

7 July 2020

Financial Services | Non-Bank Financials

RCE Capital (RCE MK)

Buy (Maintained)

Hakuna Matata; Keep BUY

Target Price (Return): MYR2.50 (30.2%)
 Price: MYR1.92
 Market Cap: USD159m
 Avg Daily Turnover (MYR/USD) 0.80m/0.19m

- **Maintain BUY on this Top Pick non-bank lender, with a higher TP of MYR2.50 from MYR2.20, 30% upside and c.6% yield.** RCE Capital was largely unscathed by COVID-19 and the Movement Control Order (MCO) and earlier worries on asset quality are largely dispelled since the asset quality remains sound and collections healthy. Credit cost likely to normalize in 1QFY21 (Mar). Business activities are gradually recovering to pre-MCO level although a short-term slowdown in receivable growth seems likely. Reiterate BUY on defensive business profile, attractive valuation (c.0.8x FY22 P/BV vs 15% ROE) and yield.

- **Normalising credit cost and smooth collections.** RCE recorded MYR8.2m in impairment charges in 4QFY20. Management clarified that the 73% QoQ jump in impairment charges included an additional MYR2.3m charges related to changes in macroeconomic variables (MEV) in their Expected Credit Loss (ECL) model. Asset quality was fairly stable as the NPL ratio improved 20bps QoQ to 4.1% in 4QFY20. As such, we expect credit cost to normalize in 1QFY21, barring any further deterioration to the economic conditions. Collections remained smooth even during the MCO as RCE was able to receive full collection amounts.

- **Moratorium hardly a concern.** Payment moratorium was offered by RCE but, unlike banks, it was not on an automatic basis. Borrowers were required to apply for the moratorium and show proof that they were affected by the pandemic or MCO. Final approvals are subject to management decisions. Only a mere 0.6% of borrowers are currently on moratorium. Management is not inclined to further extend moratorium.

- **Gradually recovering to its pre-MCO level.** Business activities were kept at minimum during the MCO where both applications and disbursements slowed considerably. Situation has improved since the relaxation of MCO. We gathered that the disbursement level is now c.50% the pre-MCO level and management is hopeful for further sequential recovery. Safeguarding asset quality is the top priority currently and management is not loosening underwriting practices to boost growth.

- **Other highlights.**

- Another tranche of *sukuk* (c.MYR120m) will be issued in August and is expected to carry an even lower rate of 4.05%;
- RCE is more mindful of opex spending but headcount rationalization is not on the menu (FY20 CIR: 22%);
- As of May, all lending products are already *shariah* compliant. *Shariah* listing status will likely be obtained in 2022;
- Management is committed in honouring a 20-40% dividend payout.

- **Earnings and TP.** We made no changes to earnings forecasts but raised TP to MYR2.50 as we rolled forward our valuation base year to FY22 (Mar).

Analysts

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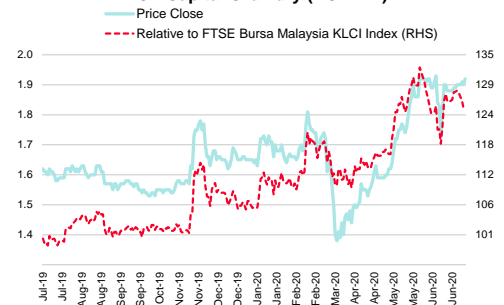
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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	16.4	1.6	27.2	17.1	18.5
Relative	17.2	0.3	9.7	18.4	24.8
52-wk Price low/high (MYR)	1.38 – 1.93				

RCE Capital Ordinary (RCE MK)



Source: Bloomberg

Forecasts and Valuation	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
Reported net profit (MYRm)	96	111	113	120	128
Net profit growth (%)	7.7	15.8	2.6	5.5	7.4
Recurring net profit (MYRm)	96	111	113	120	128
Recurring EPS (MYR)	0.28	0.32	0.32	0.34	0.37
BVPS (MYR)	1.71	1.94	2.18	2.44	2.73
DPS (MYR)	0.09	0.11	0.11	0.12	0.12
Recurring P/E (x)	6.85	6.03	5.93	5.62	5.24
P/B (x)	1.12	0.99	0.88	0.79	0.70
Dividend Yield (%)	4.7	5.7	5.7	6.0	6.3
Return on average equity (%)	17.3	17.6	15.8	14.8	14.2

Source: Company data, RHB

Note:

Small cap stocks are defined as companies with a market capitalization of less than USD1bn.

Financial Exhibits

Asia	Financial summary (MYR)	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
Malaysia	EPS	0.28	0.32	0.32	0.34	0.37
Financial Services	Recurring EPS	0.28	0.32	0.32	0.34	0.37
RCE Capital	DPS	0.09	0.11	0.11	0.12	0.12
RCE MK	BVPS	1.71	1.94	2.18	2.44	2.73
Buy						
	Valuation metrics	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
	Recurring P/E (x)	6.85	6.03	5.93	5.62	5.24
	P/B (x)	1.1	1.0	0.9	0.8	0.7
	Dividend Yield (%)	4.7	5.7	5.7	6.0	6.3
	Income statement (MYRm)	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
	Interest income	234	257	270	279	292
	Interest expense	(78)	(82)	(87)	(90)	(91)
	Net interest income	156	175	183	189	200
	Non interest income	39	46	48	50	52
	Total operating income	195	221	231	239	253
	Overheads	(45)	(49)	(53)	(55)	(57)
	Pre-provision operating profit	150	172	178	184	195
	Loan impairment allowances	(18)	(23)	(26)	(23)	(22)
	Pre-tax profit	131	149	153	161	173
	Taxation	(36)	(38)	(39)	(41)	(45)
	Reported net profit	96	111	113	120	128
	Recurring net profit	96	111	113	120	128
	Profitability ratios	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
	Return on average assets (%)	4.7	4.7	4.4	4.4	4.5
	Return on average equity (%)	17.3	17.6	15.8	14.8	14.2
	Return on IEAs (%)	12.2	12.2	12.0	11.9	11.9
	Cost of funds (%)	5.4	4.9	4.8	4.7	4.7
	Net interest spread (%)	6.9	7.3	7.2	7.1	7.1
	Net interest margin (%)	8.2	8.3	8.2	8.0	8.1
	Non-interest income / total income (%)	19.8	20.9	20.8	20.8	20.7
	Cost to income ratio (%)	23.2	22.2	23.0	23.0	22.7
	Credit cost (bps)	110	130	139	119	110
	Balance sheet (MYRm)	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
	Total gross loans	1,729	1,820	1,857	1,973	2,076
	Other interest earning assets	279	364	444	438	438
	Total gross IEAs	2,009	2,184	2,301	2,411	2,514
	Total provisions	(130)	(130)	(140)	(149)	(157)
	Net loans to customers	1,599	1,690	1,718	1,824	1,919
	Total net IEAs	1,878	2,054	2,161	2,262	2,357
	Total non-IEAs	348	377	530	539	582
	Total assets	2,226	2,431	2,691	2,801	2,939
	Other interest-bearing liabilities	1,605	1,714	1,893	1,913	1,949
	Total IBLs	1,605	1,714	1,893	1,913	1,949
	Total non-IBLs	38	43	35	32	32
	Total liabilities	1,643	1,758	1,928	1,945	1,982
	Share capital	154	172	179	185	191
	Shareholders' equity	584	673	763	856	957
	Asset quality and capital	Mar-19	Mar-20	Mar-21F	Mar-22F	Mar-23F
	Reported NPLs / gross cust loans (%)	4.4	4.1	4.7	4.6	4.6
	Total provisions / reported NPLs (%)	172.1	173.0	161.9	163.8	164.4

Source: Company data, RHB

Valuation

Our GGM-derived TP is raised to MYR2.50 from MYR2.20. We made no changes to our earnings forecast but rolled forward valuation base year to FY22 (Mar). Our TP values RCE at 1.04x FY22 P/BV which is +1 SD above its historical mean.

Figure 1: RCE's GGM valuation

Cost of equity (COE) computation:		Sustainable ROE (%)	14.9
Risk free rate (%)	2.9	COE (%)	13.9
Equity premium (%)	7.4	Long-term growth (g)	2.0
Beta (x)	1.5	Implied P/BV (x)	1.04
Cost of equity - CAPM (%)	14.4	BVPS: FY22F	MYR 2.44
		Target price	MYR 2.54
		TP (rounded)	MYR 2.50

Source: Company data, RHB

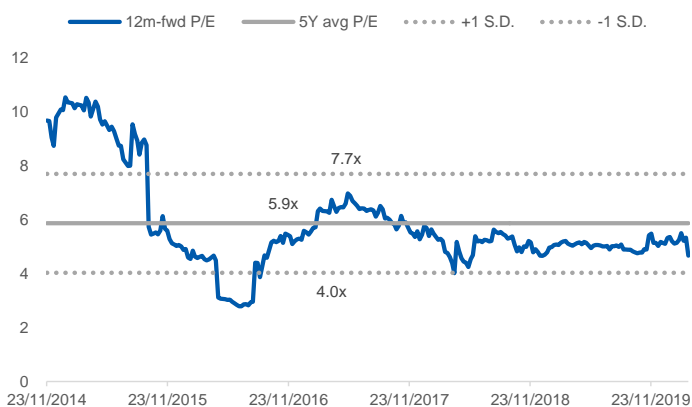
Figure 2: Peer comparison

Company	Ticker	Rec	P/BV (x)		ROE (%)		Earnings growth (%)	
			FY21F	FY22F	FY21F	FY22F	FY21F	FY22F
RCE Capital	RCE MK	BUY	0.87	0.78	15.8	14.8	2.6	5.5
AEON Credit	ACSM MK	NEUTRAL	1.4	1.28	8.5	12.9	(49.1)	66.9
ELK-Desa*	ELK MK	Non-rated	0.88	0.86	7.3	7.3	(7.7)	0.0

Source: Company data, RHB

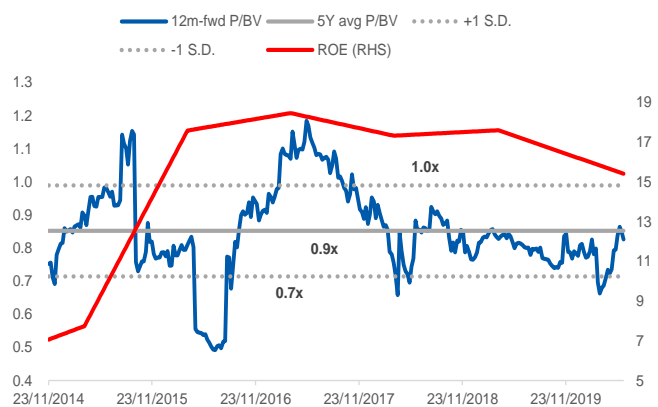
*Based on Bloomberg consensus

Figure 3: RCE's 12-month forward P/E



Source: Bloomberg, RHB

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



Source: Bloomberg, RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2020-06-16	Buy	2.20	1.81
2020-03-15	Buy	2.10	1.50
2020-02-19	Buy	2.20	1.77
2020-01-10	Buy	2.10	1.72
2019-08-16	Not Rated	na	1.60

Source: RHB, Bloomberg

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