

Coway

(021240 KS)

Rental business running smoothly

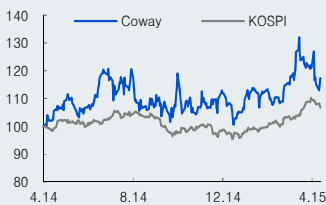
Consumer Services

Results Comment
May 7, 2015

(Maintain)	Buy
Target Price (12M, W)	130,000
Share Price (5/6/15, W)	92,000
Expected Return	41%

OP (15F, Wbn)	431
Consensus OP (15F, Wbn)	427
EPS Growth (15F, %)	24.9
Market EPS Growth (15F, %)	38.7
P/E (15F, x)	22.8
Market P/E (15F, x)	11.0
KOSPI	2,104.58
Market Cap (Wbn)	7,095
Shares Outstanding (mn)	77
Free Float (%)	65.3
Foreign Ownership (%)	54.6
Beta (12M)	0.07
52-Week Low	78,900
52-Week High	103,500

(%)	1M	6M	12M
Absolute	-8.0	7.6	15.0
Relative	-10.5	-1.0	7.1



Daewoo Securities Co., Ltd.

[Cosmetics, Hotel/Leisure, Fashion]

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1Q15 review: Consolidated OP of W100.3bn, in line with our estimate

For 1Q, Coway announced preliminary consolidated revenue of W548.2bn (+2.5% YoY) and operating profit of W100.3bn (+11.1% YoY; OP margin of 18.3%). Revenue fell 4% shy of our projection, but operating profit was in line (vs. W102.5bn).

The home appliance rental business continued solid growth, but exports were dragged down by inventory adjustments by customers as well as overseas subsidiaries. OP margin improved 1.4%p YoY on the back of a record-low churn rate and a stronger-than-anticipated increase in rental accounts.

Quality of growth continues to improve

New rental accounts: In 1Q, new rental accounts increased 7.5% YoY to 341,000 (1.5% above our estimate of 336,000), the highest on record for the first quarter. The increase is particularly impressive given that 1Q is typically an off-season for home appliances. Such stronger-than-expected growth of the rental business—Coway's primary growth driver—reinforces our confidence in the long-term outlook.

Net rental additions: In 1Q, net rental additions reached 66,000, displaying positive growth for the fourth consecutive quarter. Net rental additions are a good indicator of both qualitative and quantitative growth, reflecting new accounts, maturing accounts, and cancellations. Coway's ability to keep churn rate low (0.96%), drive new accounts, and maintain record-low asset disposal rates (2.7%; rental asset disposal losses as a percentage of rental revenue) suggests the company's underlying core competencies are strengthening.

Qualitative strength stands out; Maintain Buy

In our view, Coway's biggest strengths lie in its rental business and development capabilities. The rental business effectively creates demand for the company's own products by lowering customers' initial cost burden, providing a source of steady cash flow. The company's capability to develop new, innovative products is another important quality that should not be overlooked. The combination of these two qualities serves as a high barrier against competitors.

Coway has released a new, cutting-edge home appliance in 2Q, and is about to launch a smart homecare service that integrates its appliances with the Internet of Things (IoT). We believe Coway warrants a valuation premium for its underlying competencies in developing breakthrough products and driving continued innovation. We maintain our Buy rating and target price of W130,000 and recommend the stock as one of our top picks in consumer discretionary from a medium- and long-term view.

FY (Dec.)	12/12	12/13	12/14	12/15F	12/16F	12/17F
Revenue (Wbn)	1,993	2,118	2,160	2,289	2,461	2,627
OP (Wbn)	226	339	364	431	493	542
OP margin (%)	11.3	16.0	16.9	18.8	20.0	20.6
NP (Wbn)	94	245	250	312	357	396
EPS (W)	1,219	3,178	3,237	4,042	4,628	5,138
ROE (%)	12.3	28.4	25.2	27.8	27.8	27.0
P/E (x)	35.7	20.9	26.0	22.8	19.9	17.9
P/B (x)	3.8	4.9	5.6	5.3	4.7	4.2

Notes: All figures are based on consolidated K-IFRS; NP refers to net profit attributable to controlling interests
Source: Company data, KDB Daewoo Securities Research estimates

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Table 1. 1Q15P review (consolidated)

(Wbn, %)

	1Q14	4Q14	1Q15P			Growth	
			Preliminary	KDB Daewoo	Consensus	YoY	QoQ
Revenue	535	543	548	573	573	2.5	1.0
Operating profit	90	82	100	103	107	11.1	22.8
OP margin (%)	16.9	15.1	18.3	17.9	18.7		
Pretax profit	88	72	101	96	103	14.3	41.3
Net profit	66	53	78	72	78	17.4	45.4

Notes: Based on consolidated K-IFRS

Source: Company data, KDB Daewoo Securities Research

Table 2. Earnings forecast revisions

(Wbn, %)

	Previous		Revised		% chg.		Notes
	15F	16F	15F	16F	15F	16F	
Revenue	2,316	2,480	2,289	2,461	-1.2	-0.8	- Revised export forecasts
Operating profit	437	506	431	493	-1.3	-2.6	
Pretax profit	408	483	411	472	0.8	-2.3	- Reflected 1Q15 asset disposal income
Net profit	306	362	312	357	1.8	-1.4	

Source: KDB Daewoo Securities Research

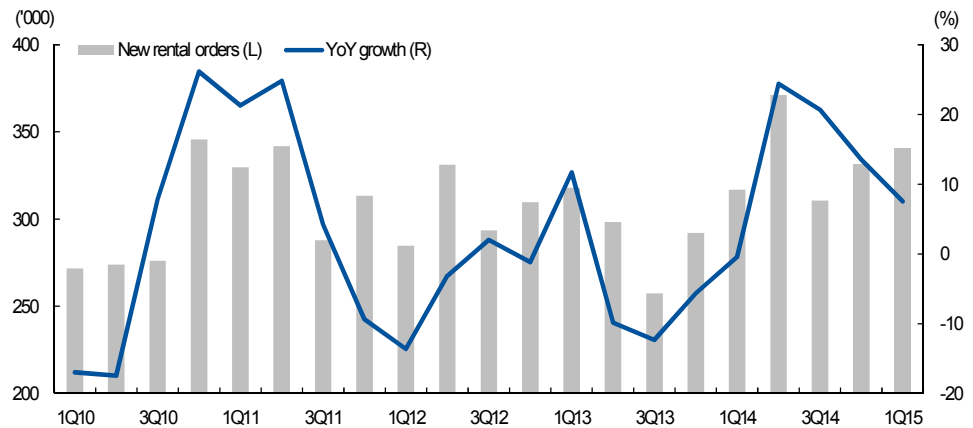
Table 3. Quarterly earnings (non-consolidated)

(Wbn, %, '000 units, '000 accounts)

	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14	1Q15P	2Q15F	3Q15F	4Q15F
Revenue	465	497	489	482	495	523	496	500	506	546	540	529
Rentals	327	332	335	339	342	347	353	359	363	371	381	386
Memberships	43	43	43	44	44	46	47	47	46	48	49	47
Lump-sum payments	37	48	35	29	28	37	32	27	30	39	33	26
Other	58	74	76	70	81	93	65	67	67	88	77	71
% YoY												
Revenue	5.2	11.3	6.8	4.9	6.4	5.3	1.4	3.6	2.3	4.3	8.8	6.0
Rentals	3.5	4.1	3.6	3.6	4.6	4.5	5.3	5.8	6.1	7.1	8.0	7.6
Memberships	10.4	9.1	5.1	3.2	2.6	7.0	8.6	7.4	4.9	4.0	4.0	-0.1
Lump-sum payments	11.9	18.1	-9.3	-9.3	-24.7	-21.8	-10.4	-9.1	8.8	5.1	5.1	-4.3
Other	7.0	55.6	38.4	21.0	38.7	25.4	-14.4	-4.4	-17.5	-6.0	18.2	5.8
Cost of goods sold	155	168	170	159	169	180	162	160	159	181	176	168
(%, revenue)	33.2	33.8	34.7	33.0	34.2	34.5	32.8	32.1	31.5	33.2	32.6	31.6
(%, YoY)	6.3	18.1	12.1	-4.2	9.4	7.5	-4.4	0.6	-5.9	0.5	8.4	4.6
SG&A expenses	241	250	222	236	236	245	237	248	248	261	260	261
(%, revenue)	51.9	50.2	45.4	48.8	47.6	46.9	47.7	49.6	49.0	47.8	48.2	49.3
Rental disposal expenses	12	10	9	8	10	11	10	10	10	10	10	11
(%, rental revenue)	3.5	3.0	2.8	2.4	2.8	3.1	2.9	2.7	2.7	2.7	2.7	2.7
Operating profit	69	79	97	88	90	98	97	91	99	104	103	101
(%, revenue)	14.9	16.0	19.8	18.2	18.1	18.7	19.5	18.3	19.5	19.0	19.2	19.1
(%, YoY)	7.9	21.9	54.3	145.6	29.7	23.0	-0.1	4.3	10.2	6.3	6.7	10.4
[Key indicators]												
Net rental orders ('000 units)	318	298	257	292	317	371	311	332	341	397	330	348
Total rental accounts ('000 accounts)	4,332	4,374	4,387	4,435	4,455	4,487	4,538	4,601	4,666	4,724	4,794	4,856
Cancellation rate (%)	1.1	1.0	0.9	0.9	1.0	1.0	1.0	0.9	1.0	1.0	1.0	1.0

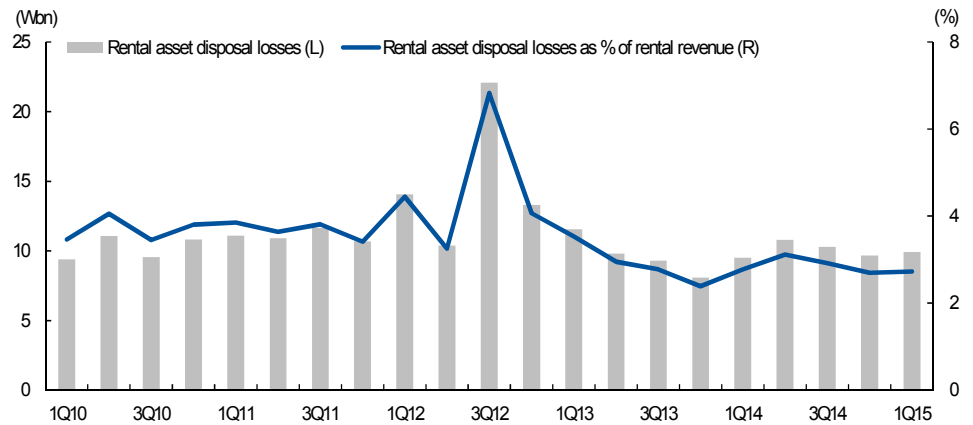
Source: Company data, KDB Daewoo Securities Research

Figure 1. New rental orders: Maintaining stable growth



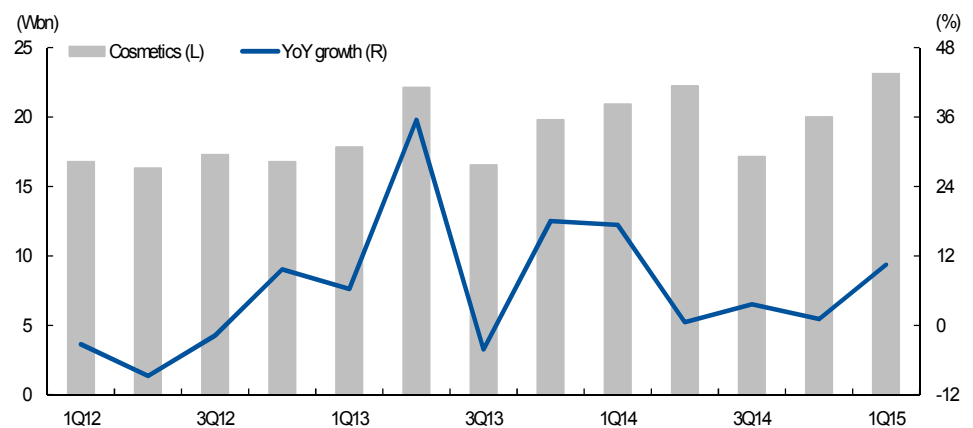
Source: Company data, KDB Daewoo Securities Research

Figure 2. Rental asset disposal losses: Record-low asset disposal rate



Source: Company data, KDB Daewoo Securities Research

Figure 3. Cosmetics revenue: Growth resumed after resolution of trademark dispute



Source: Company data, KDB Daewoo Securities Research

Coway (021240 KS/Buy/TP: W130,000)

Comprehensive Income Statement (Summarized)

(Wbn)	12/14	12/15F	12/16F	12/17F
Revenue	2,160	2,289	2,461	2,627
Cost of Sales	727	716	772	848
Gross Profit	1,433	1,573	1,689	1,779
SG&A Expenses	1,069	1,141	1,196	1,237
Operating Profit (Adj)	364	431	493	542
Operating Profit	364	431	493	542
Non-Operating Profit	-32	-20	-21	-18
Net Financial Income	-9	-2	-1	2
Net Gain from Inv in Associates	0	0	0	0
Pretax Profit	332	411	472	524
Income Tax	83	100	115	128
Profit from Continuing Operations	250	312	357	396
Profit from Discontinued Operations	0	0	0	0
Net Profit	250	312	357	396
Controlling Interests	250	312	357	396
Non-Controlling Interests	0	0	0	0
Total Comprehensive Profit	241	312	357	396
Controlling Interests	241	312	357	396
Non-Controlling Interests	0	0	0	0
EBITDA	578	621	697	761
FCF (Free Cash Flow)	231	265	221	281
EBITDA Margin (%)	26.8	27.1	28.3	29.0
Operating Profit Margin (%)	16.9	18.8	20.0	20.6
Net Profit Margin (%)	11.6	13.6	14.5	15.1

Cash Flows (Summarized)

(Wbn)	12/14	12/15F	12/16F	12/17F
Cash Flows from Op Activities	537	435	531	591
Net Profit	250	312	357	396
Non-Cash Income and Expense	415	284	315	340
Depreciation	206	183	197	213
Amortization	8	7	7	6
Others	201	94	111	121
Chg in Working Capital	-29	-60	-26	-17
Chg in AR & Other Receivables	-3	-20	-17	-16
Chg in Inventories	-3	-11	-5	-5
Chg in AP & Other Payables	18	-7	4	4
Income Tax Paid	-99	-100	-115	-128
Cash Flows from Inv Activities	-299	-137	-264	-256
Chg in PP&E	-296	-139	-267	-262
Chg in Intangible Assets	-6	0	0	0
Chg in Financial Assets	0	-4	-4	-4
Others	3	6	7	10
Cash Flows from Fin Activities	-328	-172	-206	-196
Chg in Financial Liabilities	-168	-20	-10	0
Chg in Equity	0	0	0	0
Dividends Paid	-124	-148	-192	-192
Others	-36	-4	-4	-4
Increase (Decrease) in Cash	-91	130	61	139
Beginning Balance	239	147	277	338
Ending Balance	147	277	338	477

Source: Company data, KDB Daewoo Securities Research estimates

Statement of Financial Condition (Summarized)

(Wbn)	12/14	12/15F	12/16F	12/17F
Current Assets	597	767	860	1,030
Cash and Cash Equivalents	147	277	338	477
AR & Other Receivables	225	245	264	281
Inventories	62	73	79	84
Other Current Assets	163	172	179	188
Non-Current Assets	1,025	978	1,045	1,093
Investments in Associates	0	0	0	0
Property, Plant and Equipment	675	632	701	751
Intangible Assets	171	164	157	150
Total Assets	1,622	1,744	1,905	2,123
Current Liabilities	526	482	474	483
AP & Other Payables	215	205	221	235
Short-Term Financial Liabilities	164	144	134	134
Other Current Liabilities	147	133	119	114
Non-Current Liabilities	56	60	64	69
Long-Term Financial Liabilities	10	10	10	10
Other Non-Current Liabilities	46	50	54	59
Total Liabilities	582	542	538	552
Controlling Interests	1,038	1,202	1,366	1,570
Capital Stock	41	41	41	41
Capital Surplus	126	126	126	126
Retained Earnings	986	1,149	1,314	1,518
Non-Controlling Interests	1	1	1	1
Stockholders' Equity	1,039	1,203	1,367	1,571

Forecasts/Valuations (Summarized)

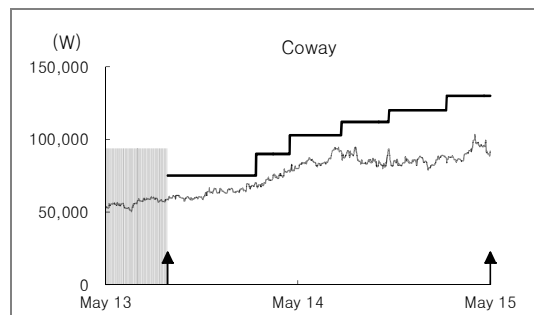
	12/14	12/15F	12/16F	12/17F
P/E (x)	26.0	22.8	19.9	17.9
P/CF (x)	9.8	11.9	10.6	9.6
P/B (x)	5.6	5.3	4.7	4.2
EV/EBITDA (x)	11.3	11.2	9.9	8.9
EPS (W)	3,237	4,042	4,628	5,138
CFPS (W)	8,622	7,717	8,710	9,544
BPS (W)	15,146	17,265	19,398	22,041
DPS (W)	2,000	2,592	3,370	4,718
Payout ratio (%)	59.4	61.7	70.1	88.4
Dividend Yield (%)	2.4	2.8	3.7	5.1
Revenue Growth (%)	2.0	6.0	7.5	6.7
EBITDA Growth (%)	7.6	7.4	12.2	9.2
Operating Profit Growth (%)	7.4	18.4	14.4	9.9
EPS Growth (%)	1.9	24.9	14.5	11.0
Accounts Receivable Turnover (x)	10.3	10.5	10.4	10.4
Inventory Turnover (x)	33.8	33.9	32.5	32.4
Accounts Payable Turnover (x)	15.2	12.8	14.2	14.5
ROA (%)	15.2	18.5	19.6	19.7
ROE (%)	25.2	27.8	27.8	27.0
ROIC (%)	27.0	31.7	34.4	35.2
Liability to Equity Ratio (%)	56.0	45.0	39.4	35.1
Current Ratio (%)	113.5	159.0	181.3	213.2
Net Debt to Equity Ratio (%)	2.0	-10.7	-14.6	-21.6
Interest Coverage Ratio (x)	31.6	112.3	133.6	155.9

APPENDIX 1

Important Disclosures & Disclaimers

2-Year Rating and Target Price History

Company (Code)	Date	Rating	Target Price
Coway (021240)	02/12/2015	Buy	130,000
	10/26/2014	Buy	120,000
	07/28/2014	Buy	112,000
	04/21/2014	Buy	103,000
	02/16/2014	Buy	90,000
	09/01/2013	Buy	75,000
		No Coverage	



Stock Ratings

Buy	: Relative performance of 20% or greater
Trading Buy	: Relative performance of 10% or greater, but with volatility
Hold	: Relative performance of -10% and 10%
Sell	: Relative performance of -10%

Industry Ratings

Overweight	: Fundamentals are favorable or improving
Neutral	: Fundamentals are steady without any material changes
Underweight	: Fundamentals are unfavorable or worsening

Ratings and Target Price History (Share price (—), Target price (—), Not covered (■), Buy (▲), Trading Buy (■), Hold (●), Sell (◆))

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