

10 Nov 2021

## Hold

**Price**  
RM3.79

**Target Price**  
RM3.60 (from RM2.80)

### Market Data

Bloomberg Code	RCE MK
No. of shares (m)	375.6
Market cap (RMm)	1,423.5
52-week high/low (RM)	3.84 / 1.91
Avg daily turnover (RMm)	1.1
KLCI (pts)	1,524.0
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 (%)	39.3	41.4	95.4
Rel Market (%)	37.5	45.1	95.4
Source: Bloomberg, KAF			

### Analyst

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# RCE Capital

## Earnings in line; Proposed bonus issue

We maintain our Hold recommendation on RCE Capital (RCE) but raise our target price to RM3.60 (from RM2.80), based on our GGM valuation. 6MFY22 results are in line with expectations. To reward its shareholders and slightly improve its capital structure, the group has proposed a 19-for-21 bonus issue. An improvement in its assets quality and its capital structure would likely support its current high valuation (vs historical). Also, the group is working towards becoming a Shariah-compliant securities. Potential listing on Shariah-compliant index would also further support its current high valuation, we believe. This is due to the limited numbers of Shariah-compliant financial counters, presently. However, considering that RCE is trading 1.6x 12-month forward PB i.e., at more than 3SD above its 5-year mean of 0.8x, we believe that the upside potential to its share price is capped.

### Financial Highlights

FYE Mar	2019	2020	2021	2022F	2023F
Operating income (RMm)	200.0	221.3	232.1	248.0	261.7
Net profit	95.5	110.6	124.6	131.7	139.1
EPS (sen)	25.4	29.4	33.2	35.1	37.0
EPS growth (%)	7.7	15.8	12.7	5.7	5.6
Net DPS (sen)	8.2	10.2	12.4	13.1	13.9
Net yield (%)	2.2	2.7	3.3	3.5	3.7
PER (x)	14.9	12.9	11.4	10.8	10.2
PB (x)	2.4	2.1	1.8	1.7	1.5
ROE (%)	17.3	17.6	17.2	16.2	15.5

Source: Company, KAF

**6MFY22 results in line.** RCE recorded net profit of RM67m in 6MFY22, +20% yoy, in line with ours and market expectations. 6MFY22's earnings made up c.51% (consensus: c.52%) of our net profit forecast of RM132m in FY22F. We maintain our FY22F's earnings forecast at RM132m.

**Lower impairment loss from write back.** RCE's impairment loss (IL) in 2QFY22 has declined by 87% yoy and 76% qoq. This is due to the write back of its earlier provision in view of improvement in real GDP in its current expected credit loss (ECL) model. Despite of better than expected IL trend in 6MFY22, we expect the group's IL to normalise in the upcoming quarters from the reopening of the economy.

**Improvement in NPL.** RCE's NPL ratio was 4.0% in 2QFY22. We have noticed that the group's assets quality has improved in recent quarters as compared to pre-pandemic at c.4.1%-4.4%. The improvement in its assets quality was due to its enhancement of its credit assessment. RCE's coverage ratio remained high at 161% in 2QFY22. High coverage ratio is justified as consumer financing is unsecured in nature.

**Declared a 7.0 sen dividend.** The group declared a 7.0 sen DPS in 2QFY22. This made up c.38% of its 6MFY22's earnings. RCE has a dividend payout policy of 20-40% of net profit. We expect a DPS of 13.0-14.0 sen in FY22-23F. Our estimate is based on the same payout ratio as FY21, i.e., 37%. At the current price, this implies a 3-4% yield.

**Proposed share dividend and bonus issue.** On a separate announcement, the group has proposed 1) a distribution of 1-for-20 share dividend and 2) 19-for-21 bonus issue. The reason for these proposals are to increase the number of shares held by its shareholders while minimising the incidence of odd lots.

**Minimal impact on fundamental but likely improve trading liquidity.** The distribution of share dividend to shareholders would be done by reclassifying its Treasury shares (average cost: RM1.111 per share) to share capital and outstanding options. We also assume that all

options are fully exercised as they are in-the-money. Overall, this would increase the shareholders fund by c.RM41m or c.5% of its enlarged shareholders fund.

As for the bonus issue, it will be done at zero consideration without any capitalisation of the company's reserve. In other words, the group's share base would increase but no changes on the group's issued share capital.

As such, these exercises only marginally improve the group's capital base but will significantly increase the number of shares outstanding. Theoretically RCE will be trading at a more affordable price adjustment. These translate into an improvement of RCE shares' trading liquidity and marketability. Refer to Exhibit 1 & 2 for more detail.

**Revised TP with higher implied PB at 1.5x.** Due to the improvement in its assets quality and capital structure, we deem the counter to be less risky in the future. As such, we lower our WACC assumption to 11.0% (from 13.5%). As a result, our implied PB from our GGM valuation is now at 1.5x (from 1.2x). As compared to RCE's PB trend, 1.5x PB valuation is already exceeded 3SD above its 5-year PB mean of 0.8x. However, in view of the overall improvement in the group's business and better risk assessment, we believe that the valuation may remain high at current level.

As compared to its peers i.e., AEON Credit (ACSM MK, RM14.24, Buy), ACSM is trading at a premium i.e., 1.9x PB FY22F. However, we believe that ACSM deserves a higher valuation as it 1) provides higher sustainable ROE at c.16.5%, 2) has better assets quality at c.2.0%, 3) has stronger receivables growth (high-single to double-digit growth), and 4) has less concentration risk with more diversified products offering.

**Stretched valuation.** Post-the steep run up in its share price, RCE is now trading at 1.6x 12-month forward PB. As mentioned in the earlier part, our GGM-derived TP of RM3.60 implies a PB of 1.5x, which already exceeded 3SD above its 5-year mean. We think valuation at 3SD above mean is more than sufficient to price in the potential positives outlook for the group. We think that the current valuation is somewhat stretched. Maintain Hold.

**Table 1: Quarterly trends**

Year to 31 March	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Jun-21	% chg		Cumulative			KAF	
	1Q21	2Q21	3Q21	4Q21	1Q22	1Q22	qoq	yoy	6M21	6M22	% chg	2022F	6M/F
<b>RM m</b>													
Interest and fee income	65	76	78	75	78	70	-11%	-8%	141	148	5%	308	48%
Interest expense	(21)	(20)	(20)	(20)	(20)	(20)	3%	4%	(41)	(40)	-1%	(80)	51%
<b>Net interest and fee income</b>	<b>44</b>	<b>56</b>	<b>58</b>	<b>55</b>	<b>58</b>	<b>49</b>	<b>-15%</b>	<b>-12%</b>	<b>100</b>	<b>108</b>	<b>8%</b>	<b>228</b>	<b>47%</b>
Non-interest income	6	5	4	4	5	5	-1%	-5%	10	9	-12%	20	46%
<b>Operating income</b>	<b>49</b>	<b>61</b>	<b>62</b>	<b>59</b>	<b>63</b>	<b>54</b>	<b>-14%</b>	<b>-12%</b>	<b>110</b>	<b>117</b>	<b>6%</b>	<b>248</b>	<b>47%</b>
Operating expenses	(12)	(11)	(14)	(13)	(12)	(11)	-11%	-2%	(23)	(24)	3%	(53)	45%
<b>Underlying profit</b>	<b>38</b>	<b>50</b>	<b>49</b>	<b>46</b>	<b>50</b>	<b>43</b>	<b>-15%</b>	<b>-14%</b>	<b>88</b>	<b>93</b>	<b>6%</b>	<b>195</b>	<b>48%</b>
Provisions	(7)	(6)	(2)	(1)	(3)	(1)	-76%	-87%	(13)	(4)	-70%	(19)	21%
Exceptional	0	0	0	0	0	0	nm	nm	0	0	na	na	na
<b>Pre-tax profit</b>	<b>31</b>	<b>44</b>	<b>47</b>	<b>46</b>	<b>47</b>	<b>42</b>	<b>-11%</b>	<b>-4%</b>	<b>75</b>	<b>89</b>	<b>20%</b>	<b>177</b>	<b>51%</b>
Taxation	(8)	(11)	(12)	(12)	(12)	(11)	-10%	-5%	(19)	(23)	19%	(45)	50%
<b>Net profit</b>	<b>23</b>	<b>33</b>	<b>35</b>	<b>34</b>	<b>35</b>	<b>32</b>	<b>-11%</b>	<b>-4%</b>	<b>56</b>	<b>67</b>	<b>20%</b>	<b>132</b>	<b>51%</b>

Source: Company, KAF

**Exhibit 1: Potential changes from share dividend and bonus issue (both refer to as “corporate exercise”) – Before revision**

	FY22F		Potential change
	Before corporate exercise	After corporate exercise	
Shareholders' funds (RM m)	856.4	897.3	5%
Number of shares	362.6	751.1	107%
Net Profit (RM m)	131.7	131.7	0%
Sustainable ROE (%)	15.5%	14.9%	-0.6ppts
Equity value (RM m)	1,016.2	1,064.8	5%
Target price (RM)	2.80	1.42	-49%
DPS (sen)	13.6	6.6	-52%
EPS (sen)	36.3	17.5	-52%
Gearing	1.2x	1.2x	0%

Source: Company, KAF

**Exhibit 2: Potential changes from share dividend and bonus issue (both refer to as “corporate exercise”) – After revision**

	FY22F		Potential change
	Before corporate exercise	After corporate exercise	
Shareholders' funds (RM m)	856.4	897.3	5%
Number of shares	375.6	751.1	100%
Net Profit (RM m)	131.7	131.7	0%
Sustainable ROE (%)	15.5%	14.9%	-0.6ppts
Equity value (RM m)	1,354.5	1,354.5	0%
Target price (RM)	3.60	1.80	-50%
DPS (sen)	13.6	6.6	-52%
EPS (sen)	36.3	17.5	-52%
Gearing	1.2x	1.2x	0%

Source: Company, KAF

**Exhibit 3: RCE's 5-year forward PB**

Source: Bloomberg, 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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