

**Company Result**

18 December 2018

**Hai-O Enterprise Berhad**

**HOLD**

*Lower Margin ahead from MLM division*

**Downgraded**

<b>Share Price</b>	<b>RM2.90</b>
<b>Target Price</b>	<b>RM3.00</b>

**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)	290.39
Par Value (RM)	0.50
Market cap. (RMm)	842.13
52-week price Range	RM2.86 – 5.59
Beta (against KLCI)	0.84
3-m Average Daily Volume	0.26m
3-m Average Daily Value <sup>^</sup>	RM0.93m

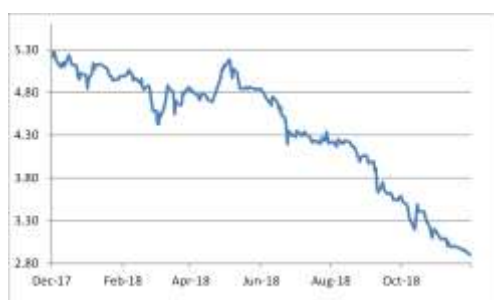
**Share Performance**

	1m	3m	12m
Absolute (%)	-9.4	-22.7	-46.4
Relative (%-pts)	-5.8	-24.0	-42.8

**Major Shareholders**

	%
Kai Hee Tan	10.14
Akintan Sdn Bhd	7.88
Excellent Communications	5.35

**Historical Chart**



Source: Bloomberg

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- **Hai-O reported a net profit of RM13.6m for its 2QFY19.** The quarterly net profit increased by 23.7% QoQ, whilst dropped by -36.6% YoY. Likewise, the Group recorded a quarterly revenue of RM92.2m, which increased 15.7% QoQ, but decreased -25.4% YoY.
- **For 6MFY19,** the Group attained a lower topline and bottomline of -30.6% and -37.4% respectively.
- **A better quarter but still disappointing for six months with result below expectations** by accounting for 30.0%/33.5% of our/consensus full year net earnings forecast. We deem the result below our expectation (2H net profit traditionally accounts for c.50~60% of actual full year net earnings).

**Comment**

- **Better earnings QoQ due to higher revenue achieved in tandem with better EBIT margin.** A better EBIT of 27% recorded in 2QFY19 as compared to 1QFY19 mainly due to increase in sale from MLM, wholesale and retail division. Meanwhile, a better EBIT margin, +1.8ppts, was contributed by small-ticket items with lower cost of sales and lower marketing cost from MLM division.
- **Disappointing YoY earnings as a result of weaker topline and bottomline.** The better revenue recorded from the wholesale and retail divisions was offset by the lower revenue from MLM. Moreover, the lower EBIT/EBIT margin, -34.4%/-2.7ppts, no thanks to one-off 6% rebate promotion prior to abolishment of GST which was absorbed by the MLM division and higher CSR cost from the wholesale division.
- **Lower 1HFY19 due to lower sales and margin.** Again, the lower revenue was mainly due to lower sales in MLM division. Also, it was partially affected by the impact of MFRS 9 and MFRS 15 which took effect in FY2018. Meanwhile, a weaker EBIT margin which offset a better gross margin no thanks to higher marketing and branding costs, one-off 6% rebate promotion prior to the abolishment of GST and higher CSR cost.
- **MLM division – Continuous expansion.** The Group continues focusing on new product development to widen its product range. It will launch a promotional and incentive campaign in 2HFY19.
- **Wholesale and retail – sales promotional campaign.** Extensive CNY promotional campaign via social media platforms to target younger and wider group of customers.

- **Neutral Outlook for 2HFY19.** Although higher revenue is anticipated for the CNY festive season, we expect a lower margin in 2HFY19 as the Group will continue its product development for MLM division, along with higher cost incurred for the CNY promotional campaign for both whole and retail divisions.
- **Risks include:** 1) Higher marketing and advertising of new products under the MLM division, and 2) Lower revenue due to weak consumer sentiment post implementation of SST.

### Earnings Outlook/Revision

- **We reduce our earnings forecasts for FY19F by 15.5% and FY20F by 25.0%** as we foresee the Group's revenue will be affected by SST along with the longer time and cost required for new product development for the MLM division. Meanwhile, higher cost is needed for the marketing and branding to build its beauty brand "infinence" and lifestyle related range of products.

### Valuation & Recommendation

- **Downgrade to HOLD from BUY with a lower target price of RM3.00** (previous target price: RM4.76) after our earnings cut and applying lower PE multiple. Our revised target price is now pegged at 13.1x PE FY19F EPS (from 14.3x), which is at its mean forward PE.

**Figure 1: Quarterly Figures**

Year ended 30 April	2QFY19	1QFY19	2QFY18	QoQ	YoY	6MFY19	6MFY18	YoY
	RM'm	RM'm	RM'm	%	%	RM'm	RM'm	%
Revenue	92.2	80.1	123.5	15.1%	-25.4%	172.3	248.1	-30.6%
Gross profit	35.7	32.2	42.7	10.9%	-16.4%	67.8	83.8	-19.0%
Operating profit	18.0	14.2	27.4	27.0%	-34.4%	32.2	50.3	-36.0%
PBT	18.3	14.4	27.9	26.5%	-34.4%	32.7	51.0	-35.8%
PAT	13.9	10.7	21.6	30.0%	-35.9%	24.5	39.2	-37.5%
Net profit	13.6	11.0	21.4	23.7%	-36.6%	24.6	39.3	-37.4%
<b>Margin (%)</b>				<b>ppts</b>	<b>ppts</b>			<b>ppts</b>
Gross profit margin	38.7%	40.2%	34.6%	-1.5	4.1	39.4%	33.8%	5.6
EBIT margin	19.5%	17.7%	22.2%	1.8	-2.7	18.7%	20.3%	-1.6
PBT margin	19.8%	18.0%	22.5%	1.8	-2.7	19.0%	20.5%	-1.6
PAT margin	15.0%	13.3%	17.5%	1.7	-2.5	14.2%	15.8%	-1.6
Net profit margin	14.8%	13.7%	17.4%	1.0	-2.6	14.3%	15.8%	-1.6

Source: Company, JF Apex

**Figure 2: Revenue and PBT by division**

Year ended 30 April	2QFY19 RM'000	1QFY19 RM'm	2QFY18 RM'000	QoQ %	YoY %
MLM division	63.2	58.0	95.5	9.0%	-33.8%
Wholesale division	17.1	13.6	16.5	25.7%	3.6%
Retail division	10.8	7.6	10.4	42.1%	3.8%
<b>Total Revenue</b>	<b>91.1</b>	<b>79.2</b>	<b>122.4</b>	<b>15.0%</b>	<b>-25.6%</b>
MLM division	14.3	10.3	19.9	38.8%	-28.1%
Wholesale division	2.4	3.7	6.2	-35.1%	-61.3%
Retail division	0.6	(0.6)	0.5	N/A	20.0%
<b>Total PBT</b>	<b>17.3</b>	<b>13.4</b>	<b>26.6</b>	<b>29.1%</b>	<b>-35.0%</b>
<b>PBT margin (%)</b>				<b>ppts</b>	<b>ppts</b>
MLM division	22.6%	17.8%	20.8%	4.9	1.8
Wholesale division	14.0%	27.2%	37.6%	-13.2	-23.5
Retail division	5.6%	-7.9%	4.8%	13.5	0.7

Source: Company, JF Apex

**Figure 3: Peer Comparison**

Company	Price RM	Recom	T.price RM	P/E		P/B	P/S	PBT margin %	Div Yield %
				19'	20'				
Hai-O	4.0	BUY	6.14	11.7	9.9	2.8	1.8	20.9	3.8
Amway	6.7	-	-	25.0	23.6	5.3	1.1	7.2	3.1

Source: Company, JF Apex

**Figure 4: Financial Summary**

Year ended 30 April	FY15	FY16	FY17	FY18	FY19F	FY20F
	RMm	RMm	RMm	RMm	RMm	RMm
Revenue	239.9	297.6	404.0	461.8	533.8	546.3
Gross profit	85.6	101.4	132.9	162.2	178.4	196.3
Operating profit	42.2	48.3	77.3	97.6	99.4	119.1
PBT	43.0	49.1	78.1	99.0	100.3	120.2
PAT	30.8	36.6	59.2	75.1	69.3	85.2
Net profit	30.1	36.3	59.3	75.4	69.1	85.0
<b>Margin (%)</b>						
Gross profit margin	35.7%	34.1%	32.9%	35.1%	33.4%	35.9%
Operating profit	17.6%	16.2%	19.1%	21.1%	18.6%	21.8%
PBT margin	17.9%	16.5%	19.3%	21.4%	18.8%	22.0%
PAT margin	12.8%	12.3%	14.7%	16.3%	13.0%	15.6%
Net profit margin	12.5%	12.2%	14.7%	16.3%	13.0%	15.6%
<b>Growth (%)</b>						
Revenue growth	-5.4%	24.1%	35.7%	14.3%	15.6%	2.3%
Gross Profit growth	-8.5%	18.5%	31.0%	22.1%	10.0%	10.0%
PBT growth	-19.7%	14.0%	59.2%	26.8%	1.3%	19.8%
PAT growth	-25.6%	18.9%	61.9%	26.9%	-7.7%	22.9%
Net profit growth	-25.4%	20.8%	63.1%	27.2%	-8.3%	22.9%
Net gearing	Net cash	Net cash	Net cash	Net cash	Net cash	Net cash
ROA	9.8%	11.3%	16.3%	19.1%	15.0%	17.3%
ROE	11.3%	13.5%	20.0%	23.7%	18.5%	21.5%
EPS (sen)	10.4	12.1	19.8	25.2	23.1	28.4
P/E	28.0	23.9	14.6	11.5	12.5	10.2
DPS (sen)	10.0	10.0	16.0	16.0	16.0	16.0
Dividend Payout	96.4%	82.3%	80.8%	63.5%	69.2%	56.3%
Dividend yield (%)	3.4%	3.4%	5.5%	5.5%	5.5%	5.5%

Source: Company, JF Apex

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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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