MIRAE ASSET
Building on principles

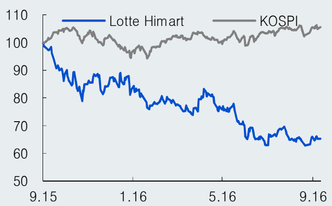
Retail

Earnings Preview
October 5, 2016

(Maintain)	Buy
Target Price (12M, W)	60,000
Share Price (10/04/16, W)	44,300
Expected Return	35%

OP (16F, Wbn)	161
Consensus OP (16F, Wbn)	160
EPS Growth (16F, %)	5.5
Market EPS Growth (16F, %)	20.0
P/E (16F, x)	9.3
Market P/E (16F, x)	10.7
KOSPI	2,054.86
Market Cap (Wbn)	1,046
Shares Outstanding (mn)	24
Free Float (%)	33.6
Foreign Ownership (%)	8.2
Beta (12M)	1.02
52-Week Low	42,600
52-Week High	66,700

(%)	1M	6M	12M
Absolute	-0.1	-13.3	-32.8
Relative	-0.9	-16.5	-35.6



Mirae Asset Daewoo Co., Ltd.

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Lotte Himart

(071840 KS)

Share price slide coming to an end

Share price to turn around on earnings improvement

We feel Lotte Himart's stock is severely undervalued. Shares are currently trading at 9x P/E, and have been dropping since June 2015. We attribute the weakness to a series of sluggish earnings results, which continue to fall short of the market consensus. Investors appear to be losing confidence in earnings, leading to discounted stock price.

We forecast earnings to improve between 3Q-4Q. Even a slight uptick in earnings could lead to improved investor confidence and a rebound in the company's undervalued shares.

3Q16 preview: OP to increase 11.0% YoY

For 3Q, we expect revenue and operating profit of W1.13tr (+6.2% YoY) and W62.3bn (+11.0% YoY), respectively. Sales of white goods and small appliances are expected to have grown in the high single digits and mid-single digits, respectively, driving top-line growth. We are particularly bullish on air conditioner sales (expecting double-digit growth) given the hotter-than-usual weather. We believe the government's subsidy program for high-efficiency home appliances only increased sales of kimchi refrigerators (+10% revenue growth).

Meanwhile, sales of mobile products are estimated to have contracted over 10%, due to 1) an absence of new product releases and 2) Samsung's Galaxy Note 7 battery issue. We estimate online channel sales mix increased to 5.4% of total revenue (vs. 1% in end-2014 and 3% in end-2015). As high-margin small appliances take up over 60% of online channel revenue, the online channel OP margin is similar to headline OP margin.

On the expense front, we expect increases in commissions as well as delivery and installation costs, although none of these should have significantly impacted earnings. Operating profit should easily increase in 4Q due to a low base of comparison stemming from high SG&A and promotional expenses generated in 4Q15. With a stable increase in revenue, operating profit should be able to grow another 10%.

Maintain Buy but Lower TP to W60,000

We maintain our Buy rating on Lotte Himart but cut our target price to W60,000, as revenue increases and margin expansion fell short of forecasts. We do not yet foresee a structural improvement in the business environment, but the weakness is already priced in and the company's share price should rebound.

Best Buy in the US has recently been attracting investors' attention after successfully improving earnings. The company increased online sales by utilizing its offline stores, which online-only retailers such as Amazon do not have. We believe Lotte Himart is worthy of a revaluation if it can achieve significant improvement in revenue through the online business, similar to Best Buy's path.

FY (Dec.)	12/13	12/14	12/15	12/16F	12/17F	12/18F
Revenue (Wbn)	3,519	3,754	3,896	4,033	4,247	4,434
OP (Wbn)	185	144	160	161	172	179
OP margin (%)	5.3	3.8	4.1	4.0	4.0	4.0
NP (Wbn)	129	96	107	112	123	132
EPS (W)	5,469	4,085	4,515	4,762	5,199	5,593
ROE (%)	8.4	5.9	6.1	6.1	6.3	6.4
P/E (x)	16.0	16.5	13.1	9.3	8.5	7.9
P/B (x)	1.3	0.9	0.8	0.6	0.5	0.5

Notes: All figures are based on non-consolidated K-IFRS; NP refers to net profit attributable to controlling interests
Source: Company data, Mirae Asset Daewoo Research estimates

Table 1. 3Q16 earnings preview (Wbn, %)

	3Q15	2Q16	3Q16F		Growth	
			Mirae Asset Daewoo	Consensus	YoY	QoQ
Revenue	1,063	951	1,129	1,124	6.2	18.8
Operating profit	56	41	62	61	10.9	52.6
OP margin	5.3	4.3	5.5	5.4		
Pretax profit	52	38	59	57	13.8	56.5
Net profit	40	29	44	45	12.3	54.2

Source: Bloomberg, Mirae Asset Daewoo Research estimates

Table 2. Quarterly and annual earnings (Wbn, %)

	2016F				2017F				2015	2016F	2017F	Growth		
	1Q16	2Q16	3Q16F	4Q16F	1Q17F	2Q17F	3Q17F	4Q17F				3Q16F	2016F	2017F
Revenue	888	951	1,129	1,066	930	1,017	1,190	1,110	3,896	4,033	4,247	6.2	3.5	5.3
Stand-alone stores	681	751	899	852	693	782	924	873	3,163	3,183	3,273	3.1	0.6	2.8
Shop-in-shops	175	152	169	154	182	160	177	160	647	650	679	1.5	0.6	4.4
Online	32	47	61	59	54	75	89	77	88	200	295	145.0	125.8	48.1
No. of stores	438	442	448	457	458	461	462	465	440	457	465	2.5	3.9	1.8
Stand-alone stores	332	336	342	347	348	350	351	353	334	347	353	3.0	3.9	1.7
Shop-in-shops	106	106	106	110	110	111	111	112	106	110	112	1.0	3.8	1.8
Revenue per store	2.0	2.2	2.5	2.3	2.0	2.2	2.6	2.4	8.9	8.8	9.1	3.6	-0.3	3.5
Stand-alone stores	2.1	2.2	2.6	2.5	2.0	2.3	2.6	2.5	9.5	9.2	9.3	0.8	-3.1	1.1
Shop-in-shops	1.6	1.4	1.6	1.4	1.7	1.4	1.6	1.4	6.2	6.0	6.1	0.5	-2.7	1.6
Gross profit	215	252	290	249	224	267	303	262	963	1,007	1,056	8.5	4.5	4.9
Operating profit	28	41	62	29	29	44	66	33	160	161	172	11.0	0.3	6.9
Gross margin	24.2	26.5	25.7	23.4	24.1	26.2	25.5	23.6	24.7	25.0	24.9			
OP margin	3.1	4.3	5.5	2.8	3.1	4.3	5.5	3.0	4.1	4.0	4.0			

Notes: Stand-alone, shop-in-shop, and online data are estimates
Source: Company data, Mirae Asset Daewoo Research estimates

Lotte Himart (071840 KS/Buy/TP: W60,000)

Comprehensive Income Statement (Summarized)

(Wbn)	12/15	12/16F	12/17F	12/18F
Revenue	**3,896**	**4,033**	**4,247**	**4,434**
Cost of Sales	**2,933**	**3,026**	**3,191**	**3,335**
Gross Profit	**963**	**1,007**	**1,056**	**1,099**
SG&A Expenses	**803**	**846**	**884**	**920**
Operating Profit (Adj)	**160**	**161**	**172**	**179**
Operating Profit	**160**	**161**	**172**	**179**
Non-Operating Profit	**-17**	**-12**	**-6**	**-1**
Net Financial Income	-18	-12	-6	0
Net Gain from Inv in Associates	0	0	0	0
Pretax Profit	143	149	166	178
Income Tax	37	37	43	46
Profit from Continuing Operations	107	112	123	132
Profit from Discontinued Operations	0	0	0	0
Net Profit	107	112	123	132
Controlling Interests	107	112	123	132
Non-Controlling Interests	0	0	0	0
Total Comprehensive Profit	**105**	**111**	**123**	**130**
Controlling Interests	105	111	123	130
Non-Controlling Interests	0	0	0	0
EBITDA	213	213	223	228
FCF (Free Cash Flow)	89	89	115	126
EBITDA Margin (%)	5.5	5.3	5.3	5.1
Operating Profit Margin (%)	4.1	4.0	4.0	4.0
Net Profit Margin (%)	2.7	2.8	2.9	3.0

Statement of Financial Condition (Summarized)

(Wbn)	12/15	12/16F	12/17F	12/18F
Current Assets	**640**	**727**	**839**	**971**
Cash and Cash Equivalents	130	142	240	352
AR & Other Receivables	69	95	100	103
Inventories	416	474	483	498
Other Current Assets	25	16	16	18
Non-Current Assets	**2,265**	**2,270**	**2,277**	**2,278**
Investments in Associates	0	0	0	0
Property, Plant and Equipment	422	416	426	431
Intangible Assets	1,705	1,704	1,699	1,696
Total Assets	**2,905**	**2,997**	**3,116**	**3,249**
Current Liabilities	**638**	**444**	**451**	**464**
AP & Other Payables	280	295	307	318
Short-Term Financial Liabilities	285	70	70	0
Other Current Liabilities	73	79	74	146
Non-Current Liabilities	**484**	**670**	**669**	**670**
Long-Term Financial Liabilities	469	649	649	0
Other Non-Current Liabilities	15	21	20	670
Total Liabilities	**1,122**	**1,114**	**1,120**	**1,133**
Controlling Interests	**1,783**	**1,884**	**1,996**	**2,116**
Capital Stock	118	118	118	118
Capital Surplus	1,056	1,056	1,056	1,056
Retained Earnings	608	711	823	945
Non-Controlling Interests	**0**	**0**	**0**	**0**
Stockholders' Equity	**1,783**	**1,884**	**1,996**	**2,116**

Cash Flows (Summarized)

(Wbn)	12/15	12/16F	12/17F	12/18F
Cash Flows from Op Activities	120	134	171	176
Net Profit	107	112	123	132
Non-Cash Income and Expense	127	110	100	96
Depreciation	49	47	47	45
Amortization	3	5	4	3
Others	75	58	49	48
Chg in Working Capital	-88	-46	-8	-6
Chg in AR & Other Receivables	3	-29	-3	-2
Chg in Inventories	-59	-57	-9	-16
Chg in AP & Other Payables	4	6	9	8
Income Tax Paid	**-25**	**-43**	**-43**	**-46**
Cash Flows from Inv Activities	-85	-60	-47	-36
Chg in PP&E	-31	-46	-56	-50
Chg in Intangible Assets	-11	-4	0	0
Chg in Financial Assets	-54	-12	-2	-1
Others	**11**	**2**	**11**	**15**
Cash Flows from Fin Activities	-11	-61	-27	-27
Chg in Financial Liabilities	21	-35	0	0
Chg in Equity	0	0	0	0
Dividends Paid	-8	-10	-10	-10
Others	**-24**	**-16**	**-17**	**-17**
Increase (Decrease) in Cash	25	13	97	112
Beginning Balance	105	130	142	240
Ending Balance	**130**	**142**	**240**	**352**

Forecasts/Valuations (Summarized)

	12/15	12/16F	12/17F	12/18F
P/E (x)	13.1	9.3	8.5	7.9
P/CF (x)	6.0	4.7	4.7	4.6
P/B (x)	0.8	0.6	0.5	0.5
EV/EBITDA (x)	9.5	7.6	6.8	6.2
EPS (W)	4,515	4,762	5,199	5,593
CFPS (W)	9,887	9,430	9,433	9,660
BPS (W)	75,519	79,786	84,555	89,633
DPS (W)	430	430	430	430
Payout ratio (%)	9.5	9.0	8.3	7.7
Dividend Yield (%)	0.7	1.0	1.0	1.0
Revenue Growth (%)	3.8	3.5	5.3	4.4
EBITDA Growth (%)	8.1	0.0	4.7	2.2
Operating Profit Growth (%)	11.1	0.6	6.8	4.1
EPS Growth (%)	10.5	5.5	9.2	7.6
Accounts Receivable Turnover (x)	74.3	65.1	58.6	58.9
Inventory Turnover (x)	10.1	9.1	8.9	9.0
Accounts Payable Turnover (x)	16.0	14.9	14.7	14.8
ROA (%)	3.8	3.8	4.0	4.1
ROE (%)	6.1	6.1	6.3	6.4
ROIC (%)	5.3	5.2	5.4	5.6
Liability to Equity Ratio (%)	63.0	59.1	56.1	53.6
Current Ratio (%)	100.3	163.8	185.9	209.5
Net Debt to Equity Ratio (%)	34.9	30.5	23.9	17.2
Interest Coverage Ratio (x)	6.7	8.9	10.2	10.7

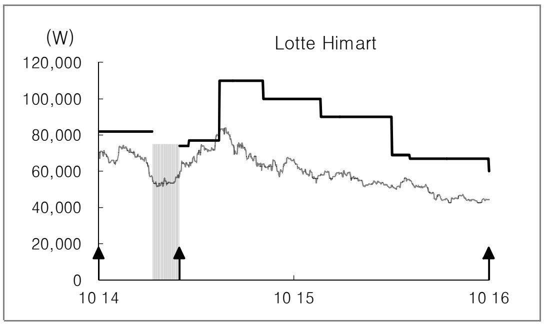
Source: Company data, Mirae Asset Daewoo Research estimates

APPENDIX 1

Important Disclosures & Disclaimers

2-Year Rating and Target Price History

Company (Code)	Date	Rating	Target Price
Lotte Himart(071840)	10/04/2016	Buy	60,000
	05/09/2016	Buy	67,000
	04/06/2016	Buy	69,000
	11/25/2015	Buy	90,000
	08/09/2015	Buy	100,000
	05/19/2015	Buy	110,000
	03/23/2015	Buy	77,000
	03/05/2015	Buy	74,000
		No Coverage	
	08/06/2014	Buy	82,000



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 Mirae Asset Daewoo Co., Ltd., 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
70.73%	17.56%	11.71%	0.00%

* Based on recommendations in the last 12-months (as of June 30, 2016)

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