

SFA Engineering

(056190 KQ)

Pursuing both growth and stability

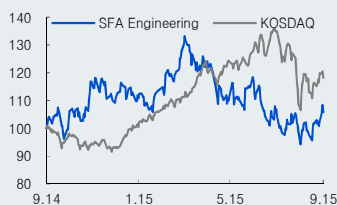
Technology

Company Update
September 24, 2015

(Maintain)	Buy
Target Price (12M, W)	60,000
Share Price (09/23/15, W)	45,150
Expected Return	33%

OP (15F, Wbn)	61
Consensus OP (15F, Wbn)	56
EPS Growth (15F, %)	7.6
Market EPS Growth (15F, %)	23.5
P/E (15F, x)	18.2
Market P/E (15F, x)	11.1
KOSDAQ	680.28
Market Cap (Wbn)	811
Shares Outstanding (mn)	18
Free Float (%)	50.6
Foreign Ownership (%)	13.9
Beta (12M)	0.40
52-Week Low	40,200
52-Week High	56,800

(%)	1M	6M	12M
Absolute	7.0	-18.8	5.9
Relative	-1.4	-23.6	-10.4



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[Semiconductor]

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Business diversification to aid stability; Back-end process market to promote growth

At a joint conference with STS Semiconductor on September 23rd, SFA Engineering explained its decision to acquire STS, plans for STS's financial normalization, and anticipated synergies. The company said the acquisition will 1) allow it to enjoy the strong growth of the semiconductor back-end market and 2) improve its competitiveness through the semiconductor equipment business. Indeed, with semiconductor tech migration reaching a limit, the back-end process is anticipated to play an increasingly important role. The back-end process market was stagnant until end-2012, but has grown at a CAGR of 5% since 2013. Given SFA Engineering's possession of Korea's largest outsourced semiconductor assembly and testing facility, as well as high-value-added packaging technologies (e.g., bumping, flip-chip, and 16-layer stacking), we expect the company to benefit from the market's growth.

To restore its balance sheet, STS will seek to expand capital, unwind its ties to ailing subsidiaries, and reduce its debt ratio (through partial repayment of debts, lowering interest rates on debts, delaying debt repayment). Creditors have agreed on the company's plan to repay W100bn (financed by a capital increase worth W148.7bn, including SFA's acquisition price of W133.4bn), lower interest rates on its remaining debts of W309.2bn to 2.5% (from 5.3%), and delay repayment for five years. Thanks to capital expansion and debt reduction, the company's equity-to-debt ratio will likely decrease from 629% to 217%. And debt reduction and lower interest rates should lead to a decline in interest expenses (from W22bn to W11bn per year). Stripping away losses related to ailing subsidiaries (W14bn) and affiliate-related expenses (W5bn), the company's margins will likely improve by W30bn per year.

Rising OLED utilization to increase the likelihood of OLED capex

We expect Samsung Display's 3Q earnings to far exceed consensus estimates, as the company's OLED utilization, which stood at around 60% in 1H, has climbed to over 80% in 3Q. The rise in OLED utilization is attributable to 1) robust sales of the Galaxy Note 5, 2) the use of OLED displays in low/mid-end smartphone models (the Galaxy A, E, and J series), and 3) the increased adoption of OLED panels at Chinese makers. Rising OLED utilization should increase the likelihood of OLED capex at Korean as well as Chinese makers.

SFA Engineering is also likely to post solid 3Q earnings. We project new orders of W130bn, including LCD equipment orders from China's CSOT (T2 Phase 2). We see revenue of W145.7bn (+2% QoQ, +18% YoY) and operating profit of W17.9bn (+2% QoQ, +46% YoY). In 4Q, we expect earnings to grow rapidly again, given large-scale capex at Trully (Phase-2) and BOE (B7)

Maintain Buy and TP of W60,000

We maintain our Buy rating and target price of W60,000 on SFA Engineering. The stock is trading at a 12-month forward P/E of 13.5x (based on an EPS of W3,353, which excludes STS Semiconductor's earnings). The value of the company's operations stands at only W510bn (vs. cash & cash equivalents of W177.3bn and a W142bn stake in STS Semiconductor).

FY (Dec.)	12/12	12/13	12/14	12/15F	12/16F	12/17F
Revenue (Wbn)	507	479	415	548	643	785
OP (Wbn)	70	65	46	61	75	94
OP margin (%)	13.8	13.6	11.1	11.1	11.7	12.0
NP (Wbn)	71	63	41	44	67	82
EPS (W)	3,972	3,514	2,301	2,475	3,744	4,583
ROE (%)	19.6	15.1	8.8	9.1	12.8	14.0
P/E (x)	11.9	11.7	21.6	18.2	12.1	9.9
P/B (x)	2.0	1.6	1.8	1.6	1.4	1.3

Note: 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. Results of STS Semiconductor’s discussions with creditors

	Plans	Notes
Debt	Repay debt of W100bn within one year of acquisition by SFA	Debt to decrease from W409.2bn to W309.2bn(*)
Interest rates	Decrease weighted average interest rate on debts from 5.3% to 2.5%	Annual interest expenses to fall W11bn
Additional support	SFA could inject W10-20bn in additional funds if STS’s financial structure is still weak after 3 years	As the majority shareholder, SFA Engineering has the right to manage STS’s debt; Maximum additional support is W20bn
Maturity	Extended 5 years	Cash flow risk over the next 5 years to be reduced

Notes: (*) Includes debt and guarantee obligation for affiliates; Does not reflect SFA’s investment of W59.7bn from convertible bonds and bonds with warrants
Source: Company data, KDB Daewoo Securities Research estimates

Table 2. Quarterly and annual earnings

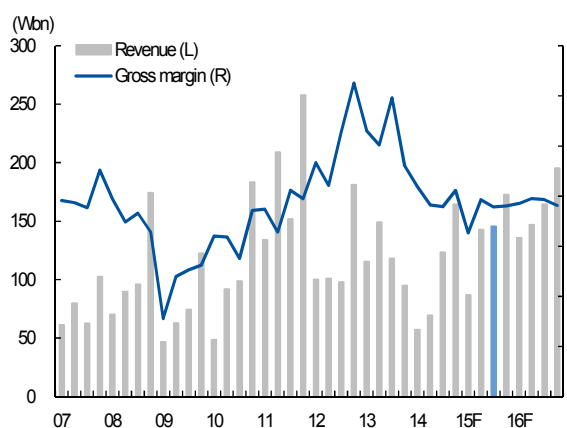
(Wbn, %)

	1Q15	2Q15	3Q15F	4Q15F	1Q16F	2Q16F	3Q16F	4Q16F	2014	2015F	2016F
New orders	92	153	130	147	119	171	112	241	487	522	643
Revenue	87	143	146	173	136	147	164	196	415	548	643
Process & precision	23	42	43	53	45	54	61	79	73	160	240
Material handling systems	58	93	93	109	81	85	92	105	306	354	363
Proportion of revenue	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Process & precision	25.9	29.4	29.3	30.7	33.2	36.9	37.3	40.5	17.6	29.2	37.3
Material handling systems	67.0	65.4	63.9	63.3	59.7	57.9	55.9	53.5	73.6	64.6	56.4
Operating profit	2.5	17.6	17.9	22.8	14.0	14.5	18.6	26.7	45.7	60.8	73.8
OP margin	2.9	12.3	12.3	13.2	10.4	9.8	11.3	13.7	11.0	11.1	11.5
Net profit	3.2	4.8	16.1	20.0	13.1	13.4	16.6	23.1	41.3	44.2	66.2
Net margin	3.7	3.4	11.1	11.6	9.6	9.1	10.1	11.8	9.9	8.1	10.3

Note: Based on consolidated K-IFRS

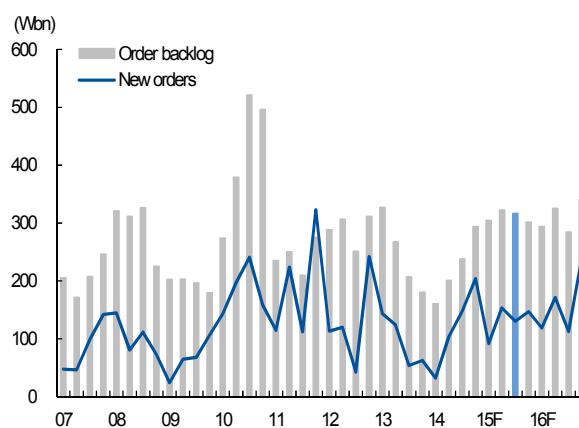
Source: Company data, KDB Daewoo Securities Research estimates

Figure 1. Quarterly revenue and gross margin



Source: Company data, KDB Daewoo Securities Research

Figure 2. New orders and backlog



Source: Company data, KDB Daewoo Securities Research

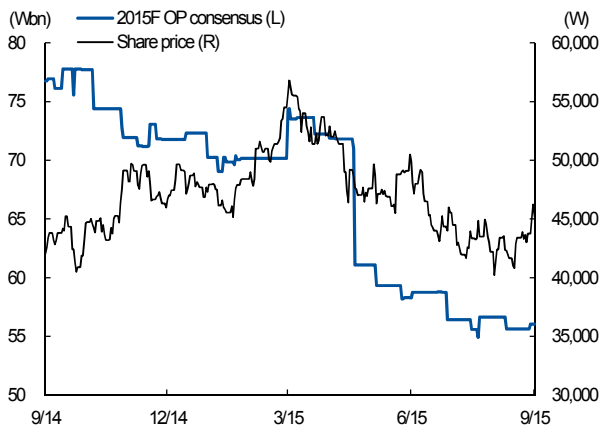
Table 3. Global peer valuation

(Wbn, %)

	Mkt. cap	Revenue		Operating profit		Net profit		ROE		P/E		P/B		EV/EBITDA	
		15F	16F	15F	16F	15F	16F	15F	16F	15F	16F	15F	16F	15F	16F
SFA Engineering	811	548	643	61	75	44	67	9.1	12.8	18.2	12.1	1.6	1.4	6.0	4.3
Wonik IPS	766	646	679	113	119	82	88	20.5	18.3	9.4	8.7	1.7	1.4	5.5	4.8
AP Systems	169	266	315	22	28	16	23	15.7	18.8	9.9	7.7	1.4	1.2	8.0	6.9
KC Tech	349	412	457	39	43	32	36	12.6	12.4	10.8	9.8	1.3	1.1	5.3	4.6
AMAT	21,627	11,339	11,691	2,183	2,397	1,587	1,678	17.7	19.7	12.7	11.0	2.4	2.4	7.9	7.3
TEL	11,175	6,296	6,349	1,020	1,079	691	750	11.3	12.2	14.6	13.2	1.7	1.6	6.5	6.2
Lam Research	12,411	6,982	7,279	1,434	1,550	1,051	1,201	18.4	17.3	10.6	9.7	1.9	1.7	5.8	5.3
Dainippon Screen	1,584	2,474	2,484	204	219	149	156	13.2	11.8	9.9	9.4	1.2	1.1	7.1	6.6
Ulvac	990	1,874	1,937	142	152	102	105	11.7	11.6	9.6	9.7	1.3	1.1	6.0	5.7
Daifuku	1,941	3,182	3,366	190	221	127	148	11.1	12.0	15.2	13.2	1.6	1.5	8.8	7.8
Average								14.2	14.7	11.8	10.5	1.6	1.5	7.2	6.5

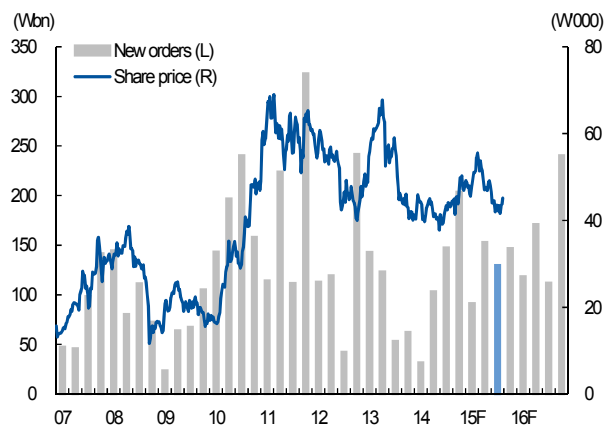
Source: Bloomberg, KDB Daewoo Securities Research estimates

Figure 3. SFA's OP consensus and share price trend



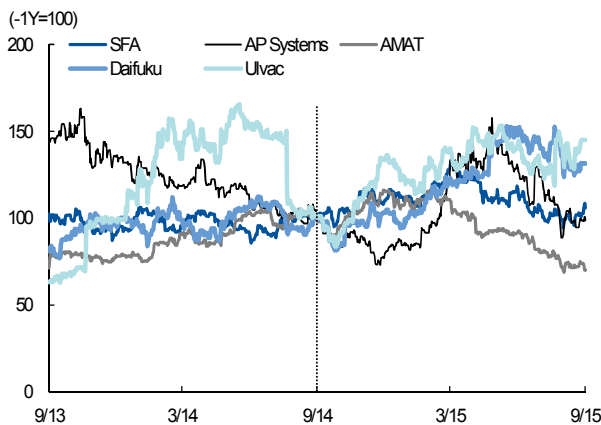
Source: Bloomberg, KDB Daewoo Securities Research

Figure 4. SFA's new orders and share price



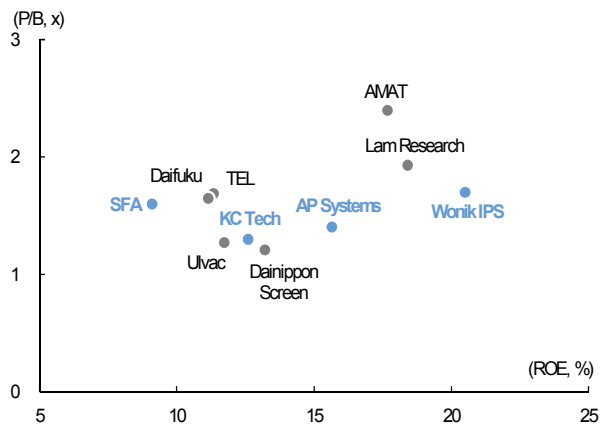
Source: Company data, KDB Daewoo Securities Research

Figure 5. Global peer valuation



Source: Bloomberg, KDB Daewoo Securities Research

Figure 6. P/B-ROE of global peers (2015F)



Source: Bloomberg, KDB Daewoo Securities Research

SFA Engineering (056190 KQ/Buy/TP: W60,000)

Comprehensive Income Statement (Summarized)

(Wbn)	12/14	12/15F	12/16F	12/17F
Revenue	415	548	643	785
Cost of Sales	333	438	514	634
Gross Profit	82	110	129	151
SG&A Expenses	37	49	54	56
Operating Profit (Adj)	46	61	75	94
Operating Profit	46	61	75	94
Non-Operating Profit	6	5	10	10
Net Financial Income	8	10	11	13
Net Gain from Inv in Associates	0	0	0	0
Pretax Profit	52	66	85	104
Income Tax	11	21	18	22
Profit from Continuing Operations	41	44	67	82
Profit from Discontinued Operations	0	0	0	0
Net Profit	41	44	67	82
Controlling Interests	41	44	67	82
Non-Controlling Interests	0	0	0	0
Total Comprehensive Profit	43	44	67	82
Controlling Interests	43	44	67	82
Non-Controlling Interests	0	0	0	0
EBITDA	56	71	86	106
FCF (Free Cash Flow)	17	37	70	87
EBITDA Margin (%)	13.5	13.0	13.4	13.5
Operating Profit Margin (%)	11.1	11.1	11.7	12.0
Net Profit Margin (%)	9.9	8.0	10.4	10.4

Cash Flows (Summarized)

(Wbn)	12/14	12/15F	12/16F	12/17F
Cash Flows from Op Activities	20	45	80	97
Net Profit	41	44	67	82
Non-Cash Income and Expense	15	25	18	20
Depreciation	10	10	11	12
Amortization	0	0	0	0
Others	5	15	7	8
Chg in Working Capital	-35	-9	2	3
Chg in AR & Other Receivables	-32	-7	-8	-17
Chg in Inventories	0	0	-1	-2
Chg in AP & Other Payables	8	3	7	15
Income Tax Paid	-10	-25	-18	-22
Cash Flows from Inv Activities	238	-272	-25	-26
Chg in PP&E	-3	-8	-10	-10
Chg in Intangible Assets	-3	0	0	0
Chg in Financial Assets	243	-264	-15	-16
Others	1	0	0	0
Cash Flows from Fin Activities	-19	-9	-12	-11
Chg in Financial Liabilities	11	3	0	1
Chg in Equity	0	0	0	0
Dividends Paid	-18	-11	-12	-12
Others	-12	-1	0	0
Increase (Decrease) in Cash	240	-236	43	60
Beginning Balance	103	342	106	149
Ending Balance	342	106	149	209

Source: Company data, KDB Daewoo Securities Research estimates

Statement of Financial Condition (Summarized)

(Wbn)	12/14	12/15F	12/16F	12/17F
Current Assets	482	515	588	695
Cash and Cash Equivalents	342	106	149	209
AR & Other Receivables	60	63	72	89
Inventories	6	6	7	8
Other Current Assets	74	340	360	389
Non-Current Assets	131	129	129	128
Investments in Associates	0	0	0	0
Property, Plant and Equipment	104	102	101	99
Intangible Assets	22	22	22	22
Total Assets	613	644	717	823
Current Liabilities	121	129	145	177
AP & Other Payables	55	58	65	81
Short-Term Financial Liabilities	12	15	15	16
Other Current Liabilities	54	56	65	80
Non-Current Liabilities	15	16	18	22
Long-Term Financial Liabilities	0	0	0	0
Other Non-Current Liabilities	15	16	18	22
Total Liabilities	136	145	163	198
Controlling Interests	477	499	554	624
Capital Stock	9	9	9	9
Capital Surplus	27	27	27	27
Retained Earnings	464	485	540	610
Non-Controlling Interests	0	0	0	0
Stockholders' Equity	477	499	554	624

Forecasts/Valuations (Summarized)

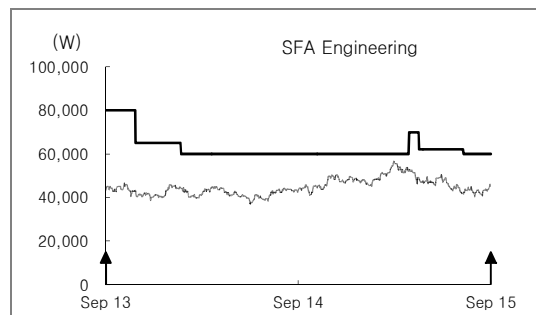
	12/14	12/15F	12/16F	12/17F
P/E (x)	21.6	18.2	12.1	9.9
P/CF (x)	15.9	11.7	9.6	7.9
P/B (x)	1.8	1.6	1.4	1.3
EV/EBITDA (x)	9.6	6.0	4.3	2.8
EPS (W)	2,301	2,475	3,744	4,583
CFPS (W)	3,123	3,869	4,722	5,722
BPS (W)	27,847	29,054	32,117	36,020
DPS (W)	652	700	1,100	1,300
Payout ratio (%)	27.5	27.5	28.6	27.6
Dividend Yield (%)	1.3	1.6	2.4	2.9
Revenue Growth (%)	-13.4	32.0	17.3	22.1
EBITDA Growth (%)	-23.3	26.8	21.1	23.3
Operating Profit Growth (%)	-29.2	32.6	23.0	25.3
EPS Growth (%)	-34.5	7.6	51.3	22.4
Accounts Receivable Turnover (x)	8.7	8.9	9.6	9.9
Inventory Turnover (x)	72.2	97.3	104.5	107.4
Accounts Payable Turnover (x)	7.9	8.3	8.9	9.2
ROA (%)	6.9	7.1	9.9	10.7
ROE (%)	8.8	9.1	12.8	14.0
ROIC (%)	30.3	31.5	45.8	57.7
Liability to Equity Ratio (%)	28.4	29.0	29.3	31.8
Current Ratio (%)	398.7	398.1	405.7	393.5
Net Debt to Equity Ratio (%)	-74.8	-76.4	-79.2	-82.2
Interest Coverage Ratio (x)	534.6	106.5	120.7	144.3

APPENDIX 1

Important Disclosures & Disclaimers

2-Year Rating and Target Price History

Company (Code)	Date	Rating	Target Price
SFA Engineering(056190)	08/03/2015	Buy	60,000
	05/11/2015	Buy	62,000
	04/22/2015	Buy	70,000
	02/14/2014	Buy	60,000
	11/20/2013	Buy	65,000
	08/22/2013	Buy	80,000



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 (◆))

* 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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