

Cosmax., Inc. (044820)

Positive
Neutral
Negative

BUY

TP W51,000
Stock (Apr 30) W55,400

1Q13 preview: Solid sales growth, but OP growth should be limited

- Consolidated sales should easily achieve 15-20% YoY growth, in line with annual guidance level (KIS estimate W84.7bn, 17% YoY)
- Sales growth by business: Korean headquarters 10-15% YoY, Cosmax China 30% YoY, Cosmax Bio 15-20% YoY (sales growth should be limited until relocation to new plant due to limited capacity of existing facility)
- Domestic sales: Despite recent concerns over domestic sales, solid growth expected on sales of new brands and new products (CC cream)
- However, OP growth should miss our previous estimate of W8.1bn (16.8% YoY) on cost burden from new facilities in Guangzhou and Indonesia

Status of overseas business

- **Guangzhou, China:** New facility should win approval for production in May, and begin commercial production afterward
- **Indonesia:** Completed additional interior construction after acquiring a plant from L'Oreal. Approval for production expected in Apr-May. Scheduled to begin commercial production after acquiring good manufacturing practice (GMP) certification. Skin care and hair care products for L'Oreal are scheduled to be produced this year, and additional ODM contracts for make-up products are expected
- **US:** Nothing has yet to materialize, but ready to give positive consideration if there is a favorable entry opportunity. Investment should be around W10~20bn, which is not excessive

Key Q&As

- 1) Reasons for positive responses from foreign investors at recent meetings
 - Investors were interested in the OEM/ODM business as it requires less investment, can make profit from overseas business in a short time and is capable of stable growth. Also, investors positively evaluated Cosmax's clear mid- to long- term growth plan (expansion of Chinese business, entry into ASEAN market, advancement of Cosmax Bio into China after stabilization of new Jaecheon plant)
- 2) Possibility of margin improvement in the China business
 - Management will maintain the current level of 9%. Margin may drop in 2013F on the operation of Guangzhou facility
 - Cosmax China will finance most investments needed, and there is a constant burden from rising labor costs and related insurance fees
- 3) Key to success of Cosmax Bio
 - Cosmax Bio is capable of producing most types of health supplement products in Korea based on R&D, facility investment and technical partnerships with Japanese and US companies. Also, Cosmax Bio changed main buyers from multi-level marketing companies to large companies, such as, AmorePacific, LG H&H, KT&G, Yakult, etc, which are performing well in health supplements business
- 4) Possibility of rights offering
 - No chance of rights offering. Investments for overseas expansion should be financed through borrowings. Thus, there is a risk of high debt ratio, but financial costs are manageable

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Valuation

- Shares trade at 31.5x 2013F PE (35.7x 2012 PE at 2012 peak share price)
- Exceeded our TP (intrinsic PE of 29x) as shares rallied after bottoming in Feb (max 48%); however, share price peaked out, on: 1) valuation burden after the surge, and 2) eroding investor sentiment for cosmetics sector
- Long-term investment merit is still valid based upon solid domestic sales growth and expanding overseas momentum

Changes to recommendation and price target

Company (Code)	Date	Recommendation	Price target
Cosmax., Inc. (044820)	05-30-11	NA	-
	03-16-12	BUY	W24,000
	08-19-12	BUY	W43,000
	11-28-12	BUY	W51,000



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