MLM continues to be main earnings driver

Hai-O reported a 1Q17 core net profit improvement of 47.1% to RM 9.7m, coming in line with our and consensus expectations. The group's multi-level-marketing (MLM) division drove earnings as the Group saw recurring sales as well as additional revenue from the increase in distributors. We increase our TP to RM 2.78 and maintain Sell.

1Q17 in line with expectations

Hai-O recorded a 1Q17 revenue and core net profit of RM 78.7m (+42.1% yoy) and RM 9.7m (+47.1% yoy) respectively. This was mainly due to higher revenue generated by its MLM division, which was its main contributor (72% of revenue). The group's 1Q17 core earnings were in line with our and consensus expectations, accounting for 23% of both full year estimates (note that 1Q has historically been weaker at 18-23% of full year earnings).

MLM division drives earnings among other segments

The group's 1Q17 results continue to be driven by its MLM division where turnover and PBT for its MLM segment increased by 53.6% yoy and 55.5% yoy to RM 56.4m and RM 9.7m respectively due to higher sales volume for most products, especially its "small ticket" items such as mineral coffee, bamboo salt, skin care and health supplements. In addition, the group has been actively growing its distributor force, which have further contributed to earnings. The wholesale division (18% of revenue) also recorded a positive revenue and EBIT increase of 53% yoy and 2% yoy due to the lower base post GST implementation as well as higher sales in Chinese medicine, inclusive of a one-off re-export sale. Nonetheless, the retail division posted a drop in revenue by 5.8% and a pre-tax loss of RM 0.5m due to lower demand for high-end health supplements and higher operating costs.

Higher TP of RM2.78 after rolling forward valuations, maintain sell

We increase our TP to RM2.78, based on its 5 year historical PE of 11.6x and rolling forward to CY17E. However, stock price has run up (peak of RM3.17 in 2010) and HAI-O is currently trading at a PE of 15.7x and therefore we maintain our SELL call. Note that HAI-O has been actively buying back its shares and currently holds close to 5% of its total issued and paid-up share capital which brings up the possibility of a share dividend distribution to shareholders.

Key risks to our call: i) a stronger upturn in consumer spending; ii) a strengthening of the RM vs. US$ which will reduce import costs; iii) higher growth of members for the MLM business (iv) special share dividend.

Earnings & Valuation Summary

FYE Apr	2015	2016	2017E	2018E	2019E
Revenue (RMm)	239.9	297.6	340.3	368.6	388.3
EBITDA (RMm)	48.5	51.7	61.9	67.4	70.7
Pretax profit (RMm)	43.0	49.1	57.9	63.5	66.9
Net profit (RMm)	30.1	36.3	42.5	46.6	49.1
EPS (sen)	15.4	18.6	21.7	23.8	25.1
PER (x)	22.2	18.3	15.7	14.3	13.6
Core net profit (RMm)	30.1	36.3	42.5	46.6	49.1
Core EPS (sen)	15.4	18.6	21.7	23.8	25.1
Core EPS growth (%)	-24.8	20.8	16.9	9.7	5.4
Core PER (x)	22.2	18.3	15.7	14.3	13.6
Net DPS (sen)	15.0	15.0	14.1	15.5	16.3
Dividend Yield (%)	4.4	4.4	4.1	4.5	4.8
EV/EBITDA (x)	11.7	10.8	9.0	8.0	7.4
Chg in EPS (%)			-	-	-
Affin/Consensus (x)			1.0	1.0	1.0

Source: Company, Affin Hwang estimates

Results Note

HAI-O

HAIO MK
Sector: Consumer

RM3.41 @ 21 September 2016

SELL (maintain)

Downside 21%

Price Target: RM2.78

Previous Target: RM2.40

Price Performance

	1M	3M	12M
Absolute	+8.3%	+27.2%	+50.9%
Rel to KLCI	+10.1%	+25.6%	+49.1%

Stock Data

Issued shares (m)	193.0
Mkt cap (RMm)/(US$m)	658.2/159.1
Avg daily vol - 6mth (m)	0.1
52-wk range (RM)	2.19-3.59
Est free float	50.6%
BV per share (RM)	1.33
P/BV (x)	2.56
Net cash/ (debt) (RMm) (1Q17)	53.20
ROE (2017E)	21.9%
Derivatives	Nil
Shariah Compliant	NO

Key Shareholders

Kai Hee Tan	10.1%
Akintan Sdn Bhd	7.9%
Siow Eng Tan	7.0%

Source: Affin Hwang, Bloomberg

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Fig 1: Results Comparison

FYE Apr (RMm)	1Q17	QoQ % chg	YoY % chg	Comment
Revenue	78.7	(11.2)	42.1	YoY growth mainly due to higher sales volume from the MLM division, coupled with its increasing distribution force QoQ contraction due to 1Q being weaker quarter
Op costs	(65.2)	(10.1)	42.2	
EBITDA	13.4	(16.1)	41.6	
EBITDA margin (%)	17.1	*-1.0ppts*	*-0.1ppts*	
Depn and amort	(0.9)	(10.0)	13.4	
EBIT	12.6	(16.5)	44.1	
EBIT margin (%)	*16.0*	*-1.0ppts*	*+0.2ppts*	
Int expense	(0.1)	23.9	(28.8)	
Int and other inc	0.2	(63.0)	41.4	
Associates	(0.1)	0.0	0.0	
Exceptional items	0.0	0.0	0.0	
Pretax	**12.6**	**(17.5)**	**43.1**	
Tax	(3.1)	(23.4)	38.5	
Tax rate (%)	*25.0*	*-1.9ppts*	*-0.8ppts*	Certain expenses not deductible for tax purposes
MI	0.3	529.8	214.9	
Net profit	**9.7**	**(13.0)**	**47.1**	
EPS (sen)	5.0	(13.0)	47.1	
Core net profit	**9.7**	**(13.0)**	**47.1**	In line with expectations

Source: Affin Hwang, Company data

	2012	2013	2014	2015	2016
External Revenue					
Wholesale	48.7	50.7	56.3	56.6	54.4
MLM	141.1	167.0	149.3	135.6	198.3
Retail	42.8	42.2	40.1	40.6	38.3
Others	6.9	8.0	7.8	7.1	6.6
Total revenue	**239.5**	**267.9**	**253.4**	**239.9**	**297.6**
% contribution to revenue					
Wholesale	20.3%	18.9%	22.2%	23.6%	18.3%
MLM	58.9%	62.3%	58.9%	56.5%	66.6%
Retail	17.9%	15.8%	15.8%	16.9%	12.9%
Others	2.9%	3.0%	3.1%	2.9%	2.2%
	100%	**100%**	**100%**	**100%**	**100%**

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

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