

Result Preview



# Woongjin Coway (021240 KS)

**Sunkyung Lee**  
(82-2) 3772-1568  
sunny.lee@goodi.com

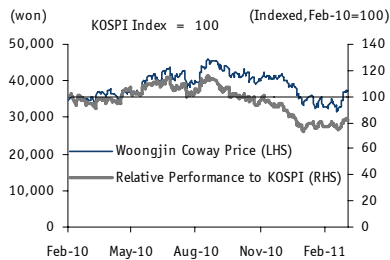
## 1Q11 earnings look fine

**BUY**

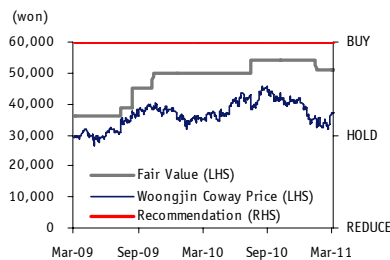
Price (Mar. 30) W37,200  
Fair Value W51,000 (37.1%)

Mkt Cap. W2,869.0bn/ US\$2,516.7mn  
Average Daily Trading Value: W13,660mn  
52 week High/Low W45,850/ W31,700

### Share Price Performance



### Fair Value & Recommendation History



- ◆ Decent sales growth vs. margin slowdown on accounting changes
- ◆ Air purifier and filtered water dispenser sales getting a boost from yellow sand and Japan radiation concerns
- ◆ Cosmetics business growth at home continues, while China operations are making steady progress
- ◆ BUY for a fair value of W51,000

### Decent sales growth vs. margin slowdown on accounting changes

Woongjin Coway is expected to report sales of W405.0bn (+9.1% YoY), operating income of W54.5bn (-8.2% YoY) and an operating profit margin of 13.5% for 1Q11. Sales growth was driven by net growth in air purifier and filtered water dispenser rental orders, a low cancellation rate kept at around 1.0% and the sales contribution from cosmetics. However, operating income is expected to retreat slightly YoY because the implementation of IFRS standards reduced the sales commission expensing period from five to two years and ad spending grew on cosmetics promotions. If these factors are excluded, margins continue to get better. The accounting changes that make 2011 profits look smaller will have margin boosting effects in 2012. The cosmetics division is expected to turn a profit in 4Q11. Defying growth slowdown concerns, Woongjin's Chinese operations are estimated to have grown more than 30% in 1Q11, and the company's 1Q11 equity method gains will rise from W2bn in 1Q10 to W2.5bn in 1Q11.

### Quarterly earnings trends

(W mn)	1Q10	2Q10	3Q10	4Q10	1Q11E	2Q11E	3Q11E	4Q11E
Sales	371,292	366,619	378,006	403,262	404,990	412,203	420,391	436,421
Operating profit	59,380	58,557	57,043	53,709	54,487	57,259	57,956	57,016
Net profit	42,072	46,693	45,196	42,968	41,831	44,139	47,020	43,263
% YoY	8.8	6.6	6.4	8.6	9.1	12.4	11.2	8.2
	13.4	20.3	21.9	6.4	(0.6)	(5.5)	4.0	0.7
	21.7	20.5	14.6	(6.0)	(8.2)	(2.2)	1.6	6.2
OPM (%)	16.0	16.0	15.1	13.3	13.5	13.9	13.8	13.1
NPM (%)	11.3	12.7	12.0	10.7	10.3	10.7	11.2	9.9

Source: Woongjin Coway, Shinhan Investment Corp.

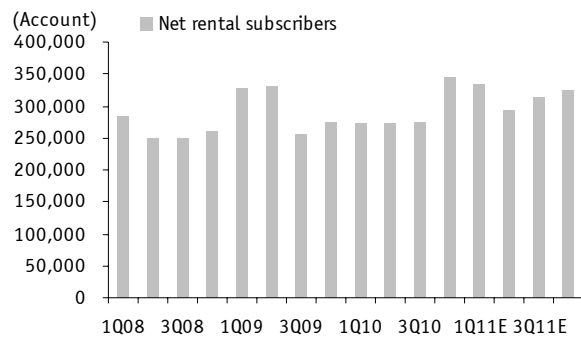
Year to Dec.	Sales (W bn)	OP (W bn)	Pre-tax (W bn)	NP (W bn)	EPS (Won)	Growth (%)	PER (x)	EV/EBITDA (x)	PBR (x)	ROE (%)	Net Debt Ratio (%)	Div. Yield (%)
2008	1,314.4	190.1	184.8	129.1	1,734	11.0	18.5	6.3	4.0	22.9	14.4	2.7
2009	1,411.9	204.3	202.7	153.3	2,023	16.7	19.3	7.9	4.4	24.0	29.5	2.6
2010	1,519.1	228.8	236.5	177.0	2,296	13.4	15.4	6.9	3.6	24.5	34.5	3.0
2011E	1,674.0	226.7	229.5	173.2	2,246	(2.2)	16.6	7.2	3.3	21.3	25.0	2.7
2012E	1,793.8	269.0	280.4	211.8	2,746	22.3	13.5	6.4	2.9	22.9	12.8	3.3

**Air purifier and filtered water dispenser sales getting a boost from yellow sand and Japan radiation concerns** The onset of the yellow sand dust storm season and fears over radiation spread from Japan are stoking consumer interest in air purifiers and filtered water dispensers. Woongjin is one of the two companies (the other being ChungHo Nais) that use the reverse osmosis water filtering method. In 2009, Woongjin's water filters were certified as effective in filtering out natural radioactive substances including radium and radon. Test results are pending for cesium and iodine filtering capabilities.

Concerns over drinking water and air safety are reflected in rising filtered water dispenser and air purifier sales. Air purifier rental subscriptions are estimated to have surged by about 60% in January and February. Filtered water dispenser rentals are estimated to have increased by about 25% during the same period, usually a low demand season. The demand for water dispensers is increasing as mass cattle culling during the foot-and-mouth disease outbreak raises area water contamination fears.

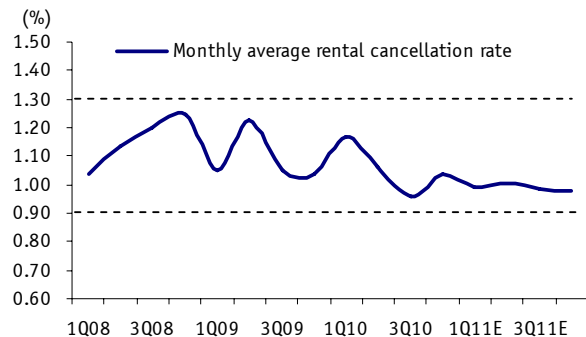
The sales boom in 1Q11 may be a temporary phenomenon, but sales momentum may continue over an extended period of time, depending on how Japan's nuclear reactor crisis develops. An upward earnings revision will be needed if that is the case.

**Quarterly net rental subscriber trend & outlook**



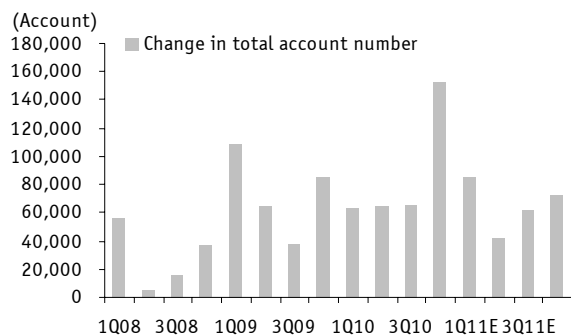
Source: Woongjin Coway, Shinhan Investment Corp.

**Monthly average cancellation rate trend & outlook**



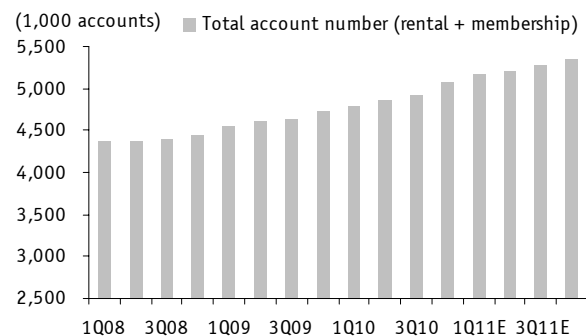
Source: Woongjin Coway, Shinhan Investment Corp.

**Quarterly total account number trend & outlook**



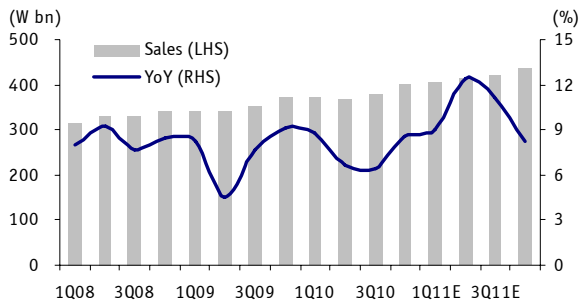
Source: Woongjin Coway, Shinhan Investment Corp.

**Total account number estimated to increase steadily**



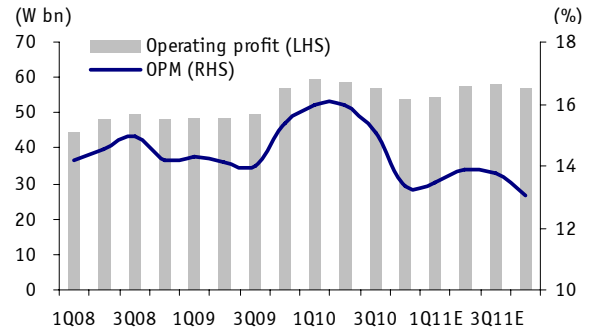
Source: Woongjin Coway, Shinhan Investment Corp.

Quarterly sales trend & outlook



Source: Woongjin Coway, Shinhan Investment Corp.

Quarterly operating profit trend & outlook



Source: Woongjin Coway, Shinhan Investment Corp.

**Cosmetics business growth at home continues, while China operations are making steady progress**

Domestic cosmetics sales in January and February are estimated at W9bn, a robust number, given the Lunar New Year holiday break in January. We forecast 1Q11 sales will reach the W15bn level. The company will easily attain annual sales of W60bn because its cosmetics line-up is strengthening with new additions of whitening skin care and men’s cosmetics. Herbal products will likely be rolled out in April. The company is looking to strengthen its brand recognition by going into upscale sales channels (duty free shops in April; three major department store chains in 1H11). The cosmetics division is expected to become profitable in 4Q11.

The China unit is estimated to have grown at more than 30% in 1Q11 despite shutdowns of small dealer shops. The company has been consolidating small dealer shops in an effort to make door-to-door sales more efficient. This could affect quarterly growth in the near term, but the China cosmetics business growth is expected to average 13% over the next years.

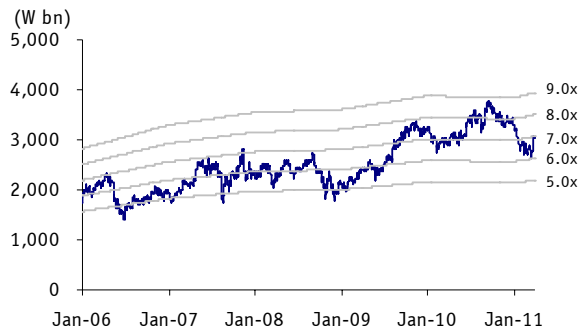
**Market share erosion by LG Electronics and smaller competitors looks unlikely**

LG Electronics is poised to move into the door-to-door sales market. Smaller rivals are also emerging, including Cuckoo and Tong Yang Magic. Woongjin's market share looks solid because it will be difficult for new entrants to muster and maintain a large sales force, which is key to success. Woongjin Coway has a 13,000-strong sales force vs. 3,000 at ChungHo Nais. It is also difficult for newcomers to retain sales people because of high compensation costs including sales commissions.

Small competitors focusing on home shopping channels with low- and mid-end products have been instrumental in broadening the market from middle-class consumers, Woongjin’s target market. However, their advance into the door-to-door sales market will be a tough call due to weak product competitiveness and brand power. Woongjin Coway plans to launch a new product line for budget-conscious consumers through home shopping channels, further raising the odds against small rivals.

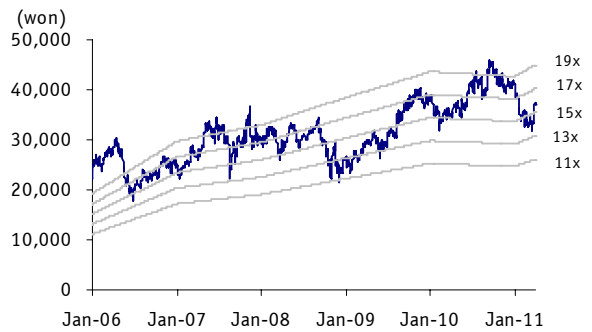
**BUY for a fair value of W51,000** We retain our BUY rating on Woongjin Coway for a fair value of W51,000. Despite strong performances by the main businesses, Woongjin Coway shares have been under pressure since 2H10 due to China business slowdown worries, cosmetics start-up costs, and subsidiary risks from Kukdong E&C. These negatives are getting out of the way. The Chinese subsidiary is regaining momentum, growing more than 30%. Cosmetics sales are rising and the cosmetics division will become able to cover costs in 2H11. A 2mn share buyback announcement is improving investor sentiment over the company's exposure to Kukdong E&C.

12-month-forward EV/EBITDA band chart



Source: Woongjin Coway, Shinhan Investment Corp.

12-month-forward PER band chart



Source: Woongjin Coway, Shinhan Investment Corp.

**Balance Sheet**

Year to Dec. (W bn)	2008	2009	2010	2011E	2012E
<b>Total Assets</b>	<b>1,071.4</b>	<b>1,270.7</b>	<b>1,439.5</b>	<b>1,553.4</b>	<b>1,584.9</b>
Current Assets	475.6	509.5	578.8	650.6	640.0
Cash & Cash Equivalents	76.1	63.7	56.3	116.3	88.5
St. Investment Assets	5.9	5.5	3.9	4.6	7.0
Accounts Receivable	149.8	194.6	207.3	224.7	240.8
Inventory	58.0	54.6	73.2	73.4	78.6
Others	185.8	191.1	238.1	231.5	225.1
Non-current Assets	595.8	761.2	860.7	902.7	944.9
Investment Assets	114.1	130.7	204.3	232.6	265.2
Tangible Assets	356.4	418.2	454.2	484.9	508.7
Intangible Assets	64.9	141.1	133.6	114.5	98.2
<b>Total Liabilities</b>	<b>474.8</b>	<b>590.0</b>	<b>674.7</b>	<b>695.3</b>	<b>593.0</b>
Current Liabilities	398.7	541.8	441.0	514.9	502.1
Accounts Payable	34.2	29.2	38.3	41.4	44.7
St. Debt	107.8	119.7	74.5	59.6	56.6
Current Portion of Lt. Debt	0.0	120.0	30.0	110.0	90.0
Others	256.7	272.8	298.2	303.9	310.9
Non-current Liabilities	76.0	48.2	233.8	180.4	90.9
Bonds	0.0	0.0	49.8	106.0	106.0
Lt. Debt	60.0	30.0	170.0	60.0	(30.0)
Others	16.0	18.2	14.0	14.4	14.8
<b>Total Stockholders Equity</b>	<b>596.6</b>	<b>680.7</b>	<b>764.8</b>	<b>858.1</b>	<b>991.9</b>
Paid-in Capital	39.3	40.7	40.7	40.7	40.7
Capital Surplus	108.7	141.9	140.0	140.0	140.0
Capital Adjustment	6.2	(31.5)	(43.0)	(43.0)	(43.0)
Other Accumulated Earnings	1.3	0.0	(2.7)	(2.7)	(2.7)
Retained Earnings	441.1	529.6	629.8	723.1	856.9
<b>Total Debt</b>	<b>167.8</b>	<b>269.7</b>	<b>324.2</b>	<b>335.6</b>	<b>222.6</b>
<b>Net Debt(Cash)</b>	<b>85.8</b>	<b>200.5</b>	<b>264.0</b>	<b>214.6</b>	<b>127.2</b>

**Cash Flow**

Year to Dec. (W bn)	2008	2009	2010	2011E	2012E
<b>Cash Flows from Operating</b>	<b>304.8</b>	<b>311.7</b>	<b>313.8</b>	<b>349.1</b>	<b>383.3</b>
Net Profit	129.1	153.3	177.0	173.2	211.8
Depreciation	126.5	128.2	131.6	131.0	133.9
Amortization	14.7	19.9	22.2	19.1	16.4
Equity Method Loss(Gain)	1.4	(13.9)	(22.1)	(24.8)	(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)	(70.6)	(20.2)	(23.0)
Others	66.9	71.6	75.4	70.7	73.3
<b>Cash Flows from Investing</b>	<b>(255.1)</b>	<b>(276.1)</b>	<b>(296.4)</b>	<b>(225.7)</b>	<b>(225.2)</b>
St. Investment Assets Dec.(Inc.)	(4.2)	(0.1)	(3.3)	(0.8)	(2.3)
Investment Securities Dec.(Inc.)	(82.4)	2.8	(64.7)	(3.0)	(3.0)
Tangible Assets Dec.(Inc.)	(142.0)	(204.1)	(211.9)	(212.0)	(209.8)
Others	(26.4)	(74.8)	(16.5)	(10.0)	(10.0)
<b>Free Cash Flow</b>	<b>49.7</b>	<b>35.5</b>	<b>17.4</b>	<b>123.4</b>	<b>158.1</b>
<b>Cash Flows from Financing</b>	<b>(2.1)</b>	<b>(52.3)</b>	<b>(20.4)</b>	<b>(63.4)</b>	<b>(186.0)</b>
St. Debt Inc.(Dec.)	15.8	(18.6)	(45.2)	(14.9)	(3.0)
Cur. Por. of Lt. Debt Inc.(Dec.)	(20.0)	0.0	(50.0)	80.0	(20.0)
Bonds Inc.(Dec.)	0.0	0.0	49.7	56.3	0.0
Lt. Debt Inc.(Dec.)	60.0	0.0	100.0	(110.0)	(90.0)
Share Capital Inc.(Dec.)	0.0	0.0	0.0	0.0	0.0
Dividend Paid	(58.1)	(64.8)	(76.8)	(79.9)	(77.9)
Others	0.1	31.0	1.9	5.2	4.9
<b>Change in Cash</b>	<b>47.6</b>	<b>(12.4)</b>	<b>(7.4)</b>	<b>60.0</b>	<b>(27.8)</b>
Beginning Cash	28.5	76.1	63.7	56.3	116.3
Ending Cash	76.1	63.7	56.3	116.3	88.5
Capex/ Sales (%)	10.8	14.5	13.9	12.7	11.7
Depreciation/ Sales (%)	9.6	9.1	8.7	7.8	7.5
Depreciation/ Capex (%)	89.1	62.8	62.1	61.8	63.8

Source: Company data, Shinhan Investment Corp. estimates

**Profit and Loss**

Year to Dec. (W bn)	2008	2009	2010	2011E	2012E
<b>Net Sales</b>	<b>1,314.4</b>	<b>1,411.9</b>	<b>1,519.1</b>	<b>1,674.0</b>	<b>1,793.8</b>
Growth (%)	8.4	7.4	7.6	10.2	7.2
Export ratio (%)	0.0	0.0	0.0	4.6	5.0
Cost of Sales	407.2	460.2	494.1	519.5	562.5
Growth (%)	5.8	13.0	7.4	5.2	8.3
Gross Profit	907.2	951.8	1,025.1	1,154.5	1,231.2
Gross Margin(%)	69.0	67.4	67.5	69.0	68.6
SG&A Expenses	717.1	747.5	796.3	927.7	962.2
Growth (%)	7.5	4.2	6.5	16.5	3.7
<b>Operating Profit</b>	<b>190.1</b>	<b>204.3</b>	<b>228.8</b>	<b>226.7</b>	<b>269.0</b>
Growth (%)	17.9	7.4	12.0	(0.9)	18.7
Operating Margin(%)	14.5	14.5	15.1	13.5	15.0
Non-Operating Inc (Exp)	(5.4)	(1.5)	7.7	2.7	11.4
Interest Income	3.3	3.1	3.5	3.7	4.3
Interest Expenses	11.3	12.5	17.6	19.3	19.5
Net F/X	10.5	(5.2)	(0.4)	(0.4)	0.0
Net Asset Disposal	(2.5)	(1.5)	(0.3)	0.0	0.0
Net Equity Method	(1.4)	13.9	22.1	24.8	29.0
Net Other non-operating	(3.9)	0.7	0.4	(6.0)	(2.4)
<b>Pre-tax Profit from Cont. Op</b>	<b>184.8</b>	<b>202.7</b>	<b>236.5</b>	<b>229.5</b>	<b>280.4</b>
Income Taxes	55.7	49.4	59.5	56.3	68.8
Profit from Cont. Op	129.1	153.3	177.0	173.2	211.8
Profit from Discont. Op	0.0	0.0	0.0	0.0	0.0
<b>Net Profit</b>	<b>129.1</b>	<b>153.3</b>	<b>177.0</b>	<b>173.2</b>	<b>211.8</b>
Growth (%)	11.0	18.8	15.5	(2.2)	22.3
Net Margin(%)	9.8	10.9	11.7	10.3	11.8
EBITDA	394.3	400.7	430.9	427.1	471.4
Growth (%)	7.8	1.6	7.5	(0.9)	10.4
<b>Dividend Payout (%)</b>	<b>50.2</b>	<b>50.1</b>	<b>45.2</b>	<b>45.0</b>	<b>45.0</b>

**Key Ratios**

Year to Dec.	2008	2009	2010	2011E	2012E
EPS (won)	1,734	2,023	2,296	2,246	2,746
Adj. EPS (won)	1,768	2,043	2,299	2,246	2,746
BPS (won)	8,016	8,826	9,916	11,126	12,861
DPS (won)	870	1,010	1,050	1,011	1,236
PER (x)	18.5	19.3	15.4	16.6	13.5
Adj. PER (x)	18.2	19.1	15.3	16.6	13.5
PBR (x)	4.0	4.4	3.6	3.3	2.9
PCR (x)	7.0	8.2	7.1	7.8	7.1
EV/ EBITDA (x)	6.3	7.9	6.9	7.2	6.4
PEG (x)	2.1	1.8	1.5	1.2	0.9
Dividend Yield (%)	2.7	2.6	3.0	2.7	3.3
<b>Profitability</b>					
Operating Margin (%)	14.5	14.5	15.1	13.5	15.0
EBITDA Margin (%)	30.0	28.4	28.4	25.5	26.3
Pre-tax Profit Margin(%)	14.1	14.4	15.6	13.7	15.6
Net Margin (%)	9.8	10.9	11.7	10.3	11.8
ROA (%)	12.9	13.1	13.1	11.6	13.5
ROE (%)	22.9	24.0	24.5	21.3	22.9
ROIC (%)	22.2	22.9	21.3	20.1	23.5
<b>Stability</b>					
Debt Ratio (%)	79.6	86.7	88.2	81.0	59.8
Net Debt Ratio (%)	14.4	29.5	34.5	25.0	12.8
Interest Coverage (x)	16.8	16.3	13.0	11.7	13.8
<b>Activity</b>					
Asset Turnover (x)	1.3	1.2	1.1	1.1	1.1
Receivables Turnover (x)	9.2	7.9	7.3	7.4	7.4
Inventory Turnover (x)	22.7	25.1	23.8	22.8	23.6
Payables Turnover (x)	43.9	44.5	45.0	42.0	41.7
Working Capital Turnover (x)	14.0	11.7	9.5	9.1	9.6

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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