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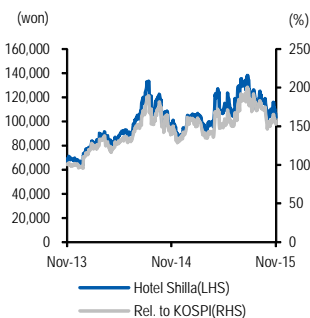
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Retail/leisure
BUY (M)
TP: W153,000 (D)

| | |
|---|------------|
| Share price (won, Nov 13) | 103,000 |
| Paid-in capital (Wbn) | 200 |
| Market cap (Wbn) | 4,094 |
| BPS (won) | 18,822 |
| Net debt to equity (%) | 81.1 |
| Shares outstanding | 40,000,000 |
| Avg daily T/O (2M, Wbn) | 34 |
| Avg daily vol (2M, shrs) | 304,428 |
| 52-week high (won) | 138,000 |
| 52-week low (won) | 85,800 |
| Foreign ownership (%) | 37.4 |
| Major shareholders (%) | |
| Samsung Life Insurance Co.,Ltd & others | 17.5 |

Stock performance (%)

| | 1M | 3M | 12M |
|------------|-------|--------|------|
| Absolute | (2.4) | (18.3) | 10.0 |
| Relative | (0.1) | (17.8) | 9.3 |
| Abs (US\$) | (3.6) | (17.5) | 3.7 |



Source: Datastream

Quarterly earnings

| (Wbn) | 3Q15 | % YoY | % QoQ | Consens | vs consens (%) |
|------------------|------|----------|----------|---------|----------------|
| Sales | 731 | -7.7 | -13.5 | 784 | -6.7 |
| Operating profit | 3 | -95.2 | -90.5 | 23 | -87.6 |
| Pre-tax profit | -7 | TTR | TTR | 18 | -137.0 |
| Net profit | -10 | TTR | TTR | 19 | -151.1 |
| Op margin (%) | 0.4 | -6.9 %pt | -3.1 %pt | 2.9 | -2.5 %pt |
| Net margin (%) | -1.3 | TTR | TTR | 2.5 | -3.8 %pt |

Note: TTB = turn to black, TTR = turn to red, RR = remain in red

Source: Yuanta Securities

Hotel Shilla (008770 KS)

Our take on Seoul, Busan downtown duty-free license awards

Results of Seoul and Busan round two downtown duty-free license review

- The Korea Customs Service announced the round 2 winners of the Seoul and Busan downtown duty-free license review on Saturday. Lotte Sogong and Shinsegae Busan retained their licenses, while SK Walkerhill and Lotte World Tower lost theirs to Shinsegae and Doosan, respectively. This is the first time that existing duty-free operators have had their licenses taken away since the government's introduction of a competitive bidding process. The loss of Lotte's World Tower branch to the duty-free rookie, Doosan, stunned many investors, as this means duty-free retailers now have to fight to retain their business every five years. The new license award system may undermine investor sentiment in the Korean duty-free market unless uncertainties shrouding detailed review items and weightings are addressed.

Go overweight when risk of Customs Act revision is removed in December

- Shilla Duty-Free, the 7th-largest global duty-free retailer, was not a party to the weekend's bidding. However, the results are significant because Lotte's loss means that the renewal of its existing licenses for its Janchung (2019), downtown Jeju (2019), and HDC (2020) stores is not guaranteed. Reflecting this uncertainty, we revise down our target price from W210,000 to W153,000. To calculate our target price, we revised down the perpetual growth of Shilla's duty-free business from 2% to 1% as we now assume the chance of its license renewal at only 50%. Moreover, the operating value of HDC Shilla Duty-Free was revised down based on its estimated earnings for the first year of operations instead of the year its operations normalize.
- Shares are likely to be weak short term on: 1) weakened sentiment on the duty-free market due to Lotte's loss of its World Tower license; 2) the relatively high portion of securities lending at 28% of its outstanding shares; and 3) revisions to the Customs Act. However, we recommend going overweight when the Customs Act revision risk eases in December for two reasons. First, Seoul's downtown duty-free market should grow 41% YoY in 2016 to W6.3tn. Due to a low base from MERS in 2015, the number of Chinese travelers to Korea is expected to grow 46% YoY to 8.81mn visitors, which should help the market digest additional supply and weather the shift in market dynamics. Second, the merits of Shilla's duty-free business—its relative advantage in cost competitiveness and merchandising, solid brand awareness among Chinese visitors, margin improvement thanks to its increasing share of downtown duty-free sales, likely market share growth upon the opening of HDC Shilla Duty-Free, and the strength of its high-margin online business—is still intact. We also expect positive news for the firm in 2016 regarding its overseas downtown duty-free operations.

Forecasts and valuations (K-IFRS, consolidated)

| | (Wbn) | | | |
|------------------|-------|-------|-------|-------|
| FY ends Dec | 2013A | 2014A | 2015E | 2016E |
| Sales | 2,297 | 2,909 | 3,262 | 3,910 |
| Operating profit | 87 | 139 | 97 | 259 |
| Net profit, CI | 11 | 73 | 38 | 192 |
| % YoY | -89.3 | 579.8 | -48.6 | 407.6 |
| P/E (x) | 220.0 | 50.7 | 107.9 | 21.1 |
| P/B (x) | 3.5 | 5.1 | 5.4 | 4.4 |
| EV/EBITDA (x) | 19.8 | 20.6 | 27.3 | 14.0 |
| ROE (%) | 1.6 | 10.4 | 5.1 | 23.0 |

Note: OP = Gross Profit - SG&A

Source: Yuanta Securities

Hotel Shilla (008770 KS) pro forma financial statements (K-IFRS, consolidate)

| Statement of comprehensive income | | | | | |
|-----------------------------------|--------------|--------------|--------------|--------------|--------------|
| FY ends Dec (Wbn) | 2013A | 2014A | 2015E | 2016E | 2017E |
| Sales | 2,297 | 2,909 | 3,262 | 3,910 | 4,214 |
| Cost of sales | 1,327 | 1,613 | 1,855 | 2,227 | 2,383 |
| Gross profit | 970 | 1,296 | 1,407 | 1,683 | 1,831 |
| SG&A | 883 | 1,157 | 1,310 | 1,424 | 1,523 |
| Operating profit | 87 | 139 | 97 | 259 | 308 |
| EBITDA | 138 | 203 | 172 | 329 | 372 |
| Non-op profit/loss | -71 | -25 | -30 | -6 | -3 |
| Forex gain/loss | -1 | -5 | -3 | 0 | 0 |
| Net interest inc | -7 | -10 | -17 | -16 | -7 |
| Equity-meth gain/loss | 0 | 0 | -3 | -5 | -5 |
| Other | -62 | -10 | -7 | 15 | 10 |
| Net prof before income tax | 16 | 114 | 67 | 253 | 305 |
| Income tax | 5 | 40 | 29 | 61 | 74 |
| Net profit from cont op | 11 | 73 | 38 | 192 | 231 |
| Net profit from discont op | 0 | 0 | 0 | 0 | 0 |
| Net profit | 11 | 73 | 38 | 192 | 231 |
| NP for controlling int | 11 | 73 | 38 | 192 | 231 |
| Total comprehensive inc | 1 | 57 | 33 | 180 | 219 |
| TCI for controlling int | 1 | 57 | 33 | 180 | 219 |

Note: Operating profit calculation same as K-GAAP (sales - COGS - SG&A).

| Statement of financial position | | | | | |
|---------------------------------|--------------|--------------|--------------|--------------|--------------|
| FY ends Dec (Wbn) | 2013A | 2014A | 2015E | 2016E | 2017E |
| Current assets | 709 | 823 | 1,061 | 995 | 1,263 |
| Cash & cash equiv | 226 | 187 | 359 | 214 | 429 |
| Accts rec & other | 106 | 117 | 116 | 122 | 127 |
| Inventory | 337 | 494 | 555 | 628 | 677 |
| Non-current assets | 1,003 | 1,084 | 1,182 | 1,186 | 1,156 |
| Tangible assets | 643 | 704 | 725 | 702 | 682 |
| Investment in affiliate | 5 | 6 | 32 | 66 | 61 |
| Other non-current | 331 | 339 | 392 | 392 | 392 |
| Total assets | 1,712 | 1,907 | 2,242 | 2,181 | 2,419 |
| Current liabilities | 433 | 435 | 491 | 264 | 385 |
| Accts payable & other | 235 | 331 | 380 | 403 | 424 |
| ST financial liabilities | 0 | 0 | 0 | 0 | 100 |
| Liquid LT liabilities | 140 | 0 | 0 | 0 | 0 |
| Non-current liabilities | 601 | 742 | 1,002 | 1,002 | 902 |
| LT financial liabilities | 0 | 0 | 0 | 0 | 0 |
| Debentures | 449 | 599 | 848 | 848 | 748 |
| Total liabilities | 1,034 | 1,177 | 1,493 | 1,266 | 1,287 |
| Equity, controlling int | 679 | 730 | 749 | 915 | 1,132 |
| Paid-in capital | 200 | 200 | 200 | 200 | 200 |
| Capital surplus | 197 | 197 | 197 | 197 | 197 |
| Retained earnings | 288 | 344 | 367 | 545 | 762 |
| Equity, non-control int | 0 | 0 | 0 | 0 | 0 |
| Total equity | 679 | 730 | 749 | 915 | 1,132 |
| Net debt | 362 | 411 | 607 | 503 | 288 |
| Total debt | 589 | 599 | 968 | 718 | 718 |

Cash flow statement

| FY ends Dec (Wbn) | 2013A | 2014A | 2015E | 2016E | 2017E |
|-----------------------------------|-------------|-------------|-------------|-------------|------------|
| Operating cash flow | 153 | 122 | 156 | 265 | 323 |
| Net profit | 11 | 73 | 38 | 192 | 231 |
| Depreciation & amort | 42 | 52 | 65 | 63 | 60 |
| Forex gain/loss | 0 | 0 | 0 | 0 | 0 |
| Affiliate invest gain/loss | 0 | 1 | 3 | 5 | 5 |
| Inc(dec) net working cap | 55 | -62 | 25 | -15 | 9 |
| Other | 45 | 57 | 26 | 21 | 18 |
| Investing cash flow | -285 | -141 | -180 | -83 | -43 |
| Investment | -3 | -4 | -82 | -40 | 0 |
| Inc in tangible assets | -218 | -130 | -98 | -40 | -40 |
| Dec in tangible assets | 2 | 2 | 0 | 0 | 0 |
| Other | -66 | -8 | -1 | -3 | -3 |
| Financing cash flow | 85 | -20 | 224 | -264 | -14 |
| Inc(dec) in ST fin liab | 0 | 0 | 249 | 0 | 100 |
| Inc(dec) in LT fin liab | 119 | 9 | 0 | 0 | -100 |
| Inc(dec) in equity | 0 | 0 | 0 | 0 | 0 |
| Cash dividend | -12 | -6 | -14 | -14 | -14 |
| Other | -22 | -24 | -11 | -250 | 0 |
| Other cash flow | 0 | 0 | -27 | -64 | -52 |
| Inc (dec) in cash & eq | -48 | -39 | 173 | -145 | 215 |
| Beginning cash & equiv | 274 | 226 | 187 | 359 | 214 |
| Ending cash & equiv | 226 | 187 | 359 | 214 | 429 |
| NOPLAT | 87 | 139 | 97 | 259 | 308 |
| FCF | -54 | -38 | 57 | 211 | 267 |

Note: EPS, BPS, P/E and P/B are based on controlling interest

For valuation metrics such as P/E, historical figures are based on annual averages, estimates on current price

For ROA or ROE, assets and equity are averages of end-of-year figures for given year and year prior

Data to 2010 based on K-GAAP and from 2011, K-IFRS

Source: Yuanta Securities

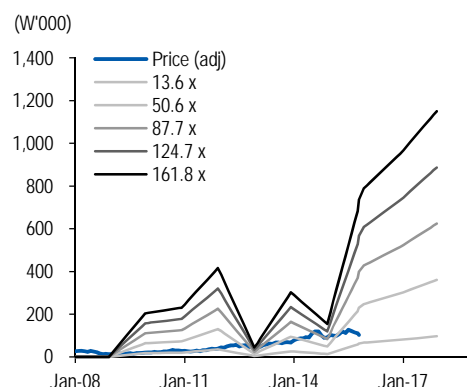
Valuation

| FY ends Dec | 2013A | 2014A | 2015E | 2016E | 2017E |
|----------------------|--------------|-------------|--------------|-------------|-------------|
| EPS (won) | 272 | 1,865 | 954 | 4,876 | 5,879 |
| BPS (won) | 17,243 | 18,549 | 19,031 | 23,244 | 28,763 |
| EBITDA/shr (won) | 3,442 | 5,070 | 4,306 | 8,226 | 9,308 |
| SPS (won) | 57,425 | 72,724 | 81,551 | 97,748 | 105,345 |
| DPS (won) | 150 | 350 | 350 | 350 | 350 |
| P/E (x) | 220.0 | 50.7 | 107.9 | 21.1 | 17.5 |
| P/B (x) | 3.5 | 5.1 | 5.4 | 4.4 | 3.6 |
| EV/EBITDA (x) | 19.8 | 20.6 | 27.3 | 14.0 | 11.8 |
| PSR (x) | 1.0 | 1.3 | 1.3 | 1.1 | 1.0 |

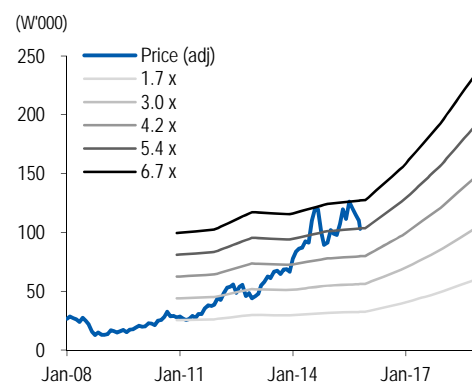
Key financial data

| FY ends Dec | 2013A | 2014A | 2015E | 2016E | 2017E |
|--------------------------------|--------------|--------------|--------------|--------------|-------------|
| Sales (% YoY) | 3.5 | 26.6 | 12.1 | 19.9 | 7.8 |
| Operating profit (%YoY) | -33.0 | 60.5 | -30.3 | 166.9 | 19.0 |
| NP, CI (%YoY) | -89.3 | 579.8 | -48.6 | 407.6 | 20.5 |
| Gross margin (%) | 42.2 | 44.6 | 43.1 | 43.0 | 43.5 |
| Operating margin (%) | 3.8 | 4.8 | 3.0 | 6.6 | 7.3 |
| NP, CI margin (%) | 0.5 | 2.5 | 1.2 | 4.9 | 5.5 |
| EBITDA margin (%) | 6.0 | 7.0 | 5.3 | 8.4 | 8.8 |
| ROIC (%) | 7.4 | 10.0 | 5.8 | 20.1 | 23.5 |
| ROA (%) | 0.7 | 4.1 | 1.8 | 8.7 | 10.0 |
| ROE (%) | 1.6 | 10.4 | 5.1 | 23.0 | 22.6 |
| Debt-to-equity (%) | 152.3 | 161.3 | 199.4 | 138.4 | 113.7 |
| Net debt-to-equity (%) | 53.4 | 56.3 | 81.1 | 55.0 | 25.5 |
| OP/financing cost (x) | 3.2 | 5.3 | 3.1 | 9.6 | 11.4 |

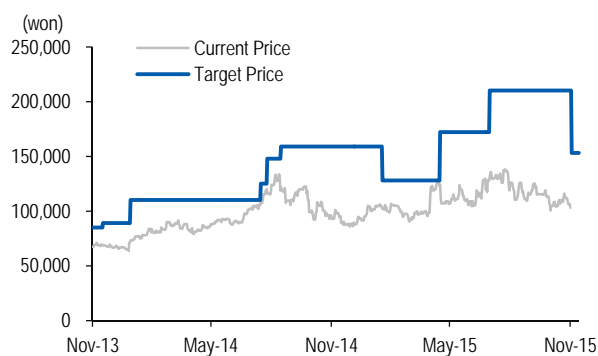
P/E band



P/B band



Hotel Shilla (008770 KS) ratings and target price history



| Date | Rating | TP (won) |
|------------|------------|----------|
| 2015-11-15 | BUY | 153,000 |
| 2015-11-02 | BUY | 210,000 |
| 2015-10-30 | BUY | 210,000 |
| 2015-10-12 | BUY | 210,000 |
| 2015-10-05 | BUY | 210,000 |
| 2015-08-31 | BUY | 210,000 |
| 2015-07-31 | Strong Buy | 210,000 |
| 2015-07-29 | Strong Buy | 210,000 |
| 2015-07-22 | Strong Buy | 210,000 |
| 2015-07-13 | Strong Buy | 210,000 |

Source: Yuanta Securities

Current distribution of Yuanta Securities Korea ratings

| Rating | Share (%) |
|------------|-----------|
| STRONG BUY | 1.2 |
| BUY | 80.2 |
| HOLD | 18.5 |
| SELL | 0.0 |
| Total | 100.0 |

Note: As of Nov 13

※ Excluding reports written or published by overseas affiliates

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- **Stock ratings** include an Investment Rating (Strong Buy, Buy, Hold, Sell) based on the expected absolute return of a stock over the next 6 -12 months.
 - Strong Buy: Expected to return 30% or more
 - Buy: Expected to return between 10% and 30%
 - Hold: Expected to return between -10 and +10%
 - Sell: Expected to return -10% or less
- **Sector ratings** suggest 6 to 12 - month forward investment weighting of a given sector compared to its market capitalization weighting.
 - Overweight: Investment weighting is higher than the market capitalization weighting
 - Neutral: Investment weighting is equal to the market capitalization weighting
 - Underweight: Investment weighting is lower than the market capitalization weighting

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