

Coway

(021240 KS)

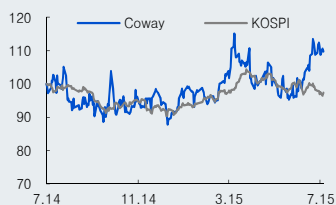
Unrivaled leader of the rental market

Consumer Services

Results Comment
August 5, 2015

(Maintain)	Buy
Target Price (12M, W)	130,000
Share Price (8/4/15, W)	98,600
Expected Return	32%

OP (15F, Wbn)	441
Consensus OP (15F, Wbn)	420
EPS Growth (15F, %)	30.7
Market EPS Growth (15F, %)	27.6
P/E (15F, x)	23.3
Market P/E (15F, x)	11.2
KOSPI	2,027.99
Market Cap (Wbn)	7,605
Shares Outstanding (mn)	77
Free Float (%)	65.3
Foreign Ownership (%)	53.7
Beta (12M)	0.54
52-Week Low	78,900
52-Week High	103,500
(%)	1M 6M 12M
Absolute	8.6 11.0 11.4
Relative	12.7 7.5 14.3



Daewoo Securities Co., Ltd.

[Cosmetics, Hotel/Leisure, Fashion]

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2Q15 review: Above-consensus parent OP of W111.7bn (+14.4% YoY)

For 2Q, Coway reported preliminary non-consolidated revenue of W527.5bn (+0.8% YoY) and operating profit of W111.7bn (+14.4% YoY; OP margin of 21.2%). Both revenue and operating profit reached record highs, with the latter topping our estimate and the consensus by 7.7% and 4.6%, respectively.

At the health appliance division, revenue expanded 6.2% YoY to W463.5bn. More specifically, rental revenue grew 7% YoY to W371.2bn, in line with our expectation (W371.4bn; +7.1% YoY). New rental accounts reached 371,000, flat YoY. However, we believe actual new accounts (excluding rental renewals) were robust YoY, considering that last year's new rental account figure was inflated by a large number of customers switching to new products due to a temporary increase in expiring accounts.

Churn rate (which is correlated to asset quality) slightly inched up QoQ to 1.01% because of the expiry of three-year contracts for many accounts acquired in 2012 as part of an aggressive promotion campaign. Meanwhile, the ratio of rental asset disposal expenses to revenue remained at a record low 2.7%, as increasing customer satisfaction led to a decline in early defections. Exports to third parties (revenue of W18.8bn; -54.9% YoY) and the cosmetics business (revenue of W21.1bn; -5.3% YoY) have yet to show a meaningful recovery, but were more resilient than expected considering the unfavorable business environment.

Growing competitiveness in the rental market

We believe Coway's core strength lies in its R&D capabilities and rental model focusing on high-end health appliances. Because health appliances are less essential than regular domestic appliances, demand hinges on meeting consumers' qualitative needs. Confidence in product quality, sanitation, and customer service is critical to ensuring continued use. Therefore, companies that do not have strong customer support struggle to gain ground.

Even as cheaper products continue to flood the market, Coway has managed to further solidify its market position, releasing new innovative products and accelerating its presence in offline channels. In particular, we believe the simultaneous strength of new rentals and lump-sum sales of high-end products speaks to the company's underlying competitiveness.

Systemic strengths and new strategy to create synergy effect

We maintain our Buy rating and target price of W130,000 on Coway. In our view, Coway merits a valuation premium for its continued innovation and systemic strengths. We continue to recommend the stock from a medium- to long-term view, as it boasts one of the strongest business portfolios in the consumer sector.

FY (Dec.)	12/12	12/13	12/14	12/15F	12/16F	12/17F
Revenue (Wbn)	1,993	2,118	2,160	2,246	2,437	2,612
OP (Wbn)	226	339	364	441	498	532
OP margin (%)	11.3	16.0	16.9	19.6	20.4	20.4
NP (Wbn)	94	245	250	326	365	393
EPS (W)	1,219	3,178	3,237	4,230	4,733	5,092
ROE (%)	12.3	28.4	25.2	31.0	31.8	29.7
P/E (x)	35.7	20.9	26.0	23.3	20.8	19.4
P/B (x)	3.8	4.9	5.6	6.4	5.6	4.9

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. 2Q15P non-consolidated review

(Wbn, %)

	2Q14	1Q15	2Q15P			Growth	
			Preliminary	KDB Daewoo	Consensus	YoY	QoQ
Revenue	523	506	528	546	539	0.8	4.2
Operating profit	98	99	112	104	107	14.4	12.9
OP margin (%)	18.7	19.5	21.2	19.0	19.8		
Pretax profit	87	98	111	97	106	28.5	13.3
Net profit	65	75	85	73	79	30.3	13.2

Source: Company data, KDB Daewoo Securities Research

Table 2. 2Q15P consolidated review

(Wbn, %)

	2Q14	1Q15	2Q15P			Growth	
			Preliminary	KDB Daewoo	Consensus	YoY	QoQ
Revenue	557	548	555	586	590	-0.3	1.3
Operating profit	97	100	111	106	108	13.7	10.2
OP margin (%)	17.4	18.3	19.9	18.1	18.3		
Pretax profit	87	101	109	97	106	25.9	7.7
Net profit	66	78	83	74	80	24.8	6.6

Source: Company data, KDB Daewoo Securities Research

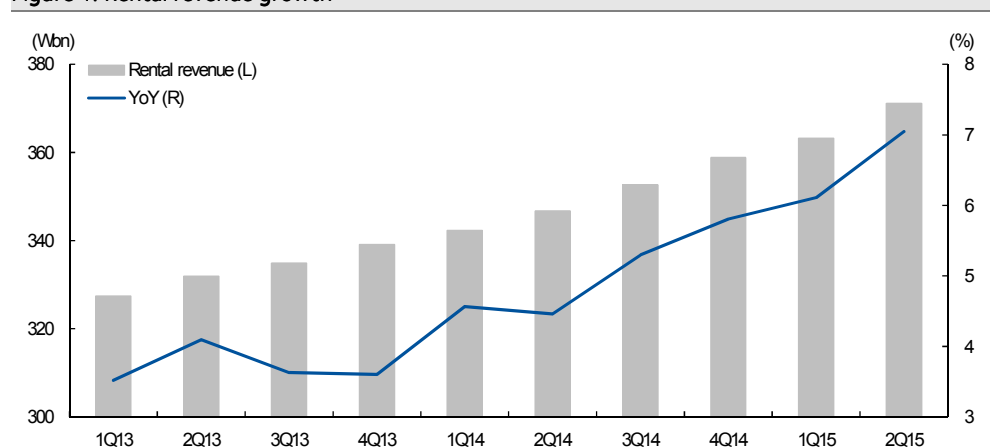
Table 3. Earnings forecast revisions

(Wbn, %, W)

	Previous		Revised		% chg.		Notes
	2015F	2016F	2015F	2016F	2015F	2016F	
Revenue	2,289	2,461	2,246	2,437	-1.9	-1.0	- Reflects lower exports and cosmetics revenue
Operating profit	431	493	441	498	2.3	1.1	- Reflects lower rental COGS
Pretax profit	411	472	428	480	4.1	1.6	- Reflects higher non-operating profit
Net profit	312	357	326	365	4.6	2.3	
EPS	404	463	423	473	4.6	2.3	

Source: Company data, KDB Daewoo Securities Research

Figure 1. Rental revenue growth



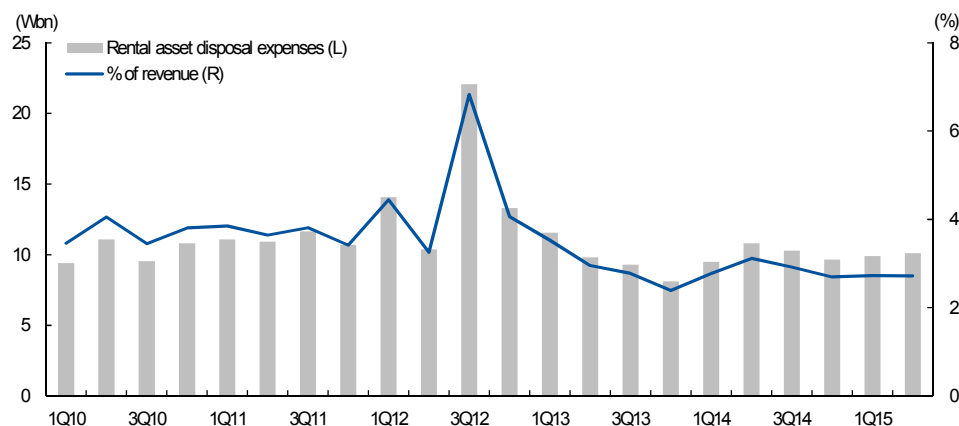
Source: Company data, KDB Daewoo Securities Research

Table 4. Quarterly non-consolidated earnings forecasts (Wbn, %, '000 units, '000 accounts)

	1Q14	2Q14	3Q14	4Q14	1Q15	2Q15P	3Q15F	4Q15F
Revenue	495	523	496	500	506	527	532	525
Rental	342	347	353	359	363	371	383	388
% YoY								
Revenue	6.4	5.3	1.4	3.6	2.3	0.8	7.3	5.1
Rental	4.6	4.5	5.3	5.8	6.1	7.0	8.6	8.1
COGS	169	180	162	160	159	167	167	165
(% of revenue)	34.2	34.5	32.8	32.1	31.5	31.6	31.4	31.5
SG&A	236	245	237	248	248	249	257	259
(% of revenue)	47.6	46.9	47.7	49.6	49.0	47.2	48.2	49.3
Rental asset disposal	10	11	10	10	10	10	10	11
(% of rental revenue)	2.8	3.1	2.9	2.7	2.7	2.7	2.7	2.7
Operating profit	90	98	97	91	99	112	109	101
(% of revenue)	18.1	18.7	19.5	18.3	19.5	21.2	20.4	19.2
(% YoY)	29.7	23.0	-0.1	4.3	10.2	14.4	11.9	10.3
[Key indicators]								
New rental accounts	317	371	311	332	341	371	330	348
Net rental accounts	4,455	4,487	4,538	4,601	4,666	4,747	4,817	4,878
Churn rate (%)	1.0	1.0	1.0	0.9	1.0	1.0	1.0	1.0

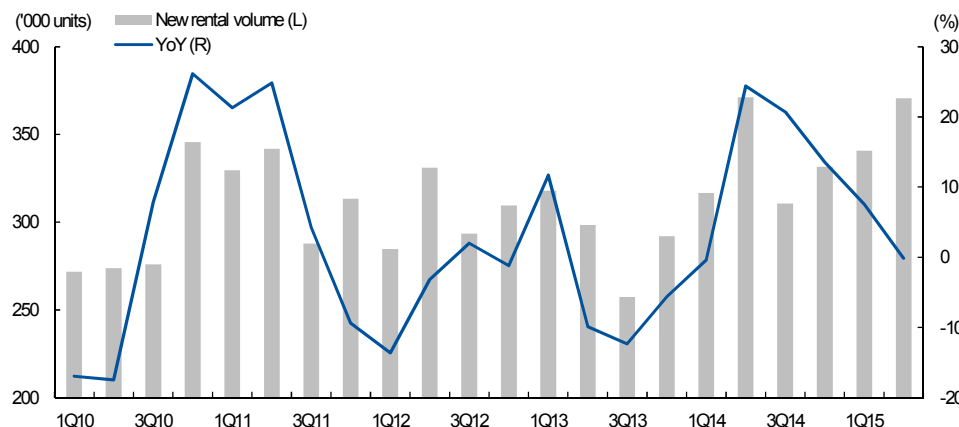
Source: Company data, KDB Daewoo Securities Research

Figure 2. Rental asset disposal expenses stayed at record-low level



Source: Company data, KDB Daewoo Securities Research

Figure 3. New rental volume trend



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	2,246	2,437	2,612
Cost of Sales	727	685	748	844
Gross Profit	1,433	1,561	1,689	1,768
SG&A Expenses	1,069	1,120	1,191	1,237
Operating Profit (Adj)	364	441	498	532
Operating Profit	364	441	498	532
Non-Operating Profit	-32	-13	-18	-16
Net Financial Income	-9	-3	-1	2
Net Gain from Inv in Associates	0	0	0	0
Pretax Profit	332	428	480	516
Income Tax	83	102	115	123
Profit from Continuing Operations	250	326	365	393
Profit from Discontinued Operations	0	0	0	0
Net Profit	250	326	365	393
Controlling Interests	250	326	365	393
Non-Controlling Interests	0	0	0	0
Total Comprehensive Profit	241	320	365	393
Controlling Interests	241	320	365	393
Non-Controlling Interests	0	0	0	0
EBITDA	578	641	704	754
FCF (Free Cash Flow)	231	233	323	283
EBITDA Margin (%)	26.8	28.5	28.9	28.9
Operating Profit Margin (%)	16.9	19.6	20.4	20.4
Net Profit Margin (%)	11.6	14.5	15.0	15.0

Cash Flows (Summarized)

(Wbn)	12/14	12/15F	12/16F	12/17F
Cash Flows from Op Activities	537	404	583	583
Net Profit	250	326	365	393
Non-Cash Income and Expense	415	331	327	349
Depreciation	206	193	199	216
Amortization	8	7	7	6
Others	201	131	121	127
Chg in Working Capital	-29	-155	6	-35
Chg in AR & Other Receivables	-3	-4	-10	-9
Chg in Inventories	-3	-8	-5	-5
Chg in AP & Other Payables	18	-8	4	4
Income Tax Paid	-99	-98	-115	-123
Cash Flows from Inv Activities	-299	-165	-224	-256
Chg in PP&E	-296	-148	-217	-252
Chg in Intangible Assets	-6	-2	0	0
Chg in Financial Assets	0	3	-5	-4
Others	3	-18	-2	0
Cash Flows from Fin Activities	-328	-164	-215	-205
Chg in Financial Liabilities	-168	-12	-10	0
Chg in Equity	0	1	0	0
Dividends Paid	-124	-148	-201	-201
Others	-36	-5	-4	-4
Increase (Decrease) in Cash	-91	75	144	122
Beginning Balance	239	147	222	366
Ending Balance	147	222	366	487

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	635	807	958
Cash and Cash Equivalents	147	222	366	487
AR & Other Receivables	225	223	235	245
Inventories	62	64	69	73
Other Current Assets	163	126	137	153
Non-Current Assets	1,025	994	1,010	1,044
Investments in Associates	0	0	0	0
Property, Plant and Equipment	675	615	633	670
Intangible Assets	171	165	158	152
Total Assets	1,622	1,628	1,817	2,002
Current Liabilities	526	490	509	496
AP & Other Payables	215	208	224	240
Short-Term Financial Liabilities	164	150	140	140
Other Current Liabilities	147	132	145	116
Non-Current Liabilities	56	72	78	85
Long-Term Financial Liabilities	10	13	13	13
Other Non-Current Liabilities	46	59	65	72
Total Liabilities	582	562	587	581
Controlling Interests	1,038	1,065	1,229	1,420
Capital Stock	41	41	41	41
Capital Surplus	126	127	127	127
Retained Earnings	986	1,014	1,177	1,369
Non-Controlling Interests	1	1	1	1
Stockholders' Equity	1,039	1,066	1,230	1,421

Forecasts/Valuations (Summarized)

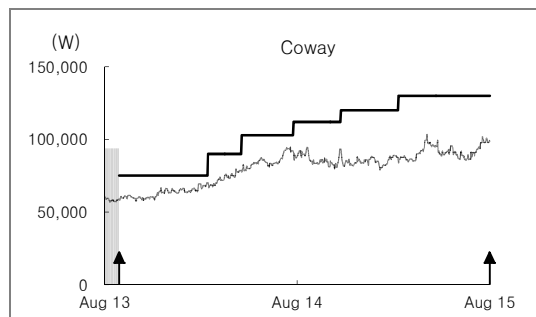
	12/14	12/15F	12/16F	12/17F
P/E (x)	26.0	23.3	20.8	19.4
P/CF (x)	9.8	11.6	11.0	10.3
P/B (x)	5.6	6.4	5.6	4.9
EV/EBITDA (x)	11.3	11.8	10.5	9.6
EPS (W)	3,237	4,230	4,733	5,092
CFPS (W)	8,622	8,525	8,970	9,619
BPS (W)	15,146	15,455	17,576	20,056
DPS (W)	2,000	2,712	3,526	4,936
Payout ratio (%)	59.4	61.8	71.8	93.4
Dividend Yield (%)	2.4	2.8	3.6	5.0
Revenue Growth (%)	2.0	4.0	8.5	7.2
EBITDA Growth (%)	7.6	10.9	9.8	7.1
Operating Profit Growth (%)	7.4	21.2	12.9	6.8
EPS Growth (%)	1.9	30.7	11.9	7.6
Accounts Receivable Turnover (x)	10.3	10.8	11.5	11.8
Inventory Turnover (x)	33.8	35.8	36.9	36.8
Accounts Payable Turnover (x)	15.2	12.3	13.8	14.5
ROA (%)	15.2	20.1	21.2	20.6
ROE (%)	25.2	31.0	31.8	29.7
ROIC (%)	27.0	33.5	38.4	39.3
Liability to Equity Ratio (%)	56.0	52.7	47.8	40.9
Current Ratio (%)	113.5	129.5	158.5	193.0
Net Debt to Equity Ratio (%)	2.0	-5.6	-17.3	-23.6
Interest Coverage Ratio (x)	31.6	110.0	128.4	144.9

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 (◆))

* Our investment rating is a guide to the relative return of the stock versus the market over the next 12 months.

* Although it is not part of the official ratings at Daewoo Securities, we may call a trading opportunity in case there is a technical or short-term material development.

* The target price was determined by the research analyst through valuation methods discussed in this report, in part based on the analyst's estimate of future earnings.

* The achievement of the target price may be impeded by risks related to the subject securities and companies, as well as general market and economic conditions.

Equity Ratings Distribution

Buy	Trading Buy	Hold	Sell
72.36%	13.57%	14.07%	0.00%

* Based on recommendations in the last 12-months (as of June 30, 2015)

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