

SK Materials

(036490 KQ)

Lee Su-bin
subin.lee@daishin.com

Rating **BUY**
initiate

6M TP (₩) **200,000**
initiate

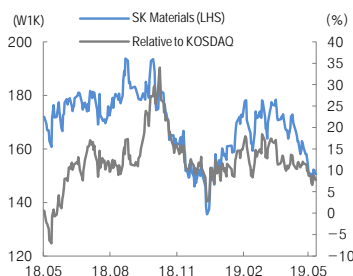
CP (₩)
(19.06.03) **150,600**

Semiconductors

Industry 4.0 safety rating ■ Sky Blue

KOSDAQ	697.50
Market cap (Wbn)	1,588
Market cap portion (%)	0.66
Paid-in capital (common; Wbn)	5
52w high/low (₩)	193,800 / 135,600
120d avg. trading volume (Wbn)	5.6
Foreign ownership (%)	14.42
Major shareholders	SK+1: 49.11%

(%)	1M	3M	6M	12M
abs. return	-11.2	-11.8	-9.7	-7.6
Rel. return	-3.0	-7.5	-8.2	17.0



Scaling-up efforts to pay off

BUY and 6M TP of ₩200,000

- The target price of ₩200,000 is based on the 2019E EPS and a target P/E of 13.5x.
- The target multiple represents a 20% discount to the global semiconductor display materials suppliers' average P/E of 17.5x. Also taken into account is the company's position as the nation's largest display materials vendor and its solid growth trajectory, which is supported by its synergies with SK affiliates.

2019 preview: revenue ₩804.1bn(+17%yoy), OP ₩226.4bn(+24%yoy)

- The company reported in-line OP of ₩54.5bn (up 61% yoy) in 1Q19, a quarter when other materials suppliers fared poorly due to delayed capacity expansions and reduced utilization rates at memory chip makers. Sales volume fell to mid-single digits for both NF3 and WF6, but the company was able to maintain its OP margin thanks to the price drop in HF, a major raw material.
- Contrary to market concerns over industry conditions, the company's OP growth is likely to remain similar yoy at 24% for the whole of 2019 thanks to its business diversification push, which should help ease the company's reliance on a specific downstream industry and ultimately improve both the top and bottom line results.

Scaling-up efforts continue; 2020 revenue, OP to rise 27%, 30% yoy

- The special gas unit is forecast to expand its production capacity by 1,500 tons in 2H19, which, in turn, should increase both revenue and OP in 2020. It will also benefit from a more efficient manufacturing process, which should push up the capacity of NF3 and WF6 by 600 tons (+3%) and 300 tons (+25%), respectively, in 2019.
- There are a number of positive catalysts ahead for the company: an uptick in NF3 demand following a shift from LCD to OLED, a rise in POLED production by Korea's display panel makers in 2H19, a production line change at Samsung Display (L8-1 to manufacture QD-OLED), the opening of LG Display's Guangzhou fab, and new capex investments by Chinese display panel companies.
- SK Airgas, a wholly owned subsidiary, is poised to improve its product mix, and by extension, earnings, once its production capacity expansion is completed in 2H20 as scheduled. Since it was acquired in 2016, SK Airgas has been widening OP margin each year thanks to growing orders from captive customers and stabilized production facilities. Its OP margin is 12%p higher than that of the company.

Operating results and major financial data

(Wbn, ₩, x, %)

	2017A	2018A	2019F	2020F	2021F
Revenue	512	687	804	1,022	1,124
OP	148	183	226	293	326
Pretax profit	135	160	202	269	299
NP	104	123	156	208	231
NP (controlling int.)	102	113	156	208	231
EPS	9,660	10,682	14,821	19,702	21,929
PER	18.6	14.1	10.2	7.6	6.9
BPS	36,567	35,670	47,118	63,447	82,003
PBR	4.9	4.2	3.0	2.2	1.7
ROE	25.3	29.6	35.8	35.6	30.2

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

Tab 1. SK Materials' earnings trend and forecast

(Wbn)

	1Q18	2Q18	3Q18	4Q18	1Q19E	2Q19F	3Q19F	4Q19F	2018	2019F	2020F
Revenue	142	158	186	201	184	189	206	225	687	804	1022
YoY%	22%	27%	41%	44%	29%	20%	11%	12%	34%	17%	27%
OP	34	41	51	57	55	56	57	59	183	226	293
YoY%	2%	8%	28%	56%	61%	38%	11%	3%	24%	24%	30%
OP margin%	24%	26%	28%	28%	30%	30%	28%	26%	27%	28%	29%
EBITDA	54	64	76	83	82	84	88	93	277	347	447
EBITDA margin%	38%	40%	41%	41%	44%	45%	43%	41%	40%	43%	44%
Revenue by business											
Special gas (SK Materials, SK Showa Denko)	115	123	132	137	121	124	134	142	507	520	626
Industrial gas (SK Airgas)	24	26	32	40	40	41	48	57	122	186	269
Precursors (SK Trichem)	3	8	22	25	23	24	25	26	59	98	126
Total	142	158	186	201	184	189	206	225	687	804	1022
Revenue by business QoQ%											
Special gas (SK Materials, SK Showa Denko)	1%	7%	7%	4%	-12%	2%	8%	6%	21%	3%	20%
Industrial gas (SK Airgas)	-5%	10%	21%	24%	0%	5%	15%	20%	33%	53%	45%
Precursors (SK Trichem)	120%	148%	172%	10%	-5%	1%	5%	4%	3769%	67%	29%
Total	1%	11%	18%	8%	-9%	3%	9%	9%	34%	17%	27%
Revenue share (%)											
Special gas (SK Materials, SK Showa Denko)	81%	78%	71%	68%	66%	65%	65%	63%	74%	65%	61%
Industrial gas (SK Airgas)	17%	17%	17%	20%	21%	22%	23%	25%	18%	23%	26%
Precursors (SK Trichem)	2%	5%	12%	12%	13%	13%	12%	12%	9%	12%	12%
Total	100%	100%	100%	100%	100%	100%	100%	100%	210%	-50%	59%
OP											
Special gas (SK Materials, SK Showa Denko)	26	30	30	31	27	30	29	30	117	116	140
Industrial gas (SK Airgas)	7	8	10	13	16	16	16	18	38	66	95
Precursors (SK Trichem)	1	3	11	13	12	11	11	11	28	45	58
Total	34	41	51	57	55	56	57	59	183	226	293
OP margin (%)											
Special gas (SK Materials, SK Showa Denko)	23%	24%	23%	22%	22%	24%	22%	21%	23%	22%	22%
Industrial gas (SK Airgas)	30%	29%	31%	34%	40%	38%	34%	32%	31%	36%	35%
Precursors (SK Trichem)	19%	39%	48%	52%	51%	45%	45%	42%	47%	46%	46%
Total	24%	26%	28%	28%	30%	30%	28%	26%	27%	28%	29%

Source: SK Materials, Daishin Securities Research Center

Tab 2. SK Materials's valuation table

(Wbn, x, %)

	2019F	12MF
NP (contr. int.) (Wbn)	156	181
# of outstanding shares ('000 shares)	10,548	
EPS (W)	14,821	17,157
Target P/E	13.5	14.0
Fair value (W)	200,089	240,204
TP (W)	200,000	
CP (W)	150,600	
Current P/E	10.2	8.8
Upside potential (%)	33%	71%

Note: As of June 3, 2019

Source: SK Materials, Daishin Securities Research Center

Tab 3. SK Materials's historical valuations

(W, x)

	2015	2016	2017	2018	2019F
EPS (contr. int.)	6,270	10,299	9,660	10,682	14,821
PER (contr. int.) (End)	19	17	19	14	10
PER (contr. int.) (High)	23	18	22	18	12
PER (contr. int.) (Low)	8	9	16	13	9
PER (contr. int.) (Avg)	16	13	19	16	11
BPS (contr. int.)	35,670	39,945	36,567	35,670	47,118
PBR (contr. int.) (End)	3.3	4.5	4.9	4.2	3.2
PBR (contr. int.) (High)	4.0	4.7	5.7	5.5	3.9
PBR (contr. int.) (Low)	1.4	2.3	4.2	3.8	2.8
PBR (contr. int.) (Avg)	2.8	3.3	5.0	4.7	3.5
EV/EBITDA (End)	8.2	9.8	10.9	8.8	7.6
EV/EBITDA (High)	9.9	10.1	12.3	10.5	8.4
EV/EBITDA (Low)	4.2	5.8	9.8	8.3	7.1
EV/EBITDA (Avg)	7.2	7.6	11.1	9.5	8.0

Note: EPS (contr. int.) includes treasury shares.

Source: SK Materials, Daishin Securities Research Center

Tab 4. SK Materials's peers

		SK Materials	Hyosung Chemical	Foosung	Entegris	Air Products	Kanto Denka	Air Liquide
FY ends in		12	12	12	12	09	03	12
Currency		KRW	KRW	KRW	\$	\$	JPY	EUR
Share price (local currency)		152,600	147,500	7,190	34	204	704	112
Market cap.(local currency)		1,588	471	666	4,654	44,817	41	48
Market cap.(\$mn)		1,334	395	560	4,654	44,817	373	53,463
Stock exchange		KOSDAQ	KOSPI	KOSPI	SDAQ GS	New York	Tokyo	EN Paris
Revenue	2018	687	1,117	275	1,550	8,930	5,131	21,011
(local currency)	2019F	804	1,919	306	1,601	9,234	5,450	22,187
	2020F	1,022	2,334	387	1,708	9,963	6,450	23,257
OP	2018	183	65	40	293	1,966	905	3,287
(local currency)	2019F	226	143	46	369	2,247	570	3,809
	2020F	293	181	70	429	2,529	1,183	4,106
OP margin	2018	26.6	5.8	14.4	18.9	22.0	17.6	15.6
(%)	2019F	28.2	7.4	15.0	23.0	24.3	10.5	17.2
	2020F	28.7	7.7	18.1	25.1	25.4	18.3	17.7
NP	2018	113	20	28	241	1,498	6,116	2,113
(local currency)	2019F	156	72	37	267	1,821	4,100	2,362
	2020F	208	94	57	307	2,086	8,253	2,601
PER	2018	14.1	13.7	29.8	18.4	22.2	10.1	21.9
(x)	2019F	10.2	6.5	16.8	17.6	24.7	9.9	20.1
	2020F	7.6	5.0	11.5	15.4	21.7	4.9	18.4
PBR	2018	4.2	1.3	4.4	3.8	3.4	1.6	2.6
(x)	2019F	3.2	1.1	2.7	4.1	3.9	0.8	2.5
	2020F	2.4	0.9	2.2	3.6	3.5	0.7	2.4
ROE	2018	29.6	0.0	12.4	24.0	14.3	17.3	12.4
(%)	2019F	35.8	17.9	13.9	26.7	16.1		12.9
	2020F	35.6	19.5	18.3	21.3	17.0		13.3
EV/EBITDA	2018	8.8	9.8	13.1	9.9	12.6	4.9	11.4
(x)	2019F	7.6	6.3	6.1	11.6	13.4		10.7
	2020F	6.2	5.8	4.4	10.4	11.9		10.1
Payout ratio	2018	28.8	15.6		16.5	64.0	10.3	55.1
(%)	2019F	22.7	5.4		16.5	64.0	11.4	55.1
	2020F	17.1	4.6		16.5	64.0	11.4	55.1
EPS	2018	10,682	11,059	303	2	7	106	5
(local currency)	2019F	14,821	22,614	397	2	8	71	6
	2020F	19,702	29,515	619	2	9	144	6
BPS	2018	35,670	115,567	2,651	7	49	672	42
(local currency)	2019F	47,118	137,580	3,065	8	53	890	44
	2020F	63,447	166,157	3,702	10	58	1,013	47
DPS	2018	3,750	1,000		0.3	4	11	3
(local currency)	2019F	3,750	1,214		0.3	4	13	3
	2020F	3,750	1,357					

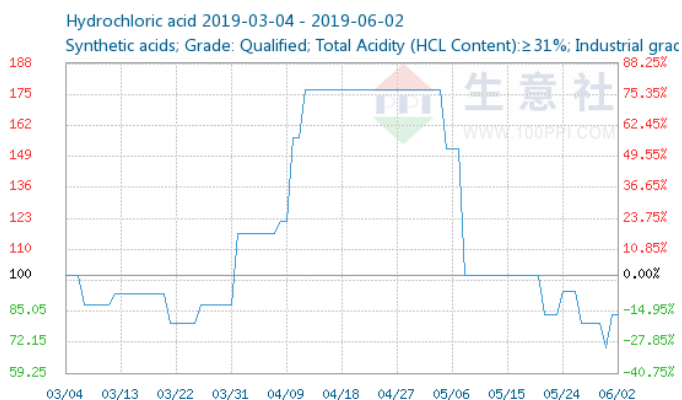
Note 1: Domestic companies' data are as of June 3, while those of overseas companies are as of May 31.

Note 2: Revenue, OP, and NP are in terms of Wbn, million yuan, million Taiwan dollars, 100 million yen, million dollars, and million euros

Note 3: The share price, EPS, BPS, and DPS are in terms of won, yuan, Taiwanese dollars, yen, dollars, and euro.

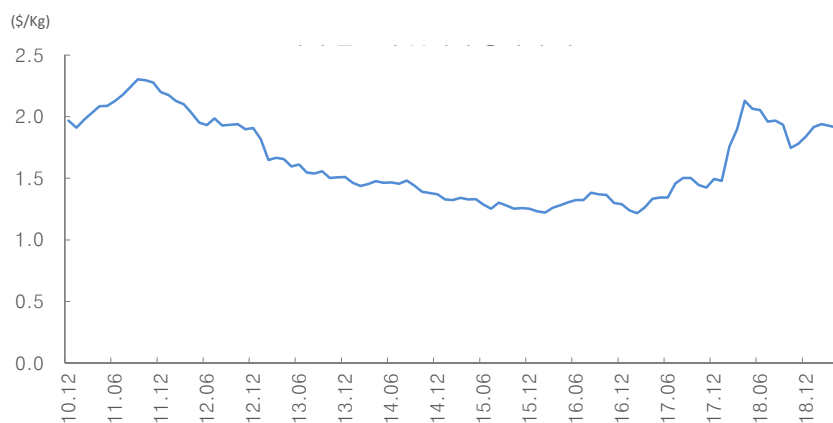
Source: Bloomberg, Quantwise, Daishin Securities Research Center

Fig 1.HF: price trend



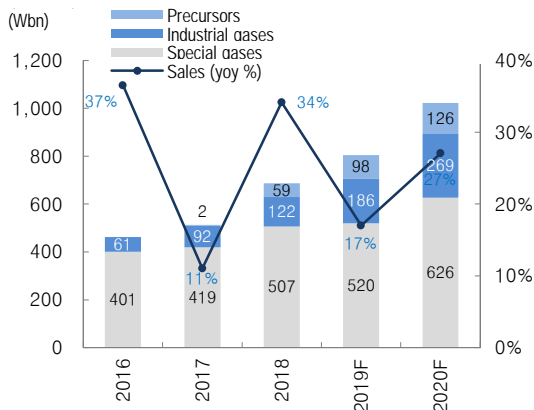
Source: SunSirs, Daishin Securities Research Center

Fig 2.HF: import price trend



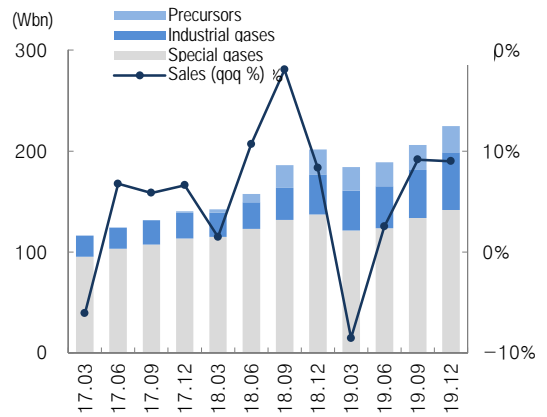
Source: Trade statistics, Daishin Securities Research Center

Fig 3. Yearly revenue trend



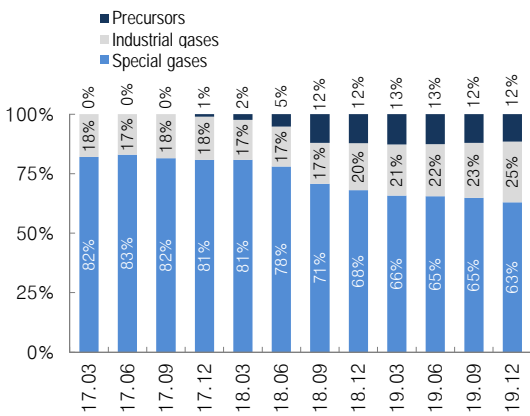
Source: SK Materials, Daishin Securities Research Center

Fig 4. Quarterly revenue trend



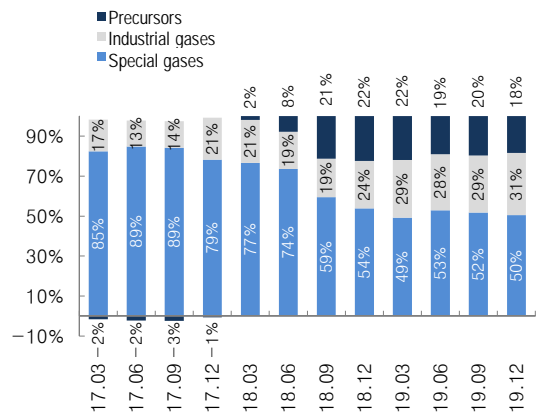
Source: SK Materials, Daishin Securities Research Center

Fig 5. Revenue breakdown by business



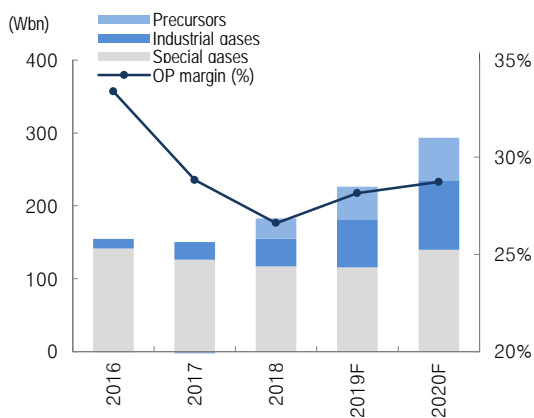
Source: SK Materials, Daishin Securities Research Center

Fig 6. OP breakdown by business



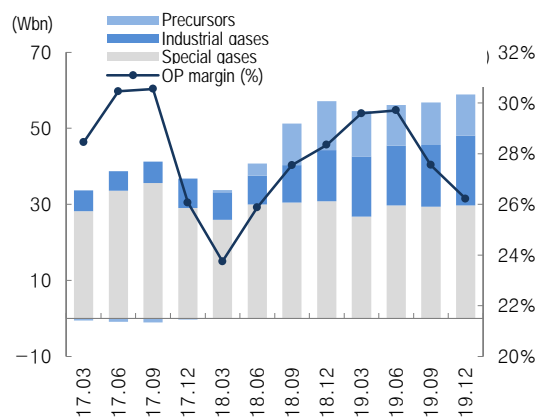
Source: SK Materials, Daishin Securities Research Center

Fig 7. Annual OP by business



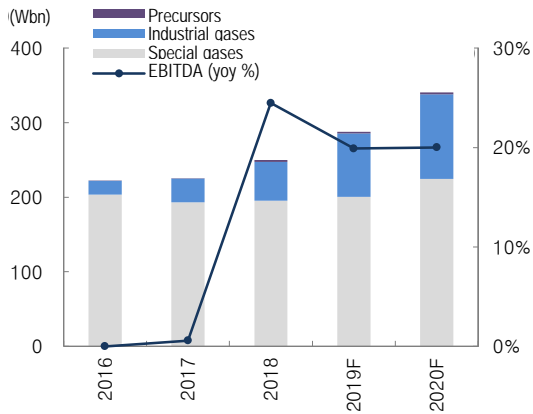
Source: SK Materials, Daishin Securities Research Center

Fig 8. Quarterly OP by business



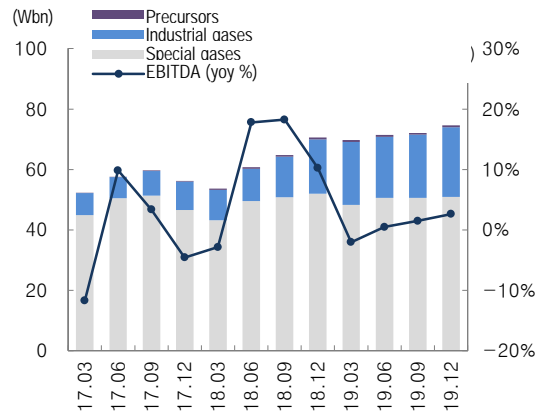
Source: SK Materials, Daishin Securities Research Center

Fig 9. Annual EBITDA by business



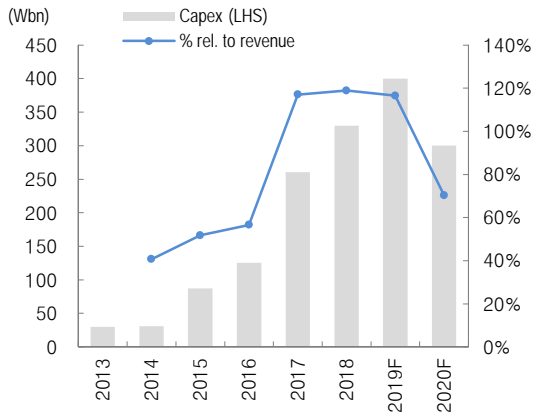
Source: SK Materials, Daishin Securities Research Center

Fig 10. Quarterly EBITDA by business



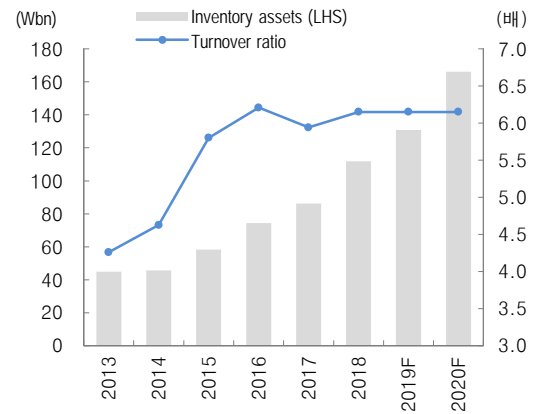
Source: SK Materials, Daishin Securities Research Center

Fig 11. Capex trend



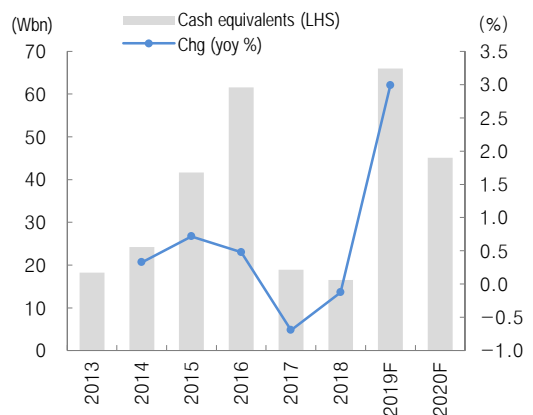
Source: SK Materials, Daishin Securities Research Center

Fig 12. Inventory assets trend



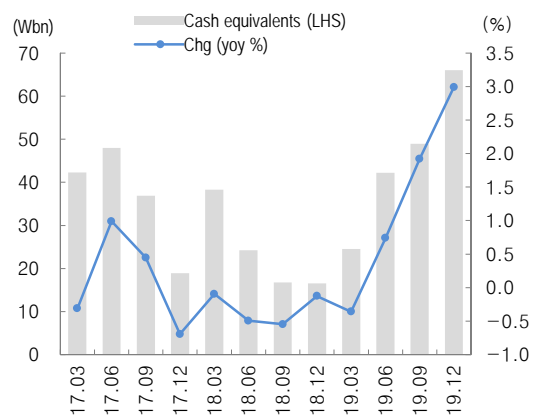
Source: SK Materials, Daishin Securities Research Center

Fig 13. Cash & cash equivalents



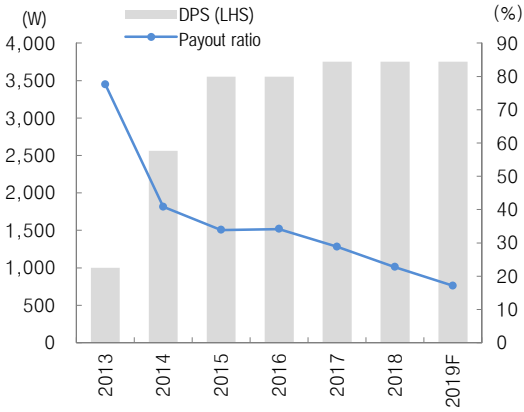
Source: SK Materials, Daishin Securities Research Center

Fig 14. Cash & cash equivalents



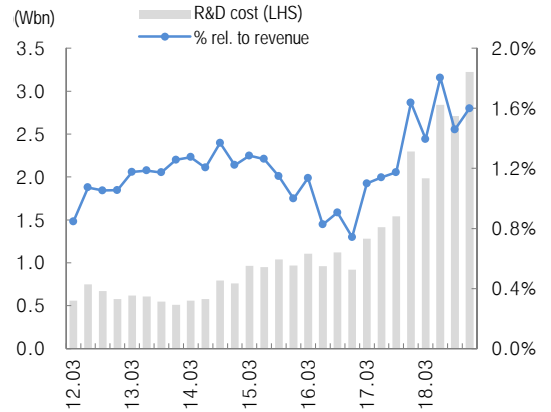
Source: SK Materials, Daishin Securities Research Center

Fig 15. Payout ratio and DPS



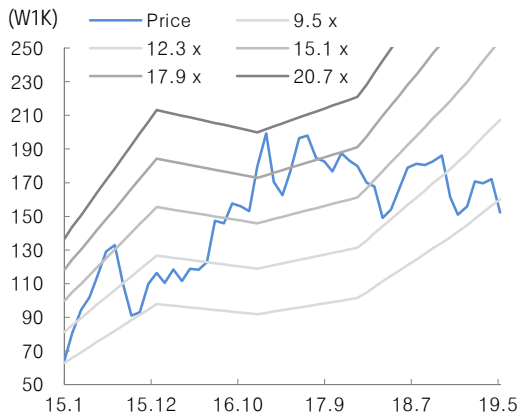
Source: SK Materials, Daishin Securities Research Center

Fig 16. R&D expenses



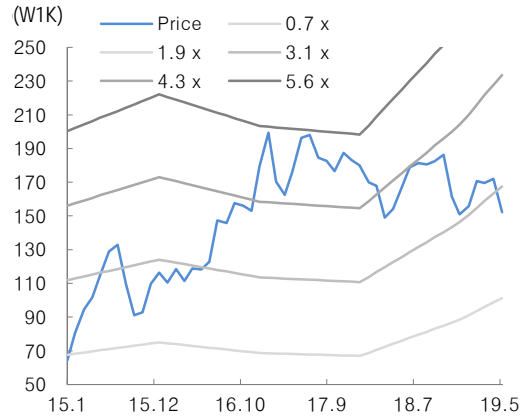
Source: SK Materials, Daishin Securities Research Center

Fig 17. P/E band



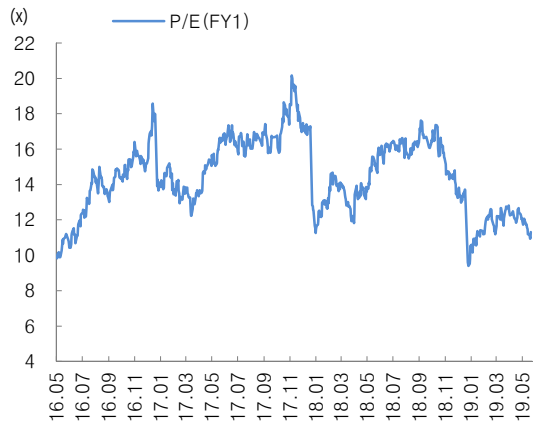
Source: SK Materials, Daishin Securities Research Center

Fig 18. P/B band



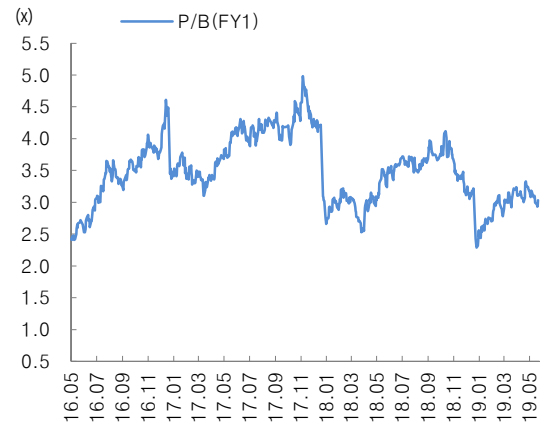
Source: SK Materials, Daishin Securities Research Center

Fig 19. P/E trend



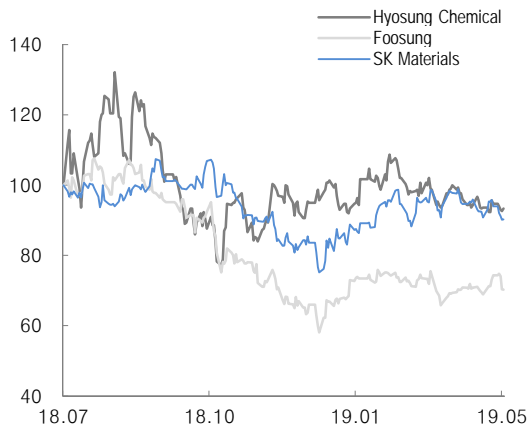
Source: SK Materials, Daishin Securities Research Center

Fig 20. P/B trend



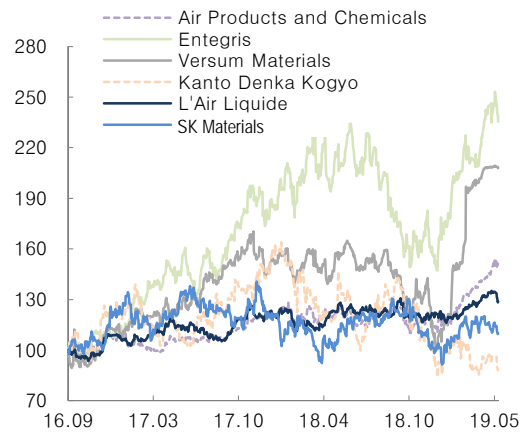
Source: SK Materials, Daishin Securities Research Center

Fig 21. SK Materials' share price rel. to domestic peers



Note: Jul 13, 2018 share prices = 100
 Source: SK Materials, Daishin Securities Research Center

Fig 22. SK Materials' share price rel. to global peers



Note: Sep 19, 2016 share prices = 100
 Source: SK Materials, Daishin Securities Research Center

Company profile

Overview

- Produces special gases (NF3, WF6, SiH4) used in the manufacturing of semiconductors, display panels, and solar cells
- Major shareholders: SK 49.10%
- # of outstanding shares: 10,547,673
- Payout ratio: 31.6%

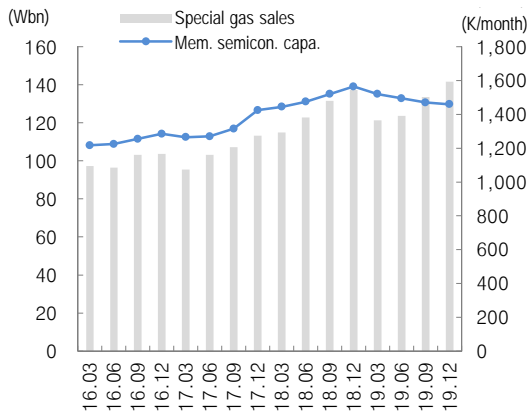
Share price catalysts

- Import price of HF (raw material)
- Capacity expansions at competitors
- Conditions of downstream industries (semiconductor, display)

Note: The stock count is based on both common and preferred shares (Mar 2019).
Based on 2018 payout ratio.
Source: SK Materials, Daishin Securities Research Center

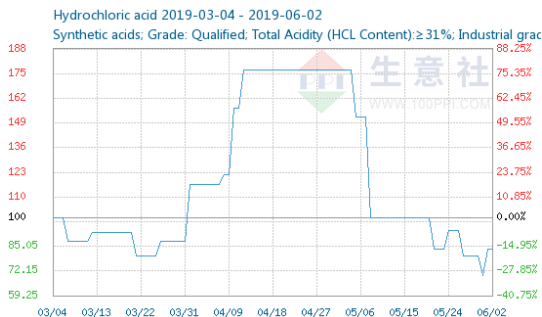
Earnings drivers

Fig 23. Memory semiconductor makers' capacity vs. Special gas sales



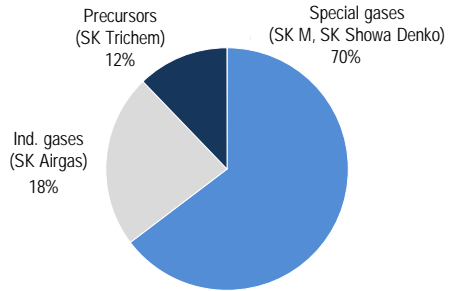
Source: SK Materials, Daishin Securities Research Center

Fig 25. HF: price trend



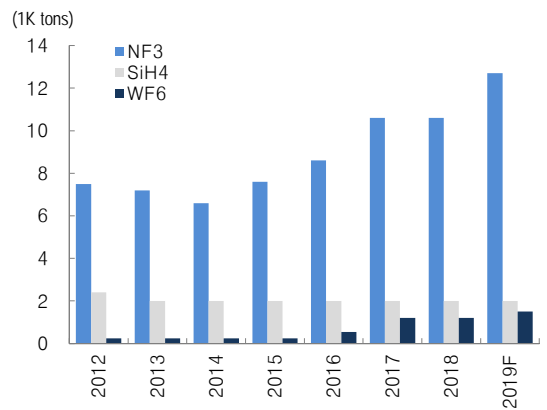
Source: SK Materials, Daishin Securities Research Center

Revenue share



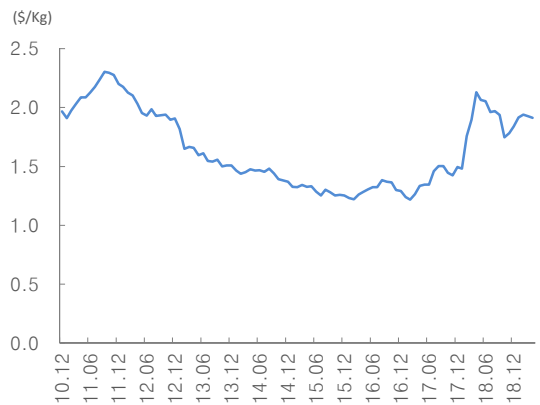
Note: Based on 2019E revenue.
Source: SK Materials, Daishin Securities Research Center

Fig 24. Production capacity of special gases



Source: SK Materials, Daishin Securities Research Center

Fig 26. HF: import price trend



Source: SK Materials, Daishin Securities Research Center

Financial statements

Income statement	(Wbn)				
	2017A	2018A	2019F	2020F	2021F
Revenue	512	687	804	1,022	1,124
Cost of goods sold	315	430	497	633	708
Gross profit	198	257	307	388	416
SG&A expenses	50	74	81	95	90
OP	148	183	226	293	326
OP margin	28.8	26.6	28.2	28.7	29.0
EBITDA	223	277	343	427	474
Non-OP	-13	-23	-24	-25	-27
Income from affiliates	0	0	0	0	0
Financial revenue	14	10	7	7	7
FX related gains	0	0	0	0	0
Financial expense	-26	-31	-32	-32	-34
FX related losses	11	8	4	4	4
Others	-2	-2	0	0	0
Income before taxes	135	160	202	269	299
Income tax expense	30	36	46	61	68
Income from cont. op.	104	123	156	208	231
Income from discount op.	0	0	0	0	0
NP	104	123	156	208	231
NP margin	20.3	18.0	19.4	20.3	20.6
NP for non-contr. interest	2	11	0	0	0
NP for contr. interest	102	113	156	208	231
Valuation of AFS fin. assets	0	0	0	0	0
Other compreh. income	-1	2	0	0	0
Comprehensive income	99	146	156	208	231
Comp. income for non-contr. Int.	2	11	0	0	0
Comp. income for contr. int.	97	135	156	208	231

Valuation metrics	(W, x, %)				
	2017A	2018A	2019F	2020F	2021F
EPS	9,660	10,682	14,821	19,702	21,929
PER	18.6	14.1	10.2	7.6	6.9
BPS	36,567	35,670	47,118	63,447	82,003
PBR	4.9	4.2	3.0	2.2	1.7
EBITDAPS	21,124	26,295	32,551	40,458	44,941
EV/EBITDA	10.9	8.8	7.6	6.2	5.6
SPS	48,569	65,157	76,234	96,858	106,544
PSR	3.7	2.3	2.0	1.6	1.4
CFPS	21,530	26,905	33,146	41,052	45,535
DPS	3,550	3,750	3,750	3,750	3,750
		10,682	14,821	19,702	21,929

Financial ratios	(W, x, %)				
	2017A	2018A	2019F	2020F	2021F
Growth potential					
Revenue growth	11.0	34.2	17.0	27.1	10.0
OP growth	-4.2	23.9	23.8	29.6	11.1
NP growth	-5.8	18.6	26.7	32.9	11.3
Profitability					
ROIC	12.7	12.1	11.9	13.2	13.1
ROA	14.6	14.5	14.4	15.9	15.6
ROE	25.3	29.6	35.8	35.6	30.2
Stability					
Debt ratio	173.9	246.7	225.8	171.4	141.9
Net borrowings ratio	125.5	205.8	184.7	142.8	107.0
Interest coverage ratio	11.4	8.6	8.6	11.0	11.3

Balance sheet	(Wbn)				
	2017A	2018A	2019F	2020F	2021F
Current assets	202	264	329	377	523
Cash & cash equiv.	19	16	66	45	159
Trade & other receive.	91	126	123	156	171
Inventories	86	112	131	166	183
Other current assets	6	10	10	10	10
Long-term assets	916	1,135	1,406	1,570	1,720
Tangible assets	885	1,106	1,388	1,553	1,703
Investments in affiliates	11	0	0	0	0
Other long-term assets	20	29	18	17	16
Total assets	1,118	1,398	1,736	1,947	2,243
Current liabilities	337	501	694	652	737
Payables & other liab.	140	110	113	118	121
Borrowings	149	275	325	375	425
Current portion of LT debts	30	94	233	135	167
Other current liabilities	17	23	24	24	25
Long-term liabilities	373	494	509	577	578
Borrowings	352	478	492	560	560
Convertible securities	0	0	0	0	0
Other long-term liab.	21	16	17	18	18
Total liabilities	710	995	1,203	1,229	1,316
Controlling interest	386	376	497	669	865
Capital stock	5	5	5	5	5
Capital surplus	34	19	19	19	19
Retained earnings	446	521	642	814	1,010
Other capital changes	-100	-170	-170	-170	-170
Non-controlling interest	22	27	36	48	62
Total shareholder's equity	408	403	533	717	927
Net borrowings	512	830	984	1,024	992

Cash flow statement	(Wbn)				
	2017A	2018A	2019F	2020F	2021F
Operating cash flows	137	176	288	307	378
NP	104	123	156	208	231
Non-cash items	123	160	193	225	249
Depreciation	75	94	117	133	148
FX gains	-2	2	-2	-2	-2
Equity method gain	0	0	0	0	0
Others	50	64	78	94	103
Chg in assets & liab.	-46	-56	11	-38	-5
Other cash flows	-45	-52	-72	-88	-97
Investing cash flow	-268	-330	-381	-290	-290
Investment assets	-11	-10	9	0	0
Tangible assets					-261
Others	3	7	7	7	7
Financing cash flows	92	152	136	-48	14
Short-term borrowings	88	126	50	50	50
Bonds payable	99	140	0	50	0
Long-term borrowings	86	109	14	17	0
Rights offering	0	0	0	0	0
Cash dividends	-37	-36	-36	-36	-36
Others	-144	-187	107	-130	0
Net chg in cash	-42	-3	50	-21	114
Beginning cash balance	60	19	16	66	45
Ending cash balance	19	16	66	45	159
NOPLAT	114	141	175	227	252
FCF	-71	-94	-108	60	100

Source: SK Materials,, Daishin Securities Research Center

[Daishin House View: Industry 4.0 safety rating]

- Daishin Securities assigns safety ratings to individual sectors and companies based on analyses and discussions by our analysts.
- 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:

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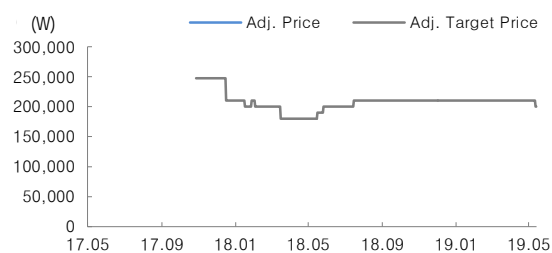
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[Investment rating & Target price history]

SK Materials (036490 KQ)



Date	19.06.04		19.02.07	18.08.07	18.06.18	18.06.08
Rating	BUY		6M passed	BUY	BUY	BUY
Target price	200,000	Analyst changed	210,000	210,000	200,000	190,000
Diff. (avr. %)			(20.42)	(19.95)	(11.37)	(8.29)
Diff. (max./min., %)			(15.05)	(7.71)	(9.15)	(6.63)
Date	18.04.08	18.02.25	18.02.19	18.02.08	18.01.08	17.11.19
Rating	BUY	BUY	BUY	BUY	BUY	BUY
Target price	180,000	200,000	210,000	200,000	210,000	247,300
Diff. (avr. %)	(12.16)	(20.90)	(17.31)	(15.89)	(21.56)	(25.77)
Diff. (max./min., %)	(2.06)	(12.90)	(16.43)	(11.40)	(17.14)	(17.23)
Date						
Rating						
Target price						
Diff. (avr. %)						
Diff. (max./min., %)						
Date						
Rating						
Target price						
Diff. (avr. %)						
Diff. (max./min., %)						

Investment rating breakdown and framework (Jun 1, 2019)

	BUY	MARKETPERFORM	UNDERPERFORM
Ratio	88.4%	11.1%	0.0%

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.