

Corporate Highlights



RHB Research
Institute Sdn Bhd
A member of the
RHB Banking Group
Company No: 233327 -M

Company Update

27 October 2009

Hai-O Enterprise

Recruitment Drives Growth

Share Price : RM7.08
Fair Value : RM8.80
Recom : **Outperform**
(Maintained)

Table 1 : Investment Statistics (HAIO; Code: 7668)

Bloomberg: HAIO MK

FYE	Net				Net						
	Revenue	Profit	EPS	Growth	PER	C. EPS *	P/NTA	Gearing	ROE	GDY	
Apr	(RMm)	(RMm)	(sen)	(%)	(x)	(sen)	(x)	(x)	(%)	(%)	
2009a	435.2	52.4	62.0	7.9	11.3	-	2.0	Net cash	34.2	6.0	
2010f	619.3	67.5	79.9	28.9	8.9	79.0	2.5	Net cash	36.1	5.6	
2011f	811.5	89.9	106.4	33.1	6.7	90.0	3.1	Net cash	38.0	7.5	
2012f	942.9	106.5	126.0	18.5	5.6	100.0	3.9	Net cash	35.7	8.9	

Main Board Listing / Trustee Stock

* Consensus Based On IBES Estimates

We recently spoke to Hai-O's management and obtained the following key highlights:

- ◆ **4,000-5,000 new members per month.** Since Jun 09, Hai-O's MLM division recruitment of new members has increased to an average of 4-5k/mth (vs. 3-4k in 1HCY09), representing an average increase of +29%. The increase in new members was mainly attributed to the success of its advertising activities i.e. celebrity endorsement and TV commercials for its water filter product (BioAura). Following the stronger-than-expected membership growth, we have increased our monthly membership growth forecast to 4k (vs. 3k previously) for FY10, 2.5k (vs. 1.5k previously) for FY11 and 2k (vs. 1k previously) for FY12.
- ◆ **Revenue/distributor remains strong.** Sales from its recently launched products i.e. health supplements (Dec 08) and anti-aging skincare range (Mar 09) have picked up despite initial mediocre sales performance. Nevertheless, Hai-O's star product remains its water filter, which is still gaining popularity especially amongst the Bumiputera community. While no figures were provided, management guided that average revenue/distributor continues to grow yoy. We forecast average revenue/distributor to increase by an unchanged 5%, 3% and 1% for FY10-12.
- ◆ **Indonesia the wild card?** Hai-O obtained its licence from the Association of MLM in Indonesia back in Aug 09, and hence, started the initial phase of its recruitment activities in the Indonesian market. Recall that Hai-O only invested a total of US\$480k (or RM1.7m) for its Indonesia venture, which is a minimal amount for the vast potential growth in the Indonesian market. Management targets a conservative 5-10k in new members in FY10, and projects a minimum one year to break even. We have yet to input any contributions from Indonesia.
- ◆ **Risks.** The risks include: 1) termination of supply agreements from its suppliers in China; 2) stronger-than-expected strengthening of US\$; and (3) weaker-than-expected increase in consumer spending.
- ◆ **Forecasts.** We have revised our FY10-12 forecasts up by 4-26% after increasing our projection for new members/mth.
- ◆ **Investment case.** Indicative fair value for Hai-O has been increased to RM8.80 (from RM6.80), based on higher PER of 9x CY10 EPS (vs. 8x CY10 EPS previously), representing a 38% discount to our target PE for the consumer sector of 14.5x on account of its smaller market capitalisation as well as low liquidity. We raised our target PER to reflect increase investor participation in mid cap stocks, lower risk premium and improved market sentiment. Maintain **Outperform**.

Issued Capital (m shares)	84.5
Market Cap(RMm)	598.0
Daily Trading Vol (m shs)	0.1
52wk Price Range (RM)	2.86 – 7.15

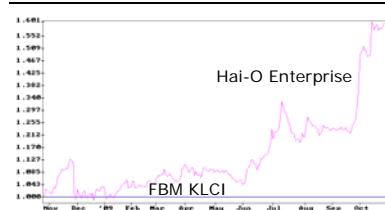
Major Shareholders:	(%)
Tan Family	30.0

FYE Apr	FY10	FY11	FY12
EPS chg (%)	3.7	19.4	25.8
Var to Cons (%)	1.2	18.2	26.0

PE Band Chart



Relative Performance To FBM KLCI



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Table 2. Earnings Forecasts				
FYE Apr (RMm)	FY09a	FY10F	FY11F	FY12F
Turnover	435.2	619.3	811.5	942.9
Wholesale	42.2	40.1	42.1	44.2
MLM	348.9	534.4	723.6	851.8
Retail	39.1	42.3	42.9	43.4
Manufacturing	2.5	2.5	3.0	3.5
Other	2.5	0.0	0.0	0.0
<i>Turnover growth (%)</i>	<i>16.4</i>	<i>42.3</i>	<i>31.1</i>	<i>16.2</i>
Cost of Sales	(305.13)	(397.55)	(518.74)	(601.34)
Gross Profit	130.1	221.7	292.8	341.5
EBITDA	78.2	99.7	129.9	150.7
EBITDA margin (%)	18.0	16.1	16.0	16.0
Depreciation	(2.1)	(4.3)	(4.4)	(4.4)
Net Interest	(0.2)	1.1	1.1	1.6
Associates	0.0	0.0	0.0	0.0
Pretax Profit	75.9	96.5	126.6	147.9
Tax	(22.8)	(27.0)	(34.2)	(38.4)
Minorities	(0.7)	(1.9)	(2.5)	(3.0)
Net Profit	52.4	67.5	89.9	106.5

Table 3. Forecast Assumptions			
FYE Apr	FY10F	FY11F	FY12F
Core distributor force (CDF)	107,500	121,000	133,000
Distributor productivity (RM/CDF)	4,741	4,883	4,932
Opening of new retail outlets	1	0	0
Revenue per outlet (RM'000)	705	716	723

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Outperform = The stock return is expected to exceed the FBM KLCI benchmark by greater than five percentage points over the next 6-12 months.

Trading Buy = Short-term positive development on the stock that could lead to a re-rating in the share price and translate into an absolute return of 15% or more over a period of three months, but fundamentals are not strong enough to warrant an Outperform call. It is generally for investors who are willing to take on higher risks.

Market Perform = The stock return is expected to be in line with the FBM KLCI benchmark (+/- five percentage points) over the next 6-12 months.

Underperform = The stock return is expected to underperform the FBM KLCI benchmark by more than five percentage points over the next 6-12 months.

Industry/Sector Ratings

Overweight = Industry expected to outperform the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Neutral = Industry expected to perform in line with the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

Underweight = Industry expected to underperform the FBM KLCI benchmark, weighted by market capitalisation, over the next 6-12 months.

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