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Company Update



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AT A GLANCE

SELL HOLD **BUY**

Target price KRW513,000 (28.9%)

Current price KRW398,000

Market cap	KRW4.2t/USD3.7b
Shares (float)	10,556,513 (54.4%)
52-week high/low	KRW442,500/KRW318,000
Avg daily trading value (60-day)	KRW14.1b/ USD12.4m

ONE-YEAR PERFORMANCE

	1M	6M	12M
KCC (%)	-4.6	19.2	-5.1
Vs Kospi (%pts)	-1.3	5.9	-16.7

KEY CHANGES

(KRW)	New	Old	Diff
Recommend.	BUY	BUY	
Target price	513,000	525,000	-2.3%
2017E EPS	20,775	20,872	-0.5%
2018E EPS	19,952	20,052	-0.5%

SAMSUNG vs THE STREET

No of estimates	10
Target price	499,500
Recommendation	4.0

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

KCC (002380)

Construction materials solid, paint recovers

- KCC's comprehensive 2H results revealed a strong performance by the construction-materials division and a return to top-line growth and improving margin in the paint business in 2Q. Preliminary 2Q figures reported Aug 4 showed an operating profit of KRW92b that missed the consensus by 5.2%.
- Reflecting the 2Q results and changes in value of equity holdings, we trim our target price for KCC from KRW525,000 to KRW513,000 but maintain BUY. We expect both the construction-materials and paint businesses to keep improving.

WHAT'S THE STORY?

2Q review: KCC's comprehensive 2H results, released after the market close Aug 14, revealed a strong performance by the construction-materials division and a return to top-line growth and improving margin in the paint business in 2Q. We expect both units to keep improving in the quarters ahead. In its preliminary release on Aug 4, KCC posted a 2Q operating profit of KRW92b that missed the consensus by 5.2% and a net profit of KRW70b that beat by 8.6% thanks to lower-than-expected currency swap valuation losses on and forex losses.

Construction materials thrive, 2H outlook even brighter: The construction-materials division achieved double-digit growth in 2Q for a second straight quarter, its sales increasing 12.6% y-y to KRW405.1b. Operating margin was decent at 15.2%, helped by a gradual rise in move-in volume since end-2016 following hikes in presales volume over 2015-2016. We believe results will keep improving through 2H, as nationwide move-in volume is likely to increase 53% from 150,000 units in 1H to 230,000 in 2H and the company's high-margin plaster board capacity has risen 40% with a capacity expansion that was completed in June and went operational in July.

Paint unit returns to growth, margin improves: The paint business delivered its first y-y growth in nine quarters, its sales climbing 0.4% y-y in 2Q17 to KRW400.7b. Operating margin hit 7.1%, having steadily risen from a 4Q16 bottom of 1.2%, as ASPs for all products except domestic architecture/automotive paint rose q-q, while prices of raw materials soda ash, xylene, and toluene fell a respective 1.2%, 4.1%, and 5.1% q-q. Unless ASPs drop, profitability keep improving in 3Q on lower raw material input prices.

SUMMARY OF 2Q RESULTS

(KRWb)	2Q17	Chg		Diff (%)	
		(% y-y)	(% q-q)	Samsung	Consensus
Sales	970.3	6.8	15.1	1.1	3.2
Operating profit	92.0	(12.5)	29.3	(12.0)	(5.2)
Pre-tax profit	97.4	18.8	117.8	8.7	11.6
Net profit	70.0	15.9	105.3	(0.5)	8.6
Margins (%)					
Operating profit	9.5				
Pre-tax profit	10.0				
Net profit	7.2				

Source: Company data, Samsung Securities estimates

VALUATION SUMMARY

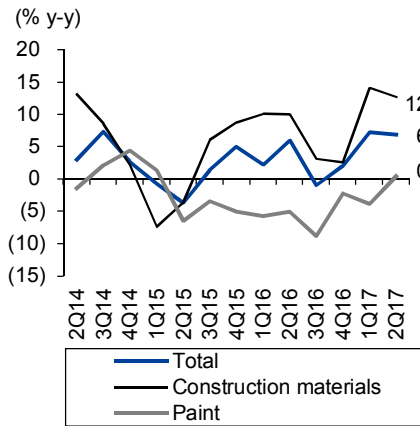
	2016	2017E	2018E
Multiples (x)			
P/E	27.6	19.2	19.9
P/B	0.7	0.6	0.6
EV/EBITDA	10.2	10.5	10.4
Div yield (%)	2.3	2.3	2.3
EPS growth (% y-y)	(17.3)	44.0	(4.0)
ROE (%)	2.6	3.6	3.4
Per-share data (KRW)			
EPS	14,430	20,775	19,952
BVPS	605,683	618,986	631,405
DPS	9,000	9,000	9,000

Quarterly results breakdown

(KRWb)	2Q16				1Q17				2Q17			
	Construction materials	Paint	Other	Total	Construction materials	Paint	Other	Total	Construction materials	Paint	Other	Total
Sales	360	399	190	909	356	348	185	843	405.1	400.7	212.0	970.3
Chg (% y-y)	10.0	(5.1)	14.4	5.9	14.1	(3.9)	17.7	7.2	12.6	0.4	11.7	6.8
Chg (% q-q)	15.3	10.3	20.6	15.5	(6.2)	(12.9)	(9.6)	(10.1)	13.8	15.2	14.5	15.1
Gross profit				249				222				249
Gross margin (%)				27.4				26.3				25.6
SG&A cost				143				136				143
SG&A cost ratio (%)				15.8				16.1				14.8
Operating profit	57	46	(1)	105	44	20	3	71	61	29	(0)	92
Operating margin (%)	15.9	11.4	(0.4)	11.6	12.3	5.8	1.9	8.4	15.2	7.1	(0.1)	9.5
Equity-method income				4				(1)				(2)
Net financial income				(22)				(23)				8
Non-operating profit				(6)				(3)				0
Tax				22				11				27
Net profit				60				34				70

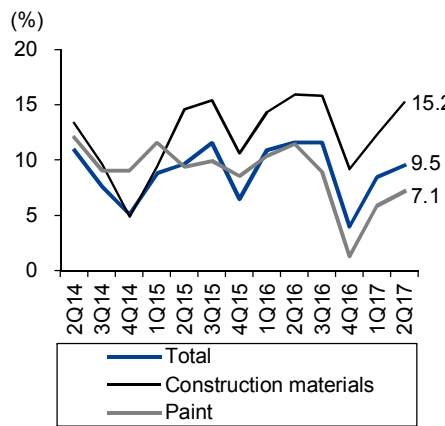
Source: Company data, Samsung Securities

Sales growth, by division



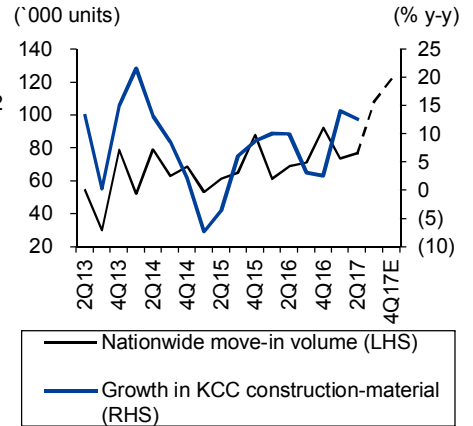
Source: Company data, Samsung Securities

Operating margin, by division



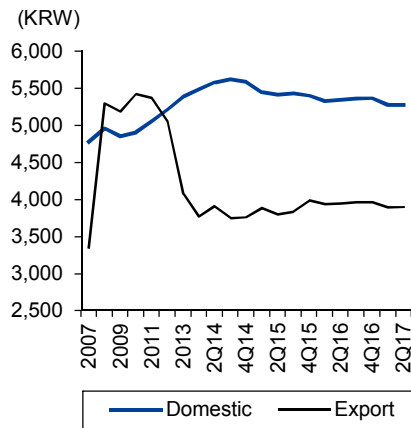
Source: Company data, Samsung Securities

Construction materials sales vs nationwide move-in volume



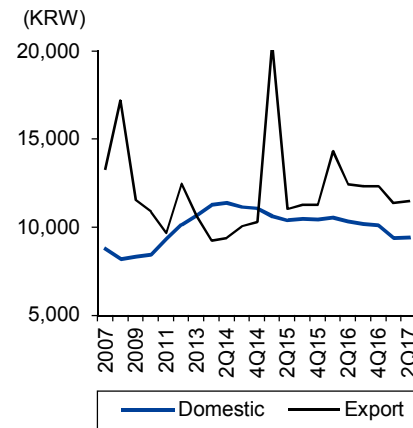
Source: Company data, r114, Samsung Securities

Mitone ASPs



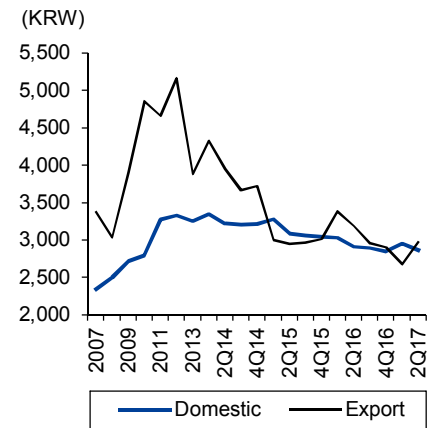
Source: Company data, Samsung Securities

PVC flooring ASPs



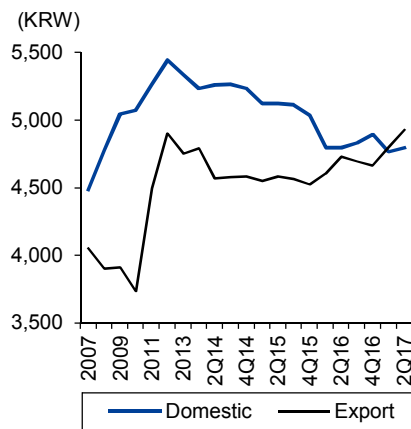
Source: Company data, Samsung Securities

Construction paint ASPs



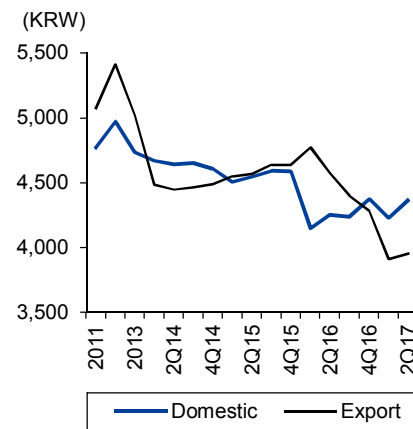
Source: Company data, Samsung Securities

Industrial paint ASPs



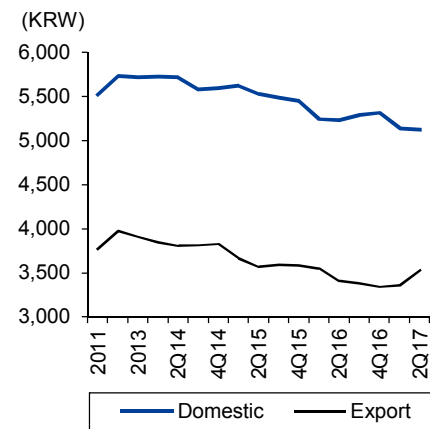
Source: Company data, Samsung Securities

Vessel paint ASPs



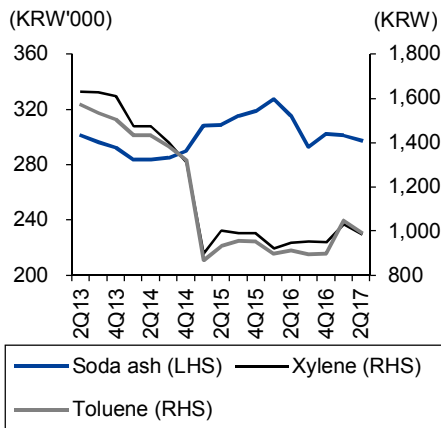
Source: Company data, Samsung Securities

Auto paint ASPs



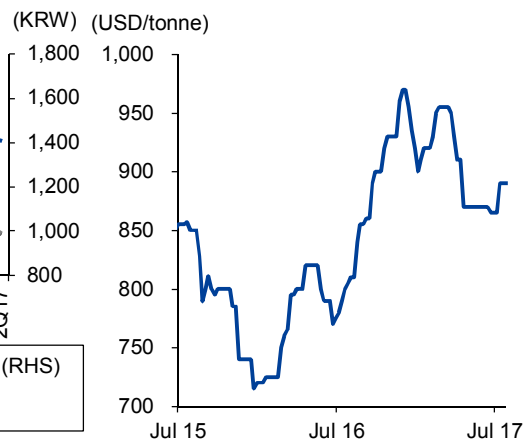
Source: Company data, Samsung Securities

KCC: Raw material costs



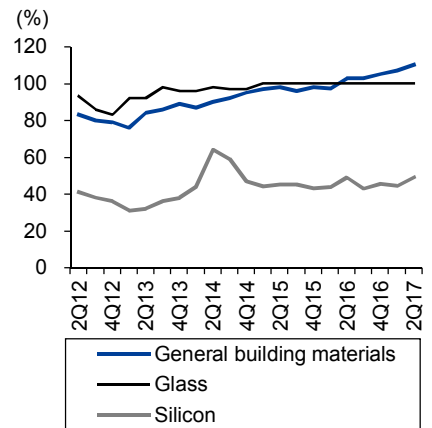
Source: Company data, Samsung Securities

PVC prices



Source: Platts, Samsung Securities

KCC: Utilization rates



Source: Company data, Samsung Securities

Sum-of-the-parts valuation

(KRWb)	Value	Note
Investment securities (A)	2,884	
Listed	2,837	23% discount to market value
Unlisted	47	23% discount to book value
Real estate (B)	1,020	Land book value as of 4Q17
Operating value (C)	2,474	5 x 2017E EBITDA
GAV (D)	6,378	D = A + B + C
Net debt (E)	981	2017E
NAV (F)	5,397	D - E
Shares ('000)	10,520	
NAVPS (KRW)	513,000	
Target price (KRW)	513,000	
Current price (KRW)	398,000	
Upside (%)	28.9%	

Source: Company data, Samsung Securities estimates

Income statement

Year-end Dec 31(KRWb)	2015	2016	2017E	2018E	2019E
Sales	3,414	3,490	3,676	3,758	3,841
Cost of goods sold	2,529	2,561	2,737	2,798	2,860
Gross profit	886	929	939	960	981
Gross margin (%)	25.9	26.6	25.5	25.5	25.5
SG&A expenses	577	603	620	631	643
Operating profit	309	327	319	329	338
Operating margin (%)	9.1	9.4	8.7	8.7	8.8
Non-operating gains (losses)	(58)	(95)	(29)	(50)	(47)
Financial profit	180	92	24	26	29
Financial costs	208	101	52	50	50
Equity-method gains (losses)	(20)	14	16	16	16
Other	(11)	(99)	(17)	(41)	(41)
Pre-tax profit	251	232	291	279	291
Taxes	66	79	70	68	70
Effective tax rate (%)	26.2	34.1	24.2	24.2	24.2
Profit from continuing operations	185	153	220	211	221
Profit from discontinued operations	0	0	0	0	0
Net profit	185	153	220	211	221
Net margin (%)	5.4	4.4	6.0	5.6	5.7
Net profit (controlling interests)	184	152	219	211	220
Net profit (non-controlling interests)	1	1	1	1	1
EBITDA	473	530	495	481	469
EBITDA margin (%)	13.8	15.2	13.5	12.8	12.2
EPS (parent-based) (KRW)	17,443	14,430	20,775	19,952	20,811
EPS (consolidated) (KRW)	17,586	14,490	20,861	20,034	20,897
Adjusted EPS (KRW)*	17,443	14,430	20,775	19,952	20,811

Cash flow statement

Year-end Dec 31(KRWb)	2015	2016	2017E	2018E	2019E
Cash flow from operations	95	431	408	366	352
Net profit	185	153	220	211	221
Non-cash profit and expenses	337	426	258	228	208
Depreciation	162	202	174	150	130
Amortization	1	2	2	1	1
Other	173	223	82	76	77
Changes in A/L from operating activities	(246)	(47)	1	(6)	(7)
Cash flow from investments	(865)	(498)	(67)	(53)	(52)
Change in tangible assets	(358)	(289)	0	0	0
Change in financial assets	68	(167)	(91)	(78)	(80)
Other	(575)	(42)	24	26	29
Cash flow from financing	464	202	(241)	(139)	(139)
Change in debt	600	358	(100)	0	0
Change in equity	22	0	0	0	0
Dividends	(88)	(89)	(89)	(89)	(89)
Other	(70)	(67)	(52)	(50)	(50)
Change in cash	(301)	144	117	183	169
Cash at beginning of year	745	445	588	705	888
Cash at end of year	445	588	705	888	1,057
Gross cash flow	522	579	478	440	429
Free cash flow	(265)	141	408	366	352

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)	2015	2016	2017E	2018E	2019E
Current assets	2,206	2,289	2,450	2,672	2,881
Cash & equivalents	445	588	705	888	1,057
Accounts receivable	879	910	954	975	997
Inventories	527	526	525	536	548
Other current assets	355	265	267	273	279
Fixed assets	6,463	6,874	6,789	6,718	6,669
Investment assets	3,406	3,530	3,622	3,702	3,785
Tangible assets	2,515	2,572	2,398	2,248	2,118
Intangible assets	41	40	39	37	36
Other long-term assets	501	731	731	731	731
Total assets	8,668	9,162	9,239	9,390	9,550
Current liabilities	1,375	1,678	1,615	1,630	1,645
Accounts payable	226	261	275	281	288
Short-term debt	810	963	963	963	963
Other current liabilities	338	453	377	385	394
Long-term liabilities	1,425	1,518	1,525	1,538	1,552
Bonds & long-term debt	829	936	936	936	936
Other long-term liabilities	596	581	589	602	615
Total liabilities	2,800	3,195	3,141	3,168	3,196
Owners of parent equity	5,858	5,956	6,087	6,209	6,340
Capital stock	56	56	56	56	56
Capital surplus	468	468	468	468	468
Retained earnings	4,363	4,440	4,571	4,693	4,824
Other	971	992	992	992	992
Non-controlling interests' equity	11	11	12	13	14
Total equity	5,869	5,967	6,099	6,222	6,354
Net debt	1,069	1,198	981	794	620

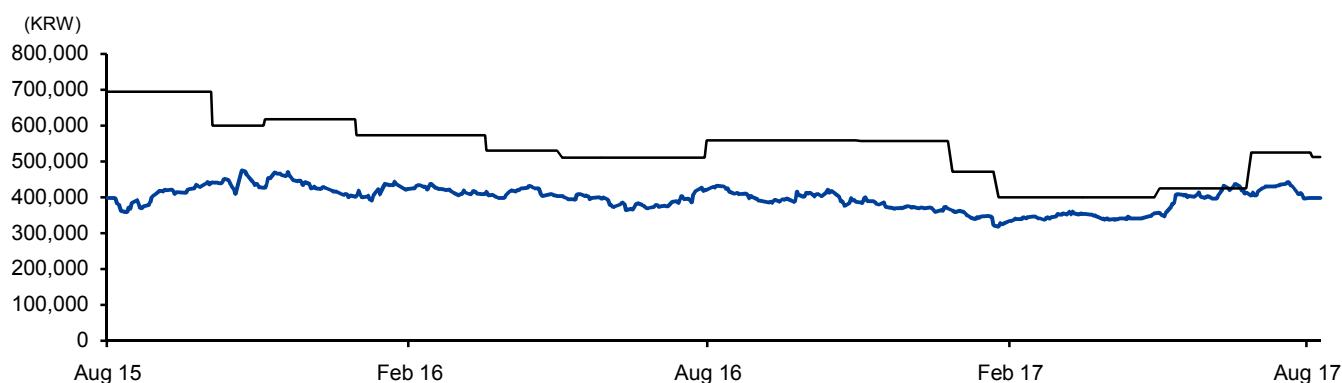
Financial ratios

Year-end Dec 31	2015	2016	2017E	2018E	2019E
Growth (%)					
Sales	0.4	2.2	5.3	2.2	2.2
Operating profit	13.1	5.6	(2.3)	3.0	2.9
Net profit	(43.4)	(17.3)	44.0	(4.0)	4.3
Adjusted EPS**	(43.7)	(17.3)	44.0	(4.0)	4.3
Per-share data (KRW)					
EPS (parent-based)	17,443	14,430	20,775	19,952	20,811
EPS (consolidated)	17,586	14,490	20,861	20,034	20,897
Adjusted EPS**	17,443	14,430	20,775	19,952	20,811
BVPS	595,712	605,683	618,986	631,405	644,747
DPS (common)	9,000	9,000	9,000	9,000	9,000
Valuations (x)					
P/E***	22.8	27.6	19.2	19.9	19.1
P/B***	0.7	0.7	0.6	0.6	0.6
EV/EBITDA	11.2	10.2	10.5	10.4	10.3
Ratios (%)					
ROE	3.0	2.6	3.6	3.4	3.5
ROA	2.1	1.7	2.4	2.3	2.3
ROIC	6.4	6.0	7.0	7.9	8.4
Payout ratio	48.2	58.1	40.4	42.0	40.3
Dividend yield (common)	2.3	2.3	2.3	2.3	2.3
Net debt to equity	18.2	20.1	16.1	12.8	9.8
Interest coverage (x)	9.0	6.8	6.2	6.5	6.7

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Target price changes in past two years



Rating changes in past two years

Date	2015/8/16	10/16	11/17	2016/1/12	3/31	5/16	8/12	11/14	2017/1/9	2/6	5/15	7/9
Recommendation	BUY	BUY	BUY	BUY	BUY	BUY	BUY	BUY	BUY	BUY	BUY	BUY
Target price (KRW)	694,000	600,000	617,000	573,000	530,000	510,000	559,000	557,000	472,000	400,000	424,000	525,000
Date	8/16											
Recommendation	BUY											
Target price (KRW)	513,000											

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Company

BUY	Expected to increase in value by 10% or more within 12 months and is highly attractive within sector
HOLD	Expected to increase/decrease in value by less than 10% within 12 months
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Industry

OVERWEIGHT	Expected to outperform market by 5% or more within 12 months
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UNDERWEIGHT	Expected to underperform market by 5% or more within 12 months

Percentage of ratings in 12 months prior to Jun 30, 2017

BUY (81.5%) | HOLD (18.5%) | SELL (0%)

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