

Coway (021240)

12M rating **BUY (Maintain)**

12M TP **W117,000** from W106,000

Up/downside **+23%**

Stock Data

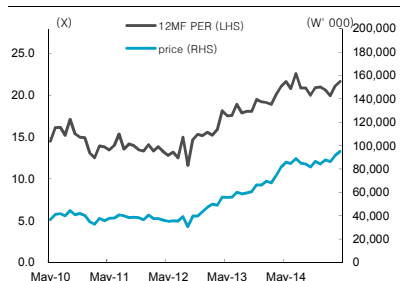
KOSPI (Apr 16, pt)	2,140
Stock price (Apr 16, KRW)	94,900
Market cap (USD mn)	6,722
Shares outstanding (mn)	77
52-Week high/low (KRW)	103,500/77,500
6M avg. daily turnover (USD mn)	14.9
Free float / Foreign ownership (%)	65.3/54.8
Major shareholders (%)	

	Coway Holdings, Inc. and 9 others	NPS
	Coway Holdings, Inc. and 9 others	NPS

Performance

	1M	6M	12M
	11.0	13.5	22.3
	3.3	2.0	14.9

12MF PE trend



Source: WISEfn consensus

1Q15 preview: Steady march forward

Lift TP on moderate improvement

We lift our TP by 10% from W106,000 to W117,000 as we applied a target PE of 25x (historical high) to 2015-2016 average EPS. Coway offers a 24% upside on moderate earnings growth and change to the valuation base period. As margins have already improved sharply since 2013, when Coway was acquired by a private equity fund, expectations for additional rapid growth have faded. However, 1) increasing demand for domestic environmental home appliances and rentals, 2) moderate growth driven by the CODY channel and salesforce, 3) potential high profit from the rental business, 4) likely overseas business expansion and 5) favorable stakeholder policies are key drivers. Dividend yield in 2015-2016 are forecast at 2.5% and 3.0% respectively.

1Q15 OP to be in line with expectations, solid rental business

We estimate 1Q15 consolidated sales at W575bn, up 8% YoY, and OP at W106bn, up 18% YoY, in line with expectations. OPM should climb 1.6%p YoY to 18.5%. Rental sales (77% of total sales) should grow 6.3% YoY and non-rental (20%) should rebound 8.2% YoY, after eroding for two quarters. The number of rental accounts should reach 5.68mn, up 3.9% YoY, and ARPU should grow 2.7% YoY. New rental sales should improve ~10% YoY, and with churn less than 1% per month, net rental account additions should improve by 65,000 QoQ despite off-seasonality. Non-rental lump-sum payments sales should rise 10% YoY and cosmetics 25% YoY, but exports should be flat YoY on competition and a high base effect. Cost to sales should fall as ARPU rises and as major SG&A expenses, including ads, should be stable.

Expanding growth in 2015, robust key indicators despite competition

We forecast 2015 consolidated sales of W2.4tn, up 9.4% YoY, and OP at W437bn, up 20% YoY as rental sales grow 7.3% YoY and non-rentals increase 15% YoY. Top-line growth slowed in 2013 and 2014 as management focused on margins, but sales should climb this year on more new rental sales and net rental account additions in 2014. Expectations and concerns for the rental business have been mixed due to Hyundai Home Shopping Network (057050, BUY TP W190,000)'s new rental subsidiary. We believe Coway has a competitive advantage in terms of product quality and service networks, in addition to much larger sales and OP. Major competitiveness indicators are: 1) new sales, 2) churn, and 3) marketing costs. Coway is posting brisk growth in mattresses and air purifiers, and the core water purifier business is also robust. Churn is stable, and there are no major marketing expenses for repurchases or subscriber additions underway. Coway is

Yr to	Sales	OP	NP	EPS	% chg	EBITDA	PE	EV/EBITDA	PB	ROE	DY
Dec	(W bn)	(W bn)	(W bn)	(KRW)	(YoY)	(W bn)	(x)	(x)	(x)	(%)	(%)
2013A	2,118	339	245	3,283	159.1	537	20.2	9.5	4.9	28.4	4.1
2014A	2,160	364	250	3,361	2.4	578	25.1	11.0	5.6	25.2	2.4
2015F	2,364	437	327	4,407	31.1	661	21.5	10.8	5.6	29.4	2.5
2016F	2,567	488	368	4,957	12.5	721	19.1	9.8	5.0	29.0	3.0
2017F	2,796	538	408	5,491	10.8	782	17.3	9.0	4.4	28.5	3.4

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

Analysts who prepared this report are registered as research analysts in Korea but not in any other jurisdiction, including the U.S. PLEASE SEE ANALYST CERTIFICATIONS AND IMPORTANT DISCLOSURES & DISCLAIMERS AT THE END OF THIS REPORT.

responding to competition with high value-added new products, channel expansion and Cody salesforce expansion.

Table 1. 1Q15 preview: In line with consensus

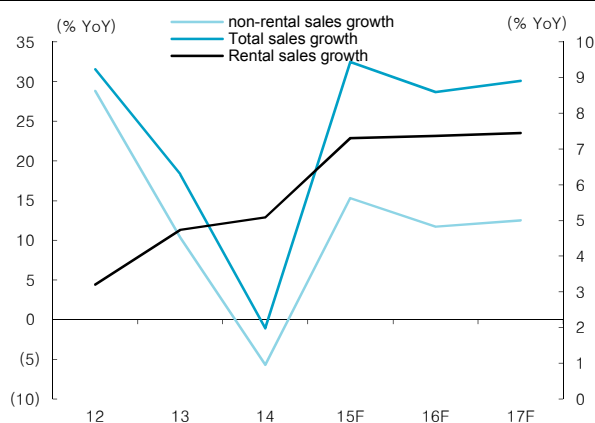
(W bn, %)

	1Q15F	YoY	QoQ	Consensus	1Q14	4Q14	2015F
Sales	575	7.5	5.9	532	535	543	2,364
OP	106	17.7	30.0	100	90	82	437
EBT	105	19.0	47.1	104	88	72	433
NP	79	20.3	48.9	77	66	53	327

Note: Consensus are on parent basis

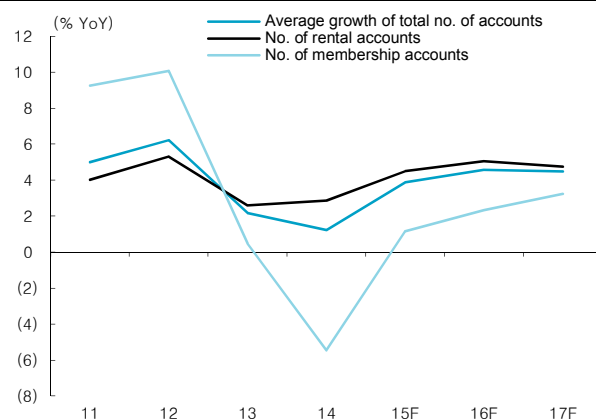
Source: Coway, Quantwise, Korea Investment & Securities

Figure 1. Sluggish non-rental in 2014, slow top-line growth



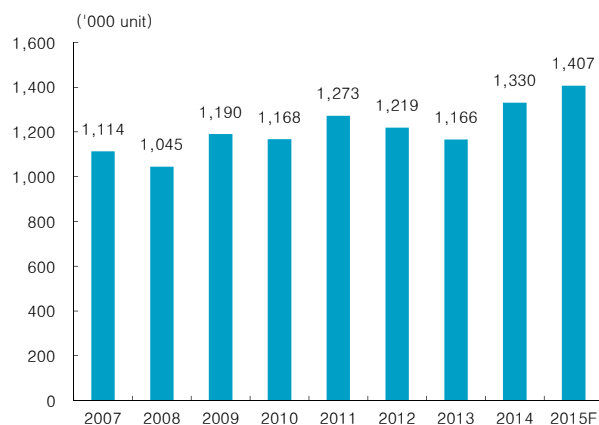
Source: Company data, Korea Investment securities & Investment

Figure 2. No. of accounts in recovery after bottoming in 2013



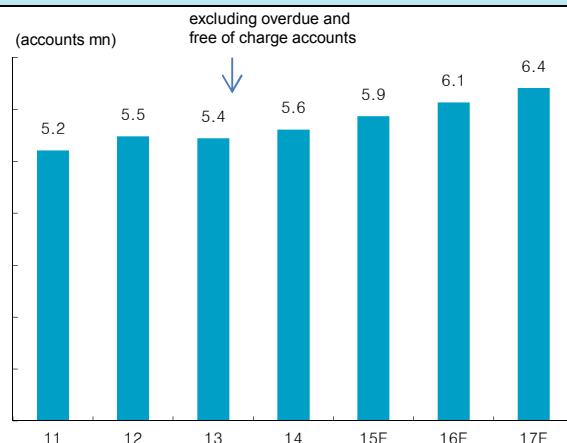
Source: Company data, Korea Investment securities & Investment

Figure 3. Brisk new rental sales from 2014



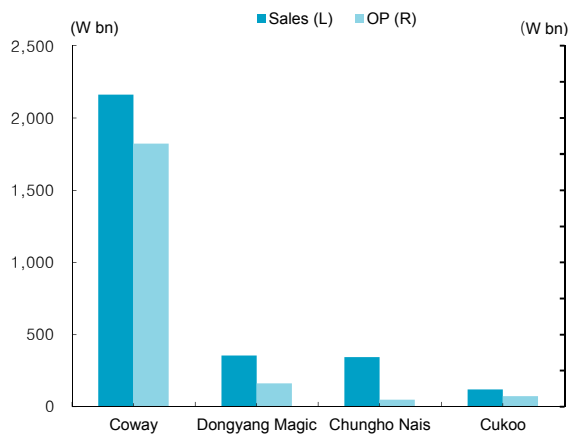
Source: Company data, Korea Investment securities & Investment

Figure 4. Total no. of accounts



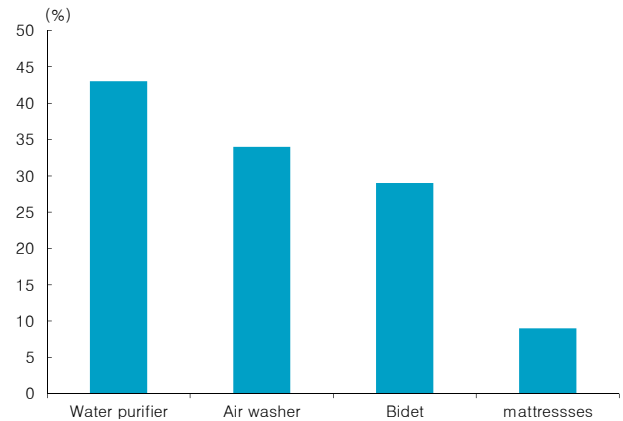
Source: Company data, Korea Investment securities & Investment

Figure 5. Coway vs. competitors 2014 earnings



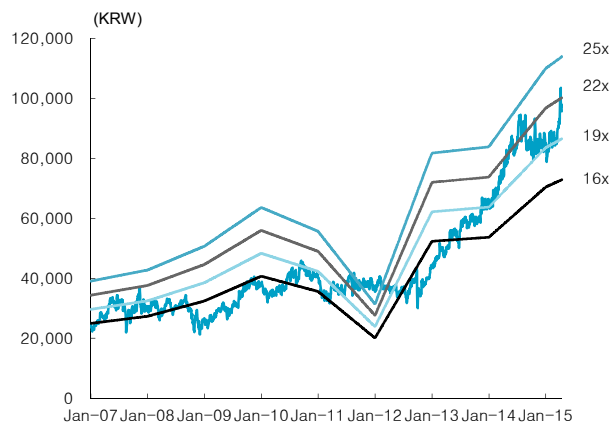
Source: Company data, Korea Investment securities & Investment

Figure 6. Coway major rental products share



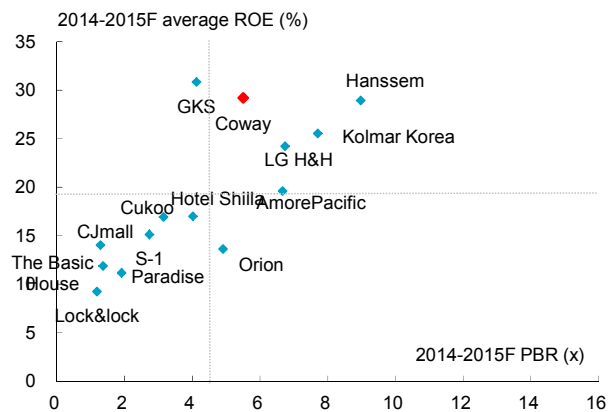
Source: Company data, Korea Investment securities & Investment

Figure 7. PE band



Source: Company data, Korea Investment securities & Investment

Figure 8. PB/ROE compared to major consumer goods firms



Source: Company data, Korea Investment securities & Investment

Table 3. Annual earnings breakdown

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

	10	11	12	13	14	15F	16F	17F
Total no. of accounts	4,855	5,215	5,482	5,446	5,617	5,876	6,141	6,414
Net increase (YoY)	118	360	267	(36)	170	259	266	273
% YoY	2.5	7.4	5.1	(0.6)	3.1	4.6	4.5	4.4
No. of rental accounts ('000, EoY)	3,917	4,213	4,349	4,435	4,601	4,840	5,077	5,311
Net increase (YoY)	18	296	136	86	166	240	237	234
No. of membership accounts ('000, EoY)	938	1,002	1,133	1,012	1,016	1,035	1,064	1,103
Net increase (YoY)	100	64	131	(121)	4	19	29	39
No. of new rental sales ('000 units)	1,168	1,273	1,219	1,166	1,330	1,407	1,470	1,549
No. of new rental sales (% YoY)	(1.9)	9.0	(4.2)	(4.3)	14.1	5.8	4.4	5.4
Churn rate (%)	1.07	1.10	1.07	0.95	0.99	1.01	1.02	1.03
Total ARPU (KRW)	21,378	22,584	22,061	22,755	23,863	24,364	25,019	25,730
Total ARPU (% YoY)	2.6	5.6	(2.3)	3.1	4.9	2.1	2.7	2.8
Rental ARPU (KRW)	23,114	24,698	24,430	25,050	25,614	26,391	27,096	27,834
Rental ARPU (% YoY)	3.5	6.9	(1.1)	2.5	2.2	3.0	2.7	2.7
Membership ARPU (KRW)	13,738	13,723	12,560	13,358	15,073	15,150	15,381	15,986
Membership (% YoY)	(1.3)	(0.1)	(8.5)	6.3	12.8	0.5	1.5	3.9
Sales	1,584	1,824	1,993	2,118	2,160	2,364	2,567	2,796
% YoY	(31.1)	15.2	9.2	6.3	2.0	9.4	8.6	8.9
Rental-based	1,272	1,394	1,439	1,507	1,584	1,700	1,825	1,961
% YoY	6.4	9.6	3.2	4.7	5.1	7.3	7.4	7.4
Rental	1,126	1,235	1,278	1,335	1,401	1,513	1,631	1,753
% YoY	6.3	9.7	3.5	4.5	4.9	8.0	7.8	7.5
Membership	146	160	161	172	183	186	194	208
% YoY	7.1	9.1	0.8	6.8	6.7	1.7	3.9	7.3
Non-rental	311.7	429.9	553.7	611.0	576.3	664.5	742.4	835.2
% YoY	(71.8)	37.9	28.8	10.4	(5.7)	15.3	11.7	12.5
Lump-sum payment	93	102	145	149	124	136	151	171
% YoY	22.4	9.8	41.4	3.2	(17.3)	9.9	11.5	12.9
Cosmetics	23	68	67	76	80	90	100	112
% YoY		191.4	(1.5)	13.7	5.3	13.0	10.0	11.0
Exports	69	98	110	145	167	193	221	255
% YoY	24.2	41.6	11.8	31.9	15.8	15.0	15.0	15.0
Others	44	47	46	56	58	64	71	78
% YoY	(48.0)	6.9	(1.5)	21.6	3.9	10.0	10.0	10.0
Overseas subsidiaries	105.9	150.5	207.8	214.1	202.8	227.6	248.9	275.3
% YoY		42.0	38.1	3.0	(5.3)	12.2	9.4	10.6
GP	1,073	1,244	1,315	1,397	1,434	1,582	1,720	1,879
GPM (%)	67.7	68.2	66.0	66.0	66.4	66.9	67.0	67.2
OP	304	235	226	339	364	437	488	538
% YoY	27.3	(22.8)	(3.7)	49.9	7.5	20.0	11.5	10.3
OPM (%)	19.2	12.9	11.3	16.0	16.9	18.5	19.0	19.3

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

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)	2013A	2014A	2015F	2016F	2017F
Current assets	691	597	657	714	777
Cash & cash equivalent	239	147	165	180	196
Accounts & other receivables	250	229	251	272	297
Inventory	66	62	68	74	80
Non-current assets	976	1,025	1,099	1,174	1,253
Investment assets	55	55	60	65	71
Tangible assets	638	675	717	758	800
Intangible assets	177	171	187	203	221
Total assets	1,668	1,622	1,757	1,888	2,030
Current liabilities	677	526	506	471	437
Accounts & other payables	224	251	274	298	324
ST debt & bond	182	164	114	64	34
Current portion of LT debt	146	0	0	0	0
Non-current liabilities	50	56	63	68	74
Debentures	0	0	0	0	0
LT debt & financial liabilities	8	11	13	14	15
Total liabilities	727	582	568	539	512
Controlling interest	941	1,039	1,187	1,348	1,518
Capital stock	41	41	41	41	41
Capital surplus	126	126	126	126	126
Other Reserves	(94)	(114)	(114)	(114)	(114)
Retained earnings	868	986	1,135	1,295	1,465
Minority interest	0	1	1	1	1
Shareholders' equity	941	1,039	1,188	1,348	1,518

Cash flow

FY-ending Dec. (W bn)	2013A	2014A	2015F	2016F	2017F
C/F from operating	537	537	542	579	604
Net profit	245	250	327	368	408
Depreciation	191	206	215	224	233
Amortization	8	8	9	9	10
Net incr. in W/C	(41)	(29)	(10)	(24)	(49)
Others	134	102	1	2	2
C/F from investing	(76)	(299)	(298)	(308)	(322)
CAPEX	(268)	(306)	(266)	(275)	(285)
Decr. in fixed assets	10	10	10	10	10
Incr. in investment	180	0	(5)	(5)	(6)
Net incr. in intangible assets	(2)	(6)	(25)	(25)	(28)
Others	4	3	(12)	(13)	(13)
C/F from financing	(373)	(328)	(226)	(257)	(266)
Incr. in equity	5	5	0	0	0
Incr. in debts	(262)	(162)	(48)	(49)	(29)
Dividends	(78)	(124)	(148)	(178)	(208)
Others	(38)	(47)	(30)	(30)	(29)
C/F from others	(1)	(1)	0	0	0
Increase in cash	86	(91)	18	14	16

Note: Based on K-IFRS (consolidated)

Income statement

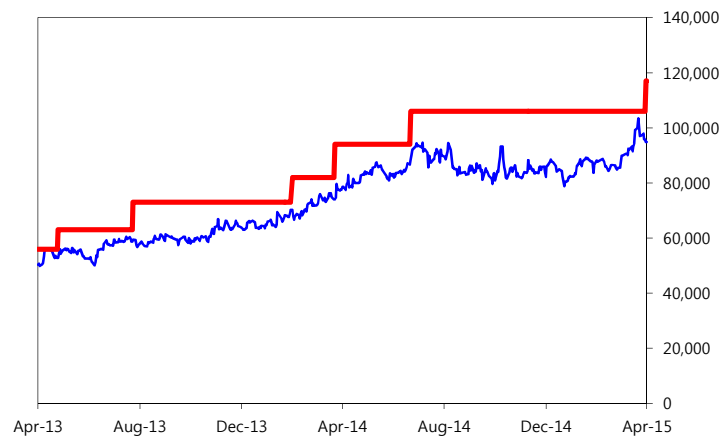
FY-ending Dec. (W bn)	2013A	2014A	2015F	2016F	2017F
Sales	2,118	2,160	2,364	2,567	2,796
COGS	721	727	783	847	917
Gross profit	1,397	1,434	1,582	1,720	1,879
SG&A expense	1,058	1,069	1,144	1,232	1,341
Operating profit	339	364	437	488	538
Financial income	4	3	2	2	3
Interest income	4	3	2	2	3
Financial expense	19	12	7	5	3
Interest expense	19	12	7	5	3
Other non-operating profit	(15)	(23)	0	2	2
Gains (Losses) in associates, subsidiaries and JV	18	0	0	0	0
Earnings before tax	327	332	433	487	540
Income taxes	82	83	106	119	132
Net profit	245	250	327	368	408
Net profit of controlling interest	245	250	327	368	408
Other comprehensive profit	(1)	(9)	0	0	0
Total comprehensive profit	244	241	327	368	408
Total comprehensive profit of controlling interest	244	241	327	368	408
EBITDA	537	578	661	721	782

Key financial data

FY-ending Dec.	2013A	2014A	2015F	2016F	2017F
per share data (KRW)					
EPS	3,283	3,361	4,407	4,957	5,491
BPS	13,535	15,146	17,077	19,153	21,358
DPS	2,710	2,000	2,400	2,800	3,200
Growth (%)					
Sales growth	6.3	2.0	9.4	8.6	8.9
OP growth	49.9	7.5	20.0	11.5	10.3
NP growth	160.6	1.9	31.0	12.5	10.8
EPS growth	159.1	2.4	31.1	12.5	10.8
EBITDA growth	31.1	7.6	14.3	9.1	8.4
Profitability (%)					
OP margin	16.0	16.9	18.5	19.0	19.3
NP margin	11.6	11.6	13.8	14.3	14.6
EBITDA margin	25.4	26.8	28.0	28.1	28.0
ROA	14.3	15.2	19.4	20.2	20.8
ROE	28.4	25.2	29.4	29.0	28.5
Dividend yield	4.1	2.4	2.5	3.0	3.4
Dividend payout ratio	82.4	59.4	54.5	56.5	58.3
Stability					
Net debt (W bn)	98	21	(45)	(109)	(168)
Debt/equity ratio (%)	36.5	16.8	10.7	5.8	2.4
Valuation (X)					
PE	20.2	25.1	21.5	19.1	17.3
PB	4.9	5.6	5.6	5.0	4.4
EV/EBITDA	9.5	11.0	10.8	9.8	9.0

Changes to recommendation and price target

Company (Code)	Date	Recommendation	Price target
Coway (021240)	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
	04-16-15	BUY	W117,000



■ 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.

■ Analyst Certification

I/We, as the research analyst/analysts who prepared this report, do hereby certify that the views expressed in this research report accurately reflect my/our personal views about the subject securities and issuers discussed in this report. I/We do hereby also certify that no part of my/our compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in this research report.

■ Important compliance notice

As of the end of the month immediately preceding the date of publication of the research report or the public appearance (or the end of the second most recent month if the publication date is less than 10 calendar days after the end of the most recent month), Korea Investment & Securities Co., Ltd., or its affiliates does not own 1% or more of any class of common equity securities of Coway.

There is no actual, material conflict of interest of the research analyst or Korea Investment & Securities Co., Ltd., or its affiliates known at the time of publication of the research report or at the time of the public appearance.

Korea Investment & Securities Co., Ltd., or its affiliates has not managed or co-managed a public offering of securities for Coway in the past 12 months;

Korea Investment & Securities Co., Ltd., or its affiliates has not received compensation for investment banking services from Coway in the past 12 months; Korea Investment & Securities Co., Ltd., or its affiliates does not expect to receive or intend to seek compensation for investment banking services from Coway in the next 3 months.

Korea Investment & Securities Co., Ltd., or its affiliates was not making a market in Coway's securities at the time that the research report was published.

Korea Investment & Securities Co., Ltd. does not own over 1% of Coway shares as of April 17, 2015.

Korea Investment & Securities Co., Ltd. has not provided this report to various third parties.

Neither the analyst/analysts who prepared this report nor their associates own any shares of the company/companies covered in this report as of April 17, 2015.

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

Prepared by: Eun-chaе Na

Global Disclaimer

■ General

This research report and marketing materials for Korean securities are originally prepared and issued by the Research Center of Korea Investment & Securities Co., Ltd., an organization licensed with the Financial Supervisory Service of South Korea. The analyst(s) who participated in preparing and issuing this research report and marketing materials is/are licensed and regulated by the Korea Financial Investment Association in Korea only. This report and marketing materials are copyrighted and may not be copied, redistributed, forwarded or altered in any way without the consent of Korea Investment & Securities Co., Ltd.

This research report and marketing materials are for information purposes only. They are not and should not be construed as an offer or solicitation of an offer to purchase or sell any securities or other financial instruments or to participate in any trading strategy. This research report and marketing materials do not provide individually tailored investment advice. This research report and marketing materials do not take into account individual investor circumstances, objectives or needs, and are not intended as recommendations of particular securities, financial instruments or strategies to any particular investor. The securities and other financial instruments discussed in this research report and marketing materials may not be suitable for all investors. The recipient of this research report and marketing materials must make their own independent decisions regarding any securities or financial instruments mentioned herein and investors should seek the advice of a financial adviser. Korea Investment & Securities Co., Ltd. does not undertake that investors will obtain any profits, nor will it share with investors any investment profits. Korea Investment & Securities Co., Ltd., its affiliates, or their affiliates and directors, officers, employees or agents of each of them disclaim any and all responsibility or liability whatsoever for any loss (director consequential) or damage arising out of the use of all or any part of this report or its contents or otherwise arising in connection therewith. Information and opinions contained herein are subject to change without notice and may differ or be contrary to opinions expressed by other business areas or Korea Investment & Securities Co., Ltd. The final investment decision is based on the client's judgment, and this research report and marketing materials cannot be used as evidence in any legal dispute related to investment decisions.

■ Country-specific disclaimer

United States: This report is distributed in the U.S. by Korea Investment & Securities America, Inc., a member of FINRA/SIPC, and is only intended for major U.S. institutional investors as defined in Rule 15a-6(a)(2) under the U.S. Securities Exchange Act of 1934. All U.S. persons that receive this document by their acceptance thereof represent and warrant that they are a major U.S. institutional investor and have not received this report under any express or implied understanding that they will direct commission income to Korea Investment & Securities Co., Ltd. or its affiliates. Pursuant to Rule 15a-6(a)(3), any U.S. recipient of this document wishing to effect a transaction in any securities discussed herein should contact and place orders with Korea Investment & Securities America, Inc., which accepts responsibility for the contents of this report in the U.S. The securities described in this report may not have been registered under the U.S. Securities Act of 1933, as amended, and, in such case, may not be offered or sold in the U.S. or to U.S. person absent registration or an applicable exemption from the registration requirement.

United Kingdom: This report is not an invitation nor is it intended to be an inducement to engage in investment activity for the purpose of section 21 of the Financial Services and Markets Act 2000 of the United Kingdom ("FSMA"). To the extent that this report does constitute such an invitation or inducement, it is directed only at (i) persons who are investment professionals within the meaning of Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended) of the United Kingdom (the "Financial Promotion Order"); (ii) persons who fall within Articles 49(2)(a) to (d) ("high net worth companies, unincorporated associations etc.") of the Financial Promotion Order; and (iii) any other persons to whom this report can, for the purposes of section 21 of FSMA, otherwise lawfully be made (all such persons together being referred to as "relevant persons"). Any investment or investment activity to which this report relates is available only to relevant persons and will be engaged in only with relevant persons. Persons who are not relevant persons must not act or rely on this report.

Hong Kong: This research report and marketing materials may be distributed in Hong Kong to institutional clients by Korea Investment & Securities Asia Limited (KISA), a Hong Kong representative subsidiary of Korea Investment & Securities Co., Ltd., and may not otherwise be distributed to any other party. KISA provides equity sales service to institutional clients in Hong Kong for Korean securities under its sole discretion, and is thus solely responsible for provision of the aforementioned equity selling activities in Hong Kong. All requests by and correspondence with Hong Kong investors involving securities discussed in this report and marketing materials must be effected through KISA, which is registered with The Securities & Futures Commission (SFC) of Hong Kong. Korea Investment & Securities Co., Ltd. is not a registered financial institution under Hong Kong's SFC.

Singapore: This report is provided pursuant to the financial advisory licensing exemption under Regulation 27(1)(e) of the Financial Advisers Regulation of Singapore and accordingly may only be provided to persons in Singapore who are "institutional investors" as defined in Section 4A of the Securities and Futures Act, Chapter 289 of Singapore. This report is intended only for the person to whom Korea Investment & Securities Co., Ltd. has provided this report and such person may not send, forward or transmit in any way this report or any copy of this report to any other person. Please contact Korea Investment & Securities Singapore Pte Ltd in respect of any matters arising from, or in connection with, the analysis or report (Contact Number: 65 6501 5600).

Copyright © 2015 Korea Investment & Securities Co., Ltd. All rights reserved. No part of this report may be reproduced or distributed in any manner without permission of Korea Investment & Securities Co., Ltd.