

Hyundai E&C

(000720 KS)

Construction

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Rosy growth prospects to overshadow uncertainties

■ Maintain Buy rating with TP of W130,000

We maintain our Buy rating on Hyundai E&C with a target price of W130,000. Hyundai-Kia Automotive Group (HKAG) reached an agreement with Hyundai E&C's creditors to acquire the company for W4.96tr (W127,600 per share). This move has effectively dissipated uncertainties surrounding the constructor's corporate governance. In addition, Hyundai E&C is expected to join the ranks of global engineering companies this year on the back of strong overseas growth momentum.

■ Time to bet on growth prospects, not on near-term uncertainty

Hyundai E&C has focused on its overseas business, rather than on domestic operations. Indeed, overseas orders (worth W12.77tr) drove the company's growth in 2010, representing 69.6% of total orders. Given the importance of overseas markets for Hyundai E&C, it is true that the recent uprisings in Libya darkened the outlook for the company's overseas order performance.

However, since the value of the remaining construction projects in Libya is estimated at only US\$510mn and construction on a 1,400-megawatt steam turbine power plant project in west Tripoli (worth US\$1.36bn) has not started yet (although Hyundai E&C has received US\$200mn in advances), the company's uncollected receivables should be limited at W52bn.

■ Full-swing growth to begin in 2011

HKAG agreed to acquire Hyundai E&C from its creditors at the price of W4.96tr (W127,600 per share). The final contract is scheduled to be executed on March 8th, and HKAG is slated to complete payments within a month. Under the management of HKAG, Hyundai E&C should be able to deliver full-swing growth starting in 2011.

FY	Sales (Wbn)	OP (Wbn)	OP Margin (%)	NP (Wbn)	EPS (W)	EBITDA (Wbn)	FCF (Wbn)	ROE (%)	P/E (x)	P/B (x)	EV/EBITDA (x)
12/08	7,271	480	6.6	373	3,363	516	618	14.4	17.0	2.2	12.4
12/09	9,279	419	4.5	457	4,107	490	724	15.4	17.3	2.6	15.7
12/10P	10,005	584	5.8	545	4,888	630	557	16.5	14.8	2.3	12.1
12/11F	12,744	852	6.7	831	7,452	872	789	21.0	10.5	2.0	8.9
12/12F	14,171	987	7.0	962	8,627	1,006	708	20.1	9.1	1.7	7.3

Source: Company data, Daewoo Securities Research estimates

Buy (Maintain)

Bloomberg: 000720 KS

Target Price (12M, W): 130,000

Share Price (03/04/11, W): 78,200

Expected Return (%): 66.2

Sector: Construction and Engineering

Sector Rating: Overweight

EPS Growth (11F, %): 52.5

Market EPS Growth (11F, %): 24.3

P/E (X): 10.5

Market P/E (03/04/11F, x): 9.8

Market Cap (Wbn): 8,708

Shares Outstanding (mn): 111

Avg Trading Volume (60D, '000): 1,550

Avg Trading Value (60D, Wbn): 119

Margin Balance ('000 sh): 1,426

Dividend Yield (11F, %): .9

Free Float (%): 88.9

52-Week Low/High: 46,050/91,800

Beta (12M, Daily Rate of Return): 1.1

Price Return Volatility (12M Daily, %, SD): 2.6

Foreign Ownership (%): 19.2

Major Shareholder(s):

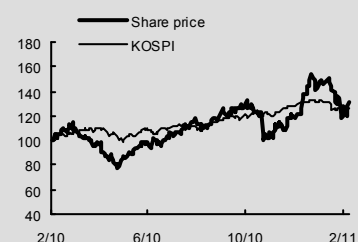
Korea Finance Corporation (11.13%)

Korea Exchange Bank (8.74%)

Woori Bank (7.52%)

Price Performance

(%)	1M	6M	12M
Absolute	-9.3	19.6	28.8
Relative	-6.0	7.0	4.9



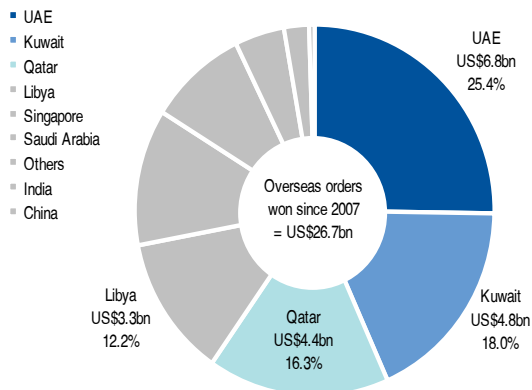
■ Time to bet on growth prospects, not on near-term uncertainty

Hyundai E&C has focused on its overseas business, rather than on domestic operations. Indeed, overseas orders (worth W12.77tr) drove the company's growth in 2010, representing 69.6% of total orders. Given the importance of overseas markets for Hyundai E&C, it is true that the recent uprisings in Libya darkened the outlook for the company's overseas order performance. Since 2007, the company has won orders worth US\$3.25bn from Libya, which accounted for 12.2% of overseas orders taken during the same period (US\$26.7bn).

Hyundai E&C's ongoing construction projects in Libya include: 1) a power plant construction project in Al-Khalij (worth US\$692mn; 50.8% completed), 2) an 855-megawatt power plant in Sarir (worth US\$252mn; 94.8% completed), 3) a 400-kilowatt power line phase-4 construction project (worth US\$142mn; 83.7% completed), and 4) a 400-kilowatt power line construction job (worth US\$134mn; 3.5% completed). The value of the remaining construction projects is estimated at US\$510mn. Moreover, construction on a 1,400-megawatt steam turbine power plant project in west Tripoli (worth US\$1.36bn) has not started yet (although Hyundai E&C has received US\$200mn in advances). As such, even if the turmoil in Libya persists for an extended period of time, the company's uncollected receivables should be limited at W52bn.

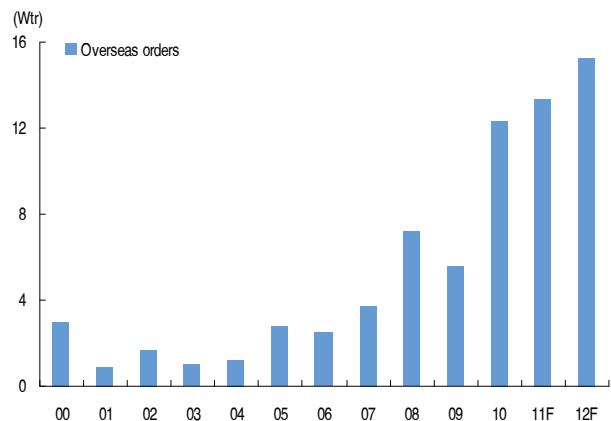
Although investors are worrying that the revolts, which began in Tunisia and swept through Egypt and Libya, may further spread to neighboring monarchies (like Saudi Arabia, the U.A.E., Kuwait) and Iran, we believe the likelihood of such a development is low, since these countries are more affluent. In fact, the uprisings were triggered by economic issues—including runaway inflation, high unemployment rates among young people, and serious economic inequality—not only by political ones. In addition, the turmoil in Libya is likely to ease, as: 1) the United Nations Security Council has imposed sanctions on Libya's leaders, and 2) the U.S. announced that it would take all necessary actions to resolve the situation. As such, now is the time to take an optimistic approach to Hyundai E&C despite lingering short-term uncertainties.

Figure 1. Hyundai E&C's overseas orders by country (since 2007)



Source: ICAK, Daewoo Securities Research

Figure 2. Hyundai E&C's annual overseas order outlook



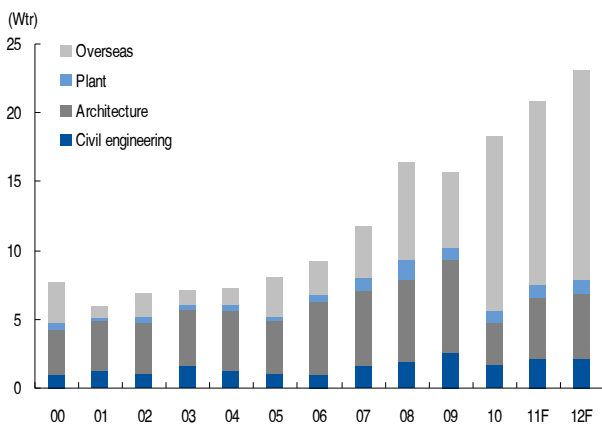
Source: ICAK, Daewoo Securities Research estimates

■ Full-swing growth to begin in 2011

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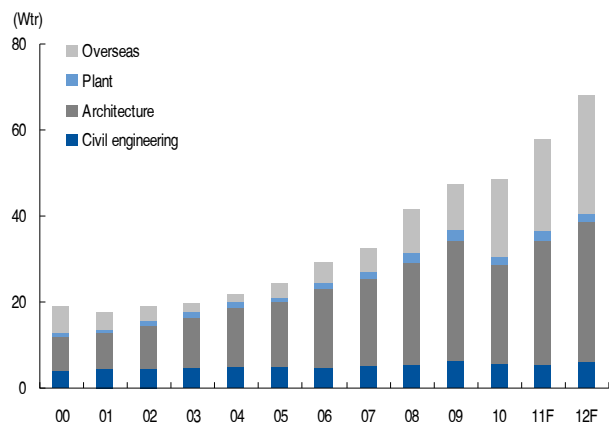
Under the management of HKAG, Hyundai E&C should be able to deliver full-swing growth starting in 2011, as: 1) the new management will likely enable the company to aggressively take new orders (Hyundai E&C maintained conservative operations under the supervision of creditors), 2) the company can use HKAG's global networks to collect information necessary for order-taking, and 3) HKAG's tight cost controls should enable the company to improve margins and expand overseas orders.

Figure 3. Hyundai E&C's overseas orders outlook by division



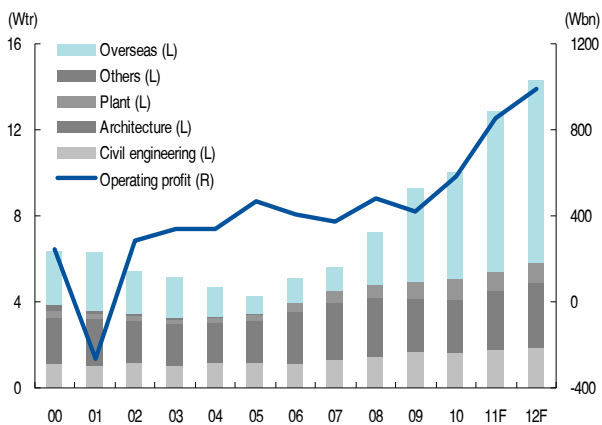
Source: Company data, Daewoo Securities Research estimates

Figure 4. Hyundai E&C's overseas order backlog outlook by division



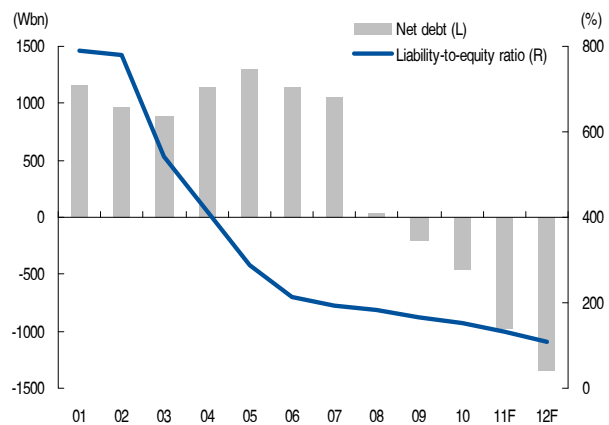
Source: Company data, Daewoo Securities Research estimates

Figure 5. Hyundai E&C's sales and operating profit outlook



Source: Company data, Daewoo Securities Research estimates

Figure 6. Hyundai E&C's net debt and liability-to-equity ratio outlook



Source: Company data, Daewoo Securities Research estimates

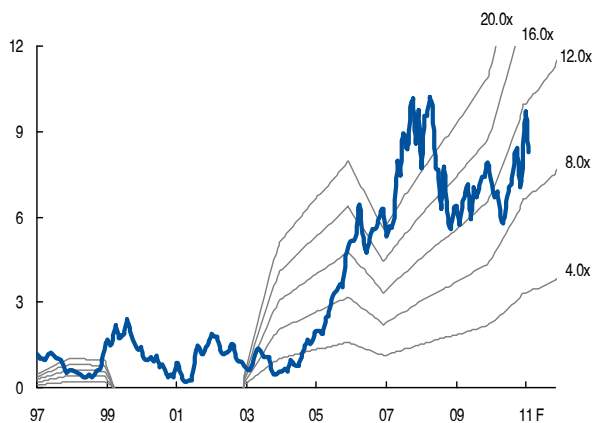
Table 1. Hyundai E&C's overseas projects

(US\$m, %)

Country	Project	Client	Contract amount	Beginning of construction	Status	Progress rate
Libya	Power transmission lines 400kv single circuit	General Electronics Co. of Libya	134	10/04/15	Initiated	3.5
Libya	Libya 400kv over head transmission line ph. 4	General Electronics Co. of Libya	142	07/09/16	Initiated	83.7
Libya	Al-Sarir 855MW power plant	General Electronics Co. of Libya	252	08/03/01	Initiated	94.8
Libya	Al Khalij power plant	General Electronics Co. of Libya	692	07/11/29	Initiated	50.8
Libya	Tripoli West 1,400MW steam power plant	General Electronics Co. of Libya	1,360	10/09/19	Initiated	0.0
Saudi Arabia	Karan gas field development pkg. 1	Saudi Aramco	1,348	09/03/01	Initiated	61.1
Singapore	Facilities and jetty of ph. 1 Jurong Rock cavern	Jurong Town Corporation	592	09/06/15	Initiated	9.4
Singapore	Reclamation for Pasir Panjang Terminal ph. 3-4	Maritime&Port Authority	632	07/10/01	Initiated	70.8
UAE	Borouge-3 expansion project: U&O package	Abu Dhabi Polymers Co.	935	10/05/26	Initiated	0.0
UAE	Integrated gas development pkg. 2 – Habshan 5 U&O	GASCO	1,702	09/07/29	Initiated	14.1
UAE	UAE nuclear energy power plant	ENEC	3,077	10/03/26	Initiated	0.8
India	Western Freeway Sea Link ph. 2A	Maharashtra State Road Co.	603	10/11/24	Uninitiated	0.0
Qatar	Ras Laffan C IWPP project	Qatar General Electricity & Water Co.	2,071	08/05/01	Initiated	98.2
Qatar	Qatar QAFCO fertilizer project ph. 5	Qatar Fertilizer Co.	1,109	07/12/14	Initiated	84.5
Qatar	Hamad Medical City - Hospital fit-out	Ashagal	534	11/02/01	Uninitiated	0.0
Kuwait	Boubyan Seaport project ph. 1, stage 2	Ministry of Public Works	1,133	10/08/01	Initiated	0.0
Kuwait	Shuaiba North power & distillation plant	Ministry of Electricity and Water	711	07/06/26	Initiated	99.9
Kuwait	New refinery project at Al-Zour pkg. 5	Kuwait National Petroleum Company	1,121	08/07/24	Initiated	2.1
Kuwait	Oil & Gas (LSFO) pipeline	Kuwait Oil Company	1,406	10/08/01	Initiated	0.0
Others			7,140			
Total			26,695			
Subtotal (Libya)			3,247			
% of Libya			12.2			

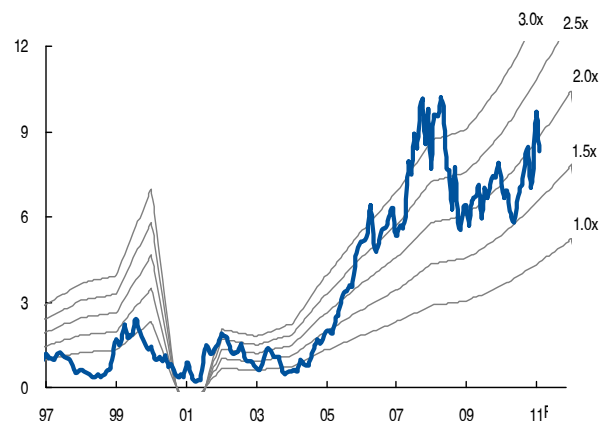
Note: Projects under the size of US\$500mn are included under 'Others', Source: ICAK, Daewoo Securities Research

Figure 7. P/B band of Hyundai E&C



Source: Company data, Daewoo Securities Research

Figure 8. P/E band of Hyundai E&C



Source: Company data, Daewoo Securities Research

Hyundai E&C (000720 KS/Buy/TP: W130,000)

Income Statement (Summarized)				
(Wbn)	12/09	12/10P	12/11F	12/12F
Sales	9,279	10,005	12,744	14,171
Cost of Goods Sold	8,554	8,958	11,513	12,757
Gross Profit	725	1,046	1,232	1,413
SG&A	306	462	379	426
Operating Profit	419	584	852	987
Non-Operating Income	169	138	199	230
Interest Income/Expense	-8	10	67	91
F/X-Related Gain/Loss	-15	1	55	0
Equity Method Gain/Loss	101	129	148	160
Asset Disposal Gain/Loss	129	-16	0	0
Other Non-Operating Profit/Loss	-38	15	-71	-21
Pretax Profit	587	723	1,051	1,217
Tax	131	178	221	256
Profit from Continuing Operation	457	545	831	962
Profit from Discontinued Operation	0	0	0	0
Tax Effect	0	0	0	0
Net Profit	457	545	831	962
Residual Income	457	545	831	962
EBITDA	490	630	872	1,006
Free Cash Flow	724	557	789	708
Gross Profit Margin (%)	7.8	10.5	9.7	10.0
EBITDA Margin (%)	5.3	6.3	6.8	7.1
Operating Margin (%)	4.5	5.8	6.7	7.0
Net Margin (%)	4.9	5.5	6.5	6.8

Cash Flow (Summarized)				
(Wbn)	12/09	12/10P	12/11F	12/12F
Cash Flow from Operating Activities	856	572	819	708
Net Profit	457	545	831	962
Non-Cash Income and Expense	-36	53	-179	-107
Tangible Assets Depreciation	71	46	19	18
Intangible Assets Depreciation	0	0	0	0
Others	-107	8	-199	-125
Chg in Working Capital	435	-26	167	-146
Chg in Accounts Receivable	0	-127	-26	-133
Chg in Inventories	74	151	9	19
Chg in Accounts Payable	87	117	-42	-50
Others	275	-167	226	17
Cash Flow from Investment Activities	-146	-167	-401	-431
Chg in Tangible Assets	-132	-31	-30	0
Chg in Intangible Assets	0	0	0	0
Chg in Investment Assets	-144	-129	-417	-419
Others	130	-8	46	-13
Cash Flow from Financing Activities	-360	14	-14	21
Chg in Borrowings	-319	226	50	99
Chg in Equity	-56	-212	-67	-78
Dividends	-56	67	-67	-78
Others	14	0	2	0
Chg in Cash	349	419	403	298
Beginning Cash Balance	698	1,048	1,466	1,870
Ending Cash Balance	1,048	1,466	1,870	2,168

Source: Company data, Daewoo Securities Research estimates

Balance Sheet (Summarized)				
(Wbn)	12/09	12/10P	12/11F	12/12F
Current Assets	5,010	5,557	5,973	6,360
Cash and Cash Equivalents	1,048	1,466	1,870	2,168
Accounts Receivable	1,583	1,652	1,675	1,773
Inventories	734	583	574	554
Other Current Assets	1,645	1,855	1,854	1,865
Non-Current Assets	3,081	3,451	4,027	4,587
Investment Assets	2,405	3,044	3,609	4,187
Property, Plant and Equipment	676	407	418	399
Intangible Assets	0	0	0	0
Total Assets	8,091	9,008	9,999	10,947
Current Liabilities	4,311	4,298	4,391	4,287
Accounts Payable	1,266	1,383	1,341	1,291
Short-Term Debt	378	398	378	362
Current Long-Term Debt	349	204	140	87
Other Current Liabilities	2,318	2,313	2,532	2,547
Non-Current Liabilities	754	1,141	1,275	1,443
Bonds	199	373	323	303
Long-Term Debt	46	192	213	244
Other Non-Current Liabilities	509	576	740	897
Total Liabilities	5,066	5,439	5,667	5,731
Paid-In Capital	557	557	557	557
Capital Surplus	828	828	828	828
Retained Earnings	1,488	1,966	2,730	3,613
Stockholders' Equity	3,026	3,569	4,333	5,216

Forecasts/Valuations (Summarized)				
	12/09	12/10P	12/11F	12/12F
P/E (x)	17.3	14.8	10.5	9.1
P/CF (x)	14.9	11.4	7.9	6.8
P/B (x)	2.6	2.3	2.0	1.7
EV/EBITDA (x)	15.7	12.1	8.9	7.3
EPS (W)	4,107	4,888	7,452	8,627
CFPS (W)	4,747	5,297	7,626	8,793
BPS (W)	27,147	32,022	38,874	46,801
DPS (W)	600	600	700	800
Payout Ratio (%)	14.7	12.3	9.4	9.3
Dividend Yield (%)	0.9	0.8	0.9	1.0
Sales Growth (%)	27.6	7.8	27.4	11.2
EBITDA Growth (%)	-5.0	28.5	38.4	15.4
Operating Profit Growth (%)	-12.8	39.5	45.9	15.9
EPS Growth (%)	22.1	19.0	52.5	15.8
Accounts Receivable Turnover (x)	6.0	6.2	7.7	8.2
Inventory Turnover (x)	12.7	15.2	22.0	25.1
Accounts Payable Turnover (x)	7.6	7.6	9.4	10.8
ROA (%)	5.6	6.4	8.7	9.2
ROE (%)	15.4	16.5	21.0	20.1
ROIC (%)	25.8	42.1	74.3	71.7
Liability to Equity Ratio (%)	167.4	152.4	130.8	109.9
Current Ratio (%)	116.2	129.3	136.0	148.4
Net Debt to Equity Ratio (%)	-6.8	-12.8	-22.6	-25.9
Interest Coverage Ratio (x)	6.4	15.2	21.0	26.1

Important Notices

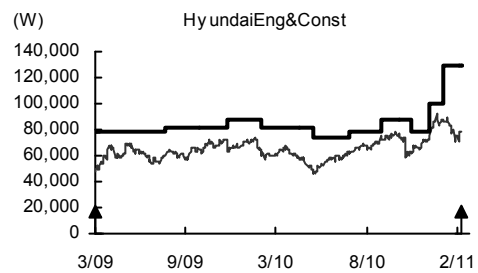
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Stock Ratings

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.

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