

Dongwon Industries

(006040 KS)

Tuna prices are rising

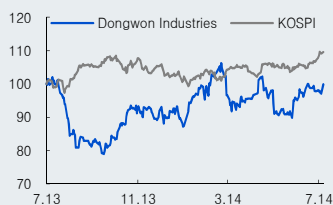
Food & Beverage

Earnings Preview
August 5, 2014

(Maintain)	Buy
Target Price (12M, W)	410,000
Share Price (8/4/14, W)	339,500
Expected Return	21%

OP (14F, Wbn)	87
Consensus OP (14F, Wbn)	130
EPS Growth (14F, %)	-22.7
Market EPS Growth (14F, %)	14.6
P/E (14F, x)	19.3
Market P/E (14F, x)	12.4
KOSPI	2,080.42
Market Cap (Wbn)	1,142
Shares Outstanding (mn)	3
Free Float (%)	40.2
Foreign Ownership (%)	3.6
Beta (12M)	-0.56
52-Week Low	268,500
52-Week High	361,000

(%)	1M	6M	12M
Absolute	2.4	8.8	0.1
Relative	-1.1	-1.3	-7.4



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2Q preview: Earnings likely hurt by soft tuna prices

For 2Q, we forecast Dongwon Industries to post an 8.2% YoY decline in revenue and a 50.5% YoY slump in operating profit, under consolidated K-IFRS. The parent company (tuna fishing) likely remained in the red, weighed down by weaker catches and lower tuna prices. StarKist (canned tuna producer) likely saw profits grow, thanks to the input of cheaper tuna (inventory) purchased in late 2013 and early 2014. We believe StarKist has held its US market share steady at 40%.

Tuna prices are picking up

We expect earnings to recover after bottoming in 1H, driven by the following catalysts:

1) Rising tuna prices should lift parent earnings. From 3Q13 to April 2014, tuna prices plummeted due to excessive inventory. Since May, however, prices have been visibly turning around, rising to US\$1,750/tonne from an April low of US\$1,180/tonne, as a result of inventory depletion. We expect tuna prices to remain at around US\$1,750-\$1,800/tonne until the end of the year. And despite the fish aggregating device (FAD) ban (July-October), tuna catch volume was up YoY to over 10,000 tonnes in July.

2) The replacement of aged vessels should help improve margins. The company plans to deploy a new longliner in July and another one in August. The new vessels, which have larger storage capacity, boast higher fuel efficiency, and operate at faster speeds, should boost catch volume and efficiency. Two more new vessels are currently under construction and are set to go into operation in 2H15.

Illegal fishing (IUU) issue

In November 2013, the EU designated Korea as a preliminary illegal, unreported, and unregulated (IUU) fishing nation. EU officials conducted an on-site assessment in Korea in June this year, and originally planned to make its final decision on whether to impose sanctions in September. Recently, however, the EU postponed its final decision to January 2015 to give authorities and the industry more time to improve the situation (GPS installation, tougher penalties, etc.). If Korea is designated as an IUU fishing country, it will be banned from exporting fish and fishery products to Europe (exports amount to W100bn annually). In our view, the IUU dispute is a national issue that is being dealt with by both the Korean government and industry officials. We thus think chances of IUU designation are low.

Maintain Buy and TP of W410,000; Profits to begin turning around in 3Q

In 3Q, Dongwon Industries should benefit from a number of positives, including: 1) rising tuna prices, 2) catch growth, 3) deployment of new vessels, and 3) StarKist's solid earnings. While the IUU issue remains an uncertainty, we believe that designation is unlikely, and even if it occurs, the damage is likely to be limited. We reiterate our Buy rating on Dongwon Industries with a target price of W410,000.

FY (Dec.)	12/11	12/12	12/13	12/14F	12/15F	12/16F
Revenue (Wbn)	1,327	1,544	1,444	1,427	1,545	1,614
OP (Wbn)	97	140	111	87	124	142
OP margin (%)	7.3	9.1	7.7	6.1	8.0	8.8
NP (Wbn)	68	103	77	59	87	104
EPS (W)	20,331	30,497	22,794	17,619	25,799	30,786
ROE (%)	15.6	20.0	12.9	9.1	12.2	13.0
P/E (x)	8.3	9.4	13.9	19.3	13.2	11.0
P/B (x)	1.2	1.7	1.7	1.7	1.5	1.4

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. 2Q14 earnings preview

(Wbn, %)

	2Q13	1Q14	2Q14F		Growth	
			KDB Daewoo	Consensus	YoY	QoQ
Revenue	359.5	377.8	330.0	330.0	-8.2	-12.7
Operating profit	44.2	22.4	21.9	21.9	-50.5	-2.4
Pretax profit	40.0	17.4	24.8	24.8	-37.9	42.9
Net profit	28.1	11.1	18.9	18.9	-32.8	69.5
OP margin	12.3	5.9	6.6	6.6	-	-
Net margin	7.8	2.9	5.7	5.7	-	-

Note: Net profit refers to net profit attributable to controlling interests

Source: Company data, KDB Daewoo Securities Research estimates

Table 2. Quarterly and annual earnings

(Wbn, %)

	2013				2014				2013	2014F	2015F
	1Q	2Q	3Q	4Q	1Q	2QF	3QF	4QF	Annual	Annual	Annual
Revenue	405	359	369	311	378	330	384	335	1,444	1,427	1,545
Operating profit	34	44	30	3	22	22	32	11	111	87	124
Pretax profit	27	40	30	9	17	25	31	8	106	81	116
Net profit	29	28	10	10	11	19	23	6	77	59	87
OP margin	8.3	12.3	8.2	1.0	5.9	6.6	8.4	3.2	7.7	6.1	8.0
Net margin	7.1	7.8	2.7	3.2	2.9	5.7	6.0	1.8	5.3	4.2	5.6
Revenue growth	0.5	-8.5	-6.7	-11.9	-6.6	-8.2	4.2	7.8	-6.5	-1.1	8.2
OP growth	-5.1	-17.0	-16.6	-78.3	-33.5	-50.5	6.7	240.9	-20.3	-21.5	41.6
Pretax profit growth	-16.2	-14.5	-14.8	-49.4	-34.8	-37.9	0.3	-13.8	-19.8	-24.1	43.4
Net profit growth	28.9	-20.7	-65.9	-37.9	-61.4	-32.8	136.1	-38.9	-25.3	-22.7	46.4

Note: Net profit refers to net profit attributable to controlling interests

Source: Company data, KDB Daewoo Securities Research estimates

Table 3. Earnings forecast revisions

(Wbn, %)

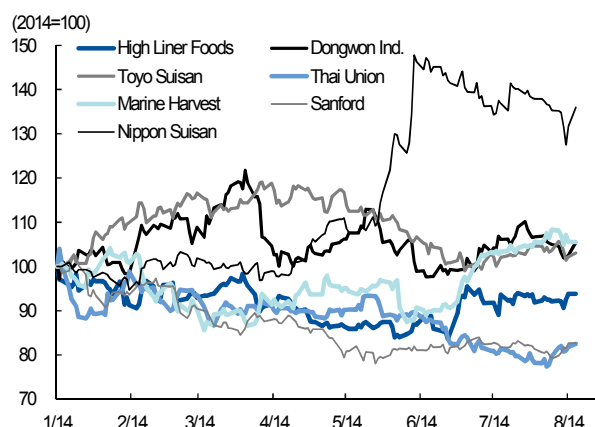
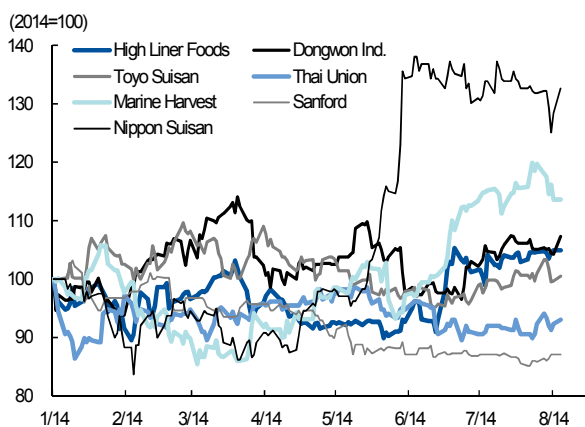
	Previous		Revised		% chg.		Notes
	14F	15F	14F	15F	14F	15F	
	Revenue	1,442	1,527	1,427	1,545	-1.0	
Operating profit	90	109	87	124	-2.9	13.5	
Pretax profit	83	100	81	116	-2.2	15.7	
Net profit	61	75	59	87	-2.1	15.7	
OP margin	6.2	7.1	6.1	8.0	-	-	
Net margin	4.2	4.9	4.2	5.6	-	-	

Note: Net profit refers to net profit attributable to controlling interests

Source: Company data, KDB Daewoo Securities Research estimates

Figure 1. Global peers' share performances

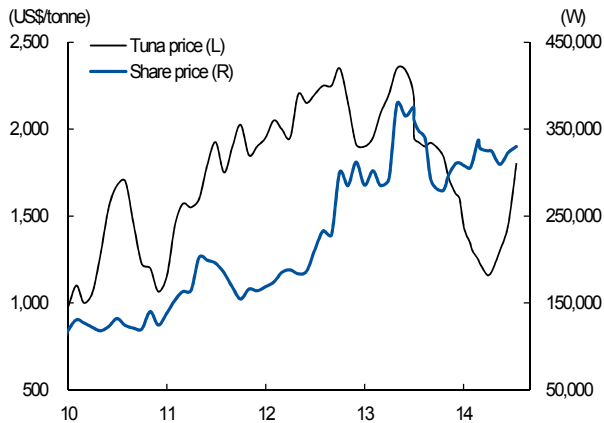
Figure 2. Share performances relative to the market



Source: Bloomberg, KDB Daewoo Securities Research

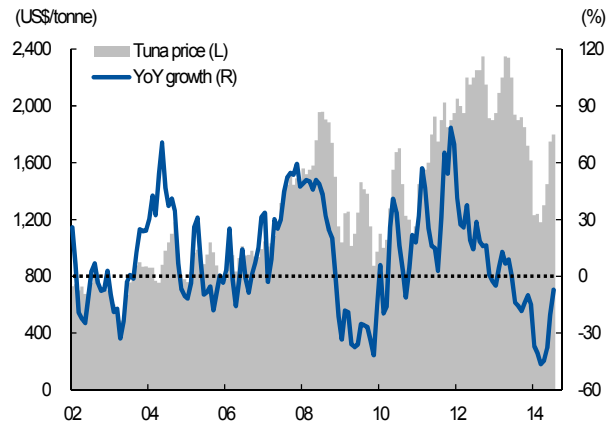
Source: Bloomberg, KDB Daewoo Securities Research

Figure 3. Tuna price: A key determinant of earnings



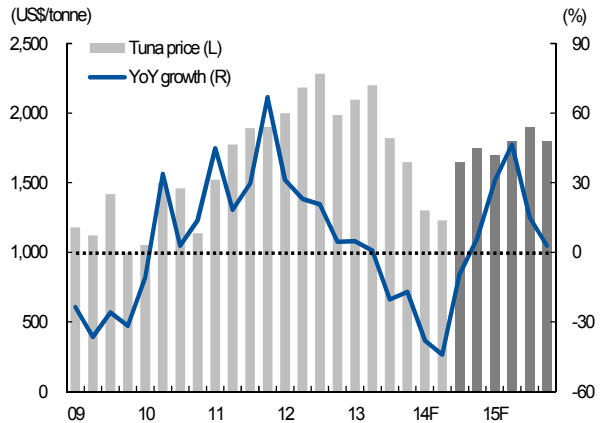
Source: Company data, KDB Daewoo Securities Research

Figure 4. Tuna price bottomed out after April



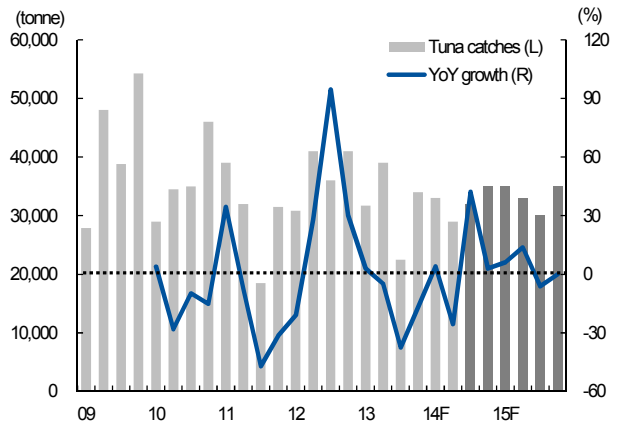
Source: Company data, KDB Daewoo Securities Research

Figure 5. Tuna price turning around in 2H14



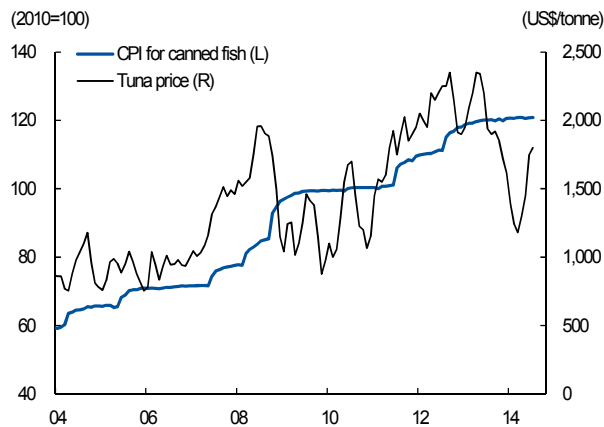
Source: Company data, KDB Daewoo Securities Research

Figure 6. Tuna catches



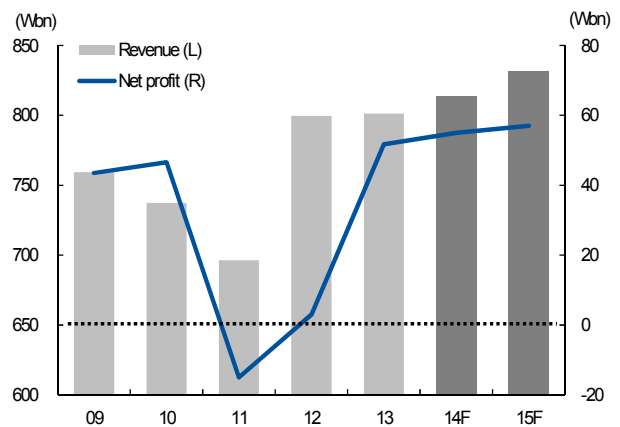
Source: Company data, KDB Daewoo Securities Research

Figure 7. Tuna price vs. CPI for canned fish



Source: Company data, Statistics Korea, KDB Daewoo Securities Research

Figure 8. StarKist's earnings have stabilized



Source: Company data, KDB Daewoo Securities Research

Dongwon Industries (006040 KS/Buy/TP: W410,000)

Comprehensive Income Statement (Summarized)

(Wbn)	12/13	12/14F	12/15F	12/16F
Revenue	1,444	1,427	1,545	1,614
Cost of Sales	1,204	1,209	1,280	1,325
Gross Profit	240	218	265	289
SG&A Expenses	129	131	141	147
Operating Profit (Adj)	111	87	124	142
Operating Profit	111	87	124	142
Non-Operating Profit	-5	-6	-8	-6
Net Financial Income	-18	-8	-9	-6
Net Gain from Inv in Associates	0	0	0	0
Pretax Profit	106	81	116	136
Income Tax	22	23	31	34
Profit from Continuing Operations	84	58	85	102
Profit from Discontinued Operations	0	0	0	0
Net Profit	84	58	85	102
Controlling Interests	77	59	87	104
Non-Controlling Interests	7	-1	-2	-2
Total Comprehensive Profit	79	61	85	102
Controlling Interests	72	63	88	105
Non-Controlling Interests	7	-2	-3	-4
EBITDA	175	149	189	210
FCF (Free Cash Flow)	19	6	43	93
EBITDA Margin (%)	12.1	10.4	12.2	13.0
Operating Profit Margin (%)	7.7	6.1	8.0	8.8
Net Profit Margin (%)	5.3	4.1	5.6	6.4

Statement of Financial Condition (Summarized)

(Wbn)	12/13	12/14F	12/15F	12/16F
Current Assets	612	637	692	753
Cash and Cash Equivalents	31	11	32	74
AR & Other Receivables	116	125	132	138
Inventories	364	393	414	423
Other Current Assets	101	108	114	118
Non-Current Assets	666	695	730	739
Investments in Associates	13	14	15	15
Property, Plant and Equipment	506	537	568	577
Intangible Assets	70	70	73	71
Total Assets	1,278	1,332	1,422	1,492
Current Liabilities	301	311	322	297
AP & Other Payables	56	60	64	67
Short-Term Financial Liabilities	197	198	203	173
Other Current Liabilities	48	53	55	57
Non-Current Liabilities	345	349	353	356
Long-Term Financial Liabilities	277	275	275	275
Other Non-Current Liabilities	68	74	78	81
Total Liabilities	646	660	675	654
Controlling Interests	631	672	749	842
Capital Stock	17	17	17	17
Capital Surplus	50	50	50	50
Retained Earnings	589	628	705	798
Non-Controlling Interests	1	0	-2	-4
Stockholders' Equity	632	672	747	838

Cash Flows (Summarized)

(Wbn)	12/13	12/14F	12/15F	12/16F
Cash Flows from Op Activities	109	92	138	168
Net Profit	84	58	85	102
Non-Cash Income and Expense	91	87	105	108
Depreciation	62	60	64	66
Amortization	2	2	2	2
Others	27	25	39	40
Chg in Working Capital	-15	-36	-21	-7
Chg in AR & Other Receivables	-9	-2	-6	-5
Chg in Inventories	37	-30	-22	-8
Chg in AP & Other Payables	-15	-6	2	2
Income Tax Paid	-51	-17	-31	-34
Cash Flows from Inv Activities	63	-86	-99	-72
Chg in PP&E	-88	-86	-95	-75
Chg in Intangible Assets	0	0	0	0
Chg in Financial Assets	136	-5	-4	-3
Others	15	5	0	6
Cash Flows from Fin Activities	-160	-29	-18	-53
Chg in Financial Liabilities	-111	0	5	-30
Chg in Equity	13	0	0	0
Dividends Paid	-11	-10	-10	-10
Others	-51	-19	-13	-13
Increase (Decrease) in Cash	11	-20	20	43
Beginning Balance	20	31	11	32
Ending Balance	31	11	32	74

Source: Company data, KDB Daewoo Securities Research estimates

Forecasts/Valuations (Summarized)

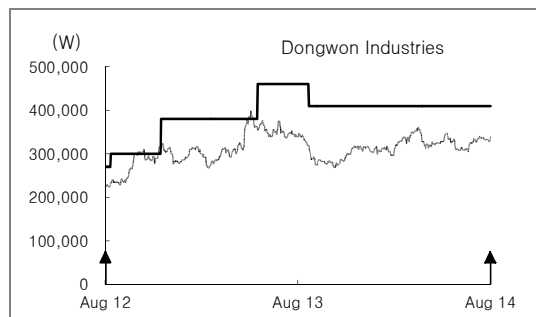
	12/13	12/14F	12/15F	12/16F
P/E (x)	13.9	19.3	13.2	11.0
P/CF (x)	6.1	7.9	6.0	5.4
P/B (x)	1.7	1.7	1.5	1.4
EV/EBITDA (x)	8.3	10.4	8.0	6.9
EPS (W)	22,794	17,619	25,799	30,786
CFPS (W)	52,008	43,087	56,424	62,296
BPS (W)	187,471	199,882	222,681	250,467
DPS (W)	3,000	3,000	3,000	3,000
Payout ratio (%)	12.0	17.4	11.9	9.9
Dividend Yield (%)	0.9	0.9	0.9	0.9
Revenue Growth (%)	-6.5	-1.2	8.3	4.5
EBITDA Growth (%)	-13.8	-14.9	26.8	11.1
Operating Profit Growth (%)	-20.7	-21.6	42.5	14.5
EPS Growth (%)	-25.3	-22.7	46.4	19.3
Accounts Receivable Turnover (x)	14.9	13.4	13.6	13.6
Inventory Turnover (x)	3.8	3.8	3.8	3.9
Accounts Payable Turnover (x)	28.9	35.1	34.9	34.4
ROA (%)	6.3	4.4	6.2	7.0
ROE (%)	12.9	9.1	12.2	13.0
ROIC (%)	8.9	6.0	8.2	9.3
Liability to Equity Ratio (%)	102.3	98.2	90.4	78.0
Current Ratio (%)	203.3	204.9	214.9	253.6
Net Debt to Equity Ratio (%)	60.9	59.5	51.0	36.4
Interest Coverage Ratio (x)	4.6	6.9	9.6	11.4

APPENDIX 1

Important Disclosures & Disclaimers

2-Year Rating and Target Price History

Company (Code)	Date	Rating	Target Price
Dongwon Industries (006040)	08/25/2013	Buy	410,000
	05/20/2013	Buy	460,000
	11/18/2012	Buy	380,000
	08/15/2012	Buy	300,000
	07/09/2012	Buy	270,000



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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