

RCE Capital a prime beneficiary of upcoming civil servant salary hike

BY **ADELINE PAUL RAJ**

It has certainly been a challenging year for RCE Capital Bhd. After 10 years of uninterrupted earnings growth, the non-bank financial institution recently saw a marginal dip in earnings for the financial year ended March 31, 2024 (FY2024). Its net profit that year came in flat at RM138.75 million against the previous year's RM138.78 million, despite revenue growing by 5.6% to RM341.66 million.

RCE's 4QFY2024 net profit of RM29.06 million — down 16.6% year on year (y-o-y) and 15.9% quarter on quarter (q-o-q) — was its lowest quarterly profit since 1QFY2021, no thanks to higher allowances for impairment loss amid an increase in non-performing financing (NPF), as well as greater operating expenses.

Its financing, which tends to track the banking industry's overall loan growth, grew at a muted 3.9% to RM2.1 billion in FY2024 — slower than the industry's 6% expansion over the same period.

Analysts see the tide turning for RCE only in December, as this is when civil servants are expected to get a pay hike of more than 13%.

Last week, Prime Minister Datuk Seri Anwar Ibrahim said that he would reveal the rate of the salary increment for civil servants before the tabling of Budget 2025 in October. The last time the salaries of civil servants were raised was a good 12 years ago, at a rate of 13%.

"This is a very big thing for RCE. It is a prime beneficiary of the civil servant pay hike," Maybank Investment Bank (Maybank IB) Research analyst Yin Shao Yang tells *The Edge*.

He expects the salary hike to boost the group's financing growth to 5% in FY2025 — with the bulk of the growth happening towards the end of the year — and to 10% in FY2026.

RCE provides personal financing products at fixed rates to civil servants, who then make monthly repayments via direct salary deductions. This makes its business a relatively stable one, with problems emerging only if borrowers quit the civil service — of which there has been a higher instance of late as workers move to the private sector to seek better wages to cope with the higher cost of living — or retire early.

Anwar had announced on May 1 that civil servants would enjoy a salary hike of "more than 13%" starting this December, in what would be the highest increment in the nation's history. The increase will cost the government over RM10 billion a year.

He said that the government would ensure that the minimum income for civil servants exceeds RM2,000 a month. Currently, the minimum income is RM1,795 a month, which includes salary and fixed allowances.

"There is a strong correlation between government emoluments and RCE's financing receivables balance," Maybank IB Research's Yin wrote in a report shortly after. "RCE explained that it will extend more financing to civil servants if they receive higher salaries, as long as their debt service ratio does not exceed 60% as per Bank Negara Malaysia guidelines."

RCE's muted financing growth of late is partly because it has been prioritising asset quality.

Strong correlation between government emoluments and RCE's financing growth (RM mil)



According to Yin, RCE has been declining financing applications more frequently recently as the credit quality of new applicants "has not been ideal" due to the higher cost of living.

RCE's allowances for impairment loss stood at RM10.3 million in 4QFY2024, the highest since 2QFY2014, mainly because of more retirements, changes in employment statuses and bankruptcies, notes CIMB Securities in a recent report. For the full year, the provisions grew by 5.4% to RM30.2 million. Consequently, RCE's NPF ratio rose slightly to 4% from 3.8%.

Yin estimates that RCE's net profit will grow by about 7.2% to RM149 million in

FY2025, and then by 8% to RM161 million in FY2026, on the assumption that civil servant salaries will go up by 15% on average.

"Financing growth would be better, and credit cost should be lower as well because fewer people resign from the civil service when they get paid higher. So, on two fronts, they should be doing better," he tells *The Edge*.

Meanwhile, until the pay hike takes effect in December, RCE's financing growth is expected to be "pedestrian", he says.

A consistent dividend payer, RCE declared a total dividend of 15 sen a share in FY2024, which translated into a dividend payout ratio of 79.2%.

Bloomberg data shows that three of four research houses — Maybank IB Research, PublicInvest Research and CIMB Securities — have a "hold" call on the stock, while RHB Research has a "sell". The average 12-month target price was RM2.89. The stock closed at RM2.84 last Thursday (June 27) for a market capitalisation of RM2.1 billion.

The shares, which hit a more than two-year high of RM3.36 on Jan 23, have since shed 15.5% of their value.

"While the impending revision to civil service wages will likely boost its financing growth prospects, we still prefer peers with similar ROE [return on equity] generation that are trading at cheaper valuations," RHB Research said in a May 27 report.

RCE's main shareholder is former AmBank Group chairman Tan Sri Azman Hashim, who has a 58.54% stake in the company via Cempaka Empayar Sdn Bhd. He also has a direct 0.21% stake. **E**