Equity | Korea | Materials

29 March 2011

Produced by: RBS Asia Limited (Seoul) Branch

Kumho Petrochemical

Growth intact

Share price correction alongside natural rubber price declines offer an attractive buying opportunity, in our view, as we believe Kumho's operations are not affected due to the wide price gap between synthetic and natural rubbers. Solid quarterly earnings should ease concerns. We raise our TP to W192,000; Buy.

Buy

Target price
W192000 (from W159000)

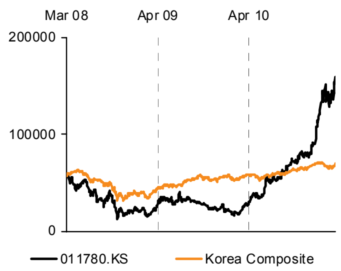
Price
W154000

Short term (0-60 days)
n/a

Market view
Underweight

Price performance

	(1M)	(3M)	(12M)
Price (W)	134000	90100	27950
Absolute (%)	14.9	70.9	451.0
Rel market (%)	8.4	68.1	354.9
Rel sector (%)	14.5	62.0	338.1



Market capitalisation
W3.92t (US$3.53bn)

Average (12M) daily turnover
W19326.75m (US$16.94m)

Sector: BBG AP Chemicals
RIC: 011780.KS, 011780 KS
Priced W154000 at close 28 Mar 2011.
Source: Bloomberg

Key forecasts

	FY08A	FY09A	FY10A	FY11F	FY12F
Revenue (Wb)	3,182	2,802	3,886	5,323	5,375
EBITDA (Wb)	353.5	218.0	468.3	802.3 ▲	824.6 ▲
Reported net profit (Wb)	-19.7	-614	595.1 ▲	592.0 ▲	631.1 ▲
Normalised net profit (Wb)[1]	-19.7	-614	425.1	592.0	631.1
Normalised EPS (W)	-777	-24,183	16,719 ▲	20,566 ▲	20,714 ▲
Dividend per share (W)	750.0	0.00	1,000 ▲	1,250 ▲	1,300 ▲
Dividend yield (%)	0.49	0.00	0.65	0.81	0.84
Normalised PE (x)	n/m	n/m	9.21	7.49	7.43
EV/EBITDA (x)	16.60	27.80	12.50	6.48	5.81
Price/book value (x)	3.37	7.32	4.45	2.87	2.11
ROIC (%)	8.78	2.70	10.50	19.20	19.20

Use of ▲ ▼ indicates that the line item has changed by at least 5%.
1. Post-goodwill amortisation and pre-exceptional items
Accounting standard: Local GAAP
Source: Company data, RBS forecasts

year to Dec, fully diluted

We raise 2011 and 2012 EPS by 17% and 13% and our target price to W192,000

We raise our 2011 and 2012 EPS forecasts by 16.8% and 13.0%, respectively, to reflect stronger-than-expected synthetic rubber prices. We increase our price assumptions to US$3,960/tonne for butadiene rubber (BR) (+10.1%) and US$3,741/tonne for styrene butadiene rubber (SBR) (+29.6%) – we consider our new assumptions conservative as they are about 10% lower than the recently set February offer prices of US$4,300/ton and US$4,000/ton, respectively. We raise our target price to W192,000 from W159,000 (+20.8%) to reflect our higher EBITDA estimate and the rise in the value of treasury shares (22% of total).

Kumho P&B: Beneficiary of strong phenol chain demand

Under the newly adopted IFRS accounting standard, Kumho P&B's performance is reflected in Kumho Petrochem's financials. Phenol and bisphenol-A (BPA) account for 60% of Kumho P&B's revenue, and both enjoy strong price spreads due to solid demand for polycarbonate (used to make hard cases for smart phones). In addition, Korea's phenol and BPA markets are oligopolies – Kumho P&B enjoys around 50% domestic market share and is a beneficiary of strong phenol chain demand. On our numbers, Kumho P&B will post 14.5% yoy operating profit growth for 2011 following record 600% operating profit growth in 2010.

Concern over falling natural rubber price overblown

Despite recent market concern about falling natural rubber prices, the spread between natural rubber and synthetic rubber prices has actually widened (more than US$1,000/tonne vs the US$172/tonne and US$25/tonne averages for SBR and BR, respectively, over the past 10 years). Therefore, we believe the recent natural rubber price decline will have no impact on synthetic rubber prices. In addition, we believe that rising butadiene prices support synthetic rubber via potential cost-led price hikes.

Analysts

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Important disclosures can be found in the Disclosures Appendix.

Raising 2011F and 2012F EPS by 17% and 13%, respectively

We raise our 2011 and 2012 EPS forecasts by 16.8% and 13.0%, respectively, to reflect stronger-than-expected BR and SBR prices. As Table 3 outlines, we raise our BR and SBR price assumptions by 10.1% and 29.6%, respectively, to reflect the currently strong price trend amid solid demand. We forecast average 2011 prices of US$3,960/tonne for BR and $3,741/tonne for SBR – we consider our new assumptions conservative as they are about 10% lower than the recently set February offer prices of US$4,300/tonne and US$4,000/tonne. Therefore, a 10-15% drop in synthetic rubber prices would not negatively impact our earnings forecasts.

Table 1 : Earnings revisions

	FY11F			FY12F		
(Wbn)	After	Before	Chg	After	Before	Chg
Revenue	5,323	4,579	16.3%	5,375	4,944	2.7%
Operating profit	696	577	20.6%	717	612	17.0%
Pre-tax profit	759	650	16.8%	809	716	13.0%
Net profit	592	507	16.8%	631	559	12.9%
EBITDA	802	699	14.8%	824	732	12.5%
EPS	20,566	17,615	16.8%	20,714	18,332	13.0%

Source: RBS forecasts

Table 2 : RBS forecasts vs Bloomberg consensus

	2011F			2012F		
(Wbn)	RBS fcsts	Consensus	Diff	RBS fcsts	Consensus	Diff
Revenue	5,323	5,200	2.4%	5,375	5,455	-1.5%
Operating profit	696	709	-1.8%	717	741	-3.2%
Pre-tax profit	759	841	-9.8%	809	885	-8.6%
Net profit	592	623	-4.9%	631	655	-3.6%
EBITDA	802	846	-5.2%	825	847	-2.7%
EPS	20,566	22,024	-6.6%	20,714	22,348	-7.3%

Source: RBS forecasts, Bloomberg

Table 3 : Major assumptions

	2006	2007	2008	2009	2010	2011F	2012F	2013F
Synthetic rubber (US$/tonne)								
BR (butadiene rubber)	1,500	1,600	2,360	1,440	2,263	3,960	4,079	3,875
(% yoy)	-6.3%	6.7%	47.5%	-39.0%	57.2%	75.0%	3.0%	-5.0%
SBR (styrene butadiene rubber)	1,745	1,760	2,960	1,590	2,771	3,741	3,928	3,731
(% yoy)	-4.1%	0.9%	68.2%	-46.3%	74.3%	35.0%	5.0%	-5.0%
Synthetic resin (US$/tonne)								
PS (polystyrene)	1,248	1,435	1,413	1,055	1,341	1,400	1,550	1,550
(% yoy)	6.7%	14.9%	-1.5%	-25.4%	27.1%	4.4%	10.7%	0.0%
ABS (acrylonitrille butadiene styrene)	1,528	1,701	1,848	1,358	1,900	2,000	2,020	2,020
(% yoy)	8.5%	11.3%	8.7%	-26.5%	39.9%	5.3%	1.0%	0.0%
Raw material (US$/tonne)								
BD (butadiene)	1,055	1,205	1,753	894	1,933	2,400	2,450	2,450
(% yoy)	13.5%	14.3%	45.4%	-49.0%	116.2%	24.2%	2.1%	0.0%
SM (styrene monomer)	1,165	1,319	1,265	953	1,190	1,400	1,520	1,550
(% yoy)	10.0%	13.2%	-4.1%	-24.7%	24.9%	17.6%	8.6%	2.0%

Source: Company data, RBS forecasts

Table 4 : Change in major assumptions

	After			Before			Change		
(US$/tonne)	2011F	2012F	2013F	2011F	2012F	2013F	2011F	2012F	2013F
BR	3,960	4,079	3,875	3,596	3,848	3,463	10.1%	6.0%	11.9%
SBR	3,741	3,928	3,731	2,886	3,319	2,987	29.6%	18.3%	24.9%
BD	2,400	2,450	2,450	2,250	2,100	1,700	6.7%	16.7%	44.1%

Source: RBS forecasts

1Q11 likely to be in line with recently raised consensus

1Q11 looks likely to surpass the numbers in our February preview. However, we expect results to be in line with consensus, as consensus numbers continue to rise due to the industry's upbeat operating environment. Operating profit looks to be on track to double yoy.

Table 5 : 1Q11 preview

(Wbn)	1Q11E	Consensus	Diff	1Q10	yoy	4Q10	qoq
Sales	1,202.4	1259.1	-4.5%	886.5	35.6%	1,022.2	17.6%
Synthetic rubbers	746.6			497.7	50.0%	591.2	26.3%
Synthetic resin	340.1			288.3	18.0%	316.2	7.6%
Others	115.6			100.5	15.0%	114.8	0.7%
Operating profit	174.9	185.3	-5.6%	65.0	169.2%	105.3	66.1%
Synthetic rubbers	126.9			37.1	242.1%	65.7	93.2%
Synthetic resin	24.8			7.4	235.5%	25.1	-1.1%
Others	23.1			20.5	12.8%	14.5	59.5%
Pre-tax profit	194.9	200.2	-2.6%	57.0	242.1%	127.4	53.0%
Equity method gains	50.0			13.4	272.6%	55.9	-10.5%
Net profit	155.9	166.5	-6.4%	46.0	238.9%	108.3	44.0%
Margin (%)							
Operating profit	14.5%		125.0%	7.3%		10.3%	
Synthetic rubbers	17.0%			7.5%		11.1%	
Synthetic resin	7.3%			2.6%		7.9%	
Others	20.0%			20.4%		12.6%	
Pre-tax profit	16.2%		58.6%	6.4%		12.5%	
Net profit	13.0%		141.8%	5.2%		10.6%	

Note: W47.3bn and W164.9bn one-off gains from disposal of investment securities were deducted in 1Q10 and 4Q10, respectively.
Source: Company data, RBS forecasts

Raising target price to W192,000

We raise our target price to W192,000 from W159,000 (+20.8%) based on our higher EBITDA estimate and the increased value of treasury shares – we have not changed our valuation multiples for Kumho Petrochemical or Kumho P&B. Our new target price provides 24.7% upside potential from the current share price. Buy Maintained.

Table 6 : Sum-of-the-parts valuation

Company	Business	Stake	Valuation methodology	(Wbn)
Main operation	Synthetic rubbers, synthetic resin		6x EV/EBITDA, 10% discount to Korean petrochemical peers	4,814
Other assets				
Kumho Polychem	EPM (copolymer of ethylene and propylene), EPDM (terpolymer of ethylene, propylene and a non-conjugated diene)	50%	Book value	61
Kumho Mitsui Chem	MDI (methylene diphenyl diisocyanate), Aniline	50%	Book value	69
Kumho P&B	Cumene, phenol, BPA, epoxy resins	78%	5x 2011F EV/EBITDA reflecting narrow production scope	938
Kumho Petro Holdings	Holding companies controlling five JVs in China	100%	Book value	71
Sub-total				1,139
Treasury shares	22% of total shares		Based on W154,000 share price	884
Other assets	Assets related with Kumho Asiana group			334
Net debt				1,284
Equity value				5,887
No of shares				30,467,693
Per share equity value	(Rounding from W192,485)			192,000
Current share price				154,000
Upside potential				24.7%

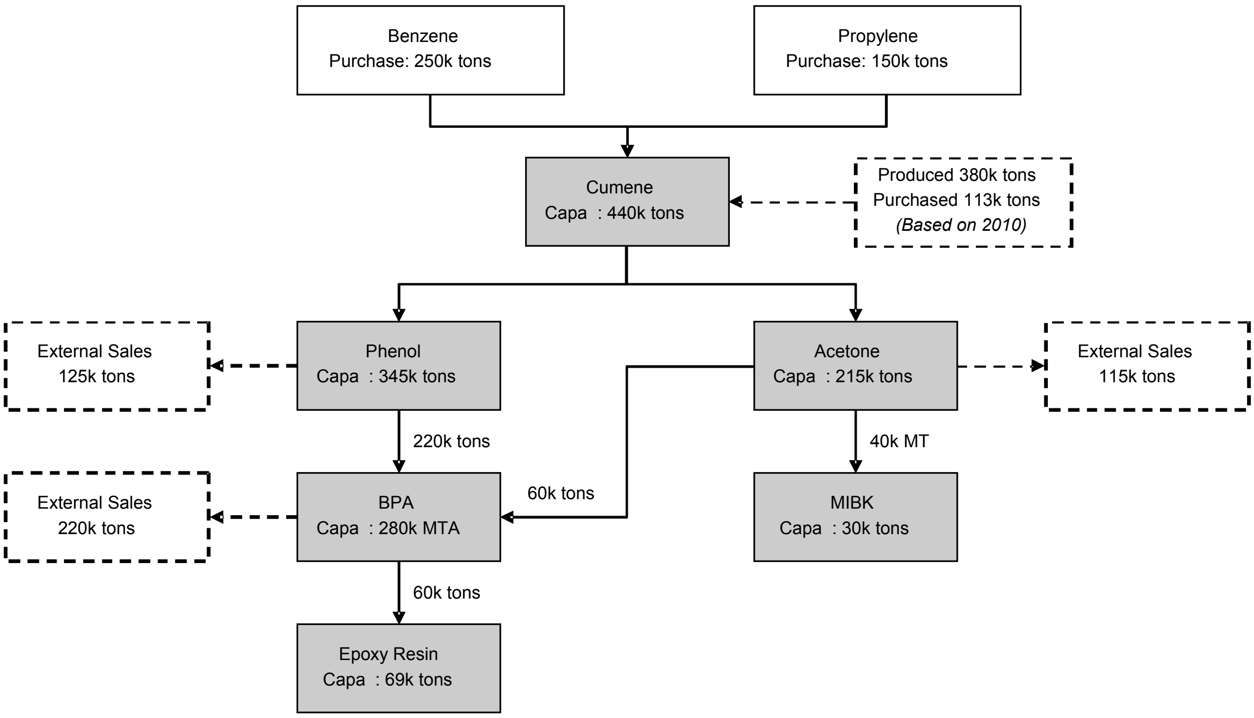
Source: Company data, RBS forecasts

Kumho P&B: beneficiary of strong phenol chain demand

Under the newly adopted IFRS accounting standard, Kumho P&B's performance is reflected in Kumho Petrochem's financials. We recently visited Kumho P&B (78.2% owned by Kumho Petrochemical) to discuss strong operating trends for phenol and BPA. As Figure 1 illustrates, phenol and BPA account for 60% of Kumho P&B's revenue.

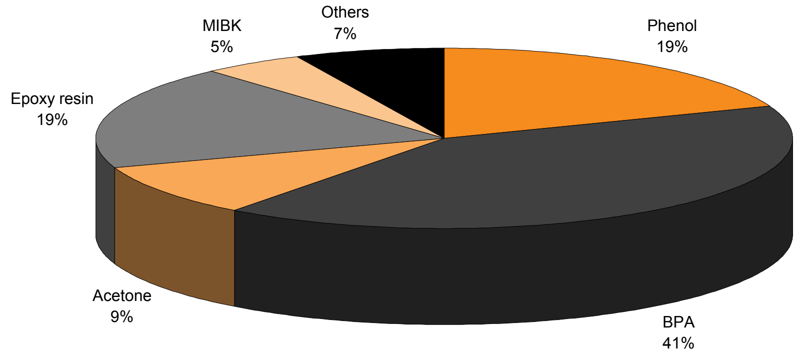
Due to limited phenol and BPA capacity addition and strong polycarbonate demand, Kumho P&B's operating profit increased 600% yoy in 2009. We expect 14.5% yoy operating profit growth in 2011 despite the record-high 2010 base.

Figure 1 : Kumho P&B: production flow chart



Source: Company data, RBS summary

Chart 1 : Revenue breakdown (2010)



Source: Company data

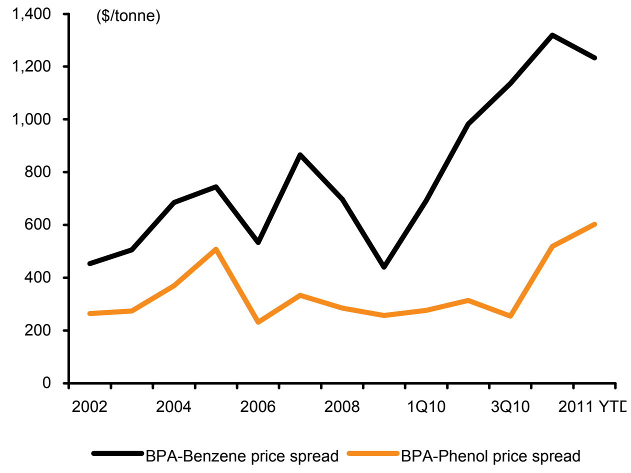
In Korea, only three companies produce BPA and Kumho P&B enjoys around 50% market share. The company's domestic-sales-to-exports ratio is usually 50:50, but it currently stands at 70:30 due to strong domestic demand.

Kumho P&B plans to add capacity in 2011 and 2013. In 2011, it plans to implement de-bottlenecking and to increase capacity by 35k tons of phenol and 22k tons of acetone. In 2013, it plans to spend about W200bn to increase capacity by 250k tons of phenol, 155k tons of acetone, and 150k tons of BPA.

Chart 2 : Price trend

Source: Datastream

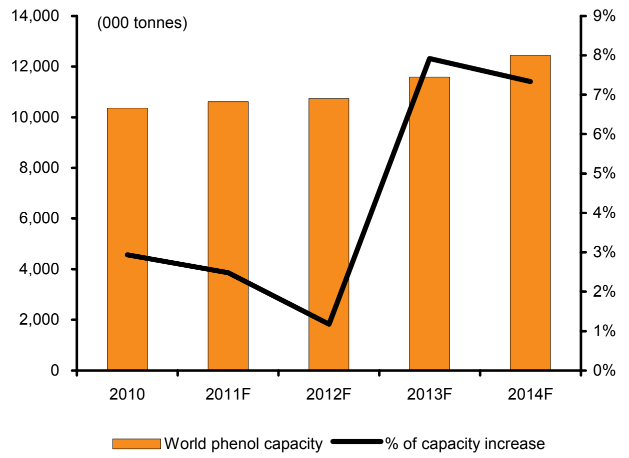
Chart 3 : Price spread trend



Source: Datastream

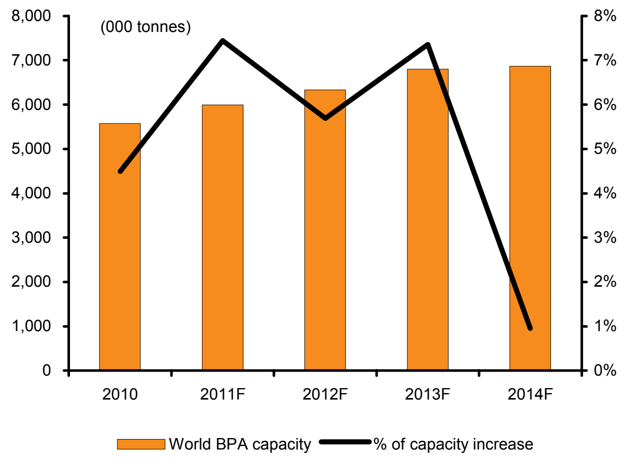
We expect industry BPA capacity to increase by 390k tons (+7.4% yoy) in 2011. One project is the Mitsubishi-Sinopec plant in China (150k ton capacity, scheduled for completion in 1Q11) and another is the SABIC plant in Saudi Arabia (240k ton capacity, scheduled for completion in 2Q11). As usual, we can't exclude the possibility of delays that could tighten supply.

Chart 4 : Phenol capacity addition



Source: RBS forecast, ChemLocus

Chart 5 : BPA capacity addition



Source: RBS forecasts, ChemLocus

Table 7 : Kumho P&B: income statement

(Wbn)	2005	2006	2007	2008	2009	2010	2011F	yoy
Sales	546.4	596.4	730.9	872.0	784.4	1,099.2	1,300.0	18.3%
Gross profit	63.6	32.6	93.6	72.3	61.6	229.0	260.0	13.5%
Operating profit	30.7	1.6	60.0	37.7	25.2	192.1	220.0	14.5%
Pretax profit	11.1	(5.1)	52.2	0.3	16.3	175.4	201.5	14.9%
Net profit	11.1	(5.1)	45.0	5.9	13.5	142.6	165.1	15.7%
Margin (%)								
Gross profit	11.6%	5.5%	12.8%	8.3%	7.8%	20.8%	20.0%	
Operating profit	5.6%	0.3%	8.2%	4.3%	3.2%	17.5%	16.9%	
Pretax profit	2.0%	-0.9%	7.1%	0.0%	2.1%	16.0%	15.5%	
Net profit	2.0%	-0.9%	6.2%	0.7%	1.7%	13.0%	12.7%	

Source: Company data, RBS forecasts

Table 8 : Kumho P&B: balance sheet

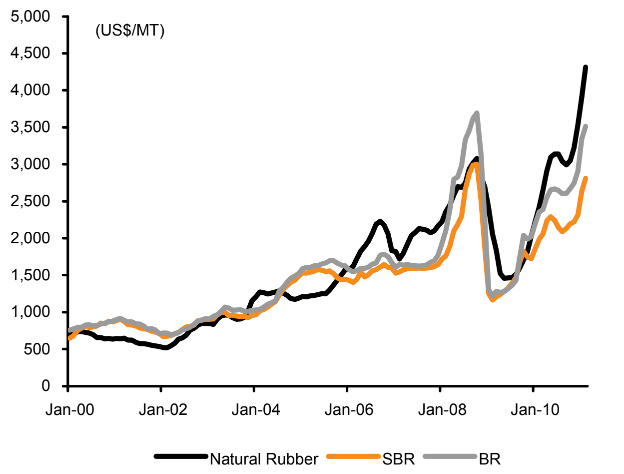
(Wbn)	2005	2006	2007	2008	2009	2010
Total assets	395.6	401.0	487.1	715.5	620.1	642.1
Current assets	160.1	168.8	195.6	240.5	228.3	267.7
Cash & cash equivalent	19.1	10.6	8.7	40.7	10.2	17.7
Accounts receivable	73.4	102.4	114.6	108.9	139.1	149.1
Inventory	61.2	47.4	67.8	70.6	61.7	77.9
Others	6.5	8.3	4.5	20.3	17.3	23.1
Non-current assets	235.4	232.2	291.6	475.0	391.8	374.4
Investment assets	5.2	12.3	11.0	112.5	65.0	66.9
Tangible assets	228.5	217.4	275.9	356.5	319.8	298.9
Intangible assets	-	-	-	-	-	
Others	1.69	2.50	4.64	5.95	7.0	8.5
Total liabilities	273.8	284.6	322.1	534.1	433.3	332.3
Current liabilities	193.9	173.0	208.5	377.8	318.3	251.5
Accounts payable	45.8	58.2	67.9	59.9	99.5	81.6
ST debt	87.5	77.7	58.2	166.3	105.8	93.2
Current portion of LT debt	15.0	11.7	54.3	112.5	88.0	22.3
Others	45.52	25.41	28.13	39.10	25.0	54.3
Non-current assets	79.9	111.6	113.6	156.2	114.9	80.8
Bonds	-	5.0	5.0	-	30.0	30.0
LT debt	70.0	93.4	94.6	142.0	70.9	42.0
Others	9.9	13.2	14.0	14.2	14.1	
Shareholders' equity	121.8	116.4	165.0	181.4	186.8	309.8
Paid-in capital	143.7	143.7	143.7	143.7	143.7	143.7
Capital surplus	-	-	3.8	3.8	3.8	3.8
Retained earnings	(22.3)	(27.4)	17.5	23.5	37.0	179.7
Other capital adjustment	0.3	0.1	(0.0)	10.5	2.3	(17.3)
Net debt	153.4	177.1	203.4	380.2	284.4	169.8
Net debt/equity	n/a	152.2%	123.3%	209.5%	152.2%	54.8%

Source: Company data

Concern over falling natural rubber price overblown

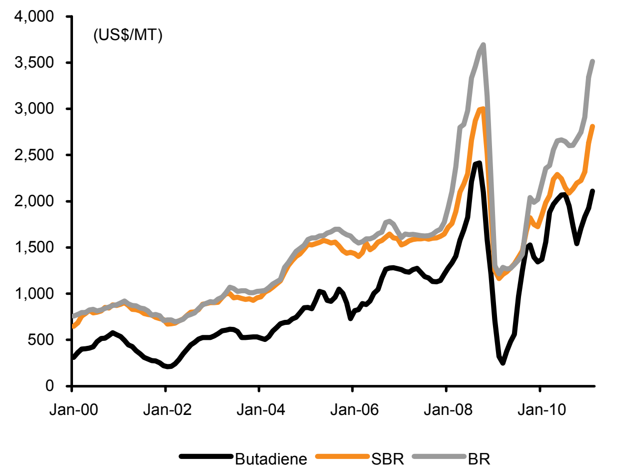
Despite recent market concern about the falling natural rubber prices, the spread between natural rubber and synthetic rubber prices has actually widened. We believe a moderate decline in natural rubber prices would not impact synthetic rubber prices, but would just narrow the gap between the two. Furthermore, the price of natural rubber has actually rebounded of late due to supply control by exporting countries (eg, Thailand)

Chart 6 : Prices of natural rubber and synthetic rubbers



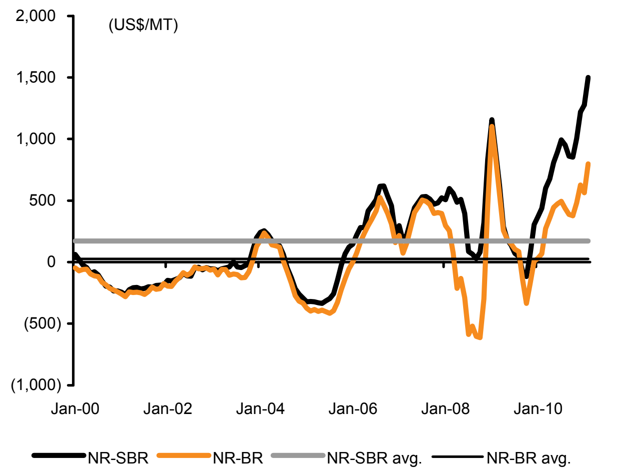
Source: KITA (The Korea International Trade Association), RBS

Chart 7 : Prices of synthetic rubbers and butadiene



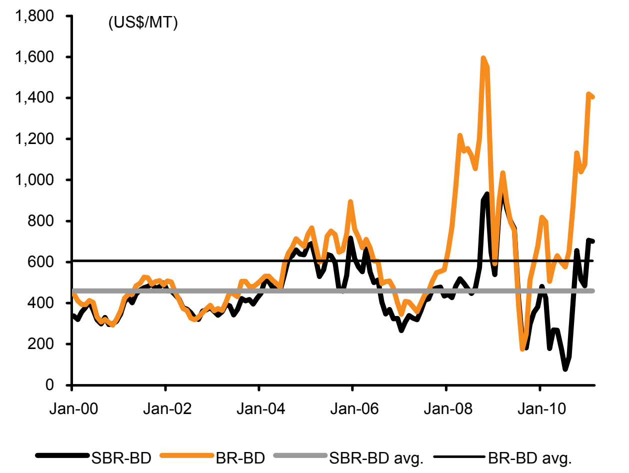
Source: KITA, RBS

Chart 8 : Spreads between natural and synthetic rubbers



Source: KITA, RBS

Chart 9 : Spreads between synthetic rubbers and butadiene

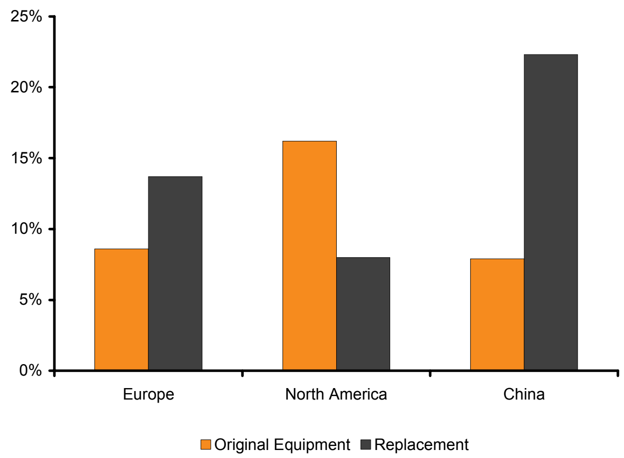


Source: KITA, RBS

Replacement tyre demand remains solid

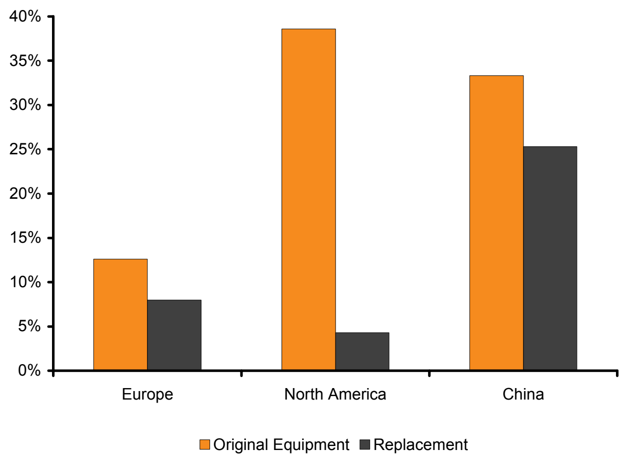
According to Michelin, the tyre market showed solid yoy growth in January and February 2011, with the focus on replacement tyres. The European and North American replacement tyre markets (which account for more than 80% of the overall tyre market in each region) posted 13.7% and 8.0% yoy growth in the same period, respectively. In China, the replacement tyre market (which accounts for around 50% of the total market) showed 22.3% yoy growth. Michelin expects replacement tyre market growth to remain strong throughout 2011.

Chart 10 : Tyre market growth (Jan-Feb 2011)



Source: Michelin

Chart 11 : Tyre market growth (2010)



Source: Michelin

Income statement

Wb	FY08A	FY09A	FY10A	FY11F	FY12F
Revenue	3182	2802	3886	5323	5375
Cost of sales	-2703	-2488	-3306	-4369	-4374
Operating costs	-126.4	-96.2	-112.1	-152.1	-176.5
EBITDA	**353.5**	**218.0**	**468.3**	**802.3**	**824.6**
DDA & Impairment (ex gw)	-72.2	-101.8	-108.7	-106.4	-107.2
EBITA	**281.3**	**116.2**	**359.6**	**695.9**	**717.3**
Goodwill (amort/impaired)	n/a	n/a	n/a	n/a	n/a
EBIT	**281.3**	**116.2**	**359.6**	**695.9**	**717.3**
Net interest	-86.3	-105.6	-116.8	-101.3	-69.3
Associates (pre-tax)	-169.1	-733.5	145.0	173.8	191.9
Forex gain / (loss)	-110.2	26.8	3.91	-5.75	-5.71
Exceptionals (pre-tax)	n/a	n/a	170.0	n/a	n/a
Other pre-tax items	57.7	-145.8	33.4	-3.65	-25.2
Reported PTP	**-26.7**	**-841.9**	**595.1**	**759.0**	**809.1**
Taxation	6.91	227.0	0.00	-167.0	-178.0
Minority interests	n/a	n/a	n/a	n/a	n/a
Exceptionals (post-tax)	n/a	n/a	n/a	n/a	n/a
Other post-tax items	0.00	0.00	0.00	0.00	0.00
Reported net profit	**-19.7**	**-614.8**	**595.1**	**592.0**	**631.1**
Normalised Items Excl. GW	0.00	0.00	170.0	0.00	0.00
Normalised net profit	**-19.7**	**-614.8**	**425.1**	**592.0**	**631.1**

Source: Company data, RBS forecasts year to Dec

Balance sheet

Wb	FY08A	FY09A	FY10A	FY11F	FY12F
Cash & market secs (1)	13.1	80.4	109.0	495.2	543.9
Other current assets	770.2	695.4	781.6	1003	984.1
Tangible fixed assets	1273	1357	1423	1405	1407
Intang assets (incl gw)	45.4	35.6	26.4	27.7	28.5
Oth non-curr assets	1613	1032	1096	1060	1257
Total assets	**3715**	**3200**	**3436**	**3992**	**4221**
Short term debt (2)	168.1	769.9	420.5	420.5	420.5
Trade & oth current liab	948.9	1289	1274	1040	640.4
Long term debt (3)	1309	585.1	858.4	894.9	935.5
Oth non-current liab	126.0	20.9	2.07	n/m	n/m
Total liabilities	**2552**	**2665**	**2555**	**2355**	**1993**
Total equity (incl min)	1163	535.1	880.3	1636	2228
Total liab & sh equity	**3715**	**3200**	**3436**	**3992**	**4221**
Net debt	1956	2150	1951	1284	871.5

Source: Company data, RBS forecasts year ended Dec

Cash flow statement

Wb	FY08A	FY09A	FY10A	FY11F	FY12F
EBITDA	353.5	218.0	468.3	802.3	824.6
Change in working capital	-250.2	-49.0	23.3	-137.8	23.0
Net interest (pd) / rec	-86.3	-105.6	-116.8	-101.3	-69.3
Taxes paid	n/a	n/a	n/a	n/a	n/a
Other oper cash items	-51.3	218.3	-121.5	-252.6	-211.4
Cash flow from ops (1)	**-34.4**	**281.7**	**253.2**	**310.6**	**567.0**
Capex (2)	-334.8	-264.1	-174.9	-80.0	-100.0
Disposals/(acquisitions)	-43.0	-199.7	125.2	210.2	-3.69
Other investing cash flow	-6.20	-4.55	-3.15	-14.7	-15.0
Cash flow from invest (3)	**-384.0**	**-468.4**	**-52.8**	**115.5**	**-118.7**
Incr / (decr) in equity	0.00	0.00	0.00	200.0	0.00
Incr / (decr) in debt	435.4	129.3	-91.9	-220.1	-363.5
Ordinary dividend paid	-17.3	-17.3	0.00	-19.8	-36.0
Preferred dividends (4)	n/a	n/a	n/a	n/a	n/a
Other financing cash flow	1.73	142.0	-78.9	0.00	0.00
Cash flow from fin (5)	**419.8**	**253.9**	**-170.8**	**-39.9**	**-399.5**
Forex & disc ops (6)	n/a	n/a	n/a	n/a	n/a
Inc/(decr) cash (1+3+5+6)	**1.40**	**67.3**	**29.6**	**386.2**	**48.8**
Equity FCF (1+2+4)	-369.2	17.6	78.3	230.6	467.0

Lines in bold can be derived from the immediately preceding lines. year to Dec
Source: Company data, RBS forecasts

Standard ratios

Performance	Kumho Petrochem FY08A	FY09A	FY10A	FY11F	FY12F	Honam Petrochemical FY10F	FY11F	FY12F	LG Chem FY10F	FY11F	FY12F
Sales growth (%)	49.8	-12.0	38.7	37.0	0.97	21.8	8.31	1.81	23.6	17.3	14.4
EBITDA growth (%)	62.1	-38.3	114.8	71.3	2.78	17.1	22.7	15.2	23.3	24.0	12.5
EBIT growth (%)	75.0	-58.7	209.5	93.5	3.08	22.1	25.6	18.0	26.3	25.4	15.0
Normalised EPS growth (%)	n/a	3014	n/a	23.0	0.72	3.15	44.2	25.9	38.6	23.1	14.6
EBITDA margin (%)	11.1	7.78	12.1	15.1	15.3	15.3	17.4	19.6	18.0	19.0	18.7
EBIT margin (%)	8.84	4.15	9.25	13.1	13.3	12.1	14.0	16.2	14.5	15.5	15.6
Net profit margin (%)	-0.62	-21.9	10.9	11.1	11.7	11.3	15.0	18.6	11.0	11.5	11.6
Return on avg assets (%)	1.34	-15.6	15.6	18.1	16.7	13.0	15.5	16.6	20.5	20.9	19.6
Return on avg equity (%)	-1.93	-72.4	60.1	47.0	32.7	20.0	23.4	23.6	33.5	30.9	27.2
ROIC (%)	8.78	2.70	10.5	19.2	19.2	20.0	18.0	17.8	33.5	33.8	31.2
ROIC - WACC (%)	-2.31	-8.38	-0.55	8.07	8.08	8.78	6.83	6.63	24.1	24.4	21.8
					year to Dec			year to Dec			year to Dec

Valuation	Kumho Petrochem FY08A	FY09A	FY10A	FY11F	FY12F	Honam Petrochemical FY10F	FY11F	FY12F	LG Chem FY10F	FY11F	FY12F
EV/sales (x)	1.85	2.17	1.51	0.98	0.89	1.81	1.66	1.60	1.50	1.26	1.07
EV/EBITDA (x)	16.6	27.8	12.5	6.48	5.81	11.8	9.57	8.16	8.36	6.64	5.71
EV/EBITDA @ tgt price (x)	19.3	32.3	14.6	7.68	6.98	9.64	7.78	6.61	9.84	7.83	6.77
EV/EBIT (x)	20.9	52.2	16.3	7.47	6.67	15.0	11.9	9.90	10.4	8.15	6.85
EV/invested capital (x)	1.87	2.24	2.07	1.78	1.55	2.70	2.21	1.81	3.59	2.83	2.32
Price/book value (x)	3.37	7.32	4.45	2.87	2.11	2.84	2.28	1.82	3.91	2.96	2.32
Equity FCF yield (%)	-9.43	0.45	2.00	5.20	9.95	3.69	4.37	6.17	2.28	2.50	4.35
Normalised PE (x)	n/m	n/m	9.21	7.49	7.43	15.6	10.8	8.57	13.5	11.0	9.57
Norm PE @tgt price (x)	n/m	n/m	11.5	9.34	9.27	12.6	8.74	6.94	15.9	12.9	11.3
Dividend yield (%)	0.49	0.00	0.65	0.81	0.84	0.37	0.50	0.62	0.92	1.03	1.15
					year to Dec			year to Dec			year to Dec

Per share data	FY08A	FY09A	FY10A	FY11F	FY12F
Tot adj dil sh, ave (b)	0.03	0.03	0.03	0.03	0.03
Reported EPS (KRW)	-777	-24183	23406	20566	20714
Normalised EPS (KRW)	-777	-24183	16719	20566	20714
Dividend per share (KRW)	750	0	1000	1250	1300
Equity FCF per share (KRW)	-14521	691	3080	8009	15327
Book value per sh (KRW)	45749	21047	34625	53708	73122
					year to Dec

Solvency	FY08A	FY09A	FY10F	FY11F	FY12F
Net debt to equity (%)	168.2	401.8	221.6	78.5	39.1
Net debt to tot ass (%)	52.7	67.2	56.8	32.2	20.6
Net debt to EBITDA	5.54	9.87	4.17	1.60	1.06
Current ratio (x)	0.70	0.38	0.53	1.03	1.44
Operating CF int cov (x)	0.60	3.67	3.17	4.07	9.19
Dividend cover (x)	-1.14	0.00	21.4	16.5	15.9
					year to Dec

Priced as follows: 011780.KS - W154000; 011170.KS - W401500; 051910.KS - W436500
Source: Company data, RBS forecasts

Valuation methodology – Sum-of-the-parts valuation

Company	Business	Stake	Valuation methodology	(Wbn)
Main operation	Synthetic rubbers, synthetic resin		6x EV/EBITDA, 10% discount to Korean petrochemical peers	4,814
Other assets				
Kumho Polychem	EPM (Copolymer of ethylene and propylene), EPDM (Terpolymer of ethylene, propylene and a non-conjugated diene)	50%	Book value	61
Kumho Mitsui Chem	MDI (Methylene diphenyl diisocyanate), Aniline	50%	Book value	69
Kumho P&B	Cumene, Phenol, BPA, Epoxy resins	78%	5x 2011F EV/EBITDA reflecting narrow production scope	938
Kumho Petro Holdings	Holding companies of five J/Vs in China	100%	Book value	71
Sub total				1,139
Treasury shares	22% of total shares		Based on W154,000 share price	884
Other assets	Assets related with Kumho Asiana group			334
Net debt				1,284
Equity value				5,887
No. of shares				30,467,693
Per share equity value	(Rounding from W192,485)			192,000
Current share price				154,000
Upside potential				24.7%

Source: Company data, RBS forecasts

Company description — Buy

Kumho Petrochem produces synthetic rubber (57% of total sales), synthetic resin (32%) and other specialty chemicals. Kumho enjoys 9-10% global synthetic rubber (eg BR, SBR) sales market share. Some 70% of synthetic rubber revenue comes from the tyre market, which shows solid demand. In the synthetic resin market, Kumho produces PS and ABS. In addition, the company has six chemical-related subsidiaries, including Kumho P&B, which produces phenol, bisphenol-A and epoxy resin. Kumho Petrochem was originally part of the Kumho Asiana group, but was spun off in early 2010 and recently began to focus on its core chemicals operation.

Price relative to country

Strategic analysis — Average SWOT company score: 4

Strengths — 4

Kumho has a leading global position in synthetic rubbers, with 9-10% sales market share, and supplies its products to a diversified group of customers.

Weaknesses — 3

Kumho is vulnerable to raw material price hikes, such as for butadiene and styrene monomer.

Opportunities — 4

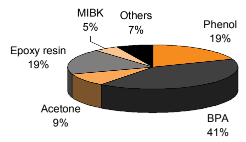
Kumho is likely to benefit from strong tyre demand, especially tyre replacement demand in China. High natural rubber prices also increase substitute demand for synthetic rubbers.

Threats — 3

Ambitous expansion plans by Middle East and China producers over the next five to seven years might cause oversupply and lower profitability.

Scoring range is 1-5 (high score is good)

Sales breakdown (FY10)



Source: Company data

Market data

Headquarters
115 Shinmunno 1-ga, Jongono-gu, Seoul, Korea

Website
www.kkpc.com

Shares in issue
25.4m

Freefloat
58%

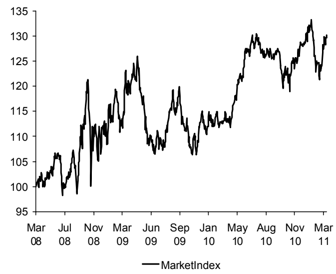
Majority shareholders
Related party (42%)

Country view: Korea

The Korean market has experienced a relative bounce over the past quarter, effectively playing catch-up to regional share prices. Nonetheless, we remain concerned over gearing to the global manufacturing cycle, historically elevated valuations and relatively tight liquidity conditions. We concede, however, that with foreign investors, in general, Underweight, the market might continue to benefit from rotational buying.

The country view is set in consultation with the relevant company analyst but is the ultimate responsibility of the Strategy Team.

Country rel to Asia Pacific



Competitive position — Average competitive score: 3-

Supplier power — 3-

The key raw material is butadiene, which is readily available. However, we are concerned about the declining self-sufficiency ratio of butadiene from 40% to 20%.

Barriers to entry — 3+

Relatively high capital costs of US$1bn and required economies of scale could be key barriers to new entrants.

Customer power — 2-

Tyre makers are more dependent on synthetic rubber providers to catch up rapidly growing demand, as there are a few synthetic rubber suppliers.

Substitute products — 4-

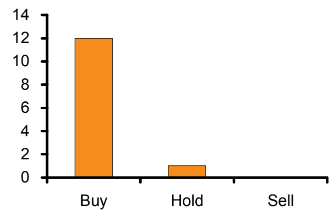
There are no substitutes for synthetic rubbers, even though natural rubbers can replace them to some degree. However, natural rubbers are more subject to tight supply.

Rivalry — 2-

New capacity in China and the Middle East could pose a threat in the long term. However, we expect limited capacity addition in the near future.

Scoring range 1-5 (high score is good) Plus = getting better Minus = getting worse

Broker recommendations



Source: Bloomberg

Recommendation structure

Absolute performance, short term (trading) recommendation: A Trading Buy recommendation implies upside of 5% or more and a Trading Sell indicates downside of 5% or more. The trading recommendation time horizon is 0-60 days. For Australian coverage, a Trading Buy recommendation implies upside of 5% or more from the suggested entry price range, and a Trading Sell recommendation implies downside of 5% or more from the suggested entry price range. The trading recommendation time horizon is 0-60 days.

Absolute performance, long term (fundamental) recommendation: The recommendation is based on implied upside/downside for the stock from the target price and, except as follows, only reflects capital appreciation. A Buy/Sell implies upside/downside of 10% or more and a Hold less than 10%. For research produced by Nedbank Capital, a Buy implies upside in excess of 20%, A Sell implies an expected return less than 10%, and a Hold implies a return between 10% and 20%. For UK-based Investment Funds research, the recommendation structure is not based on upside/downside to the target price. Rather it is the subjective view of the analyst based on an assessment of the resources and track record of the fund management company. For research produced by Nedbank Capital and for research on Australian listed property trusts (LPT) or real estate investment trusts (REIT), the recommendation is based upon total return, ie, the estimated total return of capital gain, dividends and distributions received for any particular stock over the investment horizon.

Performance parameters and horizon: Given the volatility of share prices and our pre-disposition not to change recommendations frequently, these performance parameters should be interpreted flexibly. Performance in this context only reflects capital appreciation and the horizon is 12 months.

Market or sector view: This view is the responsibility of the strategy team and a relative call on the performance of the market/sector relative to the region. Overweight/Underweight implies upside/downside of 10% or more and Neutral implies less than 10% upside/downside.

Target price: The target price is the level the stock should currently trade at if the market were to accept the analyst's view of the stock and if the necessary catalysts were in place to effect this change in perception within the performance horizon. In this way, therefore, the target price abstracts from the need to take a view on the market or sector. If it is felt that the catalysts are not fully in place to effect a re-rating of the stock to its warranted value, the target price will differ from 'fair' value.

Distribution of recommendations

The tables below show the distribution of recommendations (both long term and trading). The first column displays the distribution of recommendations globally and the second column shows the distribution for the region. Numbers in brackets show the percentage for each category where there is an investment banking relationship. These numbers include recommendations produced by third parties with which RBS has joint ventures or strategic alliances.

Long term recommendations (as at 29 Mar 2011)

	Global total (IB%)	Asia Pacific total (IB%)
Buy	787 (13)	510 (3)
Hold	421 (7)	220 (2)
Sell	112 (1)	60 (0)
Total (IB%)	1320 (10)	790 (2)

Source: RBS

Trading recommendations (as at 29 Mar 2011)

	Global total (IB%)	Asia Pacific total (IB%)
Trading Buy	1 (0)	1 (0)
Trading Sell	0 (0)	0 (0)
Total (IB%)	1 (0)	1 (0)

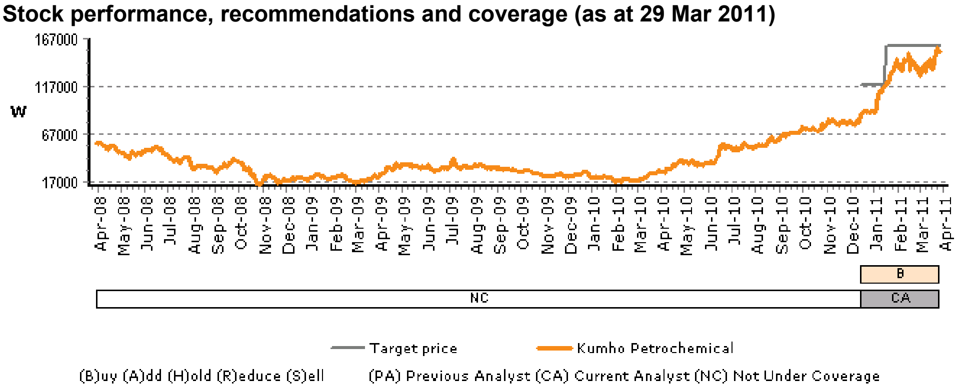
Source: RBS

Valuation and risks to target price

Kumho Petrochemical (RIC: 011780.KS, Rec: Buy, CP: W154000, TP: W192000): We value Kumho on a sum-of-the-parts basis. The downside risks to our target price are a surge in the butadiene price, increasing raw material costs for synthetic rubber and a decreasing self-sufficiency ratio in butadiene due to the renewal of existing contracts with major suppliers. The key upside risk is a strong price spread in synthetic rubbers led by tyre replacement demand in China.

Kumho Petrochemical coverage data

Stock performance, recommendations and coverage (as at 29 Mar 2011)



Angela Choi started covering this stock on 14 Dec 10. Moved to new recommendation structure between 1 November 2005 and 31 January 2006. Source: RBS

Trading recommendation history (as at 29 Mar 2011)

Date	Rec	Analyst
	n/a	

Source: RBS

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