

Monday, August 22, 2022
Sector: Finance

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Elk-Desa Resources Bhd

TP: RM1.50 (+11.1%)

A Good Start to the FY

Last Traded: RM1.35

BUY (ESG: ★★★)

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Review

- Elk-Desa reported a robust set of IQFY23 results. 3M net profit more than tripled QoQ and YoY to RM17.6mn from RM5.5mn in 4QFY22 and RM5.0mn a year ago due to stronger revenue growth and writeback in impairment allowance. With that, Elk-Desa's results exceeded our expectations, with net profit accounting for 63% of our full-year forecast.
- 3M revenue increased by 24.2% YoY (+8.3% QoQ) due to better contributions from both the hire purchase and furniture segments. Revenue in the furniture segment surged by some 70% YoY due to softer sales in IQFY22 as the MCO disruptions adversely impacted sales a year ago. Revenue from the hire purchase segment grew by 7% YoY. YTD, hire purchase receivables widened by 7% to RM502mn as at 30 June 2022.
- Although the overall operating expenses also expanded YoY due to higher staff costs and overall operating costs, the group's 3M PBT surged to RM23.4mn vs. RM6.9mn in IQFY22. Elk-Desa's cost-to-income ratio stood at 28%. The better-than-expected PBT was underpinned by a writeback in impairment allowance amounting to RM5.3mn. Management noted that this is due to a significant decrease in the non-performing accounts during the quarter, which was underpinned by a recovery in activities and a strong collection trend. The net impaired loans ratio improved from 2.89% as at 31 March 2022 to 1.83% as at 30 June 2022.
- Elsewhere, the group's balance sheet strengthened as bank borrowings fell by 11%, mainly due to repayment of block discounting facilities and term loans. As a result, the finance costs decreased by 42.4% YoY on the back of the group's concerted effort to pare down its borrowings. Elk-Desa's gearing remains at a low level of 0.33x.

Impact

- Incorporating the better-than-expected IQFY23 results, we raised Elk-Desa's FY23/24/25 net profit forecast to RM37.1/39.4/41.7mn from RM27.8/31.2/35.7mn previously. Our revision considers, 1) stronger growth assumptions for furniture sales and 2) downward revision in the FY23 credit loss charge to 3.0% from 3.5%.

Outlook

- With the domestic economy expected to remain on its recovery path, we expect the overall demand for used-car hire purchase financing to accelerate as ELK-Desa aims to bring its hire purchase receivables portfolio towards pre-pandemic levels gradually. Other catalysts driving demand for used cars include the introduction of a higher minimum wage rate of RM1500 may be positive for the industry. However, we note that potential downside risks such as rising living costs due to the increased inflationary pressures and rising interest rates could affect borrowers' disposable incomes and ability to repay.

Share Information

Bloomberg Code	ELK MK
Stock Code	ELK MK
Listing	5228
Share Cap (mn)	Main Market
Market Cap (RMmn)	303.2
52-wk Hi/Lo (RM)	409.32
12-mth Avg Daily Vol ('000 shrs)	1.45/1.20
Estimated Free Float (%)	83.1
Beta	37.6
Major Shareholders (%)	0.5
Eng Lee Kredit	- 32.2%
Amity Corp	- 5.1%

Forecast Revision

	FY23	FY24
Forecast Revision (%)	33.3	26.0
Net profit (RMmn)	37.1	39.4
Consensus	n.a.	n.a.
TA's / Consensus (%)	n.a.	n.a.
Previous Rating	Buy	
Consensus Target Price (RM)	n.a.	

Scorecard (%)

vs TA	63	Above
vs Consensus	n.a.	n.a.

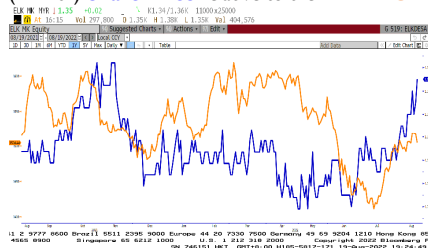
Financial Indicators

	FY23	FY24
CFPS (sen)	9.8	7.3
Price / CFPS (x)	13.8	18.4
ROA (%)	5.2	4.9
NTA/Share (RM)	1.5	1.6
Price/NTA (x)	0.9	0.9

Share Performance (%)

Price Change	ELK	FBM KLCI
1 mth	4.7	0.8
3 mth	7.3	(4.2)
6 mth	10.0	(6.5)
12 mth	4.9	(6.1)

(12-Mth) Share Price relative to the FBMKLCI



Source: Bloomberg

- Elsewhere, better business and consumer sentiments should help stimulate demand for quality and value-for-money furniture products in the furniture market. In line with plans to increase its footprint in the domestic home furniture wholesale market, ELK-Desa will continue to work closely with furniture dealers and manufacturers to find the perfect furniture products for Malaysian consumers.

Valuation

- Tagging a 30% discount to Malaysia's average NBFI (such as AEON Credit and RCE Capital) P/B ratio of 1.4x, due to Elk-Desa's smaller market cap and less superior ROE, to FY23e BV, we maintain our fair value of RM1.50/share. We maintain a Buy recommendation on Elk-Desa premised on: i) strong earnings recovery in FY23 on the back of more robust HP receivables, normalisation in impairment charges and potential writebacks, ii) high yielding HP book, iii) steady demand for furniture envisaged, and iv) attractive dividend yields of around 4.0-5.0%.

Table 1: Earnings Summary (RMmn)

FYE Mar (RMmn)	2021	2022	2023F	2024F	2025F
Revenue	143.8	128.9	146.7	163.2	179.4
Gross profit	110.0	99.6	114.2	126.9	138.7
EBITDA	64.5	49.9	65.8	74.0	82.8
EBITDA margin (%)	44.8	38.7	44.9	45.4	46.2
EBIT	61.8	47.2	63.1	71.0	79.6
PBT	46.0	34.9	48.8	51.8	54.8
PAT	35.3	25.8	37.1	39.4	41.7
Core profit	35.3	25.8	37.1	39.4	41.7
Core EPS (sen)	11.6	8.5	12.2	13.0	13.7
PER (x)	11.6	15.9	11.0	10.4	9.8
Gross dividend (sen)	7.3	5.3	6.0	6.5	7.0
Dividend yield (%)	5.4	3.9	4.4	4.8	5.2

Table 2: IQFY23 Results Analysis (RMmn)

FYE 31 Mar (RM mn)	1QFY22	4QFY22	1QFY23	QoQ	YoY	YTD FY22	YTD FY23	YoY
Revenue	31.4	36.0	39.0	8.3	24.2	31.4	39.0	24.2
Other income	0.6	0.8	0.5	(33.1)	(9.2)	0.6	0.5	(9.2)
Cost of inventories sold	(5.8)	(10.0)	(9.3)	(7.4)	60.4	(5.8)	(9.3)	60.4
Depreciation of PPE & ROU assets	(0.7)	(0.7)	(0.7)	3.0	(3.2)	(0.7)	(0.7)	(3.2)
Impairment allowance	(8.3)	(6.6)	5.3	(179.3)	(163.2)	(8.3)	5.3	(163.2)
Other expenses	(7.3)	(10.3)	(9.7)	(5.1)	32.7	(7.3)	(9.7)	32.7
Finance costs	(2.9)	(1.7)	(1.7)	0.7	(42.4)	(2.9)	(1.7)	(42.4)
Profit before taxation	6.9	7.5	23.4	210.4	238.1	6.9	23.4	238.1
Taxation	(1.9)	(2.0)	(5.8)	189.8	197.4	(1.9)	(5.8)	197.4
Net profit	5.0	5.5	17.6	217.8	254.1	5.0	17.6	254.1

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Stock Recommendation Guideline

- BUY** : Total return within the next 12 months exceeds required rate of return by 5%-point.
HOLD : Total return within the next 12 months exceeds required rate of return by between 0-5%-point.
SELL : Total return is lower than the required rate of return.
Not Rated: The company is not under coverage. The report is for information only.

Total Return is defined as expected share price appreciation plus gross dividend over the next 12 months. Gross dividend is excluded from total return if dividend discount model valuation is used to avoid double counting.

Required Rate of Return of 7% is defined as the yield for one-year Malaysian government treasury plus assumed equity risk premium.

ESG Scoring & Guideline

	Environmental	Social	Governance	Average
Scoring	★★★	★★★	★★★	★★★
Remark	The company has made notable efforts in reducing its environmental footprints and emissions by managing natural resources efficiently.	Providing low-interest financing for used car buyers who are generally underserved by mainstream financial institutions. While not obligated to, Elk-Desa took steps to alleviate borrowers' burdens, such as waiving overdue interest during the first year of MCO.	There is reasonable oversight in place. The workforce is well-balanced in terms of gender, ethnicity, and age groups. However, the BOD and upper management level still lacks the diversity in terms of gender. Elk-Desa is committed to upholding its 60% dividend policy.	

- ★★★★★ (≥80%) : Displayed market leading capabilities in integrating ESG factors in all aspects of operations, management and future directions.
 ★★★★★ (60-79%) : Above adequate integration of ESG factors into most aspects of operations, management and future directions.
 ★★★ (40-59%) : Adequate integration of ESG factors into operations, management and future directions.
 ★★ (20-39%) : Have some integration of ESG factors in operations and management but are insufficient.
 ★ (<20%) : Minimal or no integration of ESG factors in operations and management.

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As of Monday, August 22, 2022, the analyst, Li Hsia Wong, who prepared this report, has interest in the following securities covered in this report:
 (a) nil

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