

Coway (021240)

Above
In line
Below

12M rating **BUY (Maintain)**
 12M TP **W106,000** from W106,000
 Up/downside **+16%**

Stock Data

KOSPI (Jul 28, pt)	2,049
Stock price (Jul 28, KRW)	91,100
Market cap (USD mn)	6,846
Shares outstanding (mn)	77
52-Week high/low (KRW)	94,600/56,800
6M avg. daily turnover (USD mn)	16.2
Free float / Foreign ownership (%)	65.3/54.3
Major shareholders (%)	
Coway Holdings, Inc. and 12 others	31.0

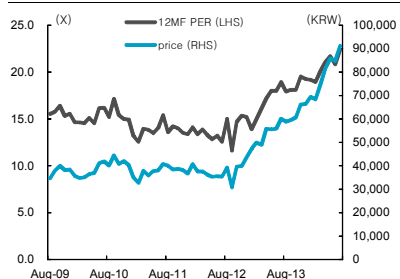
Valuation

	2013A	2014F	2015F
PE (x)	20.2	23.9	20.1
PB (x)	4.9	5.9	5.1
ROE (%)	28.4	28.0	28.7
EV/EBITDA (x)	9.5	12.1	10.7
EPS (KRW)	3,283	3,816	4,532
BPS (KRW)	13,535	15,383	17,727

Performance

	1M	6M	12M
Absolute (%)	9.5	40.2	54.4
Relative to KOSPI (%p)	6.5	33.3	47.2

12MF PE trend



Source: WISEfn consensus

Water purifiers recovery, growth of new businesses confirmed

What's new: Solid earnings, robust rentals and new sales

Coway posted 2Q14 separate sales growth of 5.3% YoY and OP growth of 23% YoY. Specifically, OP climbed to W97.6bn, in line with our estimate, as OPM firmed 2.7%p to 18.7%. EBT disappointed due to W7.1bn in FX-related losses, but stripping out the currency effects EBT was in line with our estimate. Meanwhile, consolidated OP reached W97.1bn, in line with separate results. Rental sales grew 4.7% YoY and exports 25% YoY. Cosmetics sales were flat YoY. The total number of rental subscribers climbed 1.8% YoY to 5.574mn, while ARPU firmed 3.4% YoY. New rental sales surged 24% YoY to 371,000 units, and net growth expanded 62,000 QoQ. Cancellation rate was low at 1.04% per month.

Pros: Surprising new sales, sales to recover on growing subscribers

New sales climbed to a new quarterly record, after bottoming out in 3Q13 following the price markup last April. By product, sales of water purifiers surged 30% YoY, while air purifiers climbed 14% YoY. And, water purifier market share should grow on solid sales of new products, including a micro ice water purifier. Of note, market share had eroded as new sales fell 14% due to the markup and more competition in 2013. Water purifiers are not only leading new subscriber growth, but are also impacting sales mix as these products have the highest ARPU in the rental business. Meanwhile, air purifiers are benefiting from a growing market, while Coway should rank third in mattress sales on a growing market share. Exports, led by air purifiers in China, also remain favorable.

Cons: Slow sales growth, growth to recover in 2H14

Sales growth reached only about 5% in 2Q14, but we believe growth will recover on increasing subscribers from 3Q14 as the relatively mild growth is mostly due to a high base effect and the markup since 2H13. In particular, subscribers should grow 3.5% YoY in 3Q14 and 4.6% YoY in 4Q14, versus only 0.8% YoY in 1Q14 and 1.8% YoY in 2Q14.

Conclusion: Robust earnings on firming competitiveness and growth potential; maintain BUY

We maintain BUY with a TP of W106,000 (25x 12MF PE). We remain bullish on stable cash flows from the growing environmental home appliance market and rental services. Core businesses are also recovering and overseas businesses are favorable. A high payout ratio and steady efforts to grow shareholder value should help Coway shares continue to rally.

(W bn, %, %p)

	2Q14P				Change		2014F	
	KIS est.	Actual	Diff.	Consensus	QoQ	YoY	KIS	Consensus
Sales	537	523	(2.6)	531	5.8	5.3	2,051	2,075
OP	97	98	0.6	93	8.7	23.0	384	376
OP margin	18.1	18.7	0.6	18	0.5	2.7	18.7	18.1
EBT	96	87	(9.7)	90	(1.3)	7.4	387	385
NP	73	65	(10.7)	67	(1.3)	7.7	293	283

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Table 1. Coway's 2Q14 review (consolidated)

(W bn, %)

	2Q14P		Growth	
	Actual	Consensus	QoQ	YoY
Sales	557	568	4.1	0.1
OP	97	97	7.6	18.6
OPM (%)	17.4	17.1	0.6	2.7
EBT	87	94	(2.2)	6.8
NP	66	71	0.3	11.0

Source: Fnguide, Korea Investment securities & Investment

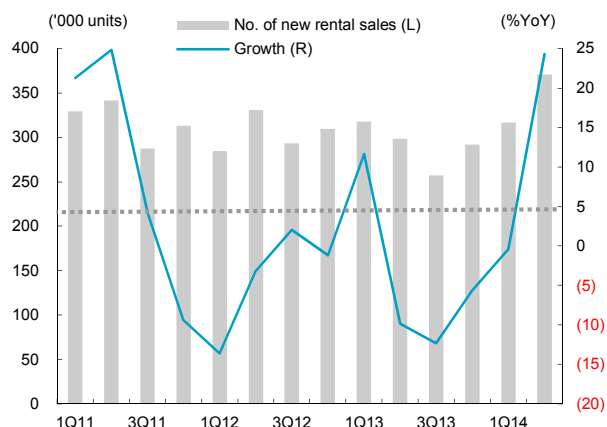
Table 2. Earnings breakdown

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

	1Q11	2Q11	3Q11	4Q11	1Q12	2Q12	3Q12	4Q12	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14
Total no. of accounts	5,201	5,333	5,411	5,452	5,484	5,600	5,670	5,741	5,467	5,474	5,474	5,501	5,513	5,574
Increase in total account (QoQ)	118	132	78	41	32	116	70	71	NM	7	0	27	12	62
%YoY	8.4	9.6	9.7	7.3	5.4	5.0	4.8	5.3	NM	NM	NM	NM	0.8	1.8
No. of rental account ('000, end of Q)	4,234	4,321	4,377	4,450	4,480	4,518	4,551	4,607	4,332	4,374	4,387	4,435	4,455	4,487
Increase in rental account (QoQ)	89	87	55	73	30	38	34	56	NA	43	12	48	20	32
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	1,088	1,066	1,058	1,087
Increase in membership accounts (QoQ)	29	44	23	(32)	2	78	36	15	2	(36)	(12)	(21)	(8)	29
No. of new rental sales ('000 units)	330	342	288	313	285	331	294	310	318	298	257	292	317	371
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)	(12.3)	(5.6)	(0.4)	24.3
Cancel rate (%)	3.1	3.0	2.9	3.2	3.0	3.0	3.0	3.0	3.0	2.9	2.7	2.2	2.9	3.1
Rental ARPU (Won)	21,206	21,493	21,511	21,706	21,715	21,667	21,550	21,595	22,021	22,831	23,024	23,347	23,380	23,598
Rental ARPU (%YoY)	(1.3)	0.4	0.5	1.2	2.4	0.8	0.2	(0.5)	NM	NM	NM	NM	NM	3.4
Membership ARPU (KRW)	22,218	22,586	22,845	22,993	23,164	23,319	23,325	23,357	NM	25,176	25,253	25,381	25,67	25,850
Membership ARPU (%YoY)	1.0	2.4	3.4	3.6	4.3	3.2	2.1	1.6	NM	NM	NM	NM	NM	2.7
Sales	13,686	13,457	13,347	13,348	12,948	12,594	12,446	12,467	12,573	12,753	13,159	13,498	13,773	14,213
%YoY	(1.9)	(3.0)	(3.8)	(3.0)	(5.4)	(6.4)	(6.8)	(6.6)	(2.9)	1.3	5.7	8.3	9.5	11.5
Rental	400	436	430	444	442	446	458	460	465	497	489	482	495	523
%YoY	9.4	19.3	15.6	11.3	10.6	2.4	6.5	3.6	5.2	11.3	6.8	4.9	6.4	5.3
Rental	327	340	347	354	356	360	364	370	370	375	378	384	386	392
%YoY	6.5	9.5	10.2	9.7	8.9	6.1	5.1	4.5	3.9	4.0	3.8	4.0	4.3	4.7
Membership	32	39	41	32	33	41	39	32	37	48	35	29	28	37
%YoY	19.2	57.0	67.3	1.6	2.7	4.5	(4.6)	1.6	11.9	18.0	(9.4)	(9.2)	(24.6)	(21.7)
Lump sum payment	17	18	18	15	17	16	17	17	18	22	17	20	21	22
%YoY	NA	NA	878.4	(29.1)	(3.3)	(8.8)	(1.8)	9.7	6.6	35.3	(4.2)	17.9	17.1	0.7
Cosmetics	18	23	25	32	30	21	20	31	32	45	38	31	45	56
%YoY	5.8	33.1	60.1	66.5	63.9	(8.0)	(18.8)	(5.6)	5.0	111.1	90.7	0.4	43.5	25.2
Export	5	17	0	11	7	8	17	11	9	8	21	20	15	15
%YoY	(63.5)	26.2	(97.7)	167.0	28.9	(50.6)	4711.7	(0.9)	36.7	(5.0)	21.1	83.9	62.6	95.9
Others	274	295	295	294	297	304	306	294	311	329	319	323	326	343
%YoY	68.6	67.6	68.7	66.1	67.1	68.2	66.9	63.9	66.8	66.2	65.3	67.0	65.8	65.5
Total no. of accounts	70	73	73	28	64	65	63	36	69	79	97	88	90	98
Increase in total account (QoQ)	(12.9)	(15.0)	1.3	(59.6)	(7.8)	(10.3)	(14.0)	27.3	7.9	21.9	54.2	145.7	29.7	23.0
Gross profit	17.4	16.7	17.0	6.3	14.5	14.6	13.7	7.7	14.9	16.0	19.8	18.2	18.1	18.7
GP margin (%)	50	55	65	55	56	56	18	32	115	81	83	72	88	87
OP	(22.1)	(27.5)	22.4	10.9	10.3	2.5	(72.6)	(42.5)	106.7	43.1	369.2	126.3	(23.6)	7.4
%YoY	39	42	49	47	41	44	13	22	80	61	62	50	66	65
OP margin (%)	(25)	(29)	37	29	6	5	(74)	(54)	95	38	382	132	(18)	8

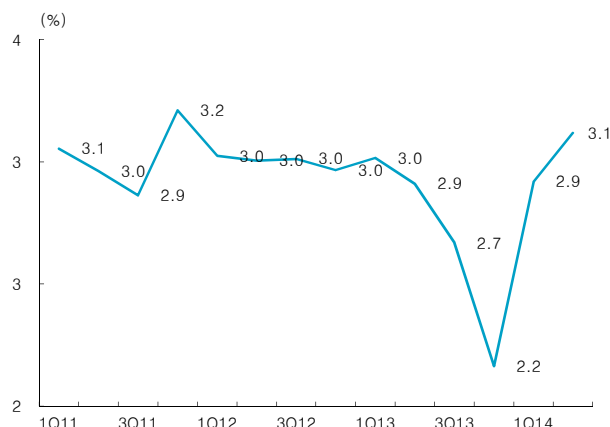
Source: Coway, Korea Investment securities & Investment

Figure 1. Record quarterly new sales



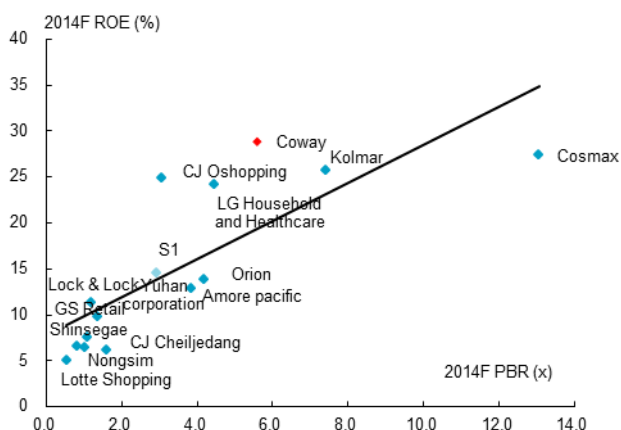
Source: Coway, Korea Investment securities & Investment

Figure 2. Cancellation rate



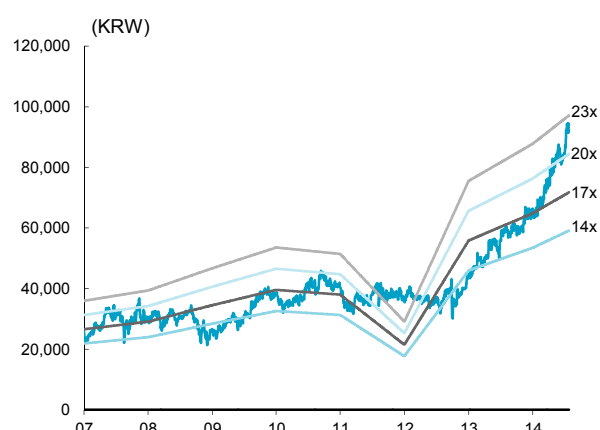
Source: Coway, Korea Investment securities & Investment

Figure 3. PB/ROE comparison



Source: Quantwise, Korea Investment securities & Investment

Figure 4. Coway band chart



Source: Quantwise, Korea Investment securities & Investment

Table 3. 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

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	734	843	968
Cash & cash equivalent	152	239	253	319	399
Accounts & other receivables	262	250	265	289	314
Inventory	72	66	70	76	83
Non-current assets	976	976	1,016	1,068	1,120
Investment assets	54	55	58	64	69
Tangible assets	630	638	657	676	695
Intangible assets	184	177	188	205	222
Total assets	1,755	1,668	1,750	1,911	2,089
Current liabilities	759	677	613	588	558
Accounts & other payables	236	224	238	260	282
ST debt & bond	330	182	132	82	32
Current portion of LT debt	110	146	146	146	146
Non-current liabilities	211	50	53	58	63
Debentures	118	0	0	0	0
LT debt & financial liabilities	36	0	0	0	0
Total liabilities	970	727	667	647	621
Controlling interest	785	941	1,083	1,264	1,468
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	1,010	1,191	1,395
Minority interest	0	0	0	0	0
Shareholders' equity	785	941	1,083	1,264	1,468

Cash flow

FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
C/F from operating	454	537	436	514	546
Net profit	94	245	284	337	375
Depreciation	175	191	183	183	183
Amortization	8	8	8	9	9
Net incr. in W/C	(24)	(41)	(39)	(16)	(23)
Others	201	134	0	1	2
C/F from investing	(319)	(76)	(230)	(243)	(244)
CAPEX	(314)	(268)	(202)	(202)	(202)
Decr. in fixed assets	4	10	0	0	0
Incr. in investment	(3)	180	(3)	(5)	(5)
Net incr. in intangible assets	(8)	(2)	(19)	(26)	(27)
Others	2	4	(6)	(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	15	65	81

Note: Based on K-IFRS (consolidated)

Income statement

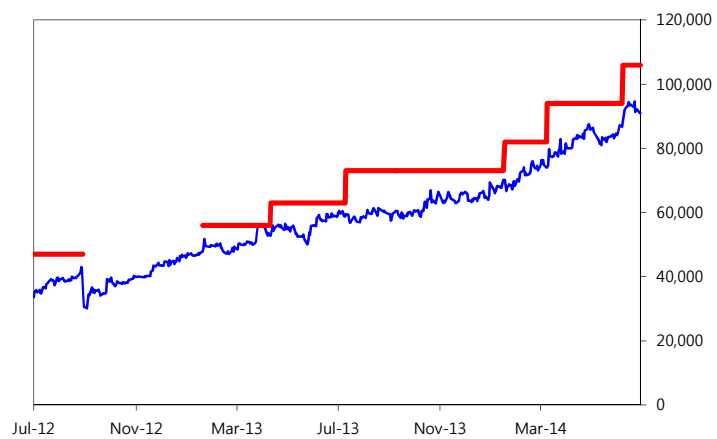
FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
Sales	1,993	2,118	2,248	2,452	2,662
COGS	678	721	760	822	887
Gross profit	1,315	1,397	1,488	1,631	1,776
SG&A expense	1,088	1,058	1,104	1,186	1,284
Operating profit	226	339	384	445	491
Financial income	2	4	(1)	7	9
Interest income	2	4	6	7	9
Financial 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	374	444	494
Income taxes	52	82	91	108	120
Net profit	94	245	284	337	375
Net profit of controlling interest	94	245	284	337	375
Other comprehensive profit	5	(1)	0	0	0
Total comprehensive profit	99	244	284	337	375
Total comprehensive profit of controlling interest	99	244	284	337	375
EBITDA	410	537	575	637	684

Key financial data

FY-ending Dec.	2012A	2013A	2014F	2015F	2016F
per share data (KRW)					
EPS	1,267	3,283	3,816	4,532	5,042
BPS	11,354	13,535	15,383	17,727	20,369
DPS	0	2,710	1,900	2,100	2,300
Growth (%)					
Sales growth	9.2	6.3	6.1	9.1	8.6
OP growth	(3.7)	49.9	13.3	15.8	10.5
NP growth	(43.7)	160.6	15.8	18.7	11.2
EPS growth	(43.3)	159.1	16.2	18.8	11.2
EBITDA growth	3.9	31.1	7.1	10.6	7.4
Profitability (%)					
OP margin	11.3	16.0	17.1	18.1	18.5
NP margin	4.7	11.6	12.6	13.7	14.1
EBITDA margin	20.6	25.4	25.6	26.0	25.7
ROA	5.6	14.3	16.6	18.4	18.7
ROE	12.3	28.4	28.0	28.7	27.4
Dividend yield	-	4.1	2.1	2.3	2.5
Dividend payout ratio	0.0	82.4	49.6	46.3	45.6
Stability					
Net debt (W bn)	439	90	25	(91)	(223)
Debt/equity ratio (%)	75.7	35.6	26.3	18.6	12.6
Valuation (X)					
PE	34.4	20.2	23.9	20.1	18.1
PB	3.8	4.9	5.9	5.1	4.5
EV/EBITDA	9.0	9.5	12.1	10.7	9.8

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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- BUY: Expected to give a return of +15% or more
- Hold: Expected to give a return between -15% and 15%
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- 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-chaе Na

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