

Company Update

Hai-O Ent

HAIO MK
RM2.65

BUY (maintain)

Target Price: RM3.20 (↑)



Price Performance

	1M	3M	12M
Absolute	+3.5%	+14.7%	+27.9%
Rel to KLCI	+5.4%	+6.5%	+16.6%

Stock Data

Issued shares (m)	196.9
Mkt cap (RMm)	521.9
Avg daily vol - 6mth (m)	0.21
52-wk range (RM)	1.93 – 2.77
Est free float	63.9%
NTA per share (RM)	1.17
P/NTA (x)	2.27
Net cash/debt (RMm) (end-Jan 13)	40.0
ROE (FY13E)	17.3%
Derivatives	Nil

Key Shareholders

Tan Kai Hee	9.6%
Akintan Sdn Bhd	7.3%
Excellent Communications	5.3%

Earnings & Valuation Revisions

	13E	14E	15E
Prev EPS (sen)	20.2	23.7	27.7
Curr EPS (sen)	22.7	25.2	29.0
Chg (%)	+12.4	+6.3	+4.7
Prev target price (RM)			2.98
Curr target price (RM)			3.20

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An attractive proposition not to be missed

Expecting FY13 core earnings to surge by +39% yoy

Hai-O is set to release its full year FY13 results on 26 June 2013. In view of the resilient growth in its core MLM division and also wholesale division backed, by the country's healthy domestic sales growth, we believe FY13 earnings has room to surprise on the upside. We forecast a revised FY13 net profit growth of +39% yoy, an uplift from our earlier growth forecast of 23%. Our +4.7% to 12.4% upgrade in FY13-15 EPS forecast takes into account: 1) the doubling in revenue per agent growth rate to 15% owing to higher sales volume in bigger ticket items; 2) higher growth rate in new members registration; and 3) stronger sales contributions from its wholesale division, leveraging on improved medical consultation services provided by the panel of Chinese Physicians from *Tong Ren Tang (TRT)*. (TRT is the world's largest traditional Chinese medicine producer)

Strong membership growth, driving its MLM division

We remain positive on Hai-O's new operating strategy in driving its core MLM division. Our check with management indicated that the growth in new members registration (80% Bumiputeras) is encouraging, with c.2.2k-2.5k new members registered each month. In addition, we gather that volume sales for its bigger ticket items such as foundation garments (selling at RM1.3k-1.5k/set), air purifier and Bio Velocity mattress continues to improve. We attribute this to the healthy domestic economic conditions with higher disposable income brought by the recent minimum wage implementation and government's cash handouts.

Bumper dividends in the offing?

As we anticipate a stronger FY04/13 net profit growth and coupled with Hai-O's generosity in streaming up surplus cash to shareholders, we believe Hai-O will likely lift its dividend payout. Embedded in our forecast is a final DPS of 7 sen, bringing the total net DPS for FY04/13 to 13 sen (FY04/12: 9 sen), based on a higher payout ratio of 57% vs 55% in FY04/12. (Note that Hai-O had already declared a single tier interim dividend of 4 sen and a special single tier dividend of 2 sen in 1HFY04/13 vis-a-vis 1H04/12's DPS of 2 sen)

Reiterate BUY with TP lifted to RM3.20. Yields remain highly attractive

Following our EPS upgrade, our price target is raised from RM2.98 to **RM3.20**, pegging the stock at 11.5x CY14 EPS. Since we upgraded our rating from ADD to BUY on 4 April 2013, the stock has appreciated by +12.8%, outperforming the KLCI by +7.8%. Notwithstanding the sharp rise in share price, we reckon that Hai-O's valuation remains highly undemanding, trading at 10.3x FY14 PER. Furthermore, the stock also offers highly attractive yields at 5%. All in, we reiterate our **BUY** rating on Hai-O.

Earnings and valuation summary

FYE 30 April	2011	2012	2013E	2014E	2015E
Revenue (RMm)	223.3	239.5	301.1	338.5	381.6
EBITDA (RMm)	44.8	52.3	68.0	75.2	86.0
Pretax profit (RMm)	41.3	48.8	64.2	71.4	82.2
Net profit (RMm)	28.4	34.0	46.0	51.2	58.9
EPS (sen)	14.0	16.8	22.7	25.2	29.0
PER (x)	18.9	15.8	11.7	10.5	9.1
Core net profit (RMm)	28.4	33.2	46.0	51.2	58.9
Core EPS (sen)	14.0	16.4	22.7	25.2	29.0
Core EPS chg (%)	-59.8	17.0	38.6	11.2	15.1
Core PER (x)	18.9	16.2	11.7	10.5	9.1
Net DPS (sen)	7.5	9.0	13.0	14.6	16.8
Net Dividend Yield (%)	2.8	3.4	4.9	5.5	6.4
EV/EBITDA (x)	10.5	8.4	6.3	5.3	4.4
Consensus profit (RMm)			42.6	47.3	54.9
Affin/Consensus (x)			1.1	1.1	1.1

Other Update

6 new products coming on stream in FY14

We gathered that its KAEAM bamboo salt remain as one of the key performers under the healthcare food products, generating c.RM1m/month of revenue, with c.10,000 boxes sold per month. (KAEAM bamboo salt was launched in 2011) Riding on the healthy domestic spending, Hai-O is set to launch another 5 new products and 1 big ticket product (in addition to foundation garments, Bio Auro water filters, food purifier and Bio Velocity mattress) in FY14.

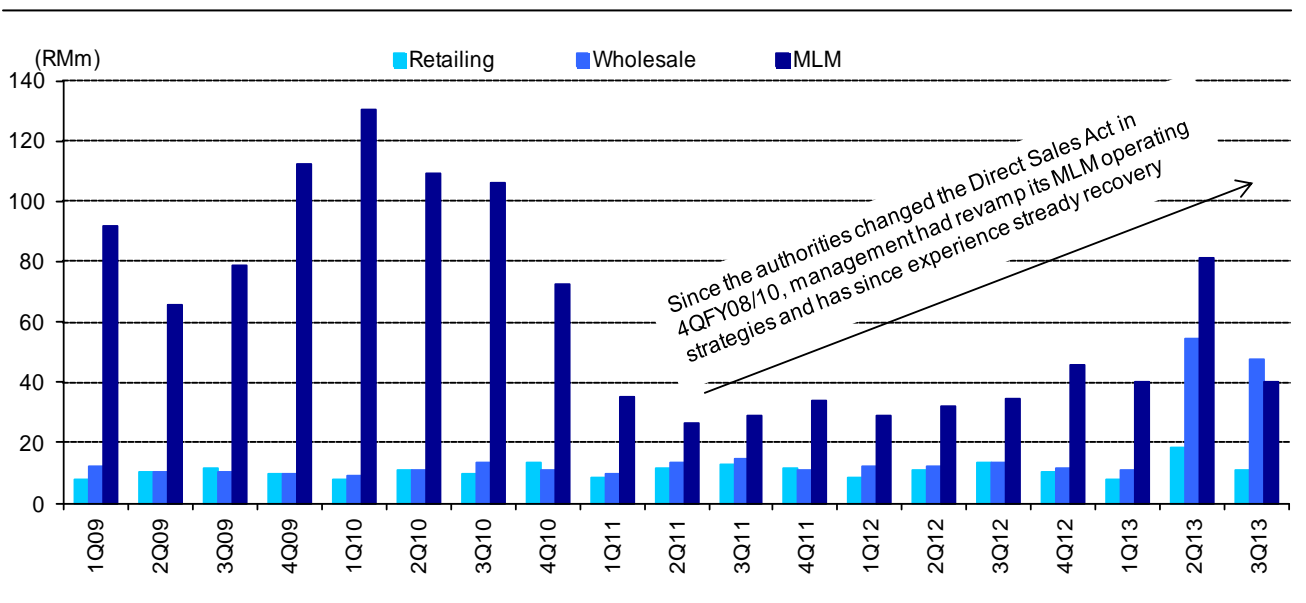
Healthy retail expansion; targeting 3-5 new outlets in FY14

The group has opened 7 new retail outlets in FY12-13, bringing to a total of 72 outlets nationwide (4 owned, 68 leased). We note that the group will continue to expand its footprint, targeting to open another 3-5 outlets in strategic locations by FY14. CAPEX is estimated at RM200-300k per outlet, and this will be funded internally. We believe funding of these CAPEX is not an issue judging from: 1) Hai-O's healthy balance sheet with a net cash per share of RM0.53 (as of 31 October 2012); and 2) strong operating cash flow of c.RM35m p.a.

Our positive view on Hai-O is warranted

Taking into consideration: 1) Hai-O's strong recovery in its core MLM division – a continuation of its strong membership growth; 2) favourable demand for its *halal* certified products; 3) undemanding valuations; 4) the group's generosity in rewarding shareholders by paying out good dividends of at least 50% of its net profits; and 5) Hai-O's highly attractive yields, our positive view on Hai-O's prospects are justifiable. We also note that the company's wholesale division is looking to expand its business network and improve its product mix as well as marketing strategies to capture the younger and newer market. (Hai-o's wholesale division is currently supplying its products to 100 wholesalers and 2,000 retailers including Chinese Medical Halls, Restaurants, Pharmacies and Modern Trade Channels).

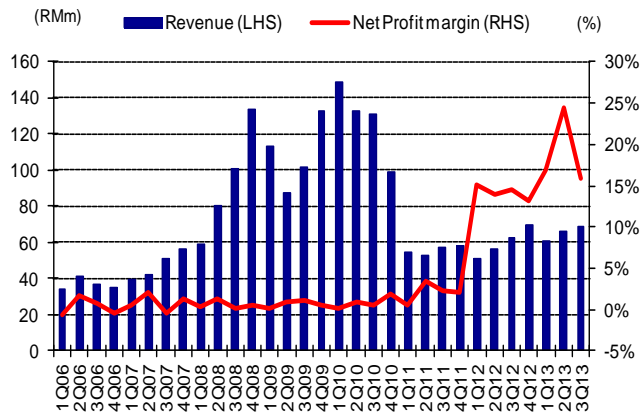
Fig: Quarterly revenue contribution



Source: Affin, Company

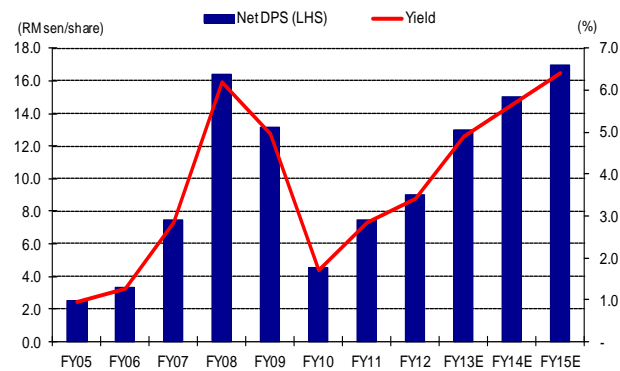
FOCUS CHART

Fig 1: Hai-O's net profit (LHS) and EBIT margin (RHS)



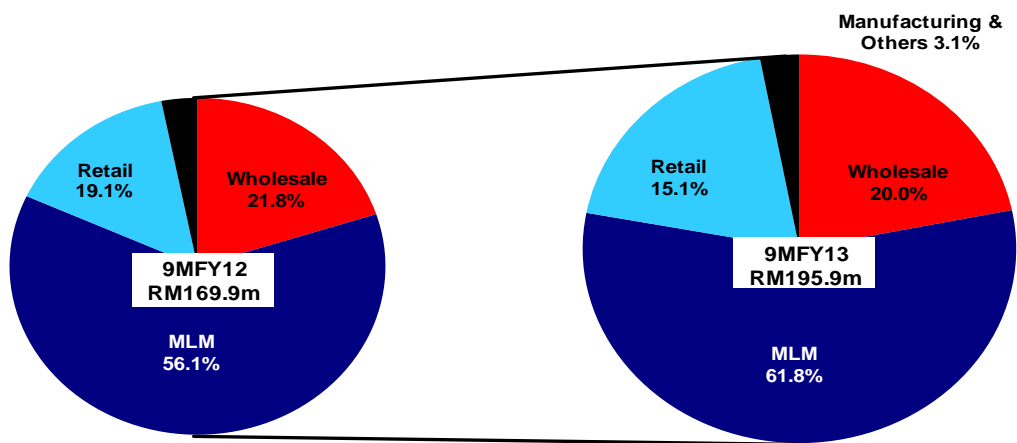
Source: Affin

Fig 3: Net DPS (LHS) and dividend yield (RHS)



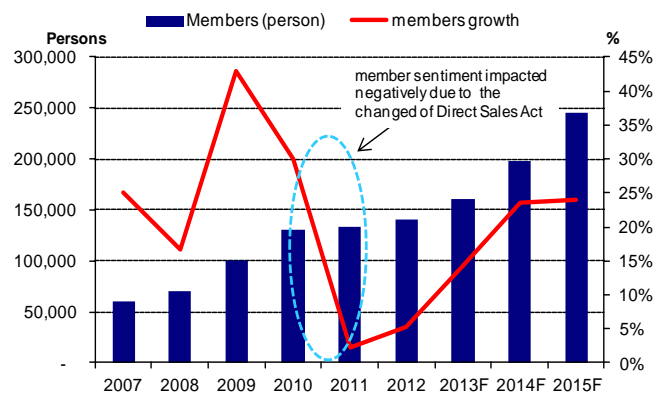
Source: Affin

Fig 5: Revenue breakdown by divisions



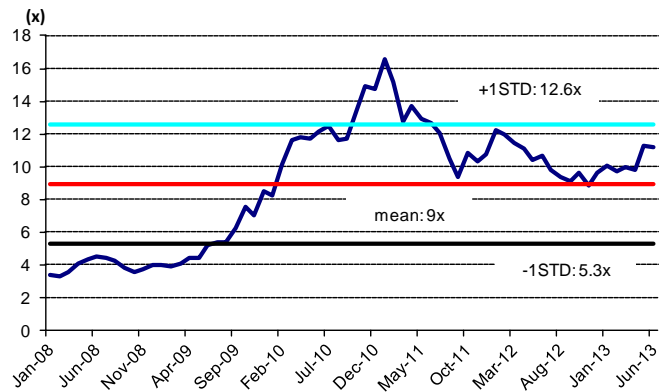
Source: Affin

Fig 2: Hai-O's members and members' growth rate



Source: Company, Affin

Fig 4: 5-yr average PER band



Source: Bloomberg, Affin

FINANCIAL SUMMARY

Profit & Loss Statement

FYE 30 April (RMm)	2011	2012	2013E	2014E	2015E
Revenue	223.3	239.5	301.1	338.5	381.6
Operating expenses	-178.4	-187.3	-233.2	-263.4	-295.7
EBITDA	44.8	52.3	68.0	75.2	86.0
Depreciation	-2.2	-2.1	-2.4	-2.5	-2.6
EBIT	42.1	49.5	64.9	72.0	82.8
Net int income/(expense)	-0.8	-0.7	-0.7	-0.6	-0.5
Associates' contribution	0.0	0.0	0.0	0.0	0.0
Pretax profit	41.3	48.8	64.2	71.4	82.2
Tax	-11.6	-13.1	-16.1	-17.9	-20.6
Minority interest	-1.3	-1.7	-2.2	-2.4	-2.8
Net profit	28.4	34.0	46.0	51.2	58.9

Balance Sheet Statement

FYE 30 April (RMm)	2011	2012	2013E	2014E	2015E
Fixed assets	72.2	62.1	64.7	67.2	69.6
Other long term assets	38.0	50.3	49.6	48.9	48.3
Total non-current assets	110.2	112.4	114.3	116.1	117.9
Cash and equivalents	46.1	54.2	65.7	89.6	113.9
Stocks	44.3	37.8	47.9	53.9	60.8
Debtors	19.1	21.9	27.5	31.0	34.9
Other current assets	37.4	63.4	63.4	63.4	63.4
Total current assets	146.8	177.3	204.5	237.9	273.0
Creditors	22.6	32.5	41.2	46.4	52.3
Short term borrowings	5.7	5.2	4.7	4.2	3.8
Other current liabilities	5.2	12.4	12.4	12.4	12.4
Total current liabilities	33.4	50.1	58.3	63.0	68.5
Long term borrowings	10.7	8.1	7.3	6.6	5.9
Other long term liabilities	0.1	0.0	0.2	0.2	0.2
Total long term liabilities	10.9	8.1	7.5	6.8	6.1
Shareholders' Funds	204.4	221.7	241.2	270.0	299.2
Minority interest	8.3	9.7	11.9	14.3	17.1

Cash Flow Statement

FYE 30 April (RMm)	2011	2012	2013E	2014E	2015E
EBIT	42.1	49.5	64.9	72.0	82.8
Depreciation & amortisation	2.6	2.7	3.1	3.1	3.2
Working capital changes	-10.4	-5.1	-7.1	-4.3	-4.9
Cash tax paid	-11.6	-13.1	-16.1	-17.9	-20.6
Others	-8.9	16.1	-0.2	0.0	0.0
Cashflow from operation	13.9	50.2	44.7	53.0	60.5
Capex	-12.3	-2.9	-5.0	-5.0	-5.0
Others	10.6	-18.5	0.0	0.0	0.0
Cash flow from investing	-1.7	-21.5	-5.0	-5.0	-5.0
Debt raised/(repaid)	-1.6	-3.1	-1.3	-1.2	-1.1
Dividends paid	-33.9	-15.0	-26.4	-22.4	-29.7
Others	-1.3	-2.4	-0.5	-0.6	-0.5
Cash flow from financing	-36.8	-20.5	-28.1	-24.2	-31.3
Free Cash Flow	1.6	47.2	39.7	48.0	55.5

Source: Affin

Key Financial Ratios and Margins

FYE 30 April (RMm)	2011	2012	2013E	2014E	2015E
Growth					
Revenue (%)	-56.3	7.3	25.7	12.4	12.7
EBITDA (%)	-54.7	16.6	30.0	10.6	14.4
Core net profit (%)	-59.8	19.9	35.3	11.2	15.1
Profitability					
EBITDA margin (%)	20.1	21.8	22.6	22.2	22.5
PBT margin (%)	18.5	20.4	21.3	21.1	21.5
Net profit margin (%)	12.7	14.2	15.3	15.1	15.4
Effective tax rate (%)	28	27	25	25	25
ROA (%)	13.0	14.2	17.1	16.8	17.2
Core ROE (%)	13.9	15.6	19.9	20.0	20.7
ROCE (%)	19.1	21.7	26.6	27.0	28.1
Dividend payout ratio (%)	53.6	53.6	57.4	58.0	58.0
Liquidity					
Current ratio (x)	4.4	3.5	3.5	3.8	4.0
Op. cash flow (RMm)	13.9	50.2	44.7	53.0	60.5
Free cashflow (RMm)	1.6	47.2	39.7	48.0	55.5
FCF/share (sen)	0.8	23.3	19.6	23.7	27.4
Asset management					
Debtors turnover (days)	31.2	33.4	33.4	33.4	33.4
Stock turnover (days)	116.8	93.2	93.2	93.2	93.2
Creditors turnover (days)	59.5	80.1	80.1	80.1	80.1
Capital structure					
Net gearing (%)		net cash	net cash	net cash	net cash
Interest cover (x)	119.0	52.8	70.3	101.5	124.8

Quarterly Profit & Loss

FYE 30 April (RMm)	3Q12	4Q12	1Q13	2Q13	3Q13
Revenue	62.8	69.4	61.1	65.9	68.9
Operating expenses	-49.8	-56.3	-45.8	-48.9	-54.8
EBITDA	13.0	13.2	15.4	16.9	14.0
Depreciation	0.0	0.0	0.0	0.0	0.7
EBIT	13.0	13.2	15.4	16.9	14.8
Net int income/(expense)	0.0	0.1	-1.5	-1.3	0.1
Associates' contribution	0.0	0.0	0.0	0.0	0.0
Exceptional Items	0.0	0.0	0.0	4.9	0.2
Pretax profit	13.0	13.3	13.8	20.5	15.1
Tax	-3.5	-3.7	-3.5	-4.0	-4.1
Minority interest	-0.4	-0.4	-0.1	-0.4	0.0
Net profit	9.1	9.2	10.3	16.1	11.0
Core net profit	9.1	9.2	10.3	11.2	10.8
Margins (%)					
EBITDA	20.7	18.9	25.2	25.7	20.4
PBT	20.7	19.1	22.6	31.1	21.9
Net profit	14.4	13.2	16.8	24.4	15.9

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +15% over a 12-month period
TRADING BUY (TR BUY)	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
ADD	Total return is expected to be between 0% to +15% over a 12-month period
REDUCE	Total return is expected to be between 0% to -15% over a 12-month period
TRADING SELL (TR SELL)	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
SELL	Total return is expected to be below -15% over a 12-month period
NOT RATED	Affin Investment Bank does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation
OVERWEIGHT	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
NEUTRAL	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
UNDERWEIGHT	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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