

No reprieve in sight for its MLM business

Hai-O posted a disappointing set of 1QFY20 results. Earnings fell 30% yoy as MLM sales slumped 28% yoy to a 4-year low during the quarter. Better performances posted by its other segments failed to provide much respite due to their minor contributions to group earnings. We cut FY20-22E earnings by 16-18% respectively in view of the unabating weakness faced by the MLM segment. We believe the recent share-price rally is thus unwarranted given this weak set of results. Maintain **SELL** with a lower 12-month TP of RM1.60 (from RM1.80).

Below expectations

Hai-O's 1QFY20 core net profit tumbled 29.6% yoy to RM7.7m as sales from its MLM segment fell for the seventh consecutive quarter yoy to RM42.1m – a four-year low since 1QFY16, despite having over 120k distributors at end-FY19 vs. 83k distributors at end-FY16. This was exacerbated by a 2.6ppts slip in the EBIT margin, led by a 2.0ppts gross margin decline on unfavourable sales mix. Increased revenue recorded for its Wholesale (+9.3% yoy), Retail (+6.7% yoy) and Others (+20.7% yoy) segments provided little relief, as they collectively account for only 20-30% of group earnings. Overall, the results were below both market and our expectations, at 17% and 18% of FY20E forecasts respectively.

Sequentially weaker

On a sequential basis, core net profit declined 22.7% qoq, as MLM sales declined 11.3% qoq owing to the Ramadan fasting period in May and a continued slowdown in members' activities, while the response from the February-May 2019 incentive trip campaign was not encouraging. Hai-O has initiated another incentive trip campaign running from July-October 2019, while management is in the midst of reviewing its core business strategies amidst the string of successively weaker performances. We remain wary of its MLM segment's prospects due to a less favourable range of product offerings following management's pivot into the highly competitive fashion and apparel space.

Maintain SELL

We cut our FY20-22E EPS estimates by 16-18% respectively, as we pencil in further downside to earnings arising from its MLM business's persisting weakness. Subsequently, we derive a lower 12-month TP of RM1.60 (from RM1.80) after rolling forward our valuation base to FY21E but with an unchanged 12x PER target. Maintain **SELL**. Current yields of 3.6%-4.1% look unattractive in view of the bearish earnings outlook. Upside risks: i) recovery in MLM distributor base; ii) better-than-expected take-up rate for its new products; and (iii) higher cost savings.

Earnings & Valuation Summary

FYE 30 Apr	2018	2019	2020E	2021E	2022E
Revenue (RMm)	461.7	328.4	287.3	294.7	302.2
EBITDA (RMm)	99.0	66.9	51.7	54.8	58.0
Pretax profit (RMm)	96.5	63.4	47.9	51.0	54.3
Net profit (RMm)	72.3	47.7	36.2	38.5	41.0
EPS (sen)	24.9	16.4	12.4	13.3	14.1
PER (x)	11.0	16.6	21.9	20.6	19.4
Core net profit (RMm)	72.3	47.7	36.2	38.5	41.0
Core EPS (sen)	24.9	16.4	12.4	13.3	14.1
Core EPS growth (%)	21.7	-33.9	-24.3	6.5	6.3
Core PER (x)	11.0	16.6	21.9	20.6	19.4
Net DPS (sen)	20.0	13.0	10.0	10.6	11.3
Dividend Yield (%)	7.3	4.8	3.6	3.9	4.1
EV/EBITDA (x)	6.7	10.4	13.3	12.4	11.6
Chg in EPS (%)			(17.8)	(17.8)	(15.6)
Affin/Consensus (x)			0.8	0.8	0.8

Source: Company, Bloomberg, Affin Hwang forecasts

Outthink. Outperform.

Results Note

Hai-O

HAIO MK
Sector: Consumer

RM2.73 @ 26 September 2019

SELL (maintain)

Downside: 41%

Price Target: RM1.60

Previous Target: RM1.80



Price Performance

	1M	3M	12M
Absolute	26.4%	21.9%	-32.4%
Rel to KLCI	27.0%	28.1%	-23.7%

Stock Data

Issued shares (m)	290.4
Mkt cap (RMm)/(US\$m)	792.7/189.0
Avg daily vol - 6mth (m)	0.2
52-wk range (RM)	2.1-4.09
Est free float	55.8%
BV per share (RM)	1.03
P/BV (x)	2.64
Net cash/ (debt) (RMm)	94.8
ROE (2020E)	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

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Fig 1: Results Comparison

FYE Apr (RMm)	1QFY19	4QFY19	1QFY20	QoQ % chg	YoY % chg	Comments
Revenue	80.1	69.9	66.1	(5.5)	(17.5)	Slump in MLM sales (-27.5% yoy) partially offset by improved Wholesale (+9.3% yoy) and Retail (+6.7% yoy) segment sales
Op costs	(64.8)	(55.4)	(54.5)	(1.5)	(15.8)	
EBITDA	15.3	14.6	11.5	(20.8)	(24.6)	
<i>EBITDA margin (%)</i>	<i>19.1</i>	<i>20.8</i>	<i>17.5</i>	<i>-3.4ppt</i>	<i>-1.6ppt</i>	
Depn and amort	(1.1)	(1.0)	(1.6)	53.2	36.9	
EBIT	14.2	13.6	10.0	(26.3)	(29.5)	
<i>EBIT margin (%)</i>	<i>17.7</i>	<i>19.4</i>	<i>15.1</i>	<i>-4.3ppt</i>	<i>-2.6ppt</i>	Led by a 2ppts decline in gross margins and lower A&P subsidy income from suppliers
Int expense	(0.1)	(0.0)	(0.1)	277.8	30.8	
Int and other inc	0.3	0.4	0.3	(27.6)	(19.0)	
Associates	0.0	(0.0)	0.0	n.m.	n.m.	
Exceptional items	0.0	0.0	0.0	n.m.	n.m.	
Pretax	14.4	13.9	10.2	(26.5)	(29.4)	
Tax	(3.8)	(4.0)	(2.7)	(34.0)	(29.4)	
<i>Tax rate (%)</i>	<i>26.2</i>	<i>29.1</i>	<i>26.2</i>	<i>-3ppt</i>	<i>0ppt</i>	
MI	0.3	0.2	0.2	n.m.	n.m.	
Net profit	11.0	10.0	7.7	(22.7)	(29.6)	
EPS (sen)	3.8	3.4	2.7	(22.7)	(29.6)	
Core net profit	11.0	10.0	7.7	(22.7)	(29.6)	Below our and consensus estimates, accounting for 18% and 17% of full-year forecasts

Source: Affin Hwang, Company data

Fig 2: Segmental Breakdown

	1QFY19	4QFY19	1QFY20	QoQ % chg	YoY % chg
<u>Segmental Revenue</u>					
MLM	58.03	47.43	42.06	(11.3)	(27.5)
Wholesale	13.56	11.99	14.81	23.5	9.3
Retail	7.62	9.57	8.13	(15.1)	6.7
Others	0.88	0.95	1.06	11.6	20.7
Total revenue	80.09	69.94	66.06	(5.5)	(17.5)
<u>Segmental Profit*</u>					
MLM	10.37	10.18	7.12	(30.0)	(31.3)
Wholesale	2.72	1.34	1.34	(0.1)	(50.8)
Retail	(0.60)	0.41	(0.26)	(163.4)	(57.1)
Others	0.84	1.06	1.48	39.1	77.1
	14.17	13.56	9.99	(26.3)	(29.5)

Source: Affin Hwang, Company data

*Total segmental profit differs from group EBIT due to elimination

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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

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