

**Company Result**

**26 March 2018**

**Hai-O Enterprise Berhad**

**BUY**

**Stronger earnings ahead**

**Maintained**

<b>Share Price</b>	<b>RM4.70</b>
<b>Target Price</b>	<b>RM6.41</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)	291.42
Par Value (RM)	0.50
Market cap. (RMm)	1,368.69
52-week price Range	RM3.20 – 5.60
Beta (against KLCI)	0.68
3-m Average Daily Volume	0.29m
3-m Average Daily Value <sup>^</sup>	RM1.49m

**Share Performance**

	1m	3m	12m
Absolute (%)	-10.6	-12.3	46.0
Relative (%-pts)	-10.8	-18.3	36.7

**Major Shareholders**

	%
Kai Hee Tan	10.11
Akintan Sdn Bhd	7.83
Excellent Communications	5.34

**Historical Chart**



Source: Bloomberg

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- **Hai-O reported a net profit of RM19.3m for its 3QFY18.** The quarterly net profit dropped by 10.2% QoQ but improved 25.3% YoY. Meanwhile, the Group recorded a quarterly revenue of RM103.1m during this quarter, which decreased by 16.6% QoQ and 3.8% YoY.
- **For 1HFY18,** the Group attained a higher topline and bottomline of 22.9% and 42.8% YoY respectively.
- **9MFY18 net profit is deemed within expectations.** The Group's 9MFY18 net profit of RM58.55m accounted for 66.3% of market forecast and 65.6% of our full year estimate. We deemed the result within our expectation as 3Q is a seasonally weaker quarter. We believe that Hai-O's 4Q net earnings will be stronger and hence able to meet our full year earnings expectation on the backdrop of Chinese New Year (CNY) festive season.

**Comment**

- **Lower QoQ earnings on the back of lower topline.** The Group reported a lower revenue in 3QFY18 as compared to 2QFY18 mainly due to higher sales generated during the previous quarter as a result of incentive trip promotion campaign and 25th grand sales promotion under its MLM division.
- **However, the Group managed to clinch a higher gross profit margin and PBT margin** of +3.7 ppts and +1.7 ppts respectively. We believe it was due to the efforts of digital marketing platform and hence further improved its operational efficiency and margins.
- **Stronger YoY bottom line.** The Group recorded a slightly lower revenue, -3.8% in 3QFY18 as compared to 3QFY17 due to lower sales generated by the MLM and retail divisions. However, it was partially offset by stellar performance posted by its wholesale division which generated a better sales from its Chinese medicated tonic and Chinese tea.
- **The wholesale division's PBT posted an increase of +260% YoY,** thanks to favourable sales mix, i.e. higher sales from its premium Chinese medicate tonic and sales of vintage Puer Tea, along with the resale of treasury shares of RM2.0m and also higher contribution from its inter-segment sales which contributed to the quantum leap of PBT in 3QFY18.
- **Higher 9MFY18 results underpinned by MLM and wholesale divisions.** The Group recorded stronger revenue and PBT, +22.9% and +42.5% respectively in 9MFY18 against 9MFY17 results. The better performance

was generated by higher sales from its MLM and wholesale division. Notably, the Group recorded a higher PBT and PBT margin of 21.6% and +2.5 ppts respectively, backed by higher sales of premium products and improvement in operational efficiency.

- **Dividend declared.** The Group has declared a second single tier dividend of 3 sen per share.
- **Product expansion.** The Group is being active in expanding lifestyle fashion brands, in the like of shoes, bags, attires and accessories, which endorsed by its brand ambassadors such as Nur Fazura Sharifuddin and Prof. Datuk Jimmy Choo. The renowned celebrities also act as the brands' fashion consultants to target the modern Muslim women and further expand the Group's market share for other related products.
- **Positive outlook.** We are sanguine on the Group's prospects and strongly believe that Hai-O is able to achieve better revenue and margin banking on: 1) Higher sales from the lifestyle fashion brands which further boost its MLM division, 2) Leverage on digital marketing platform for its MLM ecosystem which continue to enhance its operational efficiency and margins, 3) Higher recurring sales from wholesale division from its premium medicated tonic and Chinese tea, and 4) Higher contributions from its retail division for its upcoming quarter attributable to CNY festive season.

#### Earnings Outlook/Revision

- **We maintain our earnings forecast for FY18F and FY19F** as we believe that the Group will generate higher earnings in 4QFY18, which is a seasonally stronger period.

#### Valuation & Recommendation

- **Maintain BUY with an unchanged target price of RM6.41**, applying 17.5x FY2019F PE (+1.5SD above mean). We reckon that investors would appreciate the 'defensiveness' of the stock under current market sentiment by ascribing higher valuation to the stock given its strong fundamentals.
- **We continue to favour Hai-O for its:** 1) Impressive profit margin against its peers thanks to effective cost rationalization and MLM remuneration package, 2) Strong brand name among Malaysian household, and 3) Lower risk as the Group is less exposed to foreign market and foreign currency risk.

**Figure 1: Quarterly Figures**

Year ended 30 April	3QFY18	2QFY18	3QFY17	QoQ	YoY	9MFY18	9MFY17	YoY
	RM'm	RM'm	RM'm	%	%	RM'm	RM'm	%
Revenue	103.1	123.5	107.2	-16.6%	-3.8%	351.13	285.62	22.9%
Gross profit	39.4	42.7	34.9	-7.7%	12.9%	123.22	92.52	33.2%
Operating profit	24.6	27.4	21.4	-10.4%	14.9%	74.84	54.17	38.2%
PBT	25.0	27.9	21.7	-10.2%	15.3%	75.98	54.61	39.1%
PAT	19.2	21.6	15.7	-11.1%	22.7%	58.44	41.02	42.5%
Net profit	19.3	21.4	15.4	-10.2%	25.3%	58.55	41.01	42.8%
<b>Margin (%)</b>				<b>ppts</b>	<b>ppts</b>			<b>ppts</b>
Gross profit margin	38.2%	34.6%	32.6%	3.7	5.7	35.1%	32.4%	2.7
Operating profit margin	23.8%	22.2%	20.0%	1.6	3.9	21.3%	19.0%	2.3
PBT margin	24.3%	22.5%	20.2%	1.7	4.0	21.6%	19.1%	2.5
PAT margin	18.6%	17.5%	14.6%	1.1	4.0	16.6%	14.4%	2.3
Net profit margin	18.7%	17.4%	14.3%	1.3	4.3	16.7%	14.4%	2.3

Source: Company, JF Apex

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

Year ended 30 April	3QFY18	2QFY18	3QFY17	QoQ	YoY
	RM'm	RM'm	RM'm	%	%
MLM division	75.5	95.5	79.4	-21%	-5%
Wholesale division	17.1	16.5	14.2	4%	20%
Retail division	9.3	10.4	12.5	-11%	-25%
<b>Total Revenue</b>	<b>101.9</b>	<b>122.4</b>	<b>106.1</b>	<b>-17%</b>	<b>-4%</b>
MLM division	14.5	19.9	17.1	-27%	-15%
Wholesale division	8.9	6.2	2.5	44%	260%
Retail division	0.1	0.5	1.1	-80%	-91%
<b>Total PBT</b>	<b>23.5</b>	<b>26.6</b>	<b>20.6</b>	<b>-12%</b>	<b>14%</b>
<b>PBT margin (%)</b>				<b>ppts</b>	<b>ppts</b>
MLM division	19.2%	20.8%	21.5%	-1.6	-2.3
Wholesale division	52.0%	37.6%	17.4%	14.5	34.7
Retail division	1.1%	4.8%	8.6%	-3.7	-7.5

Source: Company, JF Apex

**Figure 3: Peer Comparison**

Company	Ticker	Price	Stock Rec.	Target Price	Market Cap	PE	Div Yield	EPS
	MK				RM'm	18	19	%
Hai-O	HAIO	5.1	BUY	6.41	1,411	15.4	14.7	3.3
Amway	AMW	7.6	-	-	1,249	20.1	18.6	2.7

Source: Company, JF Apex

**Figure 3: Financial Summary**

Year ended 30 April	FY15 RMm	FY16 RMm	FY17 RMm	FY18F RMm	FY19F RMm
Revenue	239.9	297.6	404.0	553.6	671.9
Gross profit	85.6	101.4	132.9	171.6	201.6
Operating profit	42.2	48.3	77.3	113.7	140.1
PBT	43.0	49.1	78.1	114.6	141.0
PAT	30.8	36.6	59.2	89.4	109.9
Net profit	30.1	36.3	59.3	89.2	109.8
<b>Margin (%)</b>					
Gross profit margin	35.7%	34.1%	32.9%	31.0%	30.0%
Operating profit	17.6%	16.2%	19.1%	20.5%	20.8%
PBT margin	17.9%	16.5%	19.3%	20.7%	21.0%
PAT margin	12.8%	12.3%	14.7%	16.1%	16.4%
Net profit margin	12.5%	12.2%	14.7%	16.1%	16.3%
<b>Growth (%)</b>					
Revenue growth	-5.4%	24.1%	35.7%	37.0%	21.4%
Gross Profit growth	-8.5%	18.5%	31.0%	29.2%	17.5%
PBT growth	-19.7%	14.0%	59.2%	46.7%	23.0%
PAT growth	-25.6%	18.9%	61.9%	51.0%	23.0%
Net profit growth	-25.4%	20.8%	63.1%	50.6%	23.0%
Net gearing	Net cash	Net cash	Net cash	Net cash	Net cash
ROA	9.8%	11.3%	16.3%	20.5%	23.8%
ROE	11.3%	13.5%	20.0%	25.6%	29.3%
EPS (sen)	10.0	12.1	19.7	29.7	36.6
P/E	17.5	17.5	17.5	17.5	17.5
DPS (sen)	10.0	10.0	16.0	16.0	16.0
Dividend Payout	98.2%	81.6%	80.6%	53.5%	43.5%
Dividend yield (%)	2.2%	2.2%	3.4%	3.4%	3.4%

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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