Expansion plans to drive growth

ELK-Desa's FY18 net profit of RM25.9m (+12.6% yoy) was in-line with our expectations. The hire purchase division remains the key earnings driver while the furniture segment showed stronger bottomline profits arising from a shift in business strategy to focus on domestic markets and forming new partnerships with local dealers. As we roll-forward our valuation to CY19, we adjust our Price Target to RM1.37 (from of RM1.18) based on a 13x P/E target. Upgrade to BUY as we remain upbeat on ELK's vertical expansion plan in the hire-purchase financing unit, which will be the key earnings driver in FY19E-20E.

FY18 results within expectations, 4Q18 net profit improved yoy & qoq

ELK-Desa FY18 net profit of RM25.9m grew by +12.6% yoy, in line with our FY2018 forecast. This was mainly driven by higher profit contribution from the hire purchase (HP) division and better profits from the furniture division. Nonetheless, FY18 EPS was down 7.2% yoy due to the dilutive effect of the RM54m rights issue and a 21% increase in weighted average number of shares. Meanwhile, 4QFY18 earnings recorded a stronger 24.2% qoq increase, driven by higher contribution from the HP division (4QFY18 pretax profit +8.5% qoq) while the furniture division returned to the black from a loss-making 3QFY18.

Hire purchase drives 99% of earnings, furniture division turnaround

The HP division contributed circa 99% of the group's FY18 pre-tax profit of RM35.3m which grew by 15.5% yoy. Underpinning this was an expansion of HP net receivables growth of 11% yoy for FY18. The furniture division saw a turnaround in 4QFY18 profits on the back of a shift in business strategy to refocus on the domestic market to expand the wholesale distribution and increase partnership with dealers.

Upgrade to BUY rating, Price Target raised to RM1.37

We upgrade ELK from a HOLD to **BUY** based on a **CY19 Price Target** of **RM1.37**, which is pegged to a 13x P/E multiple on our CY19E EPS (as we move our valuation horizon from CY18 to CY19), from RM1.18. Our P/E multiple of 13x is derived from the 1-year historical average P/E multiple of ELK (of which, is not comparable to other peers due to ELK's illiquidity in the market). Downside risk – high cost-of-living may cause higher defaults.

Earnings & Valuation Summary

FYE 31 Mar (RMm)	2017A	2018A	2019E	2020E	2021E
Revenue	94.5	104.1	120.5	129.9	138.5
Net operating income	30.2	37.0	37.8	43.1	48.4
Pretax profit	30.6	35.3	36.7	40.7	45.7
Net profit	23.0	25.9	27.9	30.9	34.7
EPS (sen)	10.7	9.9	9.8	10.8	12.1
EPS growth (%)	(17.0)	(7.2)	(1.3)	10.9	12.2
FD EPS (sen)	9.2	8.7	9.3	10.3	11.6
PER (x)	13.2	11.7	11.9	10.7	9.5
FD PER (x)	15.3	13.4	12.4	11.2	10.0
ROE (%)	7.0	7.1	7.0	7.6	8.2
BV / share	1.55	1.52	1.42	1.45	1.49
P/BV	0.75	0.77	0.82	0.80	0.78
DPS (sen)	6.8	6.3	6.8	7.6	8.5
Dividend Yield (%)	5.8	5.5	5.9	6.5	7.3
Chg in EPS (%)			-	-	-
Affin/Consensus (x)			NA	NA	NA

Source: Company, Bloomberg, Affin Hwang forecasts

Results Note

ELK-Desa

ELK MK
Sector: Finance

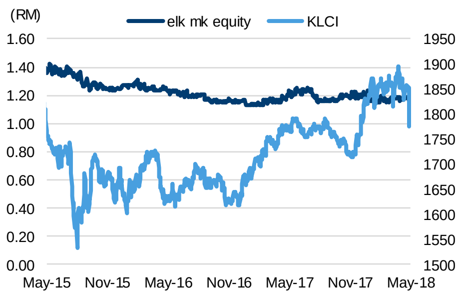
RM1.16 @ 24 May 2018

BUY (upgrade)

Upside: 18.4%

Price Target: RM1.37

Previous Target: RM1.18



Price Performance

	1M	3M	12M
Absolute	0.0%	-1.7%	-3.3%
Rel to KLCI	5.1%	3.1%	-3.6%

Stock Data

Issued shares (m)	286.6
Mkt cap	332.4/83.5
Avg daily vol - 6mth	0.1
52-wk range (RM)	1.14-1.26
Est free float	38.1%
BV per share (RM)	1.36
P/BV (x)	0.85
Net cash/(debt)	(0.4)
ROE (2019E)	7.0
Derivatives (ICULS)	14.89
Shariah Compliant	No

Key Shareholders

Eng Lee Kredit	32.5%
Amity Corporation SD	5.3%

Source: Affin, Bloomberg

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Fig 1: Results Comparison

FYE 31 Mar (RMm)	4QFY17	3QFY18	4QFY18	QoQ % chg	YoY %chg	FY17	FY18	YoY % chg	Comments
Revenue	**24.9**	**25.9**	**27.7**	*7.0*	*11.5*	**94.5**	**104.1**	*10.2*	Interest income from the hire-purchase unit remains the key topline driver, +11% yoy in 4QFY18 and 11.7% yoy for FY18. Hire purchase receivables grew by 14.3% yoy in FY18.
- Hire Purchase	17.4	18.4	19.3	*4.8*	*11.0*	65.4	73.1	*11.7*	
- Furniture	7.4	7.5	8.4	*12.3*	*12.5*	29.1	31.0	*6.9*	
Operating expenses	(16.7)	(16.5)	(17.0)	*3.2*	*1.6*	(64.9)	(68.5)	*5.6*	Most of the increase in FY18 overheads were due to higher marketing expenses and higher COGS at the furniture division.
Other Income	0.2	0.2	0.6	*135.2*	*>100*	0.6	1.8	*176.8*	
EBIT	**8.3**	**9.7**	**11.3**	*16.6*	*35.5*	**30.2**	**37.4**	*23.6*	
Net Finance Cost	(0.1)	(0.8)	(0.5)	*(39.7)*	*>100*	0.3	(2.0)	*n.m.*	Interest expense increased in tandem with higher amount of borrowings (reflected a +132% yoy growth in block discounting payables) to support the HP business.
Pre-Tax Profit	8.2	8.9	10.8	*21.4*	*31.6*	30.6	35.3	*15.6*	About 99% of contribution to PBT from hire purchase business.
Taxation	(1.8)	(2.5)	(2.9)	*13.8*	*61.7*	(7.6)	(9.4)	*24.4*	
Profit After Tax	**6.4**	**6.4**	**7.9**	*24.4*	*23.2*	**23.0**	**25.9**	*12.7*	
Net Profit	**6.4**	**6.4**	**7.9**	*24.4*	*23.2*	**23.0**	**25.9**	*12.6*	FY18 net profit in-line with our expectation, underpinned by a stronger 4QFY18.
Core EPS	**2.79**	**2.23**	**2.77**	*24.2*	*(0.7)*	**10.66**	**9.90**	*(7.2)*	Decline in FY18 core EPS growth was due to the dilution effect of the RM54m rights issue and conversion of ICULS.
Single-tier DPS (sen)	**3.50**	**-**	**3.50**	*n.m.*	-	**6.75**	**6.75**	-	A final DPS of 3.5 sen proposed for 4QFY18 (4QFY17: 3.5 sen).
Net Yield (%)	2.9	-	2.9	*n.m.*	-	5.7	5.7	-	

Source: Affin Hwang, Company data

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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