

Company Update



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■ AT A GLANCE

SELL HOLD **BUY**

Target price	KRW120,000 (25.3%)
Current price	KRW95,800
Bloomberg code	021240 KS
Market cap	KRW7.4t/USD6.7b
Shares (float)	77,124,796 (65.3%)
52-week high/low	KRW103,500/KRW77,500
Average daily trading value (60-day)	KRW 16.54b/ USD 15.08m
One-year performance	1M 6M 12M
Coway (%)	+12.2 +16.1 +23.5
Vs Kospi (%pts)	+5.4 +6.1 +17.0

■ KEY CHANGES

(KRW)	New	Old	Diff (%)
Recommendation	BUY	BUY	
Target price	120,000	113,000	6.2
2015E EPS	3,864	3,866	(0.1)
2016E EPS	4,229	4,173	1.3
2017E EPS	4,785	4,707	1.7

■ SAMSUNG vs THE STREET

No of I/B/E/S estimates	9
Target price vs I/B/E/S mean	8.1%
Estimates up/down (4 weeks)	1/0
1-year-fwd EPS vs I/B/E/S mean	1.2%
Estimates up/down (4 weeks)	0/1
I/B/E/S recommendation	Buy

Coway (021240)

Competitiveness key, not competition

WHAT'S THE STORY?

Event: We now believe 1Q sales and operating profit at Coway grew 6% and 10% y-y, respectively, to KRW568.4b and KRW99.6b—the former edging consensus, but the latter coming in 4% shy.

Impact: Although a rise in marketing expenses likely ate into profitability—hence the disappointing operating profit—we support the firm's strategy of strengthening entry barriers by boosting market share. Still, with Hyundai Home Shopping recently deciding to enter the rental market, following in the footsteps of Cuckoo Electronics, concerns over stiffening competition may dampen investment sentiment in the short term.

Action: We maintain our earnings estimates, which already anticipates stiffer competition, but our DCF-based target price rises from KRW113,000 to KRW120,000 (equivalent to 31x 2015 P/E), as a fall in interest rates has boosted enterprise value. We reiterate BUY on the stock for three reasons. First, new market entrants are not all bad, as they imply a positive outlook for the rental market. Second, we do not believe the new players will undermine Coway's earnings in the near term, as the firm's dominance over the past 20 years owes more to its maintenance service than to the rental items themselves. Third, although Coway's longer-term earnings momentum seems uninspiring, we view the stock as a long-term play, with its shares rising proportionately with its mounting cash. We advise investors to use short-term deterioration in investment sentiment as a buying opportunity.

THE QUICK VIEW

1Q preview—rising marketing costs vs market-share gains: We believe 1Q sales at Coway climbed 6% y-y to KRW568.4b, edging consensus by 1%, which indicates the firm is well on track to meet its aggressive 2015 rental sales growth target of 7%. To achieve this, it has turned from cost-cutting over 2013-2014 to aggressive marketing. Thus we estimate that operating profit increased just 10% y-y to KRW99.6b in 1Q, 4% below consensus. We are not unduly concerned over profitability erosion (stemming from higher marketing costs), as we have confidence in the Coway's strategy of strengthening entry barriers by boosting market share. The firm's monthly average cancellation rate is below 1%, while its customer retention rate (at the end of five-year contracts) is above 75%.

HHS market entry negative in short term, but implies growth potential: Hyundai Home Shopping on Apr 14 established subsidiary Hyundai Rental Care with the goal of entering the rental and maintenance business in June. Hyundai Department Store Group has run a water purifier business (under the brand Weguard) since 2008 via Hyundai H&S, and established a maintenance department in 2014. HHS's market entry may give some cause for alarm considering that Cuckoo (which entered the rental/maintenance market in 2009) saw KRW120b in sales last year, and HDS Group's sales and service networks are likely superior to those of Cuckoo. That said, we do not see any compelling reason to change our outlook that the firm will continue to grow on par with the market over the long term, given that: 1) a growing market naturally draws new market players; 2) the firm has protected its majority market share over the past 20 years—despite constant competition— thanks more to its maintenance service than to the rental items themselves; and 3) Coway's number of sales reps grew a massive 14% (from 162,000 to 185,000) in 2014, despite aggressive increases in numbers of sales reps at Cuckoo and HDS Group—which exhibits the firm's brand power.

■ SUMMARY FINANCIAL DATA

	2014	2015E	2016E	2017E
Revenue (KRWb)	2,160	2,308	2,474	2,626
Net profit (adj) (KRWb)	250	299	328	370
EPS (adj) (KRW)	3,223	3,864	4,229	4,785
EPS (adj) growth (%)	0.0	19.9	9.4	13.1
EBITDA margin (%)	26.8	28.0	28.2	29.3
ROE (%)	25.2	26.6	25.5	25.7
P/E (adj) (x)	29.7	24.8	22.7	20.0
P/B (x)	7.4	6.3	5.6	5.0
EV/EBITDA (x)	12.6	11.3	10.4	9.3
Dividend yield (%)	1.7	2.6	2.8	3.2

Source: Company data, Samsung Securities estimates

Coway

Results and forecasts, by segment

	1Q14	2Q14	3Q14	4Q14	1Q15E	2Q15E	3Q15E	4Q1E	2014	2015E	2016E	2017E
Sales												
(KRWb)												
Household electronics	413.8	429.9	431.3	432.4	440.6	457.7	459.0	459.4	1,707.4	1,816.7	1,920.0	2,001.3
Outright sales	27.6	37.4	31.8	26.7	30.3	41.0	33.0	27.7	123.5	132.1	137.8	137.8
Rental	342.4	346.7	352.7	358.8	366.3	371.0	379.1	384.8	1,400.6	1,501.2	1,598.8	1,680.1
Membership	43.9	45.7	46.9	46.9	43.9	45.7	46.9	46.9	183.4	183.4	183.4	183.4
Exports	45.2	55.7	33.0	33.5	52.0	64.1	38.0	38.5	167.4	192.5	231.0	277.2
Cosmetics	21.0	22.3	17.2	20.0	22.0	23.4	18.0	21.0	80.4	84.4	88.7	93.1
Other (water treatment)	14.8	15.4	14.6	13.6	14.8	15.4	14.6	13.6	58.4	58.4	58.4	58.4
Consolidated other	40.2	33.6	29.5	43.4	39.1	38.7	35.3	42.7	146.7	155.8	176.0	196.1
Chg (% y-y)												
Household electronics	1.7	1.7	4.3	4.9	6.5	6.5	6.4	6.2	3.2	6.4	5.7	4.2
Outright sales	(24.7)	(21.8)	(10.4)	(9.1)	10.0	9.6	4.0	3.7	(17.3)	7.0	4.3	0.0
Rental	4.6	4.5	5.3	5.8	7.0	7.0	7.5	7.2	5.0	7.2	6.5	5.1
Membership	2.6	7.0	8.6	7.4	0.0	0.0	0.0	0.0	6.4	0.0	0.0	0.0
Exports	43.6	25.1	(13.0)	9.3	15.0	15.0	15.0	15.0	15.8	15.0	20.0	20.0
Cosmetics	17.4	0.5	3.6	1.1	5.0	5.0	5.0	5.0	5.3	5.0	5.0	5.0
Other (water treatment)	63.4	98.4	(31.1)	(31.1)	0.0	0.0	0.0	0.0	1.1	0.0	0.0	0.0
Consolidated other	(4.7)	(43.5)	(28.7)	4.3	(2.8)	15.0	20.0	(1.6)	(20.6)	6.2	12.9	11.5
Portion of total sales (%)												
Household electronics	77.4	77.2	82.1	79.7	77.5	76.4	81.3	79.9	79.0	78.7	77.6	76.2
Outright sales	5.2	6.7	6.0	4.9	5.3	6.8	5.8	4.8	5.7	5.7	5.6	5.2
Rental	64.0	62.3	67.1	66.1	64.4	61.9	67.1	66.9	64.8	65.0	64.6	64.0
Membership	8.2	8.2	8.9	8.6	7.7	7.6	8.3	8.1	8.5	7.9	7.4	7.0
Exports	8.5	10.0	6.3	6.2	9.1	10.7	6.7	6.7	7.7	8.3	9.3	10.6
Cosmetics	3.9	4.0	3.3	3.7	3.9	3.9	3.2	3.7	3.7	3.7	3.6	3.5
Other (water treatment)	2.8	2.8	2.8	2.5	2.6	2.6	2.6	2.4	2.7	2.5	2.4	2.2
Consolidated other	7.5	6.0	5.6	8.0	6.9	6.5	6.3	7.4	6.8	6.8	7.1	7.5
Sales, by product												
(KRWb)												
Water purifiers	231.6	235.6	239.7	242.2	242.1	246.7	253.0	259.8	949.2	1,001.6	1,060.9	1,102.8
Bidets	68.5	69.0	69.1	70.3	70.7	71.3	71.7	72.6	276.9	286.4	296.2	307.8
Air purifiers	63.6	64.3	63.8	65.5	67.7	68.8	68.8	69.6	257.3	274.9	286.2	300.2
Water softeners	21.4	20.9	20.5	20.3	20.8	20.3	19.9	19.7	83.1	80.7	78.3	76.0
Mattresses	11.1	13.1	15.3	16.7	15.7	17.5	19.2	20.6	56.3	73.0	89.1	105.2
Other (FWTS, outsourcing, etc)	17.6	26.9	22.8	17.4	23.5	33.1	26.4	17.1	84.7	100.1	109.3	109.3
Chg (% y-y)												
Water purifiers	2.5	1.9	4.6	4.6	4.5	4.7	5.5	7.3	3.4	5.5	5.9	3.9
Bidets	2.7	3.2	3.8	3.8	3.2	3.4	3.8	3.3	3.4	3.4	3.4	3.9
Air purifiers	4.8	7.7	7.3	7.0	6.6	6.9	7.8	6.2	6.7	6.9	4.1	4.9
Water softeners	(10.2)	(8.0)	(6.4)	(6.9)	(2.9)	(2.9)	(2.9)	(2.9)	(7.9)	(2.9)	(2.9)	(2.9)
Mattresses	38.1	46.0	59.1	55.4	41.2	33.0	25.4	23.1	50.4	29.6	22.0	18.1
Other (FWTS, outsourcing, etc)	(18.1)	(18.6)	(14.9)	(8.6)	33.2	23.1	15.9	(1.9)	(15.6)	18.2	9.2	0.0
Portion of total sales (%)												
Water purifiers	43.3	42.3	45.6	44.6	42.6	41.2	44.8	45.2	43.9	43.4	42.9	42.0
Bidets	12.8	12.4	13.2	12.9	12.4	11.9	12.7	12.6	12.8	12.4	12.0	11.7
Air purifiers	11.9	11.6	12.1	12.1	11.9	11.5	12.2	12.1	11.9	11.9	11.6	11.4
Water softeners	4.0	3.8	3.9	3.7	3.7	3.4	3.5	3.4	3.8	3.5	3.2	2.9
Mattresses	2.1	2.4	2.9	3.1	2.8	2.9	3.4	3.6	2.6	3.2	3.6	4.0
Other (FWTS, outsourcing, etc)	3.3	4.8	4.3	3.2	4.1	5.5	4.7	3.0	3.9	4.3	4.4	4.2

Source: Company data, Samsung Securities estimates

Annual-forecast revisions

(KRWb)	2014	New		Old		Chg (%)	
		2015E	2016E	2015E	2016E	2015E	2016E
Sales	2,160	2,308	2,474	2,298	2,444	0.4	1.2
Operating profit	364	414	451	408	439	1.4	2.8
Pre-tax profit	332	399	437	398	429	0.4	1.8
Net profit	250	299	328	298	322	0.4	1.8
EBITDA	578	646	698	660	704	(2.2)	(0.8)
EPS (KRW)	3,223	3,864	4,229	3,866	4,173	(0.1)	1.3

Source: Company data, Samsung Securities estimates

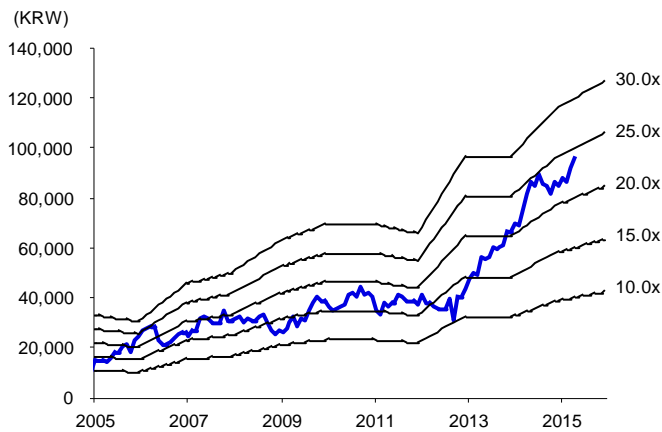
DCF valuation

(KRWb)	2013	2014	2015E	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E
FCF												
NOPLAT	256	256	303	331	373	415	457	480	504	529	556	583
Chg (% y-y)	127.4	0.1	18.3	9.0	12.7	11.3	10.2	5.0	5.0	5.0	5.0	5.0
EBIT	342	341	404	441	497	553	610	640	672	706	741	778
Chg (% y-y)	95.9	(0.1)	18.5	9.0	12.7	11.3	10.2	5.0	5.0	5.0	5.0	5.0
Taxes on EBIT	86	85	101	110	124	138	152	160	168	176	185	194
Tax rate (%)	25.1	24.9	25.0	25.0	25.0	25.0	25.0	25.0	25.0	25.0	25.0	25.0
Depreciation and amortization	198.2	213.6	231.8	247.0	262.5	282.6	306.6	306.6	306.6	306.6	306.6	306.6
Capex	261	302	318	331	344	344	344	344	344	344	344	344
Net working capital change	41	29	16	18	16	18	19	19	19	19	19	19
PV of FCF			194	210	239	278	314	315	316	317	318	319
Terminal value	10,450											
Sum of PV	3,104											
PV of TV	6,007											
Total enterprise value	9,110											
Value of debt	(83)											
Value of equity	9,269											
Equity value/share (KRW)	120,180											
Current price (KRW)	95,900											
Potential (%)	25.3											

FCF (terminal year)	527
WACC (%)	5.3
Growth (%)	0.0

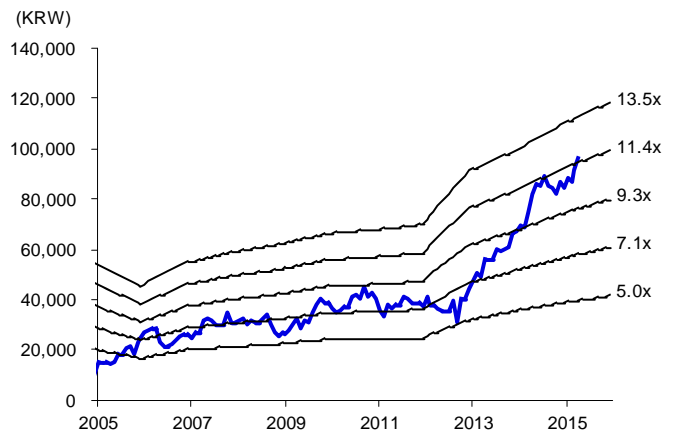
Source: Samsung Securities estimates

Forward P/E band



Source: Company data, Samsung Securities estimates

Forward EV/EBITDA band



Source: Company data, Samsung Securities estimates

Valuation summary

Year-end Dec 31	Sales (KRWb)	Op prof (KRWb)	Pre-tax prof (KRWb)	Net prof (KRWb)	EPS (KRW)	Chg (% y-y)	P/E (x)	P/B (x)	ROE (%)	EV/EBITDA (x)	Net debt (KRWb)
2012	1,824	235	218	167	2,184	(5.6)	43.9	11.2	22.5	18.5	446
2013	2,118	339	327	245	3,222	47.5	29.7	8.5	28.4	13.6	83
2014	2,160	364	332	250	3,223	0.0	29.7	7.4	25.2	12.6	12
2015E	2,308	414	399	299	3,864	19.9	24.8	6.3	26.6	11.3	(83)
2016E	2,474	451	437	328	4,229	9.4	22.7	5.6	25.5	10.4	(145)
2017E	2,626	507	494	370	4,785	13.1	20.0	5.0	25.7	9.3	(240)

Source: Company data, Samsung Securities estimates

Income statement

Year-end Dec 31 (KRWb)	2013	2014	2015E	2016E	2017E
Sales	2,118	2,160	2,308	2,474	2,626
Household electronics	1,655	1,707	1,817	1,920	2,001
Exports	145	167	193	231	277
Cosmetics	76	80	84	89	93
Others	58	58	58	58	58
Consolidated others	185	147	156	176	196
Cost of goods sold	721	727	781	854	906
Gross profit	1,397	1,434	1,527	1,620	1,720
Gross margin (%)	66.0	66.4	66.2	65.5	65.5
SG&A expenses	1,058	1,069	1,113	1,170	1,213
Operating profit	339	364	414	451	507
Operating margin (%)	16.0	16.9	18.0	18.2	19.3
Net interest income	(14)	(9)	(5)	(4)	(3)
Net forex-related gains	(4)	(0)	(0)	(0)	(0)
Net equity-method gains	0	0	0	0	0
Other	6	(23)	(10)	(10)	(10)
Pre-tax profit	327	332	399	437	494
Taxes	82	83	100	109	123
Effective tax rate (%)	25.1	24.9	25.0	25.0	25.0
Net profit	245	250	299	328	370
Net margin (%)	11.6	11.6	13.0	13.2	14.1
Operating net profit*	245	250	299	328	370
Operating net margin (%)	248	249	298	326	369
EBITDA	537	578	646	698	769
EBITDA margin (%)	25.4	26.8	28.0	28.2	29.3
Reported EPS (KRW)	3,178	3,237	3,882	4,247	4,803
Adjusted EPS (KRW)**	3,222	3,223	3,864	4,229	4,785
DPS (common, KRW)	1,660	1,661	2,500	2,700	3,050
DPS (preferred, KRW)	0	0	0	0	0
Dividend payout ratio (%)	50.4	49.3	61.9	61.1	61.1

Cash flow statement

Year-end Dec 31 (KRWb)	2013	2014	2015E	2016E	2017E
Cash flow from operations	537	537	536	578	639
Net profit	245	250	299	328	370
Depreciation & amortization	198	214	232	247	262
Net forex-translation income	0	0	(2)	(2)	(2)
Net equity-method income	0	0	0	0	0
Gross cash flow	528	490	552	596	655
(-) Change in working capital	9	47	(16)	(18)	(16)
Other	(0)	0	(0)	(0)	0
Cash flow from investments	(76)	(299)	(318)	(331)	(344)
Capex	(258)	(296)	(318)	(331)	(344)
Free cash flow	195	211	201	229	275
Change in investment assets	(1)	0	0	0	0
Other	183	(3)	0	0	0
Cash flow from financing	(373)	(328)	(118)	(187)	(205)
Change in debt	(260)	(163)	5	(2)	(5)
Change in equity	0	0	0	0	0
Dividends	(78)	(124)	(123)	(185)	(200)
Other	(34)	(42)	0	0	0
Change in cash	86	(91)	100	60	90
Cash at beginning of year	152	239	147	247	307
Cash at end of year	239	147	247	307	397

Note: * Excluding one off items

** Fully diluted, excluding one-off items

*** From companies subject to equity-method valuation

Source: Coway, Samsung Securities estimates

Balance sheet

Year-end Dec 31 (KRWb)	2013	2014	2015E	2016E	2017E
Current assets	691	597	718	801	912
Cash & equivalents	245	154	254	314	404
Accounts receivable	250	229	245	262	279
Inventories	66	62	66	71	75
Other current assets	131	152	154	154	154
Fixed assets	976	1,025	1,089	1,151	1,210
Investment assets	82	81	81	81	81
Equity in affiliated companies	0	0	0	0	0
Tangible assets	638	675	739	801	860
Intangible assets	177	171	171	171	171
Other long-term assets	80	98	98	98	98
Total assets	1,668	1,622	1,807	1,952	2,122
Current liabilities	677	526	535	538	538
Accounts payable	37	59	63	68	72
Short-term debt	182	164	170	168	163
Other current liabilities	458	303	303	303	303
Long-term liabilities	50	56	56	56	56
Bond & long-term debt	0	1	1	1	1
Other long-term liabilities	50	55	55	55	55
Total liabilities	727	582	592	594	594
Controlling interests' equity	941	1,039	1,215	1,357	1,527
Capital stock	41	41	41	41	41
Capital surplus	126	126	126	126	126
Retained earnings	868	986	1,162	1,304	1,474
Other	(94)	(114)	(114)	(114)	(114)
Non-controlling interests' equity	0	1	1	1	1
Total equity	941	1,039	1,216	1,358	1,528
Net debt	83	12	(83)	(145)	(240)
Book value per share (KRW)	11,242	12,934	15,219	17,062	19,268

Financial ratios

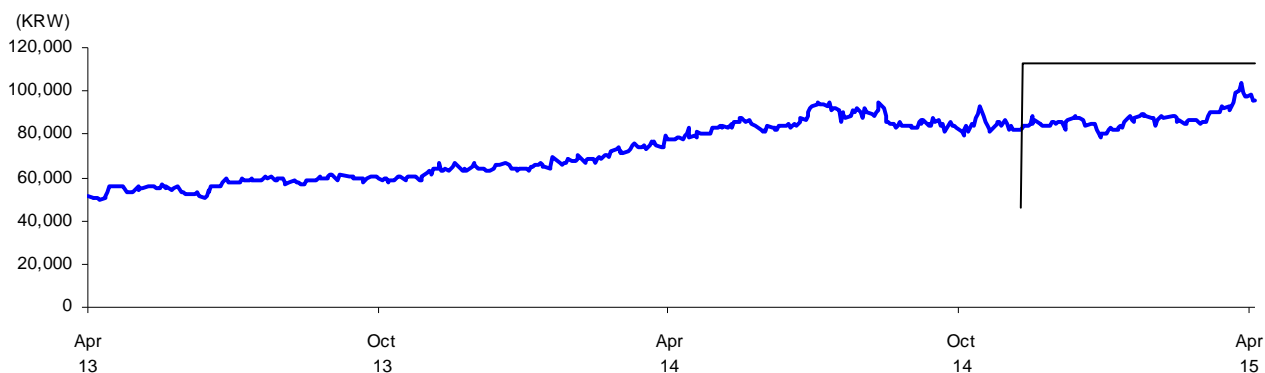
Year-end Dec 31	2013	2014	2015E	2016E	2017E
Growth (%)					
Sales	6.3	2.0	6.8	7.2	6.1
Operating profit	49.9	7.5	13.7	8.8	12.4
Pre-tax profit	124.4	1.6	20.1	9.4	13.1
Net profit	160.6	1.9	19.9	9.4	13.1
EBITDA	31.1	7.6	11.8	8.0	10.2
Adjusted EPS**	169.1	0.0	19.9	9.4	13.1
Ratios					
ROE (%)	28.4	25.2	26.6	25.5	25.7
ROA (%)	14.3	15.2	17.5	17.4	18.2
ROIC (%)	23.2	22.8	28.2	28.6	30.2
Net debt to equity (%)	8.8	1.1	(6.8)	(10.7)	(15.7)
Interest coverage (x)	18.3	29.6	51.5	55.6	63.8
Receivables turnover (days)	44.1	40.4	37.5	37.4	37.6
Payables turnover (days)	7.1	8.1	9.7	9.6	9.7
Inventory turnover (days)	11.8	10.8	10.1	10.1	10.2
Valuations (x)					
P/E	29.7	29.7	24.8	22.7	20.0
P/B	8.5	7.4	6.3	5.6	5.0
EV/EBITDA	13.6	12.6	11.3	10.4	9.3
EV/EBIT	21.4	21.4	18.1	16.4	14.4
Dividend yield (common, %)	1.7	1.7	2.6	2.8	3.2

Coway

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■ Target price changes in past two years



■ Rating changes in past two years

Date	2014/11/19	2015/4/16
Recommendation	BUY	BUY
Target price (KRW)	113,000	120,000

Samsung Securities uses the following investment ratings.

Company

- BUY★★★** Expected to increase in value by 30% or more within 12 months and is highly attractive within sector
- BUY** Expected to increase in value by 10% or more within 12 months
- HOLD** Expected to increase/decrease in value by less than 10% within 12 months
- SELL** Expected to decrease in value by 10% or more within 12 months
- SELL★★★** Expected to decrease in value by 30% or more within 12 months

Industry

- OVERWEIGHT** Expected to outperform market by 5% or more within 12 months
- NEUTRAL** Expected to outperform/underperform market by less than 5% within 12 months
- UNDERWEIGHT** Expected to underperform market by 5% or more within 12 months

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General

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