

Maeil Dairies

(267980 KQ)

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Rating **BUY**
maintain

6M TP (W) **100,000**
maintain

CP (W)
(18.12.20) **79,200**

Food & Beverage

Strong re-rating potential

BUY and 6M TP of W100,000 maintained

- The target price is derived from the residual income model.
- Our target price of W100,000 represents a 26% upside potential from the current share price level, even when assuming a conservative NP CAGR of 0.4% in 2021-2027.
- The target price translates into 13.3x 2019E EPS of W7,503, which is 13.1% lower than the food & beverage sector's average P/E of 15.3x. Maeil Dairies remains our second favorite stock in the food & beverage sector.

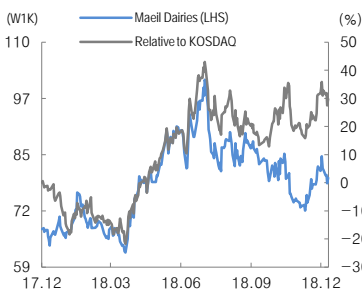
Re-rating expected

- On a non-consolidated basis, 4Q18 revenue is expected to expand 0.2% yoy, but contract 1.9% qoq to W327.1bn and OP is expected to rise 24.1% yoy, but fall 4.8% qoq to W20.2bn, coming in line with our previous forecast of W19.9bn but beating the market consensus of W19.0bn.
- We expect favorable results this quarter considering a number of factors: 1) Despite the W4 per liter rise in raw milk price in August, robust B2B sales erased some of the losses in white market milk (both yoy and qoq); 2) Exports of modified dry milk will reach W13.0bn, staging a full recovery from the THAAD standoff that hurt China-bound exports in 2017; and 3) New product rollouts will put the brakes on the slowing domestic sales of modified dry milk.
- A share price re-rating looks likely in 2019 on account of white market milk's expected return to the black, full recovery of modified dry milk exports (which will start to build momentum in 4Q18 and gain significant traction in 2019), and better product mix that will likely help curb the slump in domestic sales of modified dry milk to a considerable degree despite structural problems.

Industry 4.0 safety rating ■ Neutral Green

KOSDAQ	668.13
Market cap (Wbn)	621
Market cap portion (%)	0.27
Paid-in capital (common; Wbn)	4
52w high/low (W)	101,500 / 62,300
120d avg. trading volume (Wbn)	2.9
Foreign ownership (%)	13.64
Major shareholders	Kim Jeong-wan+11: 57.74% Shinyoung Asset Management: 6.20%

(%)	1M	3M	6M	12M
Abs. return	10.3	-5.3	-8.8	21.3
Rel. return	14.1	16.4	14.7	37.1



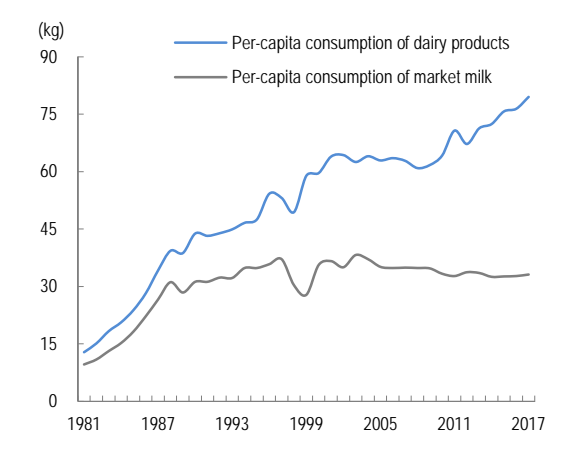
	4Q17	3Q18	Previous estimate	Daishin estimate	4Q18(F)			1Q19		
					YoY	QoQ	Consensus	Daishin estimate	YoY	QoQ
Revenue	326	334	326	327	0.2	-1.9	328	326	1.5	-0.3
OP	16	21	20	20	24.1	-4.8	19	19	18.7	-3.4
NP	9	17	12	12	39.0	-29.5	13	13	11.0	9.9

Operating results and major financial data

	2017A	2018F	2019F	2020F
Revenue	881	1,301	1,315	1,349
OP	51	77	84	89
Pretax profit	44	77	77	82
NP	35	60	59	61
NP (controlling int.)	35	60	59	61
EPS	6,932	7,773	7,503	7,802
PER	9.6	10.2	10.6	10.2
BPS	37,786	43,905	50,955	58,254
PBR	1.8	1.8	1.6	1.4
ROE	24.2	19.1	15.8	14.3

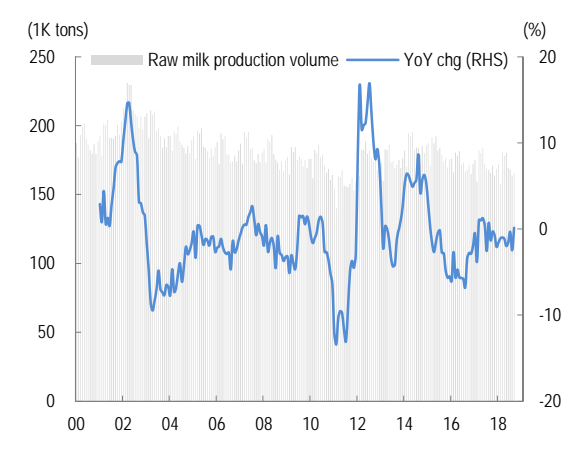
Note: EPS, BPS, and ROE are based only on the controlling interest.
Source: Maeil Dairies, Daishin Securities Research Center

Fig 1. Yearly per-capita consumption of dairy products and milk



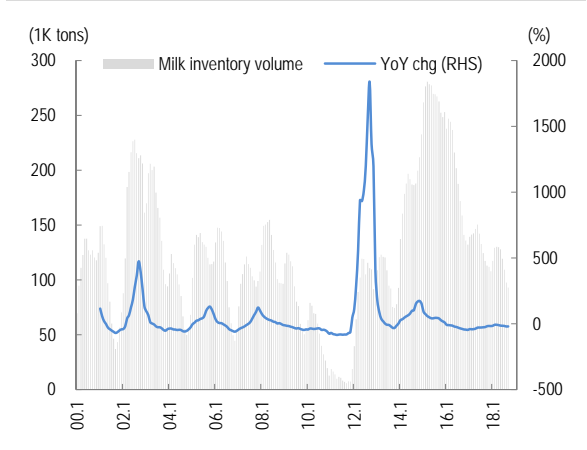
Source: Korea Dairy Committee, Daishin Securities Research Center

Fig 2. Yearly raw milk production volume



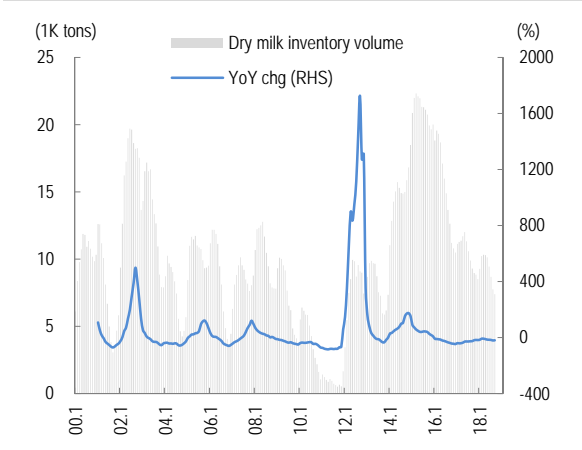
Source: Korea Dairy Committee, Daishin Securities Research Center

Fig 3. Milk inventory



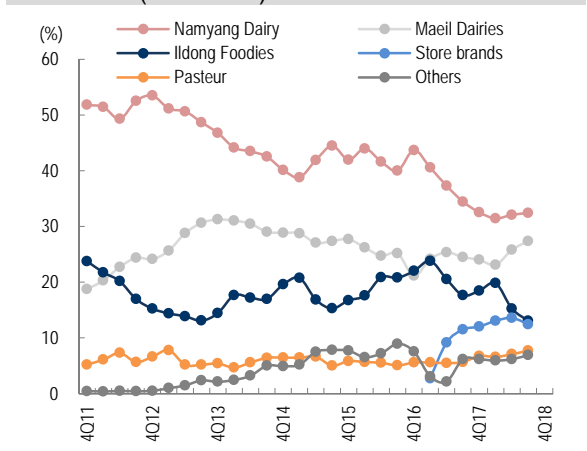
Source: Korea Dairy Committee, Daishin Securities Research Center

Fig 4. Monthly domestic inventories of dry milk



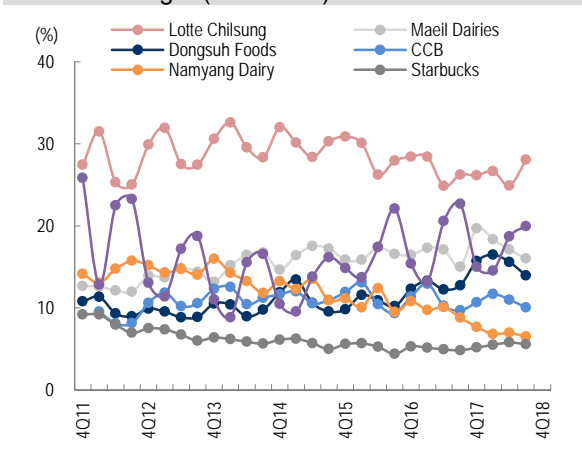
Source: Korea Dairy Committee, Daishin Securities Research Center

Fig 5. Domestic market breakdown of modified dry milk (retail stores)



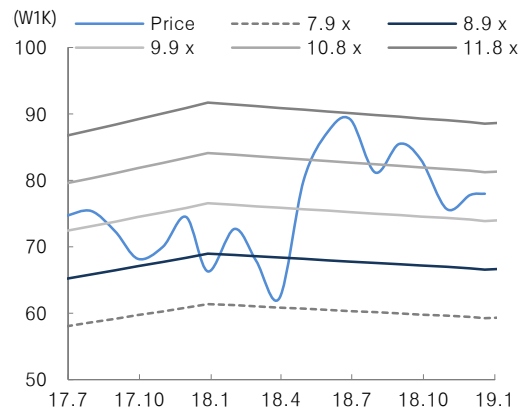
Source: Food Information Statistics System, Daishin Securities Research Center

Fig 6. Domestic market breakdown of coffee beverages (retail stores)



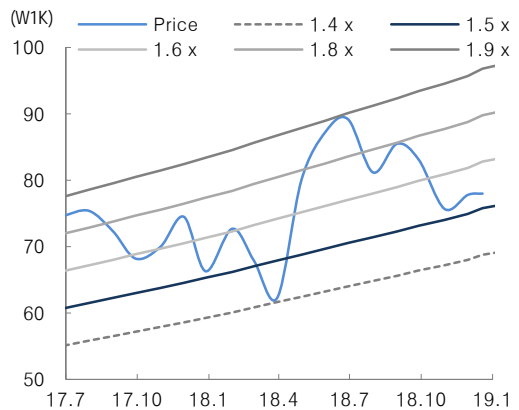
Source: Food Information Statistics System, Daishin Securities Research Center

Fig 7. Mael Dairies P/E band



Source: Mael Dairies, Valuewise, Daishin Securities Research Center

Fig 8. Mael Dairies P/B band



Source: Mael Dairies, Valuewise, Daishin Securities Research Center

Tab 1. Mael Dairies quarterly/ yearly earnings forecast (non-consolidated) (W'00mn)

	1Q18	2Q18	3Q18	4Q18E	1Q19E	2Q19E	3Q19E	4Q19E	2017	2018E	2019E	2020E
Revenue	3,211	3,192	3,335	3,271	3,260	3,223	3,365	3,304	13,178	13,008	13,152	13,487
YoY (%)	-2.0	-1.9	-1.4	0.2	1.5	1.0	0.9	1.0	-0.8	-1.3	1.1	2.5
COGS	2,352	2,260	2,361	2,313	2,364	2,259	2,359	2,313	9,019	9,286	9,295	9,513
YoY (%)	4.0	3.5	2.5	1.9	0.5	0.0	-0.1	0.0	-1.0	3.0	0.1	2.3
COGS/ Revenue (%)	73.3	70.8	70.8	70.7	72.5	70.1	70.1	70.0	68.4	71.4	70.7	70.5
S&A expense	694	742	763	756	701	757	782	773	3,457	2,955	3,014	3,083
YoY (%)	-21.1	-15.7	-11.9	-9.1	1.0	2.0	2.6	2.3	-0.5	-14.5	2.0	2.3
S&A expense ratio (%)	21.6	23.3	22.9	23.1	21.5	23.5	23.2	23.4	26.2	22.7	22.9	22.9
OP	164	189	211	202	195	206	224	218	680	767	843	891
YoY (%)	39.3	2.2	-1.2	24.1	18.5	8.8	6.2	7.9	-1.7	12.8	9.9	5.7
OP margin (%)	5.1	5.9	6.3	6.2	6.0	6.4	6.7	6.6	5.2	5.9	6.4	6.6
NP	122	183	174	123	135	144	158	152	347	602	588	612
YoY (%)	113.7	-90.4	8.8	39.0	11.0	-21.7	-9.6	24.0	0.0	73.2	-2.3	4.0
NP margin (%)	3.8	5.7	5.2	3.8	4.1	4.5	4.7	4.6	3.9	4.6	4.5	4.5

Source: Daishin Securities Research Center

Per share intrinsic value

Residual Income Model		(Wbn, W, %)									
		2018F	2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F	2027F
I	NP (contr. int.) ^(Note 2)	60	59	61	62	63	63	63	64	64	64
II	Shareholders' equity (contr. int.) ^(Note 2)	344	400	457	480	504	529	555	583	612	643
	Estimated ROE	19.1	15.8	14.3	12.9	12.4	11.9	11.4	10.9	10.4	9.9
III	Required rate of return ^(Note 3)	6.3									
	Risk free rate of return ^(Note 4)	4.0									
	Market risk premium ^(Note 5)	5.0									
	Beta	0.45									
IV	Spread (estimated ROE – required rate of return)	12.8	9.5	8.0	6.7	6.2	5.7	5.1	4.6	4.1	3.7
V	Required income	18	22	25	29	30	32	33	35	37	38
VI	Residual income (I - V)	42	37	36	33	33	32	30	29	27	25
	Present value factor	1.00	0.94	0.89	0.83	0.78	0.74	0.69	0.65	0.62	0.58
	PV of residual income	42	35	32	28	26	23	21	19	17	15
VII	Sum of residual income	257									
VIII	PV of residual income following forecasting period	235									
	Terminal growth (g) ^(Note 6)	0.0%									
IX	Beginning shareholders' equity	287									
X	Fair market cap (VII+VIII+IX)	780									
	Total number of shares (thousands)	7,844									
XI	Per share value (W)	99,449									
	Current share price (W)	79,200									
	Potential (%)	25.6%									

Note 1: Under the residual income model (RIM), we add the current shareholders' equity to the residual income based on the earnings forecast for the next ten years before adding the result to the residual income after the forecasting period to derive the value of shareholders' stakes. The RIM is considered less subjective than similar valuation models such as DDM, DCF, and EVA.

Note 2: The RIM reflects consolidated subsidiaries' earnings not in their entirety but only for the stake controlled by the company.

Note 3: The required rate of return (i.e., cost of equity) is the rate of return expected by the shareholders who take risks. It is derived by the capital asset price model: Cost of equity = Risk-free interest rate + Beta * Market risk premium.

Note 4: The yield on five-year government bonds was used as the proxy for the risk-free interest rate.

Note 5: Market risk premium refers to the gap between the expected return on the market portfolio and the risk-free interest rate. It has been lowered from 6-8% to 3-5% in reflection of the current low-growth environment.

Note 6: The terminal growth was assumed to be zero.

Tab 2. Global peers

		Nestle	Yili	Bright Dairy & Food	Mengniu Dairy	Danone	Fonterra
		NESN SW	600887 CH	600597 CH	2319 HK	BN FP	FSF NZ
Share price		82	3	1	3	72	3
Market cap (Wbn, \$mn)		252,617	19,669	1,411	11,918	49,133	4,905
Revenue	17A	91,557	10,007	3,193	8,912	27,878	13,737
(Wbn, \$mn)	18F	92,020	11,499	3,132	9,999	28,062	14,509
	19F	95,624	12,949	3,370	11,125	28,852	14,545
Revenue growth	17A	0.4	10.4	5.5	10.0	14.8	18.8
(% yoy)	18F	0.5	14.9	-1.9	12.2	0.7	5.6
	19F	3.9	12.6	7.6	11.3	2.8	0.3
OP	17A	10,273	1,051	200	470	4,218	774
(Wbn, \$mn)	18F	15,305	1,021	171	561	4,094	180
	19F	16,382	1,200	191	703	4,426	680
OP growth	17A	-23.1	35.6	4.9	-663.5	30.4	-15.9
(% yoy)	18F	49.0	-2.8	-14.2	19.3	-3.0	-76.7
	19F	7.0	17.5	11.3	25.3	8.1	277.4
OP margin (%)	17A	11.2	10.5	6.3	5.3	15.1	5.6
	18F	16.6	8.9	5.5	5.6	14.6	1.2
	19F	17.1	9.3	5.7	6.3	15.3	4.7
P/E (x)	17A	36.1	32.5	30.3	36.8	17.8	13.2
	18F	21.2	21.1	16.1	26.6	17.7	N/A
	19F	19.5	18.6	14.9	20.8	16.3	14.9
P/B (x)	17A	4.2	7.8	3.5	3.4	3.1	1.4
	18F	4.1	4.9	1.7	3.2	2.5	1.3
	19F	4.0	4.4	1.6	2.9	2.3	1.1
EV/EBITDA (x)	17A	14.5	21.5	10.3	15.2	13.1	10.6
	18F	14.9	14.6	6.2	14.6	12.4	10.6
	19F	14.0	12.7	5.8	12.2	11.7	8.9
ROE (%)	17A	11.4	24.9	11.9	9.4	17.8	10.5
	18F	19.6	23.3	10.4	12.7	14.4	-3.3
	19F	21.3	24.2	10.9	14.2	15.1	7.6
ROA (%)	17A	5.5	13.6	3.8	3.8	5.6	4.2
	18F	8.2	12.4	4.3	5.5	4.6	-1.2
	19F	8.4	13.4	4.6	6.7	5.4	5.5
EPS (\$)	17A	4.2	0.1	0.1	0.1	4.2	0.3
	18F	3.9	0.2	0.1	0.1	4.1	0.1
	19F	4.2	0.2	0.1	0.1	4.4	0.2

Source: Bloomberg, Daishin Securities Research Center

Company profile

Overview

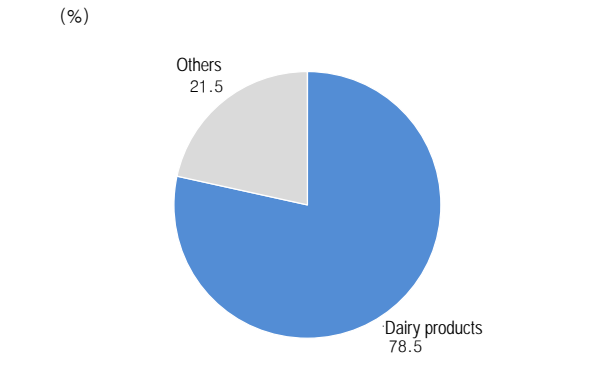
- Spun off from Maeil Holdings and re-listed on the stock market in June 2017.
- Produces milk, fermented products, modified dry milk, and what not.
- Operates four food services brands including *Paul Bassett* and *The Kitchen Salvatore*.
- Assets ₩652.4bn, liabilities ₩313.0bn, equities ₩339.4bn
- # of outstanding shares: 7,843,638 / # of treasury shares: 3,037

Share price catalysts

- Growth in exports of modified dry milk to China
- How fast domestic sales of modified dry milk are contracting
- How fast the newly established Chinese subsidiary will penetrate the Chinese coffee market

Note: Assets are as of September 2018.
Source: Maeil Dairies, Daishin Securities Research Center

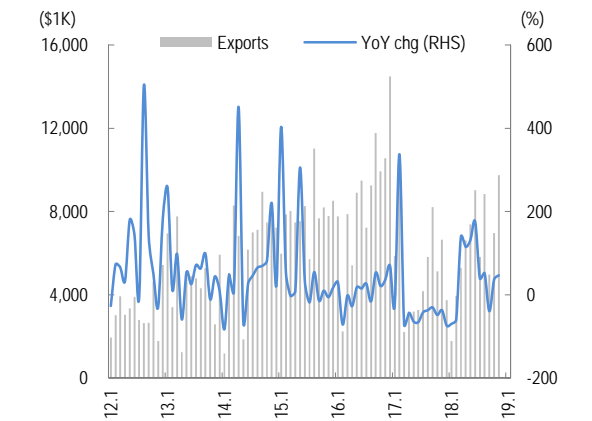
Revenue breakdown



Note 1: Based on 2018E revenue.
Note 2: Dairy products include white market milk, processed milk, fermented milk, Sang-a Farm, coffee beverages, cheese, and dry milk.
Source: Maeil Dairies, Dart, Daishin Securities Research Center

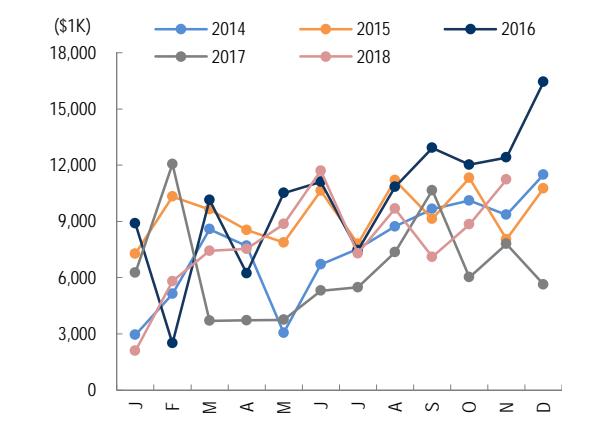
1. Earnings drivers

Fig 9. China-bound exports of modified dry milk



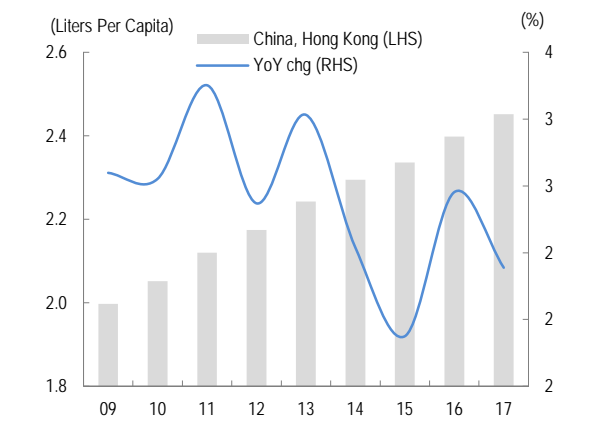
Source: Maeil Dairies, Korea Customs Service, Daishin Securities Research Center

Fig 10. Maeil Dairies' sales of modified dry milk



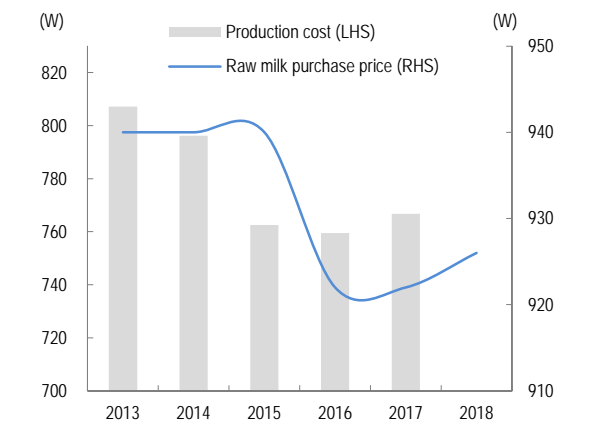
Source: Maeil Dairies, Korea Customs Service, Daishin Securities Research Center

Fig 11. China's coffee beverage market size



Source: Maeil Dairies, Bloomberg, Daishin Securities Research Center

Fig 12. Per-liter milk production cost and raw milk purchase price



Source: Maeil Dairies, Statistics Korea, Daishin Securities Research Center

Financial statements

Income statement		(Wbn)			
	2017A	2018F	2019F	2020F	
Revenue	881	1,301	1,315	1,349	
Cost of goods sold	602	929	930	951	
Gross profit	279	372	386	397	
S&A expenses	228	296	301	308	
OP	51	77	84	89	
OP margin	5.8	5.9	6.4	6.6	
EBITDA	67	99	107	112	
Non-OP	-7	0	-7	-8	
Income from affiliates	0	0	0	0	
Financial revenue	3	10	3	3	
FX related gains	1	1	1	2	
Financial expense	-7	-7	-7	-7	
FX related losses	0	0	0	0	
Others	-3	-3	-3	-3	
Income before taxes	44	77	77	82	
Income tax expense	-9	-17	-19	-20	
Income from cont. op.	35	60	59	61	
Income from discount. op.	0	0	0	0	
NP	35	60	59	61	
NP margin	3.9	4.6	4.5	4.5	
NP for non-contr. interest	0	0	0	0	
NP for contr. interest	35	60	59	61	
Valuation of AFS fin. assets	0	0	0	0	
Other compreh. income	0	0	0	0	
Comprehensive income	35	60	59	61	
Comp. income for non-contr. Int.	0	0	0	0	
Comp. income for contr. int.	35	0	0	0	

Valuation metrics		(W,x,%)			
	2017A	2018F	2019F	2020F	
EPS	6,932	7,773	7,503	7,802	
PER	9.6	10.2	10.6	10.2	
BPS	37,786	43,905	50,955	58,254	
PBR	1.8	1.8	1.6	1.4	
EBITDAPS	13,386	12,816	13,626	14,240	
EV/EBITDA	8.1	6.4	5.7	5.2	
SPS	175,688	167,906	167,676	171,945	
PSR	0.4	0.5	0.5	0.5	
CFPS	13,063	13,765	13,636	14,176	
DPS	450	450	500	500	

Financial ratios		(W,x,%)			
	2017A	2018F	2019F	2020F	
Growth potential					
Revenue growth		47.6	1.1	2.5	
OP growth		49.9	9.9	5.7	
NP growth		73.2	-2.3	4.0	
Profitability					
ROIC	20.5	14.5	14.5	14.3	
ROA	17.3	12.2	12.2	11.8	
ROE	24.2	19.1	15.8	14.3	
Stability					
Debt ratio	105.6	92.7	80.9	72.1	
Net borrowings ratio	13.6	5.3	-3.5	-9.7	
Interest coverage ratio	19.8	24.9	26.5	27.2	

Source: Mael Dairies, Daishin Securities Research Center

Balance sheet		(Wbn)			
	2017A	2018F	2019F	2020F	
Current assets	331	363	400	439	
Cash & cash equiv.	37	59	92	124	
Trade & other receive.	168	176	178	182	
Inventories	102	104	105	108	
Other current assets	24	24	25	25	
Long-term assets	260	301	323	347	
Tangible assets	220	260	282	306	
Investments in affiliates	0	0	0	0	
Other long-term assets	40	41	41	41	
Total assets	591	664	723	786	
Current liabilities	233	247	249	253	
Payables & other liab.	177	190	191	194	
Borrowings	0	0	0	0	
Current portion of LT debts	40	40	41	42	
Other current liabilities	16	17	17	17	
Long-term liabilities	70	72	74	76	
Borrowings	53	54	55	56	
Convertible securities	0	0	0	0	
Other long-term liab.	17	18	19	20	
Total liabilities	303	319	323	329	
Controlling interest	287	344	400	457	
Capital stock	4	4	4	4	
Capital surplus	249	249	249	249	
Retained earnings	35	92	147	204	
Other capital changes	0	0	0	0	
Non-controlling interest	0	0	0	0	
Total shareholder's equity	287	344	400	457	
Net borrowings	39	18	-14	-44	

Cash flow statement		(Wbn)			
	2017A	2018F	2019F	2020F	
Operating cash flows	97	109	102	102	
NP	35	60	59	61	
Non-cash items	31	46	48	50	
Depreciation	16	23	23	23	
FX gains	0	1	1	1	
Equity method gain	0	0	0	0	
Others	14	23	25	26	
Chg in assets & liab.	36	21	15	13	
Other cash flows	-4	-19	-20	-22	
Investing cash flow	-58	-100	-85	-87	
Investment assets	2	0	0	0	
Tangible assets	-43	-87	-72	-74	
Others	-16	-14	-13	-13	
Financing cash flows	-49	-3	-3	-3	
Short-term borrowings	-20	0	0	0	
Bonds payable	0	1	1	1	
Long-term borrowings	0	0	0	0	
Rights offering	14	0	0	0	
Cash dividends	0	-3	-4	-4	
Others	-43	-1	-1	0	
Net chg in cash	-9	22	33	32	
Beginning cash balance	46	37	59	92	
Ending cash balance	37	59	92	124	
NOPLAT	41	60	64	67	
FCF	12	27	30	31	

[Daishin House View: Industry 4.0 safety rating]

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- Depending on whether Industry 4.0 will have a positive, neutral, or negative impact, each industry and company is assigned one of three safety ratings:

Dark Gray (negative)	Neutral Green (neutral)	Sky Blue (positive)
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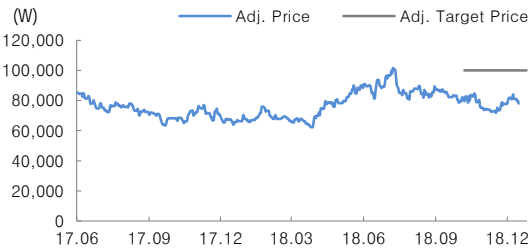
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[Investment rating & Target price history]

Maeil Dairies (267980 KQ)



Date	18.12.21	18.12.10	18.11.19	18.10.30	18.10.11
Rating	Buy	Buy	Buy	Buy	Buy
Target price	100,000	100,000	100,000	100,000	100,000
Diff. (avr. %)		(22.07)	(22.54)	(22.38)	(18.45)
Diff. (max/min, %)		(15.30)	(15.30)	(15.30)	(15.30)
Date					
Rating					
Target price					
Diff. (avr. %)					
Diff. (max/min, %)					
Date					
Rating					
Target price					
Diff. (avr. %)					
Diff. (max/min, %)					
Date					
Rating					
Target price					
Diff. (avr. %)					
Diff. (max/min, %)					

Investment rating breakdown and framework (Dec 17, 2018)

	BUY	MARKETPERFORM	UNDERPERFORM
Ratio	85.0%	14.0%	1.0%

Sector ratings breakdown

- Overweight: industry indicators are expected to outperform the market over the next six months.
- Neutral: industry indicators are expected to be in line with the market over the next six months.
- Underweight: industry indicators are expected to underperform the market over the next six months.

Company ratings breakdown

- Buy: the stock is expected to outperform the market by at least 10%p over the next six months.
- Marketperform: the stock is expected to either outperform or underperform the market by less than 10%p over the next six months.
- Underperform: the stock is expected to underperform the market by at least 10%p over the next six months.