Syarikat Takaful M’sia Keluarga

MFRS 17 Explained

OUTPERFORM ↔

Price :	**RM3.54**
Target Price :	**RM4.25 ↔**

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TAKAFUL hosted a sharing session to explain the nature and implications of MFRS 17 comes 1 January 2023. It presents a more comparable revenue recognition measures based on the tenure and coverage of insurance contracts. However, the reclassification would lead to immediate dents to accounting revenue and book value. That said, these are purely accounting treatments and do not affect the prospects of the group. Maintain OP and TP of RM4.25 based on our hypothetically adjusted FY23E BVPS.

Recognition is more reflective of timing. Effective 1 January 2023, the insurance industry will be adopting MFRS 17 (to replace MFRS 4) pertaining to insurance contracts. In essence, insurers (and takaful operators) will move away from a lumpy Day 1 recognition of revenue and will instead defer its contract revenues throughout the tenure of the contracts in adjustment to future cashflows.

At the same time, the new standard will call for a re-presentation of a company’s books to account for the newly introduced Contractual Service Margin (CSM), which will be the cumulation of all unearned profits into Takaful Contract Liabilities. Unearned profits from contracts issued prior to 2023 will then be reclassified from retained earnings to liabilities, to be amortised over time in accordance with the terms of their respective contracts.

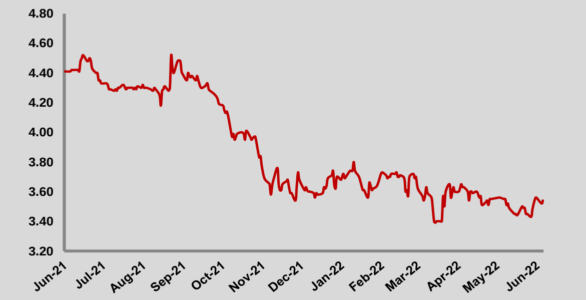
Key impact. Corresponding to the changes in revenue recognition, TAKAFUL anticipates that **net profits would be toned down by 15-20%** based on current year readings. However, this is also to say that the lost sum would be recorded in the subsequent years in line with the term of the contracts’ coverage. Meanwhile, as the previous earnings from these contracts are to be retracted, the extraction from CSM is estimated to **reduce 30-45% of present retained earnings** into Takaful Contract liabilities. Note that there is no equivalent of CSM in the current MFRS 4 standard. Following the above, as equities are reducing at a larger quantum than earnings, **ROE is thus expected to expand, closer towards c.25%**.

Prospects unchanged as the matters above are purely accounting treatments and do not impact the fundamental business of the group. We still anticipate the group to be a sound beneficiary of the recovery of the economy where overall earned premiums should pick up. This should also be uplifted by more aggressive physical sales strategies. That said, a resurgence of claims could be expected as more activities will most likely lead to more incidences and claims. Pre-pandemic, claims incurred ratio could reach upwards to 40-50%, although we anticipate a more moderate increase for the time being at 36% (from 34% during movement control periods).

Post update, we leave no changes to our assumptions for now as the new standards have yet to be implemented.

Maintain OUTPERFORM and TP of RM4.25. Our TP is based on an unchanged 2.2x PBV (implying 0.5SD below mean) on a hypothetically adjusted FY23E BVPS of RM1.94 which captures the factors of -30% to retained earnings and -15% to EPS in FY23E. The stock could have been sold down due to scepticism of the new accounting standards and possible earnings weakness arising from higher claims. We believe this presents a buying opportunity as the current adjustments above illustrate that its merits could have been underpriced. Additionally, valuation levels still linger below pre-Covid levels (3-4x PBV) which could suggest strong re-rating gains should sentiment revert as well.

Share Price Performance



KLCI	1,523.86
YTD KLCI chg	-2.8%
YTD stock price chg	-4.3%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	STMB MK Equity
Market Cap (RM m)	2,964.1
Shares Outstanding	837.3
52-week range (H)	4.52
52-week range (L)	3.39
3-mth avg daily vol	852,372
Free Float	42%
Beta	0.7

Major Shareholders

Lembaga Tabung Haji	28.2%
Employees Provident Fund	10.9%
Kumpulan Wang Persaraan	6.8%

Summary Earnings Table

FY Dec (RM m)	2021A	2022E	2023E
Gross Premium	**2,766**	**2,886**	**3,010**
Net Premium	**2,243**	**2,351**	**2,451**
Other Income	525	540	540
Total Income	**2,768**	**2,891**	**2,991**
Pre-tax Profit	439	452	482
PATAMI	**411**	**345**	**363**
Core PATAMI	**411**	**345**	**363**
Consensus NP		336	389
Earnings Revision		0%	0%
Core EPS (sen)	49.2	41.3	43.5
EPS growth (%)	13.5	-16.0	5.2
DPS (sen)	12.0	14.0	16.0
BVPS (RM)	2.16	2.44	2.71
ROE (%)	24.8	18.0	16.9
PER (x)	7.2	8.6	8.1
PBV (x)	1.6	1.5	1.3
Net Div. Yield (%)	3.4	4.0	4.5

Risks to our call include: (i) lower premium underwritten, (ii) higher-than-expected claims incurred, and (iii) higher-than-expected management expense ratio.

Income Statement

FY Dec (RM m)	2019A	2020A	2021A	2022E	2023E
Operating revenue	**3,125**	**2,957**	**3,179**	**2,863**	**2,963**
Takaful op. income	1,094	979	1,047	1,130	1,220
Gross earned premium	2,749	2,514	2,766	2,886	3,010
Net earned premium	**2,354**	**2,073**	**2,243**	**2,351**	**2,451**
Other income	483	510	525	540	540
Net benefits & claims	-988	-889	(949)	(1,027)	(1,076)
Other operating exp	-724	-602	(659)	(693)	(692)
Pre-tax profit	418	427	439	452	482
Zakat	-1	-1	(1)	(1)	(1)
Tax expense	-50	-62	(25)	(103)	(116)
PATAMI	**365**	**362**	**411**	**345**	**363**
Core PATAMI	**365**	**362**	**411**	**345**	**363**

Balance Sheet

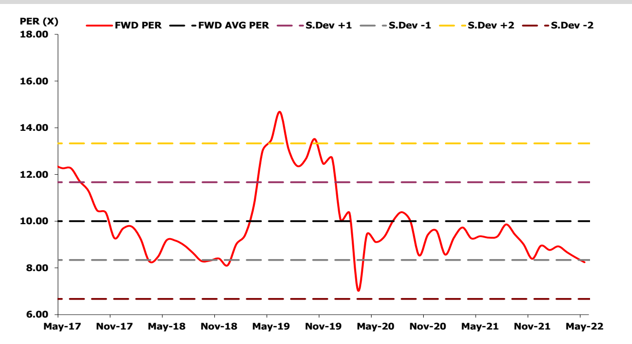
FY Dec (RM m)	2019A	2020A	2021A	2022E	2023E
Net fixed assets	223	225	227	136	96
Other investments	5,806	9,346	9,504	9,504	9,504
Retakaful assets	756	978	1,156	1,546	1,592
Receivables	2,834	303	336	305	318
Cash equivalents	603	713	847	1,919	2,193
Other assets	123	229	638	192	192
Total assets	**10,346**	**11,793**	**12,709**	**13,603**	**13,894**
Takaful liabilities	8,258	9,224	9,786	9,786	9,786
Total payables	490	671	756	1,423	1,484
Other liabilities	343	356	324	324	324
Total liabilities	**9,092**	**10,251**	**10,866**	**11,533**	**11,594**
Share capital	197	212	231	231	231
Reserves	1,026	1,298	1,578	1,807	2,036
Shareholders' eq.	**1,223**	**1,509**	**1,809**	**2,037**	**2,267**
Minority interest	32	32	33	33	33
Total liability & eq.	**10,346**	**11,793**	**12,708**	**13,603**	**13,894**

Financial Data & Ratios

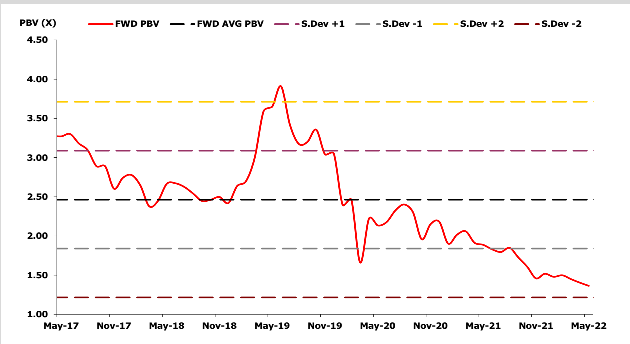
FY Dec (RM m)	2019A	2020A	2021A	2022E	2023E
Growth					
Operating revenue	18.4%	-5.4%	7.5%	-9.9%	3.5%
Takaful op. Income	21.1%	-10.5%	6.9%	8.0%	7.9%
Gross earned premium	19.8%	-8.5%	10.0%	4.3%	4.3%
Net earned premium	21.3%	-12.0%	8.2%	4.8%	4.2%
Other income	47.7%	5.6%	3.0%	2.9%	0.0%
Pre-tax Profit	24.0%	2.2%	2.8%	2.9%	6.7%
Core PATAMI	31.1%	-0.7%	13.5%	-16.0%	5.2%
EPS	24.8%	-0.9%	12.4%	-15.9%	5.2%
Operating Metrics					
Reinsurance ratio	14%	18%	19%	19%	19%
Retention ratio	86%	82%	81%	81%	81%
Claims incurred ratio	36%	35%	34%	36%	36%
Commission expenses	8%	8%	8%	7%	7%
Mgmt expense ratio	16%	16%	19%	16%	16%
Combined ratio	59%	59%	61%	59%	59%
Effective tax	12%	15%	6%	20%	24%
ROA	3.8%	3.3%	3.4%	2.6%	2.6%
ROE	33.1%	26.5%	24.8%	18.0%	16.9%
Valuation					
Core EPS (RM)	0.44	0.44	0.49	0.41	0.43
PER (x)	8.0	8.0	7.1	8.5	8.1
Div. Yld. (%)	5.7%	3.4%	3.4%	4.0%	4.6%
BVPS (RM)	1.48	1.82	2.16	2.44	2.71
PBV (x)	2.4	1.9	1.6	1.4	1.3

Source: Kenanga Research

Fwd PER Band



Fwd PBV Band



Source: Bloomberg, Kenanga Research

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	14.80	3,778.6	N	02/2023	10.0%	7.0%	18.2%	15.1%	10.6	9.0	7.8	1.9	1.7	19.9%	3.4%	16.45	OP
CTOS DIGITAL BHD	6.66	5,389.9	Y	12/2022	-11.7%	-2.6%	-22.8%	3.6%	15.2	19.6	19.0	6.6	6.4	33.1%	4.7%	7.05	MP
BURSA MALAYSIA BHD	1.41	3,257.1	Y	12/2022	24.5%	15.2%	31.8%	16.7%	54.8	41.6	35.7	11.0	5.7	18.1%	1.3%	2.00	OP
LPI CAPITAL BERHAD	13.74	5,473.8	N	12/2022	-3.7%	1.7%	-25.5%	27.4%	15.9	21.3	16.7	2.6	2.5	11.9%	4.4%	14.10	MP
SYARIKAT TAKAFUL MALAYSIA KELUARGA BHD	3.54	2,964.1	Y	12/2022	4.3%	4.3%	-16.0%	5.2%	7.2	8.6	8.1	1.6	1.5	18.0%	4.0%	4.25	OP
Simple Average					4.7%	5.1%	-2.9%	13.6%	20.7	20.0	17.5	4.7	3.6	20.2%	3.5%		

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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