

HEERIM (037440, KQ)

'Real' Inter-Korean Economic Cooperation Stock Appeared

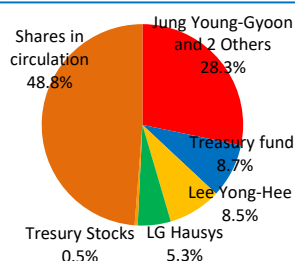
Business Issues

On September 12, the company announced that it has signed a MOU with China's largest Korean-Chinese owned company, 'XinXing Industry Company' for joint advancement into business in North Korea. XinXing Industry is a comprehensive investment group with an annual turnover of W4tr in real estate development and construction materials, mainly in Liaoning Province, China. In addition, XinXing Industry is currently engaged in various businesses including duty free shops, textile factories, shopping malls, and retail businesses in North Korea. The company plans to take charge of a variety of projects in North Korea, such as architectural design and construction management (CM), which will be carried out with XinXing Industry in the future.

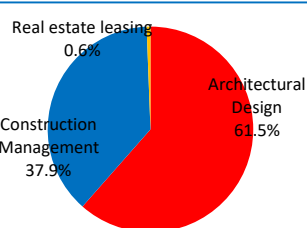
Keynote for Investment

- ① Establish a base for advancement into the North Korean market through business agreements with XinXing Industry, and the company will participate in businesses such as hotels, duty free shops, casinos and airports in the future.
- ② After the third inter-Korean summit, economic cooperation between the two Koreas is expected to take off in earnest. In particular, the resumption of operations at the Kaesong Industrial Complex is to be noted as one of President Moon Jae-In's pledges.
- ③ The company acquired references in charge of designing major buildings such as factories, comprehensive support centers, and the inter-Korean economic cooperation consultation office building in the Kaesong Industrial Complex.
- ④ Highly probable winner of large-scale design projects such as Vietnam's Long Thanh International Airport (W25bn) and Uzbekistan's Tashkent International Airport (W13bn) in 2H18.
- ⑤ 'Urban Renewal New Deal Project' to invest W10tr annually for the next five years is imminent, the company will benefit as #1 domestic construction design company.
- ⑥ For the calculation of the fair value, we applied average PER multiple of 15x for domestic and overseas architectural design and CM-related companies (AECOM, HANMI GLOBAL, etc.) to 2019E EPS of KRW 577.

Shareholders



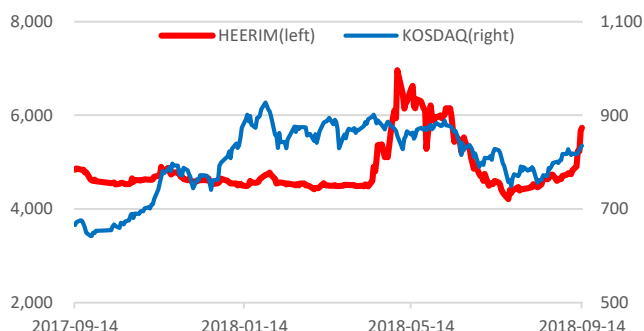
Sales composition (2018E)



Market Cap (W bn)	Forecast	Fair Value (KRW)	Share Price (KRW)	Upside (%)
79.8	Positive	8,650	5,730	51.0 ↑

HEERIM & KOSDAQ Closing Price

(Unit : KRW, pt)



Investor trading status

(Unit : share)

Date	Foreign	Individual	Institutional	Date	Contents
09/14	2,714	-1,509	-	08/14	Semi Annual Report
09/13	-12,418	2,527	2,152		1H18 Performance Disclosure
09/12	-1,907	-17,251	20,000	07/02	[Updated] Supply contract
09/11	-43,795	46,834	-4,102		Change the contract date
09/10	112	816	-	05/15	Quarterly Report
09/07	2,684	-2,756	102		1Q18 Performance Disclosure

Recent announcement

Operating results and major financial data

(Unit : W bn, W, x, %)

Category	2016	2017	2018E	YoY	2019E	2020E	1Q17	2Q17	3Q17	4Q17	1Q18	2Q18	3Q18E	4Q18E
Revenue	139.8	159.5	179.4	12.5%	204.5	217.3	35.2	39.0	41.0	44.2	37.2	45.1	47.8	49.4
Architectural design	89.6	92.8	110.4	18.9%	128.4	137.1	20.0	20.1	22.9	29.7	21.1	26.4	30.1	32.8
Construction management	49.0	65.7	68.0	3.5%	75.0	79.0	15.0	18.6	17.8	14.3	15.9	18.4	17.4	16.3
Real estate leasing	1.2	0.9	1.0	5.5%	1.1	1.2	0.2	0.3	0.3	0.2	0.3	0.3	0.3	0.3
Operating profit	5.4	8.7	9.0	4.1%	12.2	13.5	1.9	1.3	1.8	3.7	1.0	1.7	2.6	3.8
OP margin	3.9%	5.4%	5.0%	-	6.0%	6.2%	5.4%	3.3%	4.4%	8.3%	2.7%	3.7%	5.4%	7.7%
Net income	2.1	3.7	5.7	55.2%	8.0	9.3	0.2	1.0	0.9	1.6	0.4	1.5	1.8	2.0
PER	33.5	17.5	13.9	-	9.9	11.1	-	-	-	-	-	-	-	-
EPS	154	266	413	-	577	517	-	-	-	-	-	-	-	-

Signed MOU with XinXing Group, A North Korean Business Operator, Expected Market Preemptive Effect in Expanding Inter-Korean Economic Cooperation

Attention to The Results of The 3rd Inter-Korean Summit, Reaching The Peak of Interest in Inter-Korean Economic Cooperation Stock

Once again, the eyes of the world are focused on the Korean peninsula. The third inter-Korean summit will be held in Pyongyang for two nights and three days from 18-20. The third inter-Korean summit is expected to be a full-scale practical talks on economic cooperation after the summit, as a bridgehead going toward a declaration of cease-fire and a peace treaty. We believe that the closer we are to the period of inter-Korean economic cooperation, the greater the selection of 'real' inter-Korean economic cooperation stocks.

Through the declaration of Panmunjom on April 27, the South Korea and North Korea promised economic cooperation for balanced development and common prosperity on the Korean Peninsula. The establishment of the South Korea-North Korea Joint Liaison Office in Kaesong Industrial Complex, which was one of the follow-up measures to the Panmunjom Declaration, was completed on September 14 and led to economic cooperation. When the third inter-Korean summit is successfully concluded, it is anticipated that the inter-Korean exchanges, which had been suspended, will be expanded in earnest through the restoration of the aging transportation and rail infrastructure in North Korea, the restart of the Kaesong Industrial Complex, and the opening of Mt. Baektu and Mt. Geumgang.

A Symbol of Inter-Korean Economic Cooperation, Expected to Restart at Kaesong Industrial Complex

The restart of the Kaesong Industrial Complex was President Moon Jae-in's pledge. President Moon said he would expand the Kaesong Industrial Complex to 6,612ha(hectare) as planned in the participatory government period when the government was replaced. Initially, the Kaesong Industrial Development Project was divided into three stages, and it was aimed to be constructed with a total area of 6,612ha including 1,983ha of industrial complex and 331ha of living area. Currently, it has completed the development of the first stage goal of 331ha for industrial complex. Considering that more than W1tr of funds were invested to build the industrial complex, it will cost more than W9tr to develop the industrial ~ tourism complex of 2,975ha.

As the company has a reference in charge of designing major buildings such as factories, comprehensive support centers, and the Inter-Korea Economic Cooperation Consultation Office building in the Kaesong Industrial Complex, it is expected to secure orders in the additional development project of the Kaesong Industrial Complex. Design and supervision costs are usually set at around 10% of the total project cost, which should lead to large-scale top-line growth when the company wins the orders. Also, opening the special tourism zones in North Korea is expected to increase the opportunities for the company to participate in new construction such as hotels, duty free shops, casinos and airports.

Signed MOU with XinXing Group, China's Largest Korean-Chinese Owned Company, to Jointly Enter North Korea Business

The company has recently signed an MOU with Shenyang XinXing Industry Company, China's largest Korean-Chinese owned company, to jointly advance into the North Korean business. XinXing Industry Company, a MOU partner, is a comprehensive investment group with an annual turnover of W4tr, which is engaged in real estate development, construction materials and steel distribution business centering on Liaoning Province, China. It has a friendly relationship with North Korea so that it participated in large-scale events such as the 65th anniversary of the founding of the North Korean Workers' Party in 2010, the funeral of Kim Jong Il, and the 100th anniversary of President Kim Il Sung's birthday. XinXing Industry is currently carrying out various businesses such as duty free shops, textile factories, shopping malls, and retail businesses in North Korea. It is anticipated to have a preemptive effect when entering the North Korean market. The company will be responsible for the architectural design and construction business management (CM) in various projects in North Korea that are to be carried out with XinXing Group.

[Figure 1] XinXing Group's Main Business Area



Sources : ResearchARUM

[Figure 2] Kaesong Industrial Complex Development Plan

(Unit : ha)

Category	Step 1	Step 2	Step 3	Total
Industrial area	331	496	1,157	1,983
Living area		99	231	331
Business area		66	99	165
Tourist area		165	331	496
Others				
Existing city		1,322		1,322
Areas to expand in the future		2,314		2,314
Total				6,612

Sources : HDASAN, ResearchARUM

Expected to Secure Large-Scale Domestic and Overseas Orders in 2H18,
Expected to Reevaluate with Entry into Structural Growth Period

Growing Profitable Overseas Sales Portion, Earnings to Improve Sharply in 2H18

In 1H18, the company's sales and operating profit came in at W82.3bn (+10.8%, YoY) and W2.6bn (-17.3% YoY). In the profitability section, it missed our expectation, which is attributable to a special bonus of W1bn in 1Q18. We present revised earnings estimates based on this assumption.

Based on IFRS, we revise up 2018 sales and operating profit to W179.4bn (+12.5%, YoY) and W9.0bn (+4.1%, YoY), respectively. Sales remained at our previous estimates, and operating profit fell to W1bn considering 1H18 earnings. Although earnings were sluggish in 1H18, the company's earnings are expected to improve significantly in 2H18. As the company's overseas sales portion is expanding, the KRW/USD rate has shown a strong upward trend since June. Therefore, the high growth is expected.. Overseas sales accounted for only 6% of sales in 2016, but grew to 10% last year. It increased to 12% in the first half of this year and it is forecast to expand to 15% annually by the effect of the KRW/USD exchange rate rise. The average KRW/USD exchange rate in August this year was KRW 1,121.15, 5.1% higher than January's average KRW 1,063.50.

Highly Probable Winning of Major Projects such as Overseas Airports in 2H18

It is also positive that the company's new orders volume is sharply increasing every year. Beginning from W181bn in 2015 when new orders expanded, , the company's annual order receipts amounted to W210.3bn in 2016. Last year, the company recorded W237.4bn, growing at an annual average rate of more than 15%. New orders for the first half of this year amounted to W138.7bn, up 13.4% YoY. In 2H18, it is highly probable for the company to win orders for large projects such as Vietnam's Long Thanh International Airport(W25.0bn) and Uzbekistan's Tashkent Airport(W13.0bn), which will lead into an additional growth.

Domestic Public Order Expansion Expected Through Full Implementation of 'Urban Renewal New Deal Project'

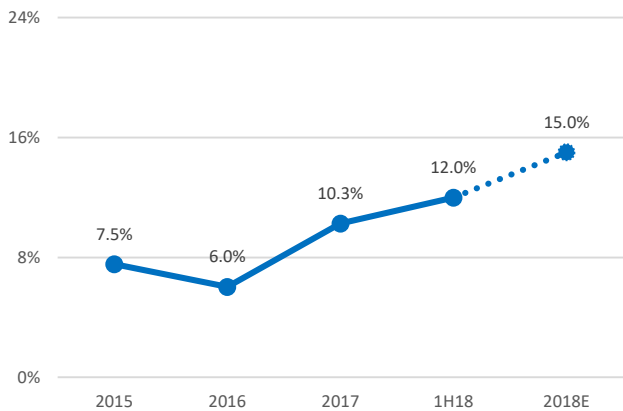
The fact that 'Urban Renewal New Deal Project', which has a total budget of W50tr, will be implemented in earnest this year will also serve as an investment momentum for the company. The 'Urban Regeneration New Deal Project' is an economic stimulus package of the government that develops around 500 old residential areas around the country and will invest W10tr a year for the next five years. On August 31, the government voted '2018 Urban Renewal New Deal Project' and selected 99 cities nationwide as business sites. This year, an administrative fee of W7.9tr has been set, including government and private investment.

As the 'Urban Renewal New Deal Project' is in full swing, we believe that order for design services located at the front of the construction project is imminent. The company is expected to gain a competitive edge in future orders based on industry-leading references such as the rebuilding business of the Emma apartment complex, the complex development project of the old government complex, and the Smart City master plan services.

'Positive' Outlook For Stock Price Raise a Fair Value to KRW 8,650

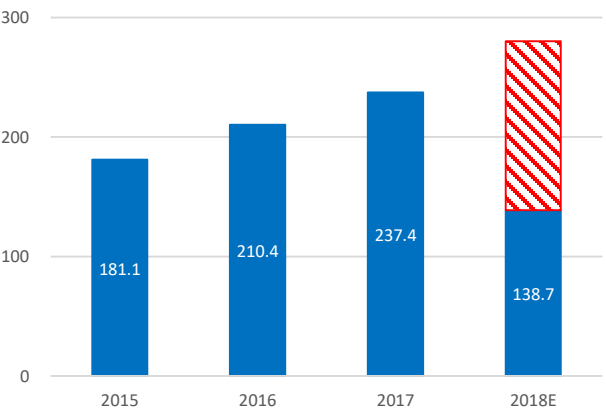
We raise a fair value to KRW 8,650 with a 'positive' share price outlook for the company. We applied average PER of 15x for domestic and overseas architectural design and CM-related companies (AECOM, HANMI GLOBAL, etc.) to 2019E EPS of KRW 577. We believe that the PER 15x is reasonable as there are many positive factors such as the expansion of the Kaesong Industrial Complex project, participation in construction projects in North Korea through MOU with XinXing Group, increase of profitable overseas sales portion, and expanding domestic business opportunities boosted by the implementation of urban renewal new deal project.

[Figure 3] Annual Overseas Sales Weight (Unit : %)



Sources : Heerim, ResearchARUM

[Figure 4] Annual New Orders Volume Trend (Unit : W bn)



Sources : Heerim, ResearchARUM

(Based on 1H18)

HEERIM estimated financial statements

(Unit : W bn)

Income Statement					
	2016A	2017A	2018F	2019F	2020F
Sales	139.8	159.5	179.4	204.5	217.3
Cost of Sales	119.4	131.3	148.1	167.5	177.5
Rate of sales cost(%)	85.5	82.3	82.6	81.9	81.7
Gross Profit	20.3	28.2	31.3	37.0	39.8
Gross Profit Margin(%)	14.5	17.7	17.5	18.1	18.3
SG&A	14.9	19.5	22.3	24.8	26.3
Operating Income	5.4	8.7	9.0	12.2	13.5
Operating Income Margin(%)	3.9	5.4	5.0	6.0	6.2
EBITDA	6.5	10.4	11.3	14.0	15.3
EBITDA Margin(%)	4.7	6.5	6.3	6.8	7.0
Non-Operating Profit	-2.4	-3.9	-1.7	-1.9	-1.5
Gains(Losses) in Associates, Subsidiaries and JVs	-0.1	0.0	0.0	0.0	0.0
Financial Income	1.0	0.7	1.7	1.1	1.0
Financial Costs	3.1	4.4	2.9	2.8	2.1
Others	-0.3	-0.3	-0.5	-0.2	-0.4
Pre-Tax Income	3.0	4.7	7.4	10.3	12.0
Pre-Tax Income Margin(%)	2.2	3.0	4.1	5.0	5.5
Income Tax Expenses	0.9	1.0	1.6	2.3	2.7
Tax Rate(%)	29.2	21.9	22.1	22.1	22.1
Income from Continuing Operations	2.1	3.7	5.7	8.0	9.3
Income from Discontinued Operations	0.0	0.0	0.0	0.0	0.0
Net Income	2.1	3.7	5.7	8.0	9.3
Net Income Margin(%)	1.5	2.3	3.2	3.9	4.3
Net Income Attri. to Controlling Shareholders	2.1	3.7	5.7	8.0	9.3
Net Income Margin(%)	1.5	2.3	3.2	3.9	4.3
Net Income Attri. to Non-Controlling Shareholders	0.0	0.0	0.0	0.0	0.0
Other Comprehensive Income	0.1	0.1	0.1	0.1	0.0
Total Comprehensive Income	2.2	3.8	5.8	8.1	9.4

(Unit : W bn)

Cashflow Statement					
	2016A	2017A	2018F	2019F	2020F
Cash Flows from Operating Activities	7.4	8.5	2.6	9.4	6.3
Net Income	2.1	3.7	5.7	8.0	9.3
Non-Cash Expenses	5.8	8.7	7.4	7.5	6.1
Depreciation	0.9	0.9	1.0	0.9	0.9
Gains(Losses) on Foreign Exchange	-0.4	-2.0	-1.1	-1.1	-0.9
Gains(Losses) in Associates, Subsidiaries and JVs	-0.1	0.0	0.0	0.0	0.0
Others	5.5	9.8	7.5	7.7	6.1
Changes in A/L from Operating Activities	3.3	-0.2	-5.1	-1.5	-4.2
Other Cash Flows	-1.8	-1.5	-1.6	-2.3	-2.7
Cash Flows from Investing Activities	-0.5	-1.6	-1.3	-1.8	-1.6
Investment Assets	0.0	0.0	0.1	-0.1	0.0
Tangible Assets	-2.3	-1.5	-0.7	-0.9	-0.5
Others	1.8	-0.1	-0.7	-0.9	-1.1
Cash Flows from Financing Activities	-4.8	-7.1	-6.8	-6.3	-5.9
Short-Term Borrowings	-1.0	-2.0	-4.0	-5.0	-4.7
Short-Term Bonds	0.0	0.0	0.0	0.0	0.0
(Long-Term)Borrowings	3.0	0.0	-0.5	0.0	0.0
(Long-Term)Bonds	0.0	-2.8	0.0	0.0	-9.0
Dividend payment	-1.3	-1.3	-1.3	-1.3	-1.3
Others	-5.5	-1.0	-1.0	0.0	9.0
Other Cash Flows	0.0	-0.1	0.4	-0.4	-0.1
Incr.(Decr.) in Cash and Cash Equivalents	2.1	-0.3	-5.1	0.9	-1.3
Beginning Cash and Cash Equivalents	16.2	18.3	17.9	12.8	13.7
Ending Cash and Cash Equivalents	18.3	17.9	12.8	13.7	12.4
NOPLAT	2.6	6.1	6.8	9.8	9.9
FCF	4.2	5.8	2.6	8.3	6.0

(Unit : W bn)

Balance Sheet					
	2016A	2017A	2018F	2019F	2020F
Current Assets	117.1	108.1	109.8	114.0	118.7
Cash and Cash Equivalents	18.3	17.9	12.8	13.7	12.4
Trade and Other Current Receivables	90.9	83.1	89.7	93.0	98.8
Inventories	0.0	0.0	0.0	0.0	0.0
Other Current Assets	8.0	7.1	7.2	7.4	7.5
Non-Current Assets	26.3	26.5	25.3	24.6	25.0
Tangible Assets	3.3	2.2	1.9	2.0	1.6
Investments in Associates, Subs and JVs	0.0	0.0	0.0	0.1	0.1
Other Financial Assets	0.0	0.0	0.0	0.0	0.0
Non-Current Assets	22.9	24.2	23.3	22.6	23.4
Assets	143.4	134.6	135.0	138.6	143.7
Current Liabilities	92.5	73.0	69.2	66.3	63.0
Trade and Other Current Payables	37.1	31.4	33.2	35.2	36.6
ST Borrowings	36.1	34.1	30.1	25.1	20.4
Current Portion of Long-Term Debt	12.4	1.0	0.0	0.0	0.0
Other Current Liabilities	6.9	6.5	6.0	6.0	6.0
Non-Current Liabilities	2.0	10.0	9.7	9.4	0.9
Bonds	0.0	9.0	9.0	9.0	0.0
LT Borrowings	1.5	0.5	0.0	0.0	0.0
Other Non-Current Liabilities	0.5	0.5	0.8	0.5	0.9
Liabilities	94.6	83.0	78.9	75.7	63.9
Owners of Parent Equity	48.9	51.6	56.1	62.9	79.8
Capital Stock	7.0	7.0	7.0	7.0	8.0
Capital Surplus	7.4	7.6	7.6	7.6	15.6
Retained Earnings	42.2	44.6	49.0	55.8	63.6
Others	-7.6	-7.5	-7.4	-7.4	-7.4
Non-Controlling Interests Equity	0.0	0.0	0.0	0.0	0.0
Stockholders' Equity	48.9	51.6	56.1	62.9	79.8
Interest-Bearing Debts	50.0	44.5	39.0	34.0	20.4

(Unit : KRW, %, x)

Valuation Indicator					
	2016A	2017A	2018F	2019F	2020F
EPS	154	266	413	577	517
PER	33.5	17.5	13.9	9.9	11.1
BPS	3,510	3,705	4,031	4,519	5,014
PBR	1.5	1.3	1.4	1.3	1.1
EBITDAPS	469	750	815	1,005	847
EV/EBITDA	15.2	8.3	8.9	6.8	5.4
SPS	10,039	11,456	12,886	14,688	12,029
PSR	0.5	0.4	0.4	0.4	0.5
CFPS	524	844	877	1,061	829
DPS	100	100	100	100	100

(Unit : %, x)

Financial Ratio					
	2016A	2017A	2018F	2019F	2020F
Earnings Growth					
Sales Growth	2.9	14.1	12.5	14.0	6.3
OP Growth	-22.4	60.9	4.1	34.8	10.6
NP Growth	-41.1	72.4	55.2	39.7	16.4
Profitability					
ROIC	4.1	10.4	11.5	15.7	15.3
ROA	1.5	2.7	4.3	5.9	6.6
ROE	4.4	7.4	10.7	13.5	13.1
Stability					
Current Ratio	126.6	148.1	158.6	172.1	188.4
Debt Ratio	193.5	160.8	140.6	120.3	80.1
Interest Coverage	2.0	3.8	4.5	6.9	12.7

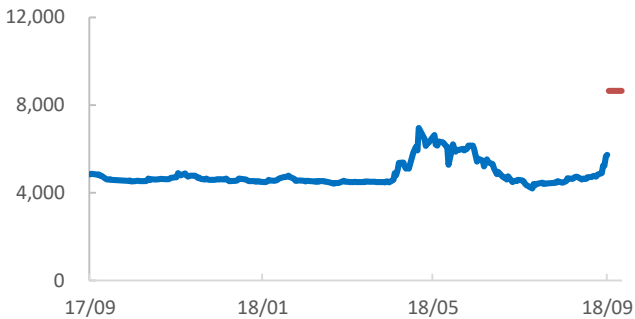
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- ❖ This report accurately reflects the views of the analyst's person and was not affected by any adverse influence or interference. (analyst : Leo Choi)
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- ❖ As of the publication date, we do not own 1% or more of the company's shares outstanding but the research analyst who prepared this report owns 27,999 shares of the company.

Company & Industry opinion category

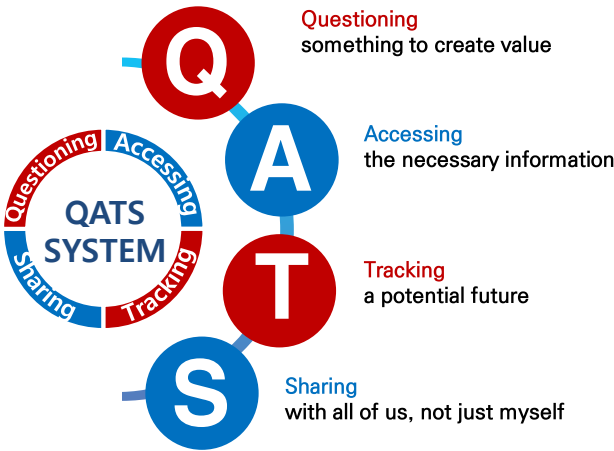
Positive	Expected to rise by more than 30% in 3 months
Neutral	Expected to fluctuate by -10% ~ 10% in 3 months
Negative	Expected to decline by more than 10% in 3 months

HEERIM Closing Price & Fair Value (Unit : KRW)



Rating Change

Date	Fair Value (KRW)	Rating
2018.09.17	8,650(Upward)	Positive
2018.03.12	6,900	Positive



Independent ResearchARUM with QATS System is Truly An Unbiased Milestone to Your Success.



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The Company has been notified to the Financial Supervisory Service (FSS) in conducting similar investment advisory business.

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