

Daelim Industrial (000210)

12M rating **BUY (Maintain)**

12M TP **W106,000** from W106,000

Up/downside **+25%**

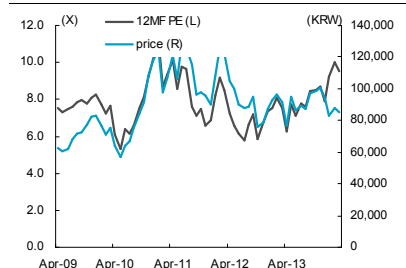
Stock Data

KOSPI (Mar 26, pt)	1,964
Stock price (Mar 26, KRW)	84,900
Market cap (USD mn)	2,748
Shares outstanding (mn)	35
52-Week high/low (KRW)	108,500/73,500
6M avg. daily turnover (USD mn)	24.5
Free float / Foreign ownership (%)	76.0/30.4
Major shareholders (%)	
DaeLim Corporation and 10 others	24.0
National Pension Service (NPS)	10.1

Performance

	1M	6M	12M
Absolute (%)	(4.6)	(15.1)	(7.3)
Relative to KOSPI (%p)	(4.3)	(13.0)	(6.3)

12MF PE trend



Source: WISEfn consensus

1Q14 preview: Shares to break above 0.6x PB

1Q14 preview: Earnings turning point

Despite relatively small losses, Daelim Industrial shares fell on concerns over cost overruns after 4Q13 earnings. However, we believe additional losses are unlikely. Earnings should improve going forward as unexpected losses are not likely, considering that 1) unclaimed construction receivable is stable and 2) construction at the Shoaiba power plant and Sadara hydrocarbon plan should be completed in 1H14 (technical completion in September to October). As such, we estimate 1Q14 sales at W2.2tn (down 10.7% YoY), OP at W55bn (down 56% YoY) and EBT at W67bn (down 58% YoY). Of note, we assumed W5.5bn in SG&A expenses from the Daegu subway bid rigging fine as a one-off expense. Given the sharp sales erosion in 1Q14, we do not believe a W10-20bn difference in OP will be meaningful. Going forward, additional overseas costs should be a critical factor to 2014 earnings direction.

Top-line growth concerns to fade in 2Q14

Growth concerns currently outweigh worries over margins. If new overseas orders fall short of W5tn this year, sales growth YoY is unlikely in 2015. Management is targeting W6.7tn in overseas orders, but has only secured USD300mn YTD. This is also lagging peers, which have already won more than half of their targets, including secured projects. However, we note Daelim Industrial typically ramps up order taking in 2H. And, the company is bidding on: 1) the Malaysian RAPID refinery (three packages, each worth USD1-1.4bn), 2) the Kuwaiti Lower Fars Heavy Oil project (heavy oil development, about USD2bn), and 3) the Saudi Arabian IGCC power plant project (three packages, each worth USD1-2bn). Results should be announced from 2Q14. Of note, Daelim Industrial recognized substantial losses in Malaysia in the mid-1990s, but has since won profitable orders in the country. Furthermore, Daelim Industrial is the only company bidding on all three packages for the IGCC project. Overall, we believe the company has a competitive advantage as it is the only Korean company with CCS technology certification, which is key to the IGCC project.

PB falls to 0.6x, but further downside limited, maintain as top pick

Earnings should bottom out in 1Q14 as the company should recognize sales of high-margin projects, including the Oman Sohar refinery, Saudi Arabian Maaden plant and Malaysian Manjung IPP, which were awarded in 2013, from 2H14. As earnings visibility firms, we believe there are more positive earnings catalysts, including solid new orders and improving subsidiary earnings. In addition, earnings upside should pick up once sanctions ease against Iran, which is a traditionally

Kyung ja Lee

822-3276-6155

kyungja.lee@truefriend.com

Hyungjun Ahn

822-3276-4460

hyungjoon@truefriend.com

Yr to	Sales	OP	EBT	NP	EPS	% chg	EBITDA	PE	EV/EBITDA	PB	ROE
Dec	(W bn)	(W bn)	(W bn)	(W bn)	(won)	(YoY)	(W bn)	(x)	(x)	(x)	(%)
2012A	10,253	486	560	391	10,128	7.0	548	8.6	5.2	0.7	8.5
2013A	9,847	40	(14)	(25)	(648)	0.0	112	NM	30.1	0.8	(0.5)
2014F	9,908	366	380	301	7,818	0.0	448	10.9	6.8	0.6	6.2
2015F	10,145	467	537	399	10,354	32.4	559	8.2	5.6	0.6	7.7
2016F	10,835	490	561	417	10,820	4.5	592	7.8	5.2	0.6	7.5

Note: Net profit and EPS are based on figures attributed to controlling interest

strong market for Daelim Industrial. Meanwhile, shares currently trade at only 0.6x PB, the lowest among major builders and a historical bottom. As such, we believe further downside is limited, and we maintain Daelim Industrial as our top pick.

Table 1. Quarterly earnings

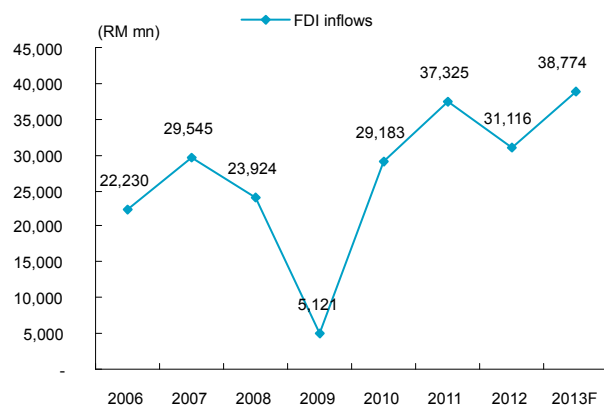
(W bn)

	1Q13	2Q13	3Q13	4Q13	1Q14F	2Q14F	3Q14F	4Q14F	2013	2014F
Sales	2,516	2,474	2,418	2,439	2,246	2,272	2,384	3,006	9,847	9,908
YoY	22.7	0.2	(11.3)	(18.9)	(10.7)	(8.2)	(1.4)	23.2	(4.0)	0.6
Parent	2,144	2,027	2,042	2,232	1,909	1,805	2,057	2,543	8,446	8,313
DSA	231	277	248	60	189	284	189	284	815	945
Others	141	170	128	147	148	183	139	179	586	649
COGS ratio	89.6%	91.1%	90.1%	108.6%	91.8%	91.7%	89.9%	91.4%	94.8%	91.2%
Parent	89.6%	90.5%	88.7%	96.9%	91.9%	91.4%	89.9%	91.0%	91.5%	91.0%
DSA	97.8%	104.7%	108.9%	603.9%	102.0%	102.0%	99.0%	99.0%	141.0%	100.5%
OP	124	112	124	(320)	55	84	121	107	40	366
OPM	4.9%	4.5%	5.1%	-13.1%	2.4%	3.7%	5.1%	3.6%	0.4%	3.7%
(Parent)	4.9%	5.0%	6.4%	-2.7%	2.1%	3.3%	4.6%	3.3%	3.3%	3.3%
(DSA)	1.2%	-5.3%	-9.5%	-506.3%	-2.0%	-2.0%	1.0%	1.0%	-41.9%	-1.2%
Equity-gain method	10	(5)	20	29	22	25	30	24	55	100
Korea development	(5)	2	1	2	1	2	2	4	(1)	9
Samho	0	0	0	3	2	3	2	4	4	11
YNCC	16	(6)	19	25	16	15	22	14	54	67
KRCC	0	2	1	1	0	2	1	0	3	3
Polymirae	3	3	3	1	3	3	3	2	11	11
Pochun IPP	(4)	(6)	(4)	(1)	0	0	0	0	(16)	0
EBT	158	103	116	(391)	67	104	131	79	(14)	380
NP	121	78	90	(299)	51	78	100	75	(10)	304

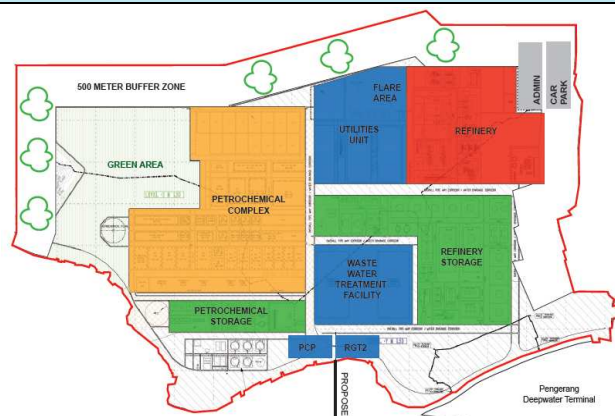
Source: Daelim Ind. Korea investment & Securities

Bid 1) Malaysian RAPID refinery complex

The project consists of refinery and chemical facilities and was tendered by Petronas in Pengerang in southern Malaysia. The overall project consists of 24 packages, and nine refinery packages are currently up for bid. Daelim is waiting for results on three packages, which should be announced in April-May. Margin concerns are limited, unlike the price competition-driven Middle East market, as technical capacity and prices are both under consideration. While there are concerns over the ASEAN economy, Malaysia is the soundest member. Foreign investment peaked in 2013 (RM216.5bn), and new jobs increased 190,000. And, the prime minister has mentioned that many projects, including the RAPID complex, should progress smoothly in early-2014.

Figure 1. Malaysia FDI inflow

Source: Bank of Malaysia

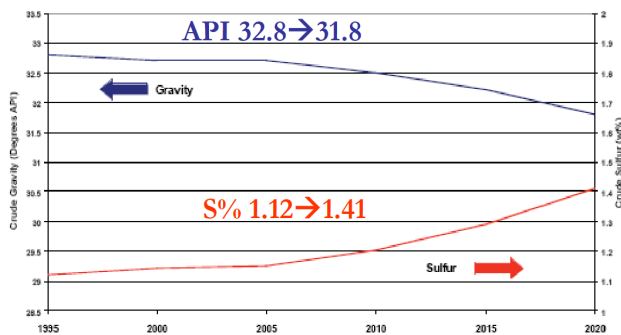
Figure 2. Rapid complex plan

Source: Petronas

Bid2) Kuwaiti Lower Fars Heavy Oil Project (LFHO)

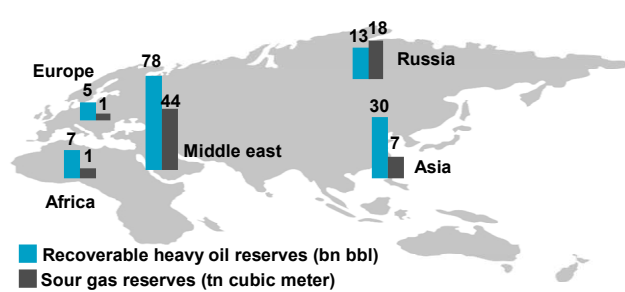
The project is a heavy oil development project in the desert with 7-15bn barrels of reserves in northern Kuwait. Production of heavy oil with high viscosity and sulfur content is increasing as oil and gas reserves mature across the world. Heavy oil reserves are especially concentrated in the Middle East compared to North Africa. Heavy oil facilities require high technology, and these types of projects should continue to be tendered in the region. While the average API of Kuwaiti oil reserves is 30, LFHO oil gravity rating reaches 11-17 API. Oil produced from this field should be transported to a new refinery project that should be tendered in early-2015 to be used as feedstock. The value of the project is USD4.2bn, and Daelim is bidding by establishing consortium with SK E&C. Competing consortiums are Saipem+HHI, Hyundai E&C+GS E&C+Dossal, Samsung Engineering+Petrofac.

Figure 3. Global crude oil: More heavy & sour oil



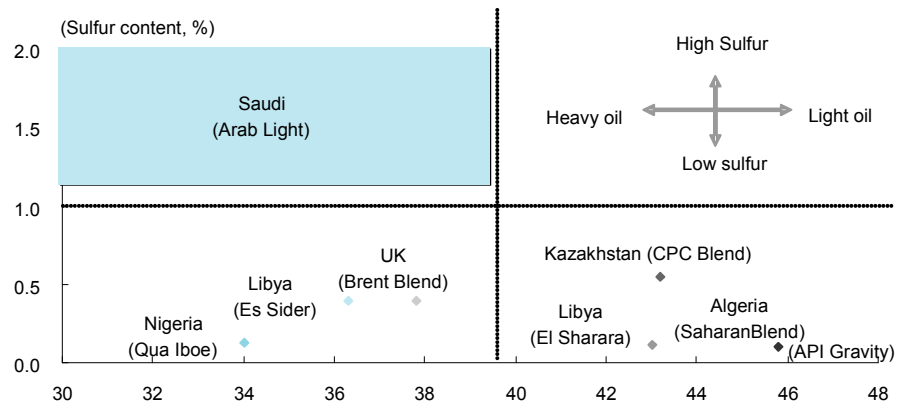
Source: 10th Biennial Sulfur Market Symposium, Beijing, China

Figure 4. Extractable heavy oil and sour gas reserves

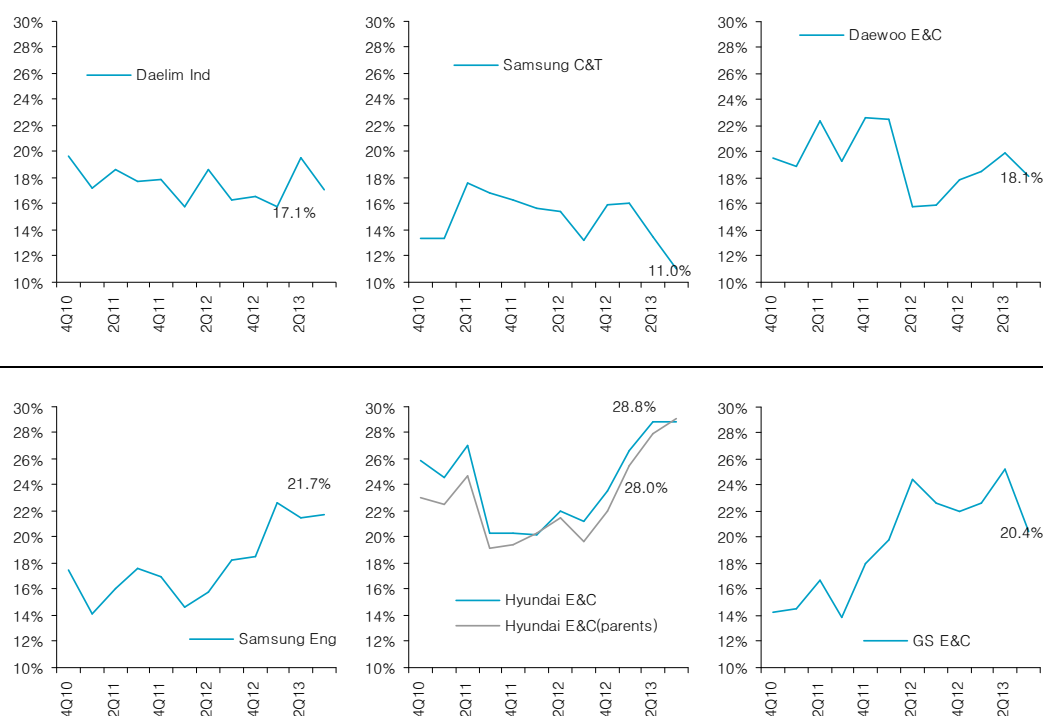


Source: BP

Figure 5. ME crude with high sulfur content



Source: EIA, Korea Investment & Securities

Figure 6. Unclaimed construction receivable to sales ratio trend (As of 4Q13)

Note: Unclaimed construction receivable is accounts receivable that has yet been claimed due to a disagreement with the client
Source: Company data

Table 2. Valuation

(Wbn)

	Value	Note
1) OP value	2,841	
Construction OP value	2,320	
Construction NOPLAT	232	Based on 12MF OP
Construction multiple	10.0	Market PE
Petrochem OP value	521	
Petrochem NOPLAT	65	Based on 12MF OP
Petrochem multiple	8.0	8x
2) YNCC	428	Based on 12MF equity method, 8x
3) Daelim Energy	242	Pochun power, DCF
4) Net debt	-195	2014F
Shareholder's value (1+2+3-4)	3,706	
# of shares ('000)	34,800	
TP (KRW)	106,000	

Source: Korea investment & Securities

Table 3. Overseas projects and cost overrun

(W bn)

Parent- Project	Contract	Completion	Value	Residual value	Progress	Cost overrun					
						2012	1Q13	2Q13	3Q13	4Q13	Total
Libya BIA Passenger Terminal	Apr-13	Feb-14	22	19	13.6%						
Vietnam OMon TPP Unit No.2	Aug-12	Nov-15	276	237	14.1%						
Vietnam Thai Binh2 PP	May-12	Aug-15	756	642	15.1%						
Brunai Sungai bridge	Jun-13	Jun-16	102	98	4.2%						
Saudi Elastomers	Jul-12	Apr-16	505	382	24.5%						
Saudi Rabigh II CP1/CP2	Jul-12	Oct-16	313	285	9.2%						
Saudi SABUCO Butanol&Syngas	Dec-12	Sep-15	223	178	20.2%						
Saudi SADARA MFC	Jul-11	Oct-14	751	166	77.8%						
Saudi SAMAPCO CA/EDC	Mar-10	Oct-13	361	16	95.6%						
Saudi Shoaiba II power	Oct-11	Sep-14	910	154	83.0%						
Saudi YERP-3	Jul-10	May-14	958	82	91.5%						
Saudi YERP-4	Jul-10	Jun-14	582	64	89.0%						
Saudi JER	Jul-09	Dec-13	559	11	98.1%						
Saudi SADARA Isocyanates	Sep-11	Mar-15	773	352	54.4%						
Singapore MCE	Oct-08	Jun-14	477	11	97.7%						
Iran SPGD PH-12 Teherran	Sep-09	Apr-14	607	103	83.0%						
Iran LNG U&J	Jun-09	Feb-14	120	117	2.6%						
Kuwait KNPC FCC Revamp	Jun-13	Aug-16	201	201	0.0%						
Kuwait KNPC SHFP	May-13	Aug-16	574	574	0.0%						
Kuwait KOC Telemetry	Jun-12	Mar-15	183	141	23.0%						
Kuwait LPG TRAIN 4	Jul-10	Feb-14	981	28	97.1%					79	79
Phillipine SM200 Phase I	Mar-11	Sep-15	162	130	19.5%						
Phillipine JG Summit NCC	Dec-09	Feb-14	369	13	96.4%						
Phillipine Petron RMP-2	Dec-10	Jun-15	1,617	326	79.8%						
Phillipine SRPI 100 Coal fired Power Station	Dec-12	Jul-16	167	167	0.0%						
Nepal, Upper Trishuli(E)	Apr-12	Oct-18	233	233	0.0%						
OLD HARBOUR 360MW	Jun-12	Jan-15	417	417	0.0%						
Kuwait KNPC FCC Revamp	Jun-13	Aug-16	176	175	0.5%						
Malaysia Fast Track 3A	Aug-13	Oct-17	917	917	0.0%						
Total			14,293	6,239	56.3%						
DSA- Project	Contract	Completion	Value	Residual value	Progress	Cost overrun					
						2012	1Q13	2Q13	3Q13	4Q13	Total
Saudi DSA Elastomer Project	Sep-12	Apr-16	295	239	18.8%						
Saudi DSA JER	Jul-09	Dec-13	358	1	99.7%						
Saudi DSA Kayan HDPE	Aug-08	Dec-13	267	0	99.8%						
Saudi DSA Kayan LDPE	Dec-09	Dec-13	177	1	99.2%						
Saudi DSA Kayan PC	Feb-07	Dec-13	557	3	99.5%						
Saudi DSA NCP POLYMER	Dec-07	Dec-13	545	0	100.0%						
Saudi DSA Rabigh II CP-1/CP-2	Jul-12	Oct-16	163	157	3.2%						
Saudi DSA RTIP MFC	Jul-11	Oct-14	280	160	42.8%					137	137
Saudi DSA SABUCO Butanol&Syngas	Dec-12	Sep-15	96	94	1.3%						
Saudi DSA SAMAPCO CA/EDC	Mar-10	Oct-13	316	44	86.2%						
Saudi DSA SHOAIBA II power	Oct-11	Sep-14	412	58	85.9%	15		13	22	227	277
Saudi DSA SADARA ISOCYANATES	Sep-11	Mar-15	477	347	27.2%					26	26
Saudi DSA YERP-3	Jul-10	May-14	375	115	69.5%					38	38
Saudi DSA YERP-4	Jul-10	Jun-14	159	51	68.2%						
Total			4,478	1,271	71.6%	15	0	13	22	536	587

Note: As of 3Q13

Source: Company data, Korea investment & Securities

Glossary

- API : Measure of how heavy or light a petroleum liquid is compared to water. It is used to compare the relative densities of petroleum liquids. Also, it determines the price of oil.

Balance sheet

FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
Current assets	7,292	6,933	6,889	7,203	7,693
Cash & cash equivalent	1,477	1,563	1,486	1,522	1,625
Accounts & other receivables	3,481	3,263	3,283	3,449	3,684
Inventory	1,155	1,036	1,043	1,217	1,300
Non-current assets	3,714	3,850	3,835	3,868	4,020
Investment assets	1,693	1,682	1,692	1,733	1,850
Tangible assets	1,517	1,402	1,372	1,346	1,327
Intangible assets	79	81	81	83	89
Total assets	11,006	10,783	10,724	11,070	11,713
Current liabilities	4,779	4,460	4,266	4,166	4,385
Accounts & other payables	2,961	2,858	2,477	2,536	2,275
ST debt & bond	336	327	324	323	322
Current portion of LT debt	341	538	606	665	727
Non-current liabilities	1,309	1,452	1,305	1,368	1,390
Debentures	448	563	513	563	553
LT debt & financial liabilities	432	469	369	372	375
Total liabilities	6,088	5,913	5,571	5,534	5,775
Controlling interest	4,779	4,714	4,992	5,367	5,760
Capital stock	219	219	219	219	219
Capital surplus	507	506	506	506	506
Capital adjustments	(0)	0	0	0	0
Retained earnings	4,005	3,961	4,259	4,653	5,066
Minority interest	140	156	162	170	178
Shareholders' equity	4,919	4,870	5,154	5,537	5,938

Cash flow

FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
C/F from operating	817	35	9	(47)	232
Net profit	401	(10)	307	407	425
Depreciation	57	65	75	85	95
Amortization	5	7	7	7	7
Net incr. in W/C	136	(156)	(287)	(454)	(207)
Others	218	129	(93)	(92)	(88)
C/F from investing	(333)	(270)	14	(16)	(170)
CAPEX	(156)	(137)	(60)	(74)	(91)
Decr. in fixed assets	2	15	15	15	15
Incr. in investment	(172)	(214)	70	43	(31)
Net incr. in intangible assets	(9)	(5)	(7)	(9)	(13)
Others	2	71	(4)	9	(50)
C/F from financing	(331)	320	(99)	99	42
Incr. in equity	0	2	0	0	0
Incr. in debts	(290)	339	(89)	111	54
Dividends	(19)	(19)	(4)	(4)	(4)
Others	(22)	(2)	(6)	(8)	(8)
C/F from others	(1)	1	0	0	0
Increase in cash	152	86	(77)	36	104

Note: Based on K-IFRS (consolidated)

Income statement

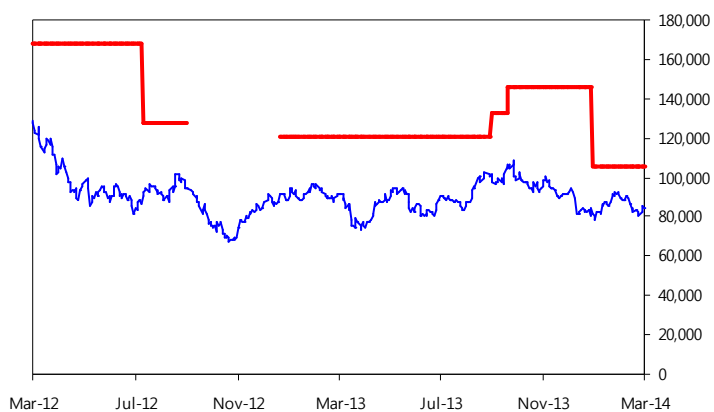
FY-ending Dec. (W bn)	2012A	2013A	2014F	2015F	2016F
Sales	10,253	9,847	9,908	10,145	10,835
COGS	9,219	9,338	9,037	9,113	9,743
Gross profit	1,034	509	871	1,032	1,092
SG&A expense	548	469	505	565	602
Operating profit	486	40	366	467	490
Financial income	96	117	52	51	53
Interest income	64	47	47	46	48
Financial expense	102	126	84	84	88
Interest expense	79	75	84	84	88
Other non-operating profit	36	(102)	(50)	0	0
Gains (Losses) in associates, subsidiaries and JV	45	57	100	103	106
Earnings before tax	560	(14)	384	537	561
Income taxes	159	(3)	77	130	136
Net profit	401	(10)	307	407	425
Net profit of controlling interest	391	(25)	301	399	417
Other comprehensive profit	(20)	(20)	(20)	(20)	(20)
Total comprehensive profit	381	(30)	287	387	405
Total comprehensive profit of controlling interest	372	(44)	282	379	397
EBITDA	548	112	448	559	592

Key financial data

FY-ending Dec.	2012A	2013A	2014F	2015F	2016F
per share data (KRW)					
EPS	10,128	(648)	7,818	10,354	10,820
BPS	123,800	122,126	129,319	139,041	149,228
DPS	500	100	100	100	100
Growth (%)					
Sales growth	28.4	(4.0)	0.6	2.4	6.8
OP growth	11.1	(91.8)	822.8	27.5	4.9
NP growth	7.0	0.0	0.0	32.4	4.5
EPS growth	7.0	0.0	0.0	32.4	4.5
EBITDA growth	11.4	(79.6)	300.5	24.8	6.1
Profitability (%)					
OP margin	4.7	0.4	3.7	4.6	4.5
NP margin	3.8	(0.3)	3.0	3.9	3.8
EBITDA margin	5.3	1.1	4.5	5.5	5.5
ROA	3.7	(0.1)	2.9	3.7	3.7
ROE	8.5	(0.5)	6.2	7.7	7.5
Dividend yield	0.6	0.1	0.1	0.1	0.1
Stability					
Net debt (W bn)	(418)	(180)	(195)	(106)	(189)
Debt/equity ratio (%)	31.8	39.0	35.2	34.7	33.3
Valuation (X)					
PE	8.6	NM	10.9	8.2	7.8
PB	0.7	0.8	0.6	0.6	0.6
PS	0.3	0.4	0.3	0.3	0.3
EV/EBITDA	5.2	30.1	6.8	5.6	5.2

Changes to recommendation and price target

Company (Code)	Date	Recommendation	Price target
Daelim Industrial (000210)	04-09-12	BUY	W168,000
	08-06-12	BUY	W128,000
	09-28-12	Hold	-
	01-16-13	BUY	W121,000
	09-25-13	BUY	W133,000
	10-15-13	BUY	W146,000
	01-24-14	BUY	W106,000



■ **Guide to Korea Investment & Securities Co., Ltd. stock ratings based on absolute 12-month forward share price performance**

- BUY: Expected to give a return of +15% or more
- Hold: Expected to give a return between -15% and 15%
- Underweight: Expected to give a return of -15% or less
- Korea Investment & Securities does not offer target prices for stocks with Hold or Underweight ratings.

■ **Guide to Korea Investment & Securities Co., Ltd. sector ratings for the next 12 months**

- Overweight: Recommend increasing the sector's weighting in the portfolio compared to its respective weighting in the Kospi (Kosdaq) based on market capitalization.
- Neutral: Recommend maintaining the sector's weighting in the portfolio in line with its respective weighting in the Kospi (Kosdaq) based on market capitalization.
- Underweight: Recommend reducing the sector's weighting in the portfolio compared to its respective weighting in the Kospi (Kosdaq) based on market capitalization.

■ **Analyst Certification**

I/We, as the research analyst/analysts who prepared this report, do hereby certify that the views expressed in this research report accurately reflect my/our personal views about the subject securities and issuers discussed in this report. I/We do hereby also certify that no part of my/our compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in this research report.

■ **Important Disclosures**

As of the end of the month immediately preceding the date of publication of the research report or the public appearance (or the end of the second most recent month if the publication date is less than 10 calendar days after the end of the most recent month), Korea Investment & Securities Co., Ltd., or its affiliates does not own 1% or more of any class of common equity securities of Daelim Industrial.

There is no actual, material conflict of interest of the research analyst or Korea Investment & Securities Co., Ltd., or its affiliates known at the time of publication of the research report or at the time of the public appearance.

Korea Investment & Securities Co., Ltd., or its affiliates has not managed or co-managed a public offering of securities for Daelim Industrial in the past 12 months;

Korea Investment & Securities Co., Ltd., or its affiliates has not received compensation for investment banking services from Daelim Industrial in the past 12 months; Korea Investment & Securities Co., Ltd., or its affiliates does not expect to receive or intend to seek compensation for investment banking services from Daelim Industrial in the next 3 months.

Korea Investment & Securities Co., Ltd., or its affiliates was not making a market in Daelim Industrial's securities at the time that the research report was published.

Korea Investment & Securities Co., Ltd. does not own over 1% of Daelim Industrial shares as of March 27, 2014.

Korea Investment & Securities Co., Ltd. has not provided this report to various third parties.

Neither the analyst/analysts who prepared this report nor their associates own any shares of the company/companies covered in this report as of March 27, 2014.

Korea Investment & Securities Co., Ltd. has issued ELW with underlying stocks of Daelim Industrial and is the liquidity provider.

Prepared by: Kyungja Lee

This report was written by Korea Investment & Securities Co., Ltd. to help its clients invest in securities. This material is copyrighted and may not be copied, redistributed, forwarded or altered in any way without the consent of Korea Investment & Securities Co., Ltd. This report has been prepared by Korea Investment & Securities Co., Ltd. and is provided for information purposes only. Under no circumstances is it to be used or considered as an offer to sell, or a solicitation of any offer to buy. We make no representation as to its accuracy or completeness and it should not be relied upon as such. The company accepts no liability whatsoever for any direct or consequential loss arising from any use of this report or its contents. The final investment decision is based on the client's judgment, and this report cannot be used as evidence in any legal dispute related to investment decisions.