

20 September 2013

# Hai-O Enterprise Bhd

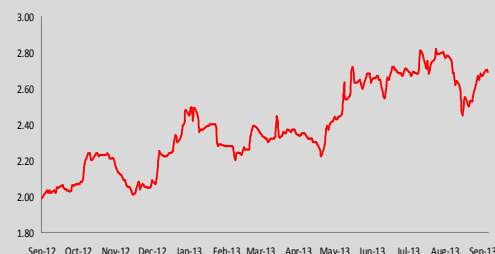
## Just a Quarterly Hiccup?

# OUTPERFORM ↔

**Price: RM2.74**
**Target Price: RM3.00 ↔**

- |                                |  |
|--------------------------------|--|
| <b>Period</b>                  | ▪ 1Q14   |
| <b>Actual vs. Expectations</b> | ▪ 1Q14 net profit (NP) of RM8.8m came in below the street and our estimate of RM51.2m and RM52.2m, respectively; making up only about 17% of both estimates. The underperformance was mainly due to the lower sales during the Ramadan month and higher base effect from aggressive promotions in the previous quarter.  |
| <b>Dividends</b>               | ▪ No dividend was declared in the quarter.   |
| <b>Key Result Highlights</b>   | <ul style="list-style-type: none"> <li>▪ <b>QoQ</b>, 1Q14 revenue declined by 24%, of which a 4% improvement in the wholesale division was insufficient to cushion the decline in multi-level marketing "MLM" (-27% QoQ), retail (-42% QoQ) and others (-9% QoQ). In line with the fall in revenue, its PBT and NP decreased by 20% and 13% QoQ respectively. MLM saw a major drop in sales due mainly to the incentive trip campaign promotion which took place in 4Q13, which had boosted the sales to register a record high in FY13. As a result, the 1Q14 sales shrunk post promotion coupled with a longer 21-day month with Ramadan falling within the quarter. On the other hand, retail sales fell drastically due to the absent of CNY festive season coupled with year-end members' sales that generated higher revenue in previous quarter.</li> <li>▪ <b>YoY</b>, its 1Q14 revenue dropped by 10% on the back of the decline in MLM (-17% YoY), retail (-7% YoY) and others (-17% YoY) despite a 10% increase in wholesale revenue. As mentioned above, MLM suffered in the quarter mainly due to the special price promotion on foundation garments in FY13 despite additional sales generated from the new wellness and health food products, which are small ticket items compared to the foundation garments. Its PBT and NP moved in line with revenue and dropped by 15% and 14% YoY, respectively. The substantial decline was caused by EBIT margin compression in MLM (-2.6ppts YoY) and a loss in the retail segment. The company saw weakening of domestic purchasing power which results in lower demand in retail division. In addition, due to higher operating costs such as rental, the division slipped into the red for the quarter.</li> </ul> |
| <b>Outlook</b>                 | ▪ The company will continue to introduce new products in the 2Q14 for its MLM division and is in the midst of introducing trip incentive program for distributors and reintroducing special price promotion for one of its key products. Hence, we remain positive on Hai-O's prospect as we anticipate its MLM segment to continue delivering decent earnings growth from a lower base through its continuous effort to enhance its product mix and expand new market channels through the recruitment of more members.   |
| <b>Change to Forecasts</b>     | ▪ We believe the underperformance was just a timing issue. Hence, we are maintaining our earnings forecasts for now.   |
| <b>Rating</b>                  | <b>Maintain OUTPERFORM</b>   |
| <b>Valuation</b>               | ▪ We are maintaining our TP of RM3.00 based on an unchanged PER of 11.8x over FY14E EPS of 25.8 sen.   |
| <b>Risks to our call</b>       | ▪ Weakening purchasing power and Ringgit.  |

### Share Price Performance



KLCI	1792.91
YTD KLCI chg	6.2%
YTD stock price chg	22.8%

### Stock Information

Bloomberg Ticker	HAIO MK Equity
Market Cap (RM m)	539.5
Issued shares	196.9
52-week range (H)	2.85
52-week range (L)	1.97
3-mth avg daily vol:	193,395
Free Float	77%
Beta	1.0

### Major Shareholders

KAI HEE TAN	9.9%
AKINTAN SDN BHD	7.6%
EXCELLANT COMMUNICAT	5.3%

### Summary Earnings Table

FY Apr (RM'm)	2013A	2014E	2015E
Turnover	267.9	302.9	335.2
EBIT	63.5	70.3	76.8
PBT	64.1	70.8	77.5
<b>Net Profit (NP)</b>	47.4	52.2	57.1
Consensus (NP)	-	51.2	57.6
Earnings Revision	-	-	-
EPS (sen)	16.82	23.46	25.80
EPS growth (%)	19.9	39.5	10.0
NDPS (sen)	9.00	14.00	14.25
BVPS (RM)	1.16	1.26	1.38
NTA/Share (RM)	1.11	1.20	1.32
PER (X)	16.29	11.68	10.62
Price/NTA (x)	2.46	2.28	2.07
Net Gearing (x)	N.Cash	N.Cash	N.Cash
Dividend Yield (%)	3.3%	5.1%	5.2%

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**Result Highlight**

FY Apr (RM'm)	1Q FY14	4Q FY13	QoQ Chg	1Q FY13	YoY Chg	3M FY14	3M FY13	YoY Chg
Turnover	54.7	72.1	-24%	60.6	-10%	54.7	60.6	-10%
PBT	11.8	14.7	-20%	13.8	-15%	11.8	13.8	-15%
Taxation	-3.1	-4.2	-27%	-3.5	-12%	-3.1	-3.5	-12%
Minority interest	0.1	-0.4	-117%	-0.1	-202%	0.1	-0.1	-202%
<b>Net Profit (NP)</b>	<b>8.8</b>	<b>10.1</b>	<b>-13%</b>	<b>10.3</b>	<b>-14%</b>	<b>8.8</b>	<b>10.3</b>	<b>-14%</b>
EPS (sen)	4.3	5.0	-13%	5.1	-14%	4.3	5.1	-14%
PBT margin	21.6%	20.3%		22.8%		21.6%	22.8%	
NP margin	16.1%	14.0%		17.0%		16.1%	17.0%	
Effective tax rate	26.0%	28.6%		25.2%		26.0%	25.2%	

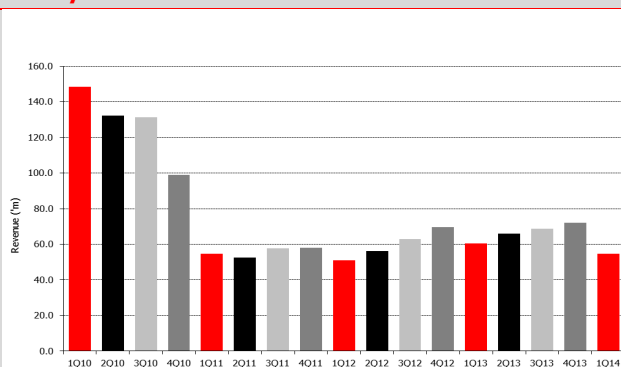
Source: Company, Kenanga Research

**Segmental Breakdown**

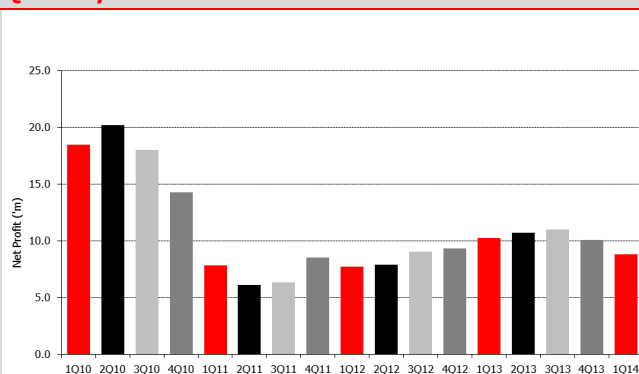
FY Apr (RM'm)	1Q FY14	4Q FY13	QoQ Chg	1Q FY13	YoY Chg	3M FY14	3M FY13	YoY Chg
- Multi-Level-Marketing	33.5	45.9	-27%	40.1	-17%	33.5	40.1	-17%
- Wholesale	12.2	11.7	4%	11.1	10%	12.2	11.1	10%
- Retail	7.4	12.7	-42%	8.0	-7%	7.4	8.0	-7%
- Others	1.6	1.8	-9%	2.0	-17%	1.6	2.0	-17%
Group Revenue	54.7	72.1	-24%	61.1	-11%	54.7	61.1	-11%
- Multi-Level-Marketing	5.3	8.1	-35%	7.4	-29%	5.3	7.4	-29%
- Wholesale	4.8	3.3	45%	3.8	27%	4.8	3.8	27%
- Retail	-0.2	1.4	-111%	0.3	-154%	-0.2	0.3	-154%
- Others	1.3	1.1	17%	1.7	-28%	1.3	1.7	-28%
- Elimination	0.3	0.4	-24%	0.6	-39%	0.3	0.6	-39%
Group EBIT	11.6	14.4	-19%	13.8	-16%	11.6	13.8	-16%
- Multi-Level-Marketing	15.8%	17.7%		18.4%		15.8%	18.4%	
- Wholesale	39.8%	28.6%		34.2%		39.8%	34.2%	
- Retail	-2.1%	10.7%		3.6%		-2.1%	3.6%	
- Others	77.1%	60.1%		88.7%		77.1%	88.7%	
Group EBIT Margin	21.1%	19.9%		22.5%		21.1%	22.5%	

Source: Company, Kenanga Research

**Quarterly Revenue**



**Quarterly NP**



Source: Bloomberg, Kenanga Research

Income Statement						Financial Data & Ratios					
FY Apr (RM m)	2011A	2012A	2013A	2014E	2015E	FY Apr (RM m)	2011A	2012A	2013A	2014E	2015E
Revenue	223.3	239.5	267.9	302.9	335.2	<b>Growth</b>					
EBITDA	44.0	51.4	66.5	73.0	79.7	Turnover (%)	-56.3%	7.3%	11.9%	13.1%	10.7%
Depreciation	2.70	2.75	2.94	2.79	2.92	EBITDA (%)	-55.3%	17.0%	29.2%	9.9%	9.1%
Operating Profit	41.3	48.7	63.5	70.3	76.8	Op. Profit (%)	-56.9%	18.0%	30.5%	10.6%	9.3%
Other Income	0.9	0.8	1.2	1.2	1.3	PBT (%)	-56.8%	18.1%	31.4%	10.4%	9.5%
Interest Exp	-0.8	-0.7	-0.6	-0.6	-0.6	Core Net Profit(%)	-59.8%	19.9%	39.5%	10.0%	9.5%
PBT	41.3	48.8	64.1	70.8	77.5	<b>Profitability (%)</b>					
Taxation	-11.6	-13.1	-15.8	-17.7	-19.4	EBITDA Margin	19.7%	21.5%	24.8%	24.1%	23.8%
Minority Interest	1.3	1.7	0.9	0.9	1.0	Operating Margin	18.5%	20.3%	23.7%	23.2%	22.9%
Net Profit	28.4	34.0	47.4	52.2	57.1	PBT Margin	18.5%	20.4%	23.9%	23.4%	23.1%
						Core Net Margin	13.8%	12.7%	14.2%	17.7%	17.2%
						Effective Tax Rate	28.0%	26.8%	24.7%	25.0%	25.0%
						ROA	11.0%	11.7%	15.5%	15.5%	15.5%
						ROE	13.9%	15.3%	19.8%	19.8%	19.8%
						<b>DuPont Analysis</b>					
						Net Margin (%)	13%	14%	18%	17%	17%
						Assets Turnover(x)	0.87	0.83	0.87	0.90	0.91
						Leverage Factor(x)	1.21	1.25	1.22	1.22	1.22
						ROE (%)	14%	15%	20%	20%	20%
						<b>Leverage</b>					
						Debt/Asset (x)	0.06	0.05	0.04	0.04	0.04
						Debt/Equity (x)	0.08	0.06	0.05	0.05	0.05
						Net Cash/(Debt)	29.64	40.90	51.51	78.03	99.35
						Net Debt/Equity	N.Cash	N.Cash	N.Cash	N.Cash	N.Cash
						<b>Valuations</b>					
						EPS (sen)	14.03	16.82	23.46	25.80	28.24
						NDPS (sen)	7.50	9.00	14.00	14.25	15.84
						NTA/share (RM)	1.02	1.11	1.20	1.32	1.45
						PER (x)	19.53	16.29	11.68	10.62	9.70
						Net Div. Yield (%)	2.7%	3.3%	5.1%	5.2%	5.8%
						P/NTA (x)	2.68	2.46	2.28	2.07	1.89
						EV/EBITDA (x)	11.93	9.98	7.56	6.52	5.70

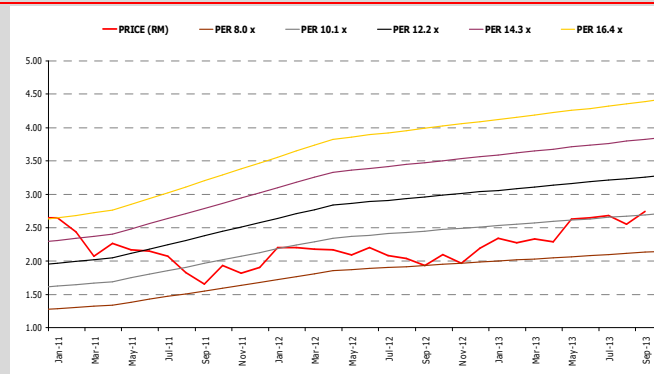
Balance Sheet					
FY Apr (RM m)	2011A	2012A	2013A	2014E	2015E
Fixed Assets	72.2	62.1	66.7	64.6	65.7
Inv. Properties	33.2	45.2	46.3	46.3	46.3
Other FA	4.7	5.1	4.6	4.6	4.6
Inventories	44.3	37.8	49.9	48.5	53.6
Receivables	19.1	21.9	20.3	27.3	30.2
Other CA	37.4	63.4	53.8	53.8	53.8
Cash	46.1	54.2	64.9	90.9	114.2
Total Assets	257.0	289.6	306.5	336.0	368.5
Payables	22.6	32.5	35.2	40.9	45.3
ST Borrowings	5.7	5.2	7.4	5.0	6.0
Other ST Liability	5.2	12.4	6.9	6.9	6.9
LT Borrowings	10.7	8.1	6.0	7.9	8.9
Other LT Liability	0.1	0.0	0.1	0.1	0.1
Minorities Int.	8.3	9.7	11.1	12.0	13.1
<b>Net Assets</b>	<b>204.4</b>	<b>221.7</b>	<b>239.7</b>	<b>263.1</b>	<b>288.2</b>
Share Capital	101.1	101.1	101.1	101.1	101.1
Treasury Shares	-4.3	-5.9	-9.7	-9.7	-9.7
Reserves	107.6	126.5	148.4	171.7	196.8
<b>Equity</b>	<b>204.4</b>	<b>221.7</b>	<b>239.7</b>	<b>263.1</b>	<b>288.2</b>

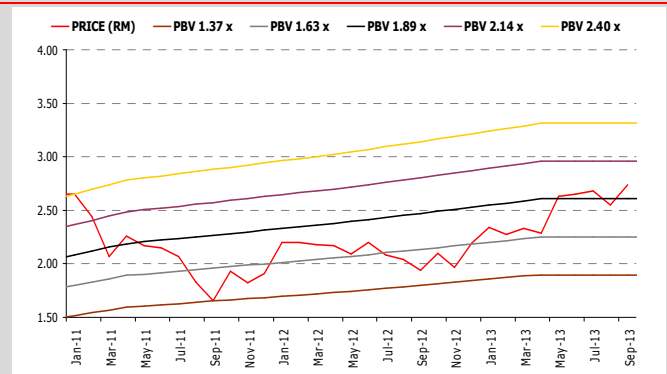
Cashflow Statement					
FY Apr (RM m)	2011A	2012A	2013A	2014E	2015E
Operating CF	13.9	50.0	51.0	43.3	44.1
Investing CF	-1.7	-21.4	4.4	-9.2	-9.2
Financing CF	-36.8	-20.5	-30.0	-28.2	-28.7
Change In Cash	-24.6	8.1	25.3	5.8	6.1

Source: Company, Kenanga Research

Forward PER



Forward PBV



Source: Bloomberg, Kenanga Research

**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 stock'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 stock's Expected Total Return is WITHIN the range of 3% to 10%  
UNDERWEIGHT : 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 are defined based on market capitalisation weighted average expected total return for stocks under our coverage.***

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Published and printed by:

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