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Company Update



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AT A GLANCE

SELL HOLD **BUY**

Target price	KRW105,000	(11.9%)
Current price	KRW93,800	
Market cap	KRW6.9t/USD6.2b	
Shares (float)	73,799,619 (70.4%)	
52-week high/low	KRW110,500/KRW81,000	
Avg daily trading value (60-day)	KRW14.2b/ USD12.7m	

ONE-YEAR PERFORMANCE

	1M	6M	12M
Coway (%)	8.3	-1.5	-5.3
Vs Kospi (%pts)	9.8	10.2	-0.9

KEY CHANGES

(KRW)	New	Old	Diff
Recommend.	BUY	BUY	
Target price	105,000	105,000	0.0%
2018E EPS	4,827	4,883	-1.1%
2019E EPS	5,483	5,552	-1.2%

SAMSUNG vs THE STREET

No of estimates	10
Target price	112,000
Recommendation	3.9

BUY★★★: 5 / BUY: 4 / HOLD: 3 / SELL: 2 / SELL★★★: 1

Coway (021240)

Overseas operations gaining traction

- Coway reported in-line 2Q results, with sales rising 9% y-y to KRW678.1b and operating profit climbing 7% y-y to KRW129.3b.
- The firm's strengths revolve around stable cash flows from domestic customers (who are particularly loyal), while its weakness centers on its low growth potential, though this negative is being overcome by overseas expansion. Overseas sales generated 80% of the play's 2Q sales growth (driving up the firm's high single-digit sales growth) and more than 20% of its total sales (for the first time in its history).
- Reflecting the in-line 2Q results, we only fine-tune our 2018 earnings forecasts, leaving our target price at KRW105,000 and our BUY rating intact. We believe that the growth potential of the overseas operations has yet to be fully priced in.

WHAT'S THE STORY?

2Q review: Coway reported in-line 2Q results, with sales and operating profit rising a respective 9% and 7% y-y to KRW678.1b and KRW129.3b (for an operating margin of 19.1%). The overseas operations drove its overall earnings growth, while the domestic operations once again posted stable figures, shrugging off intensifying competition fears.

- The firm's overseas sales jumped 49% y-y to KRW133b (or 20% of its total sales), backed by its overseas subsidiaries (sales up 62% y-y). Sales at its core overseas subsidiary (Malaysia; accounts for 70% of its overseas sales) surged 87% y-y, as: 1) the number of rental accounts there rose 47% y-y to 796,000; and 2) it booked financial lease sales of KRW20b following the launch of new products/services [the subsidiary targeted Malaysia's high-end market through 1Q18 before turning to the low-end segment in 2Q by launching a low-priced product with a seven-year maturity]. Meanwhile, its ODM exports (which account for 15% of its overseas sales; geared towards China) edged up 2% y-y, with sales at the US and Thai subsidiaries growing 11% and 14% y-y, respectively. The firm books both operating sales (eg, installment sales during a rental period) and financial lease sales, which can be confusing in understanding its fundamentals. We believe that the rental account number trend is the most accurate gauge in assessing its fundamentals.

SUMMARY OF 2Q RESULTS

(KRWb)	2Q18	Chg		Diff (%)	
		(% y-y)	(% q-q)	Samsung	Consensus
Sales	678.1	8.8	4.7	1.4	2.5
Operating profit	129.3	7.2	(1.5)	(2.2)	(0.8)
Pre-tax profit	122.7	(2.6)	(3.9)	(2.3)	(2.6)
Net profit	90.7	(4.7)	(4.7)	(2.4)	(4.1)
Margins (%)					
Operating profit	19.1				
Pre-tax profit	18.1				
Net profit	13.4				

Source: Company data, Samsung Securities estimates

VALUATION SUMMARY

	2017	2018E	2019E
Multiples (x)			
P/E	21.5	19.4	17.1
P/B	7.2	6.4	5.6
EV/EBITDA	10.6	10.1	8.9
Div yield (%)	3.4	3.4	3.7
EPS growth (% y-y)	39.2	10.7	13.6
ROE (%)	20.1	30.1	34.5
Per-share data (KRW)			
EPS	4,361	4,827	5,483
BVPS	12,938	14,659	16,766
DPS	3,200	3,500	4,000

- Coway's domestic household electronics rental and financial lease sales together rose 3% y-y in 2Q. Rental sales expanded just 1% y-y, despite a 4% y-y hike in the number of rental accounts, due to an ARPU decline, which stemmed from: 1) deteriorating product mix [on a rising portion of air purifiers]; and 2) it starting to offer low-end products [in order to defend its market share]. That its earnings are still being affected by intensifying competition is disappointing, but we are upbeat towards the facts that: 1) its rental account number is growing; and 2) its market share is holding up well. The firm should start making available its standalone closet product with clothes freshening systems (which it has been selling since May) via a rental channel from August—this development could boost its rental sales in 2H, though we have not reflected it in our earnings forecasts due to the high degree of uncertainty surrounding the outcome. Meanwhile, financial lease sales jumped 35% y-y, led by a 22% y-y hike in sales volume, an increase in cumulative rental numbers, and greater fees from services (eg, mattress cleaning and topper exchanges).

Still a BUY: Reflecting the in-line 2Q results, we fine-tune our 2018 earnings forecasts for the firm, expecting its full-year sales and operating profit to climb 7% and 8%, respectively, to KRW2.70t and KRW510.6b. We leave our target price unchanged at KRW105,000, which equates to a 2018 P/E of 22x, the average since its current major shareholder took the helm in 2013. Considering the growth potential of its overseas operations, the player deserves a higher valuation in our view, though we conservatively set our target price due to the sustained intense competition in the domestic market. We maintain BUY given the degree of upside (12%).

Results and forecasts

	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18P	3Q18E	4Q18E	2016	2017	2018E	2019E
Summary (KRWb)												
Sales	610.2	623.4	629.6	653.6	647.8	678.1	679.7	696.3	2,376.3	2,516.8	2,701.9	2,894.6
Gross profit	417.1	428.5	434.6	438.1	446.0	460.0	466.8	477.3	1,564.2	1,718.3	1,850.1	1,982.1
Operating profit	120.9	120.6	124.2	107.1	131.3	129.3	133.3	116.7	338.8	472.7	510.6	576.4
Pre-tax profit	100.6	126.0	124.2	89.1	127.8	122.7	126.6	110.1	323.8	439.9	487.2	553.9
Net profit	75.4	95.2	93.4	61.6	95.2	90.7	93.7	81.0	243.3	325.6	360.7	410.0
Margins (%)												
Gross profit	68.4	68.7	69.0	67.0	68.8	67.8	68.7	68.5	65.8	68.3	68.5	68.5
Operating profit	19.8	19.3	19.7	16.4	20.3	19.1	19.6	16.8	14.3	18.8	18.9	19.9
Pre-tax profit	16.5	20.2	19.7	13.6	19.7	18.1	18.6	15.8	13.6	17.5	18.0	19.1
Net profit	12.4	15.3	14.8	9.4	14.7	13.4	13.8	11.6	10.2	12.9	13.3	14.2
Chg (% y-y)												
Sales	(2.2)	12.3	7.9	6.4	6.2	8.8	8.0	6.5	2.6	5.9	7.4	7.1
Gross profit	0.1	20.4	11.1	9.3	6.9	7.4	7.4	9.0	(1.4)	9.9	7.7	7.1
Operating profit	(2.2)	919.4	16.1	11.1	8.6	7.2	7.3	9.0	(26.9)	39.5	8.0	12.9
Pre-tax profit	(19.7)	2,308.1	37.9	(13.7)	27.0	(2.6)	2.0	23.6	(28.8)	35.9	10.8	13.7
Net profit	(20.8)	3,331.5	38.0	(20.6)	26.2	(4.7)	0.4	31.5	(29.1)	33.8	10.8	13.7
Chg (% q-q)												
Sales	(0.6)	2.2	1.0	3.8	(0.9)	4.7	0.2	2.4				
Gross profit	4.1	2.7	1.4	0.8	1.8	3.2	1.5	2.2				
Operating profit	25.4	(0.3)	3.0	(13.8)	22.6	(1.5)	3.0	(12.4)				
Pre-tax profit	(2.5)	25.3	(1.5)	(28.3)	43.5	(3.9)	3.2	(13.0)				
Net profit	(2.9)	26.2	(1.9)	(34.0)	54.5	(4.7)	3.3	(13.6)				
Sales breakdown												
Household electronics												
Outright sales	479.1	496.9	496.8	493.0	493.4	502.0	501.4	507.3	1,961.3	1,965.8	2,004.1	2,097.9
Rental	45.9	50.4	47.3	48.6	43.9	47.3	47.3	47.9	195.7	192.2	186.3	201.5
Membership	369.5	379.5	378.5	378.5	378.7	382.7	386.1	391.2	1,492.6	1,506.0	1,538.8	1,621.9
Financial lease	37.8	36.7	35.9	34.3	32.2	31.1	30.5	29.2	167.5	144.7	123.0	110.7
Exports	25.9	30.2	35.1	31.6	38.6	40.9	37.6	38.9	105.4	122.8	156.0	163.8
Cosmetics	68.0	55.5	68.6	67.6	54.3	71.8	75.5	78.8	217.0	259.7	280.5	322.5
Other (water treatment)	20.9	18.7	19.4	20.7	20.6	18.6	21.3	27.2	74.2	79.7	87.7	92.1
Consolidated other	3.9	3.9	4.0	3.4	3.2	3.4	4.0	4.6	-48.0	15.2	15.2	15.2
Chg (% y-y)	38.3	48.3	40.8	69.0	76.2	82.3	77.5	78.4	171.8	196.4	314.4	366.9
Household electronics												
Outright sales	(3.2)	(2.4)	3.7	3.2	3.0	1.0	0.9	2.9	4.2	0.2	1.9	4.7
Rental	(8.9)	(6.7)	11.0	(0.2)	(4.5)	(6.2)	0.0	(1.5)	14.3	(1.8)	(3.1)	8.2
Membership	(2.8)	(1.2)	3.0	4.9	2.5	0.9	2.0	3.4	0.1	0.9	2.2	5.4
Financial lease	(11.9)	(13.5)	(14.7)	(14.3)	(14.9)	(15.4)	(15.0)	(14.7)	(6.8)	(13.6)	(15.0)	(10.0)
Exports	20.5	5.5	30.2	11.5	49.3	35.3	7.0	23.0	157.7	16.5	27.0	5.0
Cosmetics	19.8	(7.1)	42.6	29.1	(20.1)	29.3	10.0	16.7	45.4	19.7	8.0	15.0
Other (water treatment)	4.0	8.3	6.9	10.8	(1.6)	(0.7)	10.0	31.5	(10.7)	7.4	10.0	5.0
Consolidated other	(33.2)	(106.1)	(22.2)	(24.7)	(17.5)	(12.8)	0.0	34.8	(204.0)	(131.6)	0.0	0.0
Portion of total sales (%)	(16.9)	50.7	23.7	13.7	99.2	70.2	90.0	13.7	11.6	14.3	60.1	16.7
Household electronics												
Outright sales	78.5	79.7	78.9	75.4	76.2	74.0	73.8	72.9	82.5	78.1	74.2	72.5
Rental	7.5	8.1	7.5	7.4	6.8	7.0	7.0	6.9	8.2	7.6	6.9	7.0
Membership	60.6	60.9	60.1	57.9	58.5	56.4	56.8	56.2	62.8	59.8	57.0	56.0
Financial lease	6.2	5.9	5.7	5.2	5.0	4.6	4.5	4.2	7.0	5.8	4.6	3.8
Exports	4.2	4.8	5.6	4.8	6.0	6.0	5.5	5.6	4.4	4.9	5.8	5.7
Cosmetics	11.1	8.9	10.9	10.3	8.4	10.6	11.1	11.3	9.1	10.3	10.4	11.1
Other (water treatment)	3.4	3.0	3.1	3.2	3.2	2.7	3.1	3.9	3.1	3.2	3.2	3.2
Consolidated other	0.6	0.6	0.6	0.5	0.5	0.5	0.6	0.7	(2.0)	0.6	0.6	0.5

Source: Company data, Samsung Securities estimates

Accounts overview

Accounts ('000)	1Q15	2Q15	3Q15	4Q15	1Q16	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18
Total	5,661	5,714	5,730	5,771	5,794	5,846	5,732	5,704	5,713	5,746	5,745	5,748	5,784	5,842
Chg (% y-y)	3.5	3.2	2.8	2.8	2.4	2.3	0.0	(1.2)	(1.4)	(1.7)	0.2	0.8	1.3	1.7
Rental	4,666	4,747	4,780	4,832	4,861	4,921	4,823	4,849	4,875	4,923	4,935	4,970	5,032	5,106
Chg (% y-y)	4.7	5.8	5.3	5.0	4.2	3.7	0.9	0.4	0.3	0.0	2.3	2.5	3.2	3.7
Membership	994	967	950	939	933	924	908	854	838	823	810	778	752	735
Chg (% y-y)	(2.0)	(8.1)	(8.1)	(7.6)	(6.2)	(4.4)	(4.5)	(9.0)	(10.2)	(11.0)	(10.8)	(8.9)	(10.2)	(10.7)
Rental cancellations	134	143	151	138	146	148	224	183	174	175	148	128	152	167
Monthly churn (%)	0.97	1.02	1.06	0.97	1.01	1.02	1.52	1.26	1.20	1.20	1.00	0.87	1.02	1.10
Rental account additions	341	371	338	359	351	385	285	381	350	397	318	317	377	389
Chg (% y-y)	7.5	(0.1)	8.7	8.4	2.9	3.7	(15.6)	5.8	(0.3)	3.2	11.5	(16.6)	7.9	(2.0)
Outright sales account additions	40	60	63	63	66	68	54	57	55	78	62	56	49	54
Chg (% y-y)	0.1	1.3	21.5	95.9	67.2	12.2	(14.8)	(8.9)	(17.6)	14.5	14.8	(1.6)	(10.1)	(30.3)

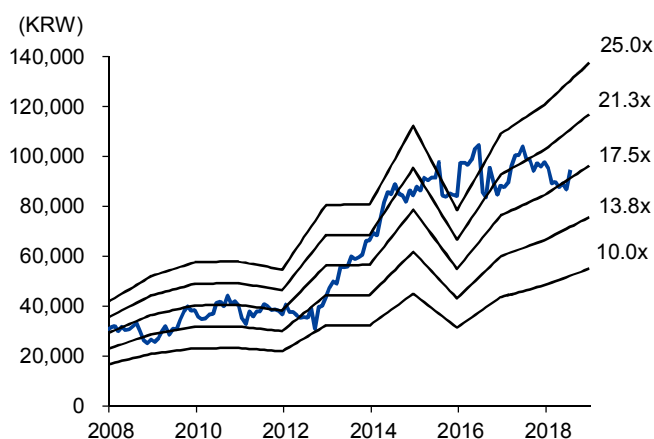
Source: Company data, Samsung Securities estimates

Forecasts and valuations

Year-end Dec 31	Sales (KRWb)	Operating profit (KRWb)	Pre-tax profit (KRWb)	Net profit (KRWb)	EPS (KRW)	Chg (% y-y)	P/E (x)	P/B (x)	ROE (%)	EV/EBITDA (x)	Net debt (KRWb)
2015	2,315	463	454	343	4,492	39.3	20.9	6.1	30.1	10.7	(38)
2016	2,376	339	324	243	3,134	(30.2)	29.9	6.1	20.1	12.9	210
2017	2,517	473	440	326	4,361	39.2	21.5	7.2	30.1	10.6	512
2018E	2,702	511	487	361	4,827	10.7	19.4	6.4	34.5	10.1	493
2019E	2,895	576	554	410	5,483	13.6	17.1	5.6	34.5	8.9	429
2020E	3,115	625	605	448	5,981	9.1	15.7	5.0	33.2	8.0	353

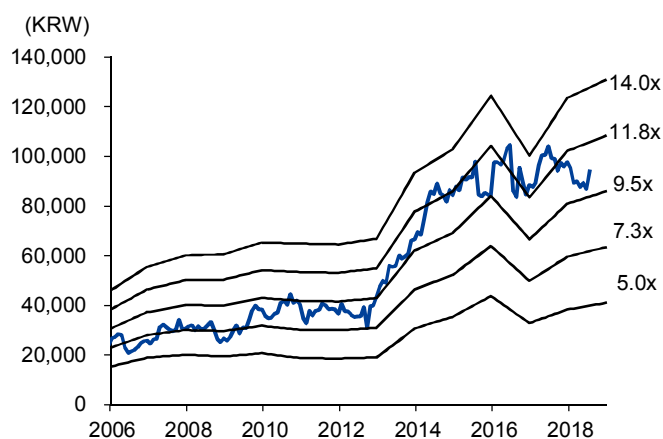
Source: Company data, Samsung Securities estimates

Forward P/E



Source: Company data, Samsung Securities estimates

Forward EV/EBITDA



Source: Company data, Samsung Securities estimates

Income statement

Year-end Dec 31(KRWb)	2016	2017	2018E	2019E	2020E
Sales	2,376	2,517	2,702	2,895	3,115
Cost of goods sold	812	798	852	913	982
Gross profit	1,564	1,718	1,850	1,982	2,133
Gross margin (%)	65.8	68.3	68.5	68.5	68.5
SG&A expenses	1,225	1,246	1,339	1,406	1,508
Operating profit	339	473	511	576	625
Operating margin (%)	14.3	18.8	18.9	19.9	20.1
Non-operating gains (losses)	(15)	(33)	(23)	(22)	(21)
Financial profit	1	1	1	1	1
Financial costs	6	12	16	15	13
Equity-method gains (losses)	0	0	0	0	0
Other	(10)	(22)	(8)	(8)	(8)
Pre-tax profit	324	440	487	554	605
Taxes	80	114	127	144	157
Effective tax rate (%)	24.8	26.0	26.0	26.0	26.0
Profit from continuing operations	243	326	361	410	448
Profit from discontinued operations	0	0	0	0	0
Net profit	243	326	361	410	448
Net margin (%)	10.2	12.9	13.3	14.2	14.4
Net profit (controlling interests)	244	326	361	411	448
Net profit (non-controlling interests)	(0)	(0)	(1)	(1)	(1)
EBITDA	572	708	745	841	919
EBITDA margin (%)	24.1	28.1	27.6	29.1	29.5
EPS (parent-based) (KRW)	3,167	4,328	4,793	5,450	5,948
EPS (consolidated) (KRW)	3,163	4,321	4,786	5,442	5,939
Adjusted EPS (KRW)*	3,134	4,361	4,827	5,483	5,981

Cash flow statement

Year-end Dec 31(KRWb)	2016	2017	2018E	2019E	2020E
Cash flow from operations	358	554	597	677	741
Net profit	243	326	361	410	448
Non-cash profit and expenses	155	254	263	295	325
Depreciation	225	227	226	256	285
Amortization	8	8	8	8	8
Other	(78)	19	29	30	31
Changes in A/L from operating activities	(41)	(26)	(27)	(28)	(32)
Cash flow from investments	(367)	(290)	(347)	(361)	(375)
Change in tangible assets	(313)	(323)	(347)	(361)	(375)
Change in financial assets	(39)	(27)	0	0	0
Other	(16)	61	0	0	0
Cash flow from financing	(40)	(218)	(251)	(316)	(365)
Change in debt	264	330	(19)	(64)	(77)
Change in equity	0	0	(1)	0	0
Dividends	(208)	(409)	(231)	(252)	(288)
Other	(96)	(140)	0	(0)	0
Change in cash	(50)	44	0	0	0
Cash at beginning of year	116	66	110	110	110
Cash at end of year	66	110	110	110	110
Gross cash flow	399	580	624	705	772
Free cash flow	111	206	233	297	343

Note: * Excluding one off items, ** Fully diluted, excluding one-off items

*** From companies subject to equity-method valuation

Source: Company data, Samsung Securities estimates

Balance sheet

Year-end Dec 31(KRWb)	2016	2017	2018E	2019E	2020E
Current assets	733	791	815	838	866
Cash & equivalents	66	110	110	110	110
Accounts receivable	323	340	365	391	421
Inventories	70	75	80	86	93
Other current assets	274	266	259	251	242
Fixed assets	1,235	1,367	1,458	1,532	1,592
Investment assets	89	89	89	89	89
Tangible assets	669	712	803	877	937
Intangible assets	183	184	184	184	184
Other long-term assets	293	382	382	382	382
Total assets	1,968	2,159	2,273	2,371	2,458
Current liabilities	735	1,125	1,110	1,050	978
Accounts payable	59	54	58	62	67
Short-term debt	34	66	64	58	51
Other current liabilities	643	1,004	987	930	861
Long-term liabilities	49	52	52	52	52
Bonds & long-term debt	12	12	12	12	12
Other long-term liabilities	37	40	40	40	40
Total liabilities	784	1,177	1,162	1,102	1,030
Owners of parent equity	1,183	982	1,111	1,269	1,428
Capital stock	41	41	40	40	40
Capital surplus	127	129	129	129	129
Retained earnings	1,180	963	1,093	1,251	1,410
Other	(165)	(151)	(151)	(151)	(151)
Non-controlling interests' equity	1	0	0	0	0
Total equity	1,183	982	1,111	1,269	1,428
Net debt	210	512	493	429	353

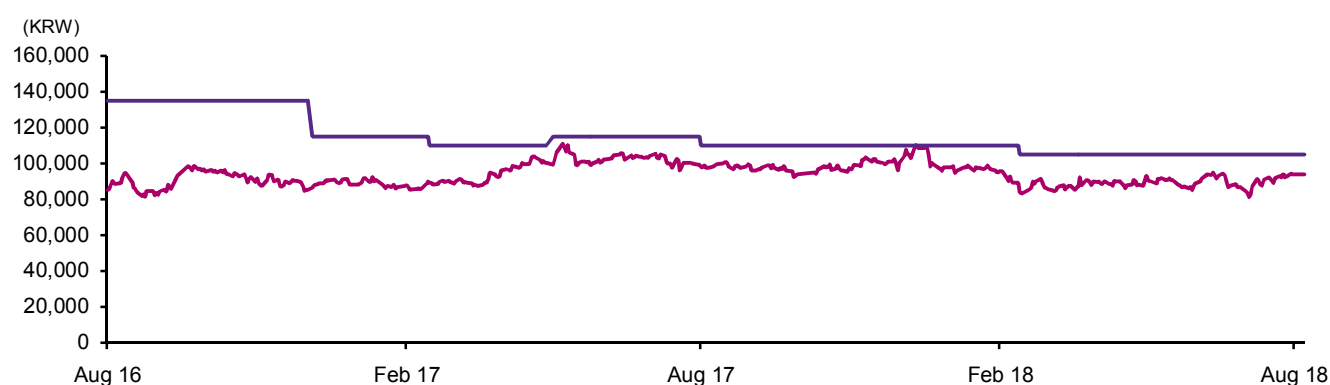
Financial ratios

Year-end Dec 31	2016	2017	2018E	2019E	2020E
Growth (%)					
Sales	2.6	5.9	7.4	7.1	7.6
Operating profit	(26.9)	39.5	8.0	12.9	8.5
Net profit	10.2	12.9	13.3	14.2	14.4
Adjusted EPS**	(30.2)	39.2	10.7	13.6	9.1
Per-share data (KRW)					
EPS (parent-based)	3,167	4,328	4,793	5,450	5,948
EPS (consolidated)	3,163	4,321	4,786	5,442	5,939
Adjusted EPS**	3,134	4,361	4,827	5,483	5,981
BVPS	15,496	12,938	14,659	16,766	18,891
DPS (common)	3,200	3,200	3,500	4,000	4,400
Valuations (x)					
P/E***	29.9	21.5	19.4	17.1	15.7
P/B***	6.1	7.2	6.4	5.6	5.0
EV/EBITDA	12.9	10.6	10.1	8.9	8.0
Ratios (%)					
ROE	30.1	20.1	30.1	34.5	34.5
ROA	13.0	13.0	15.8	16.3	17.7
ROIC	19.1	19.1	23.2	24.0	25.5
Payout ratio	96.4	96.4	70.9	70.0	70.4
Dividend yield (common)	3.0	3.4	3.4	3.7	4.3
Net debt to equity	(3.0)	17.8	52.1	44.4	33.9
Interest coverage (x)	55.5	55.5	38.3	31.8	38.2

Compliance notice

- As of Jul 31, 2018, the covering analyst(s) did not own any shares, or debt instruments convertible into shares, of any company covered in this report.
- As of Jul 31, 2018, Samsung Securities' holdings of shares and debt instruments convertible into shares of each company covered in this report would not, if such debt instruments were converted, exceed 1% of each company's outstanding shares.
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Target price changes in past two years



Rating changes over past two years (adjusted share prices)

Date	2016/2/17	12/4	2017/2/15	4/29	8/1	2018/2/13
Recommendation	BUY	BUY	BUY	BUY	BUY	BUY
Target price (KRW)	135,000	115,000	110,000	115,000	110,000	105,000
Gap* (average)	(29.81)	(22.99)	(14.66)	(10.98)	(10.52)	
(max or min)**	(16.30)	(19.48)	(5.45)	(3.48)	0.45	

Note: * [(average, maximum, or minimum share price over duration of target price minus target price) / target price] x 100%

** Maximum/minimum share price if new target is higher/lower than market close on the business day prior to target price change

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Company

BUY	Expected to increase in value by 10% or more within 12 months and is highly attractive within sector
HOLD	Expected to increase/decrease in value by less than 10% within 12 months
SELL	Expected to decrease in value by 10% or more within 12 months

Industry

OVERWEIGHT	Expected to outperform market by 5% or more within 12 months
NEUTRAL	Expected to outperform/underperform market by less than 5% within 12 months
UNDERWEIGHT	Expected to underperform market by 5% or more within 12 months

Percentage of ratings in 12 months prior to Jun 30, 2018

BUY (85.1%) | HOLD (14.9%) | SELL (0%)

Global Disclosures & Disclaimers

General

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