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## Potential IPOs and the beneficiaries

### What lies ahead?

The IPO of Samsung Life now draws attention to the steps ahead by Samsung Group. Given that a holding company structure works to stabilize managerial rights, the transition should be a tempting option for the group but is unlikely achievable soon due to practical restrictions. We believe Samsung should not rush to create a holding company structure but place a priority on IPOs for unlisted affiliates to address legal issues and raise funds to finance future growth.

### IPOs of unlisted affiliates to come first

We believe the probable course of events is the listing of unlisted affiliates such as Samsung Everland, Samsung SDS and iMarketKorea as it would help Samsung iron out legal issues and raise funds to finance future growth engines. Samsung Card must scale back its 26% equity interest in Samsung Everland to less than 5% no later than April 2012 to meet the equity ceiling requirement. We believe the IPO is a wise choice given the contentious nature of unlisted company valuations and the sheer size of the stake sale. There is a possibility that Samsung Everland will buy back shares back from Samsung Card and cancel them in order to put an end to the circular ownership. This would allow for a revaluation of Samsung Everland's equity stake in Samsung Card.

iMarketKorea has already said it would go public and Samsung SDS is very likely to consider a flotation to enhance future growth and secure the fair value of the major shareholders' stake.

### Potential beneficiaries – Samsung Card, Samsung C&T, Cheil Industries and SEMCO in descending order

The IPOs of unlisted group affiliates - Samsung Everland, Samsung SDS and iMarketKorea - should benefit their shareholders the most. The potential beneficiaries are Samsung Card, Samsung C&T, Cheil Industries and SEMCO. The reasons are: 1) Potential IPOs will allow for the revaluation of stakes in potential IPO candidates since we believe the stake values of IPO candidates are not fully reflected in the shareholder companies' share prices. 2) Samsung Group has sufficient ownership in IPO candidates. Therefore shareholder companies of the IPO candidates could cash out of their investments through the stake disposals after the IPOs. If Samsung Everland and Samsung SDS go public, their respective equity values should amount to W5.8trn-6.7trn and W4.1trn. In this case, the stake values in the IPO candidates – Samsung Everland, Samsung Everland and iMarketKorea – amount to 24-27% and 10% of Samsung Card and Samsung C&T's respective market cap. For Cheil Industries and SEMCO, their equity interests in the three IPO candidates represent 6% of their respective market caps.

## I. What lies ahead?

The IPO of Samsung Life now draws attention to the steps ahead by Samsung Group (the group). We predict the group will shift toward a holding company structure to tighten its managerial control. But we do not believe the group's transition to a holding company structure is possible in the short-term since there are issues to resolve. A more feasible scenario is that Samsung first address the legal hurdles through the IPO of Samsung Everland and finance future growth engines with the proceeds from IPOs of unlisted healthy affiliates such as iMarketKorea and Samsung SDS.

In this case, the primary beneficiaries would be shareholders of IPO candidates. When assuming Samsung Everland is worth W5.8trn-6.7trn post-IPO, Samsung Card would see its interest in the firm account for 24~27% of its market cap and emerge as the largest beneficiary of the IPO.

Other beneficiaries include Samsung C&T, Cheil Ind. and SEMCO whose investments in these IPO candidates represent 6-10% of their respective market caps. Given that Samsung C&T, Cheil Ind. and SEMCO are non-controlling shareholders, they can cash out their investments after the IPOs.

### Potential IPOs

	Est. market cap.	Major shareholders
Samsung Everland	W5.8trn-W6.7trn	Samsung Card 26%, Cheil Industries 4%, SEMCO 4%, Samsung SDI 4%, Samsung C&T 2%
Samsung SDS	W4.1trn	Samsung Electronics 48%, Samsung C&T 18%
iMarketKorea	W0.4trn	Samsung Electronics 11%, Samsung C&T 11%, SEMCO 10%

Source: Financial Supervisory Service, Korea Investment & Securities

### Stake values of the IPO candidates vs. market cap

(W bn, %)

	1) Stake value (A) (W bn)	2) Market cap (B) (W bn)	A / B (%)
Samsung Card	1,552	6,357	24%
Samsung C&T	877	8,405	10%
Cheil Industries	253	4,370	6%
SEMCO	626	11,353	6%
Samsung SDI	264	7,677	3%
Samsung Electronics	925	115,483	1%

Note 1) Value of stakes in Everland (25% discounted case – see 'Samsung Everland valuation'), Samsung SDS and iMarketKorea.  
Note 2) Market cap based on May 17th close price.

Source: Financial Supervisory Service, Korea Investment & Securities

## II. IPO a solution to meet legal challenges and finance growth engines

We believe the chances are good the group will pursue an IPO for Samsung Everland to meet legal requirements and list healthy subsidiaries like Samsung SDS and iMarketKorea to finance growth engines. Samsung Card must sell much of its stake in Samsung Everland no later than April 2012 as its ownership violates the Act for the Structural Improvement of the Financial Industry (Financial Industry Act). Given the magnitude of the stake sale and the contentious nature of unlisted company valuations, we believe a public offering is an effective way for Samsung Card to divest its stake in Samsung Everland.

Some speculate that Samsung Card may seek other ownership dilution methods such as a merger between Samsung Everland and another affiliate or stake transfer to group affiliates. But we believe a merger, if one occurs, would take place after an IPO to fend off controversy about fair valuation issues. A stake transfer between group affiliates runs counter to Samsung Group's commitment to unwind the circular-shareholding structure.

iMarketKorea has already said it would go public. Samsung SDI is very likely to consider a flotation to enhance future growth and secure the fair value of the major shareholders' stake.

## 1. IPOs in the pipeline: Samsung Everland

Recently, the market is buzzing about the possibility of Samsung Everland going public. Investors are counting on an IPO due to legal considerations and Samsung's vocal commitment to end intra-group circular-shareholding. Samsung Card has a legal requirement to unload part of its interest in Samsung Everland by April 2012. In addition, the group announced dramatic reform measures in April 2008, stating that it would tackle the close-knit investment structure in the group within the next four to five years.

Given the inevitable need for stake disposal and foreseeable dispute on the fair valuation of unlisted shares, we believe the group is likely to take Samsung Everland public. We peg Samsung Everland's value at W7.2trn and after the listing the market value should range between W5.8trn-6.7trn by applying a discount (10~30%) to the investment securities' value.

### 1) Samsung Card's interest must be scaled back no later than April 2012

#### A. Legal requirements

According to Article 24 of the Financial Industry Act, any financial institution must get an prior approval from the Financial Services Commission if it wishes to own 5% or more of another company. The law virtually imposes an equity ceiling of 5% on financial institutions.

But the Financial Industry Act revision in January 2000 states that any stake in excess of the 5% ruling and purchased after the enactment of Article 24 in March 1997 must be disposed of by April 2012.

Hence, Samsung Card must shed its 25.6% ownership of Samsung Everland to less than 5% by April 2012.

#### **Act on the Structural Improvement of the Financial Industry**

Article 24 (ownership limit on other companies)

(1)

A financial institution or a financial affiliate that belongs to the same conglomerate as the aforementioned financial institution, shall obtain ex-ante approval from the Financial Supervisory Commission in the following cases in accordance with the Presidential Decree

1

Holding 20% or more of the outstanding common shares in other companies, or

2

Holding 5% or more of outstanding common shares in other companies that are in fact controlled by the said financial affiliate or the said conglomerate as prescribed by the Presidential Decree

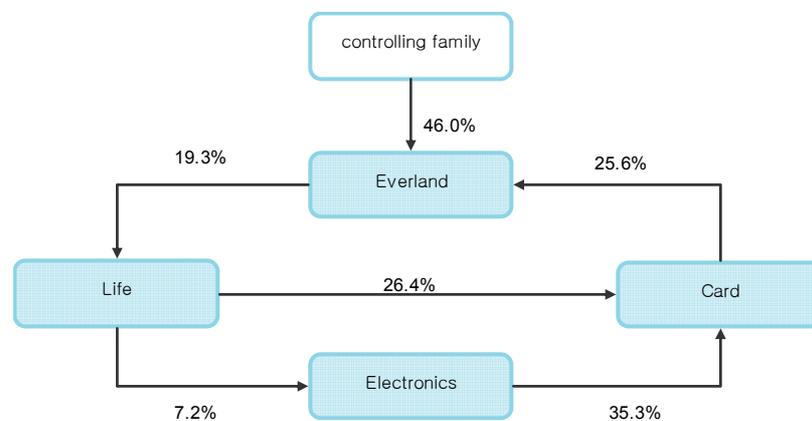
Source: National Assembly

## **B. Samsung's reform plan**

Samsung Group announced in its reform package in April 2008 that Samsung Card would dispose of Samsung Everland shares over the next four to five years to unravel intra-group circular-shareholding structure. The move is a step toward untangling the intricate web of circular-investment among Samsung Everland, Samsung Life Insurance, Samsung Electronics and Samsung Card.

The break-up of circular-investment is related to the creation of a holding company because a transition brings an end to the circular-shareholding or multiple ownership of a single company. That is, it is inevitable for the group to tidy up the circular-investment centered around Samsung Everland if the creation of a financial holding company is the mid to long-term goal.

### **Samsung Group's ownership structure**



Source: Financial Supervisory Service, Korea Investment & Securities

## **2) IPO an effective solution to draw down stake in Samsung Everland**

### **A) Why IPO?**

Given that Samsung Card must sell a chunk of its stake in Samsung Everland by April 2012, the IPO is one of the more effective channels for the disposal due to the magnitude of the stake sale and the contentious nature over the fair valuation of an unlisted company.

First, Samsung Everland's market value is estimated at W5.8trn-6.7trn. That is, the value of Samsung Card's 25.6% interest should be W1.5trn-1.7trn on a pro-rata basis. It is hard to think of ways other than an IPO for the sale of an unlisted company's shares worth more than W1trn.

Second, the sale of an unlisted company often invites controversy over fair value. A low pricing may speed up the stake disposal but stir up disputes over the fair value. In particular, Samsung Everland's landholdings are booked at W645.2bn and this figure is much less than the market value. Some investors peg the actual value of its entire real estate at W2trn or more. Considering the difficulties in assessing the fair value of Samsung Everland, the IPO should be controversy-free and an effective solution for the stake disposal.

Third, there is the possibility that Samsung Everland will buy back its shares from Samsung Card and cancel them in order to put an end to the circular ownership. However, we believe the chances are slim due to 1) the fair valuation issue and 2) the immense scale of the stock buyback.

### **B) Enterprise value of Samsung Everland**

Samsung Everland's enterprise value breaks down to investment securities, real estate and operating value. We applied the offer price of W110,000 per share to Samsung Life, W300,000 per 3.3m<sup>2</sup> for landholdings and an EBITDA of 6.6x to operating value. When assuming a discount rate of 10-30% for investment securities, the company's post-IPO market cap should reach W5.8trn-6.7trn.

Investment securities (W bn)	Used Samsung Life's IPO price of W110,000 per share	4,382
Value of operations (W bn)	Applied EV/EBITDA 6.6x	1,484
Value of tangible assets (W bn)	Assumed per 3.3m <sup>2</sup> price of W300,000	1,302
Net debt (W bn)	As at end-2009	21
NAV (W bn)		7,146
Shares		2,500,000
<b>Market value estimation</b>		
<b>1. NAV (W bn)</b>	<b>Applied 10% of discount to investment securities</b>	<b>6,707</b>
Per-share NAV (KRW)		2,682,994
<b>2. NAV (W bn)</b>	<b>Applied 25% of discount to investment securities</b>	<b>6,050</b>
Per-share NAV (KRW)		2,420,095
<b>3. NAV (W bn)</b>	<b>Applied 30% of discount to investment securities</b>	<b>5,831</b>
Per-share NAV (KRW)		2,332,461

Source: Financial Supervisory Service, Korea Investment & Securities

Per-share price of Samsung Life Land price per 3.3m <sup>2</sup>	10	11	13
	14.9 <sup>1)</sup>	204	216
30	231	242	265
45	257	268	291

Note 1) As at end-2009 (book value of land per 3.3m<sup>2</sup>)

Source: Korea Investment & Securities

### **1. Value of investment securities**

Looking at the company's equity investment portfolio, we underline its 19.3% stake in Samsung Life or 38,688,000 shares on a post-split basis. When excluding Samsung Life, the book value of its equity interest drops to W140.1bn. If assuming Samsung Life's offer price at W110,000 per share, Samsung Everland's stake value in the insurer swells to W4.3trn.

Companies	Stake	Acquisition cost <sup>1)</sup>	Book value <sup>1)</sup>	Market value <sup>2)</sup>
Samsung Life	19.3%	35	1,683	4,256
Samsung Techwin	0.3%	2	15	18
Samsung Heavy	0.1%	2	7	7
Samsung Engineering	1.1%	4	46	44
Credu	8.9%	2	29	15

Note 1) As of end-2009

2) Market cap based on May 17th close price. (Used IPO price of W110,000 for Samsung Life stake value calculation)

Source: Financial Supervisory Service, Korea Investment & Securities

## 2. Value of real estate

Samsung Everland has land measuring 14,341,893m<sup>2</sup>, which is booked at W645.2bn or W149,000 per 3.3m<sup>2</sup>. The landholdings include golf resorts such as Anyang Benest Golf Course. Although most of the land is forested area, neighboring areas sell for more than W500,000 per 3.3m<sup>2</sup>. As such, we do not believe the company's landholdings are accurately reflected on the book. According to our conservative estimate, the company's land is valued at W300,000 per 3.3m<sup>2</sup>, which brings the total real estate value to W1.3trn.

Land		(mn m <sup>2</sup> , mn 3.3 m <sup>2</sup> , W bn)		
	Area	Book value (W bn)	Official land price (W bn)	
Land	14.3 (mn m <sup>2</sup> )	4.3 (mn 3.3m <sup>2</sup> )	645.2	689.9

Note: As of end-2009.  
Source: Financial Supervisory Service

## 3. Operating value

Samsung Everland operates leisure, food catering and E&A businesses. Its operating profit reached W168.6bn and EBITDA amounted to W222.3bn in 2009. The company's businesses do not demonstrate strong potential but they do generate steady cash flow. We believe the company deserves an EBITDA of 6.6x, the market average, and this puts its operating value at W1.5trn.

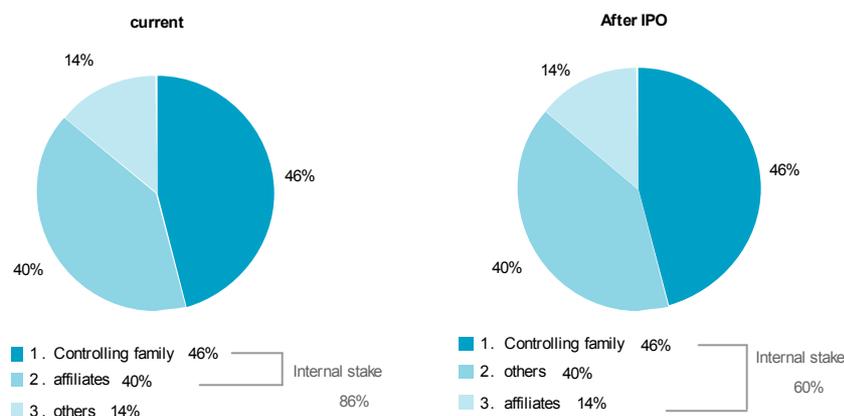
Everland's 2009 earnings by division					(W bn)
	E&A	Leisure	FC	Total	
Sales	628	353	745	1,726	
Gross profit	106	26	75	208	
Depreciation	5	43	6	54	

Source: Financial Supervisory Service

## 3) IPO not a threat to managerial control

We believe Samsung Everland is the crown jewel of Samsung's corporate governance structure. Even if Samsung Card sells its interest in Samsung Everland through an IPO, major shareholders and group affiliates would maintain their tight grip on the group with a total 60% stake.

### Changes to Everland's shareholder structure



Source: Financial Supervisory Service, Korea Investment & Securities

## 2. IPOs in the pipeline: Samsung SDS

### 1) Korea's no. 1 SI company

Samsung SDS (formerly Samsung Data Systems) was founded in 1985 as the exclusive IT and SI services provider for Samsung Group. The company provides various ICT services such as network system deployment and integration, business consulting and solutions consulting, development and sales. It dominates the domestic SI market with a 31% share, followed by LG CNS (23%) and SK C&C (16%)<sup>1</sup>. Major shareholders are Samsung Electronics (21.7%) and Samsung C&T (18.3%).

### 2) Time is ticking for IPO

We believe the IPO of Samsung SDS is very likely. First, its dependence on group business should no longer hold back the company from listing as industry rival SK C&C has already gone public. SI companies tend to generate most of their sales from group business. Accordingly, when SK C&C went public, there were loud opponents calling for tighter IPO restrictions. Second, Samsung SDS is in desperate need of a new growth engine as its sales and net profit increased a mere 5.9% and 6.3%, respectively, over the past three years. The IPO should help the company not only finance new investments but also polish its brand image. Third, Samsung SDS is among the major companies mostly held by majority shareholders. If the IPO enables the company to trade at a fair value, it would add liquidity to majority shareholdings.

### 3) Enterprise value to reach W4.1trn

Samsung SDS posted sales of W2.5trn and net profit of W265.4bn in 2009 and boasts a healthy profit structure and sound financials with a ROE of 20.6% and net cash of W566.2bn. Following the merger announcement in late 2009, Samsung SDS took over Samsung Networks as of 2010. Based on pre-merger due diligence that estimates the enterprise values of Samsung SDS at W3.2trn and Samsung Networks at W0.9trn, the merged entity is worth W4.1trn and equals a 2011F PER of 11x. Despite concerns regarding three years of stagnant growth, the current valuation appears justified given: 1) growth potential backed by recovering corporate investment and overseas market expansion, and 2) a net cash position worth W700bn.

#### Samsung SDS financial summary

(W bn, %)

Income statement	2007	2008	2009
Sales	2,164	2,519	2,494
Operating profit	256	260	268
Net profit	226	233	265
OP margin	11.8%	10.3%	10.7%
NP margin	10.5%	9.2%	10.6%
Balance sheet	2007	2008	2009
Assets	1,600	1,797	1,988
Liabilities	647	634	579
Shareholders' equity	953	1,163	1,409
Net debt	(554)	(394)	(566)
ROE	27.2%	22.0%	20.6%

Source: Financial Supervisory Service, Korea Investment &amp; Securities

<sup>1</sup> Based on SK C&C report and individual company data for 2009 sales.

**Samsung Networks financial summary**

(W bn, %)

Income statement	2007	2008	2009
Sales	651	745	795
Operating profit	56	61	85
Net profit	50	57	72
OP margin	8.7%	8.2%	10.6%
NP margin	7.6%	7.6%	9.1%

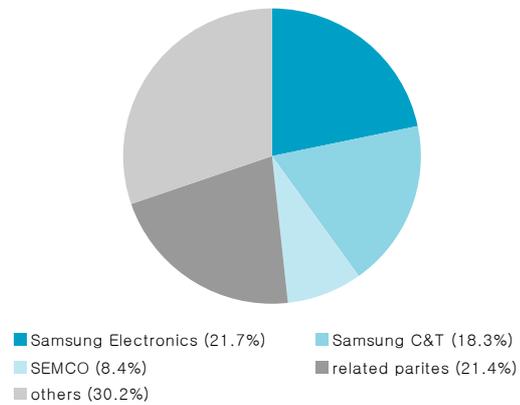
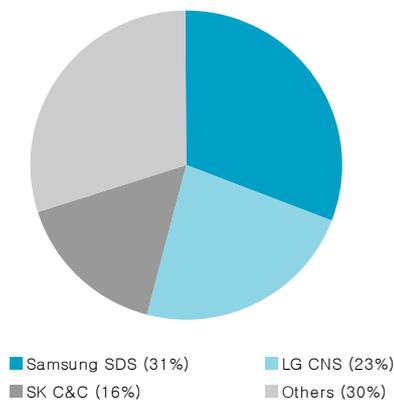
  

Balance sheet	2007	2008	2009
Assets	404	458	517
Liabilities	134	159	151
Shareholders' equity	270	299	366
Net debt	(112)	(139)	(155)
ROE	21.1%	20.0%	21.7%

Source: Financial Supervisory Service, Korea Investment & Securities

**Samsung SDS - market share**

**Samsung SDS - shareholder structure**



Source: Korea Investment & Securities

Source: Financial Supervisory Service, Korea Investment & Securities

### 3. IPOs in the pipeline: iMarketKorea

#### 1) Korea's no. 2 MRO company scheduled to list in 2H10

iMarketKorea was established in 2000 and provides MRO (maintenance, repair and operation) services in the B2B e-commerce market. The company ranks second in the domestic MRO market after Serveone, a 100%-owned affiliate of LG Group. iMarketKorea is an exclusive outsourcing provider for Samsung Group and has served 4,000 business partners both in the private and public sectors.

The company posted sales of W1.18trn and an operating profit of W28bn in 2009. Since its establishment in 2000, it has delivered a 10-year sales CAGR of over 20% and widened its service areas and customer base to manufacturing, financials, distribution, services and public institutions. Major shareholders are Samsung C&T and Samsung Electronics each with a 10.6% (reflecting the new shares issued in the IPO) stake. The company filed a registration statement for its IPO in April and is scheduled to make a public offer in July and list the shares on the KOSPI in August.

#### 2) Enterprise value to reach W400bn

The company reportedly plans to offer 9mn new shares (after 10:1 stock split) to raise between W117bn-144bn. We estimate the post-IPO market cap would amount to W460bn-550bn. It is difficult to determine the IPO's impact on share dilution due to lack of information. Given the valuation limitations, we conservatively assume the equity value at W400bn.

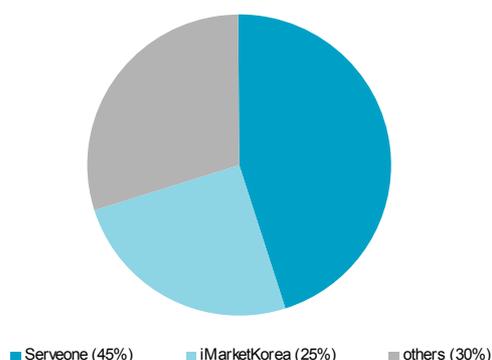
#### iMarketKorea financial summary

(W bn, %)

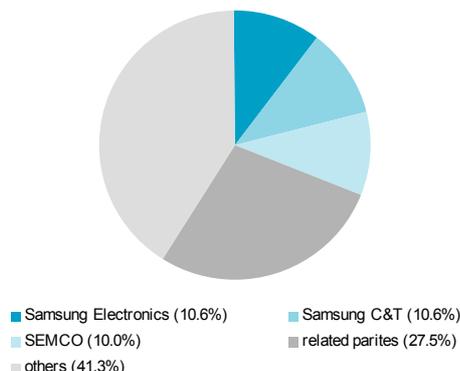
Income statement	2007	2008	2009
Sales	979	1,065	1,182
Operating profit	20	22	28
Net profit	14	13	21
OP margin	2.1%	2.0%	2.4%
NP margin	1.4%	1.2%	1.8%
Balance sheet	2007	2008	2009
Assets	369	271	347
Liabilities	303	193	250
Shareholders' equity	66	78	98
Net debt	(1)	(9)	(7)
ROE	23.4%	18.4%	24.0%

Source: Financial Supervisory Service, Korea Investment & Securities

#### iMarketKorea - market share



#### iMarketKorea - shareholder structure after IPO



Source: Korea Investment & Securities

Note: shareholding structure after the IPO  
Source: Financial Supervisory Service, Korea Investment & Securities

### III. Investment targets if IPOs go as planned

The IPOs of Samsung Everland and Samsung SDS merit attention because their worth would represent a significant portion of their shareholders' market caps. We expect Samsung Card will benefit the most as the card issuer's equity value in these IPO candidates equals 24~27% of its market cap. The equity holdings of Samsung C&T, SEMCO, Cheil Industries and Samsung SDI should also draw the market's attention.

Samsung Everland's ownership breaks down to Samsung Card (25.6%), Cheil Industries, SEMCO and Samsung SDI (4.0% each) and unaffiliated CJ (2.4%). Samsung SDS is owned by Samsung Electronics (21.7%), Samsung C&T (18.3%) and SEMCO (8.4%). If Samsung Everland and Samsung SDS go public, shareholding companies would enjoy an increase in investment asset value and thus greater enterprise value as well. Some companies may cash out their equity holdings.

#### Shareholders of the three IPO candidates

(W bn, %)

	Total (a+b+c) (W bn)	Everland (a)		Samsung SDS (b)		iMarketKorea (c)	
		Value (W bn)	Stake (%)	Value (W bn)	Stake (%)	Value (W bn)	Stake (%)
1. Affiliates	4,798	2,420	40.0%	2,143	52.6%	235	58.7%
Samsung Electronics	925			883	21.7%	42	10.6%
Samsung Card	1,552	1,552	25.6%				
Cheil Industries	253	242	4.0%			11	2.8%
Samsung C&T	877	90	1.5%	745	18.3%	42	10.6%
SEMCO	626	242	4.0%	344	8.4%	40	10.0%
Samsung SDI	264	242	4.0%			22	5.6%
Samsung Everland	11					11	2.8%
Others	289	53	0.9%	170	4.2%	66	16.4%
2. major shareholders	3,485	2,785	46.0%	700	17.2%		

Source: Financial Supervisory Service, Korea Investment &amp; Securities

If Samsung Everland goes public to comply with the law on the separation of finance and industry and untangle the complex circular-ownership structure, Samsung Card will stand to benefit the most. Given its equity interest in Samsung Everland valued at W1.5trn-1.7trn, Samsung Card would see after-tax cash inflow of more than W1trn. This figure equals 24-27% of its market cap and provides solid ground for a share re-rating after Samsung Everland's IPO.

Samsung C&T's equity holdings in unlisted affiliates (Samsung Everland, Samsung SDS and iMarketKorea) have an estimated worth of W0.9trn, equal to 10% of its market cap. As such, the IPOs would shed a new light on investment assets held by Samsung C&T. Moreover, Samsung C&T should emerge as a definite victor from the group governance overhaul because the company is likely to become the largest shareholder of Samsung Electronics.

Finally, SEMCO, Cheil Industries and Samsung SDI, which are minority shareholders of Samsung Everland, may opt to sell their stakes and generate cash inflow given that large shareholders do not need their backing.

**Stake values of the IPO candidates vs. market cap**

(W bn, %)

	1) Stake value (A) (W bn)	2) Market cap (B). (W bn)	A / B (%)
Samsung Card	1,552	6,357	24%
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Source: Financial Supervisory Service, Korea Investment & Securities

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