STANDARD & POOR'S

Esthetics International Group

Recommendation: **BUY**

Stock Code: **5081** Bloomberg: **EIG MK** Price: **MYR0.87** 12-Month Target Price: **MYR0.97** Date: **December 30, 2005**

Board: Main

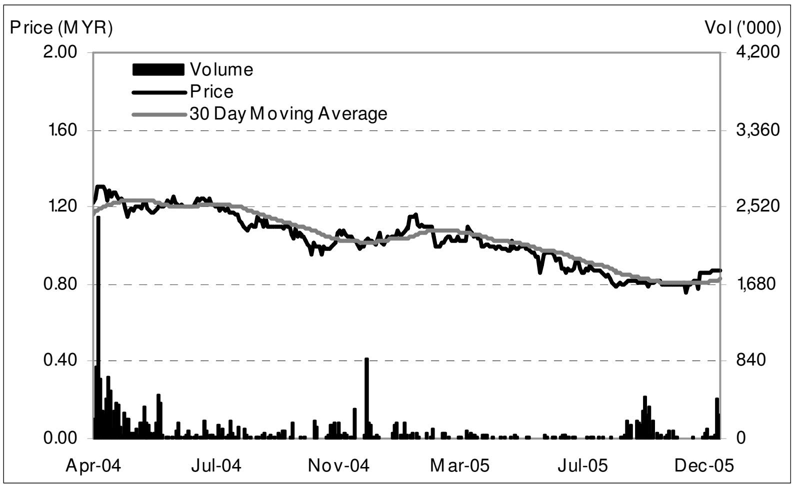
Sector: Trading / Services

GICS: Consumer Staples / Personal Products

Market Capitalization: MYR104.4 mln

Summary: Esthetics International Group (EIG) is the exclusive distributor of several brands of professional skincare and beauty products in Malaysia and parts of Asia, with the most well known brand being Dermalogica. EIG also provides professional skincare and beauty services via the operations of Leonard Drake and Belle Lina Skincare Centres in and around the Asian region. EIG was listed on the Main Board of Bursa Malaysia in March 2004.

Analyst: Hoe Lee Leng, CPA



Results Review & Earnings Outlook

- EIG's 9MFY06's (Jan.) results were slightly below our expectations, accounting for 62% of our FY06 forecast versus our expectations of 65% (given the seasonality in earnings). The main reasons for this were: (i) start-up losses incurred by EIG's direct selling operations of MYR0.75mln and by its four new corporate outlets and two new consultation pods of MYR0.4mln; and (ii) an increase in the proportion of sales from product distribution versus services, which yield higher margins. EBIT margins fell to 15.6% in 9MFY06 from 19.5% in 9MFY05.

- EIG is changing its financial year-end from Jan. 31 to March 31, and we have adjusted our earnings forecasts to take this into account. We project EIG to record a net profit of MYR13.0 mln for FY06 (14 months to Mar.) (from MYR12.4 mln previously), while net profit for FY07 is projected at a lower MYR13.9 mln (from MYR14.3 mln), after taking into account higher depreciation charges for its new corporate office in Shah Alam, which costs MYR11 mln and would be completed by Feb. 2006. On an annualized basis, we have lowered our earnings projections by 4.5% for FY06 and by 3.1% for FY07.

- Post-revision, EIG's net profit will post a three-year CAGR of 9.2% (from 10.4%). Although start-up losses for new product launches and new outlet operations are likely to continue for the first six to 12 months of operations, we believe an expansion of its strong product distribution channels would help improve EBIT margins for its product trading division, especially from the franchising operations.

Recommendation & Investment Risks

- We maintain our Buy recommendation on EIG with a 12-month target price of MYR0.97 (unchanged due to FY change and higher attributed discount). Our target price is based on a 35% discount (previously 30%) to 2006 market PER and includes the FY06 forecast net DPS of 4 sen. We attribute a higher discount for current weak market sentiment as well as for EIG's tight share liquidity and small free float of only 25%.

- We believe EIG's strong distribution system and established brand name via its Leonard Drake corporate outlets would enable it to complete its expansion plans successfully while remaining a step ahead of its competitors.

- Based on EIG's dividend policy, which is to distribute 30-50% of its net profit for at least the next two years, we forecast EIG's net dividend payout to average 40% p.a. over the next few years. This translates to net dividend yields of 5-6% p.a.

- Risks to our recommendation and target price include the extremely competitive environment EIG operates in, due to the ease of entry and low capital requirements. In addition, we believe EIG's overseas operations may be difficult to manage efficiently from Malaysia, given the diversity of cultures, operational structures and government regulations.

Key Stock Statistics

FY Mar.	Jan 2005	Mar 2006F
EPS (sen)	10.2	10.8
PER (x)	8.5	8.0
Dividend/Share (sen)	6.0	6.0
NTA/Share (MYR)	0.72	0.83
Book Value/Share (MYR)	0.72	0.83
Issued Capital (mln shares)	120.0	
52-week Share Price Range (MYR)	0.76 – 1.18	
Major Shareholders:	%	
Lim Yee Soon	25.1	
Melissa Chen	22.4	

Per Share Data

FY Mar.	Jan. 03	Jan. 04	Jan. 05	Mar. 06F
Book Value (MYR)	NA	NA	0.72	0.83
Cash Flow (sen)	NA	NA	12.1	13.3
Earnings (sen)	NA	NA	10.2	10.8
Dividend (sen)	NA	NA	6.0	6.0
Payout Ratio (%)	NA	NA	42.4	40.0
PER (x)	NA	NA	8.5	8.0
P/Cash Flow (x)	NA	NA	7.2	6.5
P/Book Value (x)	NA	NA	1.2	1.0
Dividend Yield (%)	NA	NA	6.9	6.9
ROE (%)	NA	NA	14.1	13.0
Net Gearing (%)	NA	NA	0.0	0.0

All required disclosures appear on the last page of this report. Additional information is available upon request.

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Quarterly Performance

FY Mar. / MYR mln	3QFY06	3QFY05	% Change
Revenue	25.9	20.7	24.7
Operating Profit (EBIT)	4.7	5.2	-9.7
Depreciation	NA	NA	NA
Net Interest Income / (Expense)	0.1	0.2	-50.2
Pretax Profit	4.8	5.4	-11.5
Net Profit	3.4	3.7	-8.0
Operating Margin (%)	18.1	24.9	-
Pretax Margin (%)	18.5	26.1	-
Net Margin (%)	13.3	18.0	-

Source: Company data

Profit & Loss

FY Mar. / MYR mln	Jan. 04	Jan. 05	Mar. 06F	Mar. 07F
Revenue	NA	80.7	109.9	121.1
Operating Profit (EBIT)	NA	20.7	24.1	27.5
Depreciation	NA	2.3	3.0	4.0
Net Interest Income / (Expense)	NA	1.3	1.4	1.1
Pretax Profit	NA	17.7	18.6	20.0
Effective Tax Rate (%)	NA	30.8	30.0	30.0
Net Profit	NA	12.2	13.0	13.9
Operating Margin (%)	NA	25.7	21.9	22.7
Pretax Margin (%)	NA	22.0	16.9	16.5
Net Margin (%)	NA	15.2	11.8	11.5

Source: Company data, S&P Equity Research

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Glossary

Strong Buy: Total return is expected to outperform the total return of the KLCI or KL Emas Index respectively, by a wide margin over the coming 12 months, with shares rising in price on an absolute basis.
Buy: Total return is expected to outperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months, with shares rising in price on an absolute basis.
Hold: Total return is expected to closely approximate the total return of the KLCI or KL Emas Index respectively, over the coming 12 months with shares generally rising in price on an absolute basis.
Sell: Total return is expected to underperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months and share price is not anticipated to show a gain.
Strong Sell: Total return is expected to underperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months by a wide margin, with shares falling in price on an absolute basis.

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