

Coway (021240)

Above
In line
Below

12M rating **BUY (Maintain)**

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

Up/downside **+27%**

Stock Data

KOSPI (May 6, pt)	2,105
Stock price (May 6, KRW)	92,000
Market cap (USD mn)	6,570
Shares outstanding (mn)	77
52-Week high/low (KRW)	103,500/78,900
6M avg. daily turnover (USD mn)	14.7
Free float / Foreign ownership (%)	65.3/54.6
Major shareholders (%)	
Coway Holdings, Inc. and 9 others	31.0
NPS	5.0

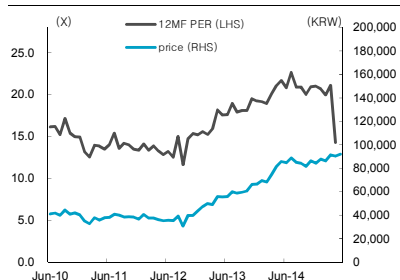
Valuation

	2014A	2015F	2016F
PE (x)	25.1	21.0	18.6
PB (x)	5.6	5.4	4.8
ROE (%)	25.2	29.3	29.0
EV/EBITDA (x)	11.0	10.6	9.6
EPS (KRW)	3,361	4,383	4,946
BPS (KRW)	15,146	17,054	19,120

Performance

	1M	6M	12M
Absolute (%)	(8.0)	7.6	15.0
Relative to KOSPI (%p)	(10.8)	(1.1)	7.6

12MF PE trend



Source: WISEfn consensus

Solid margin growth, focus on overseas recovery

What's new: ARPU- and margin-focused strategy, cost reductions

Coway posted 1Q15 OP of W100.3bn, up 11% YoY, and OPM of 18.3%, up 1.5%p YoY. OP missed our estimate by 5%, but was in line considering early execution of advertisement expenses in 1Q15. Sluggish exports and overseas subsidiary sales slowed total sales growth to 2.5%, but a brisk high-margin rental business fueled a better COGS-to-sales ratio, which improved 2.1%p YoY. Margin improvement is noticeable on the rental- and ARPU-focused strategy. NP was in line with our estimate, at W77.6bn, up 17.4% YoY.

Pros: Robust rental business, operations to fuel moderate growth in 2Q15

Rental sales (75% of total sales) grew 6% YoY while non-rental (lump-sum payments, cosmetics, exports and water treatment) sales fell 1.7% YoY. The number of total subscriber accounts reached 5.66mn, up 3.5% YoY, with ARPU climbing 2.6%. New rental sales posted robust results of 341,000 accounts (+8% YoY) and churn was stable at 0.96%. The increase in sales of new water purifiers (+9% YoY), bidets (+8% YoY) and mattresses (+53% YoY) was impressive. The uptick in ARPU was backed by: 1) higher rental fees, 2) a better product mix, and 3) net additions of rental accounts that generate higher ARPU than membership accounts. In the non-rental, recovery in cosmetics sales (+10% YoY) and lump-sum payments (+8.8% YoY) are catalysts. 1Q typically generates the smallest earnings due to off-seasonality and the booking of expenses, including payments and advertisements. In the peak 2Q season, we expect consolidated OP of W110bn, up 13% YoY.

Cons: Weak overseas sales, focus on recovery

Concerns from 1Q15 are the weak exports (6% of total sales, -27% YoY) and overseas subsidiaries' sales (6% of total sales, -20% YoY). Exports were slow on a high base and fierce competition in the China air washer market. Sales at the China cosmetics business also undermined overseas sales, but should not affect actual gains/losses significantly. The China cosmetics business has been posting losses, and air washer exports to China generated a lower margin than the rest of the company. Coway is focusing on seeking a new partner as it organizes an air washer lineup for 2H15. High growth is continuing in the US and Malaysia, where profits are becoming visible.

(W bn, %, %p)

	1Q15P				Change		2015F	
	KIS est.	Actual	Diff.	Consensus	QoQ	YoY	KIS	Consensus
Sales	575	548	(4.7)	532	1.0	2.5	2,364	2,313
OP	106	100	(5.4)	100	22.3	11.4	437	427
OP margin	18.4	18.3	(0.1)	18.8	3.2	1.5	18.5	18.5
EBT	105	101	(3.7)	104	40.4	14.9	433	425
NP	79	78	(1.8)	77	46.4	17.6	327	316

Note: Consensus are on parent basis, our estimates are on consolidated basis

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Conclusion: Moderate growth and margin-centered strategy, favorable shareholder return policy

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. We forecast 2015F consolidated OP will grow 19% and EPS 30% (16%, stripping out 2014 one-off costs). We maintain BUY and our TP at W117,000 (25x 12MF PE, historical peak). Dividend yield should reach 2.6% in 2015F and 3.0% in 2016F based on the current price.

Table 1. Quarterly earnings breakdown

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

	1Q12	2Q12	3Q12	4Q12	1Q13	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14	1Q15F
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	5,661
Net increase ('000, QoQ)	32	116	70	71	NM	24	11	39	23	70	32	45	44
% YoY	5.4	5.0	4.8	5.3	NM	NM	NM	NM	1.8	2.7	3.0	3.1	3.5
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	4,666
Net increase (QoQ)	30	38	34	56	NM	43	12	48	20	32	51	63	66
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	994
Net increase (QoQ)	2	78	36	15	NM	(18)	(1)	(9)	2	38	(18)	(18)	(22)
No. of new rental sales ('000)	285	331	294	310	318	298	257	292	317	371	311	332	341
% YoY	(14)	(3)	2	(1)	12	(10)	(12)	(6)	(0)	24	21	14	8
Churn rate (%)	1.01	1.00	1.00	0.99	1.01	0.97	0.89	0.86	0.97	1.04	0.96	0.94	0.96
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	24,196
% YoY	2.9	1.8	0.7	0.1	NM	NM	NM	NM	NM	2.5	2.8	2.4	2.6
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	26,136
Rental ARPU (% YoY)	4.3	3.2	2.1	1.6	NM	NM	NM	NM	NM	1.7	2.2	2.1	1.8
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	15,253
Membership ARPU (% YoY)	(5.4)	(6.4)	(6.8)	(6.6)	NM	NM	NM	NM	NM	15.7	13.3	13.0	5.6
Sales	478	489	507	519	507	556	531	524	535	557	526	543	548
%YoY	19.5	12.3	17.8	16.9	6.2	13.7	4.7	0.9	5.4	0.1	(0.9)	3.6	2.5
Rental-based	356	360	364	370	370	375	378	384	386	392	400	406	409
% 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	6.0
Rental	317	321	323	327	327	332	335	339	342	347	353	359	363
% 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	6.1
Membership	39	39	41	42	43	43	43	44	44	46	47	47	46
% 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	4.8
Non-rental	86	86	94	90	95	122	111	100	109	131	97	94	106.7
% YoY	18.6	(10.5)	12.3	0.1	10.4	41.9	18.5	10.1	14.1	7.0	(13.1)	(5.9)	(1.7)
Lump-sum payment	33	41	39	32	37	48	35	29	28	37	32	27	30
% 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)	8.8
Cosmetics	17	16	17	17	18	22	17	20	21	22	17	20	23
% 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	10.2
Exports	30	21	20	31	32	45	38	31	45	56	33	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	(27.0)
Others	7	8	17	11	9	8	21	20	15	15	15	14	21
% 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)	39.4
Subsidiaries	35.3	42.9	48.5	59.2	42.1	59.5	41.3	40.0	40.2	33.6	29.5	43.4	32.2
%YoY					19.1	38.7	(14.8)	(32.5)	(4.5)	(43.5)	(28.7)	8.5	(20.0)
GP	321	331	336	326	340	364	346	348	353	369	357	355	373
GPM	67.3	67.7	66.4	62.7	67.0	65.4	65.3	66.3	65.9	66.3	68.0	65.3	68.0
OP	65	64	63	34	70	82	96	91	90	97	95	82	100
% YoY	(6.9)	(11.6)	(14.1)	22.7	7.7	27.6	53.2	165.0	29.5	18.6	(1.0)	(10.3)	11.1
OPM %	13.6	13.1	12.4	6.6	13.7	14.7	18.1	17.4	16.9	17.4	18.1	15.1	18.3

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

Table 2. Annual earnings breakdown

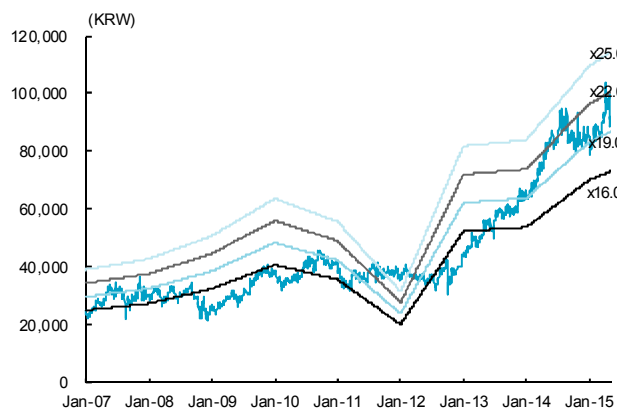
(W bn, KRW, '000 accounts, %YoY, %)

	11	12	13	14	15F	16F
Total no. of accounts	5,215	5,482	5,446	5,617	5,876	6,141
Net increase ('000, QoQ)	360	267	(36)	170	259	266
% YoY	7.4	5.1	(0.6)	3.1	4.6	4.5
No. of rental accounts ('000, end of Q)	4,213	4,349	4,435	4,601	4,840	5,077
Net increase (QoQ)	296	136	86	166	240	237
No. of membership accounts ('000, end of Q)	1,002	1,133	1,012	1,016	1,035	1,064
Net increase (QoQ)	64	131	(121)	4	19	29
No. of new rental sales ('000)	1,273	1,219	1,166	1,330	1,407	1,470
% YoY	9.0	(4.2)	(4.3)	14.1	5.8	4.4
Churn rate (%)	1.10	1.07	0.95	0.99	1.01	1.02
Total ARPU (KRW)	22,584	22,061	22,755	23,863	24,364	25,019
% YoY	5.6	(2.3)	3.1	4.9	2.1	2.7
Rental ARPU (KRW)	24,698	24,430	25,050	25,614	26,391	27,096
Rental ARPU (% YoY)	6.9	(1.1)	2.5	2.2	3.0	2.7
Membership ARPU (KRW)	13,723	12,560	13,358	15,073	15,150	15,381
Membership ARPU (% YoY)	(0.1)	(8.5)	6.3	12.8	0.5	1.5
Sales	1,824	1,993	2,118	2,160	2,302	2,491
%YoY	15.2	9.2	6.3	2.0	6.6	8.2
Rental-based	1,394	1,439	1,507	1,584	1,680	1,804
% YoY	9.6	3.2	4.7	5.1	6.1	7.4
Rental	1,235	1,278	1,335	1,401	1,494	1,610
% YoY	9.7	3.5	4.5	4.9	6.6	7.8
Membership	160	161	172	183	186	194
% YoY	9.1	0.8	6.8	6.7	1.7	3.9
Non-rental	429.9	553.7	611.0	576.3	622.2	687.2
% YoY	37.9	28.8	10.4	(5.7)	8.0	10.4
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	167	184
% YoY	41.6	11.8	31.9	15.8	0.0	10.0
Others	47	46	56	58	64	71
% YoY	6.9	(1.5)	21.6	3.9	10.0	10.0
Subsidiaries	150.5	207.8	214.1	202.8	206.1	226.4
%YoY	42.0	38.1	3.0	(5.3)	1.7	9.9
GP	1,244	1,315	1,397	1,434	1,556	1,684
GPM	68.2	66.0	66.0	66.4	67.6	67.6
OP	235	226	339	364	432	485
% YoY	(22.8)	(3.7)	49.9	7.5	18.5	12.2
OPM %	12.9	11.3	16.0	16.9	18.8	19.5

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

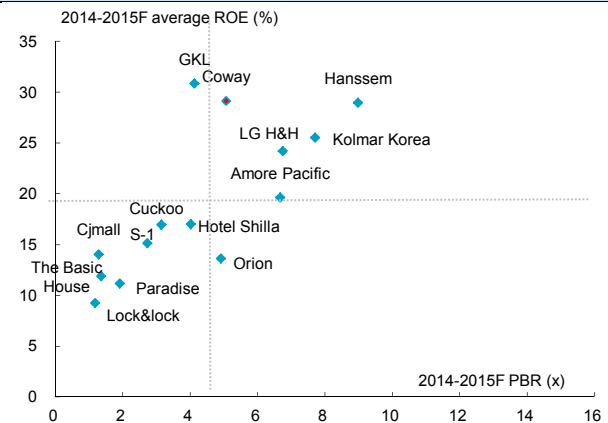
Source: Company data, Korea Investment securities & Investment

Figure 1. PE band



Source: Company data, Korea Investment securities & Investment

Figure 2. 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)	2013A	2014A	2015F	2016F	2017F
Current assets	691	597	640	693	751
Cash & cash equivalent	239	147	161	174	189
Accounts & other receivables	250	229	244	264	287
Inventory	66	62	66	71	77
Non-current assets	976	1,025	1,089	1,162	1,238
Investment assets	55	55	59	63	69
Tangible assets	638	675	717	758	800
Intangible assets	177	171	182	197	213
Total assets	1,668	1,622	1,730	1,854	1,989
Current liabilities	677	526	482	442	405
Accounts & other payables	224	251	267	289	313
ST debt & bond	182	164	114	64	34
Current portion of LT debt	146	0	0	0	0
Non-current liabilities	50	56	61	67	72
Debentures	0	0	0	0	0
LT debt & financial liabilities	8	11	13	14	15
Total liabilities	727	582	543	508	478
Controlling interest	941	1,039	1,186	1,345	1,511
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	1,133	1,292	1,458
Minority interest	0	1	1	1	1
Shareholders' equity	941	1,039	1,187	1,346	1,511

Cash flow

FY-ending Dec. (W bn)	2013A	2014A	2015F	2016F	2017F
C/F from operating	537	537	528	575	600
Net profit	245	250	325	367	403
Depreciation	191	206	215	224	233
Amortization	8	8	8	9	10
Net incr. in W/C	(41)	(29)	(22)	(27)	(48)
Others	134	102	2	2	2
C/F from investing	(76)	(299)	(288)	(305)	(319)
CAPEX	(268)	(306)	(266)	(275)	(285)
Decr. in fixed assets	10	10	10	10	10
Incr. in investment	180	0	(4)	(5)	(5)
Net incr. in intangible assets	(2)	(6)	(20)	(24)	(26)
Others	4	3	(8)	(11)	(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)	14	13	15

Note: Based on K-IFRS (consolidated)

Income statement

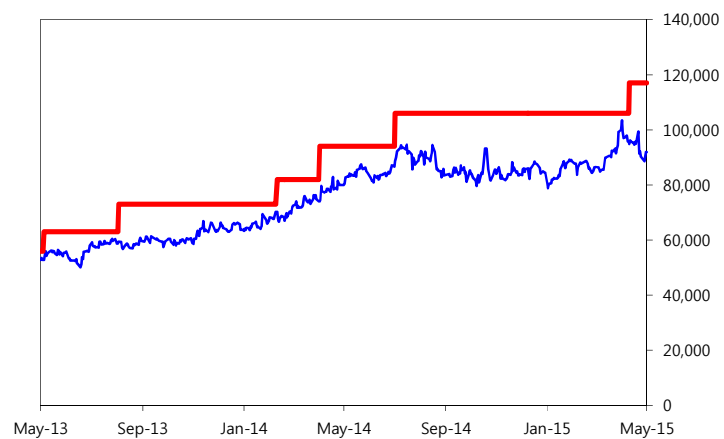
FY-ending Dec. (W bn)	2013A	2014A	2015F	2016F	2017F
Sales	2,118	2,160	2,302	2,491	2,703
COGS	721	727	746	807	870
Gross profit	1,397	1,434	1,556	1,684	1,832
SG&A expense	1,058	1,069	1,125	1,199	1,301
Operating profit	339	364	432	485	531
Financial income	4	3	2	2	3
Interest income	4	3	2	2	3
Financial expense	19	12	3	2	1
Interest expense	19	12	3	2	1
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	431	486	534
Income taxes	82	83	106	119	131
Net profit	245	250	325	367	403
Net profit of controlling interest	245	250	325	367	403
Other comprehensive profit	(1)	(9)	0	0	0
Total comprehensive profit	244	241	325	367	403
Total comprehensive profit of controlling interest	244	241	325	367	403
EBITDA	537	578	655	718	774

Key financial data

FY-ending Dec.	2013A	2014A	2015F	2016F	2017F
per share data (KRW)					
EPS	3,283	3,361	4,383	4,946	5,431
BPS	13,535	15,146	17,054	19,120	21,267
DPS	2,710	2,000	2,400	2,800	3,200
Growth (%)					
Sales growth	6.3	2.0	6.6	8.2	8.5
OP growth	49.9	7.5	18.5	12.2	9.6
NP growth	160.6	1.9	30.3	12.9	9.8
EPS growth	159.1	2.4	30.4	12.8	9.8
EBITDA growth	31.1	7.6	13.3	9.6	7.9
Profitability (%)					
OP margin	16.0	16.9	18.8	19.5	19.7
NP margin	11.6	11.6	14.1	14.7	14.9
EBITDA margin	25.4	26.8	28.4	28.8	28.7
ROA	14.3	15.2	19.4	20.5	21.0
ROE	28.4	25.2	29.3	29.0	28.2
Dividend yield	4.1	2.4	2.6	3.0	3.5
Dividend payout ratio	82.4	59.4	54.8	56.6	58.9
Stability					
Net debt (W bn)	98	21	(41)	(103)	(161)
Debt/equity ratio (%)	36.5	16.8	10.7	5.8	2.4
Valuation (X)					
PE	20.2	25.1	21.0	18.6	16.9
PB	4.9	5.6	5.4	4.8	4.3
EV/EBITDA	9.5	11.0	10.6	9.6	8.8

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



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Prepared by: Eun-chaе Na

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