

# NAVER

(035420 KS)

## Better outlook for 2Q

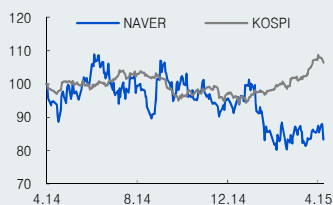
### Internet

Results Comment  
May 4, 2015

|                           |                |
|---------------------------|----------------|
| (Maintain)                | <b>Buy</b>     |
| Target Price (12M, W)     | <b>890,000</b> |
| Share Price (04/30/15, W) | 650,000        |
| Expected Return           | 37%            |

|                            |          |
|----------------------------|----------|
| OP (15F, Wbn)              | 948      |
| Consensus OP (15F, Wbn)    | 971      |
| EPS Growth (15F, %)        | 41.3     |
| Market EPS Growth (15F, %) | 38.2     |
| P/E (15F, x)               | 33.4     |
| Market P/E (15F, x)        | 11.0     |
| KOSPI                      | 2,127.17 |
| Market Cap (Wbn)           | 21,426   |
| Shares Outstanding (mn)    | 33       |
| Free Float (%)             | 78.2     |
| Foreign Ownership (%)      | 54.2     |
| Beta (12M)                 | 0.70     |
| 52-Week Low                | 626,000  |
| 52-Week High               | 849,000  |

| (%)      | 1M   | 6M    | 12M   |
|----------|------|-------|-------|
| Absolute | -4.6 | -13.3 | -11.9 |
| Relative | -8.9 | -20.2 | -18.8 |



Daewoo Securities Co., Ltd.

[Internet/Game/Entertainment]

Chang-kwean Kim  
+822-768-4321  
changkwean.kim@dwsec.com

Jeong-yeob Park  
+822-768-4124  
jay.park@dwsec.com

### 1Q review: Earnings disappoint largely due to stock-based compensation

In 1Q, NAVER reported an 18.3% YoY increase in revenue and a 3.0% YoY rise in operating profit, with the latter disappointing the consensus for the second quarter in a row.

In yen terms, LINE's consolidated revenue expanded 69.5% YoY and 8.7% QoQ to JPY28.1bn. However, won-based revenue remained flat YoY (net revenue of W228.6bn in 1Q15 vs. W221.7bn in 1Q14) due to 1) yen depreciation, and 2) an increase in deferred revenue (W45bn in 4Q14 vs. W56bn in 1Q15). Margins also deteriorated on stock-based compensations of W21.1bn. On a positive note, LINE's monthly active users (MAU) grew at a faster rate, rising 7.9% QoQ to 205mn at end-1Q15 (vs. 6.1% in 4Q14 and 5.3% in 3Q14).

### 2Q preview: Stable expenses, peak-season effects and LINE@ subscriptions

Looking ahead, we expect NAVER to display both top-line growth and margin expansion in 2Q. The company should benefit from 1) a seasonal pickup in domestic ad demand, and 2) the full-fledged sales of new mobile ad and e-commerce offerings. In Japan, LINE is set to begin charging its LINE@ accounts in May (a monthly charge of JPY5,400 per account). The number of LINE@ accounts has increased to 370,000 at end-1Q15. Sticker sales should also grow on the release of audio and animated stickers, which are pricier. Also encouraging is the recent slowdown in the yen's depreciation.

We do not see any significant expense items in 2Q, such as the marketing expenses in 4Q14 and stock options in 1Q15. All in all, we forecast 2Q revenue and operating profit to grow 14.4% and 15.3% YoY to W784.7bn (LINE net revenue of W249.8bn) and W217.9bn, respectively.

### Retain Buy, but Lower TP to W890,000

NAVER enjoys among the highest mobile traffic in Korea, Japan, Taiwan, Thailand and Indonesia. The company is expanding its mobile monetization models through its "power link" search ads in Korea, and stickers and official account ads in Japan.

We expect strong revenue growth from new domestic mobile ad and e-commerce offerings in 2Q. The upcoming launch of Naver Pay in June should further complement the company's new monetization models. In Japan, we look for visible results from new profit models such as LINE Pay and LINE Taxi.

We remain Buy on NAVER, but lower our target price to W890,000 (from W1,050,000), as we revised down our 2015-16F EPS by 13.8% and 4.9%, respectively, reflecting several variables revealed in the 1Q results (stock option expenses, higher tax rates, etc.).

| FY (Dec.)     | 12/12  | 12/13  | 12/14  | 12/15F | 12/16F | 12/17F |
|---------------|--------|--------|--------|--------|--------|--------|
| Revenue (Wbn) | 1,799  | 2,312  | 2,758  | 3,210  | 3,575  | 3,889  |
| OP (Wbn)      | 521    | 524    | 758    | 948    | 1,223  | 1,387  |
| OP margin (%) | 29.0   | 22.7   | 27.5   | 29.5   | 34.2   | 35.7   |
| NP (Wbn)      | 546    | 1,897  | 454    | 642    | 867    | 963    |
| EPS (W)       | 11,346 | 45,425 | 13,787 | 19,479 | 26,306 | 29,216 |
| ROE (%)       | 31.4   | 112.7  | 27.8   | 30.5   | 30.6   | 25.9   |
| P/E (x)       | 19.9   | 15.9   | 51.6   | 33.4   | 24.7   | 22.2   |
| P/B (x)       | 3.8    | 11.3   | 8.7    | 6.5    | 5.2    | 4.2    |

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

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Table 1. 1Q15P earnings results

(Wbn, %, %p)

|                  | 1Q14 | 4Q14 | 1Q15P       |            |           | Growth |      |
|------------------|------|------|-------------|------------|-----------|--------|------|
|                  |      |      | Preliminary | KDB Daewoo | Consensus | YoY    | QoQ  |
| Revenue          | 626  | 747  | 741         | 766        | 756       | 18.3   | -0.8 |
| Operating profit | 186  | 194  | 192         | 215        | 215       | 3.0    | -1.0 |
| OP margin        | 29.7 | 26.0 | 25.9        | 28.1       | 28.4      | -3.8   | 0.0  |
| Pretax profit    | 186  | 198  | 223         | 220        | 217       | 20.2   | 12.7 |
| Net profit       | 129  | 131  | 135         | 158        | 156       | 4.4    | 3.4  |

Source: WISEfn, KDB Daewoo Securities Research estimates

Table 2. Quarterly and annual earnings

(Wbn, %)

|                          | 1Q14  | 2Q14  | 3Q14  | 4Q14  | 1Q15P | 2Q15F | 3Q15F | 4Q15F | 2013  | 2014P | 2015F |
|--------------------------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|-------|
| Revenue                  | 626   | 686   | 700   | 747   | 741   | 785   | 794   | 891   | 2,287 | 2,759 | 3,210 |
| - Advertisements         | 477   | 504   | 498   | 540   | 530   | 545   | 548   | 634   | 1,742 | 2,019 | 2,256 |
| - Content                | 131   | 168   | 191   | 196   | 200   | 227   | 232   | 243   | 431   | 687   | 902   |
| - Other                  | 17    | 13    | 11    | 11    | 11    | 13    | 14    | 15    | 114   | 53    | 52    |
| LINE                     |       |       |       |       |       |       |       |       |       |       |       |
| - LINE (gross)           | 229   | 286   | 328   | 384   | 369   | 403   | 424   | 456   | 578   | 1,227 | 1,652 |
| - LINE (net)             | 145   | 183   | 209   | 222   | 229   | 250   | 263   | 282   | 454   | 759   | 1,023 |
| <b>Revenue breakdown</b> |       |       |       |       |       |       |       |       |       |       |       |
| Advertisements           | 76.2  | 73.5  | 71.1  | 72.3  | 71.6  | 69.4  | 69.0  | 71.1  | 76.2  | 73.2  | 70.3  |
| Content                  | 21.0  | 24.5  | 27.3  | 26.2  | 27.0  | 29.0  | 29.2  | 27.2  | 18.8  | 24.9  | 28.1  |
| Other                    | 2.8   | 1.9   | 1.6   | 1.4   | 1.4   | 1.6   | 1.7   | 1.7   | 5.0   | 1.9   | 1.6   |
| LINE                     |       |       |       |       |       |       |       |       |       |       |       |
| - LINE (gross)           | 36.6  | 41.7  | 46.9  | 51.4  | 49.8  | 51.4  | 53.4  | 51.1  | 25.3  | 44.5  | 51.5  |
| - LINE (net)             | 23.2  | 26.7  | 29.8  | 29.7  | 30.9  | 31.8  | 33.1  | 31.7  | 19.9  | 27.5  | 31.9  |
| Operating expenses       | 439   | 497   | 511   | 553   | 549   | 567   | 558   | 589   | 1,772 | 2,000 | 2,263 |
| Operating profit         | 186   | 189   | 189   | 194   | 192   | 218   | 236   | 302   | 515   | 758   | 948   |
| OP margin (%)            | 29.8  | 27.6  | 27.0  | 26.0  | 25.9  | 27.8  | 29.7  | 33.9  | 22.5  | 27.5  | 29.5  |
| Non-operating profit     | 15    | 13    | 28    | 40    | 48    | 34    | 34    | 34    | 87    | 96    | 151   |
| Non-operating expenses   | 15    | 135   | 9     | 36    | 17    | 20    | 15    | 17    | 154   | 196   | 69    |
| Taxes                    | 59    | 46    | 64    | 68    | 89    | 94    | 101   | 127   | 127   | 237   | 411   |
| Net profit               | 129   | 39    | 154   | 130   | 135   | 148   | 159   | 197   | 1,895 | 452   | 638   |
| Net margin (%)           | 20.6  | 5.7   | 22.0  | 17.4  | 18.2  | 18.8  | 20.0  | 22.1  | 82.9  | 16.4  | 19.9  |
| <b>YoY growth</b>        |       |       |       |       |       |       |       |       |       |       |       |
| Revenue                  | 21.5  | 20.1  | 22.3  | 18.8  | 18.3  | 14.4  | 13.4  | 19.4  | 22.6  | 20.6  | 16.4  |
| - Advertisements         | 15.5  | 18.2  | 16.5  | 13.6  | 11.1  | 8.0   | 10.1  | 17.3  | 44.1  | 15.9  | 11.8  |
| - Content                | 92.8  | 48.3  | 62.8  | 48.8  | 52.1  | 35.0  | 21.4  | 23.8  | 22.9  | 59.4  | 31.3  |
| - Other                  | -48.7 | -56.0 | -60.1 | -50.8 | -39.2 | -4.9  | 23.1  | 41.5  | 93.1  | -53.8 | -0.9  |
| LINE                     |       |       |       |       |       |       |       |       |       |       |       |
| - LINE (gross)           | 240.2 | 144.2 | 82.4  | 80.0  | 61.1  | 40.8  | 29.3  | 18.8  | 880.4 | 112.4 | 34.6  |
| - LINE (net)             | 115.6 | 56.2  | 57.2  | 61.9  | 57.4  | 36.3  | 26.0  | 27.3  | 670.9 | 67.0  | 34.9  |
| Operating expenses       | 13.0  | 14.8  | 8.3   | 15.6  | 24.8  | 14.1  | 9.2   | 6.6   | 31.5  | 12.9  | 13.1  |
| Operating profit         | 47.7  | 36.9  | 87.9  | 28.7  | 3.0   | 15.3  | 24.8  | 55.9  | -0.5  | 47.1  | 25.0  |
| Net profit               | -17.9 | -68.0 | -90.2 | 139.7 | 4.3   | 275.4 | 3.2   | 52.1  | 368.6 | -76.2 | 41.3  |

Notes: All figures are based on consolidated K-IFRS; Net profit is attributable to controlling interests

Source: Company data, KDB Daewoo Securities Research estimates

Table 3. Earnings forecast revisions

(Wbn, W, %, %p)

|                  | Previous |        | Revised |        | Change |       |
|------------------|----------|--------|---------|--------|--------|-------|
|                  | 2015F    | 2016F  | 2015F   | 2016F  | 2015F  | 2016F |
| Revenue          | 3,321    | 3,794  | 3,210   | 3,575  | -3.3   | -5.8  |
| Operating profit | 1,046    | 1,292  | 948     | 1,223  | -9.4   | -5.3  |
| Pretax profit    | 1,016    | 1,242  | 927     | 1,214  | -8.8   | -2.3  |
| Net profit       | 744      | 910    | 638     | 862    | -14.2  | -5.3  |
| EPS              | 22,587   | 27,648 | 19,479  | 26,306 | -13.8  | -4.9  |
| OP margin        | 31.5     | 34.1   | 29.5    | 34.2   | -2.0   | 0.2   |
| NP margin        | 22.4     | 24.0   | 19.9    | 24.1   | -2.5   | 0.1   |

Notes: All figures are based on consolidated K-IFRS

Source: Company data, KDB Daewoo Securities Research estimates

## NAVER (035420 KS/Buy/TP: W890,000)

## Comprehensive Income Statement (Summarized)

| (Wbn)                               | 12/14        | 12/15F       | 12/16F       | 12/17F       |
|-------------------------------------|--------------|--------------|--------------|--------------|
| <b>Revenue</b>                      | <b>2,758</b> | <b>3,210</b> | <b>3,575</b> | <b>3,889</b> |
| <b>Cost of Sales</b>                | <b>0</b>     | <b>0</b>     | <b>0</b>     | <b>0</b>     |
| <b>Gross Profit</b>                 | <b>2,758</b> | <b>3,210</b> | <b>3,575</b> | <b>3,889</b> |
| <b>SG&amp;A Expenses</b>            | <b>2,000</b> | <b>2,263</b> | <b>2,352</b> | <b>2,502</b> |
| <b>Operating Profit (Adj)</b>       | <b>758</b>   | <b>948</b>   | <b>1,223</b> | <b>1,387</b> |
| <b>Operating Profit</b>             | <b>758</b>   | <b>948</b>   | <b>1,223</b> | <b>1,387</b> |
| <b>Non-Operating Profit</b>         | <b>-99</b>   | <b>-21</b>   | <b>-9</b>    | <b>11</b>    |
| Net Financial Income                | 17           | 28           | 44           | 63           |
| Net Gain from Inv in Associates     | -1           | 0            | 0            | 0            |
| Pretax Profit                       | 659          | 927          | 1,214        | 1,398        |
| Income Tax                          | 237          | 289          | 352          | 441          |
| Profit from Continuing Operations   | 422          | 638          | 862          | 957          |
| Profit from Discontinued Operations | 30           | 0            | 0            | 0            |
| <b>Net Profit</b>                   | <b>452</b>   | <b>638</b>   | <b>862</b>   | <b>957</b>   |
| Controlling Interests               | 454          | 642          | 867          | 963          |
| Non-Controlling Interests           | -3           | -4           | -5           | -6           |
| <b>Total Comprehensive Profit</b>   | <b>563</b>   | <b>638</b>   | <b>862</b>   | <b>957</b>   |
| Controlling Interests               | 565          | 641          | 866          | 962          |
| Non-Controlling Interests           | -3           | -3           | -4           | -5           |
| EBITDA                              | 902          | 1,068        | 1,324        | 1,471        |
| FCF (Free Cash Flow)                | 508          | 914          | 1,091        | 1,157        |
| EBITDA Margin (%)                   | 32.7         | 33.3         | 37.0         | 37.8         |
| Operating Profit Margin (%)         | 27.5         | 29.5         | 34.2         | 35.7         |
| Net Profit Margin (%)               | 16.5         | 20.0         | 24.3         | 24.8         |

## Statement of Financial Condition (Summarized)

| (Wbn)                            | 12/14        | 12/15F       | 12/16F       | 12/17F       |
|----------------------------------|--------------|--------------|--------------|--------------|
| <b>Current Assets</b>            | <b>1,946</b> | <b>2,821</b> | <b>3,870</b> | <b>4,977</b> |
| Cash and Cash Equivalents        | 723          | 1,405        | 2,293        | 3,261        |
| AR & Other Receivables           | 414          | 475          | 529          | 575          |
| Inventories                      | 17           | 19           | 21           | 23           |
| Other Current Assets             | 792          | 922          | 1,027        | 1,118        |
| <b>Non-Current Assets</b>        | <b>1,449</b> | <b>1,371</b> | <b>1,305</b> | <b>1,251</b> |
| Investments in Associates        | 36           | 42           | 47           | 51           |
| Property, Plant and Equipment    | 901          | 791          | 700          | 623          |
| Intangible Assets                | 121          | 110          | 101          | 93           |
| <b>Total Assets</b>              | <b>3,394</b> | <b>4,192</b> | <b>5,176</b> | <b>6,227</b> |
| <b>Current Liabilities</b>       | <b>1,081</b> | <b>1,218</b> | <b>1,333</b> | <b>1,432</b> |
| AP & Other Payables              | 315          | 366          | 408          | 444          |
| Short-Term Financial Liabilities | 213          | 209          | 209          | 209          |
| Other Current Liabilities        | 553          | 643          | 716          | 779          |
| <b>Non-Current Liabilities</b>   | <b>516</b>   | <b>561</b>   | <b>597</b>   | <b>628</b>   |
| Long-Term Financial Liabilities  | 243          | 243          | 243          | 243          |
| Other Non-Current Liabilities    | 273          | 318          | 354          | 385          |
| <b>Total Liabilities</b>         | <b>1,597</b> | <b>1,779</b> | <b>1,930</b> | <b>2,060</b> |
| <b>Controlling Interests</b>     | <b>1,796</b> | <b>2,415</b> | <b>3,253</b> | <b>4,180</b> |
| Capital Stock                    | 16           | 16           | 16           | 16           |
| Capital Surplus                  | 133          | 133          | 133          | 133          |
| Retained Earnings                | 2,584        | 3,203        | 4,040        | 4,968        |
| <b>Non-Controlling Interests</b> | <b>1</b>     | <b>-2</b>    | <b>-8</b>    | <b>-13</b>   |
| <b>Stockholders' Equity</b>      | <b>1,797</b> | <b>2,413</b> | <b>3,245</b> | <b>4,167</b> |

## Cash Flows (Summarized)

| (Wbn)                          | 12/14       | 12/15F       | 12/16F       | 12/17F       |
|--------------------------------|-------------|--------------|--------------|--------------|
| Cash Flows from Op Activities  | 779         | 914          | 1,091        | 1,157        |
| Net Profit                     | 452         | 638          | 862          | 957          |
| Non-Cash Income and Expense    | 503         | 412          | 440          | 493          |
| Depreciation                   | 132         | 110          | 92           | 76           |
| Amortization                   | 12          | 11           | 9            | 8            |
| Others                         | 359         | 291          | 339          | 409          |
| Chg in Working Capital         | 35          | 116          | 88           | 76           |
| Chg in AR & Other Receivables  | -107        | -51          | -41          | -36          |
| Chg in Inventories             | -17         | -3           | -2           | -2           |
| Chg in AP & Other Payables     | 206         | 0            | 0            | 0            |
| <b>Income Tax Paid</b>         | <b>-234</b> | <b>-289</b>  | <b>-352</b>  | <b>-441</b>  |
| Cash Flows from Inv Activities | -379        | -159         | -128         | -110         |
| Chg in PP&E                    | -260        | 0            | 0            | 0            |
| Chg in Intangible Assets       | -6          | 0            | 0            | 0            |
| Chg in Financial Assets        | -178        | -159         | -128         | -110         |
| <b>Others</b>                  | <b>65</b>   | <b>0</b>     | <b>0</b>     | <b>0</b>     |
| Cash Flows from Fin Activities | -112        | -28          | -29          | -35          |
| Chg in Financial Liabilities   | 104         | -5           | 0            | 0            |
| Chg in Equity                  | 0           | 0            | 0            | 0            |
| Dividends Paid                 | -22         | -23          | -29          | -35          |
| <b>Others</b>                  | <b>-194</b> | <b>0</b>     | <b>0</b>     | <b>0</b>     |
| Increase (Decrease) in Cash    | 287         | 682          | 889          | 968          |
| Beginning Balance              | 435         | 723          | 1,405        | 2,293        |
| <b>Ending Balance</b>          | <b>723</b>  | <b>1,405</b> | <b>2,293</b> | <b>3,261</b> |

Source: Company data, KDB Daewoo Securities Research estimates

## Forecasts/Valuations (Summarized)

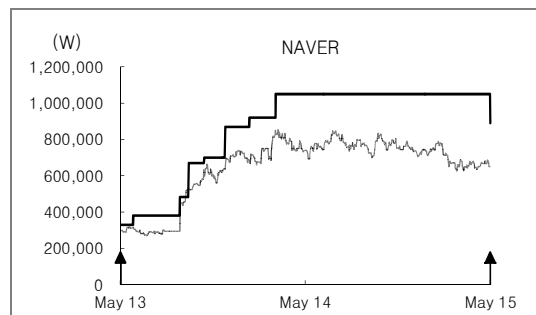
|                                  | 12/14  | 12/15F  | 12/16F  | 12/17F  |
|----------------------------------|--------|---------|---------|---------|
| P/E (x)                          | 51.6   | 33.4    | 24.7    | 22.2    |
| P/CF (x)                         | 24.6   | 20.4    | 16.5    | 14.8    |
| P/B (x)                          | 8.7    | 6.5     | 5.2     | 4.2     |
| EV/EBITDA (x)                    | 24.9   | 18.4    | 14.1    | 11.9    |
| EPS (W)                          | 13,787 | 19,479  | 26,306  | 29,216  |
| CFPS (W)                         | 28,959 | 31,876  | 39,489  | 44,000  |
| BPS (W)                          | 81,551 | 100,331 | 125,743 | 153,886 |
| DPS (W)                          | 782    | 1,000   | 1,200   | 1,400   |
| Payout ratio (%)                 | 5.1    | 4.6     | 4.1     | 4.3     |
| Dividend Yield (%)               | 0.1    | 0.2     | 0.2     | 0.2     |
| Revenue Growth (%)               | 19.3   | 16.4    | 11.4    | 8.8     |
| EBITDA Growth (%)                | 37.5   | 18.4    | 24.0    | 11.1    |
| Operating Profit Growth (%)      | 44.7   | 25.1    | 29.0    | 13.4    |
| EPS Growth (%)                   | -69.6  | 41.3    | 35.0    | 11.1    |
| Accounts Receivable Turnover (x) | 10.1   | 9.5     | 9.3     | 9.2     |
| Inventory Turnover (x)           |        |         |         |         |
| Accounts Payable Turnover (x)    | 0.0    | 0.0     | 0.0     | 0.0     |
| ROA (%)                          | 14.8   | 16.8    | 18.4    | 16.8    |
| ROE (%)                          | 27.8   | 30.5    | 30.6    | 25.9    |
| ROIC (%)                         | 68.3   | 110.8   | 208.0   | 342.8   |
| Liability to Equity Ratio (%)    | 88.9   | 73.8    | 59.5    | 49.4    |
| Current Ratio (%)                | 180.0  | 231.5   | 290.4   | 347.6   |
| Net Debt to Equity Ratio (%)     |        |         |         |         |
| Interest Coverage Ratio (x)      |        |         |         |         |

## APPENDIX 1

### Important Disclosures & Disclaimers

#### 2-Year Rating and Target Price History

| Company (Code) | Date       | Rating | Target Price |
|----------------|------------|--------|--------------|
| NAVER(035420)  | 05/03/2015 | Buy    | 890,000      |
|                | 03/06/2014 | Buy    | 1,050,000    |
|                | 01/13/2014 | Buy    | 920,000      |
|                | 11/26/2013 | Buy    | 870,000      |
|                | 10/16/2013 | Buy    | 700,000      |
|                | 09/15/2013 | Buy    | 670,000      |
|                | 08/29/2013 | Buy    | 483,000      |
|                | 05/29/2013 | Buy    | 382,000      |
|                | 03/11/2013 | Buy    | 330,000      |



#### Stock Ratings

|             |   |
|-------------|---|
| Buy         | : Relative performance of 20% or greater                      |
| Trading Buy | : Relative performance of 10% or greater, but with volatility |
| Hold        | : Relative performance of -10% and 10%                        |
| Sell        | : Relative performance of -10%                                |

#### Industry Ratings

|             |  |
|-------------|--|
| Overweight  | : Fundamentals are favorable or improving              |
| Neutral     | : Fundamentals are steady without any material changes |
| Underweight | : Fundamentals are unfavorable or worsening            |

Ratings and Target Price History (Share price (—), Target price (—), Not covered (■), Buy (▲), Trading Buy (■), Hold (●), Sell (◆))

\* Our investment rating is a guide to the relative return of the stock versus the market over the next 12 months.

\* Although it is not part of the official ratings at Daewoo Securities, we may call a trading opportunity in case there is a technical or short-term material development.

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