

RESULTS UPDATE

 FBMKLCI: 1,484.26
 Friday, February 17, 2023
 Sector: Finance

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Elk-Desa Resources Bhd

TP: RM1.80 (+5.9%)

9M Net Profit Doubles to RM40.2mn

Last Traded: RM1.70

HOLD (ESG: ★★★)

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Review

- Elk-Desa reported yet another strong results performance. 9M net profit doubled YoY to RM40.2mn from RM20.2mn a year ago due to solid revenue growth and writeback in impairment allowance. Elk-Desa's results exceeded our expectations, with net profit accounting for 93% of our full-year forecast.
- 9M revenue jumped by 24% YoY due to better contributions from both the hire purchase and furniture segments. Revenue in the furniture segment surged to RM40.4mn from RM29.1mn a year ago. To recap, 9M FY22 was adversely impacted by movement restrictions. Revenue from the hire purchase segment grew by 17% YoY. Hire purchase receivables widened by some 19% YoY to RM560.3mn as of 31 December 2022.
- Overall operating expenses expanded YoY due to higher staff costs and overall operating costs as the hire purchase portfolio also ballooned. Despite that, the group's 9M PBT surged to RM53.4mn vs. RM27.4mn in 9MFY22. Elk-Desa's cost-to-income ratio stood at a manageable level of 29%. The better-than-expected PBT was underpinned by an impairment allowance of RM0.5mn, vs RM15.8mn a year ago.
- Credit loss charge decreased from 2.92% to 0.04%. Management noted that this is due to a significant reduction in the non-performing accounts YTD, which was underpinned by a recovery in activities and an improvement in the repayment trend. The net impaired loans ratio strengthened to 1.58% as of 31 December 2022 from 2.89% as of 31 March 2022.
- Elsewhere, the group's bank borrowings increased by 52%, attributed to the higher drawdown of block discounting facilities to support the increase in hire purchase receivables. Despite that, Elk-Desa's gearing levels remain manageable at 0.43x.

Impact

- Incorporating the better-than-expected 9MFY23 results, we raised Elk-Desa's FY23 net profit forecast to RM51.1mn from RM43.1mn on further downward revision in the credit loss charge to 0% from 2.0%. FY24/25 net profit forecasts are maintained at RM45.0/45.8mn.

Outlook

- We expect the overall demand for used-car hire purchase financing to remain buoyant as economic activities remain healthy. As ELK-Desa focuses on steadily raising the hire purchase receivables portfolio towards pre-pandemic levels, management remains cautious of the ongoing challenging macro environment. While the hire purchase segment was also largely driven by a reversal of impairment allowance, management expects credit charge trends to normalise. We continue to note that potential

Share Information

Bloomberg Code	ELK MK
Stock Code	5228
Listing	Main Market
Share Cap (mn)	303.2
Market Cap (RMmn)	515.44
52-wk Hi/Lo (RM)	1.70/1.20
12-mth Avg Daily Vol ('000 shrs)	92.8
Estimated Free Float (%)	36.5
Beta	0.38
Major Shareholders (%)	
Eng Lee Kredit	- 32.2%
Amity Corp	- 5.1%

Forecast Revision

	FY23	FY24
Forecast Revision (%)	18.5	0.4
Net profit (RMmn)	51.1	45.0
Consensus	39.0	43.0
TA's / Consensus (%)	131.0	104.8
Previous Rating	Buy (downgraded)	
Consensus Target Price (RM)	1.74	

Scorecard (%)

vs TA	93	Above
vs Consensus	103	Above

Financial Indicators

	FY23	FY24
CFPS (sen)	26.8	35.5
Price / CFPS (x)	14.5	21.0
ROA (%)	7.2	5.6
NTA/Share (RM)	1.5	1.6
Price/NTA (x)	1.1	1.1

Share Performance (%)

Price Change	ELK	FBM KLCI
1 mth	6.9	(0.1)
3 mth	27.0	(0.3)
6 mth	35.8	(1.8)
12 mth	35.0	(7.7)

(12-Mth) Share Price relative to the FBMKLCI



Source: Bloomberg

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.

- Elsewhere, better business and consumer sentiments should uphold the solid demand for quality and value-for-money furniture products. 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. In the meantime, efforts are being made to optimise stock and logistics management capabilities, including managing potential supply chain bottlenecks resulting from logistics interruptions, to ensure the timely delivery of customer orders.
- Separately, Elk-Desa announced that the ex and entitlement dates for the Bonus Issue would be on 17 and 20 March 2023. To recap, the company had proposed to undertake a bonus issue of 151.6mn new shares on the basis of 1 new share for every 2 existing Elk-Desa shares held. The proposed bonus issue is not expected to have any material effect on the earnings of the group. However, the group's EPS is estimated to dilute by around 33% due to the increase in the number of shares in issues arising from this proposal.

Valuation

- Tagging a lower 15% (from 20%) discount to Malaysia's average NBFI (such as AEON Credit and RCE Capital) P/B ratio of 1.3x due to Elk-Desa's smaller market cap, we raise the stock's fair value to RM1.80/share from RM1.66/share. Elk-Desa's share price has risen sharply since we initiated coverage on the stock. However, the stock's risk-reward potential has narrowed, given the substantial increase. As such, we downgrade our recommendation on the stock to HOLD from buy.

Table 1: Earnings Summary (RMmn)

FYE Mar (RMmn)	2021	2022	2023F	2024F	2025F
Revenue	143.75	128.89	144.99	161.34	177.25
Gross profit	110.01	99.57	113.12	125.65	137.28
EBITDA	64.47	49.89	80.89	78.20	84.86
EBITDA margin (%)	44.85	38.71	55.79	48.47	47.88
EBIT	61.78	47.19	78.14	75.21	81.68
PBT	46.02	34.89	67.22	59.25	60.33
PAT	35.29	25.77	51.09	45.03	45.85
Core profit	35.29	25.77	51.09	45.03	45.85
Core EPS (sen)	11.64	8.50	16.85	14.85	15.12
PER (x)	14.61	20.00	10.09	11.45	11.24
Gross dividend (sen)	7.25	5.25	9.00	9.00	9.00
Dividend yield (%)	4.26	3.09	5.29	5.29	5.29
ROE (%)	8.14	5.80	11.15	9.42	9.24

Table 2: 3QFY23 Results Analysis (RMmn)

FYE 31 Mar (RM mn)	3QFY22	2QFY23	3QFY23	QoQ	YoY	YTD FY22	YTD FY23	YoY
Revenue	38.2	36.0	40.0	10.9	4.6	92.9	114.9	23.7
Other income	0.5	0.5	0.4	(22.3)	(8.4)	1.6	1.5	(5.5)
Cost of inventories sold	(10.3)	(6.9)	(9.0)	30.1	(12.8)	(19.3)	(25.2)	30.5
Depreciation of PPE & ROU assets	(0.7)	(0.7)	(0.7)	(5.7)	0.0	(2.0)	(2.0)	(0.3)
Impairment allowance	(2.1)	(2.0)	(3.7)	88.5	76.8	(15.8)	(0.5)	(97.1)
Other expenses	(9.6)	(9.6)	(9.7)	0.9	1.2	(22.1)	(29.1)	31.5
Finance costs	(1.9)	(2.1)	(2.5)	18.2	36.1	(7.9)	(6.4)	(19.9)
Profit before taxation	14.1	15.2	14.8	(3.1)	4.4	27.4	53.4	95.0
Taxation	(3.6)	(3.7)	(3.6)	(2.0)	0.7	(7.1)	(13.1)	84.0
Net profit	10.5	11.5	11.1	(3.5)	5.7	20.2	40.2	98.9

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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 Friday, February 17, 2023, 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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