

# Coway (021240.KS)

Company Comment | Feb 13, 2015

## Earnings at core business domain remain solid

While Coway's 2014 net profit missed consensus (on the reflection of impairment losses at its overseas subsidiaries), we view its core business indicators as remaining sound. As such, Coway should be well positioned to maintain a high dividend payout ratio—given its well-controlled accounting practices and stable cash flow, we anticipate a 2015 payout ratio of 60% (dividend yield of 3%).

### 4Q14 results: Impairment losses booked for overseas subsidiaries

- On an IFRS non-consolidated basis, Coway announced 4Q14 sales of W499.5bn (up 3.6% y-y) and operating profit of W93.2bn (up 6.4% y-y), with both figures satisfying consensus. However, net profit for the quarter came in at W45.4bn (down 9.8% y-y), falling well wide of the market's projection on the booking of W30.6bn worth of impairment losses (including for its China cosmetics arm (W22.8bn) and for its Thailand subsidiary (W4.7bn)). However, with impairment losses at Coway's China cosmetics business and its Thailand subsidiary having now been fully reflected, any further overseas-related impairment losses should be limited.
- Meanwhile, Coway's domestic rental sales increased 5.8% y-y, while the firm's cancellation rate for rental contracts was controlled at less than 1%. In addition, Coway's loss rate on rental asset disposals was stably controlled at about 2%, evidencing the earnings solidity of its core business model.

### Rental business to display robust sales growth and margin expansion in 2015

- Coway should see 2015 non-consolidated sales of W2,190.3bn (up 8.8% y-y) and operating profit of W424.8bn (up 12.5% y-y), supported by: 1) robust sales growth on sales channel expansion and a strategic focus on premium products; and 2) likely higher margins on cost control efforts and ARPU hikes. Annual guidance targets sales of W2,180.0bn (up 8.3% y-y) and operating profit of W420.0bn (up 11.3% y-y).

### Maintain Buy and target price of W100,000

- We maintain Buy and a target price of W100,000. With its shares trading at a 2015 P/E of 20x, the firm's valuations appear somewhat demanding; however, we believe that Coway's shares still warrant a valuation premium, pointing out its unique business model under which the sustainability its subscriber-based rental domain should provide long-term earnings stability and ample cash flow. Backed by this business model, Coway's earnings are relatively free from the impact of cyclical factors and other external variables. Also, we expect the firm's dividend payout to enhance going forward—with its dividend payout ratio having averaged around 50% in the past, the figure should rise to 60% in 2015 (dividend yield of 3%) and to 70% in 2016.

## Buy (maintain)

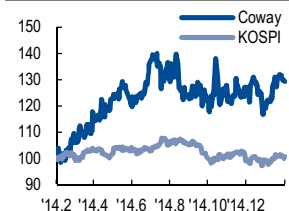
TP W100,000 (maintain)

CP ('15/02/110) W79,400

Sector Other consumer goods

Kospi	1,941.63
Kosdaq	602.24
Market cap (common)	US\$5,828.7mn
Outstanding shares (common)	77.1mn
52W high ('14/07/22)	W94,600
low ('14/02/18)	W66,7000
Average trading value (60D)	US\$18.1mn
Dividend yield (2014)	2.4%
Foreign ownership	54.0%

### Price trend



### 4Q14 results

(Units: Wbn, %)

	4Q13	1Q14	2Q14	3Q14	4Q14P					1Q15E
					Actual	y-y	q-q	Estimates	Consensus	
Sales	482	495	523	496	500	3.6	0.7	553	550	536
Operating profit	88	90	98	97	93	6.4	2.5	79	96	103
Operating margin	18.2	18.1	18.7	19.5	18.7			14.2	17.5	19.2
Pre-tax profit	72	88	87	88	67	-6.2	-23.6	115	100	101
Net profit	50	66	65	66	45	-9.8	-32.2	85	65	72

Note: IFRS non-consolidated basis. Source: Coway, FnGuide, NH I&S Research Center estimates



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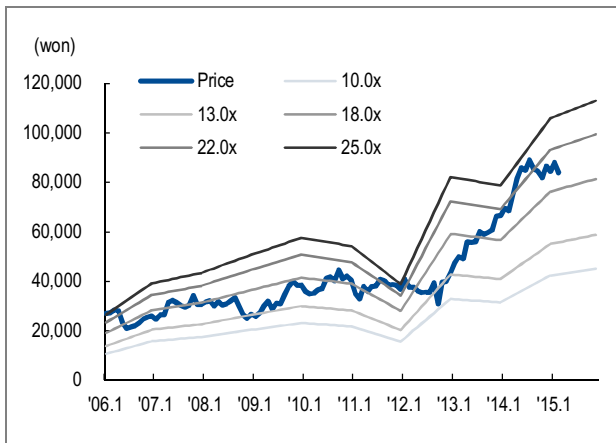
**Earnings forecasts (IFRS non-consolidated)**

(Units: Wbn, won, x, %)

		2013	2014P	2015E	2016F
Sales	- Revised	1,933.7	2,013.6	2,190.3	2,280.1
	- Previous		2,108.4	2,345.6	2,583.8
	- Change		-4.5	-6.6	-11.8
Operating profit	- Revised	333.2	377.5	424.8	458.8
	- Previous		363.7	409.0	457.8
	- Change		3.8	3.9	0.2
Operating margin	- Revised	17.2	18.7	19.4	20.1
EBITDA		521.9	540.7	606.4	648.2
Net profit (excl minority interests)		253.2	242.4	326.3	350.1
EPS	- Revised	3,283	3,142	4,230	4,539
	- Previous		3,732	4,145	4,605
	- Change		-15.8	2.1	-1.4
P/E		20.2	26.8	19.8	18.4
P/B		5.3	6.1	5.4	4.9
EV/EBITDA		10.0	12.2	10.7	9.9
ROE		28.6	23.9	28.9	27.9

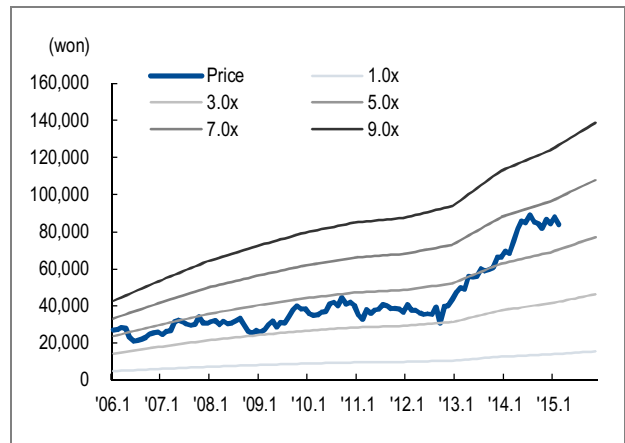
Note: Operating profit = sales – (COGS + SG&A expenses)  
 Source: NH I&S Research Center estimates

**Forward P/E band**



Source: Dataguide Pro

**Trailing P/B band**

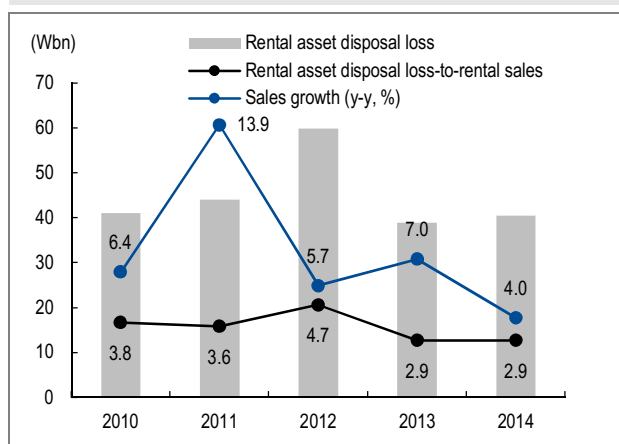


Source: Dataguide Pro

Earnings forecasts									(Units: Wbn, '000 units, W1,000, %)		
	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14P	2013	2014P	2015E
<b>Sales</b>	<b>465</b>	<b>497</b>	<b>489</b>	<b>482</b>	<b>495</b>	<b>523</b>	<b>496</b>	<b>500</b>	<b>1,934</b>	<b>2,014</b>	<b>2,190</b>
Rentals	327	332	335	339	342	347	353	359	1,333	1,401	1,564
Memberships	43	43	43	44	44	46	47	47	172	183	195
Lump-sum sales	37	48	35	29	26	37	32	27	149	122	124
Exports	31	45	38	31	45	56	33	33	145	167	176
Cosmetics	18	22	17	20	21	22	17	20	76	80	83
Others	9	8	21	20	15	15	15	14	58	58	49
<b>Sales growth</b>	<b>5.2</b>	<b>11.3</b>	<b>6.8</b>	<b>4.9</b>	<b>6.4</b>	<b>5.3</b>	<b>1.4</b>	<b>3.6</b>	<b>7.0</b>	<b>4.1</b>	<b>8.8</b>
Rentals	3.5	4.1	3.6	3.6	4.6	4.5	5.3	5.8	3.7	5.0	11.7
Memberships	10.4	9.1	5.1	3.2	2.6	7.0	8.6	7.4	6.8	6.4	6.6
Lump-sum sales	11.9	18.1	-9.3	-9.3	-29.6	-21.8	-10.4	-9.1	3.2	-18.5	1.5
Exports	5.0	111.4	35.6	0.2	43.6	25.1	-13.0	9.3	32.0	15.8	5.0
Cosmetics	6.3	35.5	-4.2	18.1	17.4	0.5	3.6	1.1	13.6	5.3	2.6
Others	16.1	-25.8	125.6	85.0	63.4	98.4	-31.0	-31.1	50.7	1.1	-15.5
<b>Gross profit</b>	<b>311</b>	<b>329</b>	<b>319</b>	<b>323</b>	<b>326</b>	<b>343</b>	<b>334</b>	<b>338</b>	<b>1,282</b>	<b>1,340</b>	<b>1,461</b>
Gross margin	66.8	66.2	65.3	67.0	65.8	65.5	67.2	67.7	66.3	66.6	66.7
<b>Operating profit</b>	<b>69</b>	<b>79</b>	<b>97</b>	<b>88</b>	<b>90</b>	<b>98</b>	<b>97</b>	<b>93</b>	<b>333</b>	<b>377</b>	<b>425</b>
Growth	7.9	21.9	54.2	145.7	29.7	23.0	-0.1	6.4	46.3	13.3	12.5
Operating margin	14.9	16.0	19.8	18.2	18.1	18.7	19.5	18.7	17.2	18.7	19.4

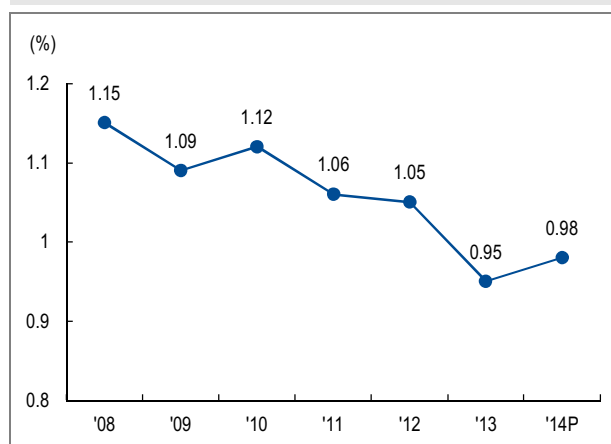
Source: Coway, NH I&S Research Center estimates

### Sales growth and rental asset disposal loss



Source: Coway, NH I&S Research Center

### Rental contract cancellation rate



Source: Coway, NH I&S Research Center

## STATEMENT OF COMPREHENSIVE INCOME

(Wbn)	2013/12A	2014/12P	2015/12E	2016/12F
<b>Sales</b>	1,934	2,014	2,190	2,280
Growth (%)	7.0	4.1	8.8	4.1
<b>COGS</b>	652	673	729	756
<b>Gross Profit</b>	1,282	1,340	1,461	1,524
Gross margin (%)	66.3	66.6	66.7	66.8
SG&A	949	963	1,036	1,065
<b>Operating Income</b>	333	377	424.8	459
Growth (%)	46.3	13.3	12.5	8.0
Operating margin (%)	17.2	18.7	19.4	20.1
<b>EBITDA</b>	522	541	606	648
<b>Non-Operating Profit</b>	17	-48	19	17
Financial Income(Costs)	-14	12	11	11
Other Non-Operating Profit	-9	0	0	0
Gains(Losses) in Associates, Subsidiaries and JVs	40	-60	8	6
<b>Pre-tax Profit from Cont. Op.</b>	351	330	444	476
<b>Income Taxes</b>	97	87	118	126
Profit from Continuing Op.	253	242	326	350
<b>Net Profit</b>	253	242	326	350
Growth (%)	111.4	-4.3	34.6	7.3
Net margin (%)	13.1	12.0	14.9	15.4
Net Profit of Parent	253	242	326	350
Net Profit to Non-Controlling	0	0	0	0
Other Comprehensive Income	-1	0	0	0
Total Comprehensive Income	253	242	326	350

## VALUATION INDEX

	2013/12A	2014/12P	2015/12E	2016/12F
Price/Earnings (x)	20.2	26.8	19.8	18.4
P/E (High, x)	20.6	30.2	21.2	19.8
P/E (Low, x)	13.1	20.0	17.7	16.5
Price/ Book Value (x)	5.3	6.1	5.4	4.9
P/B (High, x)	5.4	6.9	5.8	5.3
P/B (Low, x)	3.4	4.6	4.8	4.4
Price/ Gross Cash Flow (x)	8.5	11.4	10.2	9.6
Price/ Sales (x)	2.6	3.2	2.9	2.8
P/E / EPS growth (x)	1.8	1.7	2.4	2.3
P/E / EBITPS growth (x)	1.8	2.8	2.3	2.2
P/E / EBITDAPS growth (x)	2.7	3.0	2.5	2.4
EV/ EBITDA (x)	10.0	12.2	10.7	9.9
EV/ EBIT (x)	15.7	17.5	15.3	14.0
Enterprise Value (Wbn)	5,238	6,587	6,483	6,410
EPS CAGR (3-Yr) (%)	11.4	15.9	8.2	7.9
EBITPS CAGR (3-Yr) (%)	11.3	9.7	8.7	8.2
EBITDAPS CAGR (3-Yr) (%)	7.5	9.0	8.1	7.8
EBITPS (won)	4,320	4,895	5,508	5,949
EBITDAPS (won)	6,767	7,011	7,863	8,405
Fully diluted EPS (won)	3,283	3,142	4,230	4,539
BVPS (won)	12,543	13,761	15,551	17,034
CFPS (won)	7,789	7,400	8,200	8,703
Sales PS (won)	25,073	26,109	28,400	29,564
DPS (won)	1,660	2,000	2,538	3,178

## CASH FLOW STATEMENT

(Wbn)	2013/12A	2014/12P	2015/12E	2016/12F
<b>Operating Cash Flow</b>	518	443	473	487
Net Profit	253	242	326	350
Depreciation & Amortization	189	163	182	189
+ Loss(Gains) from Subs	-40	70	0	0
+ FC translation loss(profit)	0	0	0	0
+ Losses(Gains) on Disposal of Assets	39	0	0	0
Gross Cash Flow	601	571	632	671
- Incr. (Decr.) in WC	-42	-41	-42	-58
<b>Investing Cash Flow</b>	-58	-292	-246	-212
+ Decr. In Tangible Assets	6	0	0	0
- Incr. In Tangible Assets (capex)	-246	-199	-248	-216
+ Disp.(Acq.) of Inv. Assets	4	-74	-4	-4
Free Cash Flow	272	244	224	270
Net Cash Flow	459	151	227	275
<b>Financing Cash Flow</b>	-377	-116	-148	-188
Equity Financing	0	0	0	0
Debt Financing	-377	-116	-148	-188
Incr.(Decr.) in Cash	82	35	79	87
Ending Cash and Cash Equivalents	201	236	315	402
Net Debt (Cash)	116	94	28	-45

## RIM &amp; EVA

	2013/12A	2014/12P	2015/12E	2016/12F
<b>RIM</b>				
Spread (FROE-COE) (%)	20.8	15.1	20.6	19.6
Residual Income	184.2	165.3	240.4	254.6
12M RIM Target Price (won)	90,859			
<b>EVA</b>				
Invested Capital	952.2	1,030.9	1,102.7	1,143.8
NOPAT	253.7	278.6	313.4	338.5
ROIC (%)	24.5	28.1	29.4	30.1
ROIC - WACC (%)	18.7	21.6	23.2	23.9
EVA	177.9	223.2	255.5	273.4
<b>DCF</b>				
EBIT	333.2	377.5	424.8	458.8
+ Depreciation/Amortization	189	163	182	189
- Capex	-245.7	-199.1	-248.2	-216.4
- Incr. (Decr.) in Working Capital	164.4	-18.6	-5.2	-14.1
Free Cash Flow for Firm	19.2	260.2	250.8	324.3
<b>WACC</b>				
Cost of Debt (Tax Adj.)	2.9	2.9	2.9	2.9
Cost of Equity (COE)	7.8	8.8	8.3	8.3
WACC (%)	5.8	6.4	6.2	6.2

## STATEMENT OF FINANCIAL POSITION

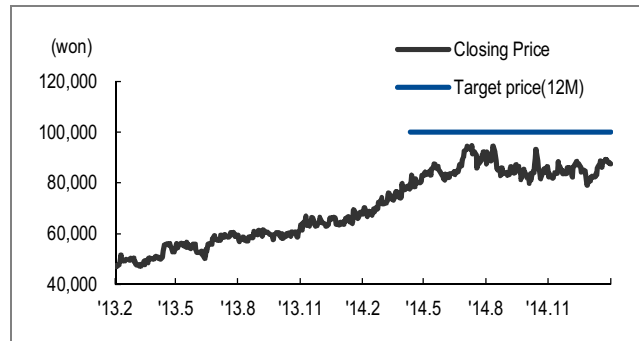
(Wbn)	2013/12A	2014/12P	2015/12E	2016/12F
Cash and Cash Equivalents	201	236	315	402
Accounts Receivables	266	283	308	321
<b>Total Current Assets</b>	642	712	833	950
Tangible Assets	597	636	706	736
Investment Assets	154	158	162	166
<b>Non-Current Assets</b>	999	1,062	1,133	1,164
<b>Assets</b>	1,641	1,774	1,966	2,114
Short-Term Debt	325	338	351	365
Account Payables	30	31	35	36
<b>Current Liabilities</b>	637	665	717	748
Long-Term Debt	0	8	8	8
Long-Term Allowance	7	8	8	9
<b>Non-Current Liabilities</b>	37	47	50	53
<b>Liabilities</b>	674	713	767	801
Capital Stock	41	41	41	41
Capital Surplus	131	131	131	131
Retained Earnings	890	984	1,122	1,237
Non-Controlling Interests Equity	0	0	0	0
<b>Shareholders' Equity</b>	967	1,061	1,199	1,314

## PROFITABILITY &amp; STABILITY

	2013/12A	2014/12P	2015/12E	2016/12F
ROE (%)	28.6	23.9	28.9	27.9
ROA (%)	15.1	14.2	17.4	17.2
ROIC (%)	24.5	28.1	29.4	30.1
EBITDA/equity (%)	54.0	50.9	50.6	49.3
EBITDA/assets (%)	31.8	30.5	30.8	30.7
Dividend Yield (%)	2.5	2.4	3.0	3.8
Payout Ratio (%)	79.8	61.2	57.7	67.3
Total Cash Dividend (Wbn)	202	148	188	236
Cash DPS (won)	1,660	2,000	2,538	3,178
Net debt(cash)/ equity (%)	12.0	8.8	2.3	-3.4
Debt/ equity (%)	69.6	67.1	63.9	60.9
Net interest exp/ sales (%)	0.9	0.6	0.6	0.6
Interest coverage (x)	19.0	29.1	31.5	32.8
Current Ratio (%)	100.9	107.0	116.3	127.1
Quick Ratio (%)	94.5	99.8	108.4	118.7
Total shares (mn)	77	77	77	77
Par value (won)	500	500	500	500
Share price (won)	66,400	84,200	83,700	83,700
Market Cap (Wbn)	5,121	6,494	6,455	6,455

## Rating and target price update

Company	Code	Date	Rating	Target price
Coway	021240.KS	2014.04.22	Buy	W100,000(12M)



## NH Investment &amp; Securities stock ratings

In order to deliver clearer investment recommendations to investors, NH Investment & Securities Research Center (as of Jan 20, 2015) will henceforth employ a three-tier rating system (Buy/Hold/Sell) rather than the previous four-tier system (Strong Buy/Buy/Hold/Reduce).

- Based on a stock's forecasted absolute return over a period of 12 months from the date of publication.
  - Buy : greater than +15%
  - Hold : -15% and +15%
  - Sell : less than -15%

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- NH I&S does not have a stake greater than or equal to 1% in Coway as of the preparation date.
- NH I&S has not provided this material to any institutional investor or other third party in advance.
- The analyst and his/her spouse do not own any securities of Coway as of the preparation date.
- This report correctly reflects the analyst's opinion and was written without any external influence or intervention.

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