

Coway (021240)

12M rating **BUY (Maintain)**

12M TP **W106,000** from W94,000

Up/downside **+6%**

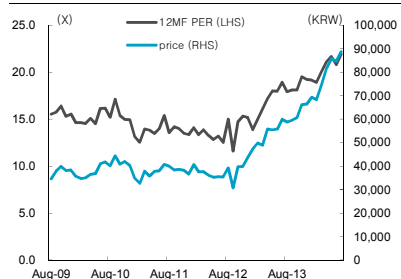
Stock Data

KOSPI (Jul 8, pt)	2,007
Stock price (Jul 8, KRW)	88,800
Market cap (USD mn)	6,768
Shares outstanding (mn)	77
52-Week high/low (KRW)	88,800/56,800
6M avg. daily turnover (USD mn)	15.5
Free float / Foreign ownership (%)	65.4/53.7
Major shareholders (%)	
Coway Holdings, Inc. and 12 others	31.0

Performance

	1M	6M	12M
Absolute (%)	5.3	38.3	50.0
Relative to KOSPI (p/p)	4.8	35.9	39.6

12MF PE trend



Source: WISEfn consensus

2Q14 preview: Reliable results despite poor conditions

Solid new sales in 2Q14, OP to just top consensus

We estimate 2Q14 separate sales will grow 8% YoY and OP 22% YoY. Specifically, OP should reach W96.8bn, slightly above the consensus of W93bn, on an OPM of 18%. After sales eroded in 2013 due to price hikes last April, 2Q14 rental sales should rebound, growing 12% YoY to 330,000 units, which would be the first increase in five quarters. And, total net subscriber growth should pick up after bottoming out in 1Q14 on strong sales. Of note, net subscriber growth was bolstered by a lower cancellation rate last year. And, the monthly cancellation rate remains below 1% as air purifiers, bidets and other products are now considered household necessities. Meanwhile, ARPU should grow about 2% on the outflow of low-price memberships and an improved product mix.

New products, exports and cosmetics continue to grow, SG&A under control

We estimate rental sales (75% of total sales) will grow 6%, while cosmetics (5% of total sales) and exports (10% of total sales) both grow almost 20%. Lump-sum payments (8% of total sales) should slip YoY on the reinforced rental strategies. Meanwhile, growth prospects are solid for new products and businesses with water purifiers, air purifiers and mattresses likely to fuel solid sales growth in 2Q14. Water purifier sales had decreased over the past five quarters, but should rebound on new products, such as the micro ice water purifier, while comprehensive air purifier sales should also be favorable. For mattresses, sales should grow on a broader line-up in terms of sizes and seasonal effects. Overall, water purifiers should reinforce its leading position, air purifiers should benefit from a growing dehumidifier market and mattresses should gain more market share. Meanwhile, exports should be strong on brisk air purifier shipments to China, despite the high base effect (111% YoY growth in 2Q13). And, home shopping sales and hit products should continue to fuel the cosmetics division. Furthermore, there appears to be no significant cost burden due to tight management, including lower marketing and sales commissions, backed by the decline in high-commission lump-sum payment sales. In addition, rental disposal losses should stabilize on the low cancellation rate.

Share re-rating to continue, raise TP to W106,000

We revise up our TP 13% from W94,000 to W106,000 as we lift 2014 and 2015 EPS by 2% to reflect favorable earnings trends. Of note, we also applied 12MF EPS to our valuation. Meanwhile, we lifted our target PE to 25x (20% premium) from 23x (10% premium to historical peak). We believe Coway has confirmed high

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Yr to	Sales	OP	NP	EPS	% chg	EBITDA	PE	EV/EBITDA	PB	ROE	DY
Dec	(W bn)	(W bn)	(W bn)	(KRW)	(YoY)	(W bn)	(x)	(x)	(x)	(%)	(%)
2012A	1,993	226	94	1,267	(43.3)	410	34.4	9.0	3.8	12.3	-
2013A	2,118	339	245	3,283	159.1	537	20.2	9.5	4.9	28.4	4.1
2014F	2,311	391	294	3,956	20.5	582	22.4	11.6	5.7	28.9	2.1
2015F	2,517	437	331	4,455	12.6	629	19.9	10.6	5.0	28.0	2.4
2016F	2,738	481	367	4,935	10.8	674	18.0	9.7	4.4	26.8	2.6

Note: Net profit and EPS are based on figures attributed to controlling interest

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earnings visibility and fundamental improvements as margins continue to trend up this year after the sharp increase in 2013. We remain bullish on stable cash flows from the growing environmental home appliance market and rental services. Furthermore, Coway should differentiate itself from other consumer plays on a high ROE and steady efforts to grow shareholder value, such as an estimated 2014 dividend yield of 2.1%.

Table 1. 2Q14 preview: Earnings to beat consensus

(W bn, %)

	2Q14F		Growth	
	KIS estimate	Consensus	QoQ	YoY
Sales	537	531	8.5	8.0
OP	97	93	7.8	22.0
OPM (%)	18.0	17.6	(0.1)	2.1
EBT	96	90	9.0	18.6
NP	73	67	9.8	19.8

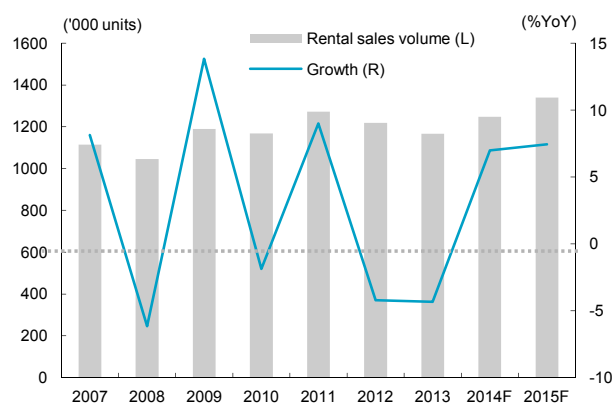
Source: Fnguide, Korea Investment securities & Investment

Table 2. Overview of major EHA market

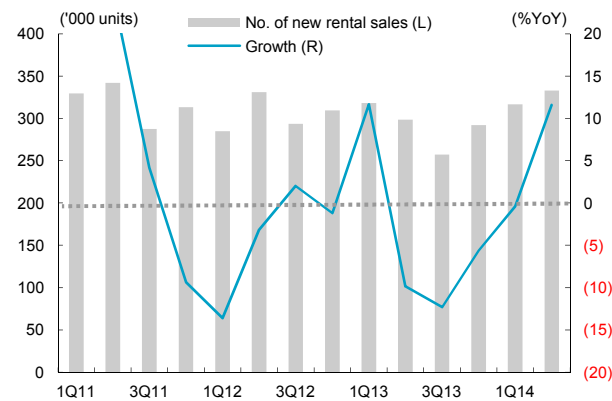
(W bn, '000 units, %, '000 accounts)

	Market size	Annual sales volume	Penetration	Estimated saturation rate	Coway market share	Accounts (sales volume)	Sales type
Water purifiers	1,5tr	1,200	34.0%	55~60%	50%	3,020	Rental/membership/lump-sum payment
Bidets	500	800-1,000	18.0%	50~60%	43%	1,350	Rental/membership/lump-sum payment
Air purifiers (Korea)	500	400	12.3%	45~50%	41%	960	Rental/membership/lump-sum payment
Air purifiers (China)	850	2,400	0.1%	45~50%	45%	500	Lump-sum payment/ODM
Mattresses (incl. frames)	800	700	70.0%	70%	10%	140	Rental/membership/lump-sum payment
Dehumidifiers	300	1,000	12.0%	50%	10%	100	Lump-sum payment
Water	100	NA	NA	NA	NA	360	Rental/membership/lump-sum payment
Food waste treatment system	Less than W100bn	NA	NA	NA	NA	36	Rental/membership/lump-sum payment

Source: Industry data, Korea Investment & Securities

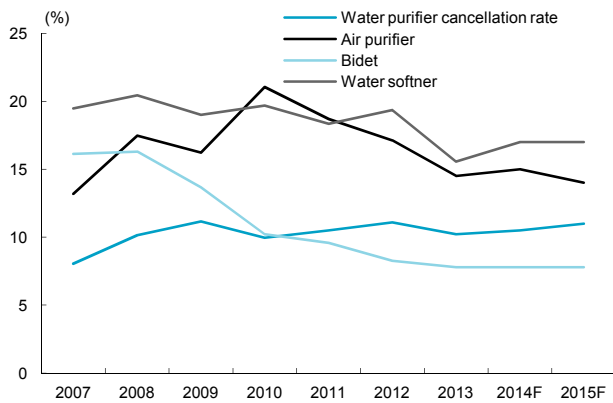
Figure 1. Rentals slipped in 2012-13, but should rebound **Figure 2. Sales pick up after five quarters**

Source: Coway, Korea Investment securities & Investment



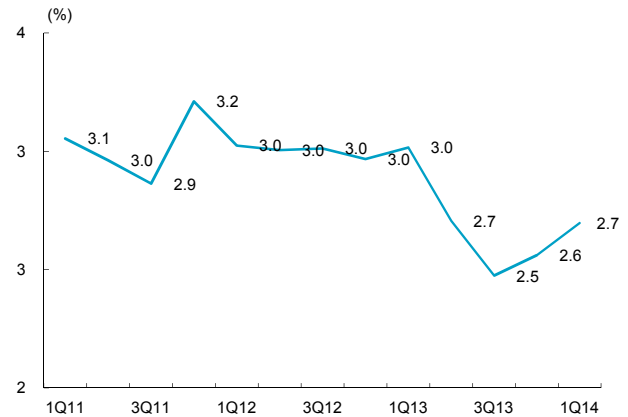
Source: Coway, Korea Investment securities & Investment

Figure 3. Moderate decline in cancellation rate



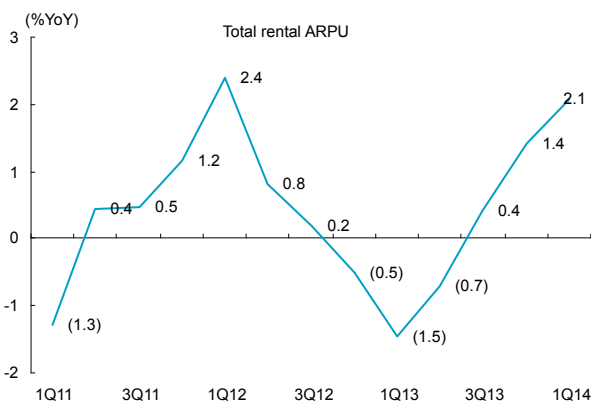
Source: Datastream, Korea Investment securities & Investment

Figure 4. 2Q14 monthly cancellation rate remained below 1%, 2Q14 should be flat



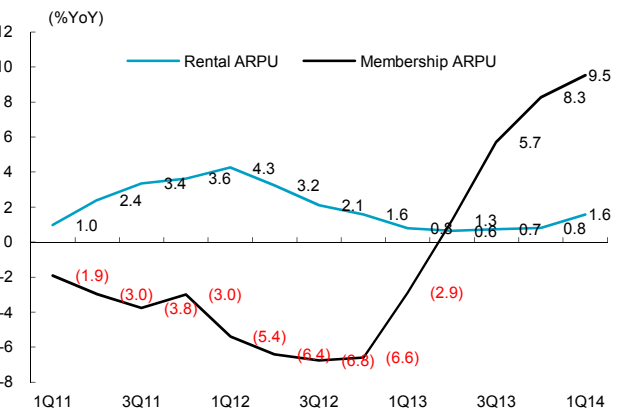
Source: Quantiwise, Korea Investment securities & Investment

Figure 5. Increasing rental ARPU



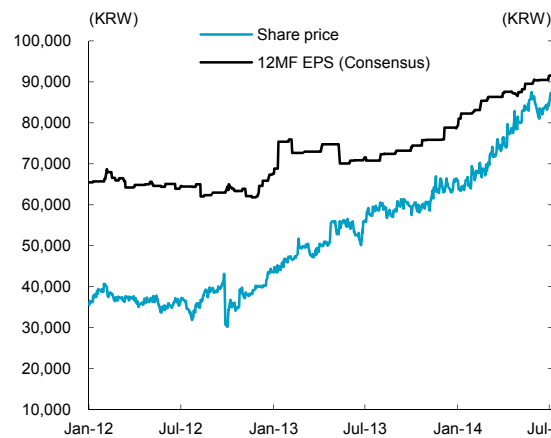
Source: Coway, Korea Investment securities & Investment

Figure 6. Membership ARPU rising rapidly on expiring service accounts and markups



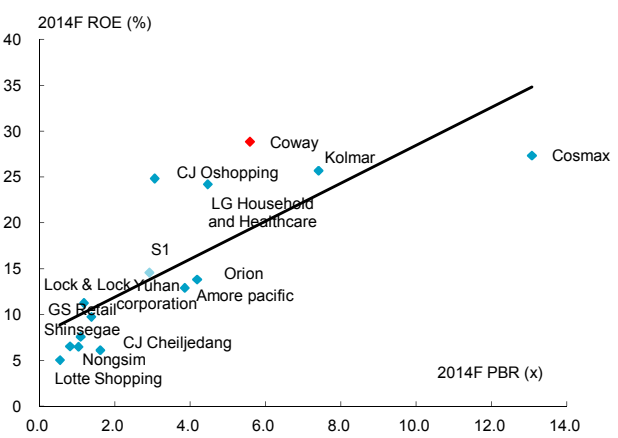
Source: Coway, Korea Investment securities & Investment

Figure 7. Moderate EPS growth



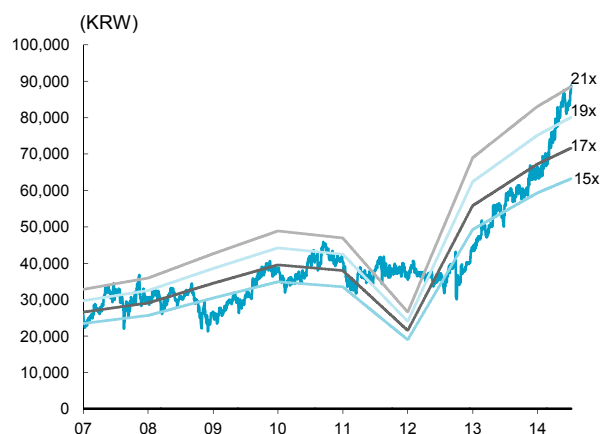
Source: Datastream, Korea Investment securities & Investment

Figure 8. PB/ROE comparison



Source: Quantiwise, Korea Investment securities & Investment

Figure 9. Coway PE band



Source: Datastream, Korea Investment securities & Investment

Figure 10. Coway PB band



Source: Quantwise, Korea Investment securities & Investment

Company overview & Glossary

■ Company overview

Coway makes and sells environmental home appliances (EHA) such as water/air purifiers, bidets, etc. The company mainly provides products through rentals and outright purchases to customers. Coway is the domestic leader in terms of market share and brand recognition with approximately 5.87mn accounts (rental users + memberships) as of end-2013. The company continues to expand its product lineup, which includes water/air purifiers, bidets, water softeners, food waste treatment systems, mattresses, etc., and is also stepping up overseas operations.

■ Glossary

- Rental: Customers gain the right to use a product by paying for registration and monthly rental fees
- Membership: Customers that have purchased a product or gained ownership receive services for product maintenance
- Outright purchase: A lump-sum payment made for a product with no maintenance service offered
- ARPU: Average revenue per user

Balance sheet

FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
Current assets	779	691	754	865	996
Cash & cash equivalent	152	239	260	327	411
Accounts & other receivables	262	250	272	296	323
Inventory	72	66	72	78	85
Non-current assets	976	976	1,026	1,078	1,132
Investment assets	54	55	60	65	71
Tangible assets	630	638	657	676	695
Intangible assets	184	177	193	210	229
Total assets	1,755	1,668	1,781	1,943	2,128
Current liabilities	759	677	632	614	598
Accounts & other payables	236	224	245	266	290
ST debt & bond	330	182	132	82	32
Current portion of LT debt	110	146	146	146	146
Non-current liabilities	211	50	55	60	65
Debentures	118	0	0	0	0
LT debt & financial liabilities	36	0	0	0	0
Total liabilities	970	727	687	674	663
Controlling interest	785	941	1,094	1,269	1,465
Capital stock	41	41	41	41	41
Capital surplus	126	126	126	126	126
Other Reserves	(85)	(94)	(94)	(94)	(94)
Retained earnings	701	868	1,021	1,196	1,392
Minority interest	0	0	0	0	0
Shareholders' equity	785	941	1,094	1,269	1,465

Cash flow

FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
C/F from operating	454	537	453	516	551
Net profit	94	245	294	331	367
Depreciation	175	191	183	183	183
Amortization	8	8	8	9	10
Net incr. in W/C	(24)	(41)	(33)	(8)	(10)
Others	201	134	1	1	1
C/F from investing	(319)	(76)	(240)	(243)	(246)
CAPEX	(314)	(268)	(202)	(202)	(202)
Decr. in fixed assets	4	10	0	0	0
Incr. in investment	(3)	180	(5)	(5)	(6)
Net incr. in intangible assets	(8)	(2)	(24)	(26)	(28)
Others	2	4	(9)	(10)	(10)
C/F from financing	(76)	(373)	(191)	(206)	(221)
Incr. in equity	12	5	0	0	0
Incr. in debts	20	(262)	(50)	(50)	(50)
Dividends	(78)	(78)	(202)	(141)	(156)
Others	(30)	(38)	61	(15)	(15)
C/F from others	(5)	(1)	0	0	0
Increase in cash	54	86	22	67	83

Note: Based on K-IFRS (consolidated)

Income statement

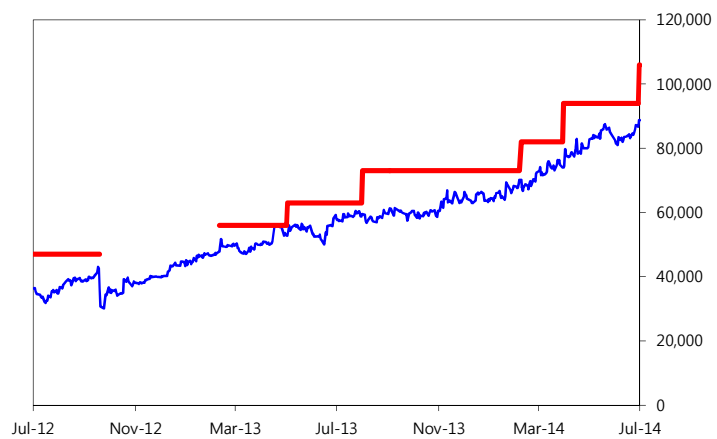
FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
Sales	1,993	2,118	2,311	2,517	2,738
COGS	678	721	786	846	920
Gross profit	1,315	1,397	1,525	1,671	1,818
SG&A expense	1,088	1,058	1,134	1,234	1,337
Operating profit	226	339	391	437	481
Financial income	2	4	6	8	9
Interest income	2	4	6	8	9
Financial expense	30	19	9	8	6
Interest expense	30	19	9	8	6
Other non-operating profit	(58)	(15)	0	0	0
Gains (Losses) in associates, subsidiaries and JV	5	18	0	0	0
Earnings before tax	146	327	388	437	484
Income taxes	52	82	94	106	117
Net profit	94	245	294	331	367
Net profit of controlling interest	94	245	294	331	367
Other comprehensive profit	5	(1)	0	0	0
Total comprehensive profit	99	244	294	331	367
Total comprehensive profit of controlling interest	99	244	294	331	367
EBITDA	410	537	582	629	674

Key financial data

FY-ending Dec.	2012A	2013A	2014F	2015F	2016F
per share data (KRW)					
EPS	1,267	3,283	3,956	4,455	4,935
BPS	11,354	13,535	15,519	17,789	20,328
DPS	0	2,710	1,900	2,100	2,300
Growth (%)					
Sales growth	9.2	6.3	9.1	8.9	8.8
OP growth	(3.7)	49.9	15.3	11.8	10.0
NP growth	(43.7)	160.6	20.1	12.5	10.8
EPS growth	(43.3)	159.1	20.5	12.6	10.8
EBITDA growth	3.9	31.1	8.4	8.0	7.1
Profitability (%)					
OP margin	11.3	16.0	16.9	17.4	17.6
NP margin	4.7	11.6	12.7	13.2	13.4
EBITDA margin	20.6	25.4	25.2	25.0	24.6
ROA	5.6	14.3	17.1	17.8	18.0
ROE	12.3	28.4	28.9	28.0	26.8
Dividend yield	-	4.1	2.1	2.4	2.6
Dividend payout ratio	0.0	82.4	48.0	47.1	46.6
Stability					
Net debt (W bn)	439	90	17	(100)	(234)
Debt/equity ratio (%)	75.7	35.6	26.0	18.5	12.6
Valuation (X)					
PE	34.4	20.2	22.4	19.9	18.0
PB	3.8	4.9	5.7	5.0	4.4
EV/EBITDA	9.0	9.5	11.6	10.6	9.7

Changes to recommendation and price target

Company (Code)	Date	Recommendation	Price target
Coway (021240)	09-28-12	Hold	-
	02-18-13	BUY	W56,000
	05-11-13	BUY	W63,000
	08-09-13	BUY	W73,000
	02-16-14	BUY	W82,000
	04-08-14	BUY	W94,000
	07-08-14	BUY	W106,000



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Prepared by: Eun-chaе Na

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