

RCE Capital Bhd (RCE MK)

Risk reward profile more even but not out of the woods yet

Upgrade to HOLD with unchanged MYR1.45 TP

We met senior management for updates. Demand has been ‘overflowing’ since the civil servants’ salary hike and the potential abolishment of Rule of 78 (R78) ([link](#)) will not impact earnings materially but any reduction in the tenure of new financings may crimp demand. We maintain our estimates pending guidance on financing growth and potential regulatory actions; and MYR1.45 TP on 2.4x end-FY25E P/BV. As its share price has eased and there is now 5% upside, we upgrade RCE to HOLD from SELL.

Demand ‘overflowing’ post-civil servants’ salary hike

Civil servants received a 8% salary hike on 1 Dec 2024 and will receive another 7% salary hike on 1 Jan 2026. Recall that there is a strong correlation between RCE’s financing receivables and government emoluments (Fig. 2). RCE stated that demand has been ‘overflowing’ to the point that some staff have to work weekends to process applications. Yet, it cautioned that the credit quality of many new applicants are less than desirable. Thus, it is not ready to guide on financing growth yet. We forecast financing growth of 15% over 2 years from Dec 2024 (Fig. 3)

Potential impact of Rule of 78 abolition minimal

Under R78, payments in the earlier part of financings go more towards paying interest than principal ([link](#)). Thus, a customer has relatively more principal to redeem if he/she settles the financing early. If R78 is abolished, RCE will have to charge less fee income should a customer settle his/her financing early as it is based on the principal outstanding. That said, RCE explained that it usually gives a discount on the fee income to customers and can vary it should R78 be abolished.

Potential impact of tenure reduction more severe

Notwithstanding, we believe that any reduction in the tenure of new personal financings to 7 years from 10 will crimp financing growth as it will push the debt service ratio of customers towards the 60% cap. When the tenure of new personal financings was reduced to 10 years from 25 in Jul 2013, RCE’s FY3/14 financing receivables eased 2% YoY even though the salaries of civil servants were hiked by 7% to 13% on 1 Apr 2012. Feedback to Bank Negara Malaysia on its proposal to reduce the tenure of new personal financings must be submitted by 14 Feb 2025.

FYE Mar (MYR m)	FY23A	FY24A	FY25E	FY26E	FY27E
Operating income	261	281	296	319	335
Pre-provision profit	213	215	227	246	258
Core net profit	139	139	147	159	167
Core FDEPS (MYR)	0.09	0.09	0.10	0.11	0.11
Core FDEPS growth(%)	3.7	(0.0)	4.5	8.3	5.0
Net DPS (MYR)	0.15	0.08	0.08	0.09	0.09
Core FD P/E (x)	9.7	14.2	14.7	13.6	13.0
P/BV (x)	1.7	2.4	2.5	2.4	2.3
Net dividend yield (%)	16.5	5.6	5.5	5.9	6.2
Book value (MYR)	0.55	0.57	0.59	0.61	0.63
ROAE (%)	16.5	17.0	17.4	18.1	18.3
ROAA (%)	4.9	4.7	4.8	4.9	4.9
Consensus net profit	-	-	132	151	160
MIBG vs. Consensus (%)	-	-	11.5	4.9	4.2

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HOLD

[Prior:SELL]

Share Price MYR 1.45
12m Price Target MYR 1.45 (+5%)
Previous Price Target MYR 1.45

Company Description

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

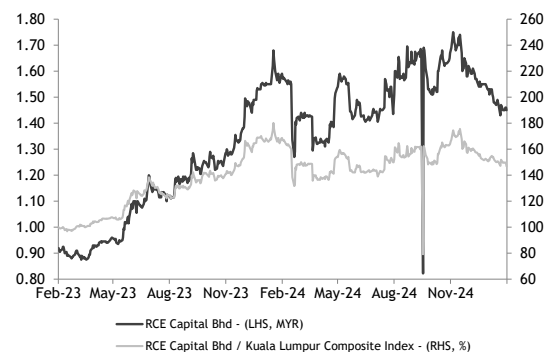
Statistics

52w high/low (MYR)	1.75/0.82
3m avg turnover (USDm)	0.3
Free float (%)	35.3
Issued shares (m)	1,482
Market capitalisation	MYR2.1B USD485M

Major shareholders:

Cempaka Empayar Sdn. Bhd.	57.9%
Khai Yoon Woo	1.5%
Employees Provident Fund	1.5%

Price Performance



	-1M	-3M	-12M
Absolute (%)	(5)	(13)	(9)
Relative to index (%)	(2)	(10)	(12)

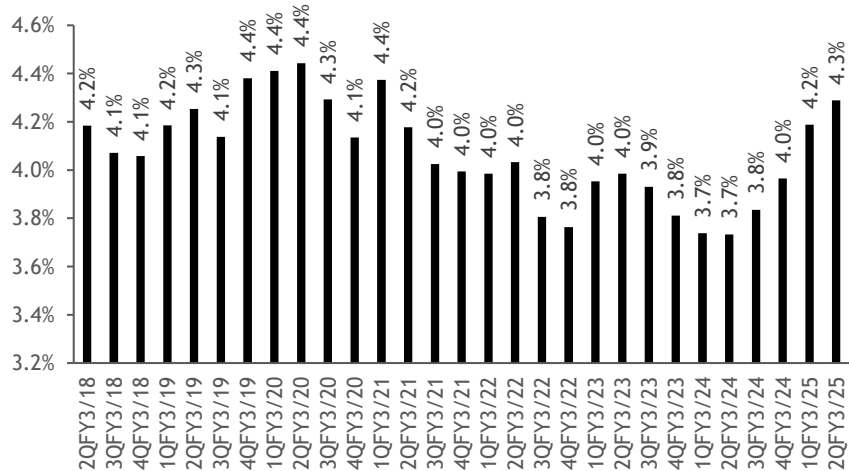
Source: FactSet

ESG@MAYBANK IBG
Tear Sheet Insert

RCE prudent to be cautious on credit quality

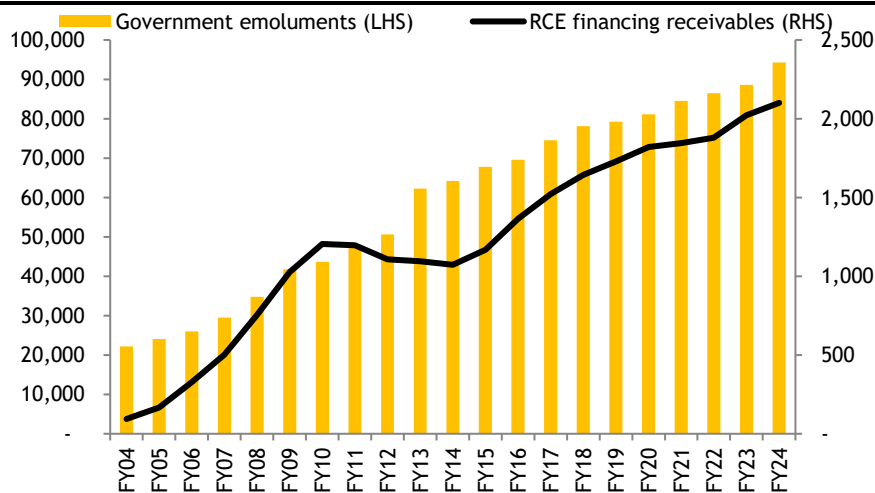
Its non-performing financing (NPF) ratio has been rising due to civil servants resigning to join the private sector and overleveraging via compressed financing (applying for multiple financings nearly simultaneously) (Fig. 1). With higher salaries effective 1 Dec 2024, we hope RCE's NPF ratio will ease to 4.0% from 4.3% as at end-2QFY3/25. In terms of financing growth, our forecast of 15% over 2 years from Dec 2024 is premised on a 1:1 ratio relative to the 15% increase in civil servants' salaries (8% on 1 Dec 2024 and 7% on 1 Jan 2026). At this point, RCE cannot comment if it expects financing growth to outpace the increase in civil servants' salaries due to the poor credit quality of many applicants.

Figure 1: Non-performing financing ratio



Source: Company

Figure 2: Government emoluments vs. RCE financing receivables (MYRm)



Source: Company

Figure 3: Major assumptions

	FY3/22A	FY3/23A	FY3/24A	FY3/25E	FY3/26E	FY3/27E
Financing growth	1.8%	7.5%	3.9%	5.0%	10.0%	2.0%
Profit spread	10.1%	9.8%	9.4%	9.4%	9.5%	9.5%
Cost to income ratio	21.1%	18.6%	23.4%	23.2%	23.1%	23.1%
Credit cost ratio	0.6%	1.5%	1.5%	1.5%	1.5%	1.5%

Sources: Company (historical), Maybank Investment Banking Group (forecasts)

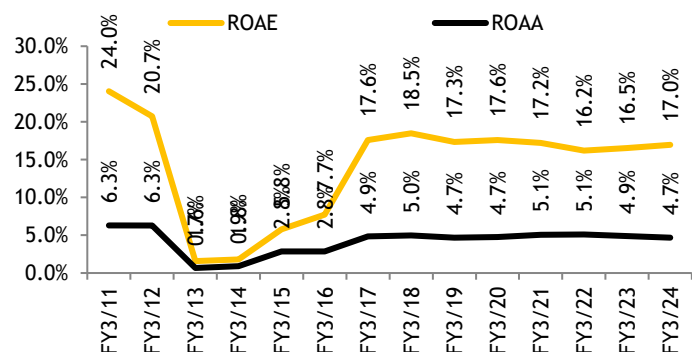
Valuation and recommendation

Our MYR1.45 TP is based on 2.4x end-FY25E P/BV. We derive a target end-FY25E P/BV of 2.4x via the following assumptions: - (i) average 2 year forward ROE of 17.7%; (ii) terminal growth rate of 2.0% as government emoluments have grown at 1.8% CAGR over the last 10 years; and (iii) cost of equity of 8.6% based on risk free rate of 4.2%, market risk premium of 6.3% and Beta of 0.70 (5-year historical Beta: 0.60).

Value Proposition

- RCE Capital provides personal financing, the ultimate customers being civil servants.
- With a gross financing balance of just MYR2.1b, we estimate that its market share is only 2%.
- Non-performing financing kept in check thanks to nondiscretionary 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.

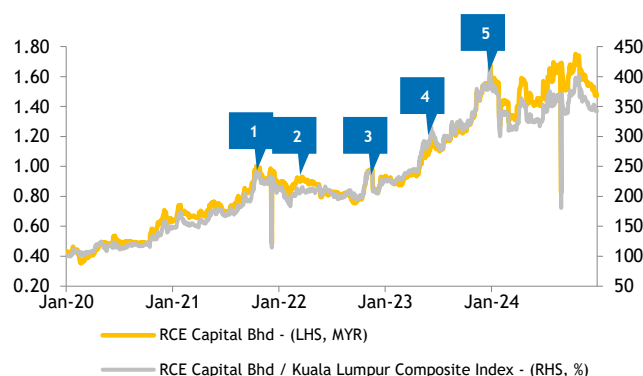
ROAE and ROAA



Source: Company

Price Drivers

Historical share price trend



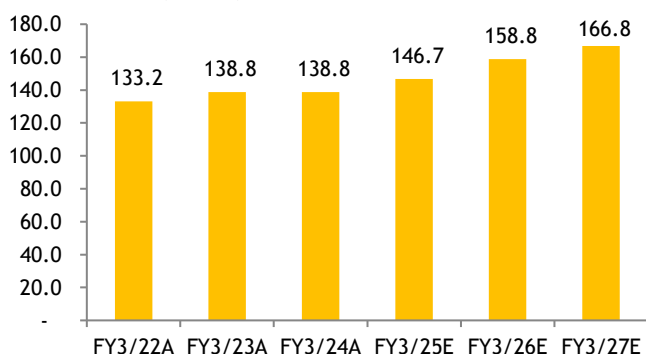
Source: Company, Maybank IBG Research

1. 2QFY21 net profit grew 21% YoY to a record high of MYR33.0m.
2. Announced share DPS of 1 treasury share for 20 shares held and bonus issue of 19 shares for 21 shares held.
3. Bank Negara Malaysia raised Overnight Policy Rate by 25bps for the first time since Jul 2020.
4. Announced a huge special DPS of 18sen and higher-than-expected interim DPS of 5sen.
5. Announced that it raised its dividend policy from 20-40% DPR to 60-80% DPR.

Financial Metrics

- Introduced better credit scoring model in 2013. We forecast gross financing CAGR of 6% p.a. over the next three years.
- Average cost of funds is rising but so is average financing yields.
- Asset quality better than before. New financings are smaller in size (<2%).
- Forecast stable three-year forward core net profit CAGR of 6% p.a.
- Recently raised DPR policy from 20-40% to 60-80%.

Core net profit (MYRm)



Source: Company (historicals), Maybank IBG Research (forecasts)

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's debt repayment.

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Risk Rating & Score ¹	N/A
Score Momentum ²	N/A
Last Updated	N/A
Controversy Score ³	N/A

Business Model & Industry Issues

- Being a non-bank financial institution (NBFI), RCE does not have a large environmental footprint. That said, we opine that it has a large social footprint by way of responsible financing.
- NBFIs were a lot more carefree in disbursing financing before Jul 2013. In Jul 2013, Bank Negara Malaysia instituted macro prudential measures to rein in high household debt levels caused by the aforementioned.
- Since then, reflecting RCE's broad transition to more socially-responsible lending parameters, tenure of its financing is capped at 10 years (25 years previously) and debt service ratio of its customers is capped at 60%.
- In CY13, RCE also put in place an in-house credit scoring model that precludes RCE from over-lending to particular customers. As a result, average financing/customer has eased from c. MYR30,000 in FY3/13 to c. MYR20,000 currently.
- To be sure, RCE does carry out related party transactions (RPT) as it places deposits and borrows from AMMB Holdings which is 12%-owned by Tan Sri Azman Hashim, the controlling shareholder of RCE.
- That said, interest rates on the aforementioned deposits and borrowings do not appear unfair to us or detrimental to minority shareholders. RCE has also been a constituent of the FTSE4Good Bursa Malaysia Index since 22 Jun 2020.
- All in all, we rate RCE's ESG credentials vis-à-vis its core business as commendable. RCE scores above-average in our proprietary scoring methodology with an overall score of 75/100 (71/100 previously).

Material E issues

- No major environmental issues. Cut paper utilisation/employee by 10% to 5.4k pieces in FY3/24 vis-à-vis FY3/20.
- The above was achieved via emails reminding employees to "Think before you Print" and printing on both sides.
- FY3/24 scope 1 and 2 emissions in CO2e tonnes per employee cut to 0.85 (FY3/20: 0.96).
- Part of the reason for the above is due to the extensive use of energy saving light bulbs.

Material S issues

- RCE is guided by Bank Negara Malaysia's (BNM) guidelines for responsible financing.
- In Jul 2013, BNM instituted macro prudential measures to rein in high household debt levels.
- Since then, tenure of its financing is capped at 10 years and debt service ratio of its customers is capped at 60%.
- In-house credit scoring model put in place in CY13 precludes RCE from over-lending to a customer.
- As a result, average financing/customer has eased from c. MYR30,000 in FY3/13 to c. MYR20,000 currently.
- Technical and soft skills trainings provided to sales team to promote responsible financing.
- Extends study grants to students pursuing the Association of Chartered Certified Accountants qualification.
- To date, RCE has extended MYR584,000 in study grants to 36 students.
- An overwhelming 74% of RCE's employees as at end-FY3/24 are women.
- FY3/24 overall employee turnover rate decreased to 12.8% (FY3/23: 16.0%, FY3/22: 17.5%).
- FY3/24 average training hours per employee was 24 (FY3/23: 35, FY3/22: 24).

Key G metrics and issues

- BOD comprises 1 Non-Independent Non-Executive Chairman (NINEC), 3 Non-Independent Non-Executive Directors (NINED) and 4 Independent Directors (ID; 50% of total).
- Largest shareholder is Cempaka Empayar Sdn Bhd, which is controlled by Tan Sri Azman Hashim (TSAH).
- NINEC, Shahman Azman is a son of TSAH. NINED, Shalina Azman is a daughter of TSAH.
- Only 2 of the 8 BOD members are women (25% representation), the aforementioned Shalina Azman and Azura Binti Rahman.
- FY3/24 directors' remuneration accounted for <1% of FY3/24 net profit.
- Deloitte PLT is the independent auditor. They have been appointed for >10 years.
- There are 4 BOD level committees. 2 are chaired by IDs (i.e. Audit and Nomination & Remuneration), 1 chaired by a NINED (i.e. Employees' Share Scheme) and 1 chaired by the NINEC (i.e. Sustainability Management).
- Carries out RPTs with AMMB Holdings (AMMB), which is 12%-owned by TSAH. As at end-FY3/24, RCE has deposits of MYR396.2m and borrowings of MYR379.9m with AMMB.
- That said, interest rates on the aforementioned deposits and borrowings appear fair to us.
- RCE hired PricewaterhouseCoopers Consulting to review its related party transactions.

¹**Risk Rating & Score** - derived by Sustainalytics and assesses the company's exposure to unmanaged ESG risks. Scores range between 0 - 50 in order of increasing severity with low/high scores & ratings representing negligible/significant risk to the company's enterprise value, respectively, from ESG-driven financial impacts. ²**Score Momentum** - indicates changes to the company's score since the last update - a **negative** integer indicates a company's improving risk score; a **positive** integer indicates a deterioration. ³**Controversy Score** - reported periodically by Sustainalytics in the event of material ESG-related incident(s), with the impact severity scores of these events ranging from Category 0-5 (0 - no reports; 1 - negligible risks; ...; 5 - poses serious risks & indicative of potential structural deficiencies at the company).

Quantitative Parameters (Score: 50)						
	Particulars	Unit	2022	2023	2024	ACSM MK (FY3/24)
E	Scope 1 emissions	tCO2e	16	19	22	200
	Scope 2 emissions	tCO2e	150	155	152	2,317
	Total	tCO2e	166	174	174	2,517
	Scope 3 emissions	tCO2e	N/A	N/A	377	N/A
	Total	tCO2e	166	174	551	2,517
	Scope 1 & 2 emissions per employee	tCO2e	0.94	0.90	0.85	0.81
	Energy consumption	GJ	1,206.6	1,300.8	1,339.9	N/A
	Water consumption	m3	N/A	N/A	267	19,457
	Paper consumption per employee	'000 pieces	3.7	3.7	5.4	N/A
	Waste generated	kg	N/A	N/A	N/A	N/A
Waste diverted from disposal	kg	322.4	796.7	1,010.7	N/A	
S	% of women in workforce	%	73%	74%	74%	66%
	% of women in managerial roles	%	64%	66%	69%	39%
	Sales team responsible financing training rate	%	100.0%	100.0%	97.2%	N/A
	Responsible financing articles posted on social media	posts	7	19	7	N/A
	Complaints received & resolved	number	7	6	8	N/A
	Employee turnover rate	%	17.5	16.0	12.8	18.2
	Employee training per employee	hours	24	35	24	21
G	Incidents of non-compliance	incidents	1	3	-	-
	Board salary as % of core net profit	%	0.7%	0.7%	0.7%	1.1%
	Independent directors on the Board	%	50%	50%	50%	56%
	% of profits returned to shareholders	%	57%	158%	79%	34%
	Female directors on the Board	%	11%	13%	25%	44%

Qualitative Parameters (Score: 100)	
a) Is there an ESG policy in place and whether there is a standalone ESG committee or is it part of a risk committee?	<i>Yes. RCE has an ESG policy in place. It has a Sustainability Working Committee which reports to the Sustainability Management Committee which in turn, reports directly to the Board of Directors.</i>
b) Is the senior management salary linked to fulfilling ESG targets?	<i>Yes.</i>
c) Does the company follow the task force of climate related disclosures (TCFD) framework for ESG reporting?	<i>Yes.</i>
e) Does the company have a mechanism to capture Scope 3 emissions - which parameters are captured?	<i>Yes. Employee commute.</i>
f) What are the 2-3 key carbon mitigation/water/waste management strategies adopted by the company?	<i>Switching off all office lights and equipment during breaks and before leaving office, retro-fitting LED lighting, recycling paper and avoiding unnecessary printing.</i>
g) Does carbon offset form part of the net zero/carbon neutrality target of the company?	<i>No, as RCE is not a major polluter.</i>

Target (Score: 100)		
Particulars	Target	Achieved
Reduce GHG emissions/employee by FY3/24E	1.0	0.9
Women representation on board by FY3/25E	30%	NA
Impact		
NA		
Overall Score: 75		
As per our ESG matrix, RCE Capital (RCE MK) has an overall score of 75.		

ESG score	Weights	Scores	Final Score
Quantitative	50%	50	25
Qualitative	25%	100	25
Target	25%	100	25
Total			75

As per our ESG assessment, RCE has an established framework, internal policies, and tangible mid/long-term targets. RCE's overall ESG score is 75, which makes its ESG rating above average in our view (average ESG rating = 50; refer to Appendix I for our ESG Assessment Scoring).

Appendix I

Methodology of our proprietary ESG scoring methodology.

We evaluate the ESG ratings based on quantitative, qualitative and ESG targets. We assign a score for each of these three parameters. The overall rating is based on the weighted average of the scores: quantitative (50%), qualitative (25%) and ESG target (25%).

For the quantitative, qualitative and ESG target, the sub-parameters are assigned a score - '0' for data not available, '+1' for improving trajectory, positive change, 'Yes', better than peers or a positive number if historical is not available and '-1' for declining trajectory, negative change, 'No', lower than peers or a negative number. The total of the scores of all the sub-parameters is divided by the total number of sub-parameters, to derive the score of each of the three parameters.

The sub-parameters may be different for different industries depending on the key areas to monitor for each industry. A company should achieve a minimum score of 50 for an average ESG rating.

FYE 31 Mar	FY23A	FY24A	FY25E	FY26E	FY27E
Key Metrics					
Core P/E (x)	9.6	14.2	14.5	13.4	12.7
Core FD P/E (x)	9.7	14.2	14.7	13.6	13.0
P/BV (x)	1.7	2.4	2.5	2.4	2.3
P/NTA (x)	1.8	2.5	2.6	2.5	2.4
Net dividend yield (%)	16.5	5.6	5.5	5.9	6.2
INCOME STATEMENT (MYR m)					
Islamic banking income	209.4	221.2	233.0	250.5	265.3
Other income	52.0	59.6	62.6	68.7	70.1
Total non-interest income	261.4	280.8	295.5	319.2	335.4
Operating income	261.4	280.8	295.5	319.2	335.4
Staff costs	(27.1)	(32.2)	(33.6)	(36.3)	(38.2)
Other operating expenses	(21.7)	(33.6)	(34.9)	(37.4)	(39.1)
Operating expenses	(48.8)	(65.8)	(68.6)	(73.7)	(77.3)
Pre-provision profit	212.6	215.1	227.0	245.5	258.1
Other allowances	(28.7)	(30.2)	(31.6)	(34.0)	(35.9)
Associates & JV income	0.0	0.0	0.0	0.0	0.0
Pretax profit	183.9	184.8	195.4	211.6	222.2
Income tax	(45.2)	(46.1)	(48.7)	(52.8)	(55.4)
Reported net profit	138.8	138.8	146.7	158.8	166.8
Core net profit	138.8	138.8	146.7	158.8	166.8
BALANCE SHEET (MYR m)					
Cash & deposits with banks	879.7	840.2	876.3	925.5	964.2
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	1,953.3	2,027.3	2,126.0	2,333.1	2,378.7
Fixed assets	7.2	7.3	7.0	6.6	6.3
Intangible assets	47.3	47.3	47.3	47.3	47.3
Other assets	59.3	73.5	73.5	73.5	73.5
Total assets	2,946.8	2,995.6	3,130.1	3,386.1	3,470.0
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	1,290.9	1,175.8	1,175.8	1,175.8	1,175.8
Other borrowings	434.3	552.9	657.6	878.7	927.3
Other liabilities	416.0	437.1	437.5	438.2	438.7
Total liabilities	2,141.2	2,165.8	2,270.9	2,492.7	2,541.8
Share capital	201.9	201.9	201.9	201.9	201.9
Reserves	603.7	627.9	657.3	691.5	726.3
Shareholders' funds	805.7	829.8	859.2	893.4	928.2
Preference shares	0.0	0.0	0.0	0.0	0.0
Minority interest	0.0	0.0	0.0	0.0	0.0
Total equity	805.7	829.8	859.2	893.4	928.2
Total liabilities & equity	2,946.8	2,995.6	3,130.1	3,386.1	3,470.0

FYE 31 Mar	FY23A	FY24A	FY25E	FY26E	FY27E
Key Ratios					
Growth (%)					
Net interest income	na	na	na	na	na
Non-interest income	9.2	7.4	5.2	8.0	5.1
Operating expenses	(3.6)	34.9	4.3	7.5	5.0
Pre-provision profit	12.6	1.2	5.5	8.2	5.1
Core net profit	4.2	(0.0)	5.7	8.3	5.0
Gross loans	7.5	3.9	5.0	10.0	2.0
Customer deposits	na	na	na	na	na
Total assets	8.1	1.7	4.5	8.2	2.5
Profitability (%)					
Non-int. income/Total income	100.0	100.0	100.0	100.0	100.0
Cost/income	18.7	23.4	23.2	23.1	23.1
Liquidity (%)					
Loans/customer deposits	na	na	na	na	na
Asset quality (%)					
Gross NPF	3.8	4.0	4.0	4.0	4.0
Capital adequacy (%)					
CET1	na	na	na	na	na
Tier 1 capital	na	na	na	na	na
Risk-weighted capital	na	na	na	na	na
Returns (%)					
ROAE	16.5	17.0	17.4	18.1	18.3
ROAA	4.9	4.7	4.8	4.9	4.9
Shareholders equity/assets	27.3	27.7	27.4	26.4	26.8

Source: Company; Maybank IBG Research

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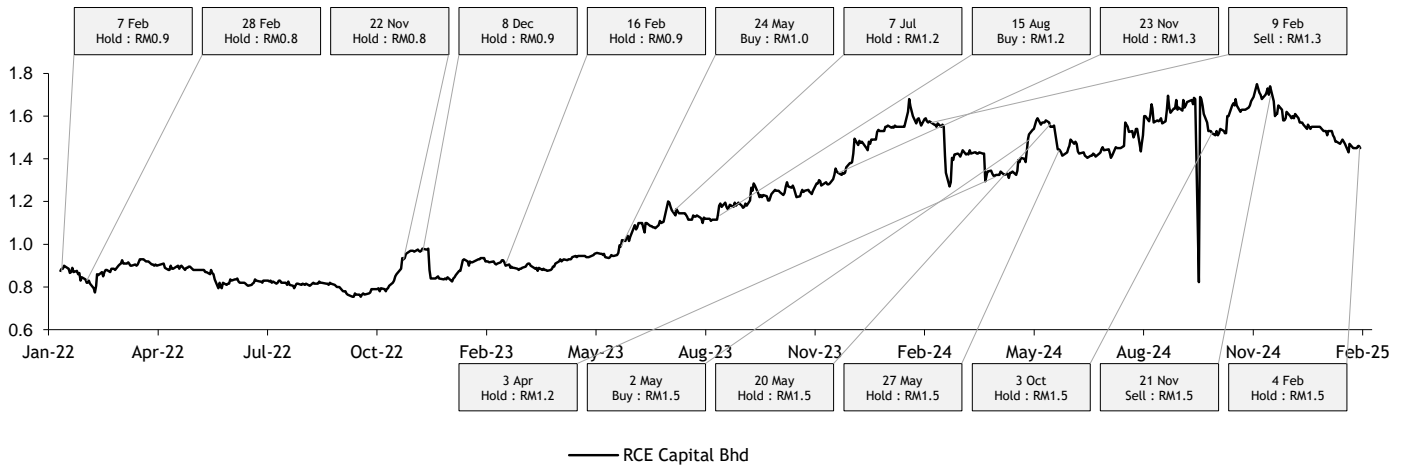
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