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MFRS 17 weighs on Syarikat Takaful Malaysia

BY **ADELINE PAUL RAJ**

Despite its strong fundamentals and numerous "buy" calls by analysts, Syarikat Takaful Malaysia Keluarga Bhd's (STMK) share price has been listless in the last few months, trading at close to two-year lows.

The takaful operator's stock, which hit an over five-year low of RM3.15 on March 23, 2020, shortly after the first Covid-19 nationwide lockdown, went on to recover quickly, moving up as much as 60.3% to peak at RM5.05 on Aug 28 that same year. However, over the last six months, the company's stock has gone back into RM3-plus territory, sinking to as low as RM3.39 on March 17.

Last Wednesday, it closed at RM3.56, which gives STMK a market capitalisation of about RM3 billion. In contrast, most other financial institutions are currently trading at around one-year highs or more. So, what's holding back STMK?

The problem, according to one analyst, is investor uncertainty over how a new accounting standard for insurance contracts, MFRS 17, will impact STMK. MFRS 17 will be applied next year across the insurance industry in Malaysia.

"Fundamentals-wise, there isn't any problem with the stock. But with MFRS 17 kicking in next year, its impact — on Day 1 retained earnings, for example — may not be well understood by investors. I think that's what investors are afraid of and, hence, there is some sort of overhang on the stock," Eddy Do, an analyst at RHB Research, tells *The Edge*.

"While it affects all insurers, for takaful operators, I think, the other concern is on the capital adequacy ratio and the way it is calculated, which might put takaful operators at risk of a capital call. But the guidelines on these are not clear yet," he says.

MFRS 17, which is the Malaysian equivalent of International Financial Reporting Standard (IFRS) 17, is meant to increase consistency, comparability and transparency in financial reporting across the insurance industry. The implications for an insurer's financials and operations will differ from company to company.

MOHD IZWAN MOHD NAZAM/THE EDGE

STMK reported a net profit of RM411.42 million in FY2021, which was 13.5% higher than a year earlier and came in above analysts' expectations

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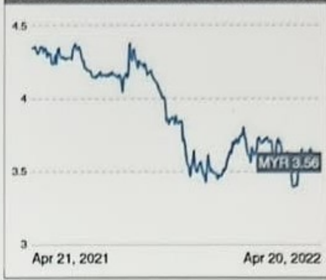

Valuation score*	2.30
Fundamental score**	1.25
TTM P/E (x)	7.23
TTM PEG (x)	0.53
P/NAV (x)	1.64
TTM Dividend yield (%)	3.37
Market capitalisation (mil)	2,974.82
Shares outstanding (ex-treasury) mil	835.62
Beta	0.76
12-month price range	3.39-4.40

*Valuation score - Composite measure of historical return & valuation
**Fundamental score - Composite measure of balance sheet strength & profitability
Note: A score of 3.0 is the best to have and 0.0 is the worst to have

Fitch Ratings, in a takaful report in February, made note of the MFRS 17 factor on the industry.

"The takaful industry continues to face uncertainty over the interpretation and application of IFRS 17 as the January 2023 implementation deadline draws nearer. Still, the selection of measurement models and treatment of various funds will be resolved," it said.

Well-liked despite uncertainties

Nevertheless, analysts believe the concerns about MFRS 17's impact on STMK may well be overblown. The stock is well-liked by analysts — Bloomberg data shows that seven have a "buy" call on it, with target prices ranging from RM4.40 to RM7, while one has a "hold" call.

"STMK is currently trading at a price-to-book value (PBV) of 1.46 times based on our FY2022 earnings forecast, against ROE (return on equity) of 16.4%," says RHB's Do, who deems the valuation attractive. He has a "buy" call and a target price of RM4.90 on STMK.

Analysts note that other issues affecting the company — such as an expected rise in claims now that more people are seeking medical treatment after coming out of Covid-19 lockdowns, as well as higher taxation as a result of Cukai Makmur (Prosperity and Windfall Tax), which will dampen this year's earnings — have already been priced into the stock.

AmInvestment Bank Research, which also has a "buy" call, notes that in the first year of adoption of MFRS 17, the guided impact is for a 15% to 20% decline in STMK's profit after tax (PAT) for the year ending Dec 31, 2023 (FY2023), compared with FY2022.

"Meanwhile, on the Day 1 retrospective adjustment, [MFRS 17] is likely to lower FY2023 opening retained earnings by 30%-45%. This will be higher than the earlier guided 20%-30% decline as a result of the additional contributions from new policies underwritten by the group in the last two years. Despite the impact on PAT and shareholders, we project ROE to rise at a faster rate, by 22% in FY2023 from 20.4% in FY2022, while the dividend payout ratio increases to 26.2% from 25.8%," it says in an April 8 report.

"We continue to peg the stock to an unchanged FY2023 PBV of 2.4 times, supported by an ROE of 22%, which has factored in the impact of [MFRS] 17," it adds. It pegs the stock's fair value at RM4.15.

STMK reported a net profit of RM411.42 million in FY2021, which was 13.5% higher than a year earlier and came in above analysts' expectations. It declared a 12 sen dividend, the same amount as in the previous year.

On its outlook, Kenanga Research notes that the resumption of face-to-face activities should drive sales of STMK's products, as seen in 4QFY2021.

"Meanwhile, its continued digital efforts should allow STMK to reach underserved segments while simplifying its go-to-market strategy. We understand that, currently, management is in discussions with banks for additional bancassurance partnerships (on top of its existing 17 partnerships). Of its four key partners — Affin, RHB, BIMB and Bank Rakyat — Affin and Bank Rakyat's agreements are due to expire in 2023, but STMK expects the partnerships to be extended due to high switching costs," it says in a report following STMK's recent results.