

## RCE Capital Bhd (RCE MK)

# Laughing all the way to this non-bank financial institution

### Lift TP to MYR3.67 but rating D/G to HOLD

On top of earnings and dividends positively surprising us again, RCE will reward shareholders with a share DPS and bonus issue. The share DPS alone is worth 19.8sen/share. We raise our EPS estimates by 11% p.a., cash DPS estimates by 1.5sen-2.0sen and end-CY22E P/BV multiple to 1.5x from MYR1.2x previously. Thus, we raise our TP to MYR3.67 from MYR3.05. Yet, with <10% upside, we downgrade RCE to HOLD from BUY.

### Earnings and dividends outperformed again

2QFY3/22 net profit of MYR31.5m brought 6MFY3/22 net profit to MYR66.9m which was above our expectations at 55% of our FY estimate. The first interim DPS of 7sen was also above our expectations at 58% of our FY estimate. Yet, 6MFY3/22 revenue of MYR147.9m was within our expectations at 50% of our FY estimate. 2QFY3/22 credit cost as a percentage of gross financing and loans receivables stood at only 0.2% (MKE forecast: 1.5%).

### Future quarters ought to be better...

2QFY3/22 gross financing and loans receivables was flat QoQ as the Full Movement Control Order (FMCO) effective 1 Jun 2021 limited the movement of marketing agents. Marketing agents have resumed their activities since early Sep 2021. We raise our EPS estimates by 11% p.a. as we cut our credit cost ratio assumption to 0.5% from 1.5% and raise our FY21E/FY22E/FY23E cash DPS estimates by 2.0sen/1.5sen/1.5sen to reflect our higher EPS estimates and higher DPR of 37% (35% previously).

### ...with share dividend and bonus issue to boot

Also, RCE announced that it will distribute ≤18.8m treasury shares on the basis of 1 treasury share for every 20 shares held. The cost of the treasury shares is MYR20.9m or 5.8sen/share (our revised FY3/22E DPS reflect this) but its market value is MYR71.2m or 19.8sen/share. Post the share dividend, RCE will effect a bonus issue of ≤360.3m bonus shares on the basis of 19 bonus shares for every 21 shares held. In summary, a shareholder holding 100 shares on entitlement date will hold 200 shares after the above. The above are expected to be completed in 1QCY22.

FYE Mar (MYR m)	FY20A	FY21A	FY22E	FY23E	FY24E
Operating income	221	232	242	252	262
Pre-provision profit	172	183	192	201	209
Core net profit	111	125	136	142	148
Core FDEPS (MYR)	0.32	0.35	0.37	0.37	0.38
Core FDEPS growth(%)	13.5	10.4	6.1	(0.8)	4.3
Net DPS (MYR)	0.11	0.13	0.20	0.14	0.15
Core FD P/E (x)	4.7	7.4	10.2	10.3	9.9
P/BV (x)	0.8	1.2	1.6	1.5	1.4
Net dividend yield (%)	7.4	5.0	5.2	3.7	3.8
Book value (MYR)	1.92	2.15	2.39	2.51	2.75
ROAE (%)	17.6	17.2	16.7	15.7	14.9
ROAA (%)	4.7	5.1	5.3	5.3	5.2
Consensus net profit	-	-	130	131	134
MKE vs. Consensus (%)	-	-	5.0	8.7	11.0

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# HOLD

[Prior:BUY]

Share Price MYR 3.79  
12m Price Target MYR 3.67 (+2%)  
Previous Price Target MYR 3.05

### Company Description

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

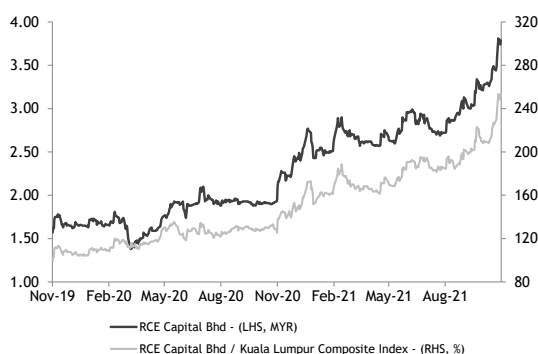
### Statistics

52w high/low (MYR)	3.81/1.94
3m avg turnover (USDm)	0.2
Free float (%)	29.7
Issued shares (m)	388
Market capitalisation	MYR1.5B USD354M

### Major shareholders:

Cempaka Empayar Sdn. Bhd.	50.5%
RCE Capital Bhd.	5.8%
Rockwills International Group Bhd	4.4%

### Price Performance



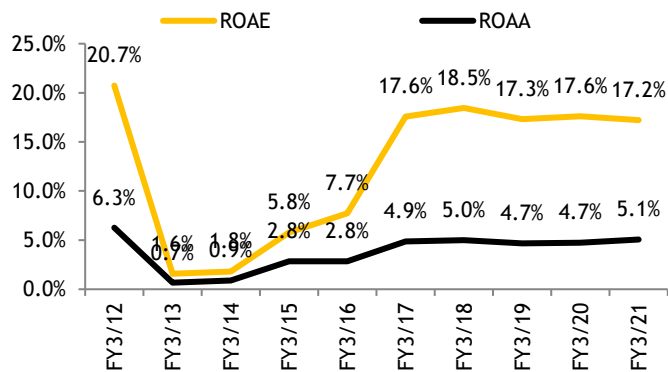
	-1M	-3M	-12M
Absolute (%)	18	39	96
Relative to index (%)	20	36	95

Source: FactSet

## Value Proposition

- RCE Capital provides personal financing, the ultimate customers being civil servants.
- With a gross financing balance of just MYR1.8b, we estimate that its market share is only 2%.
- Non-performing financing kept in check thanks to non-discretionary direct salary deductions.
- Competitive advantage lies in fast financing processing turnaround time of 48 hours.
- ROE generation surpasses that of the average for the overall banking industry.

### ROE and ROA

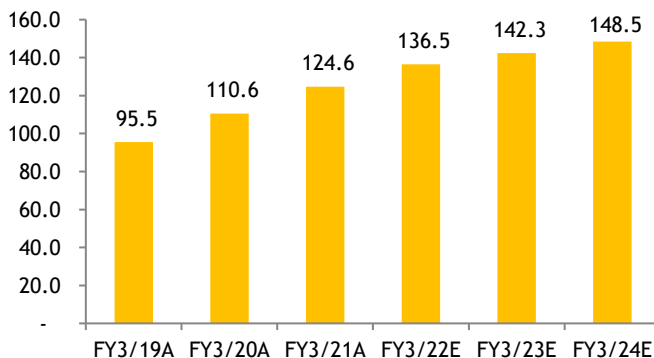


Source: Company

## Financial Metrics

- Introduced a better credit scoring model in 2013. Forecast gross financing growth of 3% p.a. over the next three years.
- Average financing yields may be peaking at 14-15% but average cost of funds is falling.
- Asset quality better than before. New financing are smaller in size (<MYR20k) and their NPF ratios are low (<2%).
- Forecast stable three-year forward core net profit CAGR of 6% p.a.
- There is room for dividends to surprise to the upside as its DPR policy is only 20-40%.

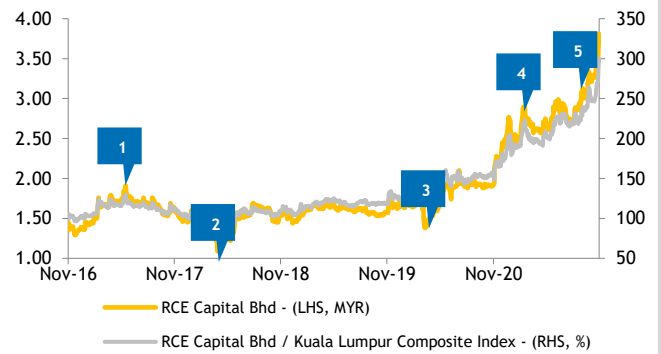
### Core net profit (MYRm)



Source: Company, Maybank Kim Eng

## Price Drivers

### Historical share price trend



Source: Company, Maybank Kim Eng

1. FY17 net profit surged 98% YoY as FY17 revenue grew 38% YoY.
2. Concerns arise that the government may reduce the size of the civil service.
3. Movement Control Order lengthened time to process new customers, resulting in less financing disbursed.
4. 2QFY3/21 net profit grew 21% YoY to a record high of MYR33.0m.
5. 1QFY3/22 net profit grew 55% YoY to another record high of MYR35.4m.

## Swing Factors

### Upside

- Easing competition - competitors have been reducing their exposure to personal financing.
- Lower cost of funds - 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 customers' total indebtedness.

### Downside

- High household debt - Household debt to GDP is elevated at >80% and may crimp customers' repayment ability.
- Need to leverage - RCE Capital cannot take deposits and thus, has to assume debt to finance its financing.
- Asset-liability duration mismatch - customers' repayment may not match RCE Capital's debt repayment.

Figure 1: Summary Results Table

FY Mar (MYRm)	2QFY3/22	2QFY3/21	% YoY	1QFY3/22	% QoQ	6MFY3/22	6MFY3/21	% YoY
Interest/profit income	63.7	70.2	(9.3)	71.6	(11.0)	135.3	131.6	2.8
Other revenue	6.1	5.7	6.9	6.5	(5.3)	12.6	9.0	39.4
<b>Revenue</b>	<b>69.8</b>	<b>75.9</b>	<b>(8.0)</b>	<b>78.0</b>	<b>(10.5)</b>	<b>147.9</b>	<b>140.6</b>	<b>5.1</b>
Other income	4.6	4.8	(5.1)	4.6	(0.7)	9.2	10.4	(12.2)
Interest/profit expense applicable to revenue	-20.4	-19.6	4.1	-19.8	2.9	-40.2	-40.6	(0.9)
Directors' remuneration and staff costs	-5.5	-5.3	4.5	-6.1	(9.8)	-11.6	-11.0	5.9
Allowances for impairment loss on receivables, net	-0.7	-5.7	(87.0)	-3.1	(75.9)	-3.8	-12.9	(70.3)
Depreciation of plant and equipment and right-of-use asset	-0.9	-0.8	9.0	-0.8	5.1	-1.7	-1.6	8.4
Other expenses	-4.6	-5.1	(10.6)	-5.5	(15.9)	-10.1	-10.2	(1.3)
Finance costs	-0.1	-0.1	(4.2)	-0.1	(1.4)	-0.1	-0.1	(4.9)
<b>Profit before tax</b>	<b>42.2</b>	<b>44.2</b>	<b>(4.4)</b>	<b>47.3</b>	<b>(10.7)</b>	<b>89.5</b>	<b>74.7</b>	<b>19.7</b>
Taxation	-10.7	-11.2	(4.5)	-11.9	(10.2)	-22.5	-18.9	19.0
<b>Net profit</b>	<b>31.5</b>	<b>33.0</b>	<b>(4.4)</b>	<b>35.4</b>	<b>(10.9)</b>	<b>66.9</b>	<b>55.8</b>	<b>19.9</b>
<b>FD EPS (sen)</b>	<b>8.7</b>	<b>9.3</b>	<b>(6.5)</b>	<b>9.8</b>	<b>(11.4)</b>	<b>18.4</b>	<b>15.7</b>	<b>17.0</b>
<b>Net DPS (sen)</b>	<b>7.0</b>	<b>6.0</b>	<b>16.7</b>	<b>-</b>	<b>N/M</b>	<b>7.0</b>	<b>6.0</b>	<b>16.7</b>
<b>Financing &amp; loans receivables, gross</b>	<b>1,852.1</b>	<b>1,802.2</b>	<b>2.8</b>	<b>1,853.4</b>	<b>(0.1)</b>	<b>1,852.1</b>	<b>1,802.2</b>	<b>2.8</b>
(Allowance for impairment)	-120.3	-131.4	(8.5)	-123.4	(2.5)	-120.3	-131.4	(8.5)
<b>Financing &amp; loans receivables, net</b>	<b>1,731.8</b>	<b>1,670.7</b>	<b>3.7</b>	<b>1,730.0</b>	<b>0.1</b>	<b>1,731.8</b>	<b>1,670.7</b>	<b>3.7</b>
	<b>2QFY3/22</b>	<b>2QFY3/21</b>	<b>+/- ppt</b>	<b>1QFY3/22</b>	<b>+/- ppt</b>	<b>6MFY3/20</b>	<b>6MFY3/20</b>	<b>+/- ppt</b>
Tax rate (%)	25.3	25.3	(0.0)	25.1	0.1	25.2	25.3	(0.1)
Gross NPF ratio (%)	4.0	4.2	(0.1)	4.0	0.0	4.0	4.2	(0.1)
Financing & loans loss coverage ratio (%)	161.0	174.6	(13.5)	167.1	(6.0)	161.0	174.6	(13.5)
Net gearing (%)	125.7	148.4	(22.7)	133.2	(7.5)	125.7	148.4	(22.7)

Source: Company

## Results analysis

2QFY3/22 net profit eased 4% YoY and 11% QoQ driven by lower early settlement income brought about by fewer customers refinancing due to the FMCO but offset by credit cost falling 87% YoY and 76% QoQ.

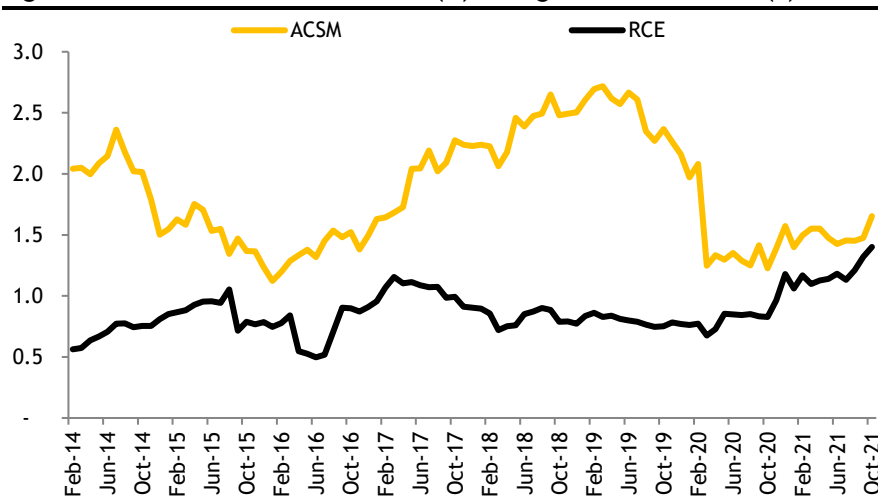
## Other updates

RCE may not be affected by Cukai Makmur as its profits are derived from multiple companies and special purpose vehicles who individually do not generate chargeable incomes of >MYR100m each.

## Valuation and recommendation

RCE's competitor, **AEON Credit Service (M) (ACSM MK, CP: MYR14.46, Not Rated)** is currently trading at 1.7x 12M forward P/BV (Fig. 2) and consensus expects it to generate FY2/22E ROAE of 18.8%. We forecast RCE to generate FY3/22E ROAE of 16.7% which is 11ppts lower than that of ACSM. Thus, we deem it reasonable to lift our end-CY22E P/BV multiple for RCE to 1.5x which is c.10% lower than that of ACSM from 1.2x previously. We gather that this gap may narrow even further should RCE obtain Shariah status later this month. For now, we raise our TP to MYR3.67 from MYR3.05. Given that there is not much upside left, we downgrade RCE to HOLD from BUY.

Figure 2: RCE vs. AEON Credit Service (M) rolling 12M forward P/BV (x)



Source: RCE, AEON Credit Service (M), Bloomberg, Maybank Kim Eng

## 2 good reasons to HOLD on to RCE

Later this month, the Securities Commission will announce a revised list of Shariah compliant securities. As we postulated earlier, we believe that RCE has fulfilled all the necessary requirements to obtain Shariah compliant status. Recall also that RCE JV-ed with **Paramount Corp (PAR MK, CP: MYR0.77, Not Rated)**, **Star Media (STAR MK, CP: MYR0.345, Not Rated)**, **Prosper Palm Oil Mill (Not Listed)** and a technology partner to bid for a digital banking license. Awards are due in 1QCY22.

FYE 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Key Metrics</b>					
Core P/E (x)	4.7	7.4	10.0	10.1	9.7
Core FD P/E (x)	4.7	7.4	10.2	10.3	9.9
P/BV (x)	0.8	1.2	1.6	1.5	1.4
P/NTA (x)	0.8	1.3	1.7	1.6	1.4
Net dividend yield (%)	7.4	5.0	5.2	3.7	3.8
<b>INCOME STATEMENT (MYR m)</b>					
Islamic banking income	187.0	204.4	207.8	216.3	225.2
Other income	34.2	27.4	34.4	35.4	36.5
<b>Total non-interest income</b>	<b>221.2</b>	<b>231.8</b>	<b>242.2</b>	<b>251.8</b>	<b>261.7</b>
<b>Operating income</b>	<b>221.2</b>	<b>231.8</b>	<b>242.2</b>	<b>251.8</b>	<b>261.7</b>
Staff costs	(24.2)	(26.3)	(26.7)	(27.5)	(28.3)
Other operating expenses	(25.0)	(22.7)	(23.1)	(23.7)	(24.3)
<b>Operating expenses</b>	<b>(49.2)</b>	<b>(49.0)</b>	<b>(49.7)</b>	<b>(51.1)</b>	<b>(52.6)</b>
<b>Pre-provision profit</b>	<b>172.0</b>	<b>182.8</b>	<b>192.5</b>	<b>200.6</b>	<b>209.1</b>
Other allowances	(23.1)	(15.6)	(9.4)	(9.6)	(9.9)
Associates & JV income	0.0	0.0	0.0	0.0	0.0
<b>Pretax profit</b>	<b>148.9</b>	<b>167.2</b>	<b>183.1</b>	<b>191.0</b>	<b>199.2</b>
Income tax	(38.3)	(42.6)	(46.6)	(48.6)	(50.7)
<b>Reported net profit</b>	<b>110.6</b>	<b>124.6</b>	<b>136.5</b>	<b>142.3</b>	<b>148.5</b>
<b>Core net profit</b>	<b>110.6</b>	<b>124.6</b>	<b>136.5</b>	<b>142.3</b>	<b>148.5</b>
<b>BALANCE SHEET (MYR m)</b>					
Cash & deposits with banks	620.2	597.9	681.8	768.7	859.9
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
Financing and advances	1,692.9	1,775.4	1,827.0	1,880.2	1,935.0
Fixed assets	7.3	7.3	7.7	8.0	8.4
Intangible assets	47.3	47.3	47.3	47.3	47.3
Other assets	63.3	62.8	62.8	62.8	62.8
<b>Total assets</b>	<b>2,431.0</b>	<b>2,490.7</b>	<b>2,626.6</b>	<b>2,767.0</b>	<b>2,913.4</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	1,059.1	1,187.4	1,180.0	1,180.0	1,180.0
Other borrowings	429.1	252.9	309.3	360.1	412.4
Other liabilities	269.5	276.3	277.2	277.6	278.0
<b>Total liabilities</b>	<b>1,757.7</b>	<b>1,716.7</b>	<b>1,766.5</b>	<b>1,817.6</b>	<b>1,870.4</b>
Share capital	172.2	188.0	188.0	188.0	188.0
Reserves	501.1	586.0	672.1	761.4	854.9
Shareholders' funds	673.4	774.0	860.1	949.4	1,042.9
Preference shares	0.0	0.0	0.0	0.0	0.0
Minority interest	0.0	0.0	0.0	0.0	0.0
<b>Total equity</b>	<b>673.4</b>	<b>774.0</b>	<b>860.1</b>	<b>949.4</b>	<b>1,042.9</b>
<b>Total liabilities &amp; equity</b>	<b>2,431.0</b>	<b>2,490.7</b>	<b>2,626.6</b>	<b>2,767.0</b>	<b>2,913.4</b>

FYE 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Key Ratios</b>					
<b>Growth (%)</b>					
Net interest income	na	na	na	na	na
Non-interest income	10.6	4.8	4.5	3.9	4.0
Operating expenses	8.9	(0.4)	1.5	2.8	2.8
Pre-provision profit	11.1	6.3	5.3	4.2	4.2
Core net profit	15.8	12.7	9.5	4.3	4.3
Gross loans	5.3	1.4	3.0	3.0	3.0
Customer deposits	na	na	na	na	na
Total assets	9.2	2.5	5.5	5.3	5.3
<b>Profitability (%)</b>					
Non-int. income/Total income	100.0	100.0	100.0	100.0	100.0
Cost/income	22.2	21.1	20.5	20.3	20.1
<b>Liquidity (%)</b>					
Loans/customer deposits	na	na	na	na	na
<b>Asset quality (%)</b>					
Gross NPF	4.1	4.0	4.0	4.0	4.0
<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	17.6	17.2	16.7	15.7	14.9
ROAA	4.7	5.1	5.3	5.3	5.2
Shareholders equity/assets	27.7	31.1	32.7	34.3	35.8

Source: Company; Maybank

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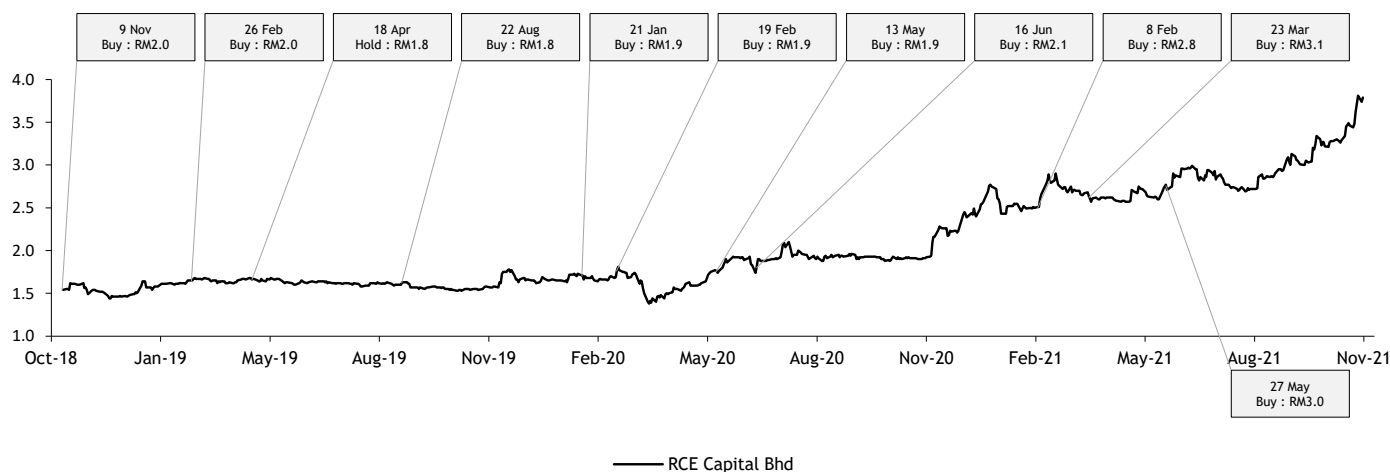
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