Company Update

12 November 2019

Hai-O Enterprise Berhad

A watershed year

HOLD

Upgraded

Share Price	RM2.20
Target Price	RM2.30

Company Description

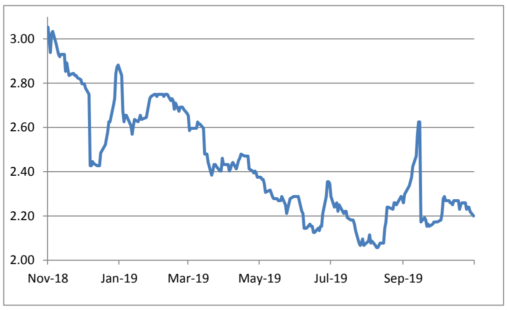
Hai-O Enterprise Berhad is offering a wide range of Chinese medicines, medicated tonic, wellness, beauty and healthcare.

Stock Data	
Bursa / Bloomberg code	7668 / HAIO MK
Board / Sector	Industrial/Food & Drug Retailers
Syariah Compliant status	No
Issued shares (m)	290.37
Par Value (RM)	0.50
Market cap. (RMm)	638.72
52-week price Range	RM2.11 – 3.30
Beta (against KLCI)	0.72
3-m Average Daily Volume	0.42m
3-m Average Daily Value^	RM0.99m

Share Performance	1m	3m	12m
Absolute (%)	-2.7	-3.5	-33.3
Relative (%-pts)	-5.8	2.8	-29.2

Major Shareholders	%
Kai Hee Tan	10.18
Akintan Sdn Bhd	8.05
Excellent Communications	5.36

Historical Chart



Source: Bloomberg

Nursuhaiza Hashim
03-87361118, ext. 752
nursuhaiza@jfapex.com.my

What's new

- **Neutral outlook**. We met Hai-O's management recently and came back feeling neutral about the Group's future prospects. Management remains conservative about current year outlook and pinning hopes that earnings will be better for 2HFY20. The Group believes contribution from Multi-Level Marketing (MLM) segment will be slightly better banking on introduction of few new products, mainly focusing on small-ticket items as well as implementation of cost optimisation strategy.

Comment

- **Better 2QFY20**. To recap, the Group's revenue and earnings during FY19 were tepid, down 28.9% yoy and 36.6% yoy respectively due to lower contribution from MLM division coupled with higher marketing and branding costs. On its recent financial results (1QFY20), Hai-O reported a net profit of RM7.7m, declining 22.7% qoq and 29.6% yoy. Similarly, the Group recorded lower quarterly revenue of RM66.1m, -5.5% qoq and -17.5% yoy. The disappointing results were due to lower sales generated from MLM division coupled with reduction in A&P subsidy incomes. Moving forward, we envisage 2QFY20 result to perform better than 1QFY20 following end of major festive season (which is normally lead to slow-down in business activities pursuant to fasting month and Hari Raya festival) coupled with launch of new products.

- **More new products under MLM to boost recurring income –** MLM division has been experienced a challenging results during FY19 due to domestic and global uncertainties such as re-introduction of sales and services tax (SST), tepid consumer sentiment as a result of rising cost of living. Numbers of membership has been depleted to c.100k as of to date (as compared to FY19: c.150k). Still, the Group is able to maintain its active membership of about 30%-40%. Despite expecting a marginal drop in recruitment of new members, the Group will continue to reward its current members with variety of rewards and incentives such as trip to overseas, cash rebates, monthly bonus and others. Notably, this business segment is mainly driven by its Food & Beverages and Health supplements & Nutrition food (c.80%). The Group is sanguine on introducing more small-ticket items to boost its recurring income and hence the overall earnings going forwards.

- **Exports of bird nest product to strengthen Wholesale division –** Currently, Wholesale division supplies to more than 100 wholesalers and 2,000 retailers such as Chinese medical halls, restaurants, supermarkets and pharmacies in

Malaysia which include Chinese medicated tonic and other health and wellness products. The Group's current strategy is to focus on non-alcoholic products such as food and beverage products (i.e. Medetop coconut oil, herbal beverages, canned food and ready-to-drink bird's nest) instead of alcoholic products (i.e. cooking wine, health tonic, tea and wine). In the previous financial results, the Group successfully obtained approval from the Chinese government to export bird nest products there. The bird nest products are produced locally. Management believes the expansion plans in China will help to bolster the Group's business expansion.

- **Extensive sales campaign ahead for Retail division –** Retail division, which mainly focuses on Traditional Chinese Medical (TCM) and Chinese physician consultation services, will continue to launch extensive sale promotions in order to expand their house brands products. Currently, the retail division has 57 outlets, including 7 franchises. Going forward, the Group expects to add one or two additional outlets in East Coast Malaysia, with the hope to have large presence in all of the states in Malaysia. Currently, the Group has two international standards manufacturing facilities which assemble for manufacturing of Halal and non-Halal products.
- **Minimal overseas contributions**. Most of the revenue of the Group thus far are derived from local. The Group also has business ventures in other countries such as Indonesia and Brunei. However, the Group expects minor contributions from overseas MLM markets as the market shares are relatively small due to less established network and team leaders.

Earnings Outlook/Revision

- **We lift our earnings forecasts for FY20F and FY21F by 4.8% and 3.6%%** to RM43.7m and RM49.1m respectively, to account for higher sales assumptions for all segments.
- Risks include: 1) Higher-than-expected operating expenses (i.e. higher marketing and branding expenses), 2) Lower-than-expected domestic spending due to higher cost of living and 3) Depreciation of MYR against USD.

Valuation & Recommendation

- **Upgraded to HOLD from SELL with a higher target price of RM2.30** (previous target price of RM2.20) following our earnings upgraded. We believe market has discounted the prevailing earnings hiccup and share price is well supported by decent dividend yield of slightly over 4%. Our revised target price is based on P/E multiple of 15.8x FY20F EPS which is at its 3-year historical mean P/E.

Figure 1: Peer Comparison

Company	Price	Recom	T.price	P/E		P/B	ROE	Div Yield
	RM		RM	19'	20'		%	%
Hai-O	2.2	HOLD	2.3	14.5	15.4	2.0	13.9	5.9
Amway	6.04	-	-	14.6	17.6	4.6	33.2	4.6

Source: Company, JF Apex

Figure 2: Financial Summary

Year ended 30 April	FY16	FY17	FY18	FY19	FY20F	FY21F
	RMm	RMm	RMm	RMm	RMm	RMm
Revenue	297.6	404.0	461.8	328.4	338.0	353.2
Gross profit	101.4	132.9	162.2	125.9	124.9	128.2
Operating profit	48.3	77.3	97.6	62.4	57.0	62.7
PBT	49.1	78.1	99.0	63.5	57.9	63.8
PAT	36.6	59.2	75.1	47.1	43.9	49.3
Net profit	36.3	59.3	75.4	47.4	43.7	49.1
Margin (%)						
Gross profit margin	34.1%	32.9%	35.1%	38.4%	37.0%	36.3%
Operating profit	16.2%	19.1%	21.1%	19.0%	16.9%	17.8%
PBT margin	16.5%	19.3%	21.4%	19.3%	17.1%	18.1%
PAT margin	12.3%	14.7%	16.3%	14.4%	13.0%	14.0%
Net profit margin	12.2%	14.7%	16.3%	14.4%	12.9%	13.9%
Growth (%)						
Revenue growth	24.1%	35.7%	14.3%	-28.9%	2.9%	4.5%
Gross Profit growth	18.5%	31.0%	22.1%	-22.3%	-0.8%	2.6%
PBT growth	14.0%	59.2%	26.8%	-35.9%	-8.8%	10.2%
PAT growth	18.9%	61.9%	26.9%	-37.2%	-6.9%	12.3%
Net profit growth	20.8%	63.1%	27.2%	-37.1%	-7.8%	12.3%
Net gearing	Net cash	Net cash	Net cash	Net cash	Net cash	Net cash
ROA	11.3%	16.3%	19.0%	14.0%	13.9%	15.5%
ROE	13.5%	20.0%	23.6%	16.5%	16.2%	18.7%
EPS (sen)	12.1	19.7	25.1	15.8	14.6	16.3
P/E	22.1	13.6	10.7	17.0	18.4	16.4
DPS (sen)	10.0	16.0	20.0	13.0	11.0	11.0
Dividend Payout	82.6%	81.1%	79.7%	82.3%	75.6%	67.3%
Dividend yield (%)	3.7%	6.0%	7.5%	4.9%	4.1%	4.1%

Source: Company, JF Apex

JF APEX SECURITIES BERHAD – CONTACT LIST

JF APEX SECURITIES BHD

Head Office:
6th Floor, Menara Apex
Off Jalan Semenyih
Bukit Mewah
43000 Kajang
Selangor Darul Ehsan
Malaysia

General Line: (603) 8736 1118
Facsimile: (603) 8737 4532

PJ Office:
15th Floor, Menara Choy Fook On
No. 1B, Jalan Yong Shook Lin
46050 Petaling Jaya
Selangor Darul Ehsan
Malaysia

General Line: (603) 7620 1118
Facsimile: (603) 7620 6388

DEALING TEAM

Head Office:
Kong Ming Ming (ext 3237)
Shirley Chang (ext 3211)
Norisam Bojo (ext 3233)

Institutional Dealing Team:
Zairul Azman (ext 746)
Nur Nadia (ext 741)
Ahmad Mansor (ext 744)

PJ Office:
Mervyn Wong (ext 363)
Azfar Bin Abdul Aziz (Ext 822)
Joanne Tan Hui Bin (Ext 111)

RESEARCH TEAM

Head Office:
Lee Chung Cheng (ext 758)
Lee Cherng Wee (ext 759)
Nursuhaiza Hashim (ext 752)
How Chi Hoong (ext 754)

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

JF APEX SECURITIES BERHAD – DISCLAIMER

Published & Printed By:

JF Apex Securities Berhad (47680-X)

(A Participating Organisation of Bursa Malaysia Securities Berhad)