

Coway (021240)

12M rating **BUY (Maintain)**

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

Up/downside **+34%**

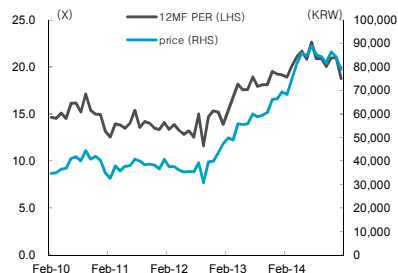
Stock Data

KOSPI (Jan 8, pt)	1,905
Stock price (Jan 8, KRW)	78,900
Market cap (USD mn)	5,548
Shares outstanding (mn)	77
52-Week high/low (KRW)	94,600/63,600
6M avg. daily turnover (USD mn)	14.4
Free float / Foreign ownership (%)	65.2/54.9
Major shareholders (%)	
Coway Holdings, Inc. and 9 others	31.0

Performance

	1M	6M	12M
Absolute (%)	(5.6)	(11.1)	22.9
Relative to KOSPI (%p)	(1.9)	(6.1)	25.7

12MF PE trend



Source: WISEfn consensus

4Q14 preview: Better earnings, as broadly expected

4Q14 OP in line with consensus; earnings growth driven by rentals

Coway's 4Q14 earnings should be largely in line with the consensus with sales growing an estimated 6% YoY to W512.4bn and OP 11% YoY to W97.6bn. OPM should rise 0.8%p YoY to 19.0%. Rental sales (80% of total) are expected to grow 6.1% YoY. Non-rental (lump-sum payments, cosmetics, exports and others) sales should increase 6.7% YoY after a 13% YoY drop in 3Q14. As of end-2014, the number of total subscribers reached 5.67mn, up 3.0% YoY, with ARPU likely up 2.9%. Net subscriber (rental + membership) growth is estimated at 62,000 in 4Q14, up from 28,000 in 3Q14. Coway has no issues in terms of costs with SG&A-to-sales ratio slightly trending downward on lower ad expenses, commissions paid and bonus payments.

Earnings in line; Solid new sales + low termination + recovering air purifier exports to China

Net growth in rental accounts that are fueling the rental business is attributed to brisk sales. 4Q14 new rental sales should be 322,000 units, up 10% YoY. In addition to seasonally strong demand for bidets and air purifiers, the company is regaining market share in water purifiers. Monthly sales volume of mattresses reached over 8,000 units, accounting for more than 7% of new rental sales. Monthly termination rate is also being held around 1%. ARPU is steadily rising, on: 1) an approximate 1% uptick in ARPU on higher rental fees, 2) a greater weighting of high value-added products, and 3) net growth in rental accounts that generate almost twice the ARPU than membership accounts. Among rental items, we are closely monitoring robust sales of water purifiers and mattresses that are outpacing average ARPU by more than 10%. We also expect the non-rental business to recover as exports, which were sluggish in 3Q14, should rise 25% YoY in 4Q14F led by China-bound air purifiers. We estimate 2015F sales will rise 8.3% YoY and OP 11.7% YoY. We also forecast rental division sales growth at 6.9% YoY and non-rentals at 13% YoY.

Growth concerns and valuation burden weigh on shares, but maintain BUY and TP of W106,000

With the pace of sales growth slowing to the 1% level in 3Q14, growth concerns and a valuation burden dragged down shares by 17% from the peak. The main rental business briefly slowed after a price increase in 2013, but we believe gradual growth is ahead given robust new sales and the ongoing diversification of rental products. While concerns were raised about intense competition at home and abroad, Coway has a firm foothold in the domestic market on stronger product

Yr to	Sales	OP	NP	EPS	% chg	EBITDA	PE	EVEBITDA	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	2,166	380	266	3,578	9.0	571	23.5	11.3	5.6	26.6	2.4
2015F	2,353	432	323	4,360	21.9	624	18.1	9.5	4.7	28.6	3.0
2016F	2,560	478	361	4,861	11.5	671	16.2	8.7	4.2	28.2	3.5

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

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Eun-chaee Na
822-3276-6160
ec.na@truefriend.com

competitiveness, sales power and sales channel additions, coupled with a thriving air purifier market in China. For the cosmetics business, sales power should be restored following the settlement of the trademark dispute. The overseas business in Malaysia and the US offers additional growth potential. Our investment points remain intact, such as: 1) gradual growth driven by firming domestic demand for environmental home appliances, 2) possible expansion of the overseas business and 3) shareholder-friendly policies. We maintain BUY and a TP of W106,000 (24x 12MF PE, a historical high).

Table 1. 4Q14F OP in line with consensus

(W bn, %)

	4Q14F	YoY	QoQ	Consensus	4Q13	3Q14	2014F
Sales	512	6.1	3.2	520	482	496	2,166
OP	98	11.4	1.0	99	88	97	380
EBT	95	31.9	7.7	100	72	88	351
NP	74	48.0	11.4	75	50	66	266

Note: Non-consolidated basis

Source: Coway, FnGuide, Korea Investment & Securities

Table 2. Quarterly earnings breakdown

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

	1Q12	2Q12	3Q12	4Q12	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14F
Total no. of accounts	5,484	5,600	5,670	5,741	5,467	5,474	5,474	5,501	5,513	5,574	5,603	5,665
Increase in total account (QoQ)	32	116	70	71	NM	7	0	27	12	62	28	62
%YoY	5.4	5.0	4.8	5.3	NM	NM	NM	NM	0.8	1.8	2.3	3.0
No. of rental account ('000, end of Q)	4,480	4,518	4,551	4,607	4,332	4,374	4,387	4,435	4,455	4,487	4,538	4,613
Increase in rental account (QoQ)	30	38	34	56	NM	43	12	48	20	32	51	75
No. of membership account ('000, end of Q)	1,004	1,082	1,118	1,133	1,135	1,100	1,088	1,066	1,058	1,087	1,065	1,052
Increase in membership accounts (QoQ)	2	78	36	15	NM	(36)	(12)	(21)	(8)	29	(22)	(13)
No. of new rental sales ('000 units)	285	331	294	310	318	298	257	292	317	371	311	322
No. of new rental sales (%YoY)	(13.6)	(3.2)	2.0	(1.2)	11.7	(9.9)	(12.3)	(5.6)	(0.4)	24.3	20.8	10.1
Churn rate (%)	1.0	1.0	1.0	1.0	1.0	1.0	0.9	0.9	1.0	1.0	1.0	1.0
Total ARPU (Won)	21,311	21,321	21,223	21,250	NM	22,638	22,836	23,146	23,159	23,362	23,589	23,744
Total ARPU (%YoY)	2.9	1.8	0.7	0.1	NM	NM	NM	NM	NM	3.2	3.3	2.6
Rental ARPU (Won)	23,164	23,319	23,325	23,357	NM	25,176	25,253	25,381	25,403	25,556	25,751	25,975
Rental ARPU (%YoY)	4.3	3.2	2.1	1.6	NM	NM	NM	NM	NM	1.5	2.0	2.3
Membership ARPU (Won)	12,948	12,594	12,446	12,467	NM	12,753	13,159	13,498	13,773	14,213	14,355	14,101
Membership (%YoY)	(5.4)	(6.4)	(6.8)	(6.6)	NM	NM	NM	NM	NM	11.5	9.1	4.5
Sales	442	446	458	460	465	497	489	482	495	523	496	512
%YoY	10.6	2.4	6.5	3.6	5.2	11.3	6.8	4.9	6.4	5.3	1.4	6.2
Rental-based	356	360	364	370	370	375	378	384	386	392	400	408
%YoY	8.9	6.1	5.1	4.5	3.9	4.0	3.8	4.0	4.3	4.7	5.7	6.1
Rental	317	321	323	327	327	332	335	339	342	347	353	363
%YoY	10.1	7.1	5.7	4.6	3.2	3.5	3.6	3.6	4.6	4.5	5.3	7.1
Membership	39	39	41	42	43	43	43	44	44	46	47	45
%YoY	(0.4)	(1.3)	0.3	3.6	9.8	8.5	5.1	3.2	2.6	7.0	8.6	2.7
Lump sum payment	33	41	39	32	37	48	35	29	28	37	32	28
%YoY	2.7	4.5	(4.6)	1.6	11.9	18.0	(9.4)	(9.2)	(24.6)	(21.7)	(10.4)	(4.2)
Cosmetics	17	16	17	17	18	22	17	20	21	22	17	21
%YoY	(3.3)	(8.8)	(1.8)	9.7	6.6	35.3	(4.2)	17.9	17.1	0.7	3.6	4.6
Export	30	21	20	31	32	45	38	31	45	56	33	38
%YoY	63.9	(8.0)	(18.8)	(5.6)	5.0	111.1	90.7	0.4	43.5	25.2	(13.0)	24.5
Others	7	8	17	11	9	8	21	20	15	15	15	18
%YoY	28.9	(50.6)	4711.7	(0.9)	36.7	(5.0)	21.1	83.9	62.6	95.9	(31.1)	(11.3)
Gross profit	297	304	306	294	311	329	319	323	326	343	334	338
Gross profit margin (%)	67.1	68.2	66.9	63.9	66.8	66.2	65.3	67.0	65.8	65.5	67.2	65.9
OP	64	65	63	36	69	79	97	88	90	98	97	98
%YoY	(7.8)	(10.3)	(14.0)	27.3	7.9	21.9	54.2	145.7	29.7	23.0	(0.1)	11.4
OPM (%)	14.5	14.6	13.7	7.7	14.9	16.0	19.8	18.2	18.1	18.7	19.5	19.0

Note: Non-consolidated basis, Account standards changed from 2013. Excluding overdue and pending accounts

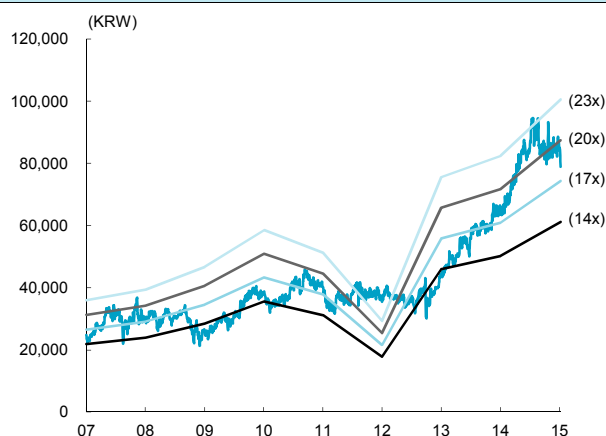
Source: Coway, Korea Investment securities & Investment

Table 3. Annual earnings breakdown

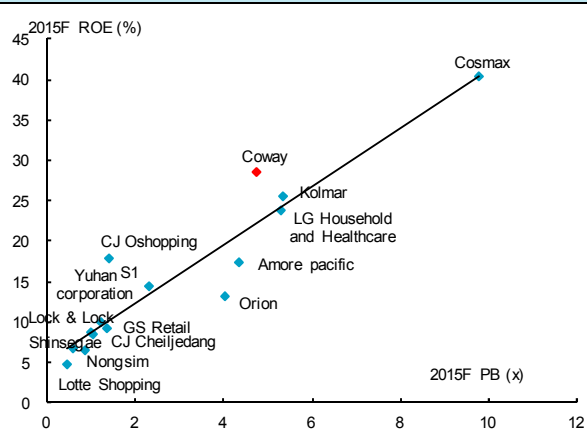
(W bn, KRW, '000 subs, %YoY, %)

	2011	2012	2013	2014F	2015F	2016F
Total no. of accounts	5,452	5,741	5,501	5,665	5,936	6,212
Increase in total account (YoY)	369	289	NM	164	271	276
% YoY	7.3	5.3	NM	3.0	4.8	4.7
No. of rental account ('000, end of Y)	4,450	4,607	4,435	4,613	4,846	5,084
Increase in rental account (YoY)	305	157	NM	178	234	238
No. of membership account ('000, end of Y)	1,002	1,133	1,066	1,052	1,089	1,128
Increase in membership accounts (YoY)	64	131	NM	(14)	37	38
No. of new rental sales ('000 units)	1,273	1,219	1,166	1,320	1,378	1,437
No. of new rental sales (%YoY)	9.0	(4.2)	(4.3)	13.2	4.4	4.3
Churn rate (%)	1.0	1.0	0.9	1.0	1.0	1.0
Total ARPU (Won)	21,587	21,084	22,122	23,404	24,089	24,744
Total ARPU (%YoY)	3.4	(2.3)	NM	5.8	2.9	2.7
Rental ARPU (Won)	23,362	23,093	24,334	25,583	26,253	26,958
Rental ARPU (%YoY)	4.0	(1.1)	NM	5.1	2.6	2.7
Membership ARPU (Won)	13,723	12,560	13,026	14,262	14,639	14,987
Membership (%YoY)	(0.1)	(8.5)	NM	9.5	2.6	2.4
Sales	1,710	1,807	1,934	2,027	2,194	2,385
%YoY	13.9	5.7	7.0	4.8	8.3	8.7
Rental-based	1,394	1,439	1,507	1,586	1,696	1,824
%YoY	9.6	3.2	4.7	5.2	6.9	7.6
Rental	1,235	1,278	1,335	1,405	1,508	1,625
%YoY	9.7	3.5	4.5	5.2	7.3	7.8
Membership	160	161	172	181	188	199
%YoY	9.1	0.8	6.8	5.5	3.7	6.0
Lump sum payment	102	145	149	125	136	151
%YoY	9.8	41.4	3.2	(16.3)	8.6	11.5
Cosmetics	68	67	76	81	91	101
%YoY	191.4	(1.5)	13.7	6.2	13.0	10.0
Export	98	110	145	172	203	234
%YoY	41.6	11.8	31.9	19.0	18.0	15.0
Others	47	46	56	62	69	75
%YoY	6.9	(1.5)	21.6	11.0	10.0	10.0
Gross profit	1,158	1,201	1,282	1,340	1,455	1,584
Gross profit margin (%)	67.7	66.5	66.3	66.1	66.3	66.4
OP	243	228	333	382	427	486
%YoY	(20.7)	(6.4)	46.3	14.6	11.7	13.9
OPM (%)	14.2	12.6	17.2	18.8	19.4	20.4

Note: Non-consolidated basis, Account standards changed from 2013. Excluding overdue and pending accounts
Source: Coway, Korea Investment securities & Investment

Figure 1. PE band

Source: Coway, Korea Investment securities & Investment

Figure 2. PB/ROE comparison

Source: Coway, Korea Investment securities & Investment

Company overview & Glossary

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.

- Rental: Customers gain the right to use a product by paying for registration and monthly rental fees
- ARPU: Average revenue per user

Balance sheet

FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
Current assets	779	691	707	785	867
Cash & cash equivalent	152	239	244	282	320
Accounts & other receivables	262	250	255	277	302
Inventory	72	66	67	73	79
Non-current assets	976	976	1,003	1,052	1,104
Investment assets	54	55	56	61	66
Tangible assets	630	638	657	676	695
Intangible assets	184	177	181	196	214
Total assets	1,755	1,668	1,710	1,837	1,971
Current liabilities	759	677	600	577	554
Accounts & other payables	236	224	229	249	271
ST debt & bond	330	182	132	82	32
Current portion of LT debt	110	146	146	146	146
Non-current liabilities	211	50	51	56	61
Debentures	118	0	0	0	0
LT debt & financial liabilities	36	0	0	0	0
Total liabilities	970	727	652	633	615
Controlling interest	785	941	1,058	1,204	1,357
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	986	1,131	1,284
Minority interest	0	0	0	0	0
Shareholders' equity	785	941	1,058	1,204	1,357

Cash flow

FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
C/F from operating	454	537	421	506	539
Net profit	94	245	266	323	361
Depreciation	175	191	183	183	183
Amortization	8	8	8	8	9
Net incr. in W/C	(24)	(41)	(36)	(10)	(15)
Others	201	134	0	2	1
C/F from investing	(319)	(76)	(217)	(239)	(243)
CAPEX	(314)	(268)	(202)	(202)	(202)
Decr. in fixed assets	4	10	0	0	0
Incr. in investment	(3)	180	(1)	(5)	(5)
Net incr. in intangible assets	(8)	(2)	(12)	(24)	(26)
Others	2	4	(2)	(8)	(10)
C/F from financing	(76)	(373)	(198)	(228)	(258)
Incr. in equity	12	5	0	0	0
Incr. in debts	20	(262)	(50)	(50)	(50)
Dividends	(78)	(78)	(202)	(148)	(178)
Others	(30)	(38)	54	(30)	(30)
C/F from others	(5)	(1)	0	0	0
Increase in cash	54	86	5	38	38

Note: Based on K-IFRS (consolidated)

Income statement

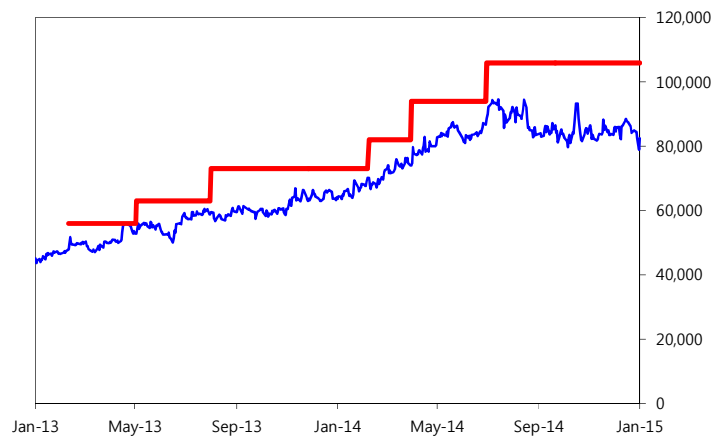
FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
Sales	1,993	2,118	2,166	2,353	2,560
COGS	678	721	743	795	858
Gross profit	1,315	1,397	1,423	1,558	1,703
SG&A expense	1,088	1,058	1,043	1,125	1,225
Operating profit	226	339	380	432	478
Financial income	2	4	(4)	3	4
Interest income	2	4	3	3	4
Financial expense	30	19	9	8	6
Interest expense	30	19	9	8	6
Other non-operating profit	(58)	(15)	(16)	(1)	0
Gains (Losses) in associates, subsidiaries and JV	5	18	0	0	0
Earnings before tax	146	327	351	427	476
Income taxes	52	82	85	103	115
Net profit	94	245	266	323	361
Net profit of controlling interest	94	245	266	323	361
Other comprehensive profit	5	(1)	0	0	0
Total comprehensive profit	99	244	266	323	361
Total comprehensive profit of controlling interest	99	244	266	323	361
EBITDA	410	537	571	624	671

Key financial data

FY-ending Dec.	2012A	2013A	2014F	2015F	2016F
per share data (KRW)					
EPS	1,267	3,283	3,578	4,360	4,861
BPS	11,354	13,535	15,059	16,945	18,926
DPS	0	2,710	2,000	2,400	2,800
Growth (%)					
Sales growth	9.2	6.3	2.3	8.6	8.8
OP growth	(3.7)	49.9	12.2	13.7	10.6
NP growth	(43.7)	160.6	8.5	21.6	11.5
EPS growth	(43.3)	159.1	9.0	21.9	11.5
EBITDA growth	3.9	31.1	6.3	9.2	7.5
Profitability (%)					
OP margin	11.3	16.0	17.6	18.4	18.7
NP margin	4.7	11.6	12.3	13.7	14.1
EBITDA margin	20.6	25.4	26.4	26.5	26.2
ROA	5.6	14.3	15.7	18.2	18.9
ROE	12.3	28.4	26.6	28.6	28.2
Dividend yield	-	4.1	2.4	3.0	3.5
Dividend payout ratio	0.0	82.4	55.8	55.0	57.6
Stability					
Net debt (W bn)	439	90	34	(55)	(143)
Debt/equity ratio (%)	75.7	35.6	26.9	19.5	13.6
Valuation (X)					
PE	34.4	20.2	23.5	18.1	16.2
PB	3.8	4.9	5.6	4.7	4.2
EV/EBITDA	9.0	9.5	11.3	9.5	8.7

Changes to recommendation and price target

Company (Code)	Date	Recommendation	Price target
Coway (021240)	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



■ **Guide to Korea Investment & Securities Co., Ltd. stock ratings based on absolute 12-month forward share price performance**

- 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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Korea Investment & Securities Co., Ltd. has issued ELW with underlying stocks of Coway and is the liquidity provider.

Prepared by: Eun-chaе Na

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