

Esthetics International Group

Recommendation: **BUY**

Stock Code: 5081

Bloomberg: EIG MK

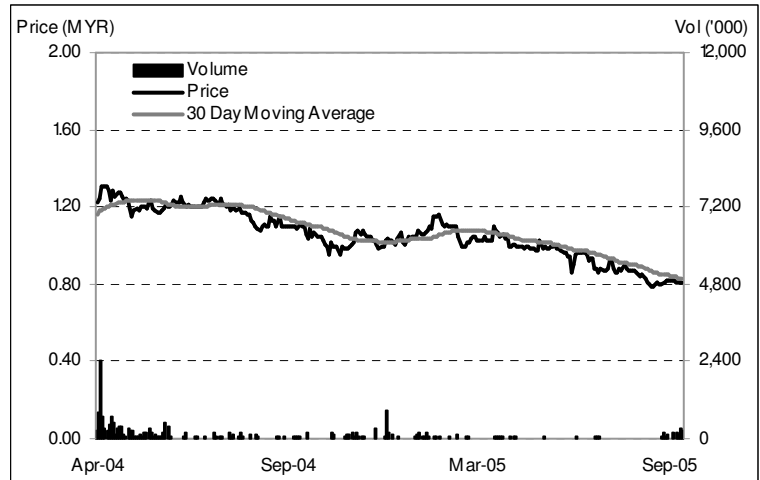
Price: MYR0.81

12-Month Target Price: MYR0.97

Date: September 28, 2005

Board: Main**Sector:** Trading / Services**GICS:** Consumer Staples / Personal Products**Market Capitalization:** MYR97.2 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 Bursa Malaysia Main Board in Mar. 2004.

Analyst: Hoe Lee Leng, CPA**Results Review & Earnings Outlook**

- EIG's 1HFY06's (Jan.) results were below our expectations, accounting for 32.3% of our full year forecast vs our expectations of 35%.
- The main reason for the weaker earnings was the lower-than-expected EBIT margin of 14.1% in 1HFY06 versus 16.4% in 1HFY05. We believe this was due to continued start-up losses from its direct selling operations; lower profit margins from a special sales arrangement it has with a major corporate client in Hong Kong; as well as lower sales to local dealers, which normally yield higher margins.
- Although we expect performance in 2HFY06 to pick up significantly due to seasonal factors, we anticipate overall profit margins to be weakened by the above factors, and have therefore revised our earnings forecasts downward by between 6.5-8.5% for the next few years. Based on our revised forecasts, EIG is forecast to record a three-year net profit CAGR of 10.4% from 13.4% previously.
- Although start-up losses for EIG's new product launches and new outlet operations are likely in the initial period, expansion of its strong product distribution channels would also expand operating profit margins for its product trading division, especially from the franchising operations.

Key Stock Statistics

FY Jan.	2005	2006F
EPS (sen)	10.2	10.4
PER (x)	8.0	7.8
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)	0.785 - 1.16	
Major Shareholders:	%	
Lim Yee Soon	25.1	
Melissa Chen	22.4	

Recommendation & Investment Risks

- We maintain our Buy recommendation on EIG with a revised 12-month target price of MYR0.97, from MYR1.00 previously. Our target price is based on a 30% discount to 2006 market PER. We attribute this discount for EIG's tight share liquidity and its 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 see through 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 between 5-7% 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 requirement.
- 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.

Per Share Data

FY Jan.	2003	2004	2005	2006F
Book Value (MYR)	NA	NA	0.72	0.83
Cash Flow (sen)	NA	NA	12.1	12.6
Earnings (sen)	NA	NA	10.2	10.4
Dividend (sen)	NA	NA	6.0	6.0
Payout Ratio (%)	NA	NA	42.4	41.6
PER (x)	NA	NA	8.0	7.8
P/Cash Flow (x)	NA	NA	6.7	6.4
P/Book Value (x)	NA	NA	1.1	1.0
Dividend Yield (%)	NA	NA	7.4	7.4
ROE (%)	NA	NA	14.1	12.5
Net Gearing (%)	NA	NA	0.0	0.0

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Quarterly Performance

FY Jan. / MYR mln	2Q06	2Q05	% Change
Revenue	22.6	18.3	23.3
Operating Profit (EBIT)	3.9	2.9	31.4
Depreciation	NA	NA	NA
Net Interest Income / (Expense)	0.1	0.2	-45.0
Pre-tax Profit	4.0	3.2	25.4
Net Profit	2.8	2.0	36.9
Operating Margin (%)	17.1	16.0	
Pre-tax Margin (%)	17.7	17.4	
Net-Margin (%)	12.3	11.0	

Source: Company data

Profit & Loss

FY Jan. / MYR mln	2004	2005	2006F	2007F
Revenue	NA	80.7	92.0	104.0
Operating Profit (EBIT)	NA	20.7	22.9	26.0
Depreciation	NA	2.3	2.7	2.8
Net Interest Income / (Expense)	NA	1.3	1.4	1.1
Pretax Profit	NA	17.7	18.1	20.9
Effective Tax Rate (%)	NA	30.8	31.0	31.0
Net Profit	NA	12.2	12.5	14.4
Operating Margin (%)	NA	25.7	24.9	25.0
Pretax Margin (%)	NA	22.0	19.7	20.1
Net Margin (%)	NA	15.2	13.5	13.8

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.

S&P 12 Month Target Price – The S&P equity analyst's projection of the market price a given security will command 12 months hence, based on a combination of intrinsic, relative, and private market valuation metrics.

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