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BUY

Target Price RM5.04
Previous Price RM5.04
Current Price RM4.42

CONSUMER (RETAIL)

Hai-O is involved in wholesaling, retailing, multi-level marketing and pharmaceuticals, and also operates modern Chinese medicinal clinics.

Stock Statistics

Bloomberg Ticker	HAIO MK
Share Capital (m)	202.7
Market Cap (RMm)	895.9
52 week H L Price (RM)	4.93 1.45
3mth Avg Vol ('000)	691.1
YTD Returns	25.2
Beta (x)	0.75

Major Shareholders (%)

Tan Kai Hee	9.59
Akintan SB	7.15
Excellent communication	5.11

Share Performance (%)

Month	Absolute	Relative
1m	2.1	-2.0
3m	25.2	20.2
6m	75.5	49.0
12m	220.1	104.9

6-month Share Price Performance



Company Update

Hai-O

Back to a Buy

We believe Hai-O is on track to achieve our FY10 profit forecast of RM72.6m, driven mainly by (i) better y-o-y MLM sales on a higher membership base, (ii) better y-o-y and q-o-q retail sales as we expect sales during the Chinese New Year, which arrived later this year, to be captured in 4Q. Management revealed that there are some developments in the technology division and that all is progressing as planned, although there are no further details. Hai-O's share price has retraced by some 5% since our downgrade on 22 March. As the stock offers a more than 10% upside at the current price, we are upgrading it to BUY at an unchanged TP of RM5.04.

MLM division to fare better. In the 9MFY10 quarterly results, the MLM division reported 9MFY10 and 3QFY10 y-o-y sales growth of 34.6% and 46.1% respectively. We believe this division will give a good showing in the upcoming 4QFY10 results given the higher y-o-y number of members to date. Compared to the same period last year, Hai-O recruited 30,000 more members. We see a y-o-y sales growth of some 20% in 4QFY10.

Retail sales to fare better q-o-q. Hai-O's 3QFY10 and 9MFY10 retail sales contracted by 19.3% and 5.3% y-o-y respectively. While this may be cause for concern, the contraction was mainly due to seasonal factors as the Chinese Lunar New Year took place late in 4Q. We believe the shortfall in 3Q sales would be made up for in 4Q and as such, we see better retail sales in the last fiscal quarter. Management said Chinese New Year sales were encouraging, with FY10 10-month same-store-sales growth coming in at 3.5% y-o-y.

Technology division progressing as planned. With regard to its newly formed thermal transfer business, despite the lack of details, management revealed that there had been some developments and that all is progressing as planned. It has also guided that the current investment cost is about RM3m and that no additional cost is needed as yet. Based on this piece of information, we believe the break even period for this business could be shorter than management's break even target of 2 years. Should this business make good progress, apart from the potentially high ROI as previously stated, this division together with the retail division should provide a strong earnings support during an economic downturn, which may render the group more resilient than other MLM players.

Upgrade to BUY. Hai-O's share price has rallied strongly since early this year, driven by its uninterrupted stream of good quarterly results. While we are maintaining our FY10 and FY11 net profit forecasts, we **upgrade Hai-O to a BUY** at an unchanged TP of RM5.04 (based on 12x FY11 EPS) given there is a price upside of more than 10% after its shares have retraced by some 5% since our downgrade on 22 March.

FYE Apr (RMm)	FY08	FY09	FY10f	FY11f	FY12f
Revenue	373.8	435.2	569.6	679.0	786.1
Net Profit	48.5	52.3	72.6	85.2	101.4
% chg y-o-y	127.0	7.7	38.8	17.3	19.1
Consensus	-	-	76.2	93.2	105.5
EPS (sen)	57.5	25.8	35.8	42.0	50.0
DPS (sen)	16.7	17.5	24.0	28.0	34.0
Dividend yield (%)	3.8	4.0	5.4	6.3	7.7
ROE (%)	34.5	31.6	33.7	30.7	29.0
ROA (%)	23.8	21.1	25.8	24.5	24.3
PER (x)	18.5	17.1	12.3	10.5	8.8
BV/share (RM)	0.69	0.82	1.06	1.37	1.73
P/BV (x)	6.4	5.4	4.2	3.2	2.6
EV/ EBITDA (x)	11.9	11.2	7.8	6.6	5.4

KEY HIGHLIGHTS

MLM division to perform better y-o-y. In its 9MFY10 quarterly results, the MLM division recorded a 9MFY10 and 3QFY10 y-o-y sales growth of 34.6% and 46.1% respectively. We believe Hai-O's MLM division will show stronger numbers in the upcoming 4QFY10 results given the bigger membership base YTD. Compared to the same period last year, the group recruited 30,000 more members, of whom 20% is active. We expect the group to reap a y-o-y sales growth of some 20% in 4QFY10.

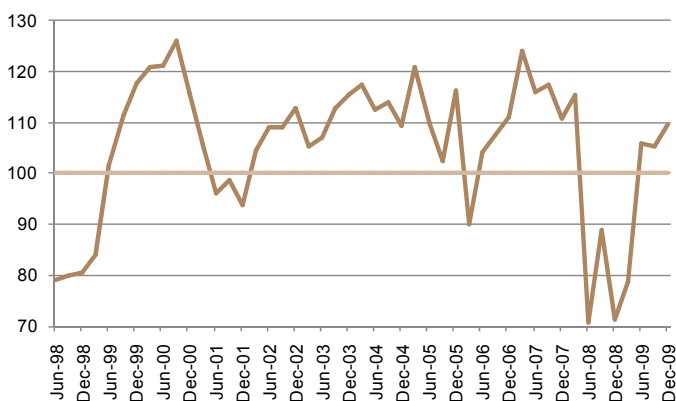
Minimal contribution from Indonesia in the near term. The group launches its MLM business in Indonesia this month. While there is ample room to grow in the long term given the republic's huge population and cultural similarities with Malaysia, we only expect a maiden revenue contribution of 1% of total FY10 sales after factoring in the weaker spending power in that country. Hai-O is targeting to break even within two years, with a target membership base of 5k-10k after the 1st year in operation.

Retail sales to be better q-o-q. In 3QFY10 and 9MFY10, retail sales contracted by 19.3% and 5.3% y-o-y respectively. While this may be cause for concern, the contraction in sales was mainly due to seasonal factors, since the Chinese Lunar New Year fell late in 4Q. We believe the sales shortfall in 3Q would be captured in 4Q and hence we expect to see stronger retail sales in the last financial quarter. Our view is indeed well-founded as Hai-O's retail FY10 10-month same-store-sales growth came in at 3.5% driven by strong Chinese New Year sales. The group currently has 65 outlets, including 10 franchise stores, with a cumulative floor space of 68,000 sq ft in Malaysia. This includes the 5 new openings in 3Q, in line with Hai-O's retail outlet expansion target of 3-5 outlets/year.

Technology division progressing well. While there are few details on its newly formed thermal transfer business, management said there had been some developments and that all activities are progressing as planned. Management said the current investment cost is about RM3m and no additional cost is needed as yet. As such, we believe the break-even period for this business could be shorter than management's targeted 2 years. Should this business make good progress, apart from the potentially high ROI as stated earlier, this division together with the retail division should provide solid earnings support during economic downturns, thus making the group more resilient than other MLM players.

Strengthening consumer sentiment and spending. Hai-O's earnings have grown by 50-fold since 2003, chalking up a bottom line CAGR of 118.2% from 2003 to 2008. Due to the economic crisis last year, which dampened consumer spending, the group only managed to report a 7.7% y-o-y earnings growth, which pulled down its overall 6-year CAGR to 94%. In tandem with recovering consumer sentiment and spending as well as a stronger RM against USD, Hai-O's earnings growth should continue to be encouraging albeit at a slower pace given the higher earnings base. We are forecasting for FY10 net profit to hit RM72.6m from RM52.3m in FY09, representing a robust 38% y-o-y growth.

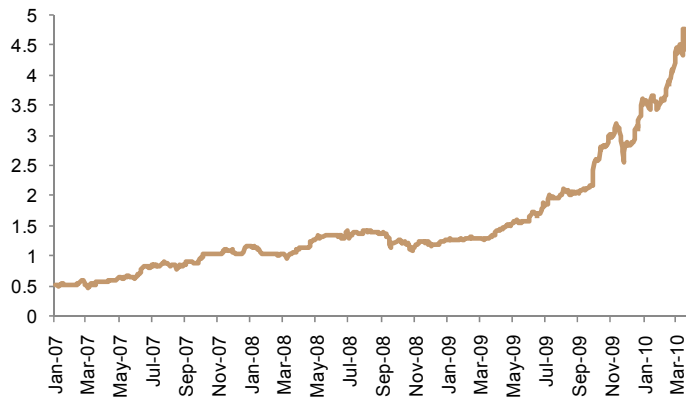
Figure 1: MIER consumer sentiment



Source: Bloomberg, OSK

Upgrade to BUY. Hai-O's share price has rallied strongly since early 2009, fuelled by a string of robust quarterly results. While we are maintaining our FY10 and FY11 net profit forecasts, we **upgrade Hai-O to a BUY** at an unchanged **TP of RM5.04** (based on 12x FY11 EPS) given the more than 10% share price upside after it retraced by some 5% since our downgrade on 22 March.

Figure 2: Hai-O's historical share price performance (RM)



Source: Bloomberg, OSK

EARNINGS FORECAST

FYE Apr (RMm)	FY08	FY09	FY10f	FY11f	FY12f
Turnover	373.8	435.2	569.6	679.0	786.1
EBIT	67.2	76.1	107.4	125.4	147.5
PBT	67.7	75.9	106.4	124.4	147.5
Net Profit	48.5	52.3	72.6	85.2	101.4
EPS (sen)	57.5	25.8	35.8	42.0	50.0
DPS (sen)	16.7	17.5	24.0	28.0	34.0
Margin					
EBIT (%)	18.0	17.5	18.9	18.5	18.8
PBT (%)	18.1	17.4	18.7	18.3	18.8
Net Profit (%)	13.0	12.0	12.7	12.5	12.9
ROE (%)	34.5	31.6	33.7	30.7	29.0
ROA (%)	23.8	21.1	25.8	24.5	24.3
Balance Sheet					
Fixed Assets	21.6	59.4	64.1	73.7	83.3
Current Assets	154.0	154.4	187.7	229.3	279.7
Total Assets	204.1	248.3	281.9	348.1	418.0
Current Liabilities	58.0	61.2	51.2	60.9	68.2
Net Current Assets	146.2	187.2	230.7	287.2	349.9
LT Liabilities	0.1	15.7	15.1	10.1	0.1
Shareholders Funds	140.6	165.4	215.6	277.1	349.8
Net Gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

OSK Research Guide to Investment Ratings

Buy: Share price may exceed 10% over the next 12 months

Trading Buy: Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

Neutral: Share price may fall within the range of +/- 10% over the next 12 months

Take Profit: Target price has been attained. Look to accumulate at lower levels

Sell: Share price may fall by more than 10% over the next 12 months

Not Rated (NR): Stock is not within regular research coverage

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