

27 May 2024

Financial Services | Banks

RCE Capital (RCE MK)

Sell (Maintained)

A Slight Miss; Keep SELL

- **Maintain SELL and MYR2.40 TP, 23% downside.** RCE Capital's FY24 (Mar) results missed our and Street's expectations on the back of higher-than-expected operating and credit costs. While the impending revision to civil service wages will likely boost its financing growth prospects, we still prefer peers with similar ROE generation that are trading at cheaper valuations.
- **Results review.** 4QFY24 net profit of MYR29.1m (-17% YoY, -16% QoQ) brought the full-year total to MYR138.8m (flat YoY) – this missed both our and consensus' estimates. The deviation from our numbers was mainly from higher-than-expected opex (+35% YoY) and greater-than-expected impairment allowances (+5% YoY). These weaknesses, however, were mitigated by strong non-ll (+7% YoY). On a sequential basis, 4QFY24 NII shrunk 5% from profit expenses climbing by 4%, while impairment allowances were up 24%. On the whole, RCE achieved FY24 ROE of 17.0% (FY23: 16.5%). A second interim DPS of MYR0.07 was declared, bringing the full-year total to MYR0.15 (FY23: MYR0.12 ex-special dividend), and implying a 79% payout ratio (FY23: 63%).
- **Rather muted financing growth.** RCE's gross financing receivables stood at MYR2.1bn at end-Mar 2024, up 4% YoY (flat QoQ) – this was slightly behind the banking system's +6% YoY (+1% QoQ) over the same period. Management had previously flagged that it would be more cautious on disbursements in order to prioritise asset quality. Moving forward, Prime Minister Dato' Seri Anwar Ibrahim's announcement of a >13% salary increase for civil servants is positive for financing growth – we note that this is set to take effect only in Dec 2024, or late 3QFY25 for RCE.
- **Is asset quality under pressure?** The group's impairment allowances spiked up by 24% QoQ (YoY: +27%) in 4QFY24, likely due to an increase in cases of workers opting for early retirement or exiting from civil service. In a similar vein, the non-performing financing ratio rose to 4.0% from 3.8% in the previous quarter (Mar 2023: 3.8%). While exit trends are unpredictable, we think the impending revision to civil service wages could help boost the attractiveness of the civil service over the long run, and curb some of the early exit cases.
- **We lower FY25-26F net profit by 1%** as we incorporate the latest full-year earnings into our model. Our key assumptions are largely unchanged – we are still forecasting mid-single digit financing receivables growth, and 1-2% credit costs. Our TP stays at MYR2.40, and includes a 0% ESG premium/discount, in line with our proprietary ESG scoring methodology.
- **Upside risks to our call** include better-than-expected disbursements and lower-than-expected credit costs.

Forecasts and Valuation	Mar-23	Mar-24	Mar-25F	Mar-26F	Mar-27F
Reported net profit (MYRm)	139	139	156	163	170
Net profit growth (%)	4.2	(0.0)	12.1	5.1	4.1
Recurring net profit (MYRm)	139	139	156	163	170
Recurring EPS (MYR)	0.19	0.19	0.21	0.22	0.23
BVPS (MYR)	1.10	1.13	1.19	1.25	1.31
DPS (MYR)	0.12	0.15	0.16	0.17	0.17
Recurring P/E (x)	16.42	16.43	14.66	13.94	13.40
P/B (x)	2.83	2.75	2.61	2.48	2.37
Dividend Yield (%)	3.8	4.8	5.1	5.4	5.6
Return on average equity (%)	16.5	17.0	18.2	18.2	18.1

Source: Company data, RHB

Target Price (Return): MYR2.40 (-23%)
 Price (Market Cap): MYR3.11 (USD484m)
 ESG score: 3.0 (out of 4)
 Avg Daily Turnover (MYR/USD) 2.70m/0.57m

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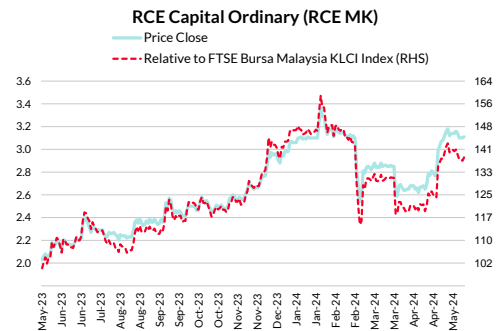


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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	1.6	11.5	16.5	16.5	56.3
Relative	(9.7)	8.5	12.0	5.1	41.4
52-wk Price low/high (MYR)	2.03 – 3.36				



Source: Bloomberg

Overall ESG Score: 3.0 (out of 4)

E: GOOD

RCE's emissions intensity (per employee) demonstrated a decrease in FY23 (Mar) despite the full reopening of the economy post-pandemic. The group has also committed to disclosing its internal Scope 3 emissions in its FY24 annual report, in line with the Bursa Malaysia Enhanced Sustainability Reporting Framework.

S: GOOD

RCE places strong focus on employee development - its employees enjoyed an average of 32 training hours in FY23, compared to 24 hours in FY22. The Group, in collaboration with Yayasan Azman Hashim, provides study grants and scholarships to deserving underprivileged students to pursue Chartered Accountancy certifications. To date, MYR572,000 has been distributed under the programme.

G: EXCELLENT

4 out of 8 members of the Board of Directors (ex-CEO) are independent directors, while all members are non-executive. Board members have a maximum allowed tenure of 9 years, to facilitate Board refreshment.

Note:

Small cap stocks are defined as companies with a market capitalisation of less than USD0.5bn.

Financial Exhibits

Asia	Financial summary (MYR)	Mar-23	Mar-24	Mar-25F	Mar-26F	Mar-27F
Malaysia	EPS	0.19	0.19	0.21	0.22	0.23
Financial Services	Recurring EPS	0.19	0.19	0.21	0.22	0.23
RCE Capital	DPS	0.12	0.15	0.16	0.17	0.17
RCE MK	BVPS	1.10	1.13	1.19	1.25	1.31
Sell						
	Valuation metrics	Mar-23	Mar-24	Mar-25F	Mar-26F	Mar-27F
Valuation basis	Recurring P/E (x)	16.42	16.43	14.66	13.94	13.40
Our GGM assumptions are:	P/B (x)	2.8	2.7	2.6	2.5	2.4
CoE of 10.8%;	Dividend Yield (%)	3.8	4.8	5.1	5.4	5.6
ROE of 18.2%;						
3.5% long-term growth rate.						
	Income statement (MYRm)	Mar-23	Mar-24	Mar-25F	Mar-26F	Mar-27F
Key drivers	Interest income	281	291	308	325	345
Our FY25 forecasts are most sensitive to changes in:	Interest expense	(90)	(99)	(103)	(109)	(115)
i. Growth in receivables;	Net interest income	190	192	205	216	230
ii. Impairment allowances;	Non interest income	71	89	96	102	104
iii. Financing margins.	Total operating income	261	281	301	318	334
	Overheads	(49)	(66)	(63)	(68)	(73)
	Pre-provision operating profit	213	215	237	250	261
	Loan impairment allowances	(29)	(30)	(30)	(32)	(34)
	Pre-tax profit	184	185	207	218	227
	Taxation	(45)	(46)	(52)	(54)	(57)
	Reported net profit	139	139	156	163	170
	Recurring net profit	139	139	156	163	170
	Profitability ratios	Mar-23	Mar-24	Mar-25F	Mar-26F	Mar-27F
Key risks	Return on average assets (%)	4.9	4.7	5.1	5.1	5.0
Upside risks include:	Return on average equity (%)	16.5	17.0	18.2	18.2	18.1
i. Greater-than-expected financing growth;	Return on IEAs (%)	10.3	10.1	10.4	10.5	10.5
ii. Lower-than-expected credit costs;	Cost of funds (%)	4.6	4.7	4.7	4.8	4.8
iii. Stronger-than-expect net financing margin.	Net interest spread (%)	5.7	5.4	5.6	5.7	5.7
	Net interest margin (%)	7.0	6.7	6.9	7.0	7.0
	Non-interest income / total income (%)	27.1	31.6	31.9	32.1	31.2
	Cost to income ratio (%)	18.7	23.4	21.0	21.4	22.0
	Credit cost (bps)	147	147	140	140	140
The converse represents upside risks.						
	Balance sheet (MYRm)	Mar-23	Mar-24	Mar-25F	Mar-26F	Mar-27F
Company Profile	Total gross loans	2,021	2,100	2,205	2,338	2,501
RCE Capital 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.	Other interest earning assets	854	800	822	845	869
	Total gross IEAs	2,875	2,900	3,027	3,183	3,370
	Total provisions	(122)	(128)	(140)	(154)	(170)
	Net loans to customers	1,899	1,973	2,066	2,184	2,332
	Total net IEAs	2,753	2,772	2,888	3,029	3,201
	Total non-IEAs	194	223	258	273	264
	Total assets	2,947	2,996	3,146	3,302	3,464
	Other interest-bearing liabilities	2,092	2,120	2,226	2,337	2,454
	Total IBLs	2,092	2,120	2,226	2,337	2,454
	Total non-IBLs	50	46	45	46	47
	Total liabilities	2,141	2,166	2,271	2,383	2,501
	Share capital	202	202	202	202	202
	Shareholders' equity	806	830	875	919	964
	Asset quality and capital	Mar-23	Mar-24	Mar-25F	Mar-26F	Mar-27F
	Reported NPLs / gross cust loans (%)	3.8	3.7	3.8	3.8	3.8
	Total provisions / reported NPLs (%)	157.8	165.8	166.9	173.0	178.3

Source: Company data, RHB

Results At a Glance

Figure 1: Summary of 4QFY24 and FY24 results

FYE Mar (MYRm)	4Q FY23	3Q FY24	4Q FY24	QoQ (%)	YoY (%)	FY23	FY24	YoY (%)	Comments
Net profit income	45.1	50.0	47.3	(5)	5	190.4	192.0	1	
Profit income	70.5	74.1	72.4	(2)	3	280.7	290.8	4	In line with +4% growth in gross financing receivables.
Profit expense	(25.4)	(24.1)	(25.1)	4	(1)	(90.3)	(98.8)	9	
Non-profit income	20.9	23.4	19.7	(16)	(6)	71.0	88.8	25	Includes interest/profit income on deposit placements.
<i>Non-IT/Total income (%)</i>	31.7	31.9	29.4			27.1	31.6		
Operating Income	66.0	73.4	67.0	(9)	2	261.4	280.8	7	
Overhead expenses	(11.4)	(19.2)	(17.5)	(9)	54	(48.8)	(65.8)	35	Driven by higher fees for drawdown of new borrowings, marketing expenses, and fees for recoveries.
<i>CIR (%)</i>	17.3	26.2	26.2			18.7	23.4		
PIOP	54.6	54.2	49.5	(9)	(9)	212.6	215.1	1	
Impairment on financing	(8.2)	(8.3)	(10.3)	24	27	(28.7)	(30.2)	5	
<i>Ann. credit costs (bps)</i>	163	159	196			147	147		
PBT	46.4	45.8	39.1	(15)	(16)	183.9	184.8	0	
Taxation	(11.6)	(11.3)	(10.1)			(45.2)	(46.1)		
<i>ETR (%)</i>	25.0	24.6	25.7			24.6	24.9		
Net Earnings	34.8	34.6	29.1	(16)	(17)	138.8	138.8	(0)	Formed 94% of our and consensus' full-year estimates.
Other key data and ratios									
Gross financing	2,020.9	2,106.8	2,100.4	(0)	4				
Total borrowings	2,091.5	2,194.7	2,119.6	(3)	1				Short-term borrowings increased 31% YoY (+11% QoQ) as management prefers to have more rate flexibility.
Total assets	2,946.8	3,049.7	2,995.6	(2)	2				
Shareholders' funds	805.7	805.9	829.8	3	3				
ROAA (%)	4.8%	4.6%	3.8%			4.9%	4.7%		
ROAE (%)	17.7%	17.0%	14.2%			16.5%	17.0%		

Source: Company data, RHB

Figure 2: Revisions to our full-year earnings forecasts

FYE Mar	Net profit (MYRm)			EPS (MYR)			DPS (MYR)		
	Previous	Revised	% Chg	Previous	Revised	% Chg	Previous	Revised	% Chg
2025F	157.3	155.5	-1.2	0.21	0.21	-1.2	0.16	0.16	-1.2
2026F	164.5	163.5	-0.6	0.22	0.22	-0.6	0.17	0.17	-0.6
2027F	na	170.1	na	na	0.23	na	na	0.17	na

Source: Company data, RHB

Valuation and TP

Our unchanged TP of MYR2.40 is based on a GGM-derived P/BV of 1.99x (from 1.97x), and includes a 0% ESG premium/discount. Our ROE assumption (18.2%, from 17.9%) was raised after incorporating FY27F numbers into our model, albeit offset by a lower BVPS assumption of MYR1.18 (from MYR1.21) for CY24.

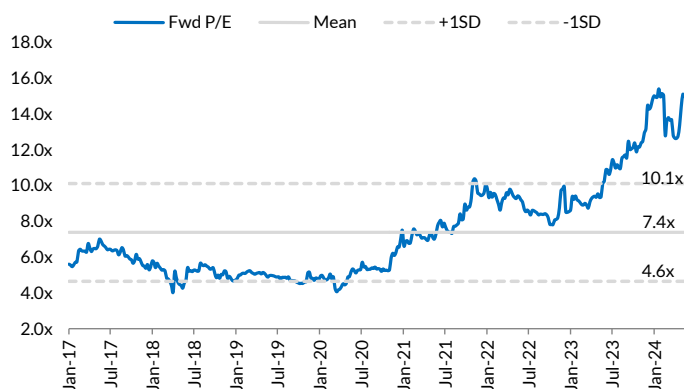
While the stock's fundamentals are holding up well in spite of ongoing challenges, we retain our SELL call on valuation grounds – at 2.6x P/BV (over +3SD from mean) against 17-18% ROE, we believe that the counter is potentially overvalued.

Figure 3: GGM valuation

Cost of equity (COE) computation:		Sustainable ROE (%)	18.2
Risk free rate (%)	4.0	COE (%)	10.8
Equity premium (%)	5.9	Long-term growth (g)	3.5
Beta (x)	1.2	Implied P/BV (x)	1.99
Cost of equity - CAPM (%)	10.8	BVPS - CY24F	MYR1.18
		Intrinsic value	MYR2.37
ESG premium/(discount) (%)	0.0	ESG premium/(discount)	MYR0.00
		TP (rounded)	MYR2.40

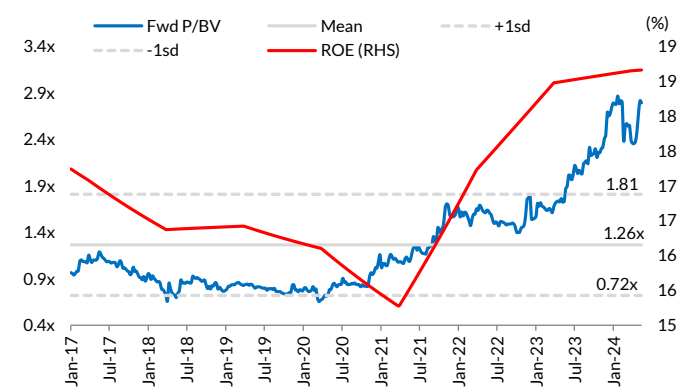
Source: Company data, RHB

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



Source: Bloomberg, RHB

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



Source: Bloomberg, RHB

Emissions And ESG

Trend analysis

RCE's total emissions intensity decreased to 0.87 tCO₂e per employee in FY23, from 0.93 tCO₂e in FY22. The group plans to disclose Scope 3 emissions in its FY24 annual report.

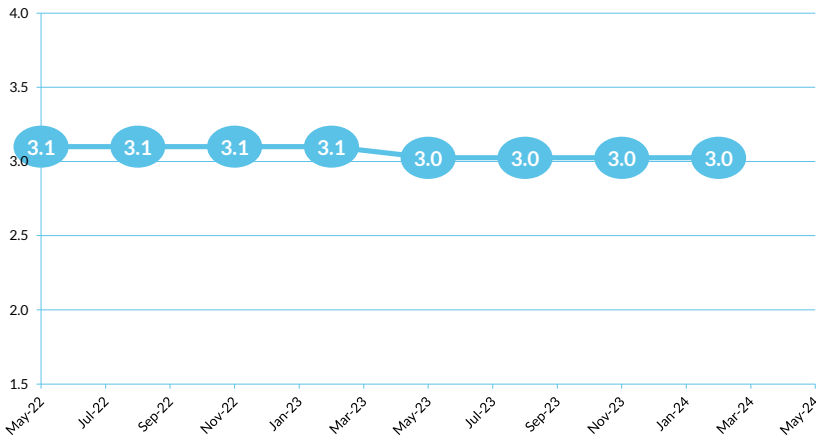
Emissions (tCO ₂ e)	Mar-22	Mar-23	Mar-24
Scope 1	16	19	na
Scope 2	150	155	na
Scope 3	-	-	na
Total emissions	166	174	na

Source: Company data, RHB

Latest ESG-Related Developments

- **Scope 3 emissions reporting:** RCE plans to introduce its (internal) Scope 3 emissions data in its FY24 annual report, which is to be released in mid-2024.
- **Emphasis on employee development:** RCE's employees received an average of 32 training hours per employee, reflecting an increase of eight hours YoY, on topics such as leadership development, regulatory and technical skills, and special interest topics.

ESG Rating History



Source: RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2024-02-08	Sell	2.40	3.14
2024-01-12	Sell	2.30	3.10
2023-11-23	Sell	2.30	2.68
2023-08-15	Neutral	2.20	2.28
2023-05-24	Neutral	1.95	1.99
2023-02-15	Neutral	1.95	1.85
2022-11-22	Neutral	1.95	1.87
2022-08-12	Buy	1.92	1.64
2022-05-31	Buy	2.00	1.76
2022-02-25	Buy	1.90	1.69
2021-11-10	Neutral	3.90	2.02
2021-08-12	Buy	3.20	1.43
2021-05-26	Buy	3.20	1.43
2021-02-09	Buy	3.00	1.32
2020-12-08	Buy	2.80	1.29

Source: RHB, Bloomberg

RHB Guide to Investment Ratings

Buy:	Share price may exceed 10% over the next 12 months
Trading Buy:	Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain
Neutral:	Share price may fall within the range of +/- 10% over the next 12 months
Take Profit:	Target price has been attained. Look to accumulate at lower levels
Sell:	Share price may fall by more than 10% over the next 12 months
Not Rated:	Stock is not within regular research coverage

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