

27 May 2021

Financial Services | Banks

RCE Capital (RCE MK)

Buy (Maintained)

Good Vibes Only; Keep BUY

Target Price (Return): MYR3.20 (17.2%)
 Price: MYR2.73
 Market Cap: USD238m
 Avg Daily Turnover (MYR/USD) 0.80m/0.20m

- **Keep BUY with higher MYR3.20 TP from MYR3.00, 17% upside and 5% yield.** RCE Capital's FY21 (Mar) results beat both our and Street's estimates on lower than expected credit cost (due to favourable changes in macro assumptions). The lender announced a second interim DPS of 7 sen which beat our expectation (6 sen). A full-year DPS of 13 sen implies a 37% payout, the highest in recent years. We still like RCE for its sturdy asset quality, consistent earnings delivery, and dividend payout.
- **Outlook and guidance.** Operations remained business-as-usual during the current MCO 3.0. Demand for credit and collection are both still healthy. We believe credit cost could be higher if the situation deteriorates, but should mostly be macro overlays in our view, instead of due to asset quality slippages. RCE's asset quality has been sturdy since the onset of the pandemic, thanks to its unique salary-deduction collection scheme.
- **FY21 beat, dividend surprise.** RCE ended its financial year with MYR124.6m PATAMI (+13% YoY). The results were 6-7% ahead of our and consensus estimates. The surprise was mainly due to lower-than-expected credit cost during 4QFY21. FY21 credit cost was also lower at 85bps as a result (FY20: 131bps). The lender announced a higher-than-expected second interim DPS of 7 sen (full-year: 13 sen, implying a 37% payout).
- **Earnings drivers.** 4QFY21 earnings and PIOP were 2% and 5% lower QoQ. NII normalized -4% QoQ from the higher base in 3QFY21 (due to higher early settlement income). Opex also normalized 5% QoQ on lower staff cost (3QFY21: higher staff cost on one-off ESOS expense). Credit cost was considerably lower at 14bps due to more favourable macroeconomic variable in its expected credit loss model.
- **Earnings and TP.** We fine-tuned our FY22-23F earnings by 5% and 3%, mostly due to housekeeping. That said, we raised our DPS assumptions on higher payout assumption (c.37%). Our TP is slightly higher at MYR3.20, which values RCE at 1.3x FY22F P/BV, against 16% ROE.

Analysts

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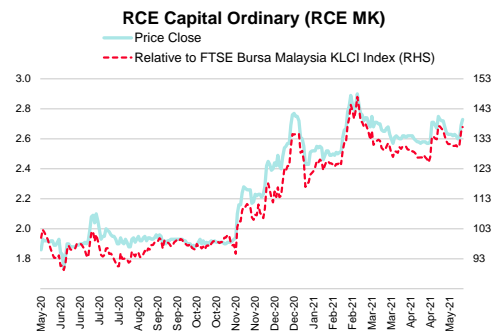


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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(0.7)	6.2	(1.5)	25.2	46.8
Relative	2.3	8.1	(1.3)	26.4	37.0
52-wk Price low/high (MYR)	1.74 – 2.90				



Source: Bloomberg

Overall ESG Score: 3.1 (out of 4)

E: Good

Some green initiatives undertaken by RCE include a lock-print policy has been implemented to limit and reduce paper wastage. As a result, a 20.0% reduction in paper utilisation per headcount is recorded in FYE 2020. Electricity consumption per square foot also dropped due to the extensive use of energy saving lights.

S: Good

RCE practises responsible lending by ensuring the customers are aware of their obligations and commitments when financing is obtained. It is also imperative that they use the financing for legitimate purposes. The product features are clearly disclosed to the borrowers for their consideration. Financing will only be disbursed after obtaining their unambiguous acceptance of our offer.

G: Excellent

RCE's board comprised eight members, entirely of Non-Executive Directors. Four are non-independent directors (including the Chairman) and four are independent directors.

Note:

Small cap stocks are defined as companies with a market capitalization of less than USD1bn.

Forecasts and Valuation	Mar-19	Mar-20	Mar-21	Mar-22F	Mar-23F
Reported net profit (MYRm)	96	111	125	131	134
Net profit growth (%)	7.7	15.8	12.7	5.5	2.1
Recurring net profit (MYRm)	96	111	125	131	134
Recurring EPS (MYR)	0.28	0.32	0.35	0.37	0.37
BVPS (MYR)	1.71	1.94	2.15	2.42	2.32
DPS (MYR)	0.09	0.11	0.13	0.14	0.14
Recurring P/E (x)	9.74	8.58	7.89	7.48	7.32
P/B (x)	1.59	1.41	1.27	1.13	1.18
Dividend Yield (%)	3.3	4.0	4.7	4.9	4.9
Return on average equity (%)	17.3	17.6	17.2	16.0	15.7

Source: Company data, RHB

Financial Exhibits

Asia	Financial summary (MYR)	Mar-19	Mar-20	Mar-21	Mar-22F	Mar-23F
Malaysia	EPS	0.28	0.32	0.35	0.37	0.37
Financial Services	Recurring EPS	0.28	0.32	0.35	0.37	0.37
RCE Capital	DPS	0.09	0.11	0.13	0.14	0.14
RCE MK	BVPS	1.71	1.94	2.15	2.42	2.32
Buy						
	Valuation metrics	Mar-19	Mar-20	Mar-21	Mar-22F	Mar-23F
Valuation basis	Recurring P/E (x)	9.74	8.58	7.89	7.48	7.32
Our GGM assumptions are:	P/B (x)	1.6	1.4	1.3	1.1	1.2
i) CoE of 12.8%;	Dividend Yield (%)	3.3	4.0	4.7	4.9	4.9
ii) ROE of 16.2%; and						
iii) 2% long-term growth rate						
	Income statement (MYRm)	Mar-19	Mar-20	Mar-21	Mar-22F	Mar-23F
Key drivers	Interest income	234	257	273	270	276
Our FY21 forecasts are most sensitive to changes in:	Interest expense	(78)	(82)	(81)	(75)	(76)
i) Financing margins;	Net interest income	156	175	192	195	200
ii) Impairment allowances; and	Non interest income	39	40	39	50	52
iii) Growth in receivables.	Total operating income	195	215	232	245	252
	Overheads	(45)	(49)	(49)	(52)	(54)
	Pre-provision operating profit	150	166	183	193	198
Key risks	Loan impairment allowances	(18)	(17)	(16)	(17)	(18)
The downside risks include:	Pre-tax profit	131	149	167	176	180
i. Higher-than-expected credit cost;	Taxation	(36)	(38)	(43)	(45)	(46)
ii. Weaker-than-expected financing growth; and	Reported net profit	96	111	125	131	134
iii. Weaker-than-expect net financing margin.	Recurring net profit	96	111	125	131	134
	Profitability ratios	Mar-19	Mar-20	Mar-21	Mar-22F	Mar-23F
Company Profile	Return on average assets (%)	4.7	4.7	5.1	5.2	5.1
RCE provides general financing services to civil servants - repayments are done via direct salary deductions. Its wholly-owned EXP Payment unit offers payroll collection management services for government departments under the purview of the Accountant General's Department.	Return on average equity (%)	17.3	17.6	17.2	16.0	15.7
	Return on IEAs (%)	12.2	12.2	11.7	10.8	10.8
	Cost of funds (%)	5.4	4.9	4.8	4.4	4.4
	Net interest spread (%)	6.9	7.3	7.0	6.4	6.4
	Net interest margin (%)	8.2	8.3	8.3	7.8	7.9
	Non-interest income / total income (%)	19.8	18.8	17.0	20.4	20.7
	Cost to income ratio (%)	23.2	22.8	21.1	21.1	21.4
	Credit cost (bps)	110	97	85	89	89
	Balance sheet (MYRm)	Mar-19	Mar-20	Mar-21	Mar-22F	Mar-23F
	Total gross loans	1,729	1,820	1,845	1,979	2,064
	Other interest earning assets	279	364	625	553	503
	Total gross IEAs	2,009	2,184	2,471	2,533	2,567
	Total provisions	(130)	(130)	(124)	(129)	(135)
	Net loans to customers	1,599	1,690	1,721	1,850	1,928
	Total net IEAs	1,878	2,054	2,346	2,404	2,432
	Total non-IEAs	348	377	144	209	196
	Total assets	2,226	2,431	2,491	2,613	2,628
	Other interest-bearing liabilities	1,605	1,714	1,671	1,708	1,759
	Total IBLs	1,605	1,714	1,671	1,708	1,759
	Total non-IBLs	38	43	46	32	32
	Total liabilities	1,643	1,758	1,717	1,740	1,792
	Share capital	154	172	188	194	201
	Shareholders' equity	584	673	774	872	836
	Asset quality and capital	Mar-19	Mar-20	Mar-21	Mar-22F	Mar-23F
	Reported NPLs / gross cust loans (%)	4.4	4.1	4.0	4.6	4.6

Source: Company data, RHB

Results At a Glance

Figure 1: RCE – Summary of 4QFY21 and FY21 results

FYE Mar (MYRm)	4QFY20	3QFY21	4QFY21	% QoQ	% YoY	FY20	FY21	% YoY	Comments – 4QFY21 vs 3QFY21
NII	45.9	51.7	49.8	(3.6)	8.4	174.9	192.3	9.9	
Interest income	66.8	71.6	69.8	(2.6)	4.5	256.8	273.0	6.3	
Interest expense	(20.9)	(20.0)	(20.0)	0.3	(4.2)	(81.8)	(80.7)	(1.4)	
Non-II	11.4	10.6	9.4	(10.7)	(17.3)	46.2	39.5	(14.6)	Lower QoQ on lower early settlement income
Non-II/Total income (%)	19.9	17.0	15.9			20.9	17.0		
Operating income	57.4	62.3	59.2	(4.9)	3.3	221.2	231.8	4.8	
Overheads	(11.3)	(13.5)	(12.8)	(5.3)	13.2	(49.2)	(49.0)	(0.4)	Lower QoQ due to lack of one-off employee share option scheme expense.
CIR (%)	19.7	21.7	21.6			22.2	21.1		
PIOP	46.1	48.8	46.4	(4.7)	0.8	172.0	182.8	6.3	
Impairment on financings	(8.2)	(2.1)	(0.6)	(68.8)	(92.1)	(23.1)	(15.6)	(32.5)	
Credit cost	181	46	14			131	85		Lower QoQ on favourable change in macroeconomic variables.
Pre-tax profit	37.8	46.7	45.8	(1.9)	21.0	148.9	167.2	12.3	
Tax	(9.5)	(11.9)	(11.7)			(38.3)	(42.6)		
ETR (%)	25.2	25.5	25.6			25.7	25.5		
Net earnings	28.3	34.8	34.1	(2.0)	20.3	110.6	124.6	12.7	
Other key data and ratios									
Gross financing	1,820.1	1,832.8	1,845.3	0.7	1.4				
Total borrowings	1,714.4	1,677.0	1,670.6	(0.4)	(2.6)				
Gross impaired financing	(130.2)	(128.1)	(130.2)	1.6	0.0				
Total assets	2,431.0	2,454.6	2,490.7	1.5	2.5				
Shareholders' funds	673.4	734.4	774.0	5.4	14.9				
ROAA	4.8%	5.9%	5.5%			4.9%	5.1%		
ROAE	17.2%	19.2%	18.1%			18.0%	17.7%		
GIL ratio	4.1%	4.0%	4.0%						

Source: Company, RHB

Earnings revisions

We fine-tuned our FY21-23F earnings forecasts by 5-3% mostly as a result of housekeeping.

Figure 2: RCE – revisions to forecasts

FYE Mar	Net profit (MYRm)			EPS (MYR)			DPS (MYR)		
	Previous	Revised	% Chg	Previous	Revised	% Chg	Previous	Revised	% Chg
2021F	125.5	131.5	4.8%	0.36	0.37	2.0%	0.12	0.14	12.5%
2022F	130.8	134.3	2.6%	0.37	0.37	-0.1%	0.13	0.14	7.7%
2023F	n.a.	137.3	n.m.	n.a.	0.38	n.m.	n.a.	0.14	n.m.

Source: RHB

Valuation

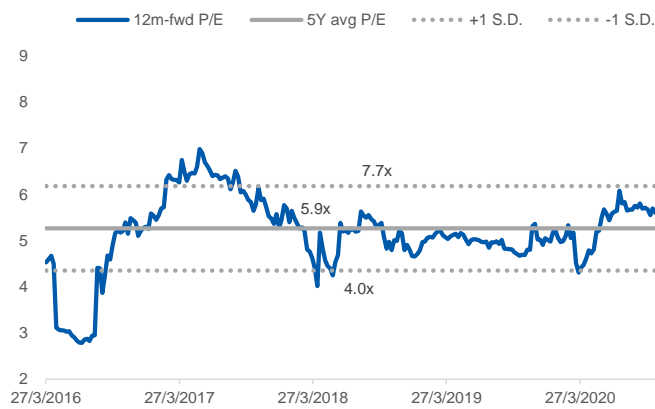
Our GGM-derived TP is raised to MYR3.20 (from MYR3.00) and values RCE Capital at 1.3x FY22F P/BV which is above +1SD from its historical mean.

Figure 3: RCE's GGM valuation

Cost of equity (COE) computation:		Sustainable ROE (%)	16.2
Risk free rate (%)	2.9	COE (%)	12.8
Equity premium (%)	7.4	Long-term growth (g)	2.0
Beta (x)	1.4	Implied P/BV (x)	1.3
Cost of equity - CAPM (%)	12.8	BVPS – FY22F	MYR 2.42
		Target price	MYR 3.17
		TP (rounded)	MYR 3.20

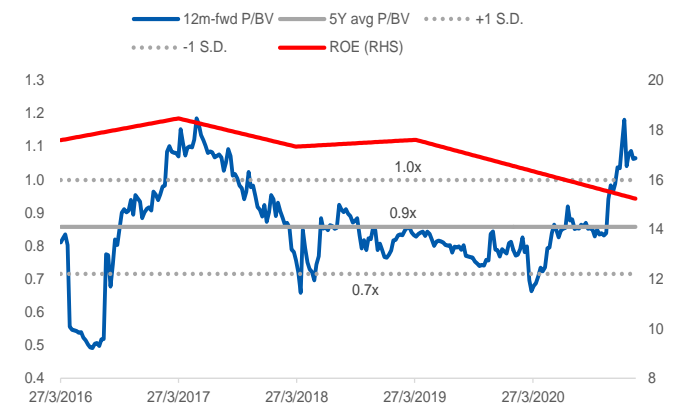
Source: Company data, RHB

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



Source: Bloomberg, RHB

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



Source: Bloomberg, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2021-02-09	Buy	3.00	2.51
2020-12-08	Buy	2.80	2.45
2020-07-06	Buy	2.50	1.92
2020-06-16	Buy	2.20	1.81
2020-03-15	Buy	2.10	1.50
2020-02-19	Buy	2.20	1.77
2020-01-10	Buy	2.10	1.72
2019-08-16	Not Rated	na	1.60

Source: RHB, Bloomberg

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Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
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Analyst	Company
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