

Downgrading: Dwindling MLM prospects

Hai-O's FY19 results missed expectations. Core net profit fell 34% yoy, accounting for only 94% of our and consensus' full-year estimates. Sales slumped 29% yoy while margins also recorded a dip, primarily driven by the MLM segment's bleak performance. Heading into FY20, the group's prospects remain challenged by tough operating conditions afflicting its MLM business, in our view. We cut FY20-21E EPS forecasts by 20-26% and subsequently downgrade Hai-O to a SELL (from Hold), with a lower TP of RM1.80.

Below expectations

Hai-O's FY19 core net profit declined 34% yoy to RM47.4m, as sales in its MLM segment fell 36% yoy amid depressed distributor activity and a shift in product mix towards smaller ticket items, which overall contributed to a 1.6ppts yoy decline in group EBIT margin despite better margins for small-ticket items. Both the Wholesale and Retail segments recorded lower revenue as well (-7% / -2% yoy respectively), led by a drop in sales for non-patented medicine products for the former, and lower sales of premium food supplements for the latter. On a brighter note, dividend payout remained high at c.80%, bringing FY19 DPS to 13sen (FY18: 20sen).

Incentive trip campaign failed to revitalise MLM sales

4QFY19's bleak MLM performance fell short of our expectation for a sequential recovery. Sales further declined 16% qoq to a multi-year low last seen in 2QFY16, while membership recruitment and renewal remained lacklustre. This came despite Hai-O's launch of its overseas incentive trip campaign (Melbourne) during the quarter, alongside other promotions such as its monthly flash sales program launched in March. We infer that the group could be bleeding market share amid an overall plateauing direct selling market, whereas 1QCY19 sales held up for the market leader, Amway. This is possibly due to less excitement for Hai-O's recently launched products such as its relatively new Infinence brand fashionwear while Amway retains a reputable brand image in the local market.

Downgrade to SELL

We cut our FY20-21E EPS estimates by -20%/-26% respectively, mainly to account for structural challenges seen hampering Hai-O's MLM segment – its key earnings driver. Subsequently, we ascribe a lower TP of RM1.80 (from RM2.50) after pegging a lower FY20E PER multiple of 12x (from 13x) based on -1SD of its 3-year historical average. Thereafter, we downgrade Hai-O to a SELL (from Hold). Upside risks: i) recovery in MLM distributor base; ii) better-than-expected take-up rate for its new products.

Earnings & Valuation Summary

FYE 30 Apr	2018	2019	2020E	2021E	2022E
Revenue (RMm)	461.7	328.4	318.2	325.8	333.5
EBITDA (RMm)	99.0	67.0	62.1	65.8	68.0
Pretax profit (RMm)	96.5	63.5	58.3	62.1	64.3
Net profit (RMm)	72.3	47.4	44.0	46.9	48.6
EPS (sen)	24.9	16.3	15.1	16.1	16.7
PER (x)	9.0	13.7	14.8	13.9	13.4
Core net profit (RMm)	72.3	47.4	44.0	46.9	48.6
Core EPS (sen)	24.9	16.3	15.1	16.1	16.7
Core EPS growth (%)	21.7	-34.4	-7.2	6.4	3.6
Core PER (x)	9.0	13.7	14.8	13.9	13.4
Net DPS (sen)	20.0	13.0	11.4	12.1	12.5
Dividend Yield (%)	8.9	5.8	5.1	5.4	5.6
EV/EBITDA (x)	5.3	8.3	8.8	8.1	7.7
Chg in EPS (%)			(20.3)	(26.2)	-
Affin/Consensus (x)			0.8	0.7	-

Source: Company, Bloomberg, Affin Hwang forecasts

Outthink. Outperform.

Results Note

Hai-O

HAIO MK
Sector: Consumer

RM2.24 @ 25 June 2019

SELL (downgrade)

Downside: 20%

Price Target: RM1.80

Previous Target: RM2.50



Price Performance

	1M	3M	12M
Absolute	-5.5%	-17.0%	-53.7%
Rel to KLCI	-9.9%	-18.4%	-53.7%

Stock Data

Issued shares (m)	290.4
Mkt cap (RMm)/(US\$m)	650.4/156.9
Avg daily vol - 6mth (m)	0.2
52-wk range (RM)	2.2-4.95
Est free float	55.3%
BV per share (RM)	1.03
P/BV (x)	2.17
Net cash/ (debt) (RMm)	90.2
ROE (2019E)	16.3%
Derivatives	Nil
Shariah Compliant	No

Key Shareholders

Kai Hee Tan	10.2%
Akintan Sdn Bhd	8.1%
Excellent Communication	5.4%

Source: Affin Hwang, Bloomberg

Lester Siew
(603) 2146 7502
lester.siew@affinhwang.com

Outthink. Outperform.

Fig 1: Results Comparison

FYE Apr (RMm)	4Q FY18	3Q FY19	4Q FY19	QoQ % chg	YoY % chg	FY18	FY19	YoY % chg	Comments
Revenue	110.6	86.2	69.9	(18.8)	(36.7)	461.7	328.4	(28.9)	Substantial sales decline in FY19, primarily led by the MLM segment (-36.2% yoy), followed by the Wholesale (-7.5% yoy) and Retailing segments (-2.2% yoy)
Op costs	(87.4)	(68.2)	(55.4)	(18.9)	(36.6)	(362.7)	(261.3)	(27.9)	
EBITDA	23.2	17.9	14.6	(18.6)	(37.1)	99.0	67.0	(32.3)	
EBITDA margin (%)	21.0	20.8	20.8	0ppt	-0.1ppt	21.4	20.4	-1ppt	
Depn and amort	(1.1)	(1.3)	(1.0)	(19.3)	(6.4)	(4.0)	(4.6)	14.7	
EBIT	22.1	16.7	13.6	(18.6)	(38.6)	94.9	62.4	(34.3)	
EBIT margin (%)	20.0	19.3	19.4	0.1ppt	-0.6ppt	20.6	19.0	-1.6ppt	Lower margins despite 1.5ppt improvement in gross margin, as sales tumbled while marketing/branding costs increased. Additional impact from one-off GST rebate (RM0.9m) and higher CSR costs amounting to RM1.4m
Int expense	(0.0)	(0.0)	(0.0)	(43.8)	157.1	(0.1)	(0.1)	8.5	
Int and other inc	0.4	0.3	0.4	22.2	(19.8)	1.7	1.2	(25.7)	
Associates	(0.0)	0.0	(0.0)	n.m.	n.m.	0.0	0.0	166.7	
Exceptional items	0.0	0.0	0.0	n.m.	n.m.	0.0	0.0	n.m.	
Pretax	22.5	16.9	13.9	(18.0)	(38.3)	96.5	63.5	(34.2)	
Tax	(6.4)	(4.1)	(4.0)	(2.0)	(37.2)	(24.0)	(16.4)	(31.8)	
Tax rate (%)	28.6	24.4	29.1	4.8ppt	0.5ppt	24.8	25.8	0.9ppt	
MI	(0.4)	(0.0)	0.2	n.m.	n.m.	(0.3)	0.3	(198.9)	
Net profit	15.7	12.8	10.0	(21.6)	(36.1)	72.3	47.4	(34.4)	
EPS (sen)	5.4	4.4	3.4	(21.6)	(36.1)	24.9	16.3	(34.4)	
Core net profit	15.7	12.8	10.0	(21.6)	(36.1)	72.3	47.4	(34.4)	Below our and consensus estimates, accounting for 94% of both full-year forecasts

Source: Affin Hwang, Company data

Fig 2: Segmental Breakdown

	4QFY18	3QFY19	4QFY19	QoQ % chg	YoY % chg	FY18	FY19	YoY % chg
Segmental Revenue								
MLM	79.10	56.27	47.43	(15.7)	(40.0)	352.55	224.89	(36.2)
Wholesale	17.02	16.22	11.99	(26.1)	(29.6)	63.66	58.91	(7.5)
Retail	13.67	12.55	9.57	(23.7)	(30.0)	41.48	40.56	(2.2)
Others	0.85	1.12	0.95	(15.0)	11.4	4.10	3.99	(2.6)
Total revenue	110.56	86.16	69.94	(18.8)	(36.7)	461.78	328.35	(28.9)
Segmental Profit*								
MLM	16.59	11.88	10.18	(14.3)	(38.6)	69.07	46.45	(32.7)
Wholesale	3.45	3.08	1.34	(56.5)	(61.2)	22.17	10.20	(54.0)
Retail	1.39	0.46	0.41	(11.7)	(70.7)	1.47	0.84	(43.1)
Others	1.21	1.40	1.06	(24.3)	(12.4)	5.08	4.29	(15.5)
	22.09	16.65	13.56	(18.6)	(38.6)	97.80	61.78	(36.8)

Source: Affin Hwang, Company data

*Total segmental profit differs from group EBIT due to elimination

Important Disclosures and Disclaimer

Outthink. Outperform.

Equity Rating Structure and Definitions

BUY	Total return is expected to exceed +10% over a 12-month period
HOLD	Total return is expected to be between -5% and +10% over a 12-month period
SELL	Total return is expected to be below -5% over a 12-month period
NOT RATED	Affin Hwang Investment Bank Berhad does not provide research coverage or rating for this company. Report is intended as information only and not as a recommendation

The total expected return is defined as the percentage upside/downside to our target price plus the net dividend yield over the next 12 months.

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

This report is intended for information purposes only and has been prepared by Affin Hwang Investment Bank Berhad (14389-U) ("the Company") based on sources believed to be reliable and is not to be taken in substitution for the exercise of your judgment. You should obtain independent financial, legal, tax or such other professional advice, when making your independent appraisal, assessment, review and evaluation of the company/entity covered in this report, and the extent of the risk involved in doing so, before investing or participating in any of the securities or investment strategies or transactions discussed in this report. However, such sources have not been independently verified by the Company, and as such the Company does not give any guarantee, representation or warranty (expressed or implied) as to the adequacy, accuracy, reliability or completeness of the information and/or opinion provided or rendered in this report. Facts, information, estimates, views and/or opinion presented in this report have not been reviewed by, may not reflect information known to, and may present a differing view expressed by other business units within the Company, including investment banking personnel and the same are subject to change without notice. Reports issued by the Company, are prepared in accordance with the Company's policies for managing conflicts of interest. Under no circumstances shall the Company, be liable in any manner whatsoever for any consequences (including but are not limited to any direct, indirect or consequential losses, loss of profit and damages) arising from the use of or reliance on the information and/or opinion provided or rendered in this report. Under no circumstances shall this report be construed as an offer to sell or a solicitation of an offer to buy any securities. The Company its directors, its employees and their respective associates may have positions or financial interest in the securities mentioned therein. The Company, its directors, its employees and their respective associates may further act as market maker, may have assumed an underwriting commitment, deal with such securities, may also perform or seek to perform investment banking services, advisory and other services relating to the subject company/entity, and may also make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report. The Company, its directors, its employees and their respective associates, may provide, or have provided in the past 12 months investment banking, corporate finance or other services and may receive, or may have received compensation for the services provided from the subject company/entity covered in this report. No part of the research analyst's compensation or benefit was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report. Employees of the Company may serve as a board member of the subject company/entity covered in this report.

Third-party data providers make no warranties or representations of any kind relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability for any damages of any kind relating to such data.

This report, or any portion thereof may not be reprinted, sold or redistributed without the written consent of the Company.

This report is printed and published by:
 Affin Hwang Investment Bank Berhad (14389-U)
 A Participating Organisation of Bursa Malaysia Securities Berhad

22nd Floor, Menara Boustead,
 69, Jalan Raja Chulan,
 50200 Kuala Lumpur, Malaysia.

T : + 603 2142 3700
 F : + 603 2146 7630
 research@affinhwang.com

www.affinhwang.com