

**3Q FYE MAR 2019 RESULTS REPORT**

**22 February 2019**

Q1 FY19 MAR 2019 RESULTS REPORT

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<b>Name of PLC:</b> ELK-Desa Resources Bhd (ELKD)		<b>PLC Website:</b> <a href="http://www.elk-desa.com.my">www.elk-desa.com.my</a>	
<b>Business Summary:</b> Involved in hire purchase financing for used motor vehicles, insurance agency business and furniture business			
<b>Top Three Shareholders as of 21 February 2019:</b>			
Teoh Hock Chai@ Tew Hock Chai		39.5%	
Dr Yeong Cheong Thye@ Yeong Yue Chai		5.2%	
<b>Market / Sector:</b>	Main / Finance	<b>Stock Code:</b>	5228
		<b>Bloomberg Ticker:</b>	ELK MK
<b>Market Capitalisation:</b>	RM417.12m	<b>Recommendation:</b>	BUY
<b>Target Price:</b>	RM 1.42	<b>Expected Capital Gain:</b>	6.0%
<b>Current Price:</b>	RM1.34	<b>Expected Div Yield:</b>	5.2%
		<b>Expected Total Return:</b>	11.2%
<b>Analyst:</b> Bryan Chan/ Teo Joo Tse   Tel: +603 2163 3200; Email: <a href="mailto:chanb@bcta.com.my">chanb@bcta.com.my</a> / <a href="mailto:jootse@bcta.com.my">jootse@bcta.com.my</a>			

Key Stock Statistics	2017	2018	2019F	2020F
EPS (sen)	7.7	8.7	10.7	11.5
P/E (x)	17.4	15.4	12.5	11.7
EPS ex-EI (sen)	14.5	15.7	16.5	18.2
P/E ex-EI (x)	9.3	8.6	8.1	7.4
Net Dividend/Share (sen)		6.5	7.0	7.0
NTA/Share (RM)	1.44	1.33	1.37	1.42
Book Value/Share (RM)	1.44	1.33	1.37	1.42
Issued Capital (mil shares)	232.2	298.4	298.4	298.4
52-weeks Share Price Range (RM)			1.13-1.35	
Estimated free float				34.7%
Average volume (shares)				146.3k

Per Share Data	2017	2018	2019F	2020F
Year-end 30 Sept				
Book Value/Share (RM)	1.44	1.33	1.37	1.42
Operating CF/Share (sen)	(20.5)	(8.6)	10.6	14.3
EPS (sen)	7.7	8.7	10.7	11.5
Net Dividend/Share (sen)	5.2	6.5	7.0	7.0
P/E (x)	17.4	15.4	12.5	11.7
P/Cash Flow (x)	(6.5)	(15.6)	12.7	9.4
P/Book Value (x)	0.93	1.01	0.98	0.95
Dividend Yield (%)	3.9	4.8	5.2	5.2
Payout Ratio (%)	67.9	74.5	65.6	61.0
ROE (%)	6.9	6.5	7.9	8.2
Net Gearing (%)	3.6	0.7	17.5	29.5

P&L Analysis (RM mil)	2017	2018	2019F	2020F
Revenue	94.5	104.1	118.3	132.6
EBITDA	32.2	38.4	47.8	53.4
Depreciation & amort	(0.6)	(0.6)	(0.7)	(0.7)
Pre-tax Profit	30.6	35.3	42.9	46.0
Net Profit	23.0	25.9	31.9	34.2
EBITDA Margin (%)	34.1	36.9	40.4	40.3
Pre-tax Margin (%)	32.4	33.9	36.3	34.7
Net-Margin (%)	24.3	24.9	27.0	25.8

**1. 3QFY19 Results Highlight**

	3Q FY19 RMm	3Q FY18 RMm	Chg %
Revenue	31.1	25.9	20.2
Impairment Allowance	(4.9)	(4.6)	8.2
Finance cost	(1.2)	(0.6)	93.6
Pre-tax Profit	10.1	9.5	5.6
Net Profit	7.7	7.0	10.1
Core Profit without Impairment	11.5	10.4	10.7
Pre-tax Margin (%)	32.4	36.9	
Net Margin (%)	24.8	27.0	
Core Margin (%)	36.9	40.1	

- 3QFY19 revenue improved 20.2% y-o-y to RM31.1m and net profit increased 10.1% y-o-y to RM7.7m, driven by top-line growth of Hire Purchase (HP) and furniture divisions.
- For HP segment, revenue grew 17.5% y-o-y to RM21.7m as HP receivables grew 23.1% y-o-y to RM456.1m. However, we saw PBT margin decline in the quarter by 6.6ppt y-o-y to 45.2% due mainly to the higher drawdown of block discounting facility to finance the higher hire purchase receivables. This resulted in lower y-o-y PBT growth of 2.6%. Meanwhile, lower income from short term fund, and higher impairment allowance and staff cost also contributed to the lower growth. Despite higher impairment allowance, credit loss charge decreased from 1.18% to 1.05%.

- The furniture segment was the main growth driver during the quarter with a strong top-line growth of 26.7% y-o-y underpinned by domestic sales. PBT surged six-fold y-o-y to RM0.27m due to higher sales, offsetting higher operating expenses.

	3Q FY19 RMm	2Q FY19 RMm	Chg %
Revenue	31.1	31.0	0.4
Impairment Allowance	(4.9)	(3.8)	30.2
Finance cost	(1.2)	(0.9)	31.0
Pre-tax Profit	10.1	11.6	(13.1)
Net Profit	7.7	8.6	(10.5)
Core Profit without Impairment	11.5	11.4	0.6
Pre-tax Margin (%)	32.4	37.4	
Net-Margin (%)	24.8	27.9	
Core Margin (%)	36.9	36.8	

- On q-o-q basis, the Company experienced slower growth by registering revenue growth of 0.4% q-o-q. The higher revenue growth of 4.6% from HP helped offset a 8.0% decline in furniture's top-line. Net profit however declined 10.5% q-o-q due to a 30.2% increase in impairment allowance. Stripping it off, core net profit is moving in tandem with top-line growth by recording growth of 0.6% q-o-q.

	9M FY19 RMm	9M FY18 RMm	Chg %
Revenue	90.9	76.4	19.0
Impairment Allowance	(12.6)	(16.3)	(22.2)
Finance cost	(2.8)	(1.7)	60.6
Pre-tax Profit	32.4	24.5	32.0
Net Profit	24.4	18.0	35.5
Core Profit without Impairment	34.0	30.0	13.4
Pre-tax Margin (%)	35.6	32.1	
Net-Margin (%)	26.8	23.6	
Core Margin (%)	37.3	39.2	

- The group's 9MFY19 net profit of RM24.4m came in within our expectations, making up 76.5% of our full year estimate of RM31.9m.
- Compared to the corresponding period last year, both 9MFY19 revenue and net profit improved by 19.0% and 35.5% y-o-y, respectively. Core net profit registered lower y-o-y growth of 13.4% due to the exclusion of lower impairment allowance impact which declined 22.2% y-o-y. Core margin still marked a 1.9ppt decline to 37.3% due to higher finance costs and other expenses.
- HP segment registered a y-o-y revenue and PBT growth of 16.0% and 29.2%, respectively. The top-line improvement was mainly due to increase in hire purchase portfolio. Meanwhile, its PBT margin improved 5.2ppt to 50.8% mainly attributable to lower impairment allowance, which offset the higher finance costs and higher staff costs. Credit loss charge decreased from 4.41% to 2.85% while total borrowings jumped 125.8% y-o-y on the back of increased hire purchase receivables.
- As for furniture segment, it registered a stellar revenue growth of 25.9% y-o-y attributable to domestic market. The PBT grew four-fold to RM0.71m y-o-y on higher sales despite increasing costs. Gross profit margin saw a marginal decline from 37.0% to 36.6%. Impairment allowance increased 89% y-o-y mainly due to slower payment from furniture dealers. Other expenses also increased by 17% to RM9.3m mainly due to higher operating expenses which is in tandem with the higher sales.
- No dividend was declared for the quarter. However, a single tier interim dividend of 3.5sen was paid on 30 January 2019 for last quarter. We estimate a DPS of 7.0sen for FY19, translating into attractive dividend yield of 5.2%.

## **2. Earnings Outlook**

- ELKDesa is a major independent hire purchase financier for motor vehicles. It is the market leader in the niche segment of entry-level small second-hand cars. The Company has registered healthy organic growth on the back of steady demand for its hire purchase loans. The Company also diversified into furniture business in 2015, but this has yet to contribute significantly. The Company has been conservative in their approach to the business, emphasizing more on quality rather than volume when growing its portfolio. More recently, it has also strategically grown its borrowings at a manageable pace in the past few quarters to further fund growth.
- In near to medium term, we believe the Company will continue to perform, especially given the new coverage area of growth. We believe net receivables will continue to trend higher underpinned by management's direction to expand its HP portfolio. The net gearing has turned from net cash position in FY18 to 0.14x during the quarter to support expansion. We view this positively as the Company has traditionally been conservative on utilising leverage, resulting in low ROEs. For now, we maintain our annual HP disbursements of RM200m and RM240m for FY19-20E. Correspondingly, we assume net HP receivables of RM460m and RM530m for FY19-20E respectively. Our earnings estimates remain unchanged at RM31.9m and RM35.3m, respectively.

## **3. Valuation and Recommendation**

- We continue to like ELKDesa for its sustainable HP growth as well as its attractive dividend yield. Management has delivered a proven track record and the market potential remains large. The stock's financial ratios will likely exhibit improvement in the coming years as more leverage is employed in expanding its business. We maintain our BUY recommendation, with TP of RM1.42 based on unchanged 1x P/BV ratio. As more leverage is employed and profitability ratios continue to improve, we believe the stock has potential to re-rate to 1.1 to 1.2x book value in the mid to longer term.

## Share Price Chart



## **Disclosures/Disclaimer**

Investment ratings:

Buy (generally >10% upside over the next 12 months)

Hold (generally negative 10% downside to positive 10% upside over the next 12 months)

Sell (generally >10% downside over the next 12 months)

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