

# Coway (021240)

Above
In line
Below

12M rating **BUY (Maintain)**  
 12M TP **₩106,000** from ₩106,000  
 Up/downside **+27%**

## Stock Data

KOSPI (Feb 12, pt)	1,942
Stock price (Feb 12, KRW)	83,700
Market cap (USD mn)	5,812
Shares outstanding (mn)	77
52-Week high/low (KRW)	94,600/66,700
6M avg. daily turnover (USD mn)	14.2
Free float / Foreign ownership (%)	65.2/54.0
Major shareholders (%)	
Coway Holdings, Inc. and 9 others	31.0

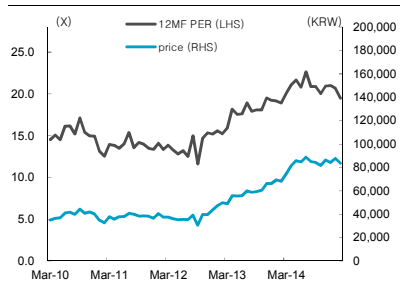
## Valuation

	2013A	2014F	2015F
PE (x)	20.2	25.0	19.3
PB (x)	4.9	5.7	5.0
ROE (%)	28.4	25.3	28.9
EV/EBITDA (x)	9.5	11.6	10.1
EPS (KRW)	3,283	3,374	4,345
BPS (KRW)	13,535	14,862	16,733

## Performance

	1M	6M	12M
Absolute (%)	3.7	(4.3)	23.6
Relative to KOSPI (%p)	2.6	0.5	23.3

## 12MF PE trend



Source: WISEfn consensus

## Sustainable gradual growth and favorable shareholder return policy

### What's new: NP misses forecast due to one-off factors

On a separate basis, 4Q14 OP grew 6.4% YoY to ₩93.2bn. Despite an increase in yearend promotions, separate OP was largely in line with our estimate (only 4.3% below) thanks to more subscribers and a higher ARPU. NP of ₩45.3bn fell far short of both our estimate and the consensus due to ₩30.6bn in losses on impaired investment securities in subsidiaries in China and Thailand and Green EnTech, a water treatment solution provider. Stripping off one-off costs, NP would have reached ₩75.9bn, in line with forecast. On a consolidated basis, OP fell 10% YoY to ₩81.7bn due to losses on subsidiary asset impairment. Excluding the costs, OP of ₩97.4bn would have met the consensus.

### Pros: Solid rental business, 2015 guidance and shareholder return policy in line with expectations

Rental sales (80% of total sales) grew 5.6% YoY while non-rental (lump-sum payment, cosmetics, exports and water treatment) sales fell 4.3% YoY. The number of total subscriber accounts reached 5.62mn, up 3.1% YoY, with ARPU up 2.4%. New rental sales were 332,000 accounts (+13.5% YoY) and churn was stable at 0.95%. An increase in sales of new water purifiers (+14% YoY) and mattresses (+89% YoY) was impressive. The uptick in ARPU was backed by: 1) higher rental fees, 2) better product mix and 3) net addition of rental accounts that generate higher ARPU than membership accounts. Coway's 2015 guidance has sales of ₩2.18tn (+8.3% YoY) and OP of ₩420bn (+11.3% YoY), which are in line with expectations. The company also projected new rental sales of 1.42mn units (+6.7% YoY) and net additions of 250,000 accounts. DPS is ₩2,000 for 2014, which translates into a 2.4% dividend yield (based on end-2014 price). Dividend propensity is improving, and dividend yield should reach 2.9% in 2015F based on the current price.

### Cons: Non-core businesses have yet to deliver visible results

Despite narrowing losses compared to 3Q14, the non-rental business performed poorly while overseas operations still face uncertainties. For cosmetics, there is hope for an earnings recovery in 2015 thanks to brisk sales via home shopping channels. For overseas operations, Coway is expected to focus on the subsidiary in Malaysia that continues to gain subscribers and the air purifier original design manufacturing (ODM) business in China.

(₩ bn, %, %p)

	4Q14P				Change		2015F	
	KIS est.	Actual	Diff.	Consensus	QoQ	YoY	KIS	Consensus
Sales	512	500	(2.5)	516	0.7	3.6	2,364	2,309
OP	98	93	(4.5)	97	(3.9)	6.4	431	431
OP margin	19.0	18.7	(0.4)	18.9	(0.9)	0.5	18.2	18.7
EBT	95	67	(29.6)	96	(24.1)	(6.8)	425	426
NP	74	45	(38.5)	72	(31.8)	(9.8)	322	321

Note: Non-consolidated 4Q14P earnings and consolidated 2015F outlook basis

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### Conclusion: Gradual growth driven by various businesses; Favorable shareholder return policies positive

Coway's investment points include: 1) excellent cash flows based on rental services, 2) modest growth backed by greater demand for domestic environmental home appliances (EHA) and rentals, and 3) shareholder-friendly policies. Although the mainstay rental business is facing concerns about heated competition, product competitiveness, stronger sales power and a wider array of new rental products are standouts. The business is also looking abroad to achieve additional growth. We forecast 2015F consolidated OP to grow 19% and EPS 29% (16% stripping out 2014 one-off costs). We maintain BUY and leave our TP unchanged at W106,000 (24x 12MF PE, historical peak).

**Table 1. 4Q14 consolidated earnings**

(W bn, %, %p)

	4Q14P		Growth	
	Actual	Consensus	QoQ	YoY
Sales	543	550	3.3	3.6
OP	82	96	(14.3)	(10.3)
OPM	15.1	17.5	(3.1)	(2.3)
EBT	72	100	(16.8)	(20.9)
Controlling int. NP	53	65	(16.5)	(21.4)

Source: Company data, Korea Investment &amp; Securities

**Table 2. Quarterly earnings breakdown**

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

	1Q12	2Q12	3Q12	4Q12	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14P
Total no. of accounts	5,484	5,600	5,670	5,741	5,372	5,396	5,408	5,446	5,469	5,539	5,571	5,617
Net increase ('000, QoQ)	32	116	70	71	NM	24	11	39	23	70	32	45
% YoY	5.4	5.0	4.8	5.3	NM	NM	NM	NM	1.8	2.7	3.0	3.1
No. of rental accounts ('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	4,601
Net increase (QoQ)	30	38	34	56	NM	43	12	48	20	32	51	63
No. of membership accounts ('000, end of Q)	1,004	1,082	1,118	1,133	1,040	1,022	1,021	1,012	1,014	1,052	1,034	1,016
Net increase (QoQ)	2	78	36	15	NM	(18)	(1)	(9)	2	38	(18)	(18)
No. of new rental sales ('000)	285	331	294	310	318	298	257	292	317	371	311	332
% YoY	(13.6)	(3.2)	2.0	(1.2)	11.7	(9.9)	(12.3)	(5.6)	(0.4)	24.3	20.8	13.5
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 (KRW)	21,311	21,321	21,223	21,250	NM	23,197	23,331	23,608	23,590	23,768	23,973	24,176
% YoY	2.9	1.8	0.7	0.1	NM	NM	NM	NM	NM	2.5	2.8	2.4
Rental ARPU (KRW)	23,164	23,319	23,325	23,357	NM	25,418	25,487	25,631	25,676	25,850	26,051	26,178
Rental ARPU (% YoY)	4.3	3.2	2.1	1.6	NM	NM	NM	NM	NM	1.7	2.2	2.1
Membership ARPU (KRW)	12,948	12,594	12,446	12,467	NM	12,753	13,159	13,498	14,441	14,757	14,905	15,253
Membership ARPU (% YoY)	(5.4)	(6.4)	(6.8)	(6.6)	NM	NM	NM	NM	NM	15.7	13.3	13.0
Sales	442	446	458	460	465	497	489	482	495	523	496	499
%YoY	10.6	2.4	6.5	3.6	5.2	11.3	6.8	4.9	6.4	5.3	1.4	3.5
Rental-based	356	360	364	370	370	375	378	384	386	392	400	406
% YoY	8.9	6.1	5.1	4.5	3.9	4.0	3.8	4.0	4.3	4.7	5.7	5.6
Rental	317	321	323	327	327	332	335	339	342	347	353	359
% YoY	10.1	7.1	5.7	4.6	3.2	3.5	3.6	3.6	4.6	4.5	5.3	5.8
Membership	39	39	41	42	43	43	43	44	44	46	47	47
% YoY	(0.4)	(1.3)	0.3	3.6	9.8	8.5	5.1	3.2	2.6	7.0	8.6	7.5
Lump-sum payment	33	41	39	32	37	48	35	29	28	37	32	27
% YoY	2.7	4.5	(4.6)	1.6	11.9	18.0	(9.4)	(9.2)	(24.6)	(21.7)	(10.4)	(9.1)
Cosmetics	17	16	17	17	18	22	17	20	21	22	17	20
% YoY	(3.3)	(8.8)	(1.8)	9.7	6.6	35.3	(4.2)	17.9	17.1	0.7	3.6	1.0
Exports	30	21	20	31	32	45	38	31	45	56	33	33
% YoY	63.9	(8.0)	(18.8)	(5.6)	5.0	111.1	90.7	0.4	43.5	25.2	(13.0)	9.3
Others	7	8	17	11	9	8	21	20	15	15	15	14
% YoY	28.9	(50.6)	4711.7	(0.9)	36.7	(5.0)	21.1	83.9	62.6	95.9	(31.1)	(31.4)
GP	297	304	306	294	311	329	319	323	326	343	334	338
GPM	67.1	68.2	66.9	63.9	66.8	66.2	65.3	67.0	65.8	65.5	67.2	67.8
OP	64	65	63	36	69	79	97	88	90	98	97	93
% YoY	(7.8)	(10.3)	(14.0)	27.3	7.9	21.9	54.2	145.7	29.7	23.0	(0.1)	6.4
OPM %	14.5	14.6	13.7	7.7	14.9	16.0	19.8	18.2	18.1	18.7	19.5	18.7

Note: On a separate basis; Subscriber account standards changed effective from 2013 to exclude overdue, pending and free accounts  
Source: Company data, Korea Investment & Securities

**Table 3. Annual earnings breakdown**

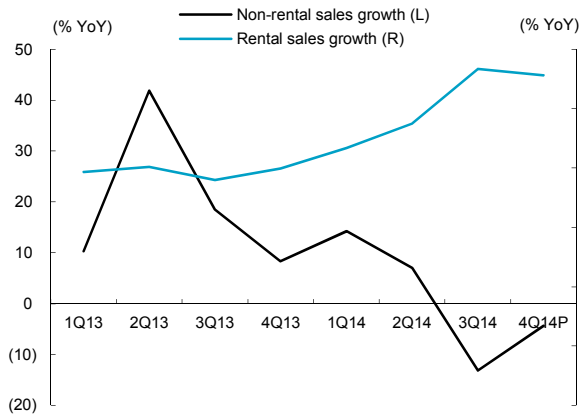
(W bn, KRW, '000 accounts, %YoY, %)

	2011	2012	2013	2014P	2015F	2016F
Total no. of accounts	5,452	5,741	5,446	5,617	5,870	6,157
Net increase (YoY)	369	289	NM	170	253	287
% YoY	7.3	5.3	NM	3.1	4.5	4.9
No. of rental accounts ('000, end of Y)	4,450	4,607	4,435	4,601	4,859	5,109
Net increase (YoY)	305	157	NM	166	259	250
No. of membership accounts ('000, end of Y)	1,002	1,133	1,012	1,016	1,011	1,049
Net increase (YoY)	64	131	NM	4	(5)	38
No. of new rental sales ('000 units)	1,273	1,219	1,166	1,330	1,399	1,460
No. of new rental sales (% YoY)	9.0	(4.2)	(4.3)	14.1	5.2	4.3
Churn rate (%)	1.0	1.0	0.9	1.0	1.0	1.0
Total ARPU (KRW)	21,587	21,084	NM	23,819	24,274	24,916
Total ARPU (% YoY)	3.4	(2.3)	NM	NM	1.9	2.6
Rental ARPU (KRW)	23,362	23,093	NM	25,560	26,292	26,972
Rental ARPU (% YoY)	4.0	(1.1)	NM	NM	2.9	2.6
Membership ARPU (KRW)	13,723	12,560	NM	15,073	14,975	15,141
Membership (% YoY)	(0.1)	(8.5)	NM	NM	(0.7)	1.1
Sales	1,710	1,807	1,934	2,014	2,180	2,368
% YoY	13.9	5.7	7.0	4.1	8.3	8.6
Rental-based	1,394	1,439	1,507	1,584	1,693	1,819
% YoY	9.6	3.2	4.7	5.1	6.9	7.5
Rental	1,235	1,278	1,335	1,401	1,511	1,632
% YoY	9.7	3.5	4.5	4.9	7.9	8.0
Membership	160	161	172	183	182	187
% YoY	9.1	0.8	6.8	6.7	(0.7)	2.7
Lump-sum payment	102	145	149	124	136	151
% YoY	9.8	41.4	3.2	(17.3)	9.9	11.5
Cosmetics	68	67	76	80	90	100
% YoY	191.4	(1.5)	13.7	5.3	13.0	10.0
Exports	98	110	145	167	198	227
% YoY	41.6	11.8	31.9	15.8	18.0	15.0
Others	47	46	56	58	64	71
% YoY	6.9	(1.5)	21.6	3.9	10.0	10.0
GP	1,158	1,201	1,282	1,340	1,454	1,580
GPM (%)	67.7	66.5	66.3	66.6	66.7	66.7
OP	243	228	333	377	424	487
% YoY	(20.7)	(6.4)	46.3	13.3	12.3	14.9
OPM (%)	14.2	12.6	17.2	18.7	19.4	20.6

Note: On a separate basis; K-IFRS effective from 2011; Subscriber account standards changed effective from 2013 to exclude overdue, pending and free accounts

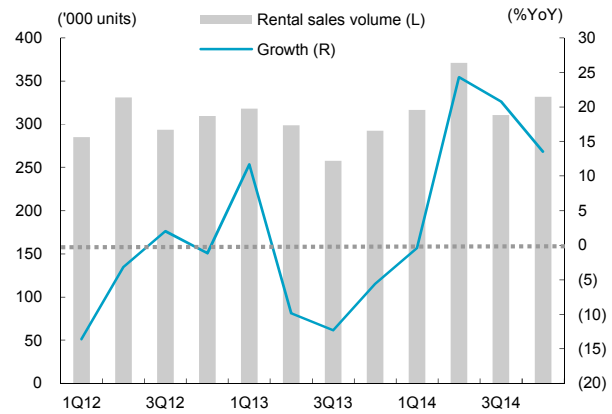
Source: Company data, Korea Investment securities & Investment

**Figure 1. Rental sales have been growing after passing a bottoming in 3Q13**



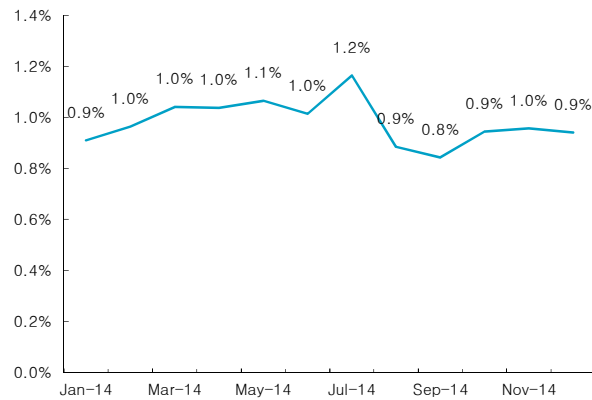
Source: Company data, Korea Investment securities & Investment

**Figure 2. New sales remain robust**



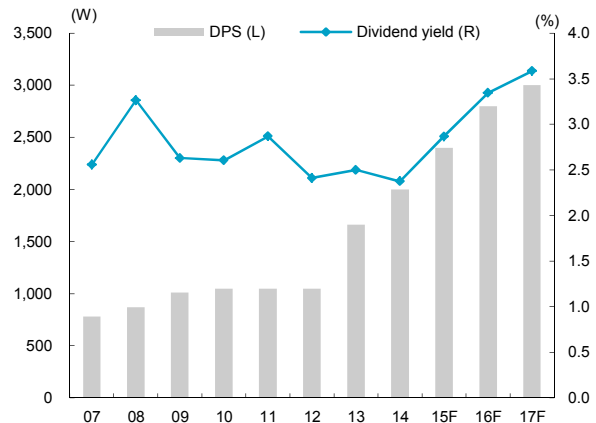
Source: Company data, Korea Investment securities & Investment

**Figure 3. Stable churn rate**



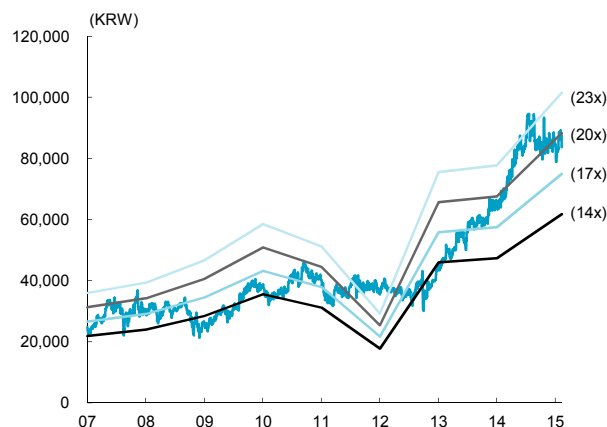
Source: Company data, Korea Investment securities & Investment

**Figure 4. DPS and dividend yield outlook**



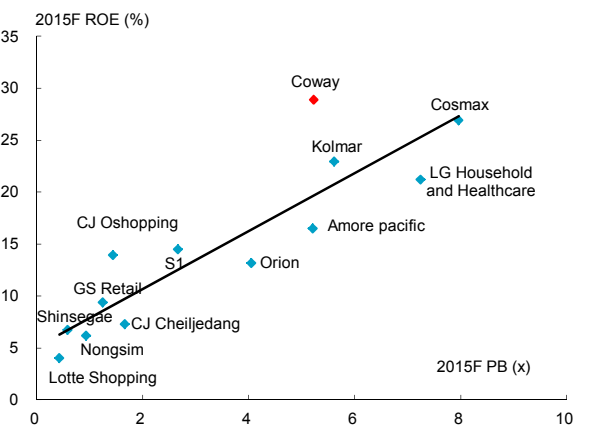
Source: Company data, Korea Investment securities & Investment

**Figure 5. PE band**



Source: Company data, Korea Investment securities & Investment

**Figure 6. PB/ROE comparison with major consumer goods firms**



Source: Company data, 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	705	789	870
Cash & cash equivalent	152	239	243	284	321
Accounts & other receivables	262	250	254	278	303
Inventory	72	66	67	73	80
Non-current assets	976	976	1,002	1,054	1,105
Investment assets	54	55	56	61	67
Tangible assets	630	638	657	676	695
Intangible assets	184	177	180	197	214
Total assets	1,755	1,668	1,707	1,843	1,975
Current liabilities	759	677	613	599	569
Accounts & other payables	236	224	229	250	272
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	664	655	630
Controlling interest	785	941	1,043	1,187	1,345
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	970	1,115	1,273
Minority interest	0	0	0	0	0
Shareholders' equity	785	941	1,043	1,187	1,345

**Cash flow**

FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
C/F from operating	454	537	420	510	538
Net profit	94	245	251	322	366
Depreciation	175	191	183	183	183
Amortization	8	8	8	8	9
Net incr. in W/C	(24)	(41)	(22)	(4)	(21)
Others	201	134	0	1	1
C/F from investing	(319)	(76)	(216)	(242)	(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)	(11)	(25)	(26)
Others	2	4	(2)	(10)	(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	40	37

Note: Based on K-IFRS (consolidated)

**Income statement**

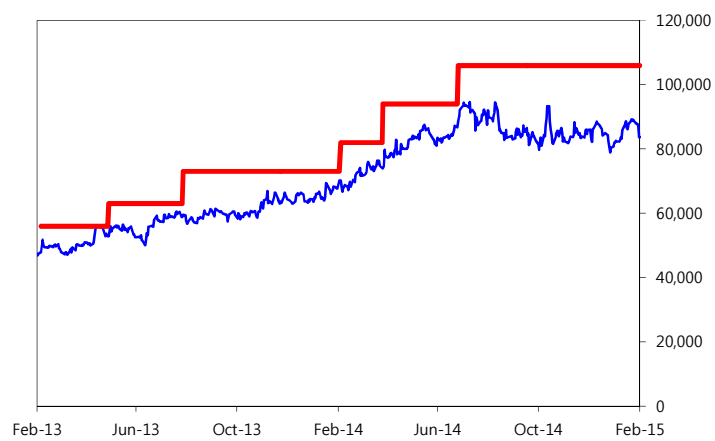
FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
Sales	1,993	2,118	2,160	2,364	2,569
COGS	678	721	727	799	855
Gross profit	1,315	1,397	1,434	1,565	1,713
SG&A expense	1,088	1,058	1,069	1,134	1,229
Operating profit	226	339	364	431	485
Financial income	2	4	(4)	3	4
Interest income	2	4	3	3	4
Financial 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	332	425	482
Income taxes	52	82	82	103	117
Net profit	94	245	251	322	366
Net profit of controlling interest	94	245	251	322	366
Other comprehensive profit	5	(1)	0	0	0
Total comprehensive profit	99	244	251	322	366
Total comprehensive profit of controlling interest	99	244	251	322	366
EBITDA	410	537	553	623	677

**Key financial data**

FY-ending Dec.	2012A	2013A	2014F	2015F	2016F
per share data (KRW)					
EPS	1,267	3,283	3,374	4,345	4,929
BPS	11,354	13,535	14,862	16,733	18,780
DPS	0	2,710	2,000	2,400	2,800
Growth (%)					
Sales growth	9.2	6.3	2.0	9.4	8.7
OP growth	(3.7)	49.9	6.8	19.0	12.5
NP growth	(43.7)	160.6	2.3	28.5	13.5
EPS growth	(43.3)	159.1	2.8	28.8	13.5
EBITDA growth	3.9	31.1	2.9	12.6	8.8
Profitability (%)					
OP margin	11.3	16.0	16.8	18.2	18.9
NP margin	4.7	11.6	11.6	13.6	14.2
EBITDA margin	20.6	25.4	25.6	26.3	26.4
ROA	5.6	14.3	14.9	18.2	19.2
ROE	12.3	28.4	25.3	28.9	28.9
Dividend yield	-	4.1	2.4	2.9	3.3
Dividend payout ratio	0.0	82.4	59.2	55.2	56.8
Stability					
Net debt (W bn)	439	90	35	(56)	(144)
Debt/equity ratio (%)	75.7	35.6	27.3	19.8	13.7
Valuation (X)					
PE	34.4	20.2	25.0	19.3	17.0
PB	3.8	4.9	5.7	5.0	4.5
EV/EBITDA	9.0	9.5	11.6	10.1	9.2

**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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