

SK Chemicals (006120 KS)

Pharmaceutical

Both chemicals and life science maintain steady growth

Maintain Buy call with TP of W97,000 (vs. current price of W76,800)

We reiterate our Buy call on SK Chemicals with a target price of W97,000, as the company's chemicals and life science divisions are both displaying solid revenue growth. Given that generic drug sales account for less than 5% of the life science division's total revenues, SK Chemicals is relatively insensitive to regulatory risks. Meanwhile, the company's slowing progress in getting approval for SID-530 from European countries needs to be closely monitored.

2Q11: Revenues of W386.4bn (up 17% YoY); OP of W19.3bn (down 3% YoY)

SK Chemicals' 2Q11 revenues jumped 17% YoY to W386.4bn (under non-consolidated K-IFRS), beating our estimate. This strong top line was driven by both the chemicals and life science divisions, which posted respective revenue growth of 17% YoY (to W275.8bn) and 20% YoY (to W93.8bn).

The company's 2Q revenues were greater than our estimate due to the stronger-than-expected performance of the bio-diesel business. Bio-diesel revenues surged 40% YoY to W54bn, exceeding our estimate of W42.5bn. PET and PETG revenues also leaped by 15% YoY and 17% YoY, respectively.

However, the company's 2Q operating profit fell shy of our estimate of W22.8bn, coming in at W19.3bn, mainly due to an increase in R&D expenses (up W2.8bn YoY). R&D expenses should continue to expand given the company's overseas clinical trials for SID-530, SID-820, and SID-710.

2011 Outlook: Revenues of W1.52tr (up 14%) and OP of W79bn (up 16%)

Given the strong performances at both the chemicals and life science divisions, we upped our estimate for SK Chemicals' 2011 full-year revenues to W1.52tr. But we are cutting our operating profit estimate to W79bn to reflect cost increases.

Since IFRS-based non-consolidated net profit does not include equity-method gains, SK Chemicals' 2011 net profit is projected at W50.2bn, W44.3bn lower than our previous K-GAAP-based estimate. Meanwhile, if things go smoothly in 2H, SK Chemicals' 2011 equity-method gains are expected to reach the W100bn level, considering that 1H equity-method gains (under K-GAAP) came in at W37.8bn (even including a loss of W23bn on the sale of SK Keris shares).

Taking into account the company's slow progress in receiving approval for SID-530 in Europe, we lowered our estimate for 2012 SID-530-related royalty income to W20bn (from W36bn).

► Earnings & Valuation Metrics

FY	Revenues (Wbn)	OP (Wbn)	OP Margin (%)	NP (Wbn)	EPS (Won)	EBITDA (Wbn)	FCF (Wbn)	ROE (%)	P/E (x)	P/B (x)	EV/EBITDA (x)
12/09	1,277	84	6.6	125	5,260	121	270	14.3	12.7	1.8	14.9
12/10	1,335	68	5.1	274	11,571	100	-46	30.1	5.3	1.6	18.6
12/11F	1,524	79	5.2	50	2,122	105	-58	5.4	36.2	2.0	17.4
12/12F	1,596	127	8.0	98	4,156	167	-29	9.9	18.5	1.8	11.0
12/13F	1,760	141	8.0	108	4,554	183	31	9.9	16.9	1.6	10.0

Note: All figures are based on non-consolidated K-IFRS; NP refers to net profit attributable to controlling interests
 Source: Company data, Daewoo Securities Research estimates

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Buy (Maintain)

Target Price (12M, W)	97,000
Share Price (11/08/16,W)	76,800
Expected Return (%)	26.3
EPS Growth (11F, %)	-81.7
Market EPS Growth (11F, %)	4.5
P/E(11F, x)	36.2
Market P/E(11F, x)	9.9
KOSPI	1,879.87
Market Cap (Wbn)	1,601
Shares Outstanding (mn)	24
Avg Trading Volume (60D, '000)	238
Avg Trading Value (60D, Wbn)	17
Dividend Yield (11F, %)	0.7
Free Float (%)	70.6
52-Week Low	55,200
52-Week High	82,800
Beta (12M, Daily Rate of Return)	0.8
Price Return Volatility (12M Daily, %,SD)	2.3
Foreign Ownership (%)	10.4

Major Shareholder(s)

SK Chemicals' treasury shares (15.53%)
 Chang-weon Choi et al. (13.85%)
 Mirae Asset Global Investments Co. Ltd. (7.31%)

Price Performance

(%)	1M	6M	12M
Absolute	-1.2	31.7	23.5
Relative	11.2	37.2	15.6

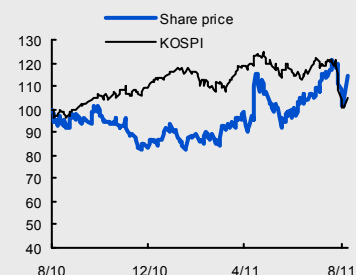


Table 1. Revisions to SK Chemicals' earnings forecasts

(Wbn, W, %)

	Before			After			%Change			Note
	11F	12F	13F	11F	12F	13F	11F	12F	13F	
Revenues	1,490.8	1,701.4	1,870.6	1,523.5	1,595.5	1,759.8	2.2	-6.2	-5.9	Reflects release of generic version of Taxotere
Operating profit	83.4	157.8	166.1	79.0	126.9	141.2	-5.3	-19.6	-15.0	Revised SID-530's royalty income
Pretax profit	121.7	220.0	239.1	58.6	126.1	138.7	-51.8	-42.7	-42.0	Under IFRS, removed equity-method gains
Net profit	94.5	166.7	181.2	50.2	98.3	108.2	-46.8	-41.0	-40.3	
EPS	3,992	7,045	7,657	2,122	4,156	4,572	-46.8	-41.0	-40.3	
OP margin	5.6	9.3	8.9	5.6	9.3	8.9				
Pretax margin	8.2	12.9	12.8	8.2	12.9	12.8				
Net margin	6.3	9.8	9.7	6.3	9.8	9.7				

Note: Before figures are based on non-consolidated K-IFRS. After figures are based on IFRS consolidated figures with equity gains excluded from pre-tax profit and net profit
Source: Daewoo Securities Research

Table 2. SK Chemicals' quarterly profit trends and forecasts

(Wbn, %)

	2011F					2012F					2Q11F	
	1Q	2QP	3QF	4QF	Year	1QF	2QF	3QF	4QF	Year	YoY	QoQ
Revenues	357.0	386.4	390.7	389.3	1,523.5	340.7	382.8	428.1	443.9	1,595.5	17.3	8.2
Operating profit	8.2	19.3	27.6	23.9	79.0	19.9	29.3	34.4	43.2	126.9	-3.3	136.2
Pretax profit	2.6	14.0	21.3	20.7	58.6	21.2	28.2	32.3	44.3	126.1	-95.3	429.4
Net profit	4.3	13.2	16.6	16.1	50.2	16.5	22.0	25.2	34.6	98.3	-94.2	210.0
OP margin	2.3	5.0	7.1	6.1	5.2	5.9	7.7	8.0	9.7	8.0		
Pretax margin	0.7	3.6	5.5	5.3	3.8	6.2	7.4	7.6	10.0	7.9		
Net margin	1.2	3.4	4.3	4.1	3.3	4.9	5.8	5.9	7.8	6.2		

Source: Company data, Daewoo Securities Research

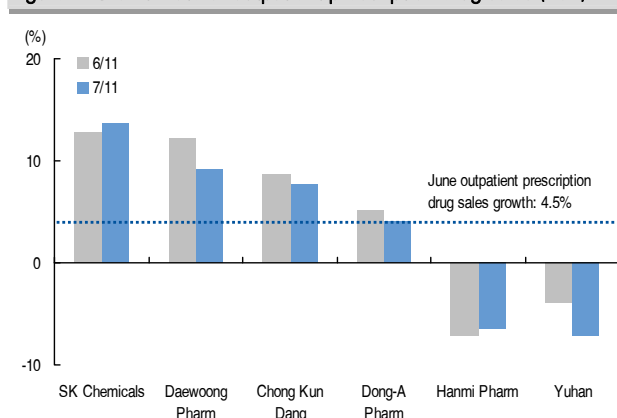
Table 3. SK Chemicals' sales trends and forecasts of flagship products

(Wbn, %)

	2011F					2012F				
	1Q	2QP	3QF	4QF	Year	1QF	2QF	3QF	4QF	Year
Total sales	357.0	386.4	390.7	389.3	1,523.5	340.7	382.8	428.1	443.9	1,595.5
Life science	77.7	93.8	117.7	112.3	401.4	91.3	105.4	128.7	138.3	463.7
Chemical	262.8	275.8	252.5	254.3	1,045.4	249.5	256.0	274.4	278.1	1,058.0
Others	16.5	16.8	20.6	22.8	76.6	-	21.4	24.9	27.6	73.8
Flagship product sales										
PET	121.2	115.4	108.7	105.4	450.7	103.3	95.3	94.8	94.8	388.2
PETG	38.9	39.5	39.6	40.2	158.1	43.4	42.2	62.7	63.0	211.3
Bio diesel	50.4	54.6	45.6	48.3	199.0	50.8	50.5	50.3	50.5	202.1
Sales growth										
PET	31.5	15.2	8.4	9.0	15.8	-14.8	-17.5	-12.8	-10.1	-13.9
PETG	17.9	16.7	15.0	23.3	18.2	11.7	6.9	58.4	56.7	33.6
Bio diesel	60.4	40.2	28.1	12.5	33.6	0.8	-7.5	10.2	4.5	1.6

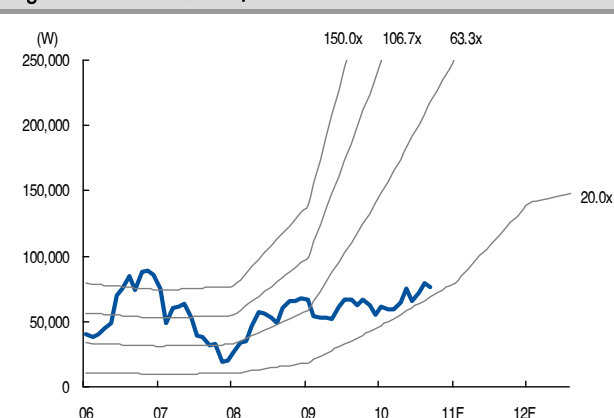
Source: Company data, Daewoo Securities Research

Figure 1. Growth rate of outpatient prescription drug sales (YoY)



Source: UBIST, Daewoo Securities Research

Figure 2. SK Chemicals' P/E band



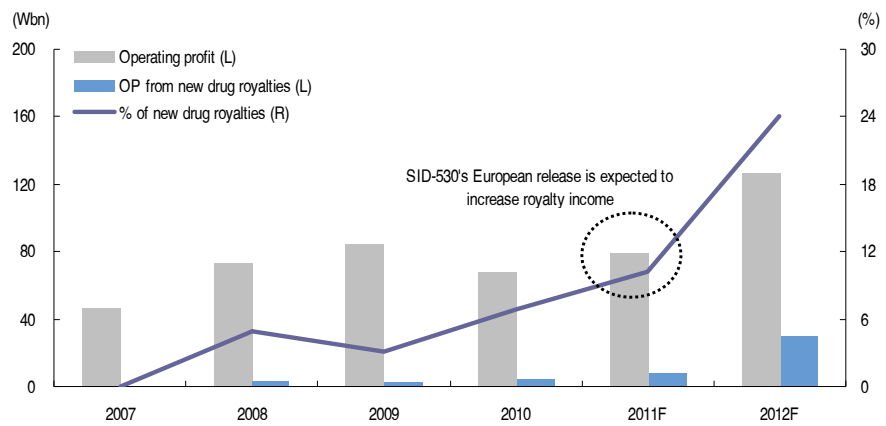
Source: Daewoo Securities Research

Table 4. Expected royalty income from new drugs

	2007	2008	2009	2010	2011F	2012F
Operating profit	46.7	73.1	84.3	68.3	79.0	126.9
OP from new drug royalties	0	3.6	2.6	4.6	8.0	30.5
SID-530 (EU, upfront & milestones)		3.6	-	-	3.1	-
SID-530 (EU, running royalty)		-	-	-	1.8	20.0
NBP-601 (global, upfront & milestones)		-	2.6	4.6	3.1	10.5
% of new drug royalties	-	5	3	7	10	24

Source: Daewoo Securities Research estimates; Note: Based on the assumption that royalty income is recognized on a quarterly basis

Figure 3. SK Chemicals' royalties from new drugs and operating profit forecasts



Source: Daewoo Securities Research

Figure 4. SK Chemicals' share price trend



Source: Daewoo Securities Research

SK Chemicals (006120 KS/Buy/TP: W97,000)

Comprehensive Income Statement (Summarized)				
(Wbn)	12/10	12/11F	12/12F	12/13F
Revenues	1,335	1,524	1,596	1,760
Cost of Sales	1,037	1,227	1,260	1,394
Gross Profit	297	297	336	366
SG&A Expenses	229	218	209	225
Operating Profit (Adj)	68	79	127	141
Operating Profit	68	79	127	141
Non-Operating Profit	278	-20	-1	-3
Net Financial Income	19	26	6	8
Net Gain from Inv in Associates	32	0	0	0
Pretax Profit	347	59	126	138
Income Tax	73	8	28	30
Profit from Continuing Operations	274	50	98	108
Profit from Discontinued Operations	0	0	0	0
Net Profit	274	50	98	108
Controlling Interests	274	50	98	108
Non-Controlling Interests	0	0	0	0
Total Comprehensive Profit	274	50	99	108
Controlling Interests	274	50	99	108
Non-Controlling Interests	0	0	0	0
EBITDA	100	105	167	183
FCF (Free Cash Flow)	-46	-58	-29	31
EBITDA Margin (%)	7.5	6.9	10.5	10.4
Operating Profit Margin (%)	5.1	5.2	8.0	8.0
Net Profit Margin (%)	20.5	3.3	6.2	6.1

Statement of Financial Condition (Summarized)				
(Wbn)	12/10	12/11F	12/12F	12/13F
Current Assets	509	740	730	842
Cash and Cash Equivalents	23	186	150	202
AR & Other Receivables	285	326	341	376
Inventories	192	219	229	253
Other Current Assets	8	10	10	11
Non-Current Assets	1,300	949	1,064	1,117
Investments in Associates	611	245	245	245
Property, Plant and Equipment	563	555	672	726
Intangible Assets	17	28	24	21
Total Assets	1,808	1,689	1,794	1,959
Current Liabilities	676	519	584	569
AP & Other Payables	213	243	254	280
Short-Term Financial Liabilities	392	195	245	195
Other Current Liabilities	71	81	85	94
Non-Current Liabilities	214	221	171	252
Long-Term Financial Liabilities	139	146	96	176
Other Non-Current Liabilities	61	62	62	63
Total Liabilities	889	740	755	821
Controlling Interests	919	949	1,039	1,138
Capital Stock	118	118	118	118
Capital Surplus	287	150	150	150
Retained Earnings	503	778	868	967
Non-Controlling Interests	0	0	0	0
Stockholders' Equity	919	949	1,039	1,138

Cash Flows (Summarized)				
(Wbn)	12/10	12/11F	12/12F	12/13F
Cash Flows from Op Activities	52	82	125	125
Net Profit	274	50	98	108
Non-Cash Income and Expense	-256	59	69	76
Depreciation	26	18	33	36
Amortization	6	8	8	6
Others	257	-7	-2	-2
Chg in Working Capital	34	-18	-15	-28
Chg in AR & Other Receivables	-25	-7	-15	-35
Chg in Inventories	11	-28	-10	-24
Chg in AP & Other Payables	3	31	12	26
Income Tax Paid	0	-9	-28	-30
Cash Flows from Inv Activities	-133	324	-135	-77
Chg in PP&E	69	-109	-150	-90
Chg in Intangible Assets	-3	-3	-3	-3
Chg in Financial Assets	38	-4	0	0
Others	-236	441	19	16
Cash Flows from Fin Activities	69	-243	-26	4
Chg in Financial Liabilities	99	-216	0	30
Chg in Equity	-20	0	0	0
Dividends Paid	-11	0	-9	-9
Others	-27	-27	-17	-17
Increase (Decrease) in Cash	-4	163	-36	52
Beginning Balance	27	23	186	150
Ending Balance	23	186	150	202

Forecasts/Valuations (Summarized)				
	12/10	12/11F	12/12F	12/13F
P/E (x)	5.3	36.2	18.5	16.9
P/CF (x)	4.8	24.0	13.1	12.1
P/B (x)	1.6	2.0	1.8	1.6
EV/EBITDA (x)	18.6	17.4	11.0	10.0
EPS (W)	11,571	2,122	4,156	4,554
CFPS (W)	12,922	3,202	5,871	6,334
BPS (W)	38,099	38,930	42,906	47,231
DPS (W)	0	500	500	500
Payout ratio (%)	3.8	17.5	9.0	8.2
Dividend Yield (%)	0.0	0.7	0.7	0.7
Revenue Growth (%)	4.6	14.2	4.7	10.3
EBITDA Growth (%)	-17.3	4.3	60.2	9.5
Operating Profit Growth (%)	-19.1	15.7	60.6	11.3
EPS Growth (%)	120.0	-81.7	95.8	9.6
Accounts Receivable Turnover (x)	5.3	5.3	5.1	5.2
Inventory Turnover (x)	6.7	7.4	7.1	7.3
Accounts Payable Turnover (x)	8.7	8.7	8.3	8.5
ROA (%)	14.4	2.9	5.7	5.7
ROE (%)	30.1	5.4	9.9	9.9
ROIC (%)	6.0	7.5	10.9	10.9
Liability to Equity Ratio (%)	96.8	77.9	72.7	72.1
Current Ratio (%)	75.3	142.7	125.0	148.0
Net Debt to Equity Ratio (%)	55.2	16.3	18.4	14.8
Interest Coverage Ratio (x)	3.1	2.9	7.3	8.1

Source: Company data, Daewoo Securities Research estimates

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Industry Ratings	Overweight	Fundamentals are favorable or improving	
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