

Company Result

25 September 2015

Hai-O Enterprise Berhad

SELL

Trading water

Maintained

| | |
|---------------------|---------------|
| Share Price | RM2.29 |
| Target Price | RM1.85 |

Result

Company Description

Hai-O Enterprise Berhad is offering a wide range of Chinese medicines, medicated tonic, wellness, beauty and healthcare.

Stock Data

| | |
|--------------------------------------|------------------------------------|
| Bursa / Bloomberg code | 7668 / HAI0 MK |
| Board / Sector | Industrial / Food & Drug Retailers |
| Syariah Compliant status | No |
| Issued shares (m) | 194.59 |
| Par Value (RM) | 0.50 |
| Market cap. (RMm) | 445.62 |
| 52-week price Range | RM1.89– 2.66 |
| Beta (against KLCI) | 0.62 |
| 3-m Average Daily Volume | 0.06m |
| 3-m Average Daily Value [^] | RM0.13m |

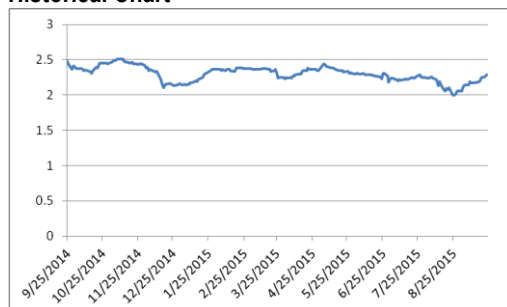
Share Performance

| | 1m | 3m | 12m |
|------------------|------|-----|-------|
| Absolute (%) | 14.5 | 5.1 | -12.6 |
| Relative (%-pts) | 8.8 | 6.4 | -0.3 |

Major Shareholders

| | % |
|-----------------|------|
| KAI HEE TAN | 10.0 |
| AKINTAN SDN BHD | 7.79 |
| SLOW ENG TAN | 6.92 |

Historical Chart



Source: Bloomberg

Team Coverage

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- **Hai-O's 1QFY2016 net earnings reported at RM6.63mil**, tumbling 29.5% q-o-q while increased by 6.5% y-o-y. Similarly, quarterly revenue declined by 21.4% q-o-q while managed to record a positive growth of 11.2% y-o-y. The positive growth recorded by both topline and bottomline for yearly basis mainly supported by higher revenue in MLM division.
- **Slightly below expectations.** 1QFY16 net profit only reached 20% of our forecast and market consensus. The poor results mainly attributable to the lackluster performance of wholesale and retail divisions that decline both in quarterly and yearly basis.

Comment

- **MLM division maintained its growth trajectory on yearly basis.** In 1QFY16, MLM division's PBT expanded by 34.4% y-o-y in line with higher topline growth of 29.4% y-o-y. The contribution of "small ticket" items as a new marketing strategy continued to cushion the drop in sales of "big ticket" items. In addition, the increase in new member recruitment also contributed to impressive performance for MLM division in 1QFY16.
- However, for its quarterly basis, MLM division's PBT declined by 28.6% q-o-q amid a negative topline growth of 4.33% q-o-q. The weaker performance was mainly due to higher base recorded in 4QFY15 following the better sales from incentive trip promotion campaign for second line distributors. Furthermore, the slowdown in distributor's activities during the fasting month in 1QFY16 also affected the earnings for MLM division.
- **Future earnings will continue to be underpinned by MLM division.** The decision to shift the business strategy to 'small ticket' items from 'large ticket' items seems yielding positive results as we start to witness the MLM division reported a positive PBT growth on quarterly basis since 2QFY15. Furthermore, the Group is aggressively promoting its existing products by having effective sales campaign activities and intensifying its new members' recruitment activities.
- **Lackluster performance posted by wholesale division.** The wholesale division's 1QFY16 PBT and revenue decreased by 15.8% y-o-y and 21.8% y-o-y respectively. The poor performance chiefly weighed down by the weak consumer sentiment in relation to slowdown in economy, rising cost of living and weakening Ringgit against USD. The lower sales volume from Chinese medicated tonic and patented medicine

from medical hall customers attributed to decline in revenue.

- Similarly, for its quarterly basis, the wholesale division's PBT and revenue slumped by 44.9% and 43.4% respectively. The weaker performance was primarily due to the impact after the implementation of GST as consumers became more cautious in their spending and cutting down their purchases after stocking up on inventories in 4QFY15. In addition, the lower PBT also caused by higher expenses incurred in commemoration of Hai-O's 40th year Anniversary coupled with higher corporate branding costs incurred to enhance Hai-O corporate image as a key player in the Traditional Chinese Medicine (TCM) industry.
- **Disappointing retail sales.** The Retail division posted decline in revenue and PBT for both yearly and quarterly basis mainly due to weakening purchasing power in addition to higher cost of living that dented the consumer spending after GST came into effect on 1 April 2015. The net loss in PBT for this quarter was mainly due to higher one-off personnel costs rewarded to staff in commemoration of Hai-O's 40th year Anniversary.
- **Consumers still adopt 'wait-and-see' stance.** We envisage that consumers will continue to be cautious in their spending after the implementation of GST which will impact to group's wholesale and retail divisions. Retail Group Malaysia has slashed its retail-sales-growth projection for this year from 4% to 3.1%, marking the 4th time it revised downwards its 2015 forecast. We only expect the consumer sentiment will start to recover in 1QCY16. Furthermore, the wholesale division will continue to be dented by the devaluation of RM against USD since 80% of its import purchases are settled in USD.

Earnings Outlook/Revision

- **We slightly tweaked down our net earnings forecasts for FY16 by 1% to RM30mil** from previous RM33.2mil following the Group posted lower-than-expected 1QFY16 net profit.

Valuation & Recommendation

- **Maintain SELL call on Hai-O with lower target price of RM1.85 (previous target price was RM1.90)** as we opine the Group's operating outlook will remain challenging moving forward amid continued fragility in consumer sentiment. Our revised target price is pegged at 12x FY2016F PE based on EPS of 15 cent (previous EPS: 17 cent).

Figure 1: Quarterly Figures

| Year to 30 Apr | 1QFY16 (RMm) | 4QFY15 (RMm) | 1QFY15 (RMm) | QoQ % chg | YoY % chg |
|--------------------------|-----------------|-----------------|-----------------|--------------|--------------|
| Revenue | 55.4 | 70.4 | 49.8 | -21.4% | 11.2% |
| Operating Profit | 8.7 | 15.9 | 8.2 | -45.3% | 6.2% |
| Pre-tax Profit | 8.8 | 15.5 | 8.4 | -43.1% | 4.7% |
| Profit After Tax | 6.5 | 10.0 | 6.2 | -34.7% | 5.0% |
| Net Profit | 6.6 | 9.4 | 6.2 | -29.5% | 6.5% |
| MARGIN (%) | | | | | |
| Operating | 15.7% | 22.6% | 16.5% | -6.9ppt | -0.7ppt |
| Profit Before Tax | 15.9% | 22.0% | 16.9% | -6.1ppt | -1.0ppt |
| Profit After Tax | 11.8% | 14.2% | 12.5% | -2.4ppt | -0.7ppt |
| Net Profit Margin | 12.0% | 13.3% | 12.5% | -1.4ppt | -0.5ppt |

Source: Company, JF Apex

Figure 2: Revenue and PBT by divisions

| Year to 30 Apr | 1QFY16 (RMm) | 4QFY15 (RMm) | 1QFY15 (RMm) | QoQ % chg | YoY % chg |
|----------------------------------|-----------------|-----------------|-----------------|----------------|---------------|
| Segment Revenue | | | | | |
| MLM | 36.75 | 38.41 | 28.41 | -4.33% | 29.35% |
| Wholesales | 9.26 | 16.36 | 11.84 | -43.41% | -21.81% |
| Retail | 7.58 | 14.15 | 7.70 | -46.46% | -1.66% |
| Total Revenue | 53.58 | 68.92 | 47.95 | -22.26% | 11.74% |
| Segment Profit Before Tax | | | | | |
| MLM | 6.24 | 8.73 | 4.64 | -28.57% | 34.37% |
| Wholesales | 1.78 | 3.23 | 2.11 | -44.89% | -15.76% |
| Retail | -0.15 | 2.14 | -0.02 | -107.03% | N/A |
| Total Profit Before Tax | 7.87 | 14.10 | 6.74 | -44.19% | 16.74% |
| Segment PBT margin | | | | | |
| MLM | 16.97% | 22.73% | 16.34 | -5.76ppt | 0.63ppt |
| Wholesales | 19.23% | 19.74% | 17.85% | -0.52ppt | 1.38ppt |
| Retail | -1.98% | 15.09% | -0.21% | -17.07ppt | -1.77ppt |

Source: Company, JF Apex

Figure 3: Financial Summary

| Year to 30 April (RMm) | FY2013 | FY2014 | FY2015 | FY2016F | FY2017F |
|------------------------|--------|--------|--------|---------|---------|
| Revenue | 266.6 | 253.5 | 239.9 | 208.0 | 251.8 |
| Operating profit | 63.1 | 52.1 | 41.8 | 48.3 | 59.2 |
| Net profit | 47.2 | 40.3 | 29.8 | 30.0 | 44.1 |
| EPS (sen) | 24.2 | 20.7 | 15.3 | 15.4 | 22.6 |
| P/E (x) | 9.5 | 11.1 | 15.0 | 14.9 | 10.1 |
| P/BV (x) | 1.8 | 1.7 | 1.7 | 1.6 | 1.6 |
| Dividend yield (%) | 4.8% | 4.6% | 4.9% | 2.9% | 4.2% |
| PBT margin (%) | 24.0% | 21.0% | 17.8% | 24.2% | 24.6% |
| Net Gearing (%) | -19.4% | -19.3% | -15.0% | -9.9% | -4.5% |
| ROE (%) | 18.8% | 15.2% | 11.2% | 11.1% | 16.1% |

Source: Company, JF Apex Estimates

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JF APEX SECURITIES - RESEARCH RECOMMENDATION FRAMEWORK

STOCK RECOMMENDATIONS

- BUY** : The stock's total returns* are expected to exceed 10% within the next 12 months.
- HOLD** : The stock's total returns* are expected to be within +10% to – 10% within the next 12 months.
- SELL** : The stock's total returns* are expected to be below -10% within the next 12 months.
- TRADING BUY** : The stock's total returns* are expected to exceed 10% within the next 3 months.
- TRADING SELL** : The stock's total returns* are expected to be below -10% within the next 3 months.

SECTOR RECOMMENDATIONS

- OVERWEIGHT** : The industry as defined by the analyst is expected to exceed 10% within the next 12 months.
- MARKETWEIGHT** : The industry as defined by the analyst is expected to be within +10% to – 10% within the next 12 months.
- UNDERWEIGHT** : The industry as defined by the analyst, is expected to be below -10% within the next 12 months.

*capital gain + dividend yield

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