

Result Comment



Woongjin Coway (021240 KS)

Sun Kyung Lee
(82-2) 3772-1568
sunny.lee@goodi.com

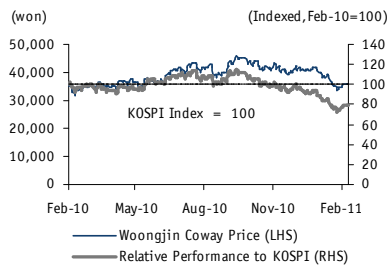
4Q10 results meet view, domestic cosmetics sales catching fire

BUY

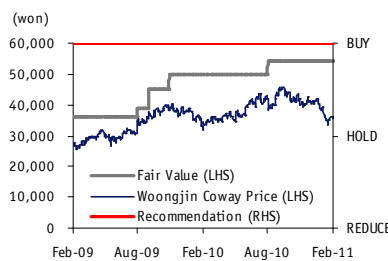
Share Price (Feb. 9) W35,650
Fair Value (% variance) W51,000 (43.1%)

Mkt Cap. W2,749.5bn/ US\$2,411.8mn
Average Daily Value W11,988mn
52 week High/Low W45,850/ W32,650

Share Price Performance



Fair Value & Recommendation History



- ◆ 4Q10 results, generally meeting our expectation
- ◆ Existing mainstay businesses had decent results, poor profitability caused by expanding cosmetics business
- ◆ Rapid cosmetics sales growth is positive
- ◆ Retain BUY, but revise down a fair value to W51,000

4Q10 results meet expectations Woongjin Coway posted 4Q10 sales of W403.2bn (+8.6% YoY), operating income of W53.7 bn (-6.1% YoY), and net income of W42.7 bn (+6.0% YoY) in line with the market's consensus. The sales growth of 8.6% was driven by mainstay businesses as well as strong cosmetics sales. However, the cosmetics division racked up a W9bn loss in 4Q10, leading to a YoY drop in 4Q10 operating income. Excluding the cosmetics division, Woongjin Coway's 4Q10 sales came in at W381.6 bn (+3% YoY), operating profit W62.7bn (10% YoY), and the operating profit margin 16.4%, the highest quarterly margin ever. The China subsidiary posted a net loss of W4.1bn in equity method losses due to lump-sum severance allowances under the IFRS and inventory disposal losses. It was more than offset by W12.8bn equity method gains from Woongjin Chemical, including a corporate tax refund. As a result, Woongjin Coway's equity method gains came to W5.1bn, exceeding our estimate of W4 bn.

Woongjin Coway 4Q10 results

(W bn)	4Q10P	4Q09	% YoY	3Q10	% QoQ	SH	Var. (%)	Cons.	2010P	2009	% YoY
Sales	403.2	371.4	8.6	378.0	6.7	397.3	1.5	402.3	1,519.1	1,411.9	7.6
Operating profit	53.7	57.1	(6.1)	57.1	(6.0)	52.3	2.7	53.7	228.8	204.3	12.0
Pre-tax profit	55.0	53.1	3.6	59.5	(7.6)	51.5	6.8	55.4	236.5	202.7	16.7
Net-profit	42.7	40.3	6.0	45.2	(5.5)	39.0	9.5	42.1	176.7	153.3	15.3
OP margin (%)	15.6	15.4		15.1		13.2		13.3	15.1	14.5	
PP margin (%)	13.6	14.3		15.7		13.0		13.8	15.6	14.4	
NP margin (%)	10.6	10.9		12.0		9.8		10.5	11.6	10.9	

Source: Woongjin Coway, FrnGuide, Shinhan Investment Corp.

Year to Dec.	Sales (W bn)	OP (W bn)	Pre-tax (W bn)	NP (W bn)	EPS (Won)	Growth (%)	PER (x)	EV/EBITDA (x)	PBR (x)	ROE (%)	Net Debt Ratio (%)	Div. Yield (%)
2008	1,314.4	190.1	184.8	129.1	1,734	11.0	18.5	6.3	4.0	22.9	14.4	2.7
2009	1,411.9	204.3	202.7	153.3	2,023	16.7	19.3	7.9	4.4	24.0	29.5	2.6
2010P	1,519.2	228.8	236.1	176.4	2,287	13.0	16.1	7.3	3.7	24.4	30.0	2.8
2011E	1,674.3	242.6	249.4	189.1	2,452	7.2	14.5	6.7	3.2	23.1	21.4	3.1
2012E	1,788.1	269.7	288.3	218.6	2,834	15.6	12.6	6.2	2.7	23.3	9.6	3.6

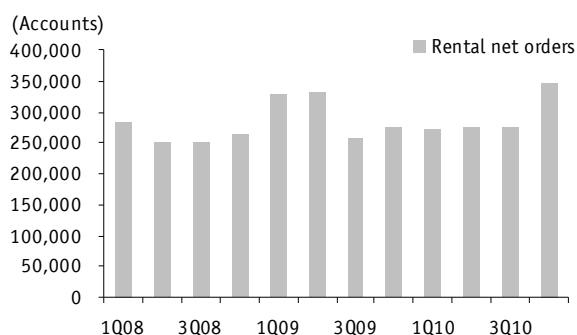
Mainstay businesses deliver decent results, expanding cosmetics business pulls down margins Rental orders grew to a net 346,000 in 4Q10, up 26% YoY and the cancellation rate was 1.03%. Rental customer accounts rose 6.3% YoY and 3.0% QoQ to 4,150,000 for 4Q10 rental sales growth of 6.8% YoY. Lump-sum accounts decreased 21% YoY due to the high base of comparison with 4Q09 when the H1N1 flu outbreak boosted sales. Sales still increased 12.4% YoY, thanks to increasing sales of high-price items.

The rental cost ratio stood at 27.5%, slightly higher than 3Q10 and 4Q09. Increasing parts replacement costs and higher sales commission fees were to blame. The overall cost ratio including low-cost cosmetics operations stood at 30.9%, down 2.1%p QoQ and down 2.0%p YoY. However, the bulk of cosmetics business costs are SG&A expenses, which outweighed an improvement in the cost ratio. The 4Q10 SG&A ratio was 55.8% (+4.1%p YoY and +3.9%p QoQ), and the operating profit margin slowed to 13.3%.

		4Q10 results by business segment				
(W bn)		4Q10	4Q09	% YoY	3Q10	% QoQ
Sales	Total	403.3	371.4	8.6	378.1	6.7
	Rental fees	284.4	266.2	6.8	276.7	2.8
	Membership fees	38.0	34.8	9.2	37.5	1.3
	Lump-sum payments	31.4	27.9	12.4	24.5	28.2
	Cosmetics	21.6			1.8	1,100.0
	Exports	19.4	14.6	33.1	15.3	26.8
	Water treatment	2.2	9.5	(76.8)	8.4	(73.8)
	others	6.3	18.4	(65.8)	13.9	(54.7)
Cost of sales	Total	124.5	122.4	1.7	124.7	(0.2)
	Rental fees	78.2	71.7	9.1	74.7	4.7
	Membership fees	11.6	9.9	17.1	11.7	(0.9)
	Lump-sum payments	11.0	7.9	39.2	9.3	18.3
	Exports	15.0	10.6	41.5	11.2	33.9
	Water treatment	1.7	7.2	(76.4)	6.2	(72.6)
	others	7.0	15.1	(53.6)	11.6	(39.7)
	COGS Ratio (%)	Total	30.9	32.9		33.0
Rental fees		27.5	26.9		27.0	
Membership fees		30.5	28.5		31.2	
Lump-sum payments		35.0	28.3		38.0	
Exports		77.3	72.7		73.2	
Water treatment		77.3	75.8		73.8	
others		25.1	82.1		73.9	
Gross profit		278.8	249.1	11.9	253.4	10.0
GP margin (%)	69.1	67.1		67.0		
SG&A	225.0	191.9	17.3	196.2	14.7	
SG&A/Sales (%)	55.8	51.7		51.9		
Operating profit	53.7	57.2	(6.1)	57.1	(6.0)	
OP margin (%)	13.3	15.4		15.1		

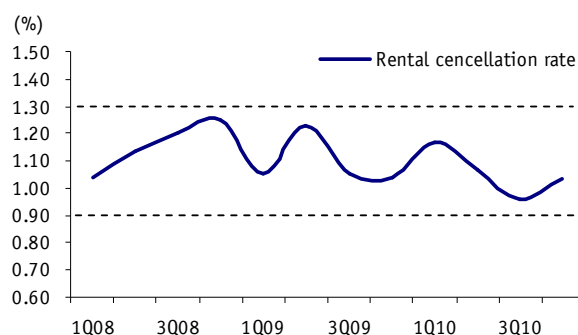
Source: Woongjin Coway, Shinhan Investment Corp.

4Q10 net rental order growth: 26%



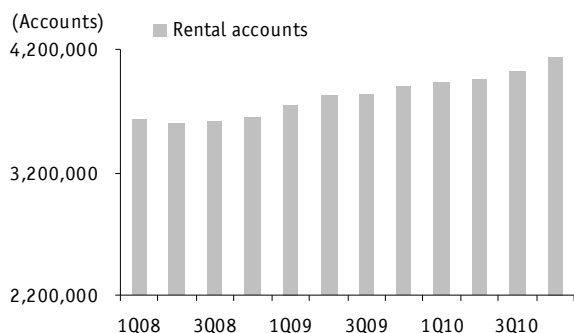
Source: Woongjin Coway, Shinhan Investment Corp.

Monthly cancellation rate trend



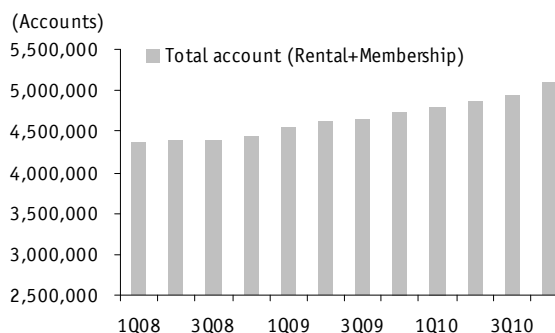
Source: Woongjin Coway, Shinhan Investment Corp.

Steady growth in rental accounts



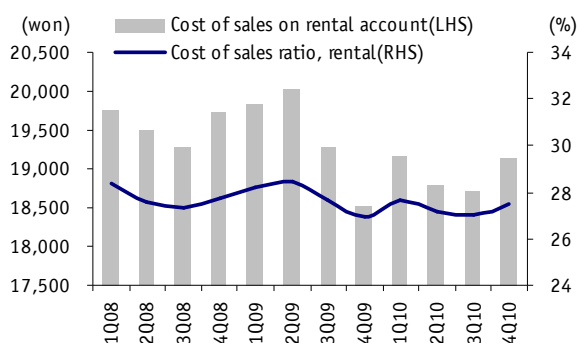
Source: Woongjin Coway, Shinhan Investment Corp.

Growth in all accounts (rental+membership)



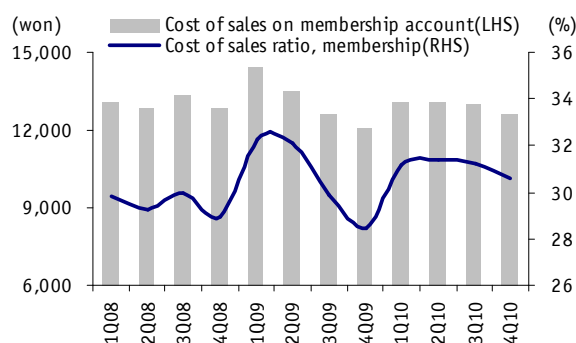
Source: Woongjin Coway, Shinhan Investment Corp.

Rental account cost ratio trend



Source: Woongjin Coway, Shinhan Investment Corp.

Membership account cost ratio trend



Source: Woongjin Coway, Shinhan Investment Corp.

China unit growth and margins weaken In 4Q10, sales from the Chinese operations increased 15.8% in yuan terms, compared to a year ago. Cosmetics sales grew 25% YoY and environmental electronics sales fell 5% YoY. Increased marketing costs associated with heavy ad spending in the start-up period and workforce restructuring costs put a dent on the cosmetics operating profit margin, which stood at 23%. The environmental electronics division chalked up a large net loss. Ahead of the IFRS rollout, lump-sum severance allowances were booked, and environmental electronics inventory losses added to one-time costs. In won terms, the China unit registered a net loss of W4.1bn.

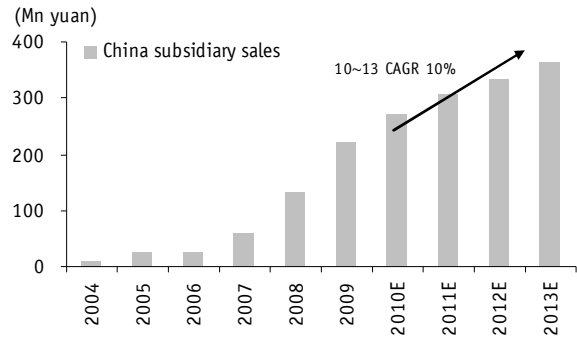
Chinese subsidiary 4Q10 results

('000 RMB)		1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	% YoY	% QoQ
Sales	Cosmetics	27,842	45,832	52,051	40,243	42,612	61,656	54,665	50,347	25.1	(7.9)
	Environmental Electronics	12,755	11,719	13,900	18,133	13,865	14,747	16,373	17,227	(5.0)	5.2
	Total	40,597	57,551	65,951	58,376	56,477	76,403	71,038	67,574	15.8	(4.9)
Operating profit	Cosmetics	11,127	28,841	20,447	14,616	15,291	23,454	17,572	11,729	(19.8)	(33.3)
	Environmental Electronics	(76)	(2,773)	(395)	178	(307)	(320)	(808)	(7,701)	TR	CR
	Total	11,051	26,068	20,052	14,794	14,984	23,134	16,764	4,028	(72.8)	(76.0)
OP margin (%)	Cosmetics	40.0	62.9	39.3	36.3	35.9	38.0	32.1	23.3		
	Environmental Electronics	(0.6)	(23.7)	(2.8)	1.0	(2.2)	(2.2)	(4.9)	(44.7)		
	Total	27.2	45.3	30.4	25.3	26.5	30.3	23.6	6.0		

Source: Woongjin Coway, Shinhan Investment Corp.

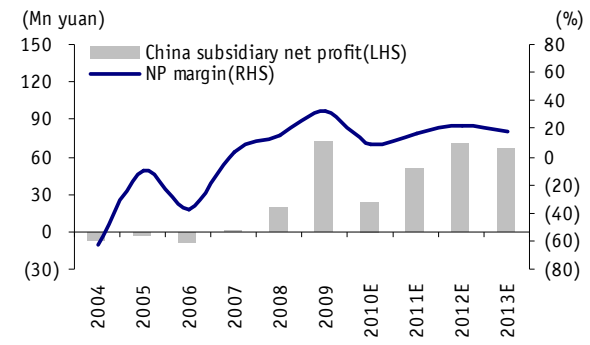
The pace of expansion in coverage areas for door-to-door cosmetics sales is slower than expected and retail sales channel expansion is also falling short. Moreover, advertising and marketing expenses associated with retail sales channel expansion will rise, bringing down the cosmetics operating profit margin to around 25%.

Chinese subsidiary sales trend and forecast



Source: Woongjin Coway, Shinhan Investment Corp.

Chinese subsidiary net-profit trend and forecast



Source: Woongjin Coway, Shinhan Investment Corp.

Domestic cosmetics sales growth accelerates The domestic cosmetics division, launched in August 2010, posted sales of W23.4bn, more than double the sales target of W10bn, with a net loss of W13bn in 2010.

Woongjin Coway's 2011 guidance calls for cosmetics sales of W60bn and an operating loss of W14bn. The company sees cosmetics sales of W100bn in 2012 with an operating profit margin of 5%. Under the plan, Woongjin Coway is ramping up a workforce restructuring and a marketing campaign using its CODY network and expanding retail sales channels to department stores, duty-free shops, and home-shopping channels. It is also broadening its new product line-up. Its CODY network will come handy for providing existing customers with cosmetics samples. Additionally, it plans to launch a men's cosmetics line and a whitening product line in February and herbal cosmetics in April.

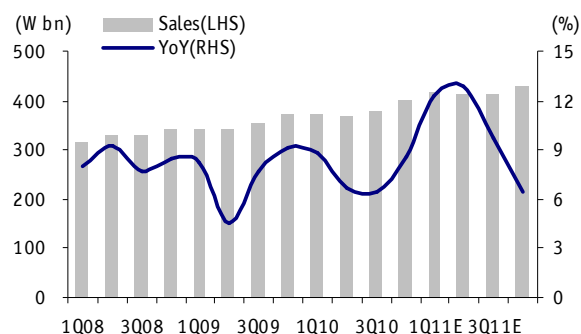
Retain BUY, but revise down fair value to W51,000 We revise down Woongjin Coway's fair value from W54,000 to W51,000. We maintain our BUY rating in view of a 43% upside potential at the current price level. The fair value reduction reflects increasing costs and working capital needs due to new business rollouts. Investments in the cosmetics business can be justified by the company's long-term growth strategy, and the level of investment looks manageable in light of the company's free cash flow. Cosmetics-related marketing costs will continue to increase in 2011, but operating income will hold steady on rental business growth and margin strength. If cosmetics sales continue to grow at the current pace, the cosmetics business will begin contributing to profits in 2012.

Valuation table

		2011E	2012E	2013E	2014E	2015E	2016E
Operating profit	a	242.6	269.7	294.9	311.8	321.2	357.9
Depreciation & Amortization	b	143.8	142.4	144.1	145.8	166.0	164.6
Non-cash costs (rental disposal, etc)	c	52.8	54.6	57.1	59.1	60.8	62.7
EBITDA	a+b+c	439.2	466.7	496.1	516.7	548.1	585.1
Tax rate (%)		25.3	24.2	24.2	24.2	24.2	24.2
EBITDA*(1-t)	A	328.1	353.8	376.1	391.7	415.4	443.5
(Depreciation & Amortization + rental dispose)*t	B	49.7	47.7	48.7	49.6	54.9	55.0
Net working capital increase (decrease)	D	43.8	17.5	17.8	8.6	9.2	9.5
CAPEX	E	196.5	194.5	198.4	202.4	206.4	210.5
FCFF	A+B-C-D-E	137.6	189.4	208.6	230.2	254.7	278.5
Discount factor		0.93	0.79	0.73	0.67	0.62	0.57
PV of FCFF		127.8	149.5	151.6	154.2	157.2	158.3
Total PV of FCFF(until 2016)	d	898.6					
Terminal value of end of 2015		5,179.2	Permanent growth rate of 3%				
NPV of terminal value	e	2,944.3	WACC 8.6%				
Total firm value	d+e	3,842.9					
Total debt	f	230.6					
Cash & cashable assets	g	68.9					
Shares available for sales	h	3.1					
Woongjin Chemical market value	I	204.3	20% discount from market price				
China subsidiaries value	j	17.0	2011 expected net profit * P/E 20x (share holding ratio of 100%)				
Total value of equity	d+e-f+g+h+I+j	3,905.6					
Total no. of stocks issued (000')		77,125					
Treasury stocks (000')		1,060					
Value per share (won)		51,346					
Fair value (won)		51,000					
Current price		35,650	2011-02-09				
Upside potential (%)		43.1					
2011E EPS (won)		2,455					
Implied PER (x)		20.8					

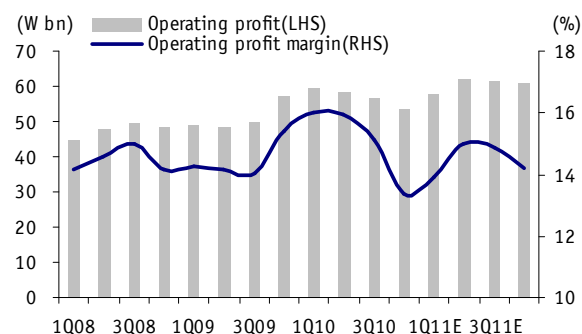
Source: Shinhan Investment Corp.

Quarterly sales trend and outlook



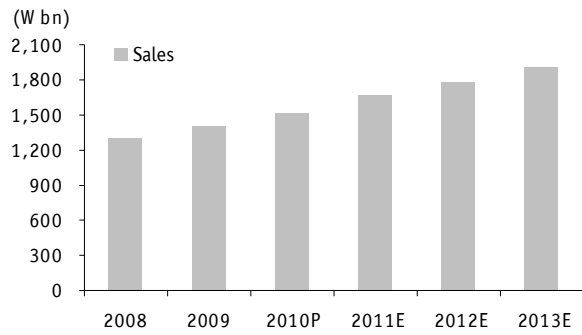
Source: Woongjin Coway, Shinhan Investment Corp.

Quarterly operating profit trend and outlook



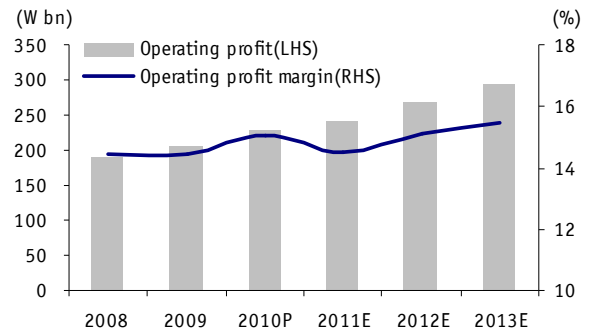
Source: Woongjin Coway, Shinhan Investment Corp.

Yearly sales trend and outlook



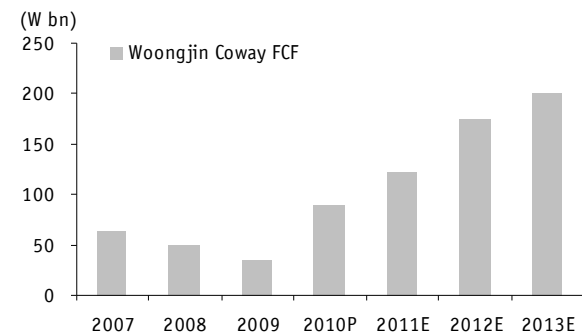
Source: Woongjin Coway, Shinhan Investment Corp.

Yearly operating profit trend and outlook



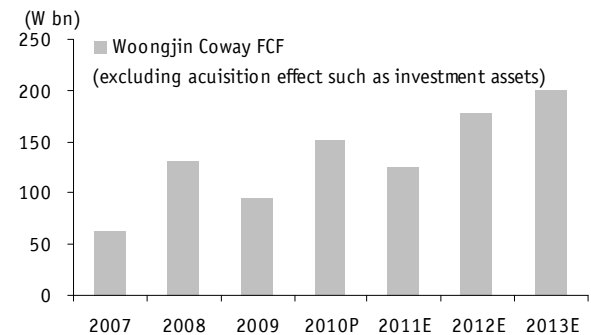
Source: Woongjin Coway, Shinhan Investment Corp.

Woongjin Coway's FCF trend and outlook



Source: Woongjin Coway, Shinhan Investment Corp.

FCF trend excluding investment assets and business acquisitions



Source: Woongjin Coway, Shinhan Investment Corp.

Balance Sheet

Year to Dec. (W bn)	2008	2009	2010P	2011E	2012E
Total Assets	1,071.4	1,270.7	1,384.1	1,413.2	1,444.0
Current Assets	475.6	509.5	526.8	523.5	517.7
Cash & Cash Equivalents	76.1	63.7	81.7	35.1	9.4
St. Investment Assets	5.9	5.5	7.1	8.6	12.9
Accounts Receivable	149.8	194.6	191.5	224.8	240.0
Inventory	58.0	54.6	60.4	73.4	78.4
Others	185.8	191.1	186.2	181.6	177.0
Non-current Assets	595.8	761.2	857.2	889.7	926.3
Investment Assets	114.1	130.7	214.9	242.1	274.4
Tangible Assets	356.4	418.2	446.8	467.3	484.2
Intangible Assets	64.9	141.1	122.2	104.7	89.8
Total Liabilities	474.8	590.0	619.5	540.4	437.7
Current Liabilities	398.7	541.8	420.7	451.7	489.1
Accounts Payable	34.2	29.2	32.1	34.7	37.5
St. Debt	107.8	119.7	38.3	30.6	29.1
Current Portion of Lt. Debt	0.0	120.0	80.0	110.0	140.0
Others	256.7	272.8	270.3	276.4	282.5
Non-current Liabilities	76.0	48.2	198.7	88.7	(51.3)
Bonds	0.0	0.0	0.0	0.0	(50.0)
Lt. Debt	60.0	30.0	200.0	90.0	0.0
Others	16.0	18.2	(1.3)	(1.3)	(1.3)
Total Stockholders Equity	596.6	680.7	764.6	872.8	1,006.3
Paid-in Capital	39.3	40.7	40.7	40.7	40.7
Capital Surplus	108.7	141.9	140.3	140.3	140.3
Capital Adjustment	6.2	(31.5)	(41.4)	(41.4)	(41.4)
Other Accumulated Earnings	1.3	0.0	(4.1)	(4.1)	(4.1)
Retained Earnings	441.1	529.6	629.2	737.4	870.8
Total Debt	167.8	269.7	318.3	230.6	119.1
Net Debt(Cash)	85.8	200.5	229.5	187.0	96.8

Cash Flow

Year to Dec. (W bn)	2008	2009	2010P	2011E	2012E
Cash Flows from Operating	304.8	311.7	368.8	333.9	386.5
Net Profit	129.1	153.3	176.4	189.1	218.6
Depreciation	126.5	128.2	124.1	126.3	127.4
Amortization	14.7	19.9	21.7	17.5	15.0
Equity Method Loss(Gain)	1.4	(13.9)	(22.0)	(23.9)	(29.0)
Investment Asset Disp Loss(Gain)	0.0	1.1	0.0	0.0	0.0
Tangible Asset Disp Loss(Gain)	2.5	0.4	0.3	0.0	0.0
Changes in Working Capital	(36.2)	(48.9)	(3.6)	(49.3)	(22.5)
Others	66.9	71.6	72.0	74.3	77.0
Cash Flows from Investing	(255.1)	(276.1)	(279.1)	(210.9)	(211.8)
St. Investment Assets Dec.(Inc.)	(4.2)	(0.1)	(1.6)	(1.4)	(4.3)
Investment Securities Dec.(Inc.)	(82.4)	2.8	(62.0)	(3.0)	(3.0)
Tangible Assets Dec.(Inc.)	(142.0)	(204.1)	(200.5)	(196.5)	(194.5)
Others	(26.4)	(74.8)	(15.0)	(10.0)	(10.0)
Free Cash Flow	49.7	35.5	89.7	123.0	174.7
Cash Flows from Financing	(2.1)	(52.3)	(71.7)	(169.6)	(200.4)
St. Debt Inc.(Dec.)	15.8	(18.6)	(81.4)	(7.7)	(1.5)
Cur. Por. of Lt. Debt Inc.(Dec.)	(20.0)	0.0	(40.0)	30.0	30.0
Bonds Inc.(Dec.)	0.0	0.0	0.0	0.0	(50.0)
Lt. Debt Inc.(Dec.)	60.0	0.0	170.0	(110.0)	(90.0)
Share Capital Inc.(Dec.)	0.0	0.0	(1.7)	0.0	0.0
Dividend Paid	(58.1)	(64.8)	(76.8)	(80.9)	(85.1)
Others	0.1	31.0	(41.8)	(1.0)	(3.8)
Change in Cash	47.6	(12.4)	18.0	(46.6)	(25.7)
Beginning Cash	28.5	76.1	63.7	81.7	35.1
Ending Cash	76.1	63.7	81.7	35.1	9.4
Capex/ Sales (%)	10.8	14.5	13.2	11.7	10.9
Depreciation/ Sales (%)	9.6	9.1	8.2	7.5	7.1
Depreciation/ Capex (%)	89.1	62.8	61.9	64.3	65.5

Source: Company data, Shinhan Investment Corp. estimates

Profit and Loss

Year to Dec. (W bn)	2008	2009	2010P	2011E	2012E
Net Sales	1,314.4	1,411.9	1,519.2	1,674.3	1,788.1
Growth (%)	8.4	7.4	7.6	10.2	6.8
Export ratio (%)	0.0	0.0	4.0	4.6	5.5
Cost of Sales	407.2	460.2	494.2	530.5	573.1
Growth (%)	5.8	13.0	7.4	7.3	8.0
Gross Profit	907.2	951.8	1,025.0	1,143.9	1,215.0
Gross Margin(%)	69.0	67.4	67.5	68.3	67.9
SG&A Expenses	717.1	747.5	796.2	901.3	945.3
Growth (%)	7.5	4.2	6.5	13.2	4.9
Operating Profit	190.1	204.3	228.8	242.6	269.7
Growth (%)	17.9	7.4	12.0	6.0	11.2
Operating Margin(%)	14.5	14.5	15.1	14.5	15.1
Non-Operating Inc (Exp)	(5.4)	(1.5)	7.4	6.9	18.6
Interest Income	3.3	3.1	3.4	3.7	1.3
Interest Expenses	11.3	12.5	18.0	17.6	12.2
Net F/X	10.5	(5.2)	(0.4)	(0.3)	0.0
Net Asset Disposal	(2.5)	(1.5)	(0.3)	0.0	0.0
Net Equity Method	(1.4)	13.9	22.0	23.9	29.0
Net Other non-operating	(3.9)	0.7	0.5	(2.7)	0.6
Pre-tax Profit from Cont. Op	184.8	202.7	236.1	249.4	288.3
Income Taxes	55.7	49.4	59.7	60.4	69.8
Profit from Cont. Op	129.1	153.3	176.4	189.1	218.6
Profit from Discort. Op	0.0	0.0	0.0	0.0	0.0
Net Profit	129.1	153.3	176.4	189.1	218.6
Growth (%)	11.0	18.8	15.1	7.2	15.6
Net Margin(%)	9.8	10.9	11.6	11.3	12.2
EBITDA	394.3	400.7	422.4	435.9	462.3
Growth (%)	7.8	1.6	5.4	3.2	6.0
Dividend Payout (%)	50.2	50.1	45.9	45.0	45.0

Key Ratios

Year to Dec.	2008	2009	2010P	2011E	2012E
EPS (won)	1,734	2,023	2,287	2,452	2,834
Adj. EPS (won)	1,768	2,043	2,291	2,452	2,834
BPS (won)	8,016	8,826	9,914	11,316	13,047
DPS (won)	870	1,010	1,049	1,103	1,275
PER (x)	18.5	19.3	16.1	14.5	12.6
Adj. PER (x)	18.2	19.1	16.1	14.5	12.6
PBR (x)	4.0	4.4	3.7	3.2	2.7
PCR (x)	7.0	8.2	7.6	7.2	6.7
EV/ EBITDA (x)	6.3	7.9	7.3	6.7	6.2
PEG (x)	1.5	1.6	1.4	1.2	na
Dividend Yield (%)	2.7	2.6	2.8	3.1	3.6
Profitability					
Operating Margin (%)	14.5	14.5	15.1	14.5	15.1
EBITDA Margin (%)	30.0	28.4	27.8	26.0	25.9
Pre-tax Profit Margin(%)	14.1	14.4	15.5	14.9	16.1
Net Margin (%)	9.8	10.9	11.6	11.3	12.2
ROA (%)	12.9	13.1	13.3	13.5	15.3
ROE (%)	22.9	24.0	24.4	23.1	23.3
ROIC (%)	22.2	22.9	22.1	23.1	24.9
Stability					
Debt Ratio (%)	79.6	86.7	81.0	61.9	43.5
Net Debt Ratio (%)	14.4	29.5	30.0	21.4	9.6
Interest Coverage (x)	16.8	16.3	12.7	13.8	22.0
Activity					
Asset Turnover (x)	1.3	1.2	1.1	1.2	1.3
Receivables Turnover (x)	9.2	7.9	7.7	7.9	7.6
Inventory Turnover (x)	22.7	25.1	26.4	25.0	23.6
Payables Turnover (x)	43.9	44.5	49.5	50.1	49.5
Working Capital Turnover (x)	14.0	11.7	11.1	11.0	10.4

Source: Company data, Shinhan Investment Corp. estimates

SHIC Rating Classifications : BUY; Over +15%, HOLD; -15% to +15%, REDUCE; -15% or More

(As of 10 Feb. 2003)

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