

Woongjin Coway (021240 KS)

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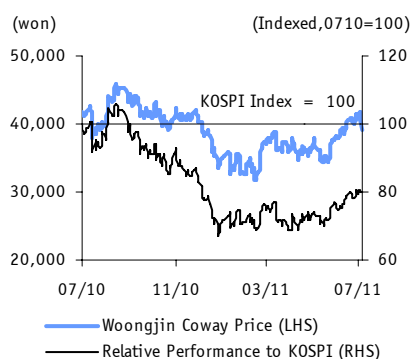
Good 2Q and better prospects for 2H

BUY

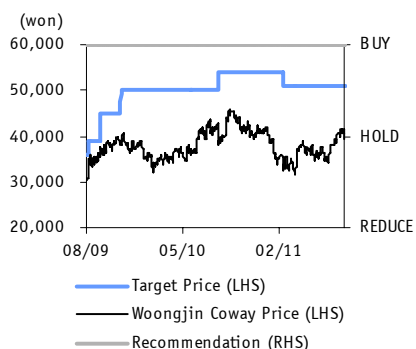
Price (Aug. 3) W39,200
Target Price (% variance) W58,000 (48.0%)

Mkt Cap. W3,023.3bn/ US\$2,879.3mn
Average Daily Trading Value: W5,965mn
52 week High/Low W45,850/ W31,700

Share Price Performance



Target Price & Recommendation History



- ◆ 2Q11 earnings beat expectations; profit margins improve after stripping away the effect of accounting changes
- ◆ Double-digit growth in 3Q11 and 4Q11, with profits improving in large strides
- ◆ Retain BUY, revising up target price to W58,000

2Q11 earnings beat expectations; profit margins improve after stripping away the effect of accounting changes

Woongjin Coway posted 2Q11 sales of W435.9bn (+19.3% YoY) and operating profit of W61.8bn (-13.3% YoY), beating our estimates and the market's expectations. Sales commissions increased YoY in 2Q11, as their recognition period has been reduced under the IFRS. Thus, the drop in operating profit was simply caused by a high base effect due to a change in accounting standards.

Excluding the cosmetics business, the operating profit margin would have been 16% in 2Q11, the same as a year ago (2Q10 sales of W58.6bn and operating profit margin of 16%). The operating profit margin of existing operations would have exceeded the upper 16% range if the sales commission adjustment is taken out of consideration.

Equity method gains/losses are included in our estimates and the market consensus, but they are excluded in the figures released by the company. We estimate Woongjin's 2Q11 equity method gains at approximately W4.8bn.

Woongjin Coway's 2Q11 earnings

(W bn, %)	2Q11P	2Q10	% YoY	1Q11	% QoQ	2Q11F K-GAAP	Var. (%)	Cons.	Var. (%)
Sales	435.9	365.3	19.3	399.8	9.0	404.5	7.8	409.6	6.4
OP	61.8	71.3	(13.3)	56.5	9.4	57.5	7.5	58.3	6.0
Pre-tax profit	55.1	76.0	(27.5)	50.4	9.2	60.0	(8.3)	59.5	(7.5)
NP	42.1	59.2	(28.9)	38.8	8.5	45.5	(7.6)	47.7	(11.8)
OPM	14.2	19.5		14.1		14.2		14.2	
Pre-tax profit	12.6	20.8		12.6		14.8		14.5	
NPM	9.7	16.2		9.7		11.2		11.6	

Source: Company data, 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 (%)
2009	1,411.9	204.3	202.7	153.3	2,023	16.7	15.9	7.5	3.6	24.0	29.5	3.1
2010	1,519.1	228.8	236.5	177.0	2,296	13.4	17.0	8.6	3.9	24.5	34.6	2.7
2011F	1,720.6	256.9	241.9	187.6	2,432	5.9	16.1	7.3	3.7	23.7	27.8	2.9
2012F	1,871.9	295.6	283.8	217.1	2,815	15.8	13.9	6.6	3.2	24.7	11.3	3.3
2013F	2,014.0	326.5	320.6	245.2	3,180	12.9	12.3	5.9	2.8	24.1	(2.2)	3.8

-Note: K-GAAP to 2010, K-IFRS-based from 2011

When broken down into divisions, the 10% growth of the highly profitable rental division powered the company's 19% growth, with lump-sum sales increasing 57% YoY in spite of a high comparison base. The domestic cosmetics business' earnings were similar to 1Q11 levels. The cosmetics division's deficit is expected to narrow in 2H11.

Woongjin Coway's 2Q11 earnings by division

(W bn)		2Q11P	2Q10	% YoY	1Q11	% QoQ
Sales	Total	435.9	365.3	19.3	399.7	9.1
	Rental	299.7	272.4	10.0	288.0	4.1
	Membership	39.9	36.6	9.0	39.1	2.0
	Lump-sum sales	38.8	24.7	57.1	31.8	22.0
	Cosmetics	17.9	0.0		17.4	2.9
	Exports	22.9	17.2	33.1	18.3	25.1
	Others	16.7	14.4	16.0	5.1	227.5
	COGS	Total	141.4	119.4	18.4	125.4
Rental		82.2	73.0	12.6	82.5	(0.4)
Membership		12.6	11.5	9.6	12.5	0.8
Lump-sum sales		13.4	9.1	47.3	10.2	31.4
Cosmetics		3.4			2.9	17.2
Exports		17.8	13.3	33.8	14.7	21.1
Others		11.9	12.5	(4.8)	2.6	357.7
COGS (%)		Total	32.4	32.7		31.4
	Rental	27.4	26.8		28.6	
	Membership	31.6	31.4		32.0	
	Lump-sum sales	34.5	36.8		32.1	
	Cosmetics	19.0			16.7	
	Exports	77.7	77.3		80.3	
	Others	71.3	86.8		51.0	
	Gross profit	294.5	245.9	19.7	274.3	7.4
Gross profit margin (%)	67.6	67.3		68.6		
SG&A	221.9	160.5	38.3	204.8	8.3	
Other operating revenue	0.1	0.3	(76.7)	3.8	(98.2)	
Other operating expenses	10.9	14.5	(24.8)	16.3	(33.1)	
SG&A /sales (%)	50.9	43.9		51.2		
OP	61.8	71.2	(13.3)	57.0	8.4	
OPM (%)	14.2	19.5		14.3		
Net rental orders	341,881	273,839	24.8	329,633	3.7	
Net lump-sum orders	58,755	40,518	45.0	56,120	4.7	
Rental accounts	4,321,185	3,966,472	8.9	4,233,969	2.1	
Lump-sum accounts	1,011,455	897,454	12.7	966,986	4.6	
Total accounts	5,332,640	4,863,926	9.6	5,200,955	2.5	
Cancelation rate (%)	0.99	1.06		1.02		

Source: Company data, Shinhan Investment Corp.

The Chinese subsidiary's cosmetics sales increased 6.6% YoY and its operating profit margin was 25%. The seeming slowdown is attributable to the high base of the previous year. The subsidiary's full-year 2011 growth is expected to be 18%.

Chinese subsidiary's cosmetics division earnings					
('000 RMB)	2Q10	3Q10	4Q10	1Q11	2Q11P
Sales	61,656	54,665	50,347	55,857	65,696
% YoY	35	5	25	31	7
% QoQ	45	(11)	(8)	11	18
OP	23,454	17,572	11,729	14,738	16,350
% YoY	(19)	(14)	(20)	(4)	(30)
% QoQ	53	(25)	(33)	26	11
OPM (%)	38.0	32.1	23.3	26.4	24.9

Source: Company data, Shinhan Investment Corp.

The earnings of overseas subsidiaries are hard to confirm due to the announcement of separate IFRS-based results. Equity method gains from subsidiaries are estimated to be W4.8bn, with Woongjin Chemical turning in W3.9bn.

Double-digit growth in 3Q11 and 4Q11, with profits improving in large strides

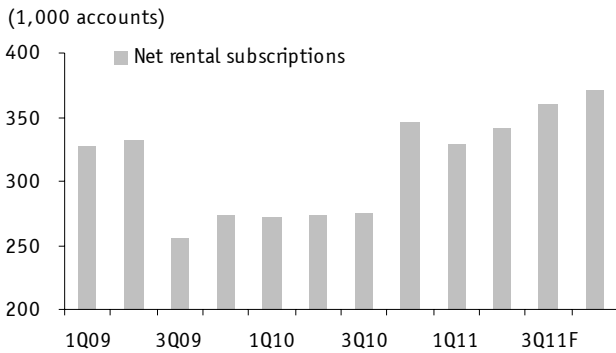
Rental orders grew sharply in 1Q11 and 2Q11 on YoY basis. At end-2Q11, rental payment accounts were up by 176,000 accounts from a year ago. Rental accounts including membership accounts grew by 250,000 accounts from a year ago.

The cancelation rate is falling due to the two-year obligatory contract period. Sales momentum should continue with an upgraded line-up of new products. The company should be able to deliver double-digit sales growth in 2H11, drawing support from robust rental sales.

Double-digit earnings growth is also expected in 2H11. In 2010, the company posted an operating profit margin of 15.1% in 3Q and 13.3% in 4Q, hit by losses from the new cosmetics line launch. In 2H11, however, profits should grow at a higher rate than sales as losses dwindle with increasing cosmetics sales.

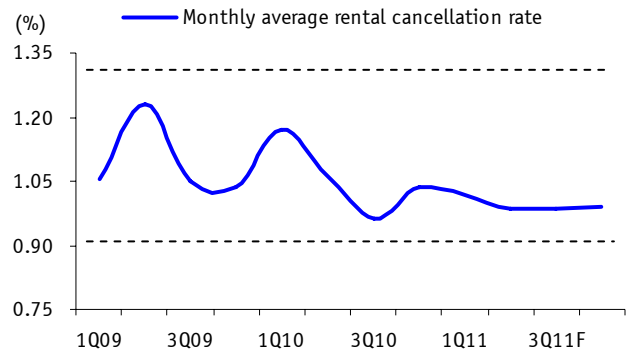
It should be noted that reported growth rates for 3Q11 and 4Q11 may differ if last year's results are adjusted based on K-IFRS. However, excluding the effect of such accounting changes, 2H11 earnings growth should exceed the 1H11 figures. Also, under the new accounting method, sales commissions are not recognized for accounts that last two years or longer, which gives a boost to profit margins. Accordingly, the commission burden should ease from 2012.

Quarterly net rental subscriptions



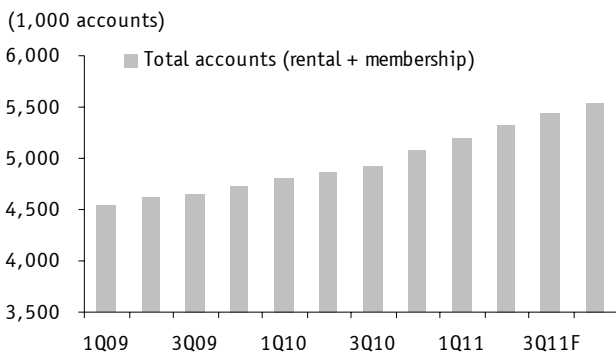
Source: Company data, Shinhan Investment Corp.

Rental cancellation rate



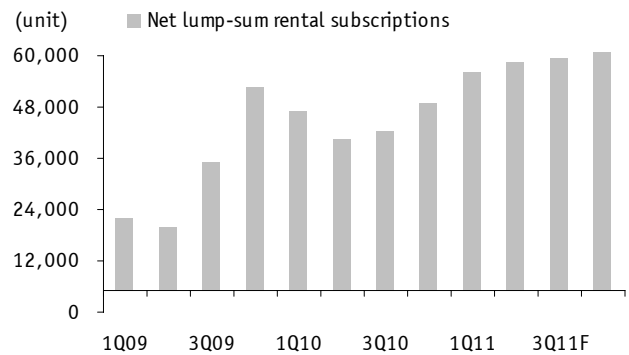
Source: Company data, Shinhan Investment Corp.

Rental accounts



Source: Company data, Shinhan Investment Corp.

Net lump-sum rental subscriptions



Source: Company data, Shinhan Investment Corp.

We revised our earnings forecasts for Woongjin Coway due to a change in accounting standards from K-GAAP to K-IFRS and reflection of better-than-expected earnings from existing businesses. Our 2011 and 2012 operating profit estimates are revised up by 10.8% and 9.8%. However, net profit estimates are revised up by a smaller extent because equity method gains are excluded under separate K-IFRS.

Woongjin Coway's earnings forecast revision

(W bn, %)	Before			After			Change (%)		
	2011F	2012F	2013F	2011F	2012F	2013F	2011F	2012F	2013F
Sales	1,649	1,778	1,872	1,721	1,872	2,014	4.3	5.3	7.6
Gross profit	1,133	1,224	1,285	1,176	1,283	1,389	3.9	4.8	8.1
OP	232	269	286	257	296	326	10.8	9.8	14.2
NP	180	213	233	188	217	245	4.3	1.9	5.0
% YoY Sales	8.6	7.8	5.3	13.3	8.8	7.6			
Gross profit	10.5	8.0	5.0	14.8	9.1	8.2			
OP	1.4	16.0	6.2	12.3	15.1	10.4			
NP	1.6	18.4	9.6	5.9	15.8	12.9			
Gross margin	68.7	68.8	68.6	68.4	68.5	69.0			
OP margin	14.1	15.1	15.3	14.9	15.8	16.2			
NP margin	10.9	12.0	12.5	10.9	11.6	12.2			

Source: Shinhan Investment Corp.

Woongjin Coway's earnings trend and forecast

(W bn, %)	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11	3Q11F	4Q11F	10	11F	12F	13F
Sales	371.3	366.6	378.0	403.2	399.8	435.9	437.7	447.2	1,519.1	1,720.6	1,871.9	2,014.0
Gross profit	247.2	245.8	253.3	278.7	274.3	294.5	301.2	306.4	1,025.1	1,176.5	1,283.1	1,388.9
OP	59.6	58.6	57.1	53.7	57.1	61.8	67.8	68.9	228.8	256.9	295.6	326.5
NP	59.0	63.0	59.5	55.0	50.4	55.1	61.4	63.4	177.0	187.6	217.1	245.2
% YoY	8.8	6.6	6.4	8.6	7.7	18.9	15.8	10.9	7.6	13.3	8.8	7.6
	7.9	6.2	4.7	11.9	11.0	19.8	18.9	9.9	7.7	14.8	9.1	8.2
	22.1	20.7	14.7	(5.9)	(4.2)	5.3	18.8	28.3	12.0	12.3	15.1	10.4
	21.4	23.1	19.5	3.5	(14.5)	(12.6)	3.1	15.3	15.5	5.9	15.8	12.9
Gross margin	66.6	67.1	67.0	69.1	68.6	67.6	68.8	68.5	67.5	68.4	68.5	69.0
OP margin	16.0	16.0	15.1	13.3	14.3	14.2	15.5	15.4	15.1	14.9	15.8	16.2
NP margin	15.9	17.2	15.7	13.6	12.6	12.6	14.0	14.2	11.7	10.9	11.6	12.2

Source: Company data, Shinhan Investment Corp.

Note: 2010 based on K-GAAP; 2Q10 figures differ from those shown in the previous K-IFRS-based result table

Retain BUY, revising up target price to W58,000

We retain our BUY rating on Woongjin Coway and revise up our target price by 14% from W51,000 to W58,000 following upward earnings revision.

The target price of W58,000 is the sum of operating value, based on terminal growth of 1.5% and free cash flow discounted by WACC of 8.5%, and investment asset value of Woongjin Chemical and the Chinese subsidiary.

Woongjin Coway has the strongest earnings stability and cash flow generating ability among domestic and foreign consumer groups. Given the nature of rental revenue, valuation based on a specific period would be akin to applying a discount. Thus, the DCF valuation seems to be the most appropriate method.

Woongjin Coway deserves attention for its bright top-line outlook for 2H11 amid rising economic uncertainties both home and abroad. The company will keep its dividend payout ratio at 45~50% this year and dividend per share is estimated at W1,150.

Woongjin Coway's target price calculation

(W bn)		2011F	2012F	2013F	2014F	2015F	2016F
Total enterprise value	E=d+e	4,288					
OP	a	257	296	326	348	375	384
Tangible/intangible asset depreciation cost + rental disposal loss	b	231	229	230	228	230	233
EBITDA	a+b	488	525	556	576	605	617
Tax rate (%)		22	24	24	24	24	24
EBITDA*(1-t)	A	378	402	425	441	463	472
(Tangible/intangible asset depreciation cost)*t	B	52	54	54	54	54	55
Net working capital increase (decrease)	C	12	6	9	10	10	12
CAPEX	D	176	176	178	167	174	173
FCFF	A+B-C-D	242	273	293	317	333	343
Discount factor		0.97	0.82	0.76	0.70	0.64	0.59
PV of FCFF		235	224	222	221	215	204
Total PV of FCFF (through 2016)	d	1,320					
Terminal value of end of 2016		4,995	Terminal growth 1.5%				
NPV of terminal value	e	2,967	WACC 8.5%				
Investment asset value	F=h+i	298					
Woongjin Chemical	h	183	Applied 30% discount to market price				
Chinese subsidiary	i	116	Applied PER of 15x to 2011F net profit				
Total value of equity	G=E+F-j+k+l	4,359					
Net debt	j	348					
Cash and cash equivalents	k	117					
Securities available for sale + securities with maturity	l	4					
Total outstanding shares (1,000 shares)	m	77,125					
Treasury shares (1,000 shares)	n	1,455					
Per-share value (won)	H=G/(m-n)	57,600					
Target price (won)		58,000					
Current share price (won)		39,200	2011-08-04				
Upside potential (%)		48.0					

Source: Company data, Shinhan Investment Corp.

Statement of Financial Position

Year to Dec. (W bn)	2009	2010	2011F	2012F	2013F
Assets	1,270.7	1,439.5	1,552.7	1,631.4	1,813.4
Current Assets	509.5	578.8	690.1	764.5	939.3
Cash and Cash Equivalents	63.7	56.3	117.5	150.8	285.6
Trade Receivables	194.6	207.3	234.7	255.4	274.8
Inventories	54.6	73.2	82.9	90.2	97.0
Others	196.6	242.0	255.0	268.2	281.9
Non-Current Assets	761.2	860.7	862.6	866.8	874.0
Property, Plant and Equipment	418.2	454.2	470.4	482.5	492.5
Intangible Assets	141.1	133.6	113.9	104.8	100.7
Investments in Associates, Subsidiaries, etc.	128.6	197.1	197.1	197.1	197.1
Others	73.4	75.9	81.2	82.4	83.8
Liabilities	590.0	674.7	737.0	686.1	721.8
Current Liabilities	541.8	441.0	542.5	540.9	575.9
Trade Payables	29.2	38.3	42.2	45.7	48.5
Short-term debts	239.7	104.5	168.2	132.1	136.2
Others	272.8	298.2	332.1	363.2	391.2
Non-Current Liabilities	48.2	233.8	194.5	145.2	145.9
Long-term debts	30.0	220.0	180.0	130.0	130.0
Provisions for Emp Benefits	11.3	6.7	7.1	7.4	7.8
Others	6.9	7.0	7.4	7.8	8.1
Stockholders' Equity	680.7	764.8	815.7	945.3	1,091.5
Capital Stock	40.7	40.7	40.7	40.7	40.7
Retained Earnings	529.6	579.8	687.4	817.0	963.2
Others	110.4	144.3	87.6	87.6	87.6
Owners of Parent Equity	680.7	764.8	815.7	945.3	1,091.5
Non-Controlling Interests Equity	0.0	0.0	0.0	0.0	0.0
Total Debt	269.7	324.5	348.2	262.1	266.2
Net Debt(Cash)	200.5	264.3	226.7	107.0	(23.9)

Statement of Cash Flow

Year to Dec. (W bn)	2009	2010	2011F	2012F	2013F
Cash Flows from Operating	311.7	313.8	384.3	388.9	436.8
Net Profit	153.3	177.0	187.6	217.1	245.2
Depreciation	128.2	131.6	159.5	164.1	167.8
Amortization	19.9	22.2	26.5	16.7	12.2
FC Translation Loss(Gain)	3.8	(0.2)	0.3	0.0	0.0
Disp PP&E Loss(Gain)	0.4	0.3	0.1	0.0	0.0
(Recovery)Imp Losses on Assets	(0.5)	(0.3)	0.0	0.0	0.0
Losses(Gains) in Equity Method	(13.9)	(22.1)	0.0	0.0	0.0
Change in Working Capital	(48.9)	(70.6)	(23.0)	(30.8)	(22.8)
Payments of Income Taxes	0.0	0.0	(54.4)	(66.7)	(75.3)
Others	69.4	75.9	87.7	88.5	109.6
Cash Flows from Investing	(276.1)	(296.4)	(197.4)	(198.7)	(177.3)
Dec(Inc) in Financial Assets	0.0	(0.4)	0.0	0.0	0.0
Dec(Inc) in Associates, ETC.	(1.0)	(63.7)	0.0	0.0	0.0
Dec(Inc) in Property and Equipment	(204.1)	(211.9)	(175.8)	(176.1)	(177.8)
Dec(Inc) in Intangible Assets	(6.2)	(9.8)	(6.8)	(7.6)	(8.1)
Others	(64.8)	(10.6)	(14.7)	(15.0)	8.6
FCF	35.5	17.4	186.9	190.2	259.5
Cash Flows from Financing	(52.3)	(20.4)	(125.8)	(12.9)	(124.7)
inc(Dec) in Total Debt	(18.6)	104.5	(23.7)	86.1	(4.1)
Dividends Paid	(64.8)	(76.8)	(87.6)	(99.0)	(114.2)
Sale(Purchase) of Treasury Stock	(38.9)	0.0	0.0	0.0	0.0
Others	70.0	(48.1)	(14.6)	0.0	(6.3)
Change of Consolidated Scope	0.0	0.0	0.0	0.0	0.0
Difference by FX rates	0.0	0.0	0.0	0.0	0.0
Change in Cash	(12.4)	(7.4)	61.1	33.4	134.8
Beginning Cash	76.1	63.7	56.3	117.5	150.8
Ending Cash	63.7	56.3	117.5	150.8	285.6

Source: Company data, Shinhan Investment Corp.

Note: K-GAAP to 2010, K-IFRS-based from 2011

Statement of Comprehensive Income

Year to Dec. (W bn)	2009	2010	2011F	2012F	2013F
Net Sales	1,411.9	1,519.1	1,720.6	1,871.9	2,014.0
Growth (%)	7.4	7.6	5.0	5.0	5.0
Cost of Sales	460.2	494.1	544.1	588.8	625.1
Gross Profit on Sales	951.8	1,025.1	1,176.5	1,283.1	1,388.9
Gross Margin (%)	67.4	67.5	68.4	68.5	69.0
Operating Expenses	747.5	796.3	919.6	987.5	1,062.5
Research & Development	7.4	6.3	5.6	7.9	10.1
Dist Costs and Adm Expenses	747.5	796.3	873.7	940.3	1,014.3
Other Income	0.0	0.0	3.9	1.4	1.5
Other Expenses	0.0	0.0	49.7	48.6	49.7
Operating Income	204.3	228.8	256.9	295.6	326.5
Growth (%)	7.4	12.0	12.3	15.1	10.4
Operating Margin (%)	14.5	15.1	14.9	15.8	16.2
Interest Income	3.1	3.5	5.1	5.8	9.2
Interest Expenses	12.5	17.6	19.6	17.9	15.5
Gains(Losses) in Equity Method	13.9	22.1	0.0	0.0	0.0
Others	(6.0)	(0.3)	(0.4)	0.4	0.5
Income Before Income Taxes Expenses	202.7	236.5	241.9	283.8	320.6
Income Taxes Expenses	49.4	59.5	54.4	66.7	75.3
Tax Rate (%)	24.4	25.1	22.5	23.5	23.5
Net Profit((Non-controlling Int Equity)	0.0	0.0	0.0	0.0	0.0
Net Profit(Owners of Parent Equity)	153.3	177.0	187.6	217.1	245.2
Growth (%)	18.8	15.5	5.9	15.8	12.9
EBITDA	352.4	382.6	443.0	476.3	506.5
Growth (%)	6.3	8.6	15.8	7.5	6.3
Adj. Operating Income	204.3	228.8	302.7	342.8	374.7
Adj. Pre-tax Net Income	203.8	236.5	242.0	283.8	320.6
Adj. Net Income(Owners of Parent Equity)	154.1	177.0	187.6	217.1	245.2

Key Ratios

Year to Dec.	2009	2010	2011F	2012F	2013F
EPS (won)	2,023	2,296	2,432	2,815	3,180
Adj. EPS (won)	2,034	2,296	2,432	2,815	3,180
BPS (won)	8,826	9,916	10,576	12,257	14,153
CFPS (won)	4,760	4,984	5,986	6,307	6,935
DPS (won)	1,010	1,050	1,150	1,300	1,500
PER (x)	15.9	17.0	16.1	13.9	12.3
Adj. PER (x)	15.8	17.0	16.1	13.9	12.3
PBR (x)	3.6	3.9	3.7	3.2	2.8
PCR (x)	10.6	12.9	13.0	13.0	13.0
EV/ EBITDA (x)	7.5	8.6	7.3	6.6	5.9
EV/ EBIT (x)	12.9	14.3	12.7	10.6	9.2
Dividend Yield (%)	3.1	2.7	2.9	3.3	3.8
Profitability					
EBITDA Margin (%)	25.0	25.2	25.7	25.4	25.1
Operating Margin (%)	14.5	15.1	14.9	15.8	16.2
Net Margin (%)	10.9	11.7	10.9	11.6	12.2
ROA (%)	13.1	13.1	12.5	13.6	14.2
ROE (%)	24.0	24.5	23.7	24.7	24.1
ROIC (%)	23.0	21.5	23.7	26.5	28.8
Stability					
Debt Ratio (%)	86.7	88.2	90.3	72.6	66.1
Net Debt Ratio (%)	29.5	34.6	27.8	11.3	(2.2)
Cash Ratio (%)	11.8	12.8	21.7	27.9	49.6
Interest Coverage (x)	16.3	13.0	13.1	16.5	21.0
Activity					
Working Capital Turnover (x)	11.7	9.5	9.1	9.5	9.8
Inventory Turnover (days)	14.6	15.4	16.6	16.9	17.0
Receivables Turnover (days)	44.5	48.3	46.9	47.8	48.0

Source: Company data, Shinhan Investment Corp.

Note: K-GAAP to 2010, K-IFRS-based from 2011

SHIC Rating Classifications: BUY; Over +15%, Trading BUY; 0 to 15%, HOLD; -15% to 0, REDUCE; -15% or More (As of 25 Jul. 2011)

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