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Company Update



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Coway (021240)

A solid investment amid macro instability

- With investment sentiment in general deteriorating sharply following the Brexit vote, we view Coway as a solid alternative investment.
- We expect 2Q results to beat forecasts, boosting investment sentiment for the firm.
- Shares have yet to reflect the growth potential from a partnership with Haier Electronics (China).

WHAT'S THE STORY?

Top pick amid uncertainty: Market interest in Coway is likely to rise, because the stock is a good alternative investment that should provide relative stability amidst the sharp deterioration in investment sentiment that has come on the heels of the UK's vote to Brexit. We see Coway as a good bet while the market outlook remains uncertain. The firm has enjoyed stable growth thanks to its dominance of the domestic market and unique business model. Our target price of KRW135,000 (based on a DCF valuation that assumes a WACC of 5.9% and terminal growth of 0.5%; equivalent to 27x 2016 P/E), factors in the firm's high earnings visibility—which is barely affected by the external environment—excellent cash-generating ability, and a dividend yield of around 3%.

2Q preview: We now expect Coway to post 2Q results showing sales and operating profit up 15% and 19% y-y, respectively (and 2% and 6% q-q), to KRW637.8b and KRW131.3b, both figures beating consensus by 3%. We estimate that growth in rental revenue will stay solid at 5.5% y-y. Results should show that growth momentum improved q-q in 2Q, given that: 1) the water purifier rental contract expirations were concentrated in 1Q; and 2) mattress and air-purifier rentals have been solid. We expect outright sales to have grown 30% y-y in 2Q, continuing an uptrend that began in 3Q15. Exports should also have remained strong at 50% y-y, as the firm's US and Malaysian subsidiaries have likely seen sales grow robustly (in the region of 30% y-y) and orders from a new ODM partner have been increasing.

Shares yet to price in tie-up with Chinese partner: To expedite Coway's overseas expansion, the firm on May 31 signed an MOU with Haier Electronics (China). An upcoming deal should allow Coway to sell premium water purifiers in China under its own brand. However, as the details will remain undisclosed until a contract is finalized later this year, Coway shares have yet to reflect related anticipation. We believe cooperation with Haier Electronics is an optimal China strategy if Coway can retain its brand and technology while leveraging the distribution strength of its new Chinese partner. We thus believe Coway will garner more attention before all of the details of the deal are revealed

SUMMARY FINANCIAL DATA

	2015	2016E	2017E	2018E
Revenue (KRWb)	2,315	2,560	2,766	2,990
Net profit (adj) (KRWb)	343	388	426	463
EPS (adj) (KRW)	4,492	5,071	5,558	6,037
EPS (adj) growth (% y-y)	39.3	12.9	9.6	8.6
EBITDA margin (%)	29.8	29.7	30.0	30.3
ROE (%)	30.1	29.2	28.2	27.1
P/E (adj) (x)	22.7	20.1	18.4	16.9
P/B (x)	6.6	5.7	5.0	4.5
EV/EBITDA (x)	11.2	10.2	9.2	8.3
Dividend yield (%)	2.7	3.1	3.4	3.7

Source: Company data, Samsung Securities estimates

AT A GLANCE

SELL HOLD BUY

Target price KRW135,000 (32.4%)

Current price KRW102,000

Market cap	KRW7.9t/USD6.7b
Shares (float)	77,124,796 (65.4%)
52-week high/low	KRW113,000/KRW79,200
Avg daily trading value (60-day)	KRW15.3b/ USD12.9m

ONE-YEAR PERFORMANCE

	1M	6M	12M
Coway (%)	2.0	13.7	14.0
Vs Kospi (%pts)	2.7	17.6	23.5

KEY CHANGES

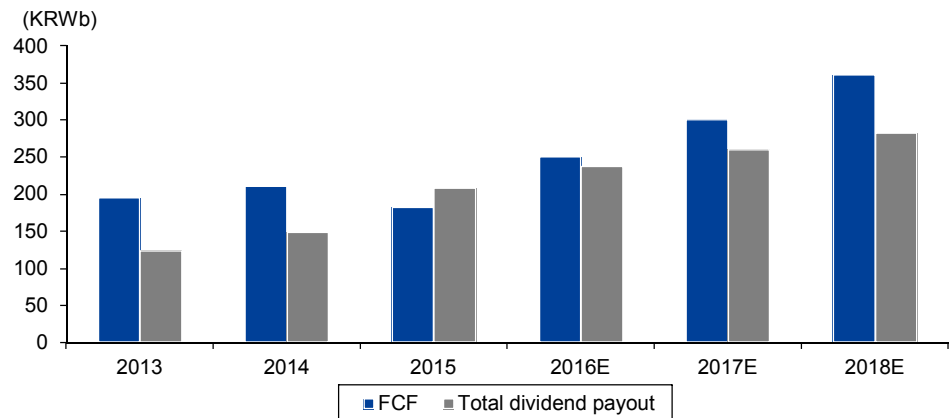
(KRW)	New	Old	Diff
Recommend.	BUY	BUY	
Target price	135,000	135,000	0.0%
2016E EPS	5,071	5,025	0.9%
2017E EPS	5,558	5,503	1.0%

SAMSUNG vs THE STREET

No of estimates	14
Target price	125,154
Recommendation	3.9

BUY★★: 5 / BUY: 4 / HOLD: 3 / SELL: 2 / SELL★★: 1

Free cash flow and total dividend payout



Source: Company data, Samsung Securities estimates

DCF valuation

(KRWb)	2015	2016E	2017E	2018E	2019E	2020E	2021E	2022E	2023E	2024E	2025E	2026E
EBIT	463	524	574	622	678	520	546	573	601	632	663	696
Tax	114	130	143	155	168	129	136	142	150	157	165	173
Capex	329	342	356	356	356	0	0	0	0	0	0	0
Change in working capital	54	25	19	21	23	(89)	(89)	(89)	(90)	(90)	(91)	(91)
Depreciation	220	227	249	275	304	49	49	49	50	50	50	50
Amortization	8	8	8	8	8	3	3	3	3	3	3	3
Free cash flow	195	261	312	373	442	531	551	572	595	618	642	668
Terminal value	11,614											
Terminal growth (%)	0.5%											
NPV of FCF	3,440											
Present value of terminal value	6,450											
Enterprise value	9,890											
Equity value (adjusted)**	10,706											
Shares outstanding	77,125											
Fair value per share (KRW)	138,814											
Current share price (KRW)*	102,000											
Upside (%)	36.1%											

Note: *As of May 3 close;

**Reflects a one-month adjustment to end-2016 discount rate

Source: Company data, Samsung Securities estimates

Valuation summary

Year-end	Sales	Op prof	Pre-tax prof	Net prof	EPS	Chg	P/E	P/B	ROE	EV/EBITDA	Net debt
Dec 31	(KRWb)	(KRWb)	(KRWb)	(KRWb)	(KRW)	(% y-y)	(x)	(x)	(%)	(x)	(KRWb)
2013	2,118	339	327	245	3,222	47.5	31.7	9.1	28.4	14.4	83
2014	2,160	364	332	250	3,225	0.1	31.6	7.9	25.2	13.4	12
2015	2,315	463	454	343	4,492	39.3	22.7	6.6	30.1	11.2	(38)
2016E	2,560	524	518	388	5,071	12.9	20.1	5.7	29.2	10.2	(107)
2017E	2,766	574	568	426	5,558	9.6	18.4	5.0	28.2	9.2	(199)
2018E	2,990	622	617	463	6,037	8.6	16.9	4.5	27.1	8.3	(330)

Source: Company data, Samsung Securities estimates

Results and forecasts

	1Q15	2Q15	3Q15	4Q15	1Q16	2Q16E	3Q16E	4Q16E	2015P	2016E	2017E	2018E
Earnings summary												
(KRWb)	548.2	555.3	580.4	631.3	623.7	637.8	631.4	667.5	2,315.2	2,560.3	2,765.8	2,990.1
Sales	373.0	384.7	402.3	426.4	416.6	435.4	438.8	450.2	1,586.4	1,741.0	1,894.6	2,048.2
Gross profit	100.3	110.5	123.9	128.6	123.6	131.3	134.7	134.9	463.3	524.4	573.8	622.1
Operating profit	101.1	108.9	121.7	122.7	125.3	128.4	131.8	132.1	454.5	517.6	567.7	616.9
Pre-tax profit	77.6	82.7	92.4	90.5	95.2	95.9	98.4	98.6	343.1	388.2	425.7	462.7
Net profit												
Margins (%)	68.0	69.3	69.3	67.5	66.8	68.3	69.5	67.4	68.5	68.0	68.5	68.5
Gross profit	18.3	19.9	21.4	20.4	19.8	20.6	21.3	20.2	20.0	20.5	20.7	20.8
Operating profit	18.4	19.6	21.0	19.4	20.1	20.1	20.9	19.8	19.6	20.2	20.5	20.6
Pre-tax profit	14.1	14.9	15.9	14.3	15.3	15.0	15.6	14.8	14.8	15.2	15.4	15.5
Net profit												
Chg (% y-y)	2.5	(0.3)	10.4	16.3	13.8	14.8	8.8	5.7	7.2	10.6	8.0	8.1
Sales	5.8	4.3	12.6	20.2	11.7	13.2	9.1	5.6	10.6	9.7	8.8	8.1
Gross profit	11.1	13.7	30.1	57.4	23.2	18.8	8.7	4.9	27.1	13.2	9.4	8.4
Operating profit	14.3	25.9	41.6	71.5	23.9	17.9	8.3	7.6	36.7	13.9	9.7	8.7
Pre-tax profit	17.4	24.8	44.5	69.6	22.7	15.9	6.6	9.0	37.4	13.1	9.7	8.7
Net profit												
Chg (% q-q)	1.0	1.3	4.5	8.8	(1.2)	2.3	(1.0)	5.7				
Sales	5.2	3.1	4.6	6.0	(2.3)	4.5	0.8	2.6				
Gross profit	22.8	10.1	12.2	3.8	(3.9)	6.2	2.6	0.2				
Operating profit	41.3	7.8	11.7	0.8	2.1	2.5	2.6	0.2				
Pre-tax profit	45.4	6.6	11.7	(2.0)	5.2	0.7	2.6	0.2				
Net profit												
Sales breakdown												
Household electronics	439.3	457.9	481.3	504.3	495.0	514.4	517.3	529.1	1,882.9	2,055.8	2,187.2	2,322.5
Outright sales	30.0	41.4	45.6	54.2	50.5	53.8	55.6	57.3	171.2	217.2	247.9	281.9
Rental	363.3	371.2	376.4	380.2	380.1	391.6	393.3	402.9	1,491.1	1,567.9	1,639.2	1,715.0
Membership	46.0	45.4	44.5	43.7	42.9	44.0	43.2	42.3	179.6	172.4	172.4	172.4
Financial lease			14.8	26.1	21.5	25.0	25.2	26.5	40.9	98.2	127.7	153.2
Exports	33.0	39.0	35.8	41.4	56.7	58.5	50.1	51.1	149.3	216.5	259.7	311.7
Cosmetics	23.1	21.1	18.6	20.2	20.1	21.1	19.5	18.2	83.1	78.9	86.8	95.5
Other (water treatment)	10.6	9.4	10.0	16.1	5.8	7.6	8.0	15.5	46.1	36.9	36.9	36.9
Consolidated other	42.1	27.9	34.7	49.3	46.1	36.2	36.4	53.6	194.9	172.3	195.2	223.5
Chg (% y-y)												
Household electronics	6.2	6.5	11.6	16.6	12.7	12.3	7.5	4.9	10.3	9.2	6.4	6.2
Outright sales	8.8	10.7	43.5	102.9	68.2	30.0	22.0	5.7	38.6	26.9	14.1	13.7
Rental	6.1	7.0	6.7	6.0	4.6	5.5	4.5	5.9	6.5	5.2	4.5	4.6
Membership	4.9	(0.8)	(5.0)	(6.7)	(6.8)	(3.0)	(3.0)	(3.1)	(2.0)	(4.0)	0.0	0.0
Financial lease							70.0	1.7			30.0	20.0
Exports	(27.0)	(30.0)	8.5	23.9	71.8	50.0	40.0	23.3	(10.8)	45.0	20.0	20.0
Cosmetics	10.5	(5.3)	8.3	1.1	(13.1)	0.0	5.0	(10.2)	3.3	(5.0)	10.0	10.0
Other (water treatment)	(28.2)	(38.6)	(31.7)	18.1	(45.3)	(20.0)	(20.0)	(3.3)	(21.0)	(20.0)	0.0	0.0
Consolidated other	4.7	(17.1)	17.7	13.6	9.4	30.0	5.0	8.8	32.9	(11.6)	13.3	14.5
Portion of total sales (%)												
Household electronics	80.1	82.5	82.9	79.9	79.4	80.7	81.9	79.3	79.9	80.3	79.1	77.7
Outright sales	5.5	7.5	7.9	8.6	8.1	8.4	8.8	8.6	7.3	8.5	9.0	9.4
Rental	66.3	66.8	64.9	60.2	60.9	61.4	62.3	60.4	63.3	61.2	59.3	57.4
Membership	8.4	8.2	7.7	6.9	6.9	6.9	6.8	6.3	7.6	6.7	6.2	5.8
Financial lease			2.6	4.1	3.4	3.9	4.0	4.0	1.7	3.8	4.6	5.1
Exports	6.0	7.0	6.2	6.6	9.1	9.2	7.9	7.7	6.3	8.5	9.4	10.4
Cosmetics	4.2	3.8	3.2	3.2	3.2	3.3	3.1	2.7	3.5	3.1	3.1	3.2
Other (water treatment)	1.9	1.7	1.7	2.5	0.9	1.2	1.3	2.3	2.0	1.4	1.3	1.2
Consolidated other	7.7	5.0	6.0	7.8	7.4	5.7	5.8	8.0	8.3	6.7	7.1	7.5

Source: Company data, Samsung Securities estimates

Income statement

Year-end Dec 31 (KRWb)	2014	2015	2016E	2017E	2018E
Sales	2,160	2,315	2,560	2,766	2,990
Cost of goods sold	727	729	819	871	942
Gross profit	1,434	1,586	1,741	1,895	2,048
Gross margin (%)	66.4	68.5	68.0	68.5	68.5
SG&A expenses	1,069	1,123	1,217	1,321	1,426
Operating profit	364	463	524	574	622
Operating margin (%)	16.9	20.0	20.5	20.7	20.8
Non-operating gains (losses)	(32)	(9)	(7)	(6)	(5)
Financial profit	3	1	2	2	4
Financial costs	12	4	3	3	3
Equity-method gains (losses)	0	0	0	0	0
Other	(23)	(6)	(5)	(5)	(5)
Pre-tax profit	332	454	518	568	617
Taxes	83	111	129	142	154
Effective tax rate (%)	24.9	24.5	25.0	25.0	25.0
Profit from continuing operations	250	343	388	426	463
Profit from discontinued operations	0	0	0	0	0
Net profit	250	343	388	426	463
Net margin (%)	11.6	14.8	15.2	15.4	15.5
Net profit (controlling interests)	250	343	388	426	463
Net profit (non-controlling interests)	(0)	(0)	(0)	(0)	(0)
EBITDA	578	691	759	830	905
EBITDA margin (%)	26.8	29.8	29.7	30.0	30.3
EPS (parent-based) (KRW)	3,237	4,449	5,034	5,521	5,999
EPS (consolidated) (KRW)	3,237	4,449	5,034	5,520	5,999
Adjusted EPS (KRW)*	3,225	4,492	5,071	5,558	6,037

Cash flow statement

Year-end Dec 31 (KRWb)	2014	2015	2016E	2017E	2018E
Cash flow from operations	537	513	620	685	747
Net profit	250	343	388	426	463
Non-cash profit and expenses	240	231	263	286	313
Depreciation	206	220	227	249	275
Amortization	8	8	8	8	8
Other	27	3	28	29	30
Changes in A/L from operating activities	47	(61)	(31)	(26)	(28)
Cash flow from investments	(299)	(329)	(342)	(356)	(356)
Change in tangible assets	(296)	(317)	(342)	(356)	(356)
Change in financial assets	0	1	0	0	0
Other	(3)	(13)	0	0	0
Cash flow from financing	(328)	(213)	(208)	(229)	(256)
Change in debt	(163)	(77)	0	9	4
Change in equity	0	0	0	0	0
Dividends	(124)	(148)	(208)	(238)	(260)
Other	(42)	12	0	(0)	0
Change in cash	(91)	(31)	70	100	135
Cash at beginning of year	239	147	116	186	286
Cash at end of year	147	116	186	286	421
Gross cash flow	490	574	651	711	776
Free cash flow	211	182	251	301	361

Note: * Excluding one off items, ** Fully diluted, excluding one-off items

*** From companies subject to equity-method valuation

Source: Company data, Samsung Securities estimates

Balance sheet

Year-end Dec 31 (KRWb)	2014	2015	2016E	2017E	2018E
Current assets	597	653	755	880	1,041
Cash & equivalents	147	116	186	286	421
Accounts receivable	229	283	313	339	366
Inventories	62	70	77	83	90
Other current assets	158	184	178	171	164
Fixed assets	1,025	1,122	1,207	1,284	1,335
Investment assets	81	78	78	78	78
Tangible assets	675	700	785	862	913
Intangible assets	171	169	169	169	169
Other long-term assets	98	176	176	176	176
Total assets	1,622	1,775	1,962	2,164	2,376
Current liabilities	526	473	480	493	503
Accounts payable	59	60	66	71	77
Short-term debt	16	8	8	9	9
Other current liabilities	451	405	406	413	417
Long-term liabilities	56	64	64	64	64
Bonds & long-term debt	1	8	8	8	8
Other long-term liabilities	55	56	56	56	56
Total liabilities	582	537	544	558	567
Owners of parent equity	1,039	1,237	1,418	1,606	1,808
Capital stock	41	41	41	41	41
Capital surplus	126	127	127	127	127
Retained earnings	986	1,177	1,357	1,545	1,748
Other	(114)	(108)	(108)	(108)	(108)
Non-controlling interests' equity	1	1	1	1	1
Total equity	1,039	1,238	1,418	1,606	1,809
Net debt	12	(38)	(107)	(199)	(330)

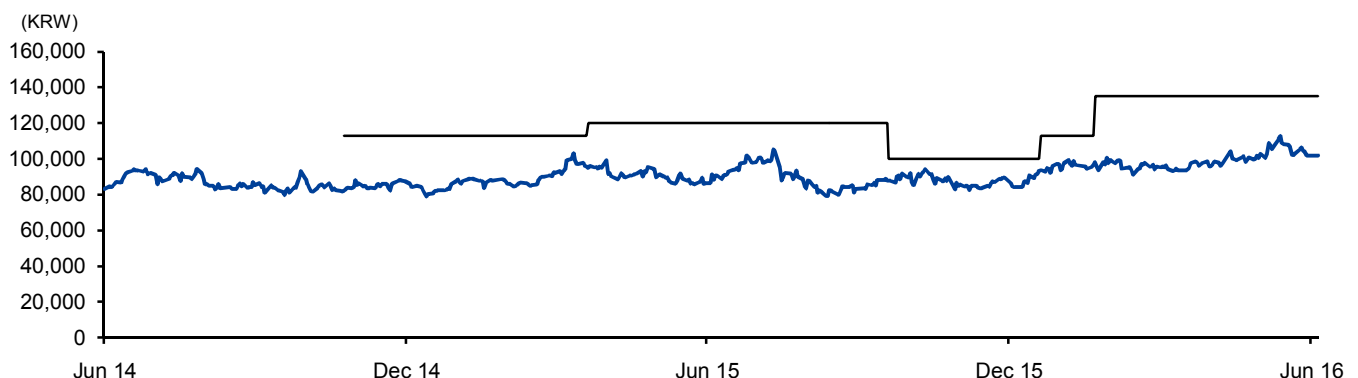
Financial ratios

Year-end Dec 31	2014	2015	2016E	2017E	2018E
Growth (%)					
Sales	2.0	7.2	10.6	8.0	8.1
Operating profit	7.5	27.1	13.2	9.4	8.4
Net profit	11.6	14.8	15.2	15.4	15.5
Adjusted EPS**	0.1	39.3	12.9	9.6	8.6
Per-share data (KRW)					
EPS (parent-based)	3,237	4,449	5,034	5,521	5,999
EPS (consolidated)	3,237	4,449	5,034	5,520	5,999
Adjusted EPS**	3,225	4,492	5,071	5,558	6,037
BVPS	12,934	15,465	17,802	20,239	22,866
DPS (common)	2,000	2,800	3,200	3,500	3,800
Valuations (x)					
P/E***	31.6	22.7	20.1	18.4	16.9
P/B***	7.9	6.6	5.7	5.0	4.5
EV/EBITDA	13.4	11.2	10.2	9.2	8.3
Ratios (%)					
ROE	25.2	30.1	29.2	28.2	27.1
ROA	15.2	20.2	20.8	20.6	20.4
ROIC	22.8	31.1	31.3	31.6	32.3
Payout ratio	59.4	60.6	61.2	61.1	61.0
Dividend yield (common)	2.0	2.7	3.1	3.4	3.7
Net debt to equity	1.1	(3.0)	(7.6)	(12.4)	(18.2)
Interest coverage (x)	31.6	106.8	173.6	180.8	183.7

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Target price changes in past two years



Rating changes in past two years

Date	2014/6/27	11/19	2015/4/16	10/15	2016/1/15	2/17
Recommendation	BUY	BUY	BUY	BUY	BUY	BUY
Target price (KRW)	46,000	113,000	120,000	100,000	113,000	135,000

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

Percentage of ratings in 12 months prior to Mar 31, 2016

BUY (69.8%) | HOLD (30.2%) | SELL (0%)

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