

2Q FYE MAR 2018 RESULTS REPORT

17 November 2017

Name of PLC: ELK-Desa Resources Bhd		PLC Website: www.elk-desa.com.my	
Business Summary: Involved in hire purchase financing for used motor vehicles, insurance agency business and furniture business			
Substantial Shareholders: Teoh Hock Chai @ Tew Hock Chai and deemed interest		35.7%	
Amity Corporation Sdn Bhd		5.1%	
Market / Sector:	Main / Finance	Stock Code:	5228
		Bloomberg Ticker:	ELK:MK
Market Capitalisation:	RM357.97 m	Recommendation:	HOLD
Target Price:	RM1.17	Expected Capital Gain:	-
Current Price:	RM1.20	Expected Div Yield:	5%
		Expected Total Return:	5%
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Key Stock Statistics	2016	2017	2018F	2019F
Fully Diluted EPS (sen)	10.76	9.99	7.98	8.48
P/E (x)	11.16	12.01	15.03	14.16
Net Dividend/Share (sen)	6.75	6.75	6.00	6.00
NTA/Share (RM)	1.84	1.45	1.17	1.26
Book Value/Share (RM)	1.84	1.45	1.17	1.26
Issued Capital (mil shares)	174.65	230.30	306.14	306.14
52-weeks Share Price Range (RM)			1.12 - 1.26	
Estimated free float				60%
Average volume (shares)				48,000

Per Share Data	2016	2017	2018F	2019F
Year-end 31 Mar				
Book Value (RM)	1.84	1.45	1.17	1.26
Operating Cash Flow (sen)	5.73	(20.64)	4.76	6.24
EPS (sen)	10.76	9.99	7.98	8.48
Net Dividend/Share (sen)	6.75	6.75	6.00	6.00
Payout Ratio (%)	72.60	67.60	75.14	70.79
P/E (x)	11.16	12.01	15.03	14.16
P/Cash Flow (x)	20.95	(5.81)	25.22	19.23
P/Book Value (x)	0.65	0.83	1.02	0.96
Dividend Yield (%)	5.63	5.63	5.00	5.00
ROE (%)	6.47	7.02	7.06	6.98
Net Gearing (%)	n.c.	n.c.	n.c.	n.c.

n.c. - net cash

P&L Analysis (RM mil)	2016	2017	2018F	2019F
Revenue	64.17	94.49	97.78	102.63
EBITDA	25.97	30.80	32.49	34.49
Depreciation	(0.45)	(0.58)	(0.58)	(0.60)
Net Interest Income	(0.20)	0.34	0.25	0.25
Pre-tax Profit	25.32	30.57	32.16	34.14
Net Profit	18.79	23.00	24.44	25.95
EBITDA Margin (%)	40.47	32.60	33.23	33.60
Pre-tax Margin (%)	39.47	32.35	32.89	33.26
Net-Margin (%)	29.28	24.34	25.00	25.28

1. 2QFY18 Results Highlight

	2QFY18	2QFY17	Chg
	RMm	RMm	%
Revenue	24.96	22.53	10.8
Other Income	0.43	0.58	-25.9
Impairment Allowance	5.08	5.04	0.8
Other Expenses	6.88	6.10	12.8
Pre-tax Profit	8.09	7.27	11.3
Net Profit	5.96	5.41	10.2
Pre-tax Margin (%)	32.4	32.3	0.3
Net Margin (%)	23.9	24.0	-0.4

- The Company's 2QFY18 revenue improved by 10.8% year-on-year ("yoy") to RM24.96m, both hire purchase and furniture segments have registered higher revenue growth. Net profit for the quarter increased by 10.2% yoy to RM5.96m supported by stable margins.
- For HP segment, revenue grew 11% yoy to RM17.67m this quarter, while PBT was also higher by 10% yoy at RM8.09m.
- The furniture segment recorded a 10% yoy growth in revenue to RM7.30m. Though PBT is small at RM4.4k, it is an improvement compared to a loss before tax of RM0.11m during the same period last year.
- For quarter-on-quarter ("qoq") performance, the Company's revenue declined marginally by 2% from the last quarter's revenue of RM25.57m, however net profit rose by 18% qoq from RM5.05m registered in the preceding quarter. Last quarter's net profit was dragged lower by higher-than-expected impairment allowance.

2. 1HFY18 Results Highlight

	1HFY18	1HFY17	Chg
	RMm	RMm	%
Revenue	50.54	44.52	13.5
Other Income	0.65	1.29	-49.6
Impairment Allowance	11.69	9.46	23.6
Other Expenses	13.41	12.18	10.1
Pre-tax Profit	14.99	14.75	1.6
Net Profit	11.01	10.91	0.9
Pre-tax Margin (%)	29.7	33.1	-10.3
Net Margin (%)	21.8	24.5	-11.0

- In 1HFY18, revenue rose 13.5% to RM50.54m from RM44.52m in 1HFY17, but net profit only increased by 0.9% to RM11.01m, attributable to the increase of 23.6% in impairment allowance, thus dragging down the margins from a year ago.
- While the Company’s 1HFY18’s revenue amounting to 51.7% of our full-year forecast of RM97.78m is within our expectations, the net profit so far has only accounted for 45% of our estimate of RM24.44m due to higher-than-expected impairment allowance recorded in 1QFY18. However, the latest 2QFY18’s net profit and margins have improved and are in line with our projections.
- The Company has announced an interim dividend of 3.25sen per share FY18 (FY17: 3.25sen), which will go ex-dividend on 23 Jan 2018 and is payable on 8 Feb 2018.

3. Earnings Outlook

We are maintaining our earnings forecast as we expect continued demand for the Company’s HP products in the coming quarters given that the macroeconomic outlook remains positive. The favourable economic environment bodes well for the overall local motor vehicle industry going forward. The risk to our earnings forecast will be a sharp deterioration in the local economy which can result in lower HP demand and higher impairment allowance.

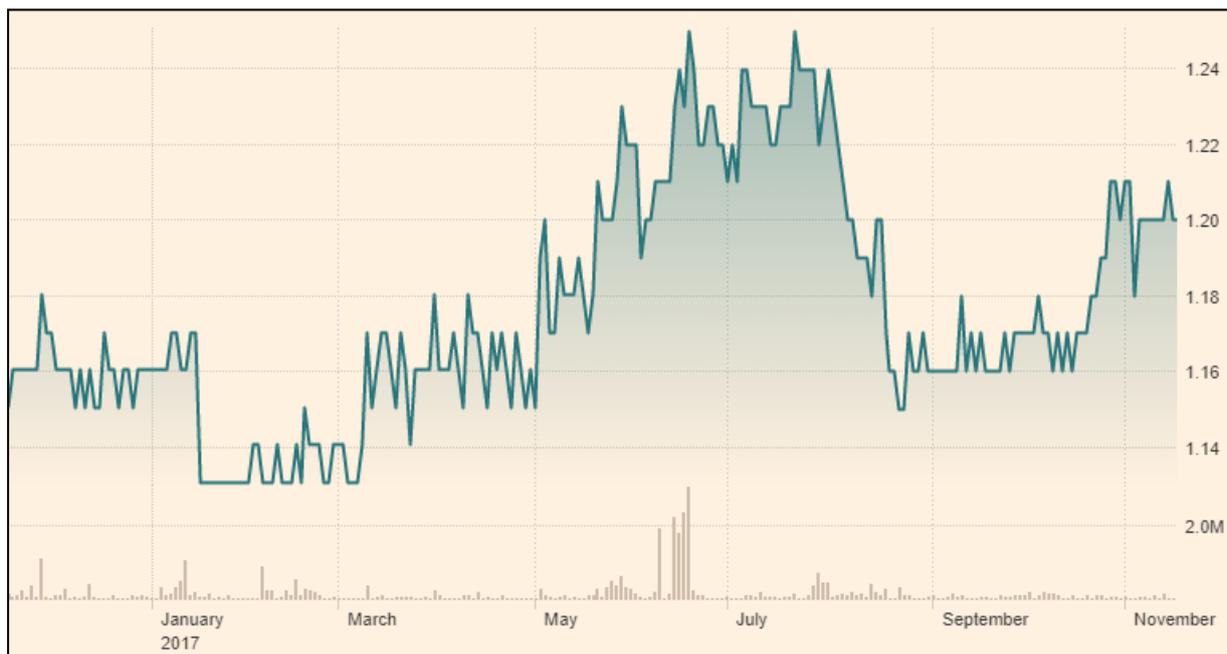
Within the auto financing industry, we believe the Company has significant room for growth given that the business segment that the Company is currently operating in is still relatively small. However, the earnings growth for the Company to a large extent will depend on the how aggressive management wants to grow its HP portfolio.

4. Corporate Update

ELK-Desa Capital Sdn Bhd, a wholly-owned subsidiary of the Company has been granted a Money Lending Licence by Ministry of Urban Wellbeing, Housing and Local Government on 13 November 2017. We are positive about this development as it represents another potential revenue stream for the Company. Small personal financing activities share many similarities with used car financing in term of operations, hence the Company can rely on the existing resources to accommodate the new business. Its current HP customer demographics also fit in well with target customers for money lending. We see both personal financing and auto financing as complementary to each other as the big market player like Aeon Credit has long been marketing both products under its portfolio.

5. Valuation and Recommendation

We are maintaining a HOLD recommendation with an unchanged price target of RM1.17 based on a current year P/BV of 1x. P/E valuations are largely in line with the broad market and we are positive on the Company’s longer term prospects. It is the leading player in its niche hire purchase segment, is able to sustain healthy profit margins and is prudent in terms of managing credit risk. The forecast dividend yield of about 5% will continue to underpin the share price at current levels.

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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