

# Coway (021240)

Above
In line
Below

12M rating **BUY (Maintain)**  
 12M TP **W73,000** from W63,000  
 Up/downside **+24%**

## Stock Data

KOSPI (Aug 8, pt)	1,884
Stock price (Aug 8, KRW)	58,800
Market cap (USD mn)	4,075
Shares outstanding (mn)	77
52-Week high/low (KRW)	60,500/30,150
6M avg. daily turnover (USD mn)	8.6
Free float / Foreign ownership (%)	65.8/52.0
Major shareholders (%)	
Coway Holdings, Inc. and 16 others	31.1
Lazard Asset Management LLC and 32 others	11.7

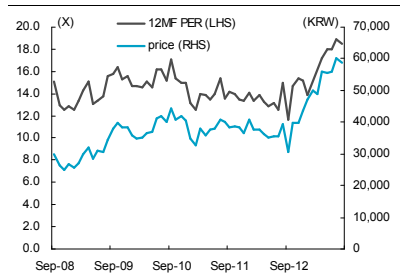
## Valuation

	2012A	2013F	2014F
PER (x)	34.3	16.9	16.6
PBR (x)	3.8	4.3	3.7
ROE (%)	12.3	29.6	25.2
EV/EBITDA (x)	9.4	10.0	8.7
EPS (KRW)	1,268	3,478	3,544
BPS (KRW)	11,354	13,739	15,902

## Performance

	1M	6M	12M
Absolute (%)	(0.7)	26.3	69.2
Relative to KOSPI (%p)	(4.4)	29.7	70.2

## 12MF PER trend



Source: WISEfn consensus

## Profitability and growth potential confirmed

### What's new: Sales and margins beat consensus

2Q13 sales grew 11% YoY to W496.9bn and OP surged 22% YoY to W79.4bn. Consolidated sales also increased 14% YoY and OP 28% YoY. Parent OP beat the consensus by 9% as OPM climbed 1.4%p to 16%. EBT jumped 43% YoY as the non-operating balance improved as financing costs fell to W4.3bn from W9.3bn. SG&A-to-sales ratio improved 3.2%p YoY as cancellation rates for rentals and losses on rental assets declined following inventory asset disposals in 2012. In addition, cosmetics losses narrowed to W600mn from W3.7bn in 2Q12 as marketing costs declined.

### Pros: Environmental appliance margins surge, rapid cosmetics and overseas growth

Environmental appliance margins surged on solid subscriber growth and a shift from low-margin memberships to rentals. In addition, the ASP hike in April also gained traction. Meanwhile, the company's overall growth potential was confirmed as lump-sum payments improved 18%, cosmetics sales 35% and exports 111%. Sales of humidifiers (outsourced product) posted the highest growth, and this trend should continue. Health-related product sales also contributed significantly to overall growth. Overseas divisions were also favorable. Total ODM sales surged 129% on higher sales to Philips and Sharp. In fact, earnings at almost all of the overseas subsidiaries (not reflected in separate earnings) improved. In particular, environmental sales surged more than 30% at the Malaysian and US subsidiaries.

### Cons: Subscriber growth slows amid focus on margins

Rental subscribers increased 3.9% YoY to 5.82mn at end-2Q13. However, net subscriber addition fell to only 23,000 QoQ due to the ASP hike and the shift from memberships to rentals. Coway forecasts full-year net subscriber addition at 270,000, with 76,000 additions in 1H13. We believe Coway will expand the low- and mid-priced channels and roll out new products to add subscribers. In addition, the company's brand image is improving, and Coway is marketing a campaign to raise water demand over the mid term.

### Conclusion: Profitability and growth potential confirmed, raise TP to W73,000

We revised up our TP from W63,000 to W73,000, as: 1) EPS growth should reach 6% in 2013 and 7% in 2014 on improved margins and non-operating conditions

(W bn, %, %p)

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	2Q13P				Change		2013F	
	KIS est.	Actual	Diff.	Consensus	QoQ	YoY	KIS	Consensus
Sales	480	497	4	482	6.8	11.3	1,985	1,933
OP	76	79	5	73	14.6	21.9	304	293
OP margin	15.8	16.0	0	15	1.1	1.4	14.9	15.1
EBT	65	81	23	66	(29.8)	43.1	339	320
NP	50	61	22	50	(24.5)	37.6	257	236

and 2) we lifted our 12MF target PE to 21x, a premium to the historic peak of 19x. Despite unfavorable conditions, Coway has a dominant domestic market share and stable earnings model. Valuations should continue to re-rate upwards on efforts to bolster margins and the confirmed growth potential.

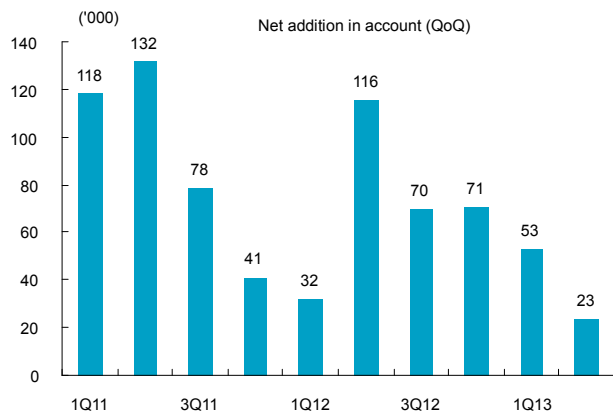
**Table 1. Earnings breakdown**

(W bn, KRW, '000, %YoY, %)

	1Q11	2Q11	3Q11	4Q11	1Q12	2Q12	3Q12	4Q12	1Q13	2Q13
Increase in total account (QoQ)	118.2	131.7	78.4	41.0	31.6	116.1	70.0	70.8	52.6	23.3
Rental ARPU (%YoY)	1.0	2.4	3.4	3.6	4.3	3.2	2.1	1.6	0.8	0.6
Membership ARPU (%YoY)	-1.9	-3.0	-3.8	-3.0	-5.4	-6.4	-6.8	-6.6	-2.9	1.3
No. of rental account ('000, end of Q)	4,234	4,321	4,377	4,450	4,480	4,518	4,551	4,607	4,658	4,717
Increase in rental account (QoQ)	88.9	87.2	55.4	73.4	30.0	37.6	33.7	56.2	50.4	59.0
Rental ARPU (Won)	22,218	22,586	22,845	22,993	23,164	23,319	23,325	23,357	23,347	23,468
No. of new rental sales ('000 units)	329.6	341.9	287.7	313.3	284.7	331.1	293.5	309.6	318.0	298.4
No. of new rental sales (%YoY)	21.3	24.8	4.2	(9.4)	(13.6)	(3.2)	2.0	(1.2)	11.7	(9.9)
No. of membership account ('000, end of Q)	967	1,011	1,034	1,002	1,004	1,082	1,118	1,133	1,135	1,100
Increase in membership accounts (QoQ)	29.3	44.5	23.0	(32.4)	1.6	78.5	36.3	14.7	2.1	(35.7)
Membership ARPU (KRW)	13,686	13,457	13,347	13,348	12,948	12,594	12,446	12,467	12,573	12,753
Cancel rate (%)	3.1	3.0	2.9	3.2	3.0	3.0	3.0	3.0	3.0	2.7
<b>Sales</b>	<b>400</b>	<b>436</b>	<b>430</b>	<b>444</b>	<b>442</b>	<b>446</b>	<b>458</b>	<b>460</b>	<b>465</b>	<b>497</b>
%YoY	9.4	19.3	15.6	11.3	10.6	2.4	6.5	3.6	5.2	11.3
<b>Rental</b>	<b>327</b>	<b>340</b>	<b>347</b>	<b>354</b>	<b>356</b>	<b>360</b>	<b>364</b>	<b>370</b>	<b>370</b>	<b>375</b>
%YoY	6.5	9.5	10.2	9.7	8.9	6.1	5.1	4.5	3.9	4.0
<b>Rental</b>	<b>288</b>	<b>300</b>	<b>306</b>	<b>313</b>	<b>317</b>	<b>321</b>	<b>323</b>	<b>327</b>	<b>327</b>	<b>332</b>
%YoY	6.0	9.5	10.3	10.0	10.1	7.1	5.7	4.6	3.2	3.5
<b>Membership</b>	<b>39</b>	<b>40</b>	<b>41</b>	<b>41</b>	<b>39</b>	<b>39</b>	<b>41</b>	<b>42</b>	<b>43</b>	<b>43</b>
%YoY	9.8	9.0	9.3	7.3	-0.4	-1.3	0.3	3.6	9.8	8.5
<b>Lump sum payment</b>	<b>32</b>	<b>39</b>	<b>41</b>	<b>32</b>	<b>33</b>	<b>41</b>	<b>39</b>	<b>32</b>	<b>37</b>	<b>48</b>
%YoY	19.2	57.0	67.3	1.6	2.7	4.5	-4.6	1.6	11.9	18.0
<b>Cosmetics</b>	<b>17</b>	<b>18</b>	<b>18</b>	<b>15</b>	<b>17</b>	<b>16</b>	<b>17</b>	<b>17</b>	<b>18</b>	<b>22</b>
%YoY	NA	NA	878.4	-29.1	-3.3	-8.8	-1.8	9.7	6.6	35.3
<b>Export</b>	<b>18</b>	<b>23</b>	<b>25</b>	<b>32</b>	<b>30</b>	<b>21</b>	<b>28</b>	<b>31</b>	<b>32</b>	<b>45</b>
%YoY	5.8	33.1	60.1	66.5	63.9	-8.0	14.2	-5.6	5.0	111.1
<b>Others</b>	<b>5</b>	<b>17</b>	<b>0</b>	<b>11</b>	<b>7</b>	<b>8</b>	<b>9</b>	<b>11</b>	<b>9</b>	<b>8</b>
%YoY	-63.5	26.2	-97.7	167.0	28.9	-50.6	2482.1	-0.9	36.7	-5.4
<b>Gross profit</b>	<b>274</b>	<b>295</b>	<b>295</b>	<b>294</b>	<b>297</b>	<b>304</b>	<b>306</b>	<b>294</b>	<b>311</b>	<b>329</b>
GP margin (%)	68.6	67.6	68.7	66.1	67.1	68.2	66.9	63.9	66.8	66.2
<b>OP</b>	<b>70</b>	<b>61.8</b>	<b>73.1</b>	<b>28.0</b>	<b>64.1</b>	<b>65.1</b>	<b>62.0</b>	<b>35.6</b>	<b>69.2</b>	<b>79.4</b>
%YoY	-12.9	-27.7	1.3	-59.6	-7.8	5.3	-15.2	27.1	7.9	22.0
OP margin (%)	17.4	14.2	17.0	6.3	14.5	14.6	13.5	7.7	14.9	16.0
<b>EBT</b>	<b>50.4</b>	<b>55.1</b>	<b>64.6</b>	<b>55.2</b>	<b>55.6</b>	<b>56.4</b>	<b>17.7</b>	<b>31.7</b>	<b>115.0</b>	<b>80.7</b>
%YoY	-22.1	-27.5	22.4	10.9	10.3	2.5	-72.6	-42.5	106.7	43.1
<b>NP</b>	<b>38.8</b>	<b>42.1</b>	<b>49.2</b>	<b>47.1</b>	<b>41.2</b>	<b>44.0</b>	<b>12.9</b>	<b>21.6</b>	<b>80.2</b>	<b>60.6</b>
%YoY	-24.7	-28.9	36.6	28.6	6.4	4.6	-73.7	-54.2	94.5	37.7

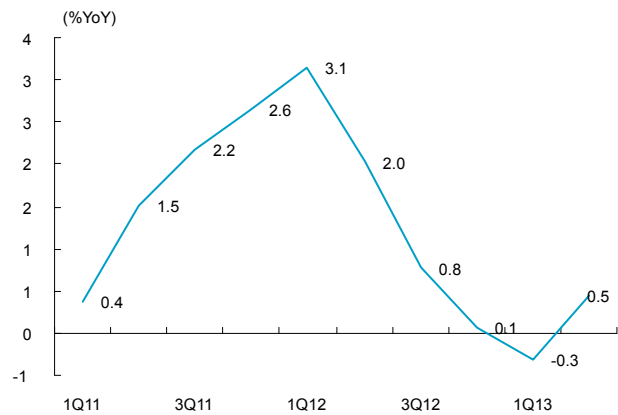
Source: Coway, Korea Investment securities &amp; Investment

**Figure 1. Net subscriber additions slow**



Source: Coway, Korea Investment securities & Investment

**Figure 2. ARPU picks up**



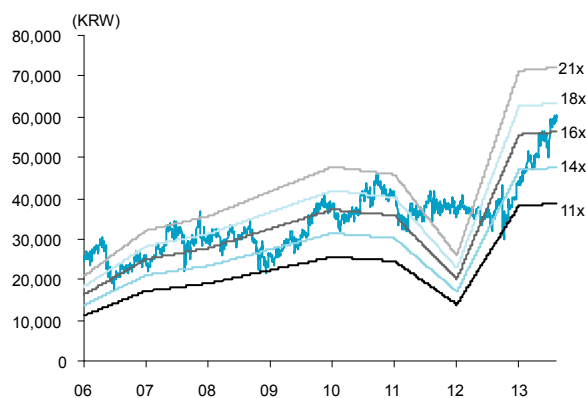
Source: Coway, Korea Investment securities & Investment

**Table 2. Subsidiaries of Coway**

Subsidiaries	Stake	2012 Sales	2012 OP	2Q13 Sales	2Q13 OP
China	100	55	0.0	18	0.1
Malaysia	100	54	1.9	19	0.9
USA	100	30	(1.6)	9	0.0
Thailand	100	12	(2.0)	3	(2.4)
Green Entech	100	53	0.6	15	0.7

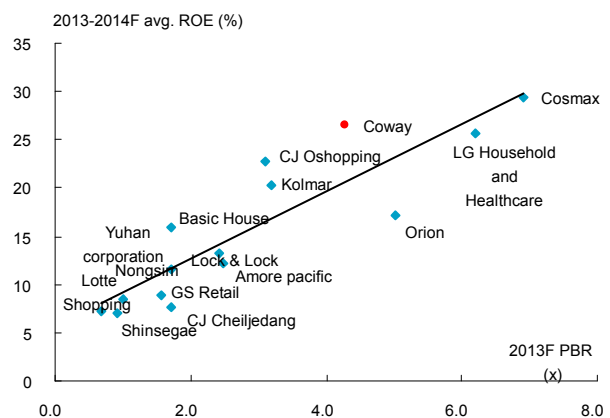
Source: Coway, Korea Investment securities & Investment

**Figure 3. Target PE at record 21x**



Source: Datastream, Korea Investment securities & Investment

**Figure 4. Coway PB band chart**



Source: Datastream, Korea Investment securities & Investment

Figure 5. Marketing efforts to grow water demand



Source: Korea Investment securities &amp; Investment

Figure 6. Water marketing campaign overview

코웨이에서 제안하는 좋은 물습관 가이드 coway

물은 적어도 하루 8잔 1.5리터 이상	물은 컵보다 조금 낮은 20-25cm	물도 마실때 꼭꼭 입어서
수분기별엔 마음껏 물을 만약학 강화	대중 여행엔 시원한 물로 탈수 예방	운동할 땀 30분 마다 한잔씩
물공수가 마시고 싶은 편 물 한 잔 먼저	수분 밸런스 조금씩 자주 마시기	마음껏 물 한 잔으로 스트레스 해소

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2. 학교에서 기말 보고	6. 6교시 앞두고 토크 타임
3. 1교시 끝나고 책이랑	7. 가랑 씨고 장애가기 전에
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Source: Korea Investment securities &amp; Investment

**Balance sheet**

FY-ending Dec. (W bn)	2011A	2012A	2013F	2014F	2015F
Current assets	511	691	664	751	822
Cash & cash equivalent	65	119	60	106	135
Accounts & other receivables	257	292	321	342	364
Inventory	73	41	45	48	52
Non-current assets	1,065	1,010	1,065	1,114	1,162
Investment assets	285	155	168	179	184
Tangible assets	535	594	624	654	685
Intangible assets	156	158	159	159	165
Total assets	1,576	1,702	1,729	1,865	1,984
Current liabilities	534	720	690	667	610
Accounts & other payables	187	205	226	241	256
ST debt & bond	165	296	196	156	106
Current portion of LT debt	110	110	110	110	110
Non-current liabilities	294	179	152	154	156
Debentures	177	118	118	118	118
LT debt & financial liabilities	90	36	6	6	6
Total liabilities	828	899	841	820	766
Paid-in capital	41	41	41	41	41
Capital surplus	131	131	131	131	131
Capital adjustments	(99)	(85)	(85)	(85)	(85)
Retained earnings	678	717	802	958	1,132
Shareholders' equity	748	803	888	1,044	1,218
Adj. shareholders' equity	738	785	969	1,136	1,322

**Cash flow**

FY-ending Dec. (W bn)	2011A	2012A	2013F	2014F	2015F
C/F from operating	318	429	385	424	440
Net profit	177	120	257	261	286
Depreciation	145	165	176	189	202
Amortization	8	7	7	7	7
Net incr. in W/C	(112)	(38)	(56)	(34)	(55)
Others	100	175	1	1	0
C/F from investing	(344)	(301)	(236)	(244)	(256)
CAPEX	(299)	(295)	(209)	(222)	(235)
Decr. in fixed assets	9	3	3	3	3
Incr. in investment	(42)	(3)	(13)	(11)	(5)
Net incr. in intangible assets	(7)	(8)	(8)	(7)	(13)
Others	(5)	2	(9)	(7)	(6)
C/F from financing	36	(74)	(208)	(133)	(155)
Incr. in equity	0	12	0	0	0
Incr. in debts	213	21	(130)	(40)	(50)
Dividends	(80)	(78)	(78)	(93)	(105)
Others	(97)	(29)	0	0	0
C/F from others	(0)	(1)	0	0	0
Increase in cash	8	54	(59)	46	29

Note: 1. Based on K-IFRS (non-consolidated)  
2. EPS and BPS are calculated using adjusted net profit and shareholders' equity that includes equity-method gains/losses

**Income statement**

FY-ending Dec. (W bn)	2011A	2012A	2013F	2014F	2015F
Sales	1,710	1,807	1,985	2,118	2,254
COGS	552	605	655	688	726
Gross profit	1,158	1,201	1,330	1,430	1,528
SG&A expense	915	974	1,026	1,080	1,149
Operating profit	243	228	304	350	379
Financial income	2	4	4	4	5
Interest income	2	1	2	2	3
Financial expense	26	62	21	18	16
Interest expense	25	29	21	18	16
Other non-operating profit	6	(5)	52	8	9
Gains (Losses) in associates, subsidiaries and JV	0	(3)	0	0	0
Earnings before tax	225	161	339	345	377
Income taxes	48	42	82	83	91
Net profit	177	120	257	261	286
Other comprehensive profit	(4)	(2)	0	0	0
Total comprehensive profit	173	118	257	261	286
EBITDA	396	400	487	545	588
Adj. net profit	167	94	260	265	290

**Key financial data**

FY-ending Dec.	2011A	2012A	2013F	2014F	2015F
per share data (KRW)					
EPS	2,235	1,268	3,478	3,544	3,881
BPS	10,962	11,354	13,739	15,902	18,321
DPS	1,050	0	2,300	1,400	1,500
Growth (%)					
Sales growth	13.9	5.7	9.9	6.7	6.4
OP growth	(20.7)	(6.4)	33.3	15.1	8.4
NP growth	(5.6)	(43.7)	176.1	1.9	9.5
EPS growth	(3.9)	(43.3)	174.4	1.9	9.5
EBITDA growth	(11.1)	1.0	21.7	12.1	7.8
Profitability (%)					
OP margin	14.2	12.6	15.3	16.5	16.8
NP margin	9.8	5.2	13.1	12.5	12.9
EBITDA margin	23.1	22.1	24.5	25.8	26.1
ROA	12.1	7.3	15.0	14.5	14.9
ROE	22.2	12.3	29.6	25.2	23.6
Dividend yield	2.9	0.0	3.9	2.4	2.6
Stability					
Net debt (W bn)	468	473	402	316	236
Debt/equity ratio (%)	72.4	73.8	52.1	40.4	30.5
Valuation (X)					
PER	16.4	34.3	16.9	16.6	15.2
PBR	3.3	3.8	4.3	3.7	3.2
PSR	1.7	1.9	2.3	2.1	2.0
EV/EBITDA	8.0	9.4	10.0	8.7	8.0

**Changes to recommendation and price target**

Company (Code)	Date	Recommendation	Price target
Coway (021240)	02-23-12	BUY	W47,000
	09-28-12	Hold	-
	02-18-13	BUY	W56,000
	05-11-13	BUY	W63,000
	08-09-13	BUY	W73,000



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- BUY: Expected to give a return of +15% or more
- Hold: Expected to give a return between -15% and 15%
- Underweight: Expected to give a return of -15% or less
- Korea Investment & Securities does not offer target prices for stocks with Hold or Underweight ratings.

■ **Guide to Korea Investment & Securities Co., Ltd. sector ratings for the next 12 months**

- Overweight: Recommend increasing the sector's weighting in the portfolio compared to its respective weighting in the Kospi (Kosdaq) based on market capitalization.
- Neutral: Recommend maintaining the sector's weighting in the portfolio in line with its respective weighting in the Kospi (Kosdaq) based on market capitalization.
- Underweight: Recommend reducing the sector's weighting in the portfolio compared to its respective weighting in the Kospi (Kosdaq) based on market capitalization.

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Prepared by: Eun-chaee Na

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