

10 April 2017

# Hai-O Enterprise Berhad

## Expanding Distributors Base

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# MARKET PERFORM ↔

**Price:** RM3.59  
**Target Price:** RM3.64 ↑

We came away feeling more positive on its prospect after a meeting with the key management featuring founder, Mr Tan Kai Hee, General Manager, Mr Tham Yoke Lon and CFO, Mr Hew Von Kin. Its MLM division is expected to continue its steady run with the backing of strong new recruitments and sound product strategy while the other business segments are expected to perform modestly. Post-meeting, we raised FY17E and FY18E net profits by 1.4% and 13.4%, respectively. Correspondingly, our Target Price is nudged higher to RM3.64 (from RM3.21), based on unchanged 15.2x PER FY18E which implies +1.5 SD over the 5-year mean. Maintain MARKET PERFORM call.

**Re-look on 9M17 results.** 9M17 revenue surged 36.3% to RM285.6m, mainly driven by impressive growth in MLM division (+58.6%), thanks to the strengthening of distributors base to 120k distributors, (9M16: 70k distributors), supported by the strong sales of personal care and household consumer products. 9M17 operating profit jumped 62.6% to RM54.2m, again boosted by MLM division (+80.3%), with expanded operating margin of 19.0% (9M16: 15.9%). The MLM division contributed 78.0% of the 9M17 group operating profit (9M16: 70.6%). As a result, 9M17 net profit grew 64.2% to RM41.3m. Moving forward, management is confident that the MLM segment momentum can be sustained with younger generation of distributors joining the force vying for extra income in amidst of the challenging economy and job market.

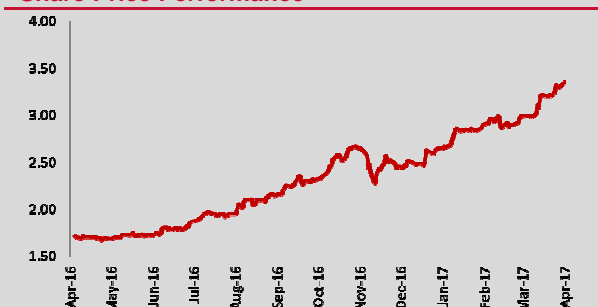
**Cautious on wholesale and retail segments.** Despite the wholesale and retail divisions' 9M17 operating profits growing at 41.9% and 41.6%, respectively, management is maintaining a conservative stance as both divisions are vulnerable to currency risk, weak consumer sentiment and attributed the strong performance to seasonality factor. The operating environment for retail segment remains challenging with its focus on high margin in-house brands (c.40% for retail sales) to remain profitable, but the company is not scaling down this division as it complements other segments.

**Incentives and Promotion to maintain momentum.** To keep its distributors momentum going, the company allocates budget of RM10m every year for its incentives and promotion. The incentive trips are divided into two trips for each half of the year. The company targeted at least 600 eligible distributors per trip for 2017 (2016: 500 distributors). In conjunction with **25<sup>th</sup> SHOM Anniversary Promotion for 2017**, the company is planning to organize recognition night for MLM top leaders. The company targeted at least 100 eligible distributors (2016: 40 eligible distributors). This incentives trips and promotion are key factors in expanding the number of its distributors while maintaining the loyalty of its existing distributors.

**MLM steady momentum.** MLM continued with its momentum, which was driven by both expansion in distributor base and the strong productivity on the back of the effective product strategy and rewarding incentive system. The increased contribution of MLM division has also reduced the risks of other operating divisions, including wholesale and retail divisions, which are exposed to the currency risk and weak consumer sentiment. Moving forwards, the company is expanding its MLM business, venturing into fashion and beauty care under the brand "Infinence", supported by the expertise of the company non-independent and non-executive director Prof. Datuk Dr Choo Yeang Keat (also known as "Jimmy Choo") and professional consultants (Currently, Rizman Ruzaini).

**Maintain MARKET PERFORM call with higher Target Price of RM3.64 (from RM3.21).** We raised FY17E and FY18E net profits by 1.4% and 13.4%, respectively, as we were previously too conservative with the distributor force growth. Correspondingly, our Target Price is nudged higher to RM3.64, based on unchanged 15.2x PER FY18E which implies +1.5 SD over the 5-year mean. We are maintaining our neutral stance on the company on its strong brand names, sturdy balance sheet and generous dividend pay-out.

### Share Price Performance



KLCI	1,741.72
YTD KLCI chg	6.1%
YTD stock price chg	35.6%

### Stock Information

Shariah Compliant	No
Bloomberg Ticker	HAIO MK Equity
Market Cap (RM m)	1,038.9
Issued shares	289.4
52-week range (H)	3.60
52-week range (L)	1.63
3-mth avg daily vol:	341,781
Free Float	72%
Beta	0.6

### Major Shareholders

Siow Eng Tan	10.5%
Kai Hee Tan	10.1%
AKINTAN Sdn Bhd	7.9%

### Summary Earnings Table

FY Apr (RM'm)	2016A	2017E	2018E
Turnover	298.1	447.1	577.6
EBIT	48.3	71.3	89.9
PBT	49.1	73.2	91.8
<b>Net Profit (NP)</b>	<b>36.4</b>	<b>54.5</b>	<b>69.3</b>
Earnings Revision	-	1.4%	13.4%
EPS (sen)	12.6	18.8	24.0
EPS growth (%)	20.8%	49.8%	27.2%
NDPS (sen)	10.2	14.2	18.0
BV/Share (RM)	1.04	1.09	1.15
PER	28.6	19.1	15.0
Price/BV (x)	3.5	3.3	3.1
Net Gearing (x)	N.Cash	N.Cash	N.Cash
Net Dvd Yield (%)	2.8%	4.0%	5.0%

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Income Statement						Financial Data & Ratios					
FY Apr (RM m)	2014A	2015A	2016A	2017E	2018E	FY Apr (RM m)	2014A	2015A	2016A	2017E	2018E
Revenue	253.4	239.9	298.1	447.1	577.6	<b>Growth (%)</b>					
EBITDA	53.5	45.4	51.8	75.1	94.2	Revenue	-4.9%	-5.3%	24.2%	50.0%	29.2%
Depreciation	-3.0	-3.2	-3.5	-3.8	-4.3	EBITDA	-9.1%	-15.2%	14.2%	45.0%	25.4%
Operating Profit	50.5	42.2	48.3	71.3	89.9	Operating Profit	-10.1%	-16.4%	14.6%	47.5%	26.1%
Int Income	1.6	1.3	1.5	1.5	1.4	Pre-tax Income	-16.9%	-19.0%	14.2%	49.0%	25.4%
PBT	53.1	43.0	49.1	73.2	91.8	Net Income	-14.6%	-25.3%	20.8%	49.8%	27.2%
Taxation	-12.3	-12.3	-12.5	-17.6	-22.0	<b>Profitability (%)</b>					
Minority Interest	-0.6	-0.7	-0.2	-1.1	-1.4	EBITDA Margin	21.1%	18.9%	17.4%	16.8%	16.3%
Net Profit	40.3	30.1	36.4	54.5	69.3	Operating Margin	19.9%	17.6%	16.2%	15.9%	15.6%
						PBT Margin	21.0%	17.9%	16.5%	16.4%	15.9%
						Core Net Margin	15.9%	12.5%	12.2%	12.2%	12.0%
						Effective Tax Rate	-23.1%	-28.5%	-25.5%	-24.0%	-24.0%
						ROE	15.9%	11.9%	12.1%	17.3%	20.9%
						ROA	13.0%	9.8%	11.3%	14.1%	16.8%
						<b>DuPont Analysis</b>					
						Net Margin (%)	15.9%	12.5%	12.2%	12.2%	12.0%
						Assets Turnover(x)	0.82	0.78	0.93	1.16	1.40
						Leverage Factor (x)	1.22	1.20	1.07	1.23	1.24
						ROE (%)	15.9%	11.9%	12.1%	17.3%	20.9%
						<b>Leverage</b>					
						Debt/Asset (x)	0.0	0.0	0.0	0.0	0.0
						Debt/Equity (x)	0.0	0.0	0.0	0.0	0.0
						Net Cash/(Debt)	54.3	44.4	53.3	65.0	47.1
						Net Debt/Equity (x)	N.Cash	N.Cash	N.Cash	N.Cash	N.Cash
						<b>Valuations</b>					
						EPS (sen)	20.5	15.4	12.6	18.8	24.0
						NDPS (sen)	14.0	15.0	10.2	14.2	18.0
						BV (RM)	1.30	1.30	1.04	1.09	1.15
						PER (x)	17.5	23.3	28.6	19.1	15.0
						Net Div. Yield (%)	3.9%	4.2%	2.8%	4.0%	5.0%
						P/BV (x)	2.77	2.76	3.45	3.31	3.13
						EV/EBITDA (x)	12.0	14.4	12.5	8.4	6.9

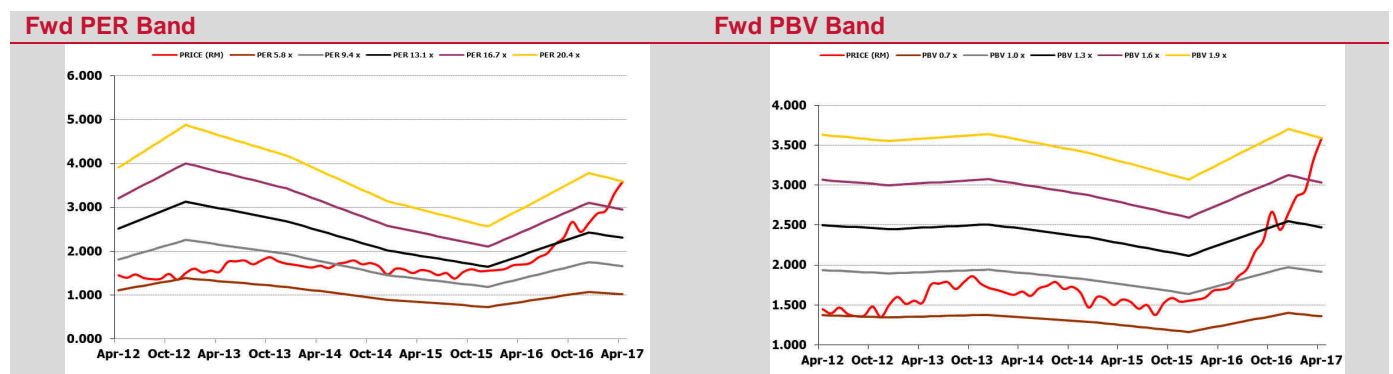
  

Balance Sheet					
FY Apr (RM m)	2014A	2015A	2016A	2017E	2018E
Fixed Assets	106.5	64.6	66.3	77.5	83.3
Intangible Assets	0.1	0.1	0.1	0.1	0.1
Other FA	5.8	55.1	54.3	54.7	55.2
Inventories	58.5	58.2	68.2	102.5	132.5
Receivables	14.1	16.9	23.6	31.7	38.9
Other CA	63.8	62.7	53.8	53.8	53.8
Cash	59.9	48.3	54.4	66.1	48.2
Total Assets	308.8	305.9	320.6	386.5	412.0
Payables	13.2	12.1	44.4	52.1	58.9
ST Borrowings	3.2	3.9	1.1	1.1	1.1
Other ST Liability	24.3	23.9	6.1	6.1	6.1
LT Borrowings	2.4	0.0	0.0	0.0	0.0
Other LT Liability	0.1	0.1	0.1	0.1	0.1
Minorities Int.	11.5	12.0	11.6	12.7	14.2
<b>Net Assets</b>	<b>254.1</b>	<b>253.9</b>	<b>257.4</b>	<b>314.3</b>	<b>331.7</b>
Share Capital	101.1	101.1	144.7	144.7	144.7
Reserves	153.0	152.8	156.3	169.6	187.0
<b>Equity</b>	<b>254.1</b>	<b>253.9</b>	<b>301.0</b>	<b>314.3</b>	<b>331.7</b>

Cashflow Statement					
FY Apr (RM m)	2014A	2015A	2016A	2017E	2018E
Operating CF	29.1	27.5	44.8	22.8	42.7
Investing CF	-0.9	-9.2	-2.6	-15.0	-10.0
Financing CF	-32.5	-32.0	-36.1	3.9	-50.6
Change In Cash	-4.3	-13.7	6.1	11.8	-17.9
Free CF	38.8	25.1	52.4	25.4	54.8

Source: Kenanga Research



Source: Bloomberg, Kenanga Research

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### Peer Comparison

NAME	Price	Mkt Cap	PER (x)			Est. Div. Yld.	Historical ROE	P/BV (x)	Net Profit (RMm)			1Y Fwd Growth (%)	2Y Fwd Growth (%)	Target Price (RM)	Rating
	(RM)	(RMm)	Historical	1Y Fwd	2Y Fwd				Historical	1Y Fwd	2Y Fwd				
<b>Consumer - Retail</b>															
AEON CO (M) BHD	2.38	3,341.5	41.9	35.1	33.2	1.7%	4.3%	1.83	75.0	92.1	100.5	22.9%	9.1%	2.38	UP
AMWAY (MALAYSIA) HLDGS BHD	7.68	1,262.5	23.1	16.9	16.2	5.2%	26.3%	5.73	54.6	74.6	77.7	36.5%	4.2%	8.98	OP
HAI-O ENTERPRISE BHD	3.59	1,038.9	28.6	19.1	15.0	3.9%	18.4%	3.45	36.4	54.5	69.3	49.8%	27.2%	3.64	MP
PADINI HOLDINGS BERHAD	2.97	1,954.0	14.2	13.2	11.3	4.0%	32.3%	3.09	137.4	148.3	173.1	7.9%	16.7%	2.83	MP
PARKSON HOLDINGS BHD	0.64	683.0	(7.7)	(15.2)	14.5	7.8%	-4.2%	0.28	(105.6)	(46.4)	48.2	-56.1%	-203.9%	0.88	OP
<b>Consumer - F&amp;B</b>															
DUTCH LADY	56.76	3,632.6	24.4	22.2	21.2	4.2%	92.4%	21.95	149.1	163.4	171.5	9.6%	4.9%	59.74	MP
NESTLE (M)	79.88	18,731.9	29.4	28.7	27.9	3.4%	94.0%	28.53	637.1	652.1	671.7	2.4%	3.0%	80.66	MP
OLDTOWN BHD	2.69	1,222.6	22.8	18.7	16.3	3.3%	18.5%	3.36	52.3	63.9	73.1	22.2%	14.4%	2.64	MP
QL RESOURCES BHD	4.58	5,716.0	29.8	26.9	24.8	1.2%	11.3%	3.59	192.1	207.3	224.6	7.9%	8.3%	4.34	UP
<b>Consumer - Sin</b>															
BRITISH AMERICAN TOBACCO BHD	46.00	13,134.4	19.5	19.1	19.0	5.1%	124.4%	21.90	675.1	688.0	693.0	1.9%	0.7%	43.44	UP
CARLSBERG BREWERY MALAYSIA B	15.10	4,645.1	22.5	19.8	17.9	4.5%	62.4%	13.56	205.0	233.7	257.8	14.0%	10.3%	14.84	MP
HEINEKEN MALAYSIA BHD	18.26	5,516.3	12.9	17.7	16.2	5.2%	71.1%	14.05	427.3	312.4	340.1	-26.9%	8.9%	21.38	OP

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% (an approximation to the 5-year annualised Total Return of FBMKLCI of 10.2%).
- MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of 3% to 10%.
- UNDERPERFORM : A particular stock's Expected Total Return is LESS than 3% (an approximation to the 12-month Fixed Deposit Rate of 3.15% as a proxy to Risk-Free Rate).

**Sector Recommendations\*\*\***

- OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10% (an approximation to the 5-year annualised Total Return of FBMKLCI of 10.2%).
- NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of 3% to 10%.
- UNDERWEIGHT : A particular sector's Expected Total Return is LESS than 3% (an approximation to the 12-month Fixed Deposit Rate of 3.15% as a proxy to Risk-Free Rate).

**\*\*\*Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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