

Outthink. Outperform.

## Results Note

## Hai-O

 HAIO MK  
Sector: Consumer

RM4.04 @ 26 September 2018

HOLD (downgrade)

Downside 1.0%

Price Target: RM4.00

Previous Target: RM5.39



## Price Performance

	1M	3M	12M
Absolute	-8.0%	-16.7%	-20.5%
Rel to KLCI	-7.5%	-22.4%	-21.9%

## Stock Data

Issued shares (m)	290.7
Mkt cap (RMm)/(US\$m)	1174.3/283.7
Avg daily vol - 6mth (m)	0.2
52-wk range (RM)	4-5.6
Est free float	55.5%
BV per share (RM)	1.03
P/BV (x)	3.94
Net cash/ (debt) (RMm)	125.21
ROE (2019E)	19.7%
Derivatives	Nil
Shariah Compliant	NO

## Key Shareholders

Kai Hee Tan	10.1%
Akintan Sdn Bhd	7.9%
Excellent Communicat.	5.4%

Source: Affin Hwang, Bloomberg

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## Some weaknesses appearing

Hai-O reported a 1Q19 net profit of RM11m (-38% yoy, -32% qoq), which came in below our and consensus expectations. The MLM segment recorded a significant decline in revenue which was attributable to the slower business activities among the distributors after the general election. This was also exacerbated by weaknesses in the Wholesale and Retail segment. As we turn more cautious on the outlook for the MLM segment, we cut our earnings estimates and downgrade Hai-O to a HOLD with a revised TP of RM4.00.

## 1Q19 earnings miss estimates

Hai-O's 1Q19 net profit declined by 38% yoy and 32% qoq, which was mainly dragged by the MLM division, of which posted a 45% yoy decline in operating profit. The MLM division was affected by a slowdown in distributors' activities during the fasting month and Hari Raya festivities, coupled with lower member recruitment rate after the general election (GE). In addition, MLM margins also saw erosion following the 6% rebate given during the month prior to the zero-rating of the GST coupled with higher marketing costs incurred for new fashion products launched. The quarter further was exacerbated by weaknesses in both the Wholesale and Retail segment due to higher costs yoy in the Wholesale segment and contracting margins in the Retail segment. There was also some minor impact from the MFRS 9 and MFRS 15 adoption which was relatively minimal at c.2% at the PAT level.

## Cautious outlook on the MLM division due to possible attrition

We foresee some downside risks to the expansion in the MLM distributor base. Management has indicated that new member interest has slowed down recently, as compared to the high double digit growth shown in the past few years. We gather that to date, the number of active members stand at 140,000, which is slightly lower compared to end-FY18 (150,000). Furthermore, we believe that there could be margin pressures moving forward in line with increasing marketing costs incurred for Hai-O's foray into the fashion segment under the newly introduced "Infincence" brand.

## Downgrade to HOLD with revised TP of RM4.00

In view of the significant earnings miss and cloudy outlook in the MLM segment, we cut our distributor growth assumptions to a 3-year CAGR of 4% from FY19-21E (from 9% previously), resulting in a downward revision of 26-27% in FY19-21E earnings forecasts. We downgrade Hai-O to a HOLD with a revised TP of RM4.00 (from RM5.39), based on an unchanged PER target of 17x on CY19E EPS. Downside/upside risks to our call: i) loss/expansion in MLM distributor base; ii) weakness in the wholesale and retail divisions; iii) weaker/better-than-expected take-up rate of the new products.

## Earnings &amp; Valuation Summary

FYE	Apr	2017	2018	2019E	2020E	2021E
Revenue (RMm)		404.2	461.8	429.0	482.2	539.7
EBITDA (RMm)		81.1	101.6	86.0	98.5	109.7
Pretax profit (RMm)		78.3	99.0	81.4	93.9	105.1
Net profit (RMm)		59.4	74.8	62.1	71.6	80.2
EPS (sen)		20.2	24.9	21.2	24.4	27.3
PER (x)		24.0	19.5	19.1	16.5	14.8
Core net profit (RMm)		59.4	74.8	62.1	71.6	80.2
Core EPS (sen)		20.2	24.9	21.2	24.4	27.3
Core EPS growth (%)		63.3	23.1	-17.6	15.4	11.9
Core PER (x)		24.0	19.5	19.1	16.5	14.8
Net DPS (sen)		16.0	20.0	13.8	15.9	17.8
Dividend Yield (%)		3.3	4.1	3.4	3.9	4.4
EV/EBITDA (x)		15.9	13.1	12.1	10.3	0.0
Chg in EPS (%)				-26.8%	-26.2%	-27.4%
Affin/Consensus (x)				0.65	0.69	0.73

Source: Company, Bloomberg, Affin Hwang forecasts

Fig 1: Results Comparison

FYE Apr (RMm)	1Q18	4Q18	1Q19	QoQ % chg	YoY % chg	Outthink. Outperform. Comments
Revenue	124.5	110.6	80.1	(27.6)	(35.7)	Dragged by a significant decline in MLM revenue (-43.3% yoy) and slowdown in the retail division. Mitigated slightly by a +4% yoy revenue increase in the wholesale segment.
Op costs	(100.7)	(86.8)	(64.8)	(25.4)	(35.7)	
EBITDA	23.8	23.8	15.3	(35.7)	(35.7)	Slight contraction of margins qoq due to higher marketing costs incurred
<i>EBITDA margin (%)</i>	19.1	21.5	19.1	(2.4)	0.0	
Depn and amort	(1.0)	(1.0)	(1.1)	10.3	18.7	
EBIT	22.8	22.8	14.2	(37.8)	(37.9)	
<i>EBIT margin (%)</i>	18.3	20.6	17.7	(2.9)	(0.6)	
Int expense	(0.1)	(0.0)	(0.1)	147.6	(13.3)	
Int and other inc	0.3	0.3	0.3	11.3	(1.6)	
Associates	0.0	0.0	0.0	n.m.	n.m.	
Exceptional items	0.0	0.0	0.0	n.m.	n.m.	
<b>Pretax</b>	<b>23.1</b>	<b>23.1</b>	<b>14.4</b>	<b>(37.4)</b>	<b>(37.5)</b>	
Tax	(5.5)	(6.4)	(3.8)	(40.7)	(31.4)	
<i>Tax rate (%)</i>	23.9	27.7	26.2	(1.5)	2.3	Higher than statutory tax rate due to certain non-deductible expenses and losses of certain subsidiaries
MI	0.3	(0.4)	0.3	n.m.	n.m.	
<b>Net profit</b>	<b>17.9</b>	<b>16.3</b>	<b>11.0</b>	<b>(32.4)</b>	<b>(38.4)</b>	
EPS (sen)	6.2	5.6	3.8	(32.4)	(38.4)	
<b>Core net profit</b>	<b>17.9</b>	<b>16.3</b>	<b>11.0</b>	<b>(32.4)</b>	<b>(38.4)</b>	Below our and consensus estimates.

Source: Affin Hwang, Company data

	1Q18	4Q18	1Q19	QoQ % chg	YoY % chg
<b>Segmental Revenue</b>					
MLM	102.38	79.10	58.03	(26.64)	(43.32)
Wholesale	13.04	17.02	13.56	(20.36)	3.95
Retail	8.12	13.67	7.62	(44.28)	(6.17)
Others	1.00	0.85	0.88	2.93	(11.66)
<b>Total revenue</b>	<b>124.54</b>	<b>110.65</b>	<b>80.09</b>	<b>(27.62)</b>	<b>(35.69)</b>
<b>Segmental Profit</b>					
MLM	18.81	16.59	10.37	(37.50)	(44.88)
Wholesale	2.95	3.45	2.72	(21.13)	(7.89)
Retail	(0.53)	1.39	(0.60)	n.m.	n.m.
Others	1.18	1.21	0.84	(31.22)	(29.00)
	<b>22.85</b>	<b>22.79</b>	<b>14.18</b>	<b>(37.79)</b>	<b>(37.95)</b>

Source: Affin Hwang, Company data

**Equity Rating Structure and Definitions**


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<b>BUY</b>	Total return is expected to exceed +10% over a 12-month period
<b>HOLD</b>	Total return is expected to be between -5% and +10% over a 12-month period
<b>SELL</b>	Total return is expected to be below -5% over a 12-month period
<b>NOT RATED</b>	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.*

<b>OVERWEIGHT</b>	Industry, as defined by the analyst's coverage universe, is expected to outperform the KLCI benchmark over the next 12 months
<b>NEUTRAL</b>	Industry, as defined by the analyst's coverage universe, is expected to perform inline with the KLCI benchmark over the next 12 months
<b>UNDERWEIGHT</b>	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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