	7%	126	136	8%	177	77%
Provisions	(6)	-5	(8)	(7)	(6)	(2)	-64%	-56%	(15)	(15)	0%	(24)	63%
Exceptional	0	0	0	0	0	0	nm	nm	0	0	na	na	na
Pre-tax profit	37	41	38	31	44	47	6%	14%	111	121	9%	154	79%
Taxation	(10)	-10	(10)	(8)	(11)	(12)	7%	19%	(29)	(31)	7%	(40)	77%
Net profit	27	31	28	23	33	35	5%	12%	82	91	10%	115	79%

Source: Company, KAF

Exhibit 1: RCE's 5-year forward PB



Source: Bloomberg, KAF

Exhibit 2: Income Statement

FYE March (RM m)	2018	2019	2020	2021F	2022F
Net interest income	149.2	156.2	175.1	181.0	195.6
Non-interest income	39.1	43.8	46.2	47.1	49.5
Total income	188.3	200.0	221.3	228.1	245.0
Operating costs	(41.3)	(45.2)	(49.3)	(50.8)	(54.6)
Pre-prov operating profit	147.0	154.8	172.0	177.3	190.4
Provision charges	(29.5)	(23.7)	(23.1)	(23.5)	(24.7)
Pre-tax profit	117.4	131.0	148.9	154.8	167.7
Taxation	(28.7)	(35.6)	(38.3)	(39.8)	(43.2)
Net Profit	88.7	95.5	110.6	114.9	124.6

Source: Company, KAF

Exhibit 3: Balance Sheet

FYE March (RM m)	2018	2019	2020	2021F	2022F
Consumer financing	1,689.9	1,598.7	1,689.9	1,723.7	1,809.9
Factoring and confirming	3.8	3.7	3.0	2.5	2.0
Deposits with financial institutions	169.6	275.8	360.7	360.4	385.1
Plant and equipment	6.2	4.5	13.1	13.1	14.0
Investment in properties	0.0	0.0	0.0	0.0	0.0
Goodwill on consolidation	47.3	47.3	47.3	47.3	50.5
Other investments	0.0	0.0	0.0	0.0	0.0
AFS financial assets	0.0	0.0	0.0	0.0	0.0
Deferred tax assets	39.5	42.0	45.4	45.4	48.5
Other receivables and deposits	40.0	37.5	12.0	12.0	12.0
Asset held for sale	0.0	0.0	0.0	0.0	0.0
Cash and bank balances	27.6	216.6	259.5	224.6	273.1
Total Assets	2,024.0	2,226.1	2,431.0	2,429.1	2,595.2
Borrowings	1,298.5	1,604.9	1,714.4	1,637.5	1,719.4
Payables and accruals	33.0	27.0	31.0	31.0	33.1
Hire purchase	1.3	1.1	0.7	0.7	0.8
Deferred tax liabilities	0.3	0.0	5.2	5.2	5.5
Tax liabilities	6.4	9.7	6.4	6.4	6.8
Total Liabilities	1,339.5	1,642.6	1,757.7	1,680.8	1,765.6
Share capital	31.3	134.5	146.3	146.3	146.3
Redeemable convertible preference shares	0.0	0.0	0.0	0.0	0.0
Reserves	487.9	449.0	527.0	602.0	683.2
Total Shareholders' Equity	519.3	583.5	674.0	749.0	830.0

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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