

AEON Credit Service (M)

1H20 Below Expectations

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1H20 core net profit of RM121.9m (-30%) is below expectations from higher-than-expected impairments recognition. Dividends declared however, are within expectation. Steps to capture a larger M40 customer base will continue but new impairment requirements will hinder performance at least through FY20. Maintain UP with a lower TP of RM13.00 (from RM14.75) following our post-results earnings cut.

1H20 missed. 1H20 CNP of RM121.9m missed both our/consensus expectations, making up 37%/34% of respective full-year estimates. The negative deviation comes almost entirely from larger-than-expected impairment losses on financing receivables with the implementation of MFRS 9. An interim dividend of 22.25 sen was declared, which we deem to be within our full-year estimate of 45.0 sen (similar to FY19).

YoY, 1H20 total income came in at RM701.0m (+14%) thanks to higher net interest income (NII, +16%) and other operating income (+7%). Though Net Interest Margin fell slightly to 12.6% (-0.1ppt), total gross financing receivables grew favourably by 22% thanks to higher transactions across key segments (i.e. auto, motor and personal financing). However, core earnings plunged by 30% to RM121.9m on higher Cost-to-Income ratio (CIR) of 39.0% (+2.6ppt), credit charge ratio (CCR) of 6.0% (+1.7ppt) and larger impairment losses (RM248.0m, +63%). This appears to be driven by the spike in receivables arising from the early recognition of impairment required by MFRS 9. **With regards to other key metrics,** non-performing loan (NPL) ratio remains healthy at 2.00% (2Q19: 2.07) but saw higher net credit cost of 4.04% (2Q19: 2.19%).

QoQ, 2Q20 total income grew by 9%, possibly from higher consumer spending for the Hari Raya festivities. However, profit was sequentially lower as better NIM (+0.5ppt) was similarly offset by a rise in CIR and CCR. 2Q20 core earnings hence registered at RM40.9m (-50%).

New rules, new pressures. The group continues to strive for a greater share within the M40 consumer space which is deemed to command higher transaction values. Such initiatives include: (i) transitioning to a B2C2B business model, (ii) promoting its e-wallet platform, and (iii) driving risk-based pricing products and specific product targeting for M40 (i.e. credit cards). Revenue factors aside, it seems like it could be a new normal for the group to be hurt by the new MFRS 9 standards. Since its implementation in 4Q19, the earlier impairment recognition required has eroded earnings and may take the full extent of FY20 for the group to recalibrate its financing strategies.

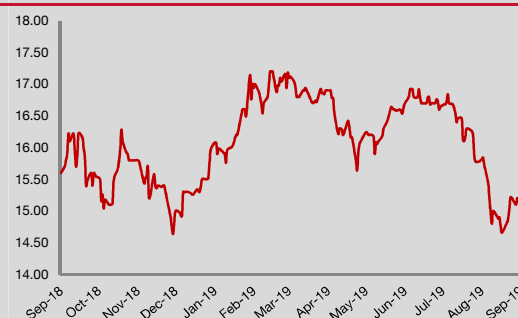
Post-results, we cut our FY20E/FY21E earnings by 15.1%/11.9%, mostly from a higher annualised CCR assumption to impute higher damage from earlier impairments.

Maintain UNDERPERFORM with a lower TP of RM13.00 (from RM14.75). Our TP is based on an unchanged 10.0x FY21E PER (close to the stock's 3-year Fwd. Avg. mean) which became lower following our earnings revision. While the group may continue to grow its market share, we believe it would come at a necessary enlarged cost of credit. Additionally, there could be fundamentally dilutive risks with an estimated balance of 49.1m units of ICULS remaining, which could expand its share base by a further 4%.

UNDERPERFORM ↔

Price : **RM14.96**
Target Price : **RM13.00** ↓

Share Price Performance



KLCI	1,593.00
YTD KLCI chg	-5.8%
YTD stock price chg	-2.2%

Stock Information

Shariah Compliant	No
Bloomberg Ticker	ACSM MK Equity
Market Cap (RM m)	3,753.5
Shares Outstanding	250.9
52-week range (H)	17.36
52-week range (L)	14.60
3-mth avg daily vol	133,155
Free Float	28%
Beta	0.7

Major Shareholders

Aeon Financial Service Co Ltd	62.6%
Kumpulan Wang Simpanan Pekerja	2.0%
Standard Life Aberdeen	1.9%

Summary Earnings Table

FYE Feb (RM'm)	2019A	2020E	2021E
Net Interest Income	937	1,081	1,266
Other Operating Inc.	329	337	348
Total Income	1,267	1,418	1,614
Pretax Profit	472	393	460
Net profit (NP)	355	295	345
Core NP	341	281	331
Consensus NP		361	410
Earnings Revision (%)		-15.1%	-11.9%
EPS (RM)	1.34	1.10	1.30
EPS Growth (%)	(4.1)	(17.5)	17.8
DPS (RM)	0.45	0.45	0.45
BV/Share (RM)	5.87	6.58	7.48
ROE (%)	19.0	15.0	15.9
PER (x)	11.2	13.6	11.5
Price/Book (x)	2.5	2.3	2.0
Dividend Yield (%)	3.0%	3.0%	3.0%

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Risks to our call include: (i) slower-than-expected margin squeeze, (ii) better-than-expected financing receivable growth, and (iii) better-than-expected improvement in asset quality.

Results Highlights

	2Q	1Q	QoQ	2Q	YoY	6M	6M	YoY
FYE Feb (RM'm)	FY20	FY20	Chg	FY19	Chg	FY20	FY19	Chg
Net interest income	278.0	253.4	9.7%	228.6	21.6%	531.4	457.1	16.3%
Other operating income	88.2	81.4	8.3%	90.6	-2.7%	169.5	158.6	6.9%
Total income	366.2	334.8	9.4%	319.2	14.7%	701.0	615.7	13.9%
Operating expenses	(144.6)	(128.8)	12.3%	(116.8)	23.8%	(273.4)	(224.4)	21.9%
Allowance for impairment losses	(154.7)	(93.3)	65.7%	(95.2)	62.4%	(248.0)	(152.3)	62.8%
Pre-tax profit	66.9	112.7	-40.6%	107.2	-37.6%	179.5	239.0	-24.9%
Taxation	(17.7)	(28.1)	-36.8%	(26.6)	-33.3%	(45.8)	(59.1)	-22.5%
Net profit	49.1	84.6	-41.9%	80.6	-39.1%	133.7	179.9	-25.7%
Core Net profit*	40.9	81.0	-49.5%	77.5	-47.1%	121.9	173.1	-29.6%
Core EPS (sen)	16.0	31.7	-49.5%	30.3	-47.2%	47.8	67.8	-29.6%
DPS declared (sen)	22.25	-		22.25		22.25	22.25	
Gross financing receivables	9,597	9,144	5.0%	7,855	22.2%	9,597	7,855	22.2%
Net financing receivables	8,940.6	8,553.0	4.5%	7,253.7	23.3%	8,940.6	7,253.7	23.3%
BV/share (RM)	5.97	6.14	-2.7%	5.46	9.4%	5.97	5.46	9.4%
Est. Annualised Net Interest Margin	13.2%	12.7%		12.7%		12.6%	12.7%	
Cost-to-Income Ratio	39.5%	38.5%		36.6%		39.0%	36.4%	
Effective Tax Rate	26.5%	24.9%		24.8%		25.5%	24.7%	
Est. Annualised Credit Charge Ratio	6.0%	4.7%		4.3%		6.0%	4.3%	
Est. Annualised ROE	10.9%	22.0%		21.3%		16.2%	23.8%	

Note:

* Core net profit is adjusted for distribution on perpetual notes and sukuk

Source: Company, Kenanga Research

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Peer Comparison

Name	Last Price (RM)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Revenue Growth		Core Earnings Growth		PER (x) - Core Earnings			PBV (x)		ROE (%)		Net Div Yld (%)		Target Price (RM)	Rating
					1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	2-Yr. Fwd.	Hist.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.				
NON-BANK FINANCIAL INSTITUTIONS																			
AEON CREDIT SERVICE M BHD	14.96	3,753.5	N	02/2020	12.0%	13.8%	-17.5%	17.8%	11.2	13.6	11.5	2.5	2.3	17.7%	3.0%	13.00	UP		
BURSA MALAYSIA BHD	6.19	5,004.6	Y	12/2019	-4.3%	16.4%	-12.9%	13.1%	22.3	25.5	22.6	5.6	5.5	21.8%	3.7%	6.85	MP		
LPI CAPITAL BHD	15.80	6,294.5	N	12/2019	-19.7%	6.2%	6.6%	1.7%	20.0	18.8	18.5	2.9	2.9	15.5%	4.6%	16.50	MP		
SYARIKAT TAKAFUL MALAYSIA KELUARGA BHD	5.95	4,919.4	Y	12/2019	19.7%	10.0%	31.5%	4.4%	17.6	13.4	12.8	5.0	4.1	33.6%	3.2%	7.15	MP		
Simple Average					1.9%	11.6%	1.9%	9.2%	17.8	17.8	16.4	4.0	3.7	22.1%	3.6%				

Source: Bloomberg, Kenanga Research

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Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
 MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
 UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
 NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
 UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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