

## Results Note

## Hai-O Ent

HAIO MK  
RM3.26

SELL (downgrade)

Target Price: RM2.71 (↓)



## Price Performance

	1M	3M	12M
Absolute	+0.9%	-11.7%	+37.5%
Rel to KLCI	-2.6%	-20.2%	+13.7%

## Stock Data

Issued shares (m)	202.2
Mkt cap (RMm)	659.1
Avg daily vol - 6mth (m)	0.6
52-wk range (RM)	2.27 – 4.93
Est free float	66.4%
NTA per share (RM) (end-Jul 10)	1.05
P/NTA (x)	3.11
Net cash/debt (RMm) (end-Jul 10)	34.6
ROE (FY11F)	29.1%
Derivatives	Nil

## Key Shareholders

Tan Kai Hee	9.6%
Akintan Sdn Bhd	7.2%

## Earnings &amp; Valuation Revisions

	11E	12E	13E
Prev EPS (sen)	32.2	36.8	41.8
Curr EPS (sen)	25.4	27.9	31.8
Chg (%)	-21.3%	-24.1%	-24.1%
Prev target price (RM)		3.53	
Curr target price (RM)		2.71	

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## Hit sharply by consolidation of MLM division

## 1QFY04/11 net profit grossly below expectations

Hai-O reported 1QFY04/11 revenue of RM54.8m (-63.1% yoy), dragged down by revenue declines of: 1) -52.6% yoy in the wholesale division, and; 2) -73% yoy in the MLM division. The sharp drop in revenue was attributed to the implementation of stricter guidelines on new member recruitment, which resulted in fewer new monthly member additions. Sales of higher margin products, the weakening US\$ against RM, and cost savings from operating efficiencies boosted EBIT margin +2-ppt to 19.7% (1QFY04/10: 17.7%). Nevertheless, 1QFY04/11 net profit slid -57.7% yoy to RM7.8m. Results are below expectations, accounting for a meagre 12% and 9% of our and consensus expectations.

## Weaker earnings on consolidation of MLM division and high base effect

On a sequential basis, 1QFY11 topline slid by -44.6%. While the consolidation activities in the MLM division are partly to blame (revenue from the MLM division declined -51.4% qoq), we also note that 4QFY04/10 was a seasonally stronger quarter as it incorporated higher sales from the Chinese New Year period. This resulted in retail and wholesale revenue declines of -40% qoq and -43.2% qoq, respectively. Sales of higher margin products, particularly in the wholesale division, lifted overall EBIT margin by +3.7ppt. Nevertheless, 1QFY04/11 net profit slid -45.3% qoq, further exacerbated by a higher effective tax rate. The exceptionally low effective tax rate of 4.9% in 4QFY04/10 was due to overprovision of tax expenses in the preceding quarters.

## Longer adjustment period for new guidelines

MLM members and leaders are still adjusting to the more stringent guidelines imposed by Hai-O. However, the adjustment period is longer than we had initially expected. Thus, we are downgrading our FY11-13 net earnings forecast by -20-24%, after accounting for: 1) weaker sales in the wholesale division; and 2) flat distributor growth rate yoy for FY11.

## Downgrade to SELL, TP lowered to RM2.71

Our target price is lowered from RM3.53 to RM2.71, pegged to an unchanged PE target of 10x on CY11 EPS. Hai-O's key attraction for now is its net dividend yields of 4-6%, premised on a minimum dividend payout policy of 50%, although risk to yields are high in view of any further negative earnings surprises. Thus, we downgrade our recommendation to a SELL. Re-rating catalysts include: 1) pick-up in new monthly member additions, both in Indonesia and Malaysia, and; 2) increased distributor activity rate.

## Earnings and valuation summary

FYE 30 April	2009	2010	2011F	2012F	2013F
Revenue (RMm)	435.2	511.1	431.2	473.1	506.1
EBITDA (RMm)	77.0	96.8	75.1	82.2	92.8
Pretax profit (RMm)	75.9	95.9	69.8	76.9	87.4
Net profit (RMm)	52.3	70.9	51.4	56.6	64.4
EPS (sen)	25.8	35.0	25.4	27.9	31.8
EPS growth (%)	7.7	35.6	-27.5	10.1	13.7
PER (x)	12.6	9.3	12.9	11.7	10.3
Core net profit (RMm)	52.3	70.9	51.4	56.6	64.4
Core EPS (sen)	25.8	35.0	25.4	27.9	31.8
Core PER (x)	12.6	9.3	12.9	11.7	10.3
Net DPS (sen)	13.1	19.6	15.2	16.8	19.1
Net Dividend Yield (%)	4.0	6.0	4.7	5.1	5.8
EV/EBITDA (x)	7.8	5.8	7.0	6.1	5.1
Consensus profit (RMm)			84.9	88.3	-
Affin/Consensus (x)			0.6	0.6	-

**Fig 1: Quarterly results comparison**

FYE April (RMm)	1QFY10	4QFY10	1QFY11	QoQ % chg	YoY % chg	Comment
Revenue	148.6	98.8	54.8	(44.6)	(63.1)	Attributed to revenue declines of: 1) -51.4% qoq in the MLM division; 2) -43.2% qoq in the wholesale division, and; 3) -40% qoq in the retail division
Op costs	(174.9)	(114.6)	(65.6)	(42.8)	(62.5)	
Exceptional gain/losses	0.0	0.0	0.0	nm	nm	
EBIT	26.3	15.8	10.8	(31.5)	(58.9)	
EBIT margin (%)	17.7	16.0	19.7	nm	nm	Supported by sales of higher margin products, lower RM/US\$ exchange rate and cost savings from operating efficiency
Int expense	(0.2)	(0.2)	(0.2)	12.6	0.0	
Int and other inc	0.2	0.2	0.2	2.8	7.6	
Associates	0.0	0.0	0.0	nm	nm	
<b>Pretax</b>	<b>26.3</b>	<b>15.8</b>	<b>10.8</b>	<b>(31.6)</b>	<b>(59.0)</b>	
Tax	(7.8)	(0.8)	(2.9)	277.1	(62.5)	
Tax rate (%)	29.6	4.9	27.0	nm	nm	
MI	(0.1)	(0.7)	(0.1)	(90.6)	nm	
<b>Net profit</b>	<b>18.5</b>	<b>14.3</b>	<b>7.8</b>	<b>(45.3)</b>	<b>(57.7)</b>	Accounts for 12% and 9% of our and consensus estimates, respectively
EPS (sen)	9.1	7.1	3.9	(45.3)	(57.7)	
<b>Core net profit</b>	<b>18.5</b>	<b>14.3</b>	<b>7.8</b>	<b>(45.3)</b>	<b>(57.7)</b>	

Source: Affin, Company

**Fig 2: Segmental revenue breakdown**

FY April (RMm)	1QFY09	2QFY09	3QFY09	4QFY09	1QFY10	2QFY10	3QFY10	4QFY10	1QFY11	QoQ % chg	YoY % chg
Wholesale	44.7	32.8	54.3	48.0	46.3	70.6	72.5	38.6	21.9	(43.2)	(52.6)
MLM	91.5	65.9	78.9	112.5	130.3	108.9	106.2	72.6	35.2	(51.4)	(73.0)
Retail	8.0	10.0	11.8	9.4	7.9	10.8	9.6	13.6	8.2	(40.0)	3.2
Manufacturing	1.2	1.1	1.3	1.7	1.2	1.2	1.4	1.4	2.0	40.8	64.4
Others	(32.5)	(22.6)	(44.2)	(38.8)	(37.1)	(59.1)	(58.4)	(27.4)	(12.6)	(54.1)	(66.2)
<b>Total</b>	<b>112.9</b>	<b>87.3</b>	<b>102.1</b>	<b>132.8</b>	<b>148.6</b>	<b>132.4</b>	<b>131.3</b>	<b>98.8</b>	<b>54.8</b>	<b>(44.6)</b>	<b>(63.1)</b>
Qoq (%)	(15.5)	(22.7)	17.0	30.1	11.8	(10.9)	(0.8)	(24.7)	(44.6)		
Yoy (%)	90.5	8.4	1.6	(0.5)	31.6	51.6	28.5	(25.6)	(63.1)		
<b>Contribution (%)</b>											
Wholesale	39.6	37.6	53.2	36.2	31.1	53.3	55.2	39.1	40.1		
MLM	81.1	75.5	77.3	84.7	87.7	82.3	80.9	73.4	64.4		
Retail	7.1	11.5	11.5	7.1	5.3	8.1	7.3	13.8	14.9		
Manufacturing	1.1	1.3	1.3	1.3	0.8	0.9	1.1	1.4	3.6		
Others	(28.8)	(25.9)	(43.3)	(29.2)	(25.0)	(44.6)	(44.5)	(27.7)	(22.9)		
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>		

Source: Affin, Company

**Fig 3: Segmental EBIT breakdown**

FY April (RMm)	1QFY09	2QFY09	3QFY09	4QFY09	1QFY10	2QFY10	3QFY10	4QFY10	1QFY11	QoQ	YoY
										% chg	% chg
Wholesale	3.6	3.9	2.9	(0.4)	4.1	5.5	3.0	(0.7)	2.6	(448.1)	(37.3)
MLM	14.2	10.1	13.8	20.8	21.2	21.8	20.5	11.8	6.4	(46.1)	(70.0)
Retailing	0.3	0.8	1.1	0.7	0.3	1.3	0.6	1.9	0.3	(83.7)	0.7
Manufacturing	0.3	0.1	0.2	0.3	0.2	0.2	0.0	0.2	0.2	7.6	15.3
Others	(0.1)	1.0	0.6	0.5	0.3	1.4	1.6	1.4	1.1	(24.1)	310.2
Elimination	0.3	(0.3)	(0.0)	1.2	0.2	(0.4)	(0.1)	1.3	0.8	(39.0)	285.4
<b>Total</b>	<b>18.6</b>	<b>15.5</b>	<b>18.6</b>	<b>23.4</b>	<b>26.3</b>	<b>28.7</b>	<b>25.2</b>	<b>15.8</b>	<b>10.8</b>	<b>(31.5)</b>	<b>(58.9)</b>
<b>Contribution (%)</b>											
Wholesale	19.4%	25.1%	15.7%	(1.7%)	15.7%	19.0%	11.7%	(4.7%)	24.0%		
MLM	76.5%	65.2%	74.1%	89.0%	80.6%	75.9%	81.2%	74.9%	58.9%		
Retailing	1.5%	5.1%	6.0%	2.8%	1.2%	4.4%	2.5%	12.0%	2.8%		
Manufacturing	1.4%	0.5%	1.0%	1.4%	0.8%	0.8%	0.2%	1.4%	2.2%		
Others	(0.7%)	6.2%	3.2%	2.0%	1.0%	5.0%	6.5%	9.1%	10.1%		
Elimination	1.7%	(2.2%)	(0.0%)	5.0%	0.8%	(1.4%)	(0.6%)	8.2%	7.3%		
<b>Margin (%)</b>											
Wholesale	8.1%	11.9%	5.4%	(0.8%)	8.9%	7.7%	4.1%	(1.9%)	11.8%		
MLM	15.6%	15.4%	17.5%	18.5%	16.3%	20.0%	19.3%	16.3%	18.0%		
Retailing	3.5%	8.0%	9.5%	7.0%	3.9%	11.7%	6.6%	13.9%	3.8%		
Manufacturing	22.2%	6.9%	13.6%	20.2%	17.5%	20.1%	2.7%	16.0%	12.3%		
Others	(7.7%)	43.4%	19.4%	16.3%	9.8%	40.8%	55.3%	33.2%	34.5%		
Elimination	(0.9%)	1.4%	0.0%	(2.8%)	(0.5%)	0.7%	0.2%	(4.1%)	(5.0%)		

Source: Affin, Company

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#### Equity Rating Structure and Definitions

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<b>BUY</b>	Total return is expected to exceed +15% over a 12-month period
<b>TRADING BUY (TR BUY)</b>	Total return is expected to exceed +15% over a 3-month period due to short-term positive development, but fundamentals are not strong enough to warrant a Buy call. This is to cater to investors who are willing to take on higher risks
<b>ADD</b>	Total return is expected to be between 0% to +15% over a 12-month period
<b>REDUCE</b>	Total return is expected to be between 0% to -15% over a 12-month period
<b>TRADING SELL (TR SELL)</b>	Total return is expected to exceed -15% over a 3-month period due to short-term negative development, but fundamentals are strong enough to avoid a Sell call. This is to cater to investors who are willing to take on higher risks
<b>SELL</b>	Total return is expected to be below -15% over a 12-month period
<b>NOT RATED</b>	Affin Investment Bank does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation
<b>OVERWEIGHT</b>	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
<b>NEUTRAL</b>	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
<b>UNDERWEIGHT</b>	Industry, as defined by the analyst's coverage universe is expected to under-perform the KLCI benchmark over the next 12 months

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