Strategy | KOREA
2011 Outlook

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ANCHOR REPORT

Land of the investing calm

We expect the Korean market to continue to rise in 2011. Although the economic recovery is still tentative in many developed economies, we are not looking for a double dip and think Korean companies' earnings should post positive growth owing to their high exposure to emerging markets. We think liquidity will sustain even though we expect the Korean central bank to normalise monetary policy from an extremely loose state as US long bonds are likely to be well behaved. Importantly, we see no signs of a bubble in the economy or in equity markets. In contrast to many other Asian markets, which have seen substantial coincident rises in their property and equity markets, the Korean property market has been subdued over the past year and the equity markets also don't appear overheated; equity prices have largely been led by earnings growth rather than multiple expansion. However, we recommend being selective rather and buying the market as a whole. With commodity prices set to rise further, we look for corporate margins to deteriorate in 2011 and the won to strengthen, although not enough to fully offset rising import prices. In this scenario, our model portfolio is tilted towards the beneficiaries of rising commodity prices, such as 1) large E&C companies; 2) companies that produce substitutes, such as petrochemicals; 3) companies less vulnerable to price controls; and 4) earnings momentum stories with attractive valuations. Top BUYs: Samsung Engineering, GS E&C, LG Chemical, Hyundai Motor Company and Samsung Electronics.

① **Forget the double dip**

② **No local overheating**

③ **Inflation, substitution, valuation**

Nomura Anchor Reports examine the key themes and value drivers that underpin our sector views and stock recommendations for the next 6 to 12 months.

Stocks for action

Company	Nomura rating	Price	Price target
Samsung Engineering (028050 KS)	BUY	197,000	250,000
GS E&C (006360 KS)	BUY	105,000	120,000
LG Chem (051910 KS)	BUY	395,500	500,000
Hyundai Motor (005380 KS)	BUY	179,000	210,000
Samsung Electronics (005930 KS)	BUY	820,000	1,050,000

Pricing as of 1 December, 2010; local currency

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And the Korea Research Team

Don't miss our companion outlook reports on Asia and Global Economics, published 6 December, 2010.

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Action

We expect Kospi earnings to rise 15% in 2011. Our market year-end target is 2230, with a fair risk premium of 6.7%. Unlike 2010, Korean equities are entering 2011 with no signs of overheating. The global economy has avoided a double dip, valuations remain inexpensive, while liquidity conditions and sentiment are favourable. We prefer those stocks benefiting from rising commodity prices.

Anchor themes

- BoK rate hikes have been much slower than expected, despite current account surpluses having reached a record high, resulting in loose monetary conditions and excess liquidity. A highly leveraged household, subdued property prices and a strengthening won are delaying aggressive monetary policy tightening, and has helped sentiment on Korea equities. We see Korea as is a key beneficiary of emerging market growth.
- Rising commodity prices suggest that companies will see growing margin pressure in 2011. Firmer oil prices would erode Korean terms of trade.

Stocks for action

As inflation pressures mount, we recommend investors acquire companies benefiting from rising commodity prices, such as major E&Cs and petrochemicals.

Company	Nomura rating	Price	Price target
Samsung Engineering (028050 KS)	BUY	197,000	250,000
GS E&C (006360 KS)	BUY	105,000	120,000
LG Chem (051910 KS)	BUY	395,500	500,000
Hyundai Motor (005380 KS)	BUY	179,000	210,000
Samsung Electronics (005930 KS)	BUY	820,000	1,050,000

Note: prices as of 1 December, 2010

Land of the investing calm

① Forget the double dip

With some lead indicators in China and the US turning upward again, we maintain our view that the global economy won't fall into a double dip. After investors priced in a double-dip scenario from 2H10, domestic-focused sectors such as Wholesalers substantially outperformed some exporters such as Tech. The reversal of this trend should come earlier, as the global economy continues to surprise and since the valuation gap between some sectors appears excessive.

② No local overheating

Entering 2010, property markets began to show signs of stabilising alongside improving transaction volumes. As Korean households are highly leveraged and property assets account for 80% of total assets, reviving property markets appear to be essential for positive sentiment towards financial assets. Despite abundant liquidity, there have been no signs of overheating in the economy as property markets remain subdued. Ironically, the best time for equities should come before any acceleration in housing prices; this acceleration should trigger concerns about monetary policy tightening or administrative measures.

③ Inflation, substitution, valuation

In 2011, Korean equities are expected to rise further while the stronger Korean won should support total returns in US dollars. Although earnings momentum remains relatively weak, we enter 2011 with a high beta concentrated portfolio. With commodity prices set to rise further in 2011, our recommended model portfolio is tilted towards: 1) companies set to benefit from rising commodity prices, such as large E&C companies; 2) companies that produce substitutes, such as petrochemicals, and; 3) companies less vulnerable to any price controls by local authorities. While Auto has better earnings momentum, the Tech sector appears cheap relative to fundamentals.

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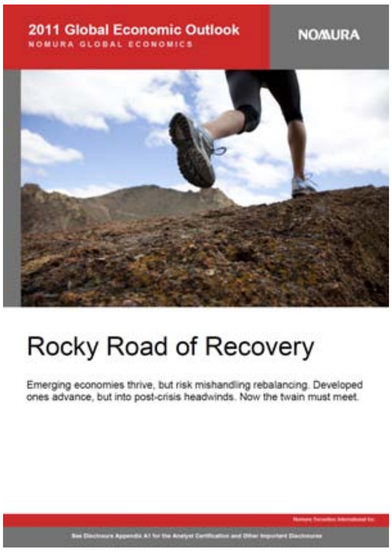
Also see our Anchor Report: Asia Pacific Strategy — *Deflation, inflation and the return of the productive economy* (6 December, 2010)

Also see our NOMURA: 2011 Global Economic Outlook — *Rocky Road of Recovery* (6 December, 2010)



Summary

Korea in 2011

Economics

- We expect GDP growth to slow from 5.9% in 2010 to 3.5% in 2011 before rising to 5.0% in 2012. On a quarterly basis, we expect year-over-year GDP growth will bottom out in 2Q11.
- A stronger KRW (we forecast KRW/USD appreciating to 1,020 by end-2011) should offset cost-push inflation from higher oil prices, but rising nominal wages and housing rents are adding to inflation pressures. We forecast CPI inflation will rise from 2.9% in 2010 to 3.7% in 2011, before easing to 3.0% in 2012.
- We expect the current account surplus to narrow to US$21bn (1.8% of GDP) in 2011 from US$35bn (3.5%) in 2010, mainly due to higher oil prices and a stronger Korean won.
- With slowing growth and the twin imbalances of a large current account surplus and high inflation, we expect policymakers to choose a compromise policy mix: implementing modest fiscal consolidation, tightening macro-prudential measures further, allowing some KRW appreciation and hiking policy rates slowly.

Strategy

- We expect Kospi earnings to rise by 15% y-y in 2011. Our market year-end target is 2230, with a fair risk premium of 6.7% (please see page 31-32).
- **Favourable liquidity conditions continue:** Backed by loose monetary conditions in the US and Japan, global liquidity remains favourable. While the Korean central bank will normalise monetary policy from an extremely loose state, we don't expect this to undermine equity returns since US long bonds are likely to be well behaved.
- **Weaker momentum but earnings continue to grow:** While Korean companies' earnings momentum is expected to remain weak in 1H11, the upward swings in lead indicators in China and the US suggest the risk of a double dip is receding. Although a subpar recovery in developed economies will continue, Korean companies which are geared to EM should have better earnings momentum.
- **Margin pressure by rising commodity prices:** With a weaker US dollar and stronger commodity prices, companies' margins are expected to deteriorate sharply.
- **A return of local funds to equities:** We believe the Korean housing market is near bottom, and a rising wealth effect should be key to redirecting local investors' fund flows into equities.
- We like: 1) companies which are set to benefit from rising commodity prices such as Korean large E&C companies; 2) companies that produce substitutes such as petrochemicals, and; 3) companies that are not affected by any government efforts to curb inflation.

Exhibit 1. Kospi level given risk premium and earnings growth

	Kospi 2011F EPS growth %					
	12	13	14	15	14	13
Fair risk premium %						
8.0	1,910	1,930	1,940	1,960	1,940	1,930
7.0	2,100	2,120	2,140	2,160	2,140	2,120
6.7	2,170	2,190	2,210	**2,230**	2,210	2,190
6.0	2,330	2,350	2,370	2,400	2,370	2,350
5.0	2,620	2,650	2,670	2,690	2,670	2,650

Note: as of 15 November, 2010; please see page 28 for full description

Source: Bloomberg, Nomura International (Hong Kong) Limited – Investment Strategy

Sectors and Top Picks

- We Overweight Korean E&C companies, Chemicals, Tech and Auto, while we have Underweight recommendations on F&B, Utility and Telecoms. Our Top Picks under Nomura coverage are Samsung Engineering, GS E&C, LG Chem, Hyundai Motor and Samsung Electronics.

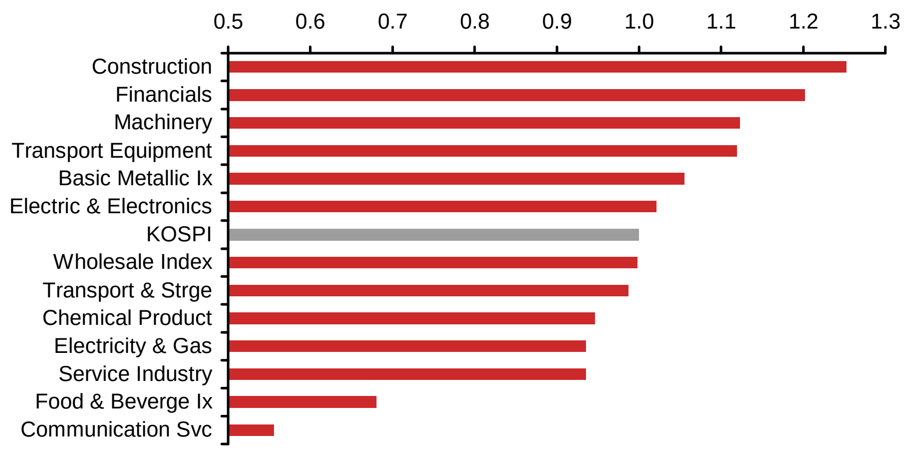
Exhibit 2. Sector weightings

Sector	Asset allocation: Benchmark %	Asset allocation: Nomura %	Asset allocation: TOP BUYs	Difference (+overweight, - underweight)	Nomura stance	Beta
Electric & Electronics	18.0	22.0	Samsung Elec.	4.0	Overweight	1.02
Financials	16.0	18.0	KB Financial g	2.0	Overweight	1.20
Transport Equipment	13.0	16.0	Hyundai Motor	3.0	Overweight	1.12
Chemical Product	12.0	15.0	LG Chem	3.0	Overweight	0.95
Service Industry	9.0	8.0	Samsung Engineering	(1.0)	Underweight	0.94
Basic Metallic Ix	7.0	6.0	Hyundai Steel	(1.0)	Underweight	1.06
Wholesale Index	6.0	4.0	Hyundai Home Shopping	(2.0)	Underweight	1.00
Construction	3.0	7.0	GS E&C	4.0	Overweight	1.25
Communication Svc	3.0	0.5	SK Telecom	(2.5)	Underweight	0.56
Transport & Strge	3.0	0.5	n/a	(2.5)	Underweight	0.99
Electricity & Gas	2.0	0.0	KEPCO	(2.0)	Underweight	0.94
Machinery	2.0	3.0	n/a	1.0	Overweight	1.12
Food & Beverge Ix	2.0	0.0	Orion	(2.0)	Underweight	0.68
Medicine	1.0	0.0	n/a	(1.0)	Underweight	0.66
Miscellaneous Indx	1.0	0.0	n/a	(1.0)	Underweight	0.50
Others	2.0	0.0	n/a	(2.0)	Underweight	n/a
				Nomura Beta		1.07

Note: please see page 33 for full description.

Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 3. Kospi sector beta



Source: Nomura International (Hong Kong) Limited – Investment Strategy

Bottom-up Sector outlook summary

Exhibit 4. Korea: sector outlook and investment horizon in 2011

Sector/ Nomura stance	Top picks	Expected momentum trend (Jan F M A M J J A S O N Dec)	Analyst comment
Auto : Bullish			
Justin Lee +822 3783 2338 justin.lee@nomura.com	BUYs – Hyundai Motor (005380 KS)	▲ ▶ ▲	1Q: Positive impact from new model launches in 4Q10 to continue into 1Q11 4Q: New model launches and seasonality factor supporting share price
Chemical: Bullish			
Cindy Park +822 3783 2324 cindy.park@nomura.com	BUY - LG Chem [051910 KS]	▶ ▲ ▶ ▼	1Q11: may soften on new petrochemical capacity start-ups in Asia. Should rebound from 2Q11 due to better LCD cycle
Construction: Bullish			
Keith Nam +82 2 3783 2304 keith.nam@nomura.com	BUYs - Samsung Engineering [028050 KS] GS E&C [006360 KS]	▲ ▶ ▲	1Q: Overseas new orders momentum to continue from 2H10 2Q: Similar new orders trend as in 1Q 3Q: Domestic housing should attempt a rebound from short supply 4Q: Domestic coupled with overseas order momentum expected
Consumer Related: Bullish			
Cara Song +822 3783 2328 cara.song@nomura.com	BUYs- Hyundai Home Shopping [057050 KS]	▲ ▶ ▲	Buy in December~ 1Q11: solid earnings momentum from continuous shift to higher-end product mix and the expected recovery in the insurance sales from 1Q11F
Financials - Bank: Bullish			
Gil Hyung Kim +82 2 3783 2335 gilhyung.kim@nomura.com	BUYs- KB Financial Group [105560 KS]	▲ ▶	We think the best part of the property-market centric credit cycle lies just ahead. Risks related to construction/real estate project financing will wash out beyond 2H10F. Normalisation of monetary policy should be on the central bank's agenda, once asset prices stabilise
Internet: Bullish			
Stanley Yang +822 3783 2331 stanley.yang@nomura.com	BUYs- Neowiz Games [095660 KS]	▲ ▶ ▲ ▶ ▲	Limited seasonality factor for Internet stocks. China play and earnings momentum are key drivers
Power: Bullish			
Keith Nam +82 2 3783 2304 keith.nam@nomura.com	BUY - KEPCO [015760 KS]	▶ ▲ ▶	1Q: Momentum may be slow, due to other favoured sectors. 2Q: Before implementation of fuel cost escalation scheme, more market interest in Kepco stock. 3Q: Implementation of new tariff scheme could continue positive trend. 4Q: Stock may move sideways after the news of fuel cost escalation implementation
Refining: Bullish			
Cindy Park +822 3783 2324 cindy.park@nomura.com	BUY - SK Energy [096770 KS]	▲ ▶ ▼	1Q11: remain strong on tight PX and middle distillates. May soften from 4Q11 as we expect higher supply growth in 2012 globally
Shipping (Bulk shipping): Bullish			
Andrew Lee +852 2252 6197 andrew.lee@nomura.com **Cecilia Chan** +852 2252 6181 cecilia.chan@nomura.com	NEUTRAL – Korea Line (005880 KS)	▲ ▼ ▲	We expect strong BDI in 1Q and 4Q due to seasonality (increasing coal demand from winter and grain harvest season). While we are positive on demand, supply is becoming a concern, with YTD newbuilding slippages tracking below expectations and Greenfield shipyards beginning to deliver
Shipping (Container shipping): Bearish			
Andrew Lee +852 2252 6197 andrew.lee@nomura.com **Cecilia Chan** +852 2252 6181 cecilia.chan@nomura.com	NEUTRAL – Hanjin Shipping (117930 KS) REDUCE – HMM (011200 KS)	▼ ▲ ▼	1Q11: we are likely to see further decline in container freight rates, which would drive share prices downward. Usually peak-season comes in from June; yet, the possible implementation of peak season surcharges depends on supply/demand balance. We are concerned about oversupply of containerships, and hence, expect a -5% decline in overall freight rates in 2011F
Steel: Bullish			
Cindy Park +822 3783 2324 cindy.park@nomura.com	BUY - Hyundai Steel [004020 KS]	▲ ▶ ▲ ▼	1Q11: strong on new blast furnace expectation 3Q11 should see industry-wide recovery
Telco: Bullish			
Stanley Yang +822 3783 2331 stanley.yang@nomura.com	BUYs - SK Telecom [017670 KS]	▲ ▶ ▲	Buy in Dec~1Q11: on the expectation of dividend and smartphone-driven positive earnings momentum
Technology – Hardware: Neutral			
James Kim +852 2252 6203 james.kim@nomura.com	BUY – SEMCO [009150 KS]	▶ ▲	1Q10: SEMCO will continue to see earnings momentum in smartphone-related business. However we still have concern on its LED business until 1H11F. We recommend investors accumulate the stocks as it has dropped significantly on slowdown of the LED industry. However, SEMCO is one of the biggest beneficiaries of the smartphone boom owing to its competitiveness edge in ultra-slim with high capacitance MLCCs
	REDUCE - Seoul Semi [046890 KS]	▼ ▶ ▲	As a pure LED company, we think Seoul Semi has weak business structure at the moment, due mainly to slowdown of LED demand and continued supply expansion.
Technology – Memory: Bullish			
CW Chang +822 3783 2317 cwchung@nomura.com	BUY - Samsung Elec. [005930 KS]	▲ ▶	1Q11: Rebound of PC DRAM prices and benign NAND demand growth should lead to momentum-driven share performance of 1st-tier memory names

Note: Key arguments for sector top picks are highlighted in the following exhibits
Source: Nomura Seoul Equity Research

Sector Top Picks summary

Exhibit 5. Korea: sector top picks in 2011

Sector/company	PT (W)	Price (W)	Nomura rating	Analyst comment	Analyst
Auto					
Hyundai Motor 005380 KS	210,000	179,000	BUY	Re-rating underway with improvement in brand equity, evident from m/s gains and strong earnings flow	**Justin Lee** +822 3783 2338 justin.lee@nomura.com
Bank					
KB Financial group 105560 KS	70,000	54,100	BUY	Highly leveraged to the property market, KBFG's asset quality, loan growth and NIM have faced strong headwinds in 2010. With downside risk likely to ease beyond 2H10F, the return of a benign credit cycle and a likely increase in the policy rate in 2011F, we expect a tenfold earnings gain in FY11F	**Gil Hyung Kim** +82 2 3783 2335 gilhyung.kim@nomura.com
Construction					
Samsung Engineering 028050 KS	250,000	197,000	BUY	Gulf plant engineering orders continue to boom, margin remains high	**Keith Nam** +82 2 3783 2304 keith.nam@nomura.com
GS E&C 006360 KS	120,000	105,000	BUY	Benefits from domestic housing pick-up, Gulf construction, Vietnam property market recovery	**Keith Nam** +82 2 3783 2304 keith.nam@nomura.com
Consumer related					
Hyundai Home Shopping* 057050 KS	143,000	95,300	BUY	Continuously improving product mix, recovery in the insurance and high operating leverage should support solid earnings growth. Valuation attractive, trading at discount to the market despite healthy fundamentals (better than physical retail) and on a sound macro outlook	**Cara Song** +822 3783 2328 cara.song@nomura.com
Internet					
Neowiz Games 095660.KS	71,000	47,600	BUY	Strengthening domestic online game publishing platform, Pmang .com and superior overseas strategies	**Stanley Yang** +822 3783 2331 stanley.yang@nomura.com
IT Hardware					
SEMCO 009150 KS	144,000	126,000	BUY	We believe growth momentum at the MLCC business, aided by the smartphone boom, has not yet been priced in. SEMCO is one of the most competitive manufacturers in ultra-small MLCCs with high capacitance. As such, we believe SEMCO is one of the beneficiaries of increased demand for smartphones, as they require a higher number of MLCCs with high capacitance per unit. We recommend investors accumulate the stocks as it has dropped significantly on a slowdown of the LED industry. However, we believe that SEMCO is undervalued given the growth momentum of its MLCC business and other businesses	**James Kim** +852 2252 6203 james.kim@nomura.com
Memory					
Samsung Elec. 005930 KS	1,050,000	820,000	BUY	A near-term crunch is expected on quarterly earnings ahead, from 4Q10F to 1Q11F. The share price may be under pressure in the short term, in our view However, Samsung is best prepared among its peers for "rising technology", such as OLED display, specialty DRAM, NAND and smartphones. With proven competitiveness in the above spaces, Samsung should recover from the current downcycle ahead of its peers We advise accumulating the stock on any weaknesses before an anticipated inflection point from 1Q11F	**CW Chung** +822 3783 2312 cwchung@nomura.com
Petrochemical					
LG Chem 051910 KS	500,000	395,500	BUY	Due to weaker 4Q10 earnings prospects, LG Chem has underperformed its Korean chemical peers in the past three months. Investors should focus on the positive trend of the petrochemical business, start of automotive battery shipments and recovery of the electronic materials from early FY11F. LGC will be a direct beneficiary of the petrochemical upturn we expect in 2011-12F. We reiterate our BU Y call	**Cindy Park** +822 3783 2324 cindy.park@nomura.com
Power					
KEPCO 015760 KS	43,000	28,350	BUY	Fuel cost escalation tariff scheme could herald the first guaranteed tariff scheme for Kepco	**Keith Nam** +82 2 3783 2304 keith.nam@nomura.com
Refining					
SK Energy 096770 KS	190,000	172,500	BUY	We see further potential upside to SKE's share price despite recent outperformance. The business spin-off, if approved at the 26 November EGM, could accelerate positive strategic moves for refining and petrochemical units. E&P production may reach 75,000 bpd in early 2011F (2Q10: 52,000pd). Brazil's Wahoo field and other potential M&As may bring an additional 3,000-5,000bpd by 2013F. Potential deals related to the Incheon refining plant may boost the share price	**Cindy Park** +822 3783 2324 cindy.park@nomura.com

Exhibit 5. Korea: sector top picks in 2011 (cont'd)

Sector/Company	PT (KRW)	Price (KRW)	Nomura rating	Analyst comment	Analyst
Shipping					
Hyundai Merchant Marine 011200 KS	26,000	42,300	REDUCE	As we estimate container freight rates have peaked and will decline in 2011F, we believe earnings will be under pressure. For the non-container business, despite expensive chartered vessels due to expire within the next two years (leading to lower breakeven for drybulk), this would still be insufficient to offset lower container earnings, in our view. While containers accounted for 69% of 9M10 revenue, total 9M10 operating profit came from container as other businesses were loss-making	**Andrew Lee** +852 2252 6197 andrew.lee@nomura.com **Cecilia Chan** +852 2252 6181 cecilia.chan@nomura.com
Steel					
Hyundai Steel 004020 KS	125,000	109,000	BUY	HS is in the nascent stage of an automotive steel development with marked upside potential owing to the relationship with Hyundai Motor Group. We rate HS as our sector top pick, based on strong sales volume growth (21% pa in FY09-11F), product mix shifting to flat steel (flat to represent 43% of volume in FY11F; 27% in FY08) and valuations that are at an 18% (PBV) discount to Asian blast furnaces	**Cindy Park** +822 3783 2324 cindy.park@nomura.com
Telco					
SK Telecom 017670 KS	223,000	171,500	BUY	SKT is expected to deliver positive earnings momentum from 1Q11 thanks to rapidly increasing smartphone penetration	**Stanley Yang** +822 3783 2331 stanley.yang@nomura.com

Note: Country top picks are highlighted; prices as of 1 December, 2010

* Price target and rating as at 3 December 2010, please see our Korea Consumer report published on 8 December for more details.

Source: Nomura Seoul Equity Research

Nomura coverage valuation

Nomura Korea universe

Exhibit 6. Nomura coverage

	Company	KS code	M/Caps US$ mn	Rating	date of rating change	TP / FV	Price 1-Dec-10	Upside potential	Price performance(%) 1day	1 week	1 m	3 m	6 m	YTD	PER (x) FY10F	PER (x) FY11F	EPS Growth(%) FY10F	EPS Growth(%) FY11F	EV/EBITDA (x) FY10F	EV/EBITDA (x) FY11F	PBR (x) FY10F	PBR (x) FY11F	ROE (%) FY10F	ROE (%) FY11F	Yield (%) FY10F	Yield (%) FY11F
Electronics / IT																										
1	Hynix	000660	11,999	Buy	9-Aug-10	33,000	23,400	41.0	(0.4)	(9.1)	3.1	12.2	(4.9)	1.1	4.2	5.6	n.a.	(24.4)	2.7	2.7	1.6	1.2	44.3	24.6	0.0	0.0
2	LG Electronics Inc.	066570	13,005	Neutral	18-Nov-09	98,000	103,500	(5.3)	0.5	(2.4)	6.8	8.0	(1.4)	(14.8)	17.7	14.1	(57.4)	25.9	10.1	7.2	1.3	1.2	7.6	8.7	1.2	1.4
3	LG Display	034220	12,433	Neutral	24-Aug-10	36,000	40,000	(10.0)	1.1	(4.5)	4.7	20.3	(10.2)	1.9	12.1	15.3	14.9	(20.8)	3.9	4.0	1.3	1.2	11.2	8.2	1.4	1.1
4	Samsung Electronics	005930	104,926	Buy	3-Jul-09	1,050,000	820,000	28.0	(0.7)	(3.6)	9.8	9.0	6.8	2.6	8.8	9.3	65.1	(5.3)	3.9	3.5	1.4	1.3	20.6	16.6	1.6	1.7
5	Samsung SDI	006400	6,471	Neutral	7-Sep-09	152,000	163,500	(7.0)	(1.2)	(3.3)	5.1	(2.7)	(2.1)	10.1	18.5	14.3	73.9	29.8	8.4	9.0	1.5	1.4	8.4	10.3	0.4	0.4
6	Samsung Techwin	012450	4,915	Buy	12-Aug-09	130,000	106,500	22.1	(1.8)	0.0	(0.9)	(4.5)	5.4	17.3	23.8	14.5	13.1	64.5	15.0	9.8	4.4	3.5	20.1	26.8	0.7	0.7
7	SEMCO	009150	8,176	Buy	28-Jul-09	144,000	126,000	14.3	0.8	(6.7)	2.9	8.6	(5.3)	17.2	16.1	12.3	118.5	31.1	6.8	5.5	3.2	2.6	20.9	23.7	0.5	0.6
8	Technosemichem	036830	1,104	Buy	11-Aug-08	37,000	31,200	18.6	0.3	3.8	(1.0)	24.6	39.0	43.4	11.1	8.8	62.4	26.2	21.3	16.1	2.1	1.7	20.3	21.2	0.8	1.3
9	Seoul Semiconductor	046890	1,975	Reduce	24-Sep-10	34,000	39,000	(12.8)	0.5	1.0	2.1	4.8	(11.1)	(15.9)	23.0	18.5	246.0	24.6	16.2	12.3	4.0	3.4	19.3	19.8	0.6	0.8
10	Jusung Engineering	036930	539	Neutral	27-Oct-10	23,000	18,400	25.0	(0.3)	(0.8)	(7.1)	2.2	(10.0)	7.3	15.2	10.1	1,815.6	51.2	14.8	7.3	3.2	2.4	22.6	27.6	0.0	0.0
11	OCI Materials	036490	1,007	Buy	10-Dec-08	150,000	109,900	36.5	0.4	(2.7)	9.5	(3.0)	3.3	16.1	19.0	11.8	20.7	60.9	10.2	6.6	4.2	3.2	24.6	30.5	0.5	0.6
12	LG Innotek	011070	2,228	Neutral	24-Sep-10	142,000	127,500	11.4	(1.9)	(5.9)	0.0	(4.1)	(18.8)	32.8	11.7	11.1	224.8	5.6	4.6	3.1	1.7	1.5	18.7	14.7	0.3	0.3
Basic Materials																										
13	Cheil Industries	001300	4,800	Neutral	30-Jun-10	93,000	110,500	(15.8)	3.8	(1.8)	15.2	4.7	32.3	95.6	23.6	19.7	84.2	20.1	11.7	10.3	2.9	2.6	12.2	14.1	0.7	0.7
14	Hanwha Chemical	009830	4,097	Buy	3-Nov-10	40,000	33,350	19.9	5.0	1.8	2.5	24.2	120.1	147.0	9.4	7.8	45.3	19.2	6.7	6.0	1.6	1.3	17.8	18.5	1.4	1.4
15	Honam Petrochemical	011170	7,141	Buy	3-Nov-10	330,000	258,000	27.9	6.0	7.5	(0.4)	37.2	108.1	151.7	10.0	8.3	2.9	21.5	6.8	5.7	1.8	1.5	19.9	20.0	0.6	0.6
16	LG Chem	051910	22,769	Buy	9-Sep-09	500,000	395,500	26.4	1.9	1.9	6.9	14.3	45.4	73.1	11.9	9.7	43.5	23.0	7.8	6.3	3.6	3.0	33.6	33.8	1.0	1.1
17	SK Energy	096770	13,856	Buy	9-Jun-09	190,000	172,500	10.1	4.2	5.2	8.8	29.2	59.7	46.8	12.1	9.7	93.8	24.8	8.6	7.1	1.8	1.6	16.0	17.3	1.1	1.1
18	S-Oil	010950	8,470	Buy	11-Oct-10	85,000	86,600	(1.8)	8.0	13.2	21.3	38.3	66.5	60.4	25.4	16.7	74.8	52.3	13.1	10.2	2.9	2.5	10.8	16.2	1.5	3.4
19	GS Holdings	078930	5,553	Buy	9-Jun-09	68,000	67,500	0.7	7.3	7.7	10.8	31.1	89.3	99.7	8.3	11.0	55.4	(24.7)	8.2	10.1	1.6	1.4	18.9	13.5	0.7	1.5
20	Dongkuk Steel	001230	1,560	Buy	5-May-09	33,000	29,050	13.6	1.9	4.7	10.5	19.5	37.0	7.6	10.5	9.6	242.0	9.1	6.4	6.0	0.7	0.7	6.4	7.1	2.6	2.6
21	Hyundai Steel	004020	8,078	Buy	25-Aug-09	125,000	109,000	14.7	(0.9)	(0.9)	0.5	0.5	24.6	26.0	10.3	8.5	(21.8)	21.1	9.8	6.9	1.2	1.1	12.8	13.7	0.5	0.5
22	POSCO	005490	34,613	Buy	5-May-09	700,000	457,000	53.2	0.6	0.7	(1.6)	(5.5)	(0.7)	(26.1)	7.9	6.9	58.4	15.2	5.2	4.4	1.1	1.0	15.3	15.6	2.2	2.2
Automobile																										
23	Halla Climate Control	018880	1,757	Neutral	19-May-10	22,800	18,950	20.3	0.8	4.1	(12.7)	3.3	22.3	40.9	9.8	9.1	35.9	7.6	8.6	7.5	1.8	1.6	19.6	18.3	2.7	3.2
24	Hankook Tire	000240	4,036	Neutral	5-Oct-10	34,000	32,000	6.3	6.7	6.8	4.7	21.2	29.0	25.5	11.8	9.9	18.0	18.9	9.1	7.8	2.0	1.7	18.6	18.7	1.0	1.2
25	Hyundai Mobis	012330	24,396	Buy	12-Nov-07	330,000	288,500	14.4	4.9	4.3	(2.2)	27.9	50.3	68.7	11.3	9.8	46.3	15.6	8.4	7.2	2.7	2.2	27.5	24.9	0.9	1.0
26	Hyundai Motor	005380	34,252	Buy	6-Jul-09	210,000	179,000	17.3	3.8	(0.6)	(0.8)	24.3	35.1	47.9	7.9	7.0	69.3	11.9	6.2	5.4	1.5	1.3	20.6	19.3	2.3	2.6
27	Kia Motors	000270	17,308	Buy	6-Jul-09	60,000	50,500	18.8	3.2	1.8	2.0	58.3	68.1	151.9	8.6	7.5	49.9	14.6	5.2	4.4	2.1	1.7	27.2	24.8	1.2	1.4
28	Mando	060980	1,844	Buy	26-Oct-10	177,000	131,500	34.6	(0.8)	5.2	(1.9)	(6.1)	6.9	0.0	9.7	8.2	49.3	18.7	8.2	6.4	2.0	1.6	22.8	22.2	0.0	0.3
29	Ssangyong Motor	003620	965	Reduce	19-Mar-09	1,170	9,200	(87.3)	0.3	(4.7)	(12.0)	1.0	(34.1)	268.0	0.0	0.0	n.a.	0.0	100.4	12.6	0.0	0.0	52.7	15.7	0.0	0.0
Financials																										
30	KB Financial Group	105560	18,157	Buy	2-Mar-10	70,000	54,100	29.4	0.0	1.3	6.1	10.3	10.0	(9.4)	82.1	7.0	(59.9)	1,065.3	0.0	0.0	1.0	0.9	1.2	13.4	1.1	1.5
31	Shinhan Financial Group	055550	16,896	Buy	2-Mar-10	60,000	44,800	33.9	0.2	3.3	1.9	(3.0)	3.5	3.7	8.4	7.0	92.0	19.8	0.0	0.0	0.9	0.8	12.3	13.3	1.8	2.0
32	Woori Financial Group	053000	9,978	Buy	30-Sep-10	18,000	14,250	26.3	(0.3)	3.3	0.0	5.2	(2.4)	2.9	10.7	5.5	4.1	95.0	0.0	0.0	0.8	0.7	7.6	13.5	0.4	0.7
33	Hana Financial Group	086790	6,984	Neutral	2-Mar-10	39,000	37,950	2.8	(0.1)	(4.4)	15.9	21.4	22.6	15.3	8.0	6.8	227.5	17.5	0.0	0.0	0.8	0.7	10.0	10.7	2.4	2.1
34	IBK	024110	9,035	Buy	2-Mar-10	20,000	16,150	23.8	(0.3)	(2.4)	(0.9)	10.6	18.3	15.4	6.7	6.1	95.6	9.7	0.0	0.0	0.9	0.8	15.2	14.6	2.8	3.9
35	KEB	004940	6,331	Buy	2-Mar-10	17,500	11,300	54.9	0.9	(7.8)	(14.4)	(12.1)	(14.1)	(22.1)	6.7	6.6	22.1	1.9	0.0	0.0	0.9	0.8	13.3	12.7	7.1	6.2
36	Busan Bank	005280	2,214	Neutral	24-Apr-09	14,000	13,650	2.6	(0.4)	(2.2)	(5.9)	5.8	25.8	(2.2)	7.1	7.2	39.1	(0.3)	0.0	0.0	0.9	0.8	14.8	12.4	0.0	2.9
37	Daegu Bank	005270	1,664	Buy	2-Mar-10	20,000	14,500	37.9	0.3	(1.4)	(3.0)	1.0	2.1	(15.7)	8.0	5.3	41.1	49.1	0.0	0.0	1.0	0.8	12.7	16.5	2.1	2.8
Telecom																										
38	SK broadband	033630	1,383	Reduce	27-Nov-08	4,600	5,380	(14.5)	0.6	5.5	(2.9)	1.7	(8.2)	12.2	0.0	38.3	n.a.	0.0	6.9	4.4	1.2	1.2	(4.7)	3.1	0.0	0.0
39	KT Corp	030200	10,468	Buy	19-Mar-09	58,000	46,150	25.7	(0.8)	0.5	3.5	3.9	(0.2)	18.0	8.9	7.6	1.9	16.5	3.5	3.5	1.0	0.9	11.6	12.3	4.3	4.3
40	LG Uplus	032640	3,184	Neutral	28-Jul-10	7,400	7,120	3.9	0.1	(0.1)	(2.2)	(5.1)	(7.5)	(16.1)	7.2	7.2	(6.9)	0.2	3.6	3.0	0.8	0.8	15.1	7.3	2.8	2.7
41	SK Telecom	017670	12,030	Buy	2-Dec-08	223,000	171,500	30.0	0.3	0.3	0.6	4.6	4.3	1.2	9.4	7.3	0.2	29.8	4.3	3.7	1.2	1.1	11.5	14.4	4.9	4.9
Internet																										
42	NHN Corp.	035420	8,090	Buy	13-Nov-07	224,000	193,500	15.8	(1.3)	(0.8)	0.3	(0.3)	8.1	0.8	18.7	14.9	17.9	25.7	13.4	10.6	6.9	5.1	42.5	39.2	0.0	0.0
43	Daum Corp.	035720	883	Buy	7-May-10	98,000	76,300	28.4	(0.3)	(4.6)	(6.2)	5.7	(1.9)	8.5	8.9	11.8	258.6	(25.1)	6.1	6.0	3.1	2.4	42.0	23.0	0.0	0.0
44	NC Soft	036570	4,376	Buy	16-Apr-09	310,000	255,000	21.6	2.8	1.2	(1.2)	7.1	34.2	70.6	26.4	18.1	3.0	45.5	15.0	11.5	6.6	5.1	25.7	28.7	0.0	0.3
45	CJ Internet	037150	311	Buy	13-Nov-07	20,000	15,700	27.4	(0.9)	1.3	9.4	33.6	43.4	13.8	9.8	8.1	45.9	20.6	4.5	3.5	1.3	1.1	14.1	15.0	1.1	1.5
46	Neowiz Games	095660	872	Buy	3-Apr-09	71,000	47,600	49.2	(1.3)	(1.8)	(13.6)	22.1	12.4	17.4	11.9	8.1	87.0	45.7	8.6	5.0	3.2	2.3	31.3	33.0	0.0	0.0
47	MegaStudy	072870	973	Neutral	29-Jul-10	182,000	176,600	3.1	(4.2)	(4.8)	(9.4)	1.5	5.7	(26.1)	15.5	13.8	6.2	11.9	11.4	10.0	3.7	3.0	27.1	24.2	1.0	1.4
Utility/Nuclear																										
48	KEPCO	015760	15,800	Buy	19-May-09	43,000	28,350	51.7	2.3	(1.6)	(4.4)	(1.9)	(14.2)	(16.9)	0.0	20.0	n.a.	0.0	7.7	6.4	0.4	0.4	(0.6)	1.9	0.0	1.6
49	KPS	051600	2,279	Buy	15-Jun-09	88,000	58,300	50.9	4.3	3.4	(5.7)	(7.2)	14.8	36.9	23.5	19.9	15.8	18.0	15.2	13.4	5.1	4.6	22.6	24.2	2.1	2.2
50	KOPEC	052690	3,486	Neutral	15-Jul-10	130,000	105,000	23.8	11.0	2.4	(19.5)	(7.9)	10.5	83.9	27.9	21.6	74.1	29.2	22.2	17.1	10.2	8.3	40.4	42.3	1.8	2.3
51	KOGAS	036460	3,004	Buy	10-Sep-09	52,000	44,750	16.2	0.9	(0.8)	(2.9)	3.0	3.7	(7.9)	15.9	11.6	(14.3)	37.7	13.9	12.6	0.7	0.7	4.7	6.3	1.9	2.6
Consumer related/Media *																										
52	KT&G	033780	7,681	Neutral	30-Mar-10	65,000	64,400	0.9	2.7	4.7	(6.9)	4.2	3.0	0.0	10.1	10.3	3.9	(2.9)	6.4	6.4	1.9	1.7	14.3	16.7	4.1	4.1
53	CJ O Shopping	035760	1,395	Buy	28-Dec-09	320,000	264,900	4.6	(0.0)	4.5	0.4	9.4	59.0	81.2	22.8	11.5	62.5	99.1	10.5	8.0	4.7	3.5	22.1	35.1	1.2	1.7
54	GS Home Shopping	028150	596	Buy	10-Sep-09	154,000	107,000	26.2	1.9	(3.6)	(5.1)	8.7	46.6	24.7	8.3	6.6	27.0	26.5	1.7	0.6	1.3	1.1	16.8	16.7	3.0	3.0
55	Hyundai Department Store	069960	2,506	Neutral	10-Sep-09	130,000	127,000	(19.7)	5.8	3.7	4.1	0.8	17.1	12.9	11.8	12.4	8.9	(4.4)	9.7	10.1	1.5	1.3	13.3	11.3	0.5	0.5
56	LG H & H	051900	5,230	Neutral	6-Aug-10	410,000	385,500	6.4	0.8	(3.4)	(2.4)	(3.6)	18.6	32.5	24.1	19.7	63.6	21.8	14.3	11.8	7.2	5.7	29.9	28.8	1.1	1.4
57	Lotte Shopping	023530	12,186	Buy	20-Jan-10	570,000	483,000	13.9	2.0	0.2	0.0	15.3	48.8	39.6	16.1	11.6	22.1	38.7	9.7	7.5	1.1	1.0	7.0	9.1	0.3	0.3
58	Orion	001800	2,067	Buy	26-Sep-08	470,000	402,000	16.9	(1.5)	(3.0)	6.2	(2.0)	20.7	39.1	12.4	20.8	422.0	(40.6)	19.0	14.5	3.7	3.2	13.7	14.9	0.4	0.4
59	Amore Pacific	090430	5,449	Neutral	25-Jun-10	1,050,000	1,073,000	(2.1)	(1.2)	(0.2)	1.7	(7.0)	14.4	14.9	22.5	19.5	23.2	15.3	15.0	12.8	4.1	3.4	21.3	20.5	0.6	0.6
60	Shinsegae	004170	9,470	Neutral	12-Oct-10	540,000	578,000	10.7	1.9	0.2	(0.3)	(2.9)	19.3	7.6	15.1	13.5	27.2	11.8	10.4	8.2	2.0	1.3	22.7	39.2	0.2	0.2
61	Seobu Truck Terminal	006730	329	Buy	10-Sep-09	34,000	18,350	85.3	0.8	(0.5)	1.4	28.3	(18.8)	(24.8)	0.0	172.2	(129.3)	0.0	125.5	64.1	0.9	0.9	(0.2)	0.5	0.2	0.2
62	Lock & Lock	115390	1,635	Buy	3-Feb-10	52,000	37,650	38.1	(0.5)	1.1	(0.4)	1.9	11.6	0.0	27.3	20.2	43.7	35.3	24.1	17.0	5.2	4.4	25.9	23.9	1.1	1.5
New	Hyundai Home Shopping	057050	1,000	Buy	8-Dec-10	143,000	95,300	50.1	(1.8)	(4.3)	(11.3)	na	na	na	10.0	7.6	(11.2)	32.0	5.1	3.2	1.7	1.4	16.6	18.6	2.0	2.6
Construction&Engineering																										
63	Daelim Industrial	000210	3,477	Buy	15-Jun-09	120,000	115,000	4.3	6.0	6.5	20.5	48.6	92.6	38.2	10.2	9.0	14.4	13.1	7.4	6.8	1.0	0.9	9.9	10.2	0.4	0.9
64	GS Eng & Construction	006360	4,652	Buy	10-Jul-08	120,000	105,000	14.3	5.0	3.4	10.2	21.0	34.4	(3.2)	12.0	10.7	16.3	12.7	7.8	6.0	1.5	1.3	12.8	13.1	1.2	1.4
65	Hyundai Development	012630	2,351	Buy	15-Jun-09	41,000	35,900	14.2	6.1	7.2	13.8	25.3	42.2	(4.9)	27.2	10.9	102.7	150.3	15.4	7.5	1.1	1.1	4.3	10.2	0.8	1.9
66	Hyundai E&C	000720	6,220	Neutral	16-Nov-10	70,000	64,300	8.9	1.7	5.9	(15.4)	(3.9)	19.7	(9.3)	11.6	10.1	34.6	15.2	9.5	8.4	2.1	1.9	19.2	19.9	1.1	1.2
67	Samsung Corporation	000830	10,517	Buy	28-Mar-09	85,000	77,500	9.7	0.9	2.1	14.1	36.2	47.6	38.1	23.9	23.8	65.9	0.7	34.6	30.7	1.6	1.5	6.7	6.4	0.9	0.9
68	Samsung Engineering	028050	6,845	Buy	14-Jan-09	250,000	197,000	26.9	6.2	5.3	4.2	48.7	82.4	82.4	24.6	15.4	29.6	59.9	14.3	7.9	7.2	4.9	34.2	37.8	1.2	1.9
69	Daewoo E&C	047040	3,381	Reduce	16-Nov-10	8,500	11,950	(28.9)	2.6	9.1	12.7	18.3	28.1	(6.6)	0.0	101.9	(484.9)	0.0	51.6	18.6	1.4	1.4	(10.7)	1.4	2.1	2.1
Shipping																										
70	Hyundai Merchant Marine	011200	5,265	Reduce	28-Sep-10	26,000	42,300	(38.5)	2.7	18.2	4.7	25.9	60.2	58.4	16.6	98.9	n.a.	(83.2)	12.4	19.8	2.2	2.3	15.1	2.3	1.6	0.3
71	Hanjin Shipping	011200	2,599	Neutral	1-Jun-10	30,000	35,200	(14.8)	(4.6)	(0.3)	11.2	17.3	17.7	74.0	17.5	52.1	n.a.	(66.5)	9.0	10.8	1.3	1.3	8.3	2.4	0.0	0.0
72	Korea Line Corp	005880	407	Neutral	28-Apr-10	63,000	28,400	121.8	(0.9)	(4.4)	(23.6)	(36.4)	(40.2)	(25.2)	71.8	112.1	n.a.	(36.0)	9.5	9.4	0.5	0.5	0.7	0.5	0.0	0.0
73	Korean Air	003490	4,464	Buy	28-Oct-10	92,000	71,400	28.9	0.6	(1.0)	0.8	(2.5)	1.9	30.1	7.1	7.0	n.a.	1.4	6.8	6.4	1.4	1.2	22.0	19.2	0.7	1.1

Note: as of 1 December, 2010; *Price target and rating for HHS, CJO, GSHS, Lotte Shopping, Shinsegae and HDS as at 3 December 2010, please see our Korea Consumer report published on 8 December for more details. GS Holdings, Korea Line and S-Oil TPs are under review; All other ratings and price targets are as of the date of the most recently published report (http://www.Nomura.com) rather than the date of this document.

Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy, Seoul Equity Research

Macro backdrop: 2011

Economic outlook: Twin imbalances

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With slowing growth and the twin imbalances of a large current account surplus and high inflation, we expect policymakers to allow some KRW appreciation but hike policy rates only modestly.

Baseline economic forecast

GDP growth

We see growth momentum picking up modestly in 2011, but annual GDP growth should slow

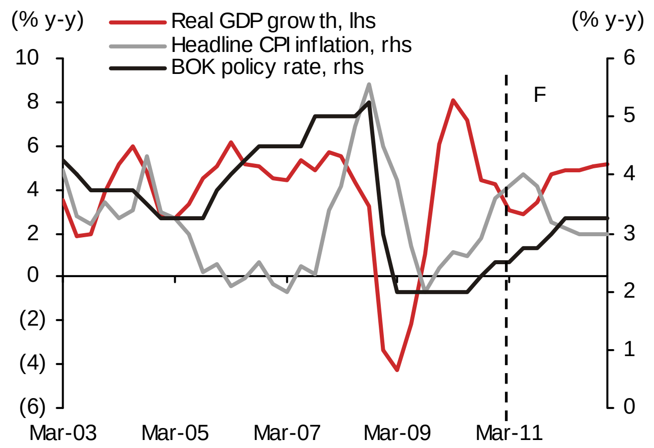
We see growth momentum picking up modestly in 2011 after sequential GDP growth eased markedly in 2H10. The positive feedback loop between strong corporate earnings and household income/job creation should gain more traction. Low interest rates should also support consumption and business investment, but construction investment is likely to suffer given elevated housing inventory. In addition to solid emerging market demand, we expect G3 (US, euro area and Japan) demand to improve gradually, but won appreciation should erode some competitiveness. In 2012, the government's stimulus measures ahead of the presidential election should help boost domestic demand. All in all, we expect GDP growth to slow from 5.9% in 2010 to 3.5% in 2011, before rising to 5.0% in 2012. On a quarterly basis, we see that year-over-year GDP growth will bottom out in 2Q11 (Exhibit below, LHS).

CPI inflation and housing prices

CPI Inflation is expected to rise to 3.7% in 2011 from 2.9% in 2010

A stronger KRW (we forecast KRW/USD appreciating to 1,020 by end-2011) should offset cost-push inflation from higher oil prices, but rising nominal wages and housing rents are adding to inflation pressures. We forecast CPI inflation will rise from 2.9% in 2010 to 3.7% in 2011, before easing to 3.0% in 2012. We expect house prices to recover only gradually in 2011-12, supported by government policy designed to prevent a housing market slump. On a quarterly basis, we see year-over-year CPI inflation peaking in 2Q11 (Exhibit below, RHS).

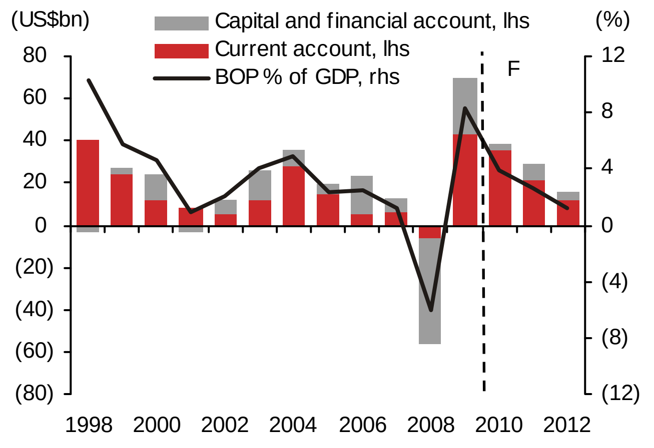
Exhibit 7. Korea's GDP, inflation and policy rates



Note: Data are quarterly and forecast is for 4Q10 ~ 4Q12.

Source: CEIC and Nomura Global Economics estimates

Exhibit 8. Korea's balance of payments



Note: Data are annual and forecast of for 2010-2012.

Source: FSS, CEIC and Nomura Global Economics estimates

Balance of payments

We expect the current account surplus to narrow to US$21bn (1.8% of GDP) in 2011 from US$35bn (3.5%) in 2010, mainly due to higher oil prices and a stronger won. The capital account surplus should widen only slightly to US$8bn in 2011 from US$3bn in 2012, reflecting the recent adoption of capital controls and macro prudential measures.

Current account surplus is likely to narrow owing to higher oil prices and a stronger Korean won

Baseline policy responses

With slowing growth and the twin imbalances of a large current account surplus and high inflation, we expect policymakers to choose a compromise policy mix: implementing modest fiscal consolidation, tightening macro-prudential measures, allowing some won appreciation and hiking policy rates only slowly.

We expect a compromise policy mix

- **Modest fiscal consolidation**: The government plans to cut the fiscal balance deficit (ex-social security) to W27.5tn (2.1% of GDP) in 2011 from W32.0tn (2.6%) in 2010. On the expenditure side, the government will cut the infrastructure investment budget, while increase the budget for welfare, education and defence.

Modest fiscal consolidation

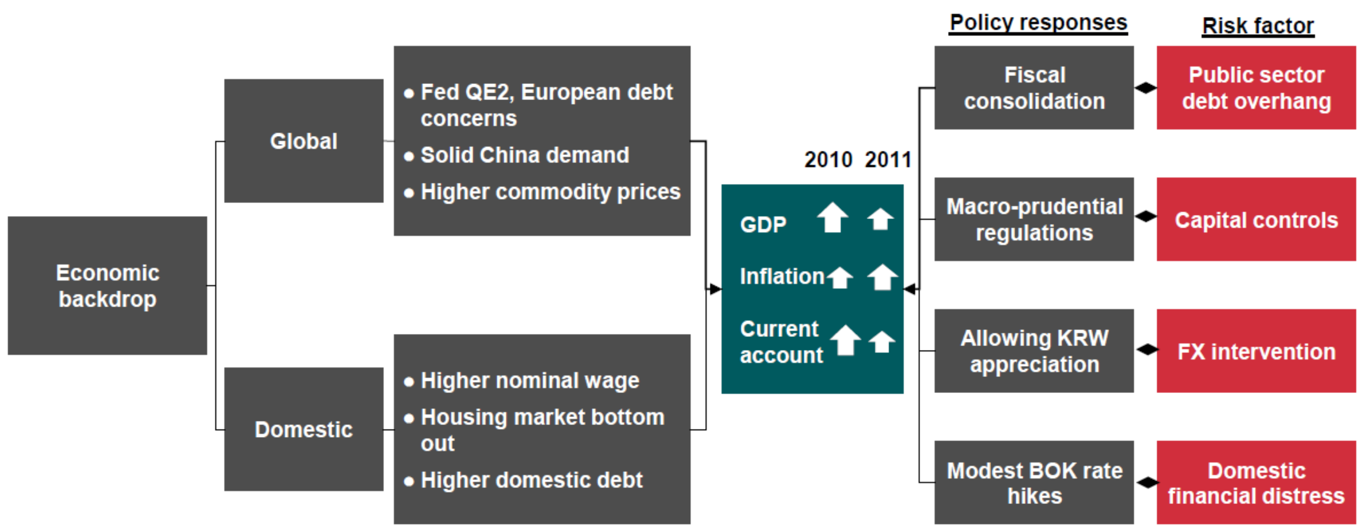
- **Capital controls/macro-prudential measures:** After the US Fed's QE2 and G20 Seoul Summit, the government announced the reintroduction of a 14% withholding tax on foreign investment in Korean Treasury Bonds and Monetary Stabilization Bonds, effective from January 2011. We expect more to come. The financial regulator will likely lower the ceiling on holdings of foreign bank branches of FX derivatives from 250% of equity capital to 200% as early as in January 2011. We cannot rule out the possibility of an introduction of a bank levy for short-term external borrowings. However, we do not expect to see draconian capital controls such as levying financial transaction taxes (Tobin tax) or imposing variable deposit requirement (VDR).

Expect more capital controls following the recent reintroduction of withholding tax on foreign investment in KTB

Given that non-performing loans (NPLs) are rising in the banking system due to a slump in real estate project financing, we expect to see further measures to deal with this. For example, the state-run Korea Asset Management Corp (KAMCO) should buy more NLPS from banks. We believe that the government's policy stance for the property market is to prevent either house prices falling too sharply or surging. Therefore, if house prices fall again, the government is likely to extend its stimulus measures. In contrast, if house prices rise sharply, the government should implement some tightening measures and the Bank of Korea would hike rates more than our baseline forecast.

Real estate project financing still needs further reform

Exhibit 9. Compromise policy mix in 2011



Source: Nomura Global Economics

- **Allowing some Korean won appreciation:** We forecast the W/US$ will appreciate to 1020 by end-2011. Indeed, Korea can reduce its twin imbalances (a large current account surplus and high inflation) with a stronger won, boosting domestic demand (imports) and taming cost-push inflation. Unless the won appreciates as much as international commodity prices gain, it will be hard to keep CPI inflation in check, given the high exchange rate pass-through. The correlation between import prices less W/US$ and CPI inflation is high, at 0.67 (based on monthly data since 2000).

  Unlike the G10, or reserve currencies (the US dollar, yen or euro), won appreciation can be achieved without rate hikes, by simply reducing the degree of FX market intervention. Indeed, there is no clear historical or statistical causality of BoK policy changes on the won. This disconnect between interest rates and the currency is mainly because won markets are not fully liberalised and the authorities intervene in the market continuously to conduct smoothing operations.

We forecast the Korean won will appreciate to 1020 US$1 by end-2011

- **Very modest monetary policy tightening:** We expect GDP growth to fall below 4% y-y in 1H11, but CPI inflation to rise to 3.9%. This, coupled with rising NPLs, will pose a policy dilemma to the BoK. We judge that the BoK will focus more on growth than inflation. As a result, we expect the BOK to raise rates three times in 25bps increments in 2Q and 4Q11 and 1Q12, lifting the terminal rate to 3.25%.

As a result, we expect the BoK to move slowly, delivering three 25bps hikes in 2Q and 4Q11 and 1Q12

Risks to our forecast

The economy is heavily reliant on external drivers: in 2009, exports accounted for 50% of GDP; its external debt was equivalent to 48% of GDP and Korea was one of Asia's largest net importers of oil (5.8% of GDP). As such, the economy is vulnerable to sudden changes in global economic conditions, credit markets and commodity prices. Domestically, if Korean policymakers are much biased to "growth over inflation", it would be positive for domestic growth only in the short run, but eventually result in a costly macro adjustment, and therefore would likely be negative for sustainable long-run economic growth.

- **Unsolved twin imbalances:** If the BoK hikes rates by more than we forecast and the authorities intervene strongly in the FX market to resist won appreciation, this policy mix should fail to contain inflation as the transmission mechanism of monetary policy through the exchange rate channel would be ineffective. Indeed, there is risk that the authorities build up their FX reserves further as a "self-insurance" against future geo-political risks or unexpected global credit shocks at the expense of higher domestic inflation. Further policy tightening risks deepening financial distress related to the housing markets and thus reducing private consumption. This policy mix should leave Korea's twin imbalances (a large current account surplus and higher inflation) unresolved.

  This scenario implies higher GDP growth than our baseline case, but policymakers will eventually need to choose between either higher CPI inflation or won appreciation.

Higher rates and a weaker won could fail to contain inflation through the exchange rate channel

- **Excess liquidity and asset price inflation:** On the other hand, if the authorities allow won appreciation faster than we forecast against the backdrop of better-than-expected global economy growth and the BoK maintains much lower policy rates than our forecast (perhaps concerned about a stronger won), this would create ripe conditions for domestic financial asset price inflation.

  In this scenario, GDP growth would be higher than our baseline assumption, but protracted low interest rates, in association with high competition in the financial sector, risks adding to even higher financial leverage, making the economy vulnerable to a potential inflation shock. Furthermore, the creation of market expectations of protracted low interest rates would risk generating new types of bubbles. For example, carry trade opportunities would help bring down long-term government bond yields, which in turn could fuel speculative demand for corporate bonds. A further concern is that already highly leveraged SMEs and self-employed

Faster appreciation of the Korean won might delay policy rate hikes further

households could obtain even more leverage on the back of the government support and low interest rates, which could lead to an eventually massive adjustment when the BoK is forced to hike rates later on.

Korean won being regarded as a "risky" currency from an overseas investment perspective can help offset wider macro risks

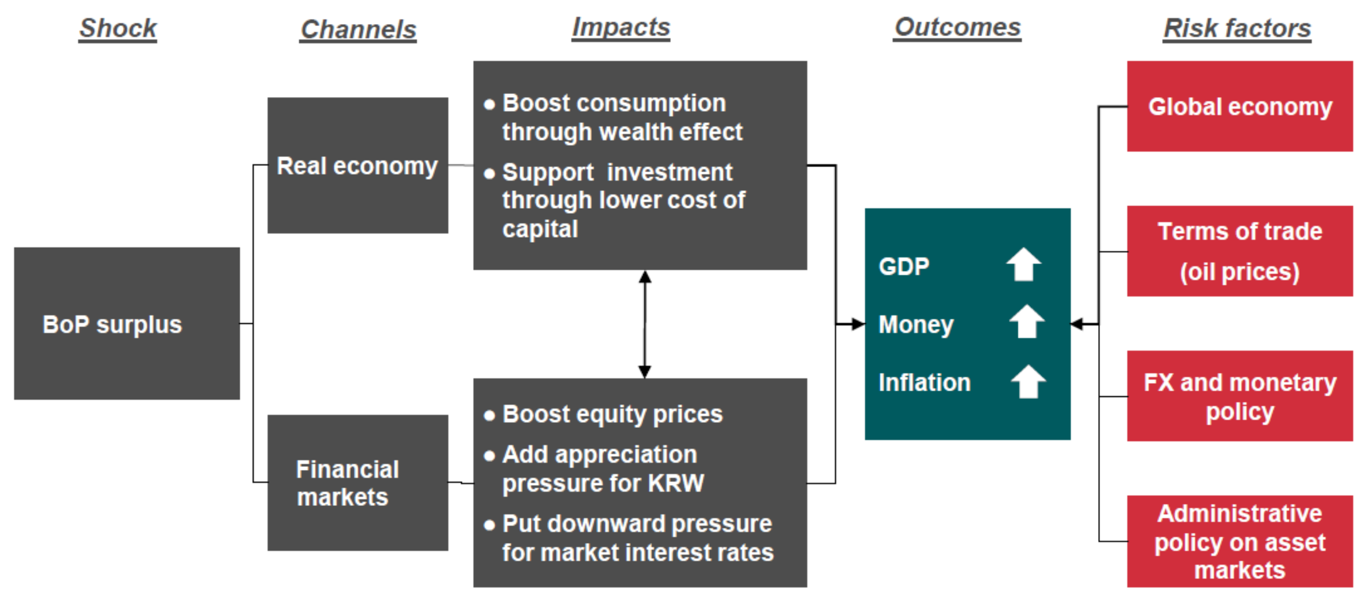
- **Automatic offsetting macro risks:** Although many Korean manufacturers are globally competitive, the Korean won is regarded as a "risky" currency from an overseas investment perspective. This can, to some extent, help offset wider global macro risks. For example, a relapse in G3 economies would have a negative impact on Korea's economy, but lower oil prices and stronger Yen/weaker Korean won should help to cushion the impact after the initial shock. In this scenario, GDP growth would be lower than our forecast, but a strong recovery would likely follow thereafter.

Although geopolitical tension in the Korean peninsular has re-emerged, a major escalation is unlikely, in our view

- **Geo-political risks:** Despite recent North Korean provocation, we still view a major escalation of geopolitical tensions on the Korean peninsula as a low probability, but admittedly high-risk event. If geopolitical risks persist or escalate further, we expect them to negatively affect domestic demand since it would hurt business and consumer sentiment. As a result, we expect Korean policymakers to do "whatever it takes" to calm market volatility and concerns. The most important policy response, in our opinion, is aimed at preventing sovereign credit rating downgrades due to geopolitical risks and to provide sufficient US dollar and Korean won liquidity in the market.

We believe that any good news could trigger a market turnaround, given Korea's solid economic fundamentals and attractive valuations. Indeed, over time there should be some offsetting factors: a weaker won should sharpen Korean export competitiveness, as it did in late 2008 and early 2009. Also, potentially lower oil prices should help improve the terms of trade (Korea is one of Asia's largest net importers of oil when scaled by GDP) and limit inflationary pressures, therefore offering room for policy responses. Nomura's GEMaRI (The Global Emerging Market Risk Index) measures the risk that a currency crisis – defined as a three-standard-deviation movement in a currency – will occur in the next 12 months. Korea's GEMaRI score was the lowest in Asia in 3Q10 due to large FX reserves and sound fiscal position.

Exhibit 10. Impact of balance of payment surplus to the economy and financial markets



Source: Nomura Global Economics

Exhibit 11. Korea macro forecast

% y-y growth unless otherwise stated	3Q10	4Q10	1Q11	2Q11	3Q11	4Q11	1Q12	2Q12	2010	2011	2012
Real GDP (sa, % q-q, annualized)	3.0	(0.4)	4.1	4.9	5.3	4.5	4.9	4.9			
Real GDP (sa, % q-q)	0.7	(0.1)	1.0	1.2	1.3	1.1	1.2	1.2			
Real GDP	4.4	4.2	3.1	2.9	3.4	4.7	4.9	4.9	5.9	3.5	5.0
Private consumption	3.3	3.6	4.0	4.0	3.8	3.6	3.3	3.6	4.2	3.8	3.5
Government consumption	2.8	6.2	1.4	2.3	4.1	4.1	5.1	5.1	4.0	3.0	5.4
Business investment	24.3	19.1	17.4	9.8	5.1	6.1	6.1	5.1	25.5	9.3	6.9
Construction investment	(2.3)	(2.6)	(4.1)	(0.5)	(2.3)	(0.3)	0.5	1.0	(1.2)	(1.8)	1.7
Exports (goods & services)	11.1	11.1	9.5	4.2	4.3	7.6	7.6	8.1	13.2	6.4	8.4
Imports (goods & services)	14.7	14.4	11.8	6.1	5.8	7.8	6.8	7.3	17.2	7.8	7.9
Contributions to GDP growth (% points):											
Domestic final sales	3.4	3.8	3.6	3.0	2.7	3.2	4.1	4.0	4.5	3.0	3.6
Inventories	1.8	0.9	(0.1)	0.4	1.1	1.1	0.0	0.0	2.0	0.7	0.7
Net trade (goods & services)	(1.2)	(0.5)	(0.4)	(0.5)	(0.3)	0.4	0.7	0.9	(0.6)	(0.2)	0.7
Unemployment rate (sa, %)	3.6	3.4	3.3	3.4	3.4	3.3	3.2	3.2	3.7	3.3	3.2
Consumer prices	2.9	3.6	3.8	4.0	3.8	3.2	3.1	3.0	2.9	3.7	3.0
Current account balance (% of GDP)									3.5	1.8	0.9
Fiscal balance (% of GDP)									(1.9)	(0.2)	0.4
Fiscal balance ex-social security (% of GDP)									(2.6)	(2.1)	(1.1)
Money supply (M2)	9.0	8.0	8.0	8.5	9.0	9.5	10.0	10.0	9.0	9.0	11.0
House prices (% q-o-q)	(0.1)	0.3	0.6	0.6	0.4	0.4	1.0	1.0	1.2	2.0	3.0
BOK official base rate (%)	2.25	2.50	2.50	2.75	2.75	3.00	3.25	3.25	2.50	3.00	3.25
3-year T-bond yield (%)	3.37	3.20	3.20	3.30	3.40	3.50	3.60	3.70	3.20	3.50	3.70
5-year T-bond yield (%)	3.76	3.90	3.90	4.00	4.10	4.20	4.30	4.30	3.90	4.20	4.30
Exchange rate (W/US$)	1,180	1,110	1,080	1,060	1,040	1,020	1,005	990	1,110	1,020	960

Note: Numbers in bold are actual values; others forecast. Interest rate and currency forecasts are end of period; other measures are period average. All forecasts are modal forecasts (i.e., the single most likely outcome). Table last revised 6 December, 2010.

Source: Bank of Korea; CEIC and Nomura Global Economics.

Geopolitical risks

Alastair Newton, Senior Political Analyst

North Korea: Brinkmanship Returns To The Korean Peninsula[1]

The sinking in late March of the South Korean corvette, the Cheonan, notwithstanding, more recent events in Pyongyang, including the emergence into the limelight of Kim Jong-un as the heir apparent to Kim Jong-il, had led us to hope that North Korea might prove less troublesome in the weeks and months ahead than was the case in the first half of this year.[2] We were further encouraged in this view by some softening in tone and stance from South Korea relative to President Lee Myung-bak's abandonment of the "sunshine policy" after he was sworn in as president in 2008. However, a series of events in November has clearly underlined that North Korea remains a major threat to regional stability.

First, press reports (which, admittedly, have been around for several weeks) resurfaced that North Korea may be making preparations for a third nuclear test.[3]

Second, the press reported in mid-November that North Korea has built and may be operating "hundreds and hundreds" of uranium enrichment centrifuges.[4]

Third, on 23 November North Korea fired "dozens" of artillery rounds towards the South Korean island of Yeonpyeong near the disputed western maritime border, some of which landed on the island. South Korea, which was conducting a military drill in the area at the time, returned fire.

Although border clashes are far from unprecedented since the 1953 armistice on the Korean peninsula, this third incident is, in our view, very serious not least since, unlike the sinking of the South Korean warship the Cheonan in March, it is an undeniable act of aggression by North Korea. Indeed, by some measures it can be seen as the most serious North Korean offensive action since the armistice.[5]

The motivation for North Korea's latest malfeasance remains unclear. We certainly do not rule out the possibility that it was designed in part at least to smooth the accession of Kim Jong-un. Equally, possible preparations for a nuclear test, the revelation of the uranium enrichment facility and this latest incident could all be North Korea, anticipating an early return to the negotiating table, resorting to its long-established practice of looking to extort concessions from the international community in return for better behaviour.

What was clear from the public statements of Lee Myung-bak at the time of the attack was that Seoul did its best to prevent the situation from escalating further and to try to defuse tensions. However, as the criticism of some opposition politicians in South Korea makes clear, the South Korean government needed to make a sterner response of some sort.

The initial iteration of this was the President's 29 November statement that North Korea "would pay the price in the event of further provocations"; and that tolerance would "spawn nothing [from North Korea] but serious provocations". Then on 3 December South Korea's new defence minister, Kim Kwan-jin, announced changes to the rules of engagement in the event of a further North Korean attack, including airstrikes. What impact this will have on thinking in Pyongyang remains to be seen.

[1] See also our report of 26 May 2010 of the same title, ie "Brinkmanship returns to the Korean peninsula", Nomura International (HK) Limited, 26 May 2010.
[2] See also "North Korea: Through A Glass Darkly", Nomura International plc, 2 June 2010.
[3] See, eg, "North Korea ready for third nuclear test, says report", The Guardian, 21 October 2010.
[4] "North Koreans Unveil Vast New Plant for Nuclear Use" by David E Sanger, The New York Times, 20 November 2010 – available at http://www.nytimes.com/2010/11/21/world/asia/21intel.html?_r=2&hp.
[5] That said, we would argue that at least in terms of loss of life the sinking of the Cheonan (in which 46 sailors died) and the downing of a South Korean airliner by a North Korean terrorist bomb in 1988 (in which all 115 people on board were killed) were more serious.

Although these statements unsettled markets (which had calmed significantly within 24 hours of the artillery exchange but which remain nervous), we judge that, in terms of domestic politics, the South Korean government had little choice but to return to the firmer stance with North Korea which Lee Myung-bak had pursued (and been criticised for at home) up to the time of the Cheonan sinking. And we note that South Korea's revised stance is consistent with the criticism of North Korea's action by much of the international community including three of the other five participants in the six-party talks. Effectively, though, this marked an end of "sunshine" policy and a return by South Korea to "sunset policy".

Tensions were further fuelled last week by the arrival in the Yellow Sea (ie the area where the artillery exchange took place) by a US carrier group which was conducting joint exercises with the South Korean navy; and by this week's South Korean live-fire navy drills. We believe that the former in particular will not have been well-received by the Chinese; but it may also have encouraged China's calls for an early round of informal talks among the participants in the six-party negotiations – which has, so far, to receive more than a cautious response from others. Indeed, the US's position remains, for now at least, that it will not resume formal negotiations unless or until North Korea comes up with concrete proposals to dismantle its nuclear facilities.

In such circumstances, we cannot rule out further malfeasance by North Korea including a third nuclear test and/or missile tests (including the medium-range Taepoodong 2), which would likely further unsettle South Korean – and, possibly, wider Asian – markets further.

One piece of good news is that, following the revelations about North Korea's uranium enrichment facility, the US Special Envoy for North Korea, Stephen Bosworth, was already in the region and engaged with Beijing, Seoul and Tokyo. This should help bring a coordinated response from participants in the six-party talks to bring appropriate pressure to bear on Pyongyang to de-escalate. However, China's ability to rein in Pyongyang should not be over-estimated, especially given that North Korea would likely have calculated (rightly, in our view) that its actions would infuriate and embarrass Beijing.

Thus, even if we do see a speedy calming of tensions on the Korean peninsula and return (in some form) to the negotiating table, these latest events suggest to us that, whatever incentives the international community offers, Pyongyang is likely to remain (a) intransigent over abandoning its nuclear capabilities and aspirations; and (b) a potential de-stabiliser in the region for the foreseeable future.[6]

[6] *As we have noted in previous updates of "Issues", the focus of six-party talks to date has been largely on the North Koreans' plutonium producing facilities at Yongbyon despite the fact that the international community has long considered that Pyongyang's willingness to suspend operations there (and even to begin dismantling the installation) was premised in part at least on their claims to be making progress with uranium enrichment. If, indeed, these latest press reports are accurate it appears that North Korea may be considerably further advanced in producing potentially weapons-grade nuclear material by this latter route than had previously been suspected.*

Korea equities in 2011

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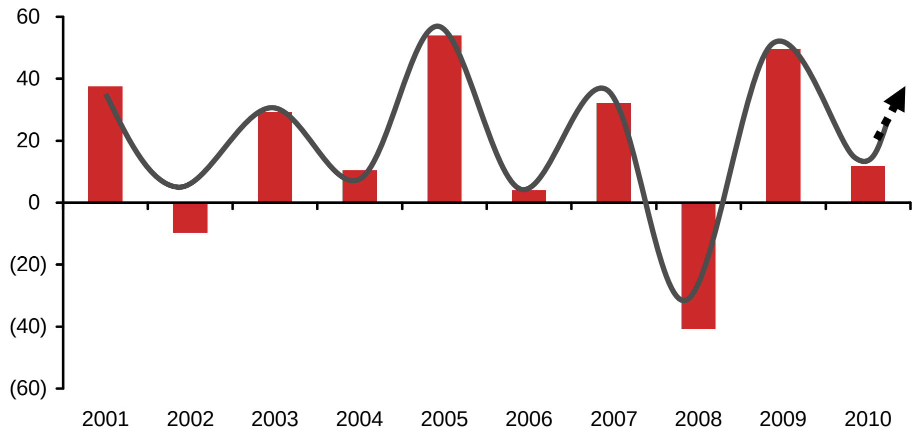
We expect the Korean market to continue to rise in 2011 on the back of continued earnings growth and favourable liquidity conditions. Although uncertainties remain about the global economic recovery in many developed economies, Korean companies' earnings should post positive earnings growth owing to their high exposure to emerging markets, which should continue to show better economic growth in 2011. Retail Investors' sentiment towards equities is expected to improve further in 2011, as the housing market stabilises.

Are we heading into a better year?

Exhibit 12. Kospi annual return (%)

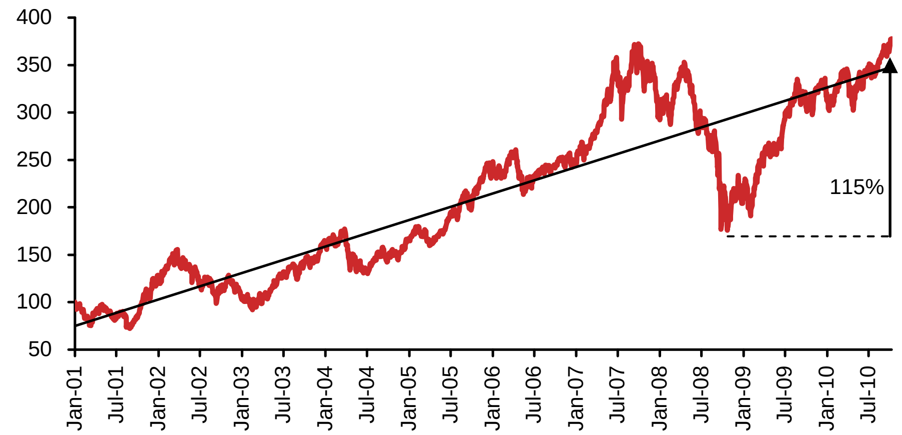


Source: CEIC; Nomura International (Hong Kong) Limited – Investment Strategy

While total market capitalisation of equities has recovered to its previous peak in 2007 there are no signs of a bubble in the economy or in equity markets. In contrast to many other Asian markets, which have seen substantial coincident rises in property and equity markets at the same time, the Korean property market has been subdued over the past year. Equity markets also don't appear overheated as equity prices have been led by earnings growth rather than multiple expansion.

Although the Kospi has risen 115% since the bottom…

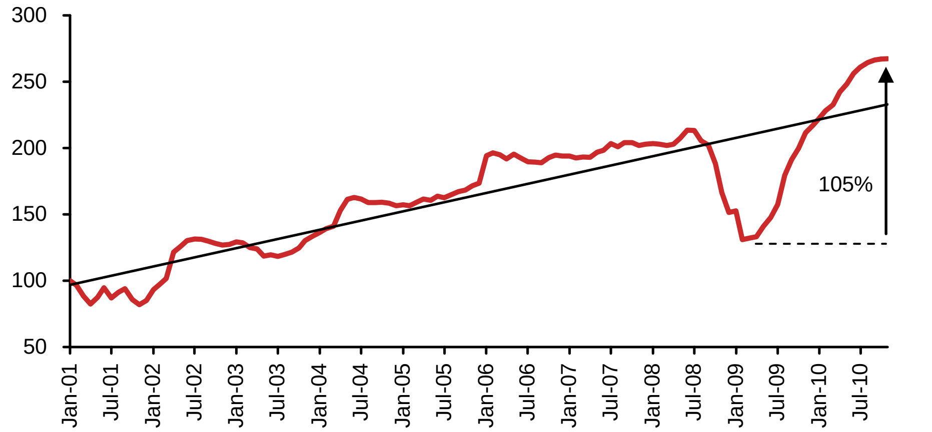
Exhibit 13. MSCI Korea (local currency)



Source: MSCI, Nomura Strategy Insight, Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 14. MSCI Korea 12-month forward earnings

…most gains are supported by earnings growth rather than multiple expansion. Equities remain inexpensive



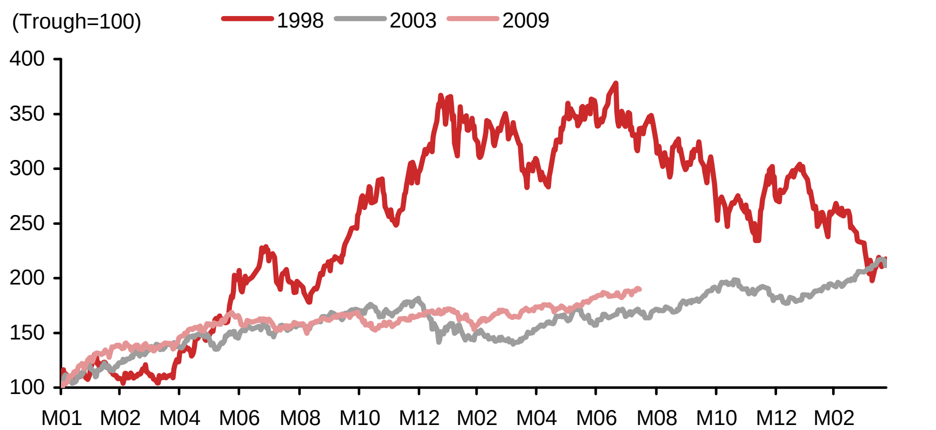
Source: MSCI, Nomura Strategy Insight, Nomura International (Hong Kong) Limited – Investment Strategy

We summarise our view on Korean market in 2011 as follows:

- **Favourable liquidity conditions continue:** Backed by loose monetary conditions in the US and Japan, global liquidity remains favourable. While the Korean central bank will normalise monetary policy from an extremely loose state, we don't expect this to undermine equity returns since US long bonds are likely to be well behaved.
- **Weaker momentum but earnings continue to grow:** Although Korean companies' earnings momentum is expected to remain weak in 1H11, the upward swings in lead indicators in China and the US suggest the risk of a double dip is receding. Although a subpar recovery in developed economies will continue, Korean companies geared to EM should have better earnings momentum.
- **Margin pressure by rising commodity prices:** With commodity prices set to rise further, companies' margins are expected to deteriorate in 2011. Our Nomura oil & gas analysts forecast oil prices will rise alongside other basic material prices. This will also be well supported by continued growth in the global economy as well as a reflationary macro environment. We don't expect the won to strengthen enough to offset rising import prices fully.
- **A return of local funds to equities:** Compared to strong fund inflows by foreign investors, retail investor sentiment remains weak. Despite extremely low borrowing costs, Korean households continued to deleverage as housing markets remain depressed. While we believe the housing market is near its bottom, rising price expectations should be the key to redirecting local investors' fund flow into equities.

Exhibit 15. Kospi index trend after historical troughs

It appears the Kospi is on the track seen after the 2003 trough



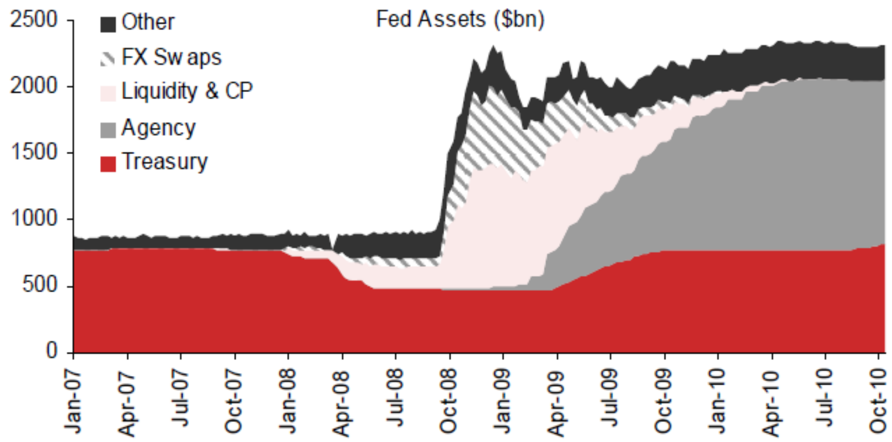
Source: Bloomberg, Nomura International (Hong Kong) Limited – Investment Strategy

Favourable Global and Korean monetary conditions

With the second round of quantitative easing, global liquidity conditions will remain favourable for financial assets. By announcing US$600bn of US treasury securities purchase plans, the Fed once again signalled the market that it would do whatever it takes to keep the US economy from falling into deflation or losing recovery momentum. While the Fed's purchase program is planned to continue until the end of 1H11, dollar liquidity should remain ample. Furthermore the BoJ also has set up an asset purchase programme of ¥1.5tn and has explicitly stated target inflation.

With QE2 announcement, the Fed's balance sheet is once again set to expand…

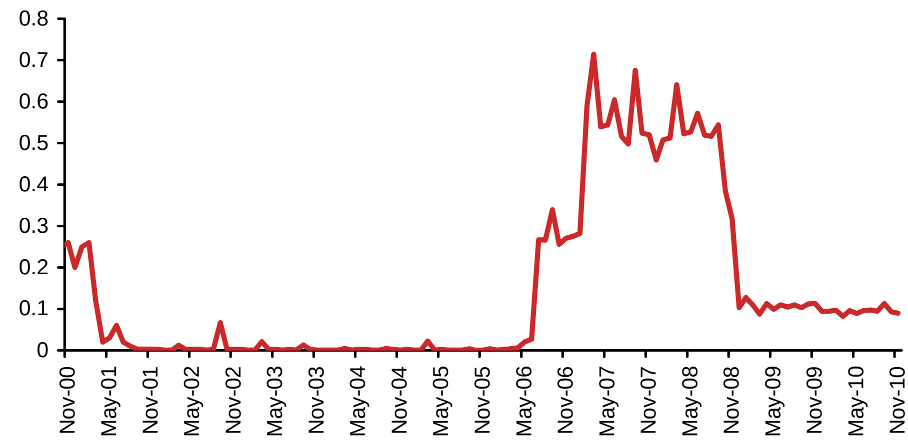
Exhibit 16. US Fed balance sheet



Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

…and BoJ has retuned to zero-interest rate policy (ZIRP) and will likely purchase JGBs outright

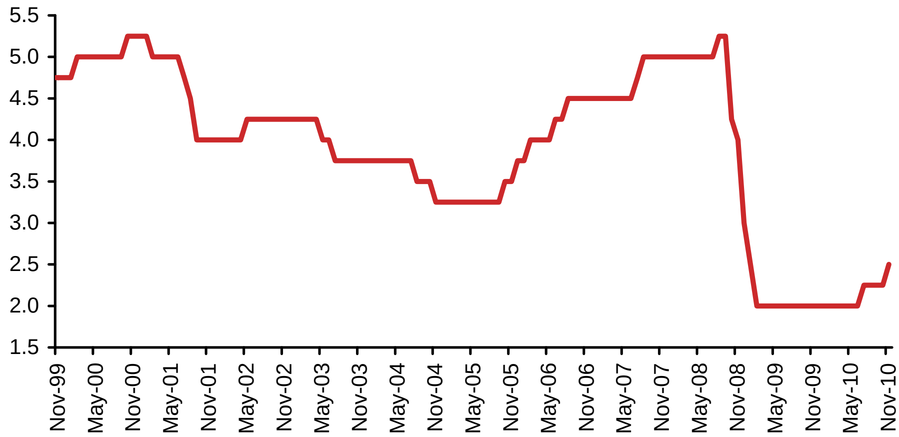
Exhibit 17. Japan policy rates % pa



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

Turning to domestic liquidity conditions, the BoK has started to resume its policy rate hike cycle by raising by 25bps in November. While the BoK's rate hikes appears to be far slower than discounted by the swap curve, we don't expect it will affect equity markets for the short team. First, historically equity returns tend to be correlated with real policy rates. Secondly, rising expectations of inflation come ahead of rate hikes. If price expectations rise, Korea financial markets will be likely to see funds flowing out of bond markets into equities. The fixed income market should provide support to the equity market after it had seen substantial money inflow in 2010 at a time when interest rates have been kept extremely low.

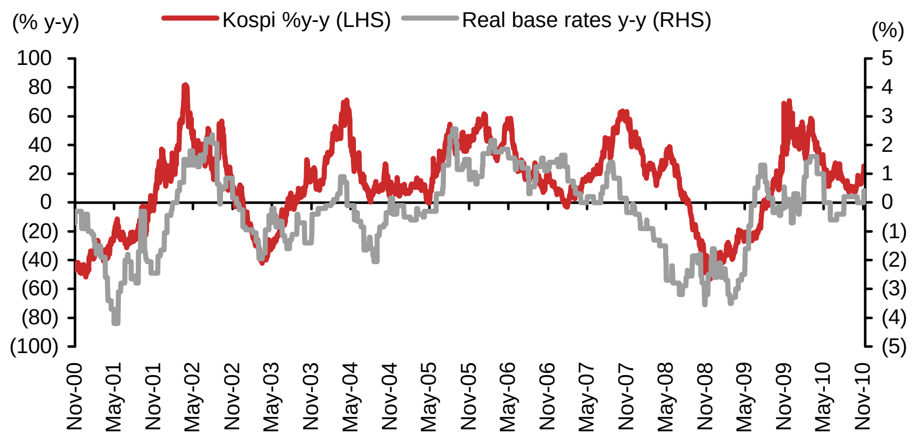
Exhibit 18. Korea: policy rates



Source: CEIC; Nomura International (Hong Kong) Limited – Investment Strategy

Policy rates remain extremely low and authorities will take more time to normalise these as they put growth over containing inflation

Exhibit 19. Kospi vs real policy rate changes



Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

Real policy rate changes and equity market returns are highly correlated

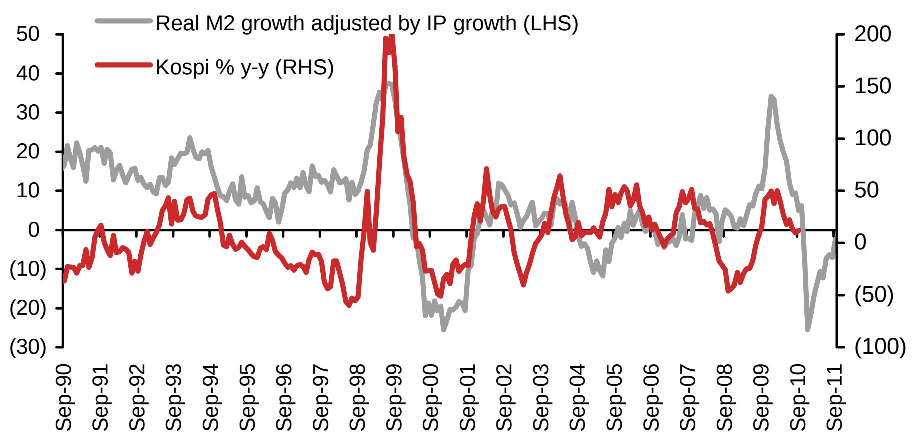
With numerous lead indicators having turned, we see little in the way of real economy activity competing for money supply at the moment. Industrial production growth has slowed while money supply growth has held up well, leaving more excess liquidity in the economy. Good for financial assets.

Little competition for money from the real economy

While the money multiplier remains resilient, any improvement in the velocity of money would result in domestic liquidity overflowing into financial assets as demand from the real economy is expected to remain subdued until economic activities start to gain momentum again. There is no real economic activity or alternative investments to compete for money inflow in the Korean domestic market at the moment.

Excess liquidity measured by the difference between M2 and industrial production suggests that Kospi performance should be well supported

Exhibit 20. Korea: real M2 growth %y-y vs Kospi %y-y

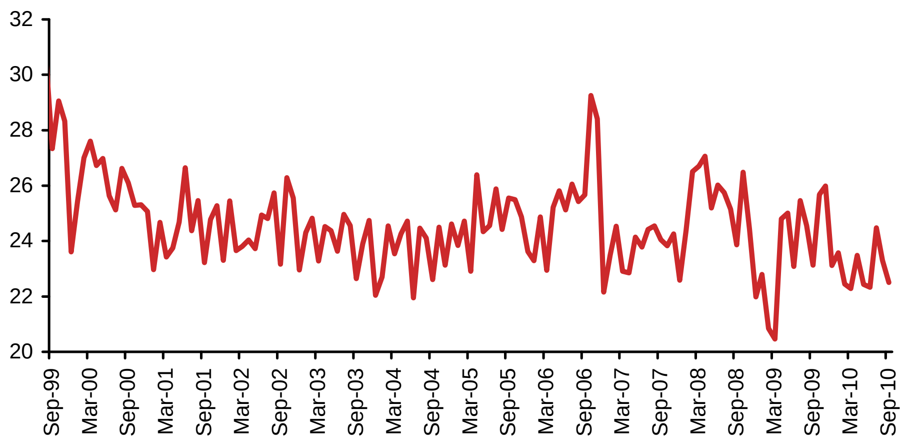


Note: Kospi performance one year lag

Source: CEIC; Nomura International (Hong Kong) limited – Investment Strategy

The money multiplier is resilient

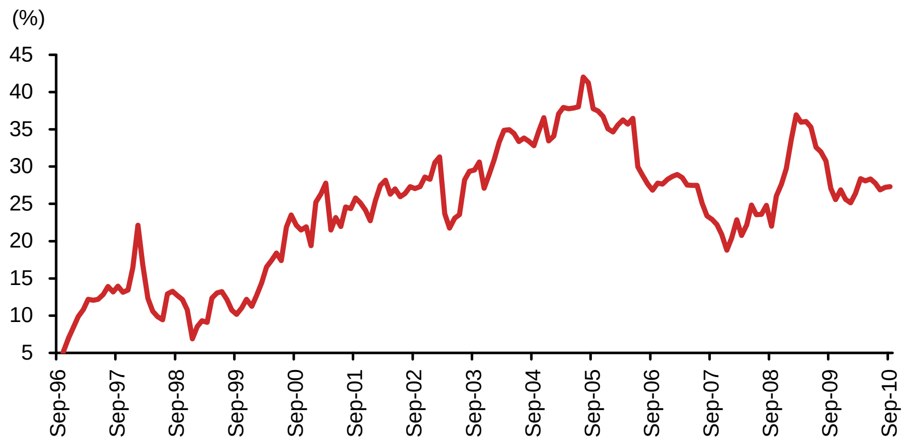
Exhibit 21. Korea: M2/ reserve money



Source: CEIC; Nomura International (Hong Kong) limited – Investment Strategy

With an extremely low level of MMF returns, MMF balance appears high…

Exhibit 22. Korea: MMF (as % of total investment fund assets)



Source: CEIC; Nomura International (Hong Kong) Limited – Investment Strategy

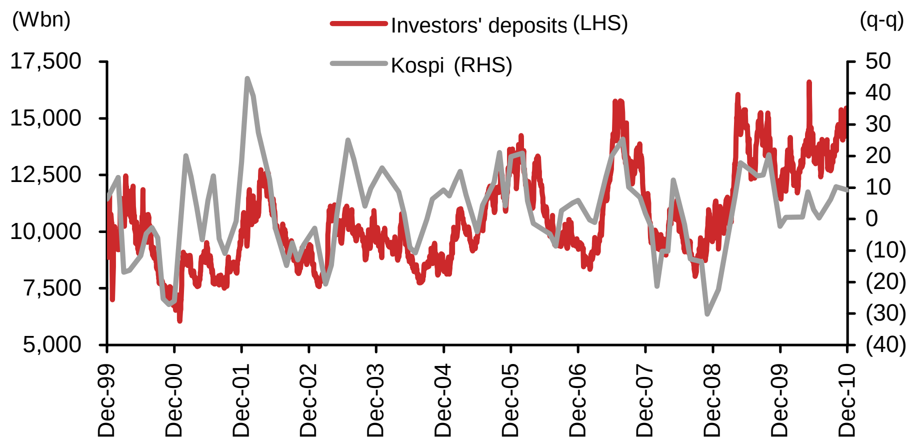
Exhibit 23. Korea: bank deposits to equity and bond market cap

...so do bank deposits

Source: CEIC; Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 24. Korea: investors' deposits held in investment companies vs Kospi performance

Investor sentiment has already moved towards equities



Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

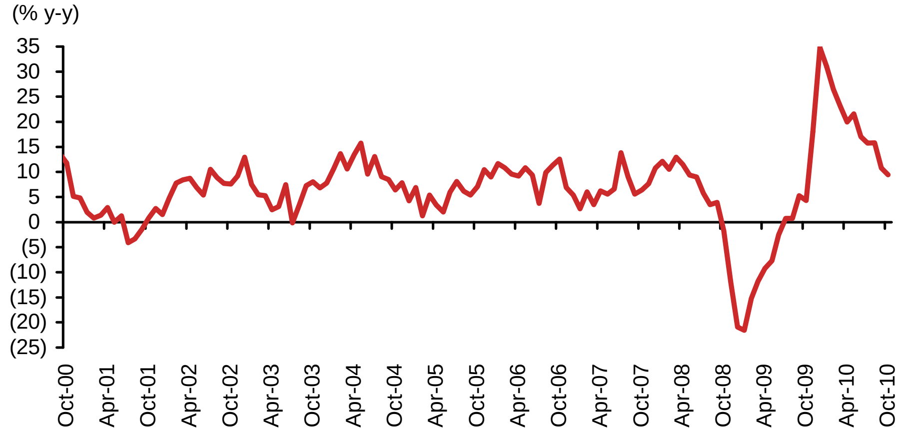
Weaker momentum but earnings continue to grow

In 2010, Asian economies grew 7.9%, in contrast to developed markets (Americas 3.7% and Euro area 1.7%). On the back of this, Korean equities proved that they are major beneficiaries of emerging economies and many companies reached record earnings during 2010. However, a number of lead indicators are still signalling relatively sluggish economic momentum since many economies have naturally cooled after the dramatic recovery.

We expect earnings momentum to remain weak until 1H11 since Christmas orders from advanced economies have hardly given any exuberance to Korean manufacturers. Korean IT sectors continue to flag excess inventories in the US channel. Cargo data suggests sales growth may prove more resilient, but one thing to bear in mind is that companies have cut prices in an attempt to flush out excess inventories.

Exhibit 25. Korea: industrial production

Earnings momentum has sharply turned…

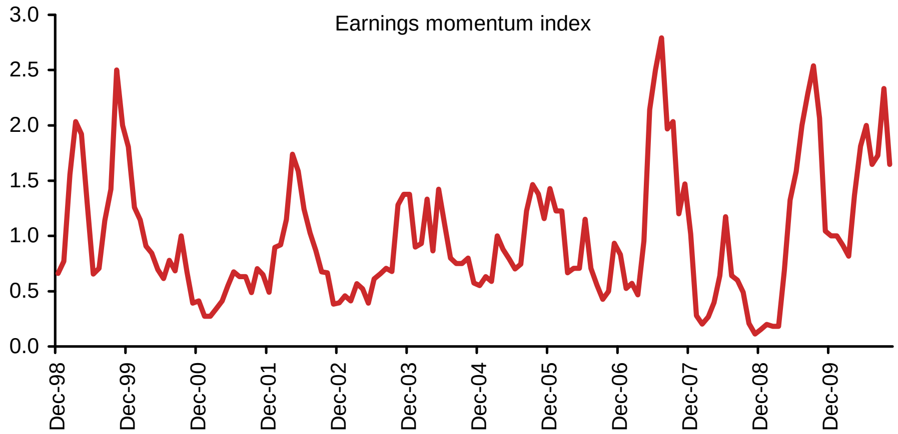


Source: CEIC; Nomura International (Hong Kong) Limited – Investment Strategy

However, companies' earnings forecasts were cut over the one quarter or so when a double-dip scare gripped investors. We believe a weaker economic environment has been largely priced in, as we can see underperformance of major manufacturers.

Exhibit 26. Korea earnings momentum index

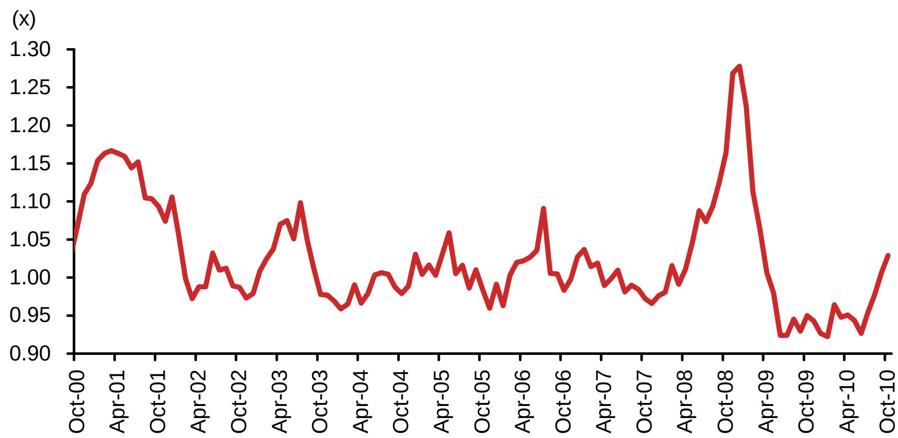
Korean earnings momentum has been weakening…



Source: Nomura International (Hong Kong) Limited – Quantitative strategies

Exhibit 27. Korea producers' inventories-to-shipment ratio

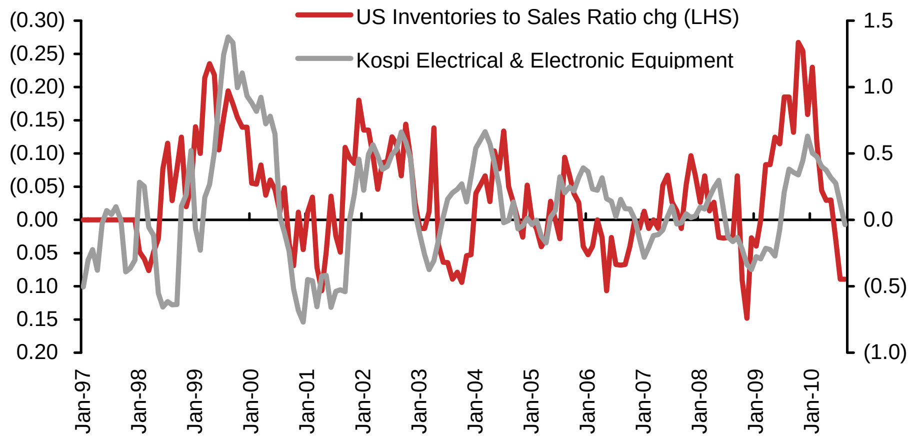
…while inventories are rising



Source: CEIC; Nomura International (Hong Kong) Limited – Investment Strategy

A careful watch should be kept on US inventories-to-sales

Exhibit 28. US inventories-to-sales ratio inverted vs Kospi IT sector performance



Source: CEIC; Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

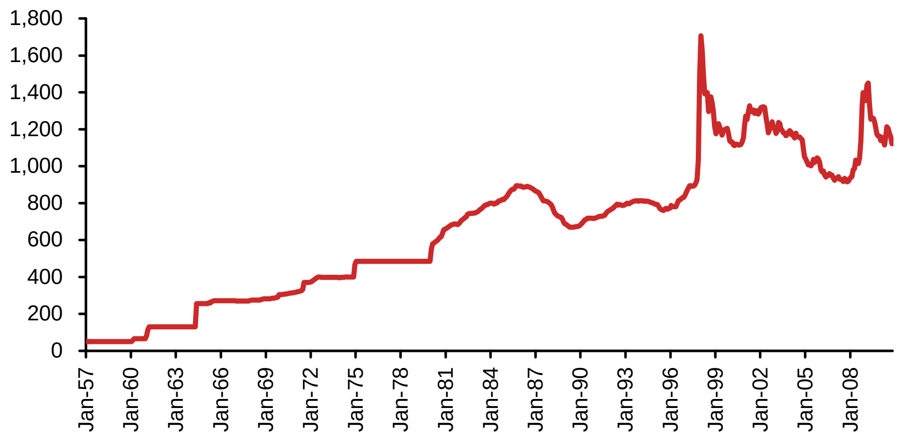
US dollar is expected to continue to weaken…

Exhibit 29. US Trade Weighted Broad Dollar index

Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

…suggesting a stronger won may hamper market-share gains by Korean companies

Exhibit 30. Korean won exchange rates against US dollar

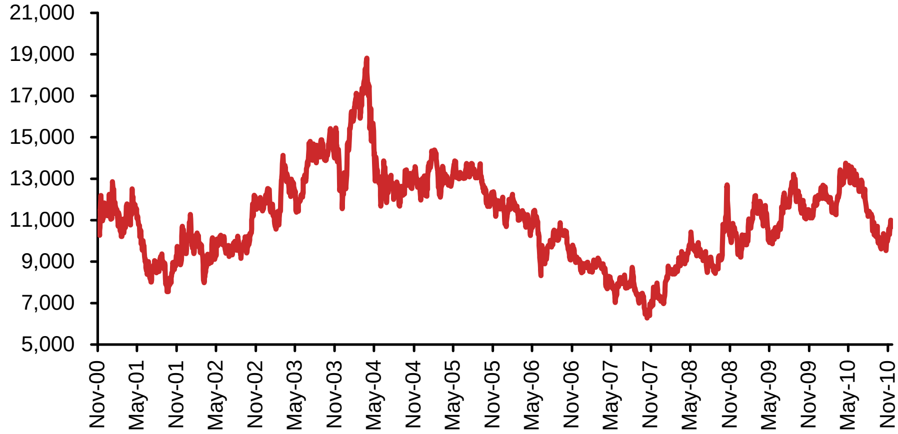


Source: CEIC; Nomura International (Hong Kong) Limited – Investment Strategy

While exporters' earnings momentum has been weakening, the recent record earnings of some retailers would suggest that the fruit of economic recovery has been distributed from exporters to domestic-focused companies. Indeed, investors began to rotate out of the Korea's major export sectors in mid-2010 and domestic-focused industries such as Service and Wholesale outperformed substantially.

Exhibit 31. Kospi: electrical & electronics relative to wholesale

Sector rotation out of Tech began in mid-2010



Source: Thomson Reuters Datastream, Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 32. Kospi: electrical & electronics relative to service

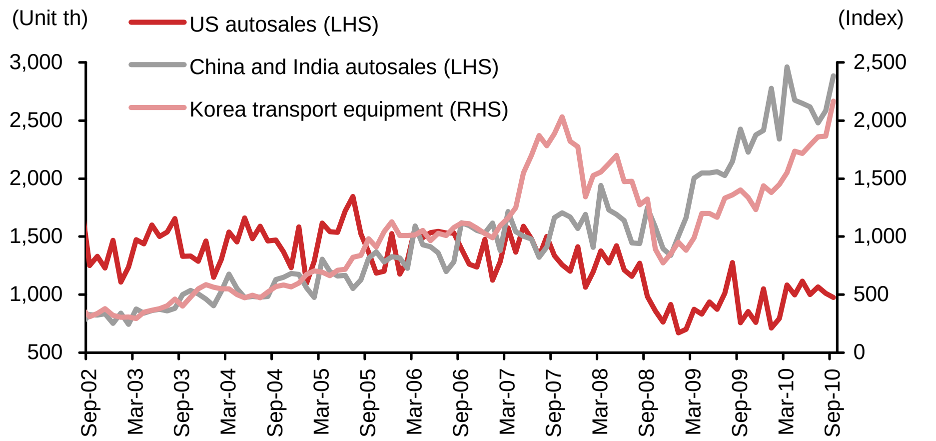
However, as the global economy continues to grow, we believe the Technology sector's underperformance to the Domestic-focused sector is overdone

Source: Thomson Reuters Datastream, Nomura International (Hong Kong) Limited – Investment Strategy

We believe the underperformance of the technology sector has been overdone and it will likely start normalising as global economic growth expands as seasonal factors reverse. The sector is significantly under-owned while valuations appear cheap.

We continue to believe companies geared to emerging markets are better positioned to benefit from ongoing decoupling in global economies. Growth momentum amongst companies in the same sector should diverge, depending on whether the company has been able to gain presence in the emerging markets.

Exhibit 33. Kospi: transport equipment vs US auto sales vs China India auto sales



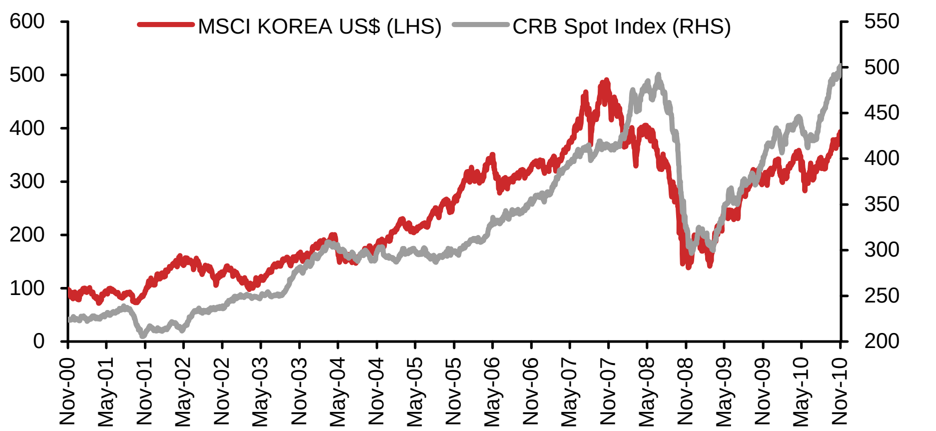
Source: CEIC; Nomura International (Hong Kong) Limited – Investment Strategy

We believe the Korean Auto sector is better positioned as it is more geared to emerging market growth while market-share gains in developed markets limit downside to earnings

Margin pressure by rising commodity prices; watch oil prices

With a weaker US dollar supporting overall commodity prices, Korean companies will likely see substantial pressure rising on margins as terms of trade is set to deteriorate. A strengthening Korean won would be able to offset some of the impact from rising input cost, but oil prices are expected to rise to US$100/bbl by end-2011, implying margin pressure is unavoidable.

Exhibit 34. MSCI Korea US$ vs CRB index

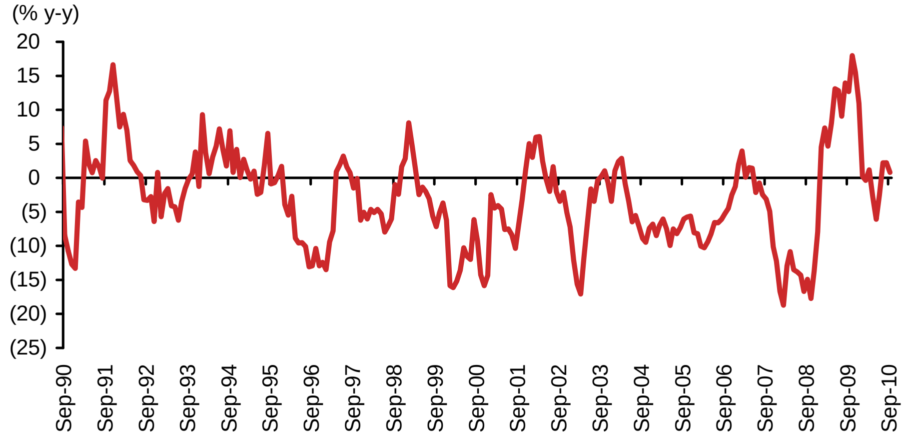


Source: CEIC, Thomson Reuters Datastream, Nomura International (Hong Kong) Limited – Investment Strategy

Due to its cyclical aspect, Korean equity markets are correlated with rising commodity prices for the short run

Exhibit 35. Korea: terms of trade index

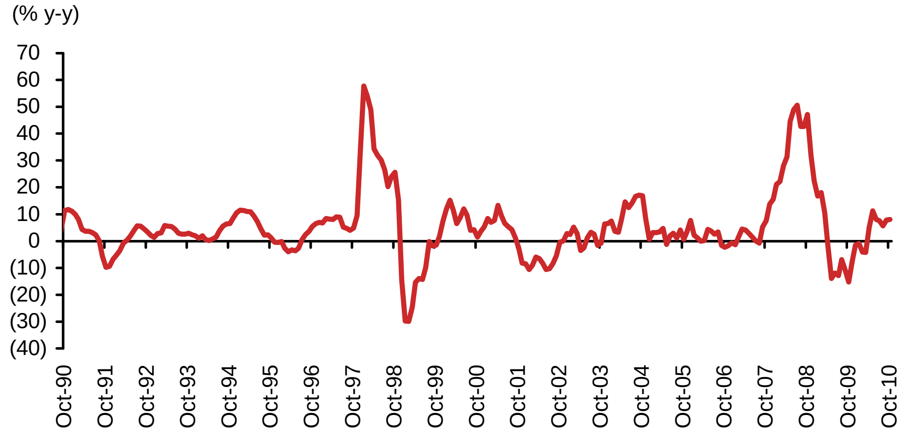
Korean terms of trend sharply deteriorated in 3Q10…



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 36. Korea: import prices

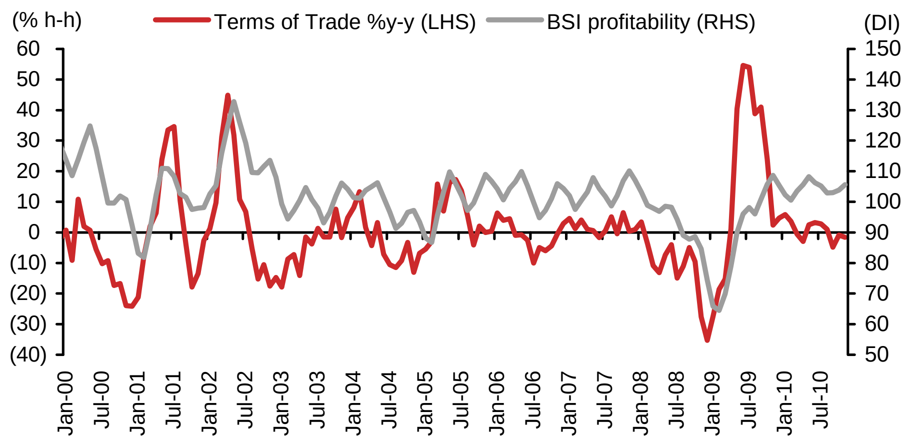
…and import prices are rising



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 37. Korea: terms of trade vs profitability

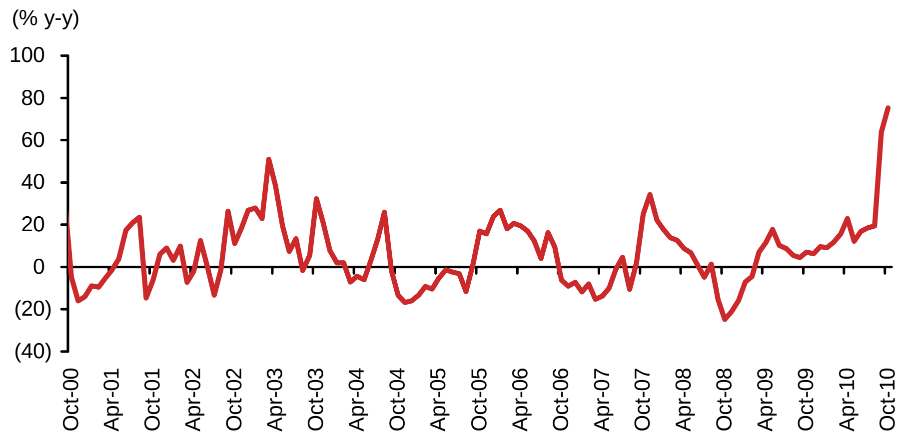
Korean companies profitability expectations are highly correlated with changes in terms of trade



Note: profitability is business survey results (3 mma)

Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 38. Korea: CPI - Vegetables and Seafood % y-y



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

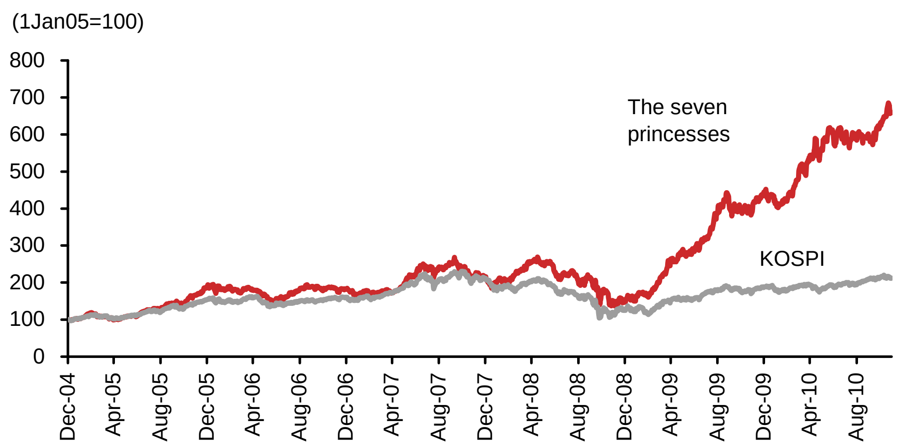
CPI inflation will be one of the major concerns of the authorities

A return of local funds to equities

We believe local domestic investors' sentiment will be the key to boosting equity markets in 2011. At first glance, there are many contradictory signals regarding retail investors' sentiment: many mutual funds are still under fund redemption pressure, while higher risk-embedded investments such as wrap accounts as well as leveraged ETFs have seen substantial fund inflows. Wrap accounts embed a higher risk due to their concentrated holdings in selected stocks. They experienced a sharp inflow after the marked outperformance of the "seven princesses" (seven stocks which are widely favoured by wrap account advisories; these are LG Chem, Hynix, Kia Motors, SEMCO, Samsung SDI, Samsung Techwin, Cheil Industries), triggering the media spotlight to fall onto these products. In turn, funds have flown into wrap accounts at quite a pace.

We believe that this signals that local investors' animal spirits are alive and when the money that flowed into time deposits over the past year starts to be relaxed broad equity markets will likely see a significant inflow by domestic investors.

Exhibit 39. Korea: the "seven princesses" vs the Kospi



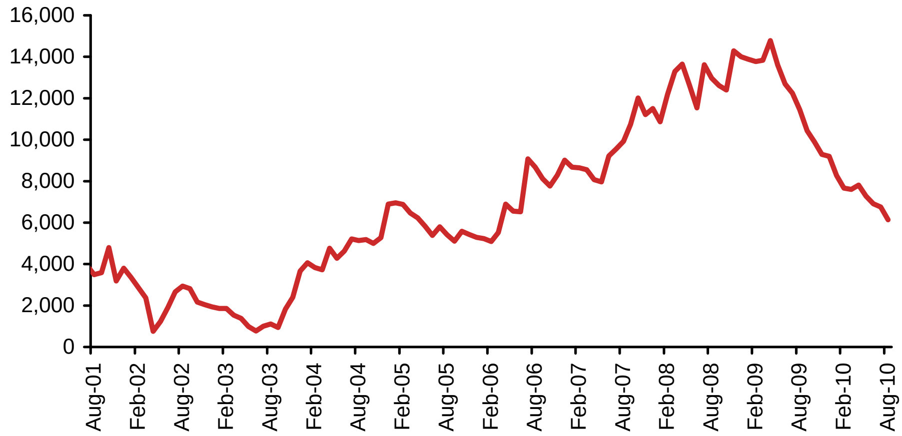
Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

Boom in wrap accounts signals local investors' risk appetite has not disappeared

Other financial asset markets are seeing reviving investor sentiment. The Korean property market has lately been one of the worst performers in the region. While other countries had to introduce regulation measures to cool down overheating housing markets, Korean authorities were more concerned about weak property prices and deteriorating transaction volume. But going into the end of 2010, property markets have begun to show some signs of stabilising and the pattern looks quite unusual as provincial areas have started to recover ahead of Seoul metropolitan area. The number of unsold apartments in Busan has been declining at a fast pace while Seoul is seeing the number pick up again. One piece of good news is that transaction volume in the Seoul area is also improving, rising recently to a 6-month high.

Exhibit 40. Korea: unsold apartment - Busan (units)

Unsold apartments have been digested rapidly in provincial areas…

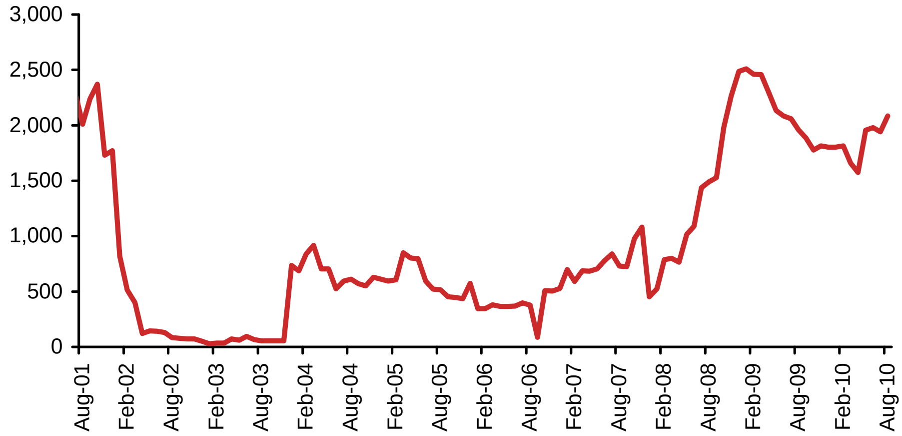


Note: Busan is the second largest city in Korea in terms of population

Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 41. Korea: unsold apartments - Seoul (units)

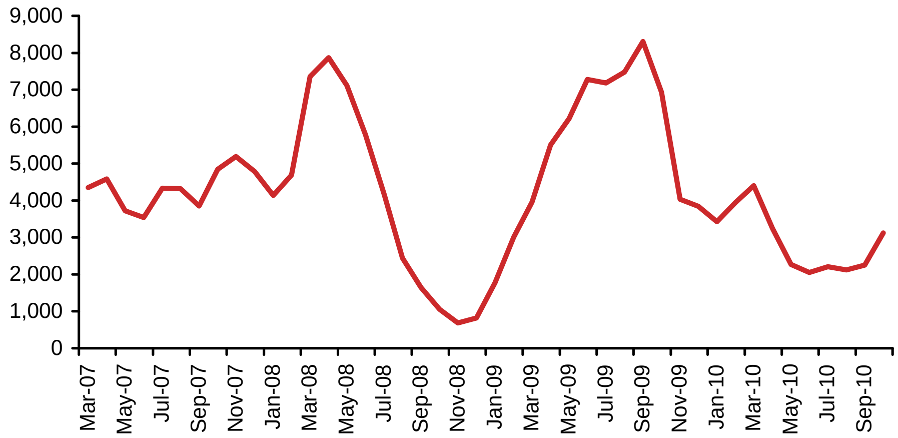
…but this is not true in Seoul



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 42. Korea: apartment transactions in Seoul

…rising transaction volume should mean the bottom is near



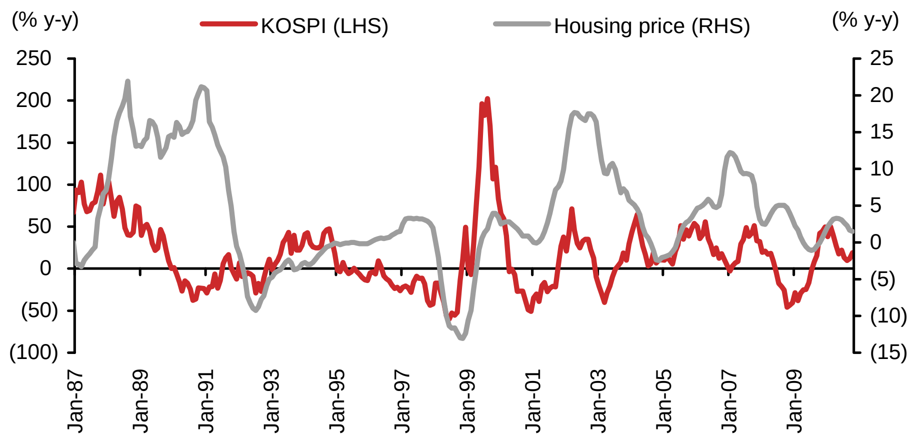
Note: number of cases

Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

With housing assets accounting for near 80% of total assets in Korea, weak property transaction volume as well as a drop in prices affects investors' sentiment directly As Korea's urbanisation rates are already high and birth rates stand at only 1.13, any sharp recovery of housing markets may be seen as bubble. The best scenario for equities should be a slow but stable recovery in the property market. If the rise in property prices accelerates, it could trigger unnecessary policy action. We believe the early recovery stage of the property market would be the best time for equities.

With property market' cycles much longer than that of equities…

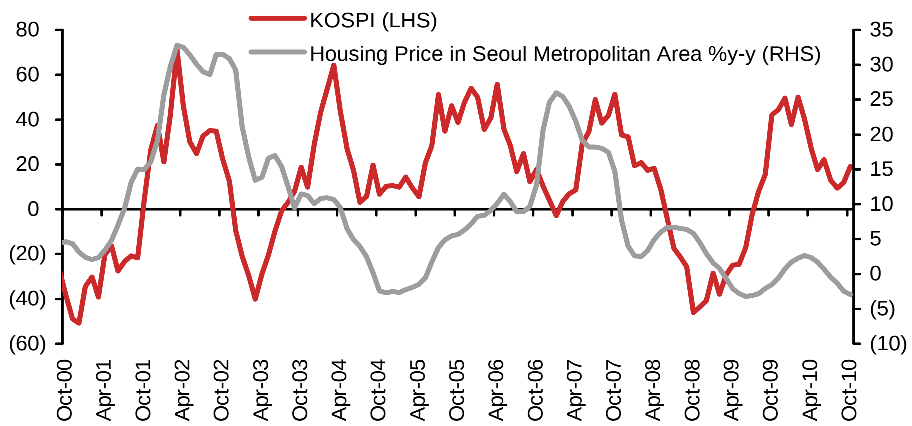
Exhibit 43. Korea: housing prices vs Kospi



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

…Korean equities appear to have decoupled from property. However, historically the early stage of recovery in the property market tends to be good for equities

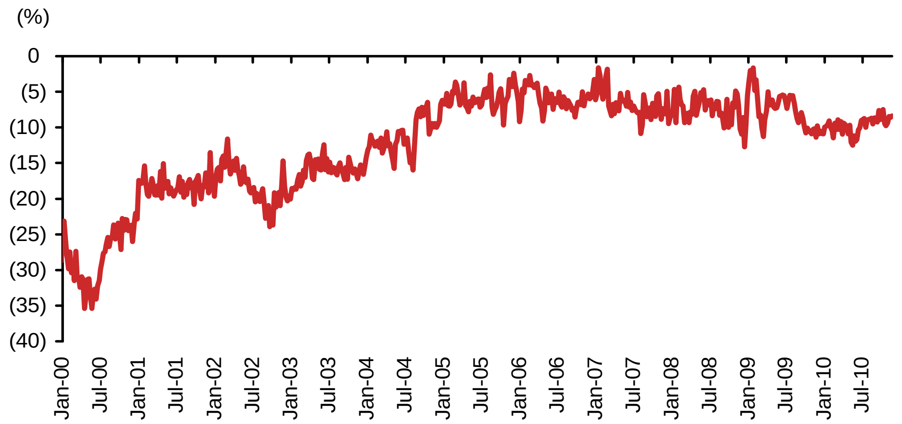
Exhibit 44. Korea: apartment prices in Seoul metropolitan area vs Kospi



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

Markets are inexpensive

Exhibit 45. Korea: closed-end fund discount to NAV % [KF US]



Source: Bloomberg, Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 46. Valuation indicators and revision indices

Country	Index universe*	P/E (x) 2010F	P/E (x) 2011F	PBV (x) 2010F	PBV (x) 2011F	P/CF (x) 2010F	P/CF (x) 2011F	P/S (x) 2010F	P/S (x) 2011F
Australia	AOI	14.2	12.1	1.8	1.7	9.8	8.5	1.5	1.4
China	CSI 300	14.9	12.5	2.3	2.0	9.7	7.4	1.2	1.0
	SHBSHR	16.2	14.9	1.8	1.7	9.1	5.5	1.5	1.4
	SZBSHR	19.6	15.8	3.2	3.1	10.1	11.4	1.5	1.2
Hong Kong	HSI	13.5	11.8	1.8	1.6	9.0	8.2	2.4	2.2
	HSCCI	13.5	12.6	2.1	1.9	7.6	6.9	2.2	1.9
	HSCEI	11.5	10.0	2.1	1.8	7.8	7.0	1.0	0.9
	HSCI	14.3	12.3	1.9	1.7	10.2	8.7	2.0	1.7
India	SENSEX	17.9	15.2	3.1	2.6	11.6	10.3	2.0	1.8
Indonesia	JCI	17.1	14.0	3.3	2.9	11.3	9.4	2.2	1.9
Korea	**KOSPI**	**10.6**	**9.4**	**1.4**	**1.2**	**7.2**	**6.8**	**0.9**	**0.8**
Malaysia	KLCI	16.5	14.5	2.3	2.1	9.2	8.6	2.0	1.9
Philippines	PASHR	14.6	13.2	2.1	1.9	8.9	9.2	2.0	1.8
Singapore	FSTAS	15.0	13.6	1.7	1.6	10.7	9.3	1.4	1.2
Taiwan	TWSE	14.2	12.5	1.9	1.8	8.9	8.2	1.0	0.8
Thailand	SET	14.1	12.0	2.1	1.9	8.4	7.6	1.0	0.9

Country	Index universe*	EPS growth (%) 2010F	EPS growth (%) 2011F	Dividend yield (%) 2010F	Dividend yield (%) 2011F	ROE (%) 2010F	ROE (%) 2011F	ROA (%) 2010F	ROA (%) 2011F
Australia	AOI	20.0	17.1	4.2	4.5	13.0	14.4	8.1	10.8
China	CSI 300	33.9	19.0	2.2	2.6	16.4	17.2	7.1	8.1
	SHBSHR	41.5	9.7	1.7	1.8	10.5	11.3	5.4	5.9
	SZBSHR	71.5	23.3	1.2	1.5	17.0	18.4	7.4	8.8
Hong Kong	HSI	29.0	14.2	3.2	3.6	13.8	14.6	7.8	8.1
	HSCCI	19.6	7.4	2.8	3.1	16.4	15.9	9.8	9.6
	HSCEI	29.4	15.4	3.3	3.9	18.8	19.4	6.5	6.9
	HSCI	30.0	14.8	2.7	3.1	13.8	14.6	7.3	7.6
India	SENSEX	11.6	18.0	1.3	1.5	18.0	18.0	9.7	10.7
Indonesia	JCI	30.1	22.4	2.2	2.7	21.2	22.6	11.2	12.6
Korea	**KOSPI**	**42.5**	**13.0**	**1.9**	**2.3**	**14.0**	**14.2**	**8.5**	**8.3**
Malaysia	KLCI	35.2	14.1	3.3	3.7	13.5	14.5	6.4	7.0
Philippines	PASHR	27.7	10.8	2.8	3.1	15.1	15.4	6.1	7.4
Singapore	FSTAS	26.5	10.9	2.9	3.0	10.3	10.8	5.7	5.7
Taiwan	TWSE	67.4	12.5	4.0	4.5	13.6	14.1	9.5	9.9
Thailand	SET	30.8	18.3	3.6	3.9	15.2	16.3	8.0	9.2

* Note that all valuation ratios are calculated using share-weighted on available I/B/E/S consensus.

For valuation calculation, companies with extreme ratios are excluded from market level aggregation.

Pricing on 30 November, 2010

Source: Bloomberg, Datastream, I/B/E/S, Nomura International (HK) Limited

Exhibit 47. Investment flows at a glance (US$mn)

Korea is one of the markets that has seen substantial fund inflows in 2010

	Mutual Funds Investing				Foreign Investing				
	4-week	12-week	YTD	2009	1-week	4-week	12-week	YTD	2009
Asia ex-Japan	3,992	12,127	19,123	19,109	1,073	7,767	33,728	56,150	59,985
India	546	3,091	5,161	5,667	468	4,198	15,928	29,006	17,591
Indonesia	314	2,186	4,090	3,975	6	-115	328	1,964	1,382
Japan	-381	-1,231	-1,842	-5,461	N/A	4,702	12,296	34,319	17,668
Korea	587	2,295	5,299	5,017	408	1,544	8,946	15,859	24,816
Philippines	359	1,047	1,653	99	-19	-33	948	1,267	137
Taiwan	406	1,165	1,176	3,423	146	2,337	6,100	6,375	14,922
Thailand	50	1,072	1,909	1,172	65	-163	1,478	1,679	1,136
Australia	293	1,663	3,030	5,301	-	-	-	-	
China	1,904	5,399	10,542	12,195	-	-	-	-	
Developed Euro	65	1,250	-10,700	2,506	-	-	-	-	
EMEA	734	2,459	5,430	2,017	-	-	-	-	
Hong Kong	507	947	1,617	1,418	-	-	-	-	
Latin America	567	3,727	1,957	8,786	-	-	-	-	
Malaysia	-43	660	1,202	457	-	-	-	-	
New Zealand	2	4	6	11	-	-	-	-	
Singapore	241	773	627	1,091	-	-	-	-	
US	1,556	14,942	-24,529	-44,349	-	-	-	-	

Note: as of 26 November, 2010

Source: Bloomberg, EPFR Global, Nomura International (HK) Ltd — Quantitative Strategies

Index

KOSPI and Earnings growth forecast

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Kospi forecast (I): Target at 2230, implying 16% upside

For the companies under Nomura coverage, we expect the aggregate earnings to rise 15%. Given that the current macro environment implies favourable sentiment, our model suggests a Kospi 2011 year-end target at 2230, implying 16% upside (as of 1 December, 2010).

We assume domestic risk free rates will rise by 25bps during 2011 and our target price-to-earnings ratio stands at 10.7x vs implied multiples at 11.1x. Our target multiple is slightly lower than implied as we believe the volatility of the Korean won has a more negative impact than currently discounted.

However, we are expecting higher earnings growth than consensus. While the earnings growth in 2011F will sharply decline from 2010F, we expect 4% and 19% growth for 2011F and 2012F, respectively, for the companies under Nomura coverage.

Exhibit 48. EPS growth: Nomura vs Consensus

(%)	CY09	CY10F	CY11F	CY12F
Kospi				
Nomura	**(26)**	56	15	16
Consensus	**(26)**	42.5	13	12

Source: Bloomberg; Nomura International (Hong Kong) Limited – investment Strategy

Our risk indicators suggest that fair equity risk premium in Korea is at 6.7%. While global risk factors are more favourable, domestic factors haven't picked up. Upside risks to our model derived index target are: 1) any sharp upturn in retail investor sentiment as well as money multipliers; 2) narrowing BBB- rated corporate spreads, and; 3) better-than-expected economic growth in developed markets.

Expected Kospi levels under different scenarios are as below:

Exhibit 49. Kospi level given risk premium and earnings growth

	Kospi 2011F EPS Growth %					
	12	13	14	15	14	13
Fair risk premium %						
8.0	1,910	1,930	1,940	1,960	1,940	1,930
7.0	2,100	2,120	2,140	2,160	2,140	2,120
6.7	2,170	2,190	2,210	**2,230**	2,210	2,190
6.0	2,330	2,350	2,370	2,400	2,370	2,350
5.0	2,620	2,650	2,670	2,690	2,670	2,650

Note: as of 15 November, 2010

Source: Bloomberg, Nomura International (Hong Kong) Limited – Investment Strategy

Kospi forecast (II): Methodology

In our model, basically we use two factors to derive the fair Kospi level; one is expected earnings growth and the other is fair risk premium.

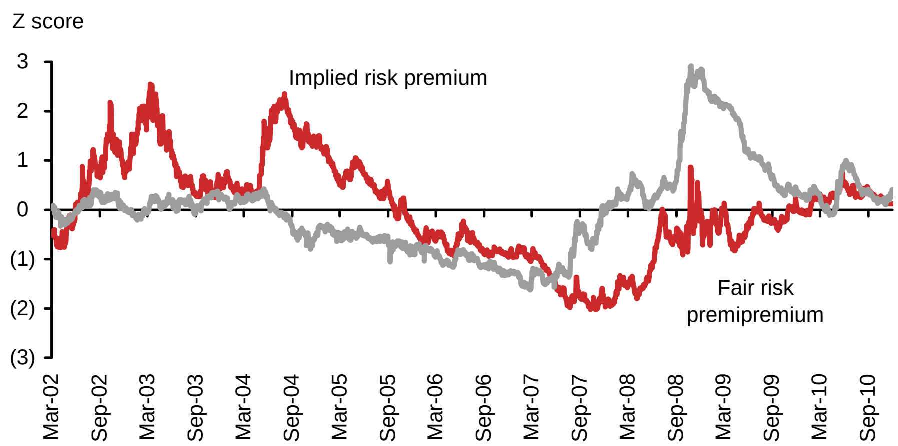
- **Earnings growths:** Our Nomura analysts cover 69 stocks in the Korean equity market and those stocks comprise approximately 65% of total Kospi market capitalisation. To measure total earnings growth of the Kospi, we aggregate bottom-up earnings forecasts by analysts for the stocks under Nomura coverage. For non-Nomura coverage companies, we use consensus EPS growth. As our coverage tends to be large cap stocks, the discrepancy between Nomura coverage growth rates and the overall Kospi's are mainly due to mid- to small cap stocks. When we have a strong view on these stocks, we may adjust expected growth rates; otherwise, we follow consensus growth rates for non-coverage stocks.
- **Risk premium:** We identified three categories to model the fair risk premium on Korean equities: 1) global risk indicators; 2) country (Korea) risk indicators, and; 3) domestic risk indicators. All factors in the model are shown below:

Exhibit 50. Risk indicators

	Current level			
	Z score/value	Risk seeking/ adverse	Momentum	Impact on risk indicator
Global risk factors (z-score)	-0.38	Risk-seeking	▲	
EM bond Spread	321.67		▼	+
VIX	23.54		▲	+
MOVE	101.90		▲	+
US Corporate bond spread	3.07		▼	+
TED Spread	13.51		▲	+
Country risk factors (z-score)	0.91	Risk-Neutral	▼	
Korea government bond CDS	121.50		▼	+
Won exchange rates volatility	12.08		▼	+
Domestic factors (z-score)	0.75	Risk-adverse	▲	
Money supply M2 growth	8.1		▼	-
Corporate bond spread (BBB-)	6.91		▼	+
Corporate bond spread (AA-)	0.84		▲	+
Risk premium (%)	6.7		▲	
Risk free rates (%)	3.0			

Source: Bloomberg; Nomura International (Hong Kong) Limited – investment Strategy

Exhibit 51. Implied risk premium EPS in 2011F: Nomura vs Consensus (%)



Source: Bloomberg; Nomura International (Hong Kong) Limited – investment Strategy

Sector stance

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Going into 2011, we would tilt our portfolio based on the below:

- As liquidity conditions remain favourable in the economy and the money multiplier will likely improve, sectors that are more sensitive to velocity of money should perform better.
- With a weak US dollar and firm demand for commodities, we Overweight beneficiaries of rising commodity prices.
- Although earnings momentum still remains weak, we see some sectors as discounting an overly pessimistic outlook. We believe those sectors will have more upside when economic indicators turn out to be better.
- Since rising price expectations would hit fixed income assets hard, we would avoid bond-like sectors.

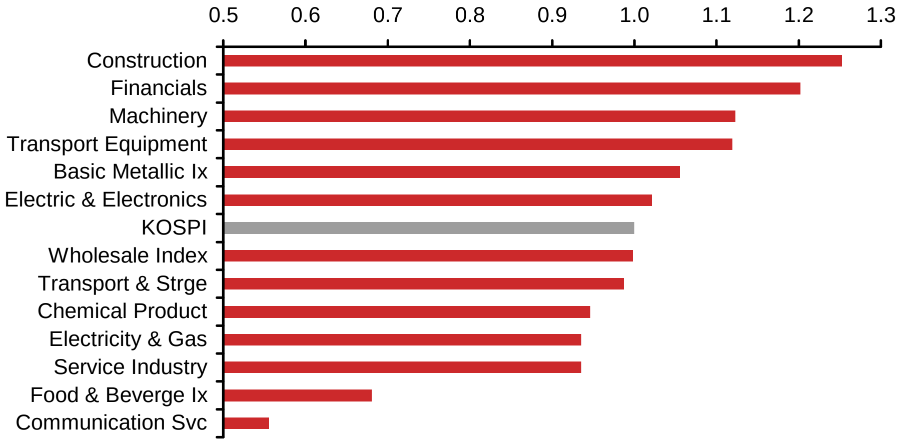
We Overweight Korean E&C companies, Chemicals, Tech and Auto while we have Underweight recommendations on F&B, Utility and Telecoms.

Exhibit 52. Sector weightings

Sector	Asset allocation: Benchmark %	Asset allocation: Nomura %	TOP BUYs	Difference (+overweight, - underweight)	Nomura stance	Beta
Electric & Electronics	18.0	22.0	Samsung Elec.	4.0	**Overweight**	1.02
Financials	16.0	18.0	KB Financial g	2.0	**Overweight**	1.20
Transport Equipment	13.0	16.0	Hyundai Motor	3.0	**Overweight**	1.12
Chemical Product	12.0	15.0	LG Chem	3.0	**Overweight**	0.95
Service Industry	9.0	8.0	Samsung Engineering	(1.0)	Underweight	0.94
Basic Metallic Ix	7.0	6.0	Hyundai Steel	(1.0)	Underweight	1.06
Wholesale Index	6.0	4.0	Hyundai Home Shopping	(2.0)	Underweight	1.00
Construction	3.0	7.0	GS E&C	4.0	**Overweight**	1.25
Communication Svc	3.0	0.5	SK Telecom	(2.5)	Underweight	0.56
Transport & Strge	3.0	0.5	n/a	(2.5)	Underweight	0.99
Electricity & Gas	2.0	0.0	KEPCO	(2.0)	Underweight	0.94
Machinery	2.0	3.0	n/a	1.0	**Overweight**	1.12
Food & Beverge Ix	2.0	0.0	Orion	(2.0)	Underweight	0.68
Medicine	1.0	0.0	n/a	(1.0)	Underweight	0.66
Miscellaneous Indx	1.0	0.0	n/a	(1.0)	Underweight	0.50
Others	2.0	0.0	n/a	(2.0)	Underweight	n/a
				Nomura Beta		**1.07**

Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

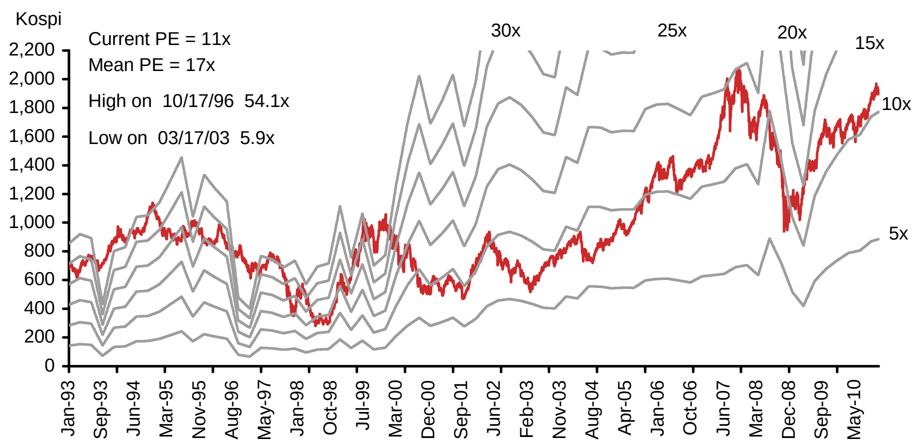
Exhibit 53. Kospi sector beta



Source: Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 54. Kospi P/E band charts

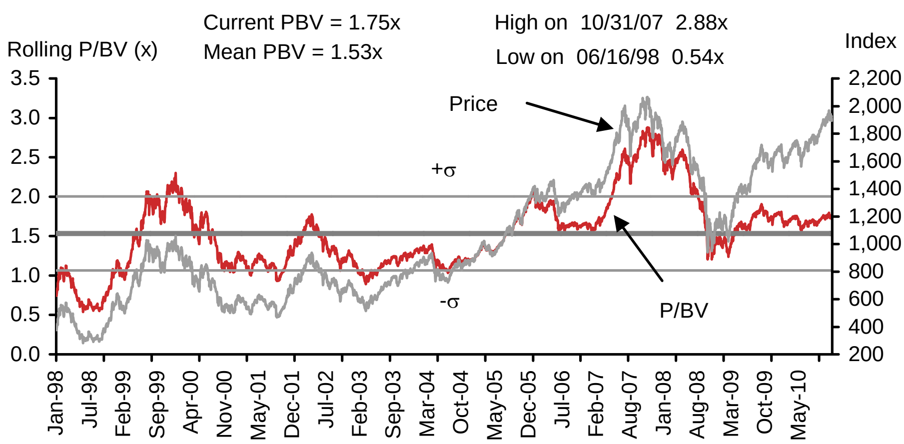
P/E not expensive…



Source: Thomson Reuters Datastream, Nomura International (Hong Kong) — Quantitative Strategies

Exhibit 55. Kospi Index — Rolling Forward PBV

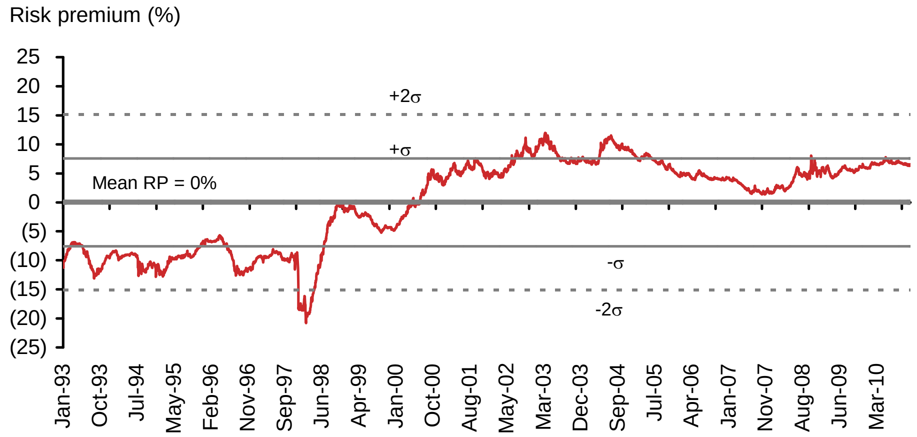
...nor PBV



Source: Thomson Reuters Datastream, Nomura International (Hong Kong) — Quantitative Strategies

Exhibit 56. Kospi Implied risk premium

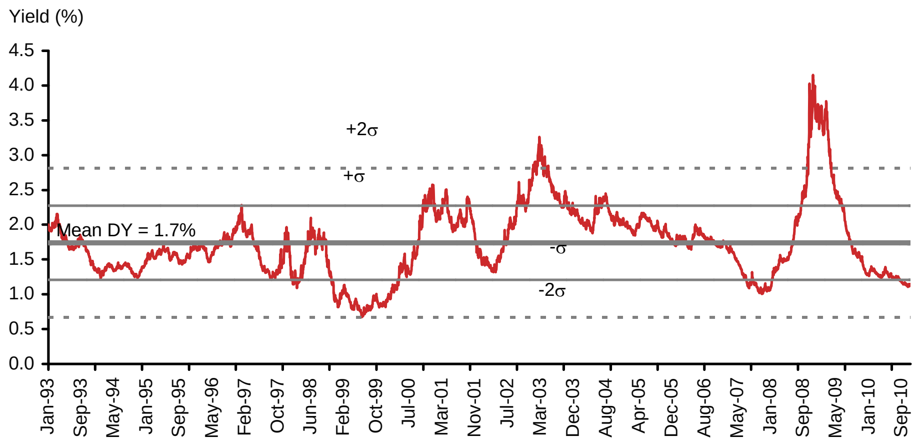
Risk premium looks rich…



Source: Thomson Reuters Datastream, Nomura International (Hong Kong) — Quantitative Strategies

Exhibit 57. Kospi dividend yield

…while dividend yield is below long-term average



Source: Thomson Reuters Datastream, Nomura International (Hong Kong) — Quantitative Strategies

Investment ideas

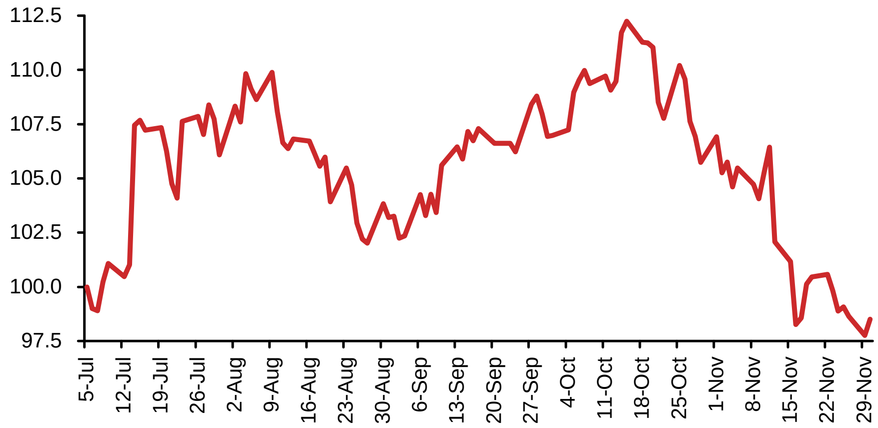
Running investment themes

Amy Lee, CFA, CAIA
+852 2252 2181 / amy.lee@nomura.com

We highlight investment themes that we are currently running.

Exhibit 58. Kospi listed securities companies vs Kospi

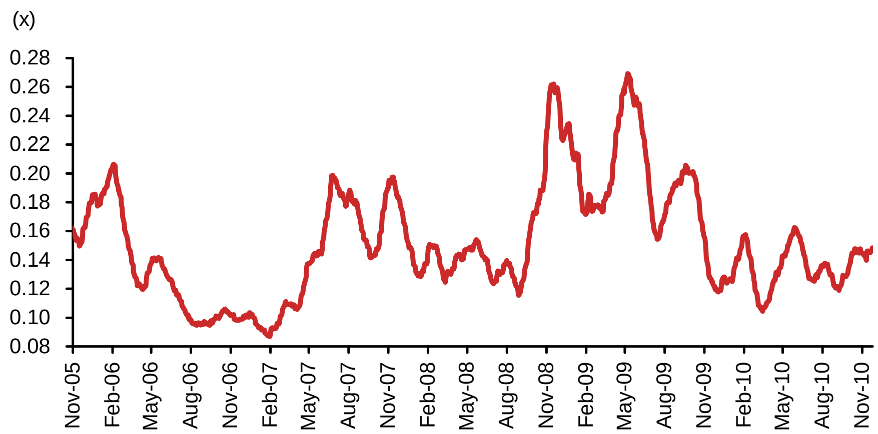
We initiated on Korean listed brokers vs the Kospi on 5 July, 2010



Source: Datastream; Nomura International (Hong Kong) limited – Investment Strategy

Exhibit 59. Kospi: turnover-to-market cap ratio

As market turnover started to recover after summer…

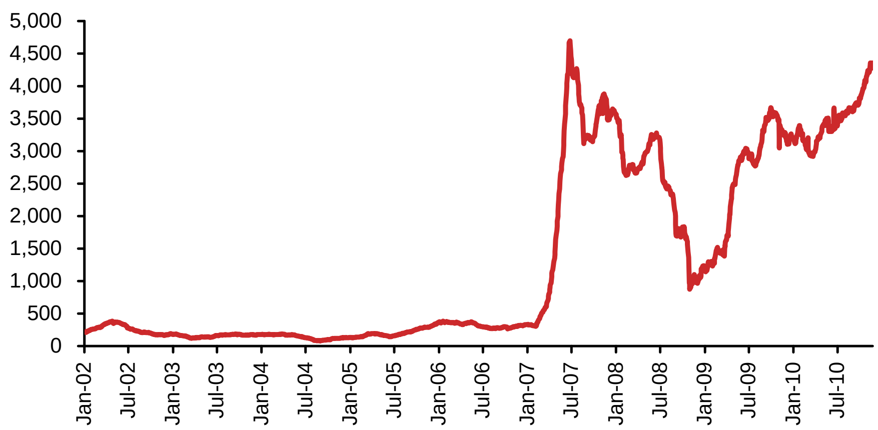


Note: one month moving average;

Source: Datastream; Nomura International (Hong Kong) limited – Investment Strategy

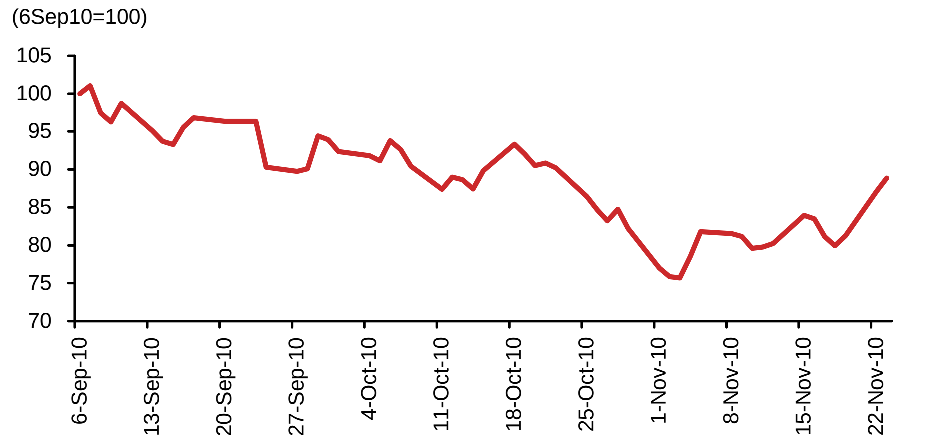
Exhibit 60. Kospi margin loans (Wbn)

…and margin loans amount have dramatically risen, we continue to like securities companies



Source: Datastream; Nomura International (Hong Kong) limited – Investment Strategy

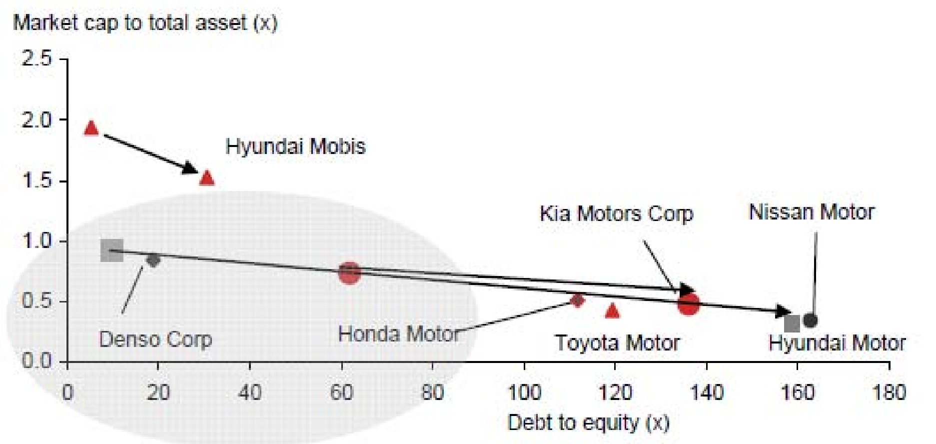
Exhibit 61. IFRS recommendation: Korea Tech vs Auto



Source: Datastream; Nomura International (Hong Kong) Limited – Investment Strategy

We would expect the upcoming move towards consolidated accounting to highlight a significant difference between the Auto and Technology sector…

Exhibit 62. Debt-to-equity and market cap to total assets: Auto and Auto Parts & Equipment

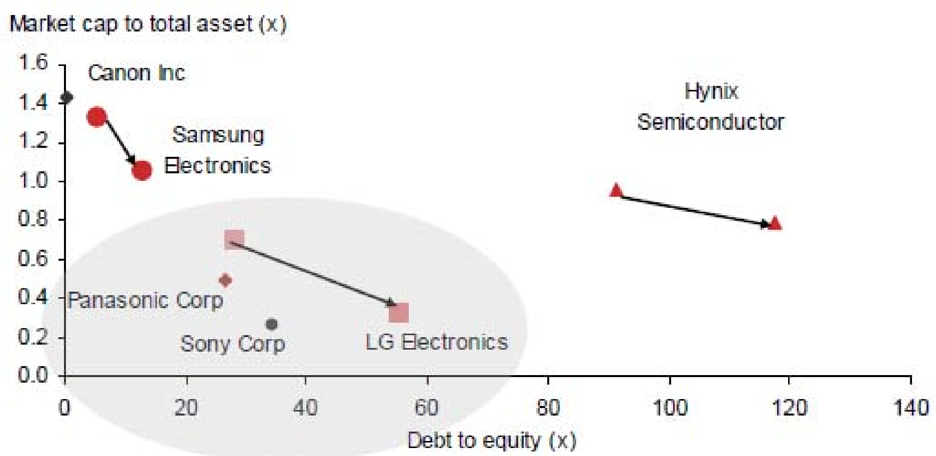


Note: end-FY09

Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

…as the leverage ratios on a consolidated basis are much higher in the Auto sector…

Exhibit 63. Debt-to-equity and market cap to total assets: technology



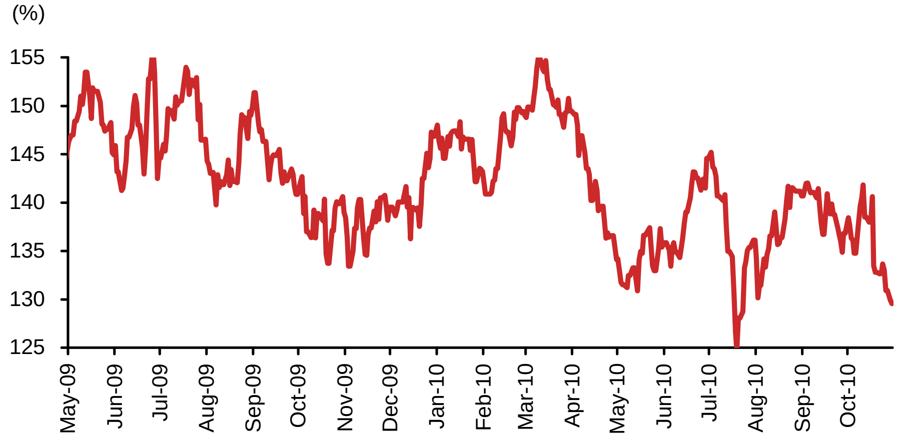
Note: end-FY09

Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

…vs technology

Exhibit 64. Korea: premium of common shares to preferred shares (since 25 May, 2010)

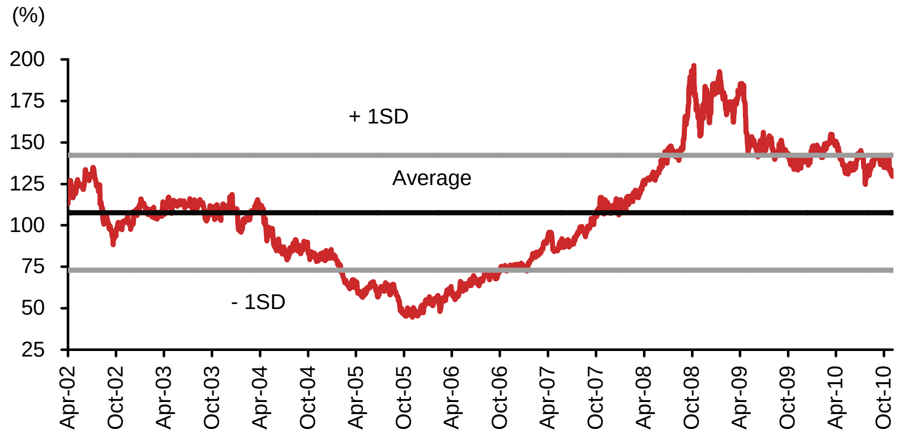
We highlighted arbitrage opportunities in Korea preferred shares on 25 May, 2010. While the discount has narrowed substantially…



Source: Datastream; Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 65. Korea: premium of common shares to preferred shares (long term)

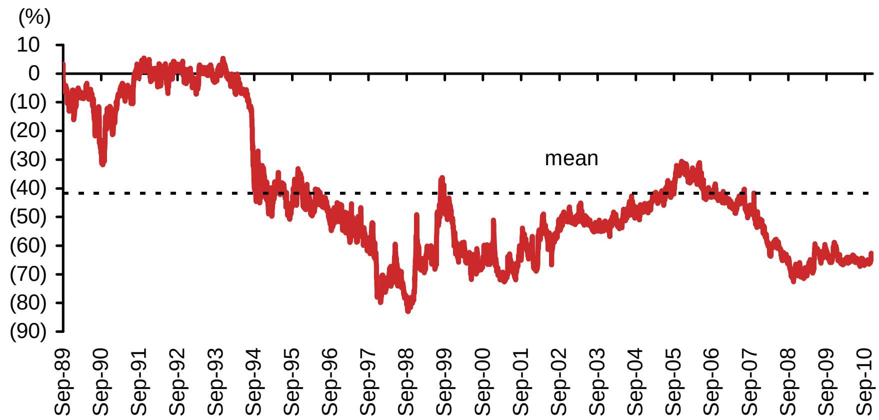
…the premium of common shares still remains one standard deviation above the historical mean, implying more room to narrow



Source: Datastream; Nomura International (Hong Kong) Limited – Investment Strategy

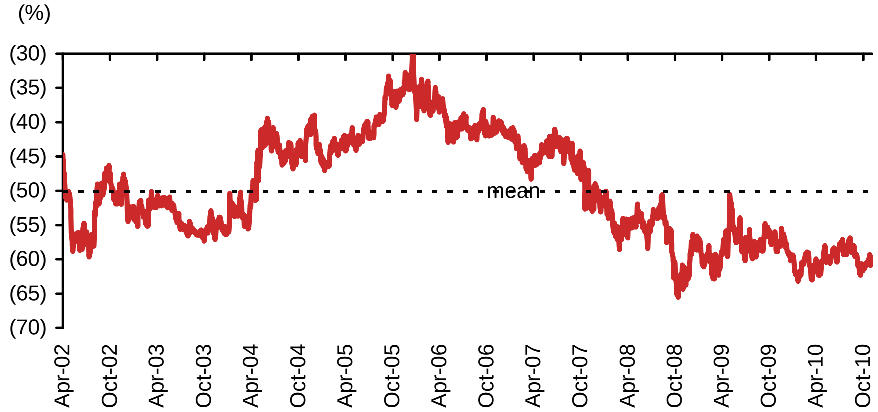
Exhibit 66. Hyundai Motor: discount of preferred shares to common shares

Indeed, some preferred shares remain at a deep discount to common shares



Source: Datastream; Nomura International (Hong Kong) Limited – Investment Strategy

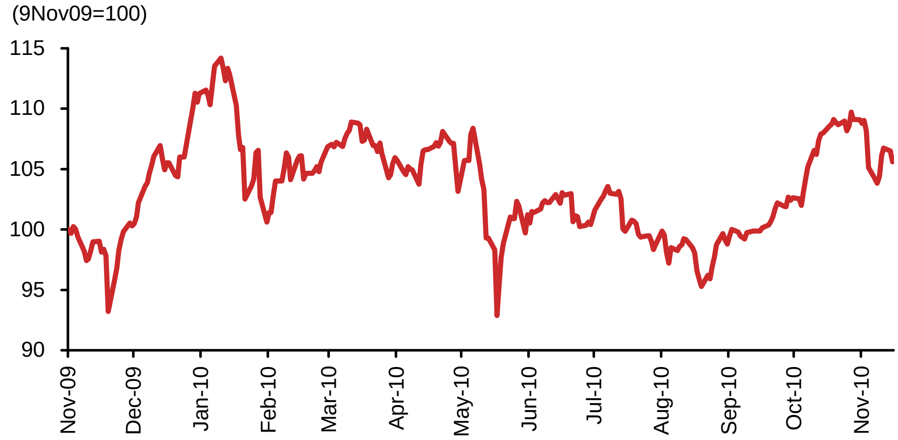
Exhibit 67. LG electronics: discount of preferred shares to common shares



Source: Datastream; Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 68. Kosdaq index

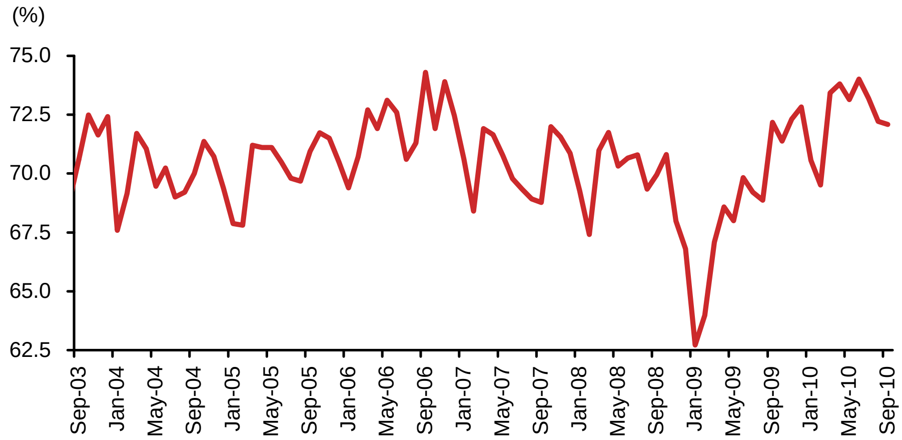
We were more Bullish on the Kosdaq in 2010…



Source: Datastream; Nomura International (Hong Kong) limited – Investment Strategy

Exhibit 69. Operation ratio: SMEs

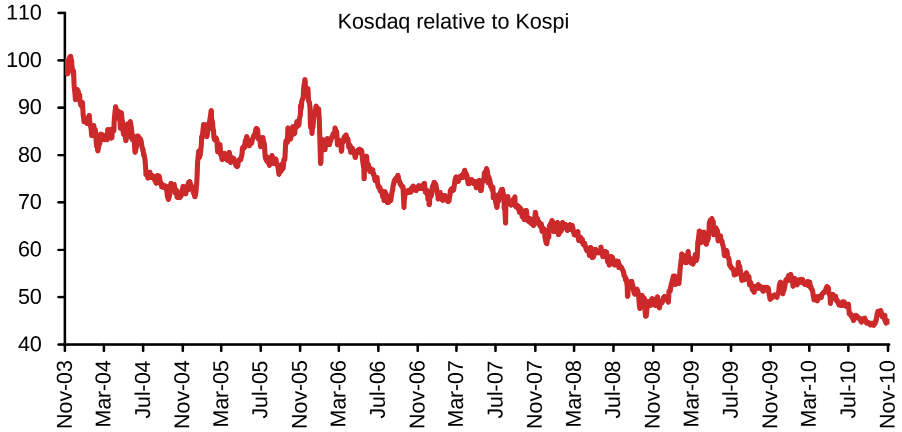
…as a sharp swing in SMEs' operation ratios in early 2010…



Source: Datastream; Nomura International (Hong Kong) limited – Investment Strategy

Exhibit 70. Kosdaq: relative performance

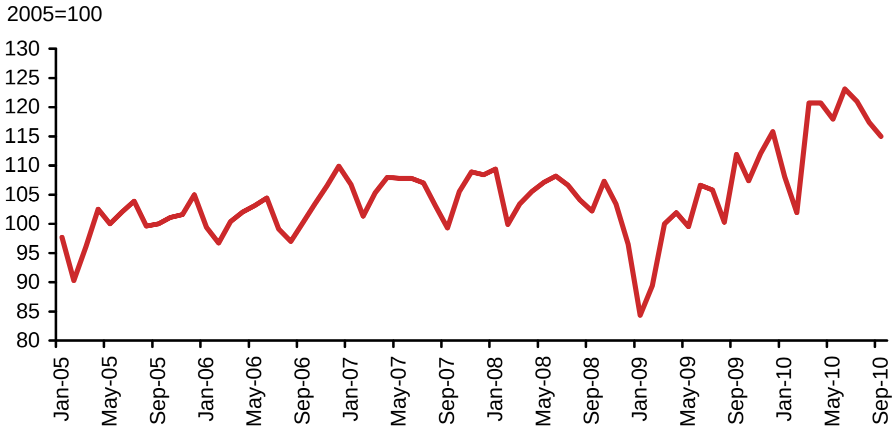
…had not been reflected in the prices



Source: Datastream; Nomura International (Hong Kong) limited – Investment Strategy

Exhibit 71. Korea: industrial production – SMEs

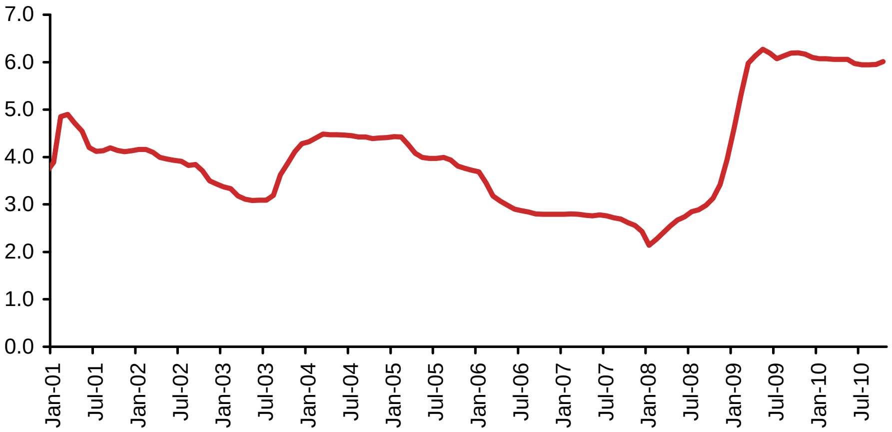
While fundamentals of SMEs appeared solid, Korean economies failed to redistribute the fruit of economic recovery and favourable credit conditions...



Source: Datastream; Nomura International (Hong Kong) limited – Investment Strategy

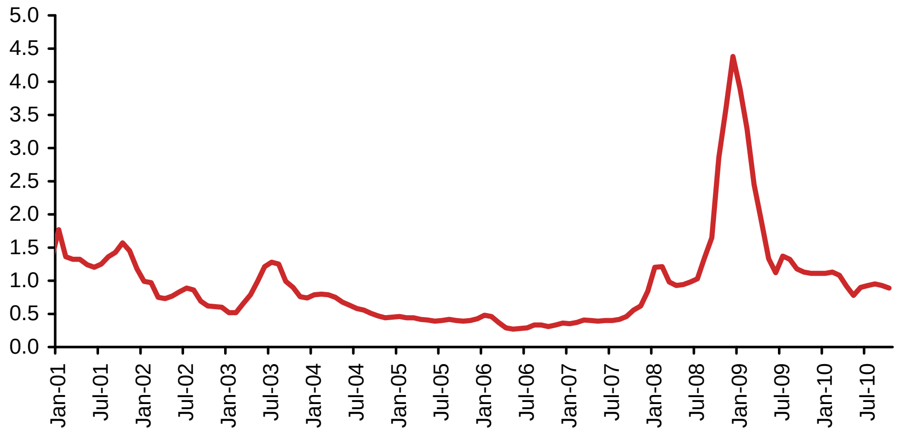
Exhibit 72. Yield spreads between corporate bonds BBB- and AA- (%)

…as seen in a widened gaps between BBB- and AA-…



Source: Datastream; Nomura International (Hong Kong) limited – Investment Strategy

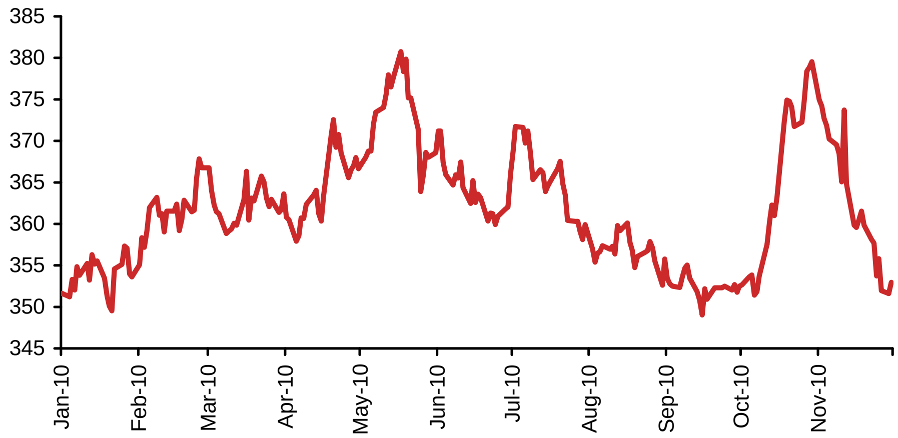
Exhibit 73. Korea Corporate bond spreads: AA- (%)



Source: Datastream; Nomura International (Hong Kong) limited – Investment Strategy

…in contrast to sharply narrower corporate bond spreads for large companies with a higher credit rating

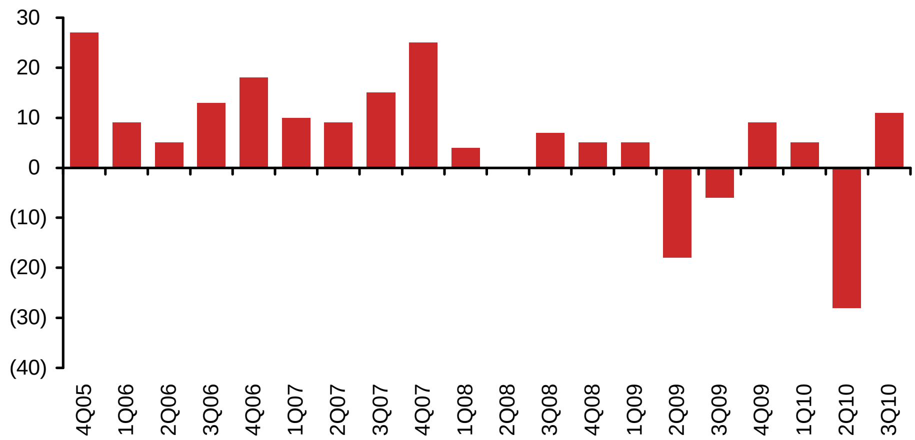
Exhibit 74. Kospi small cap relative to Kospi (over the past one year)



Source: Datastream; Nomura International (Hong Kong) Limited – Investment Strategy

Another asset class with similar attributes, Kospi small caps index performed largely in line with the Kospi…

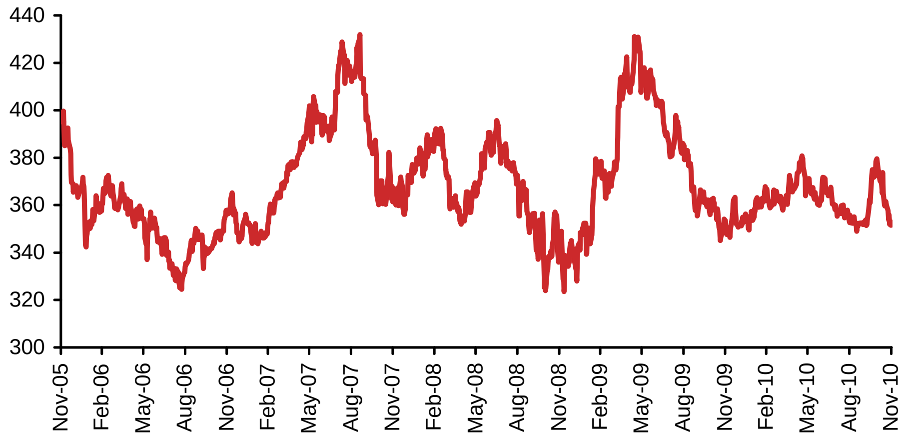
Exhibit 75. Kosdaq - the number of listed companies (q-q change)



Source: CEIC; Nomura International (Hong Kong) Limited – Investment Strategy

It appears that a series of delisting of microcap companies weighed down the Kosdaq during 2010

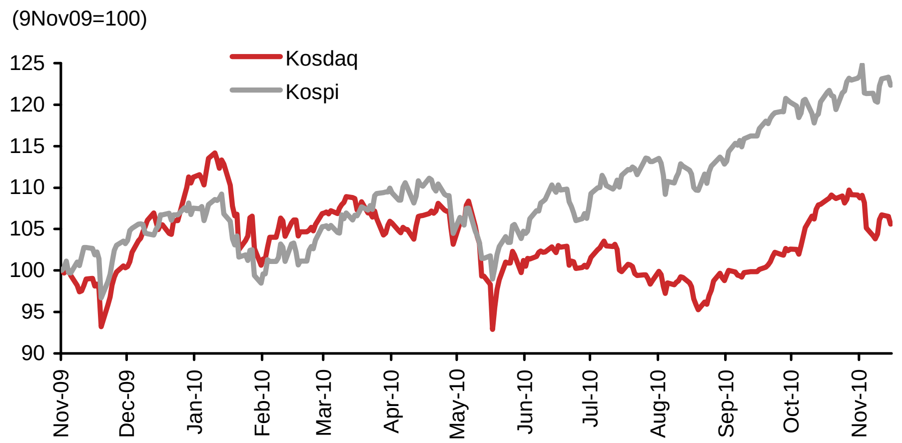
Exhibit 76. Kospi small cap index relative to Kospi



Source: Datastream; Nomura International (Hong Kong) Limited – Investment Strategy

While we continue to believe the fundamentals of small cap companies' remain solid, we turn more selective, initiating a trade between the Kospi small cap index vs Kospi…

Exhibit 77. Kosdaq vs Kospi



Source: Datastream; Nomura International (Hong Kong) limited – Investment Strategy

…and closing the Kosdaq vs Kospi. When retail investors participation accelerates, we will revisit the Kosdaq

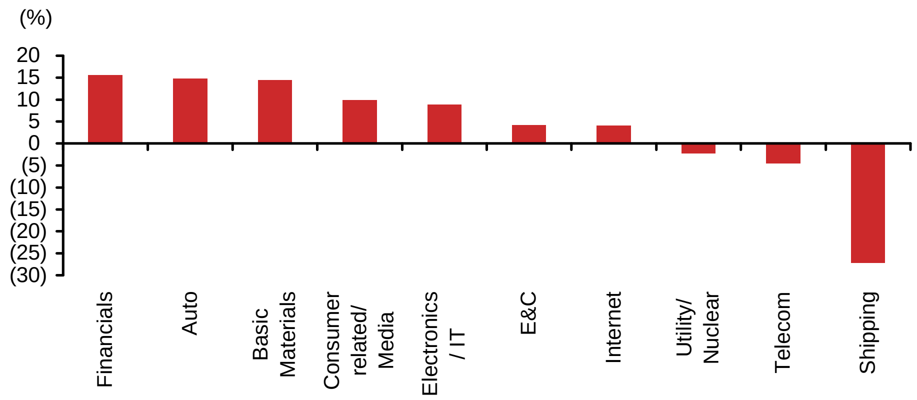
Nomura vs consensus

Bottom-up Earnings Forecast

Korean companies' earnings momentum in 2011 is expected to be weaker after surge in 2010. Although we have cautious view on earnings growths in 2010, it appears that weaker earnings growths have been largely discounted in the market.

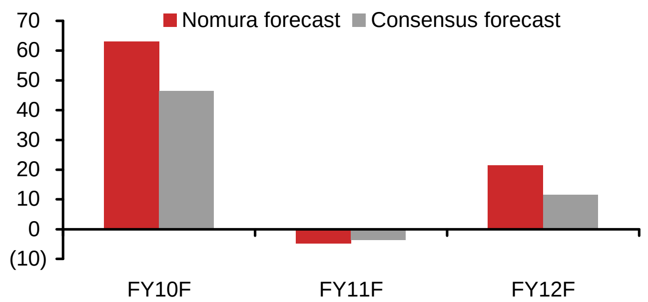
While we have most bullish bottom-up view on financial sector's earnings followed by auto and basic materials, we are more bearish on Shipping and the Utility sector compared to consensus.

Exhibit 78. EPS growth (%): Nomura vs Consensus



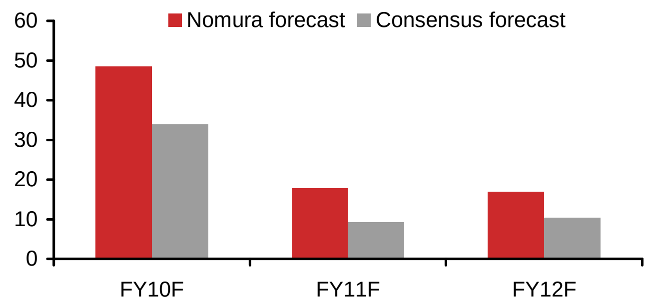
Source: Bloomberg; Nomura International (HK) Limited – Investment Strategy

Exhibit 79. EPS growth %: Electronics / IT



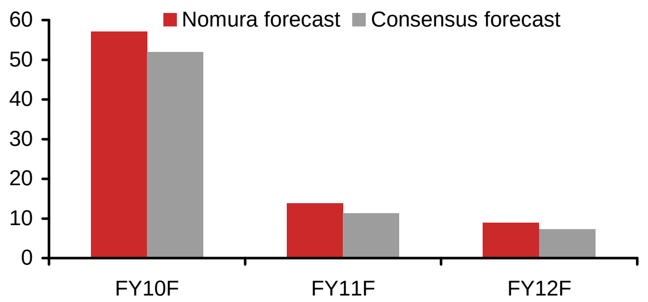
Source: Bloomberg; Nomura International (HK) Limited – Investment Strategy

Exhibit 80. EPS growth %: Basic Materials



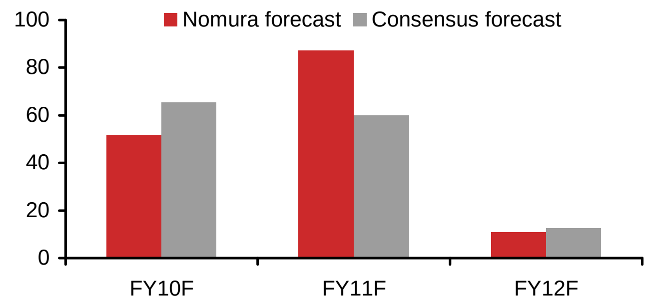
Source: Bloomberg; Nomura International (HK) Limited – Investment Strategy

Exhibit 81. EPS growth %: Automobile



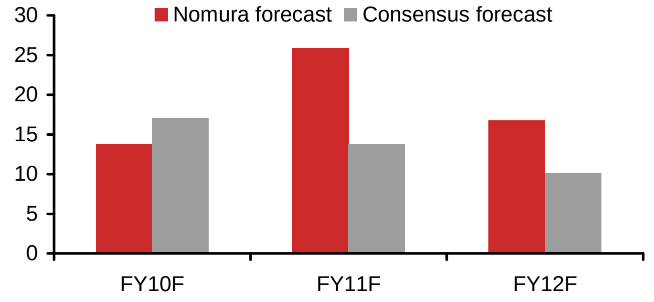
Source: Bloomberg; Nomura International (HK) Limited – Investment Strategy

Exhibit 82. EPS growth %: Financials



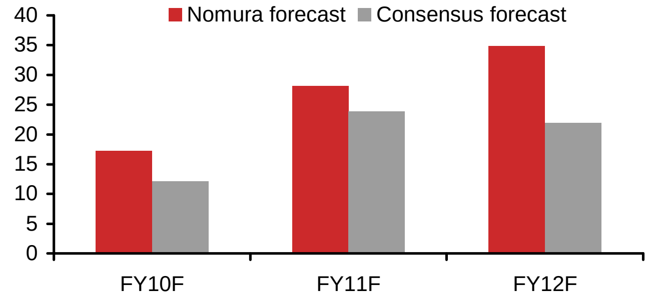
Source: Bloomberg; Nomura International (HK) Limited – Investment Strategy

Exhibit 83. EPS growth %: Telecom



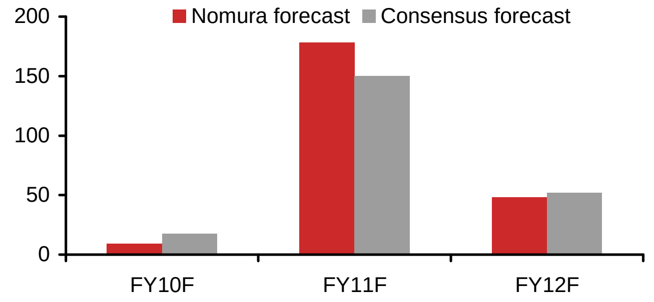
Source: Bloomberg; Nomura International (HK) Limited – Investment Strategy

Exhibit 84. EPS growth %: Internet



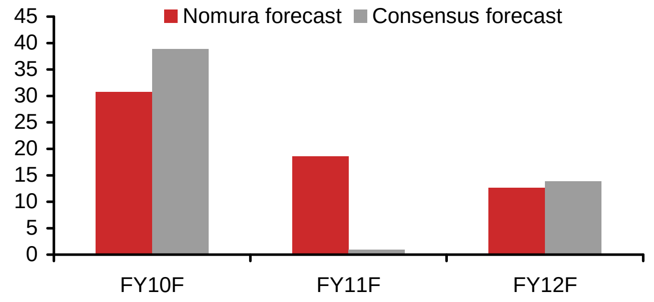
Source: Bloomberg; Nomura International (HK) Limited – Investment Strategy

Exhibit 85. EPS growth %: Utility/Nuclear



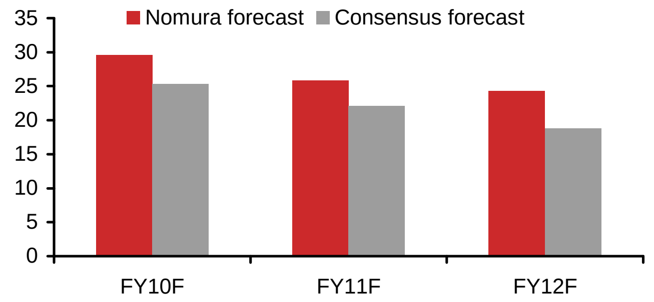
Source: Bloomberg; Nomura International (HK) Limited – Investment Strategy

Exhibit 86. EPS growth %: Consumer related/Media



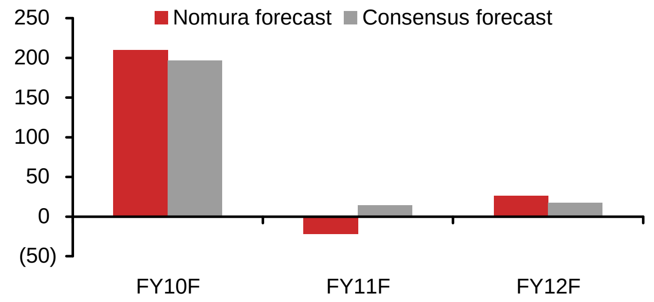
Source: Bloomberg; Nomura International (HK) Limited – Investment Strategy

Exhibit 87. EPS growth %: E&C



Source: Bloomberg; Nomura International (HK) Limited – Investment Strategy

Exhibit 88. EPS growth %: Shipping



Source: Bloomberg; Nomura International (HK) Limited – Investment Strategy

A review of 2010

A review of Korean equities in 2010

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+852 2252 2181 / amy.lee@nomura.com

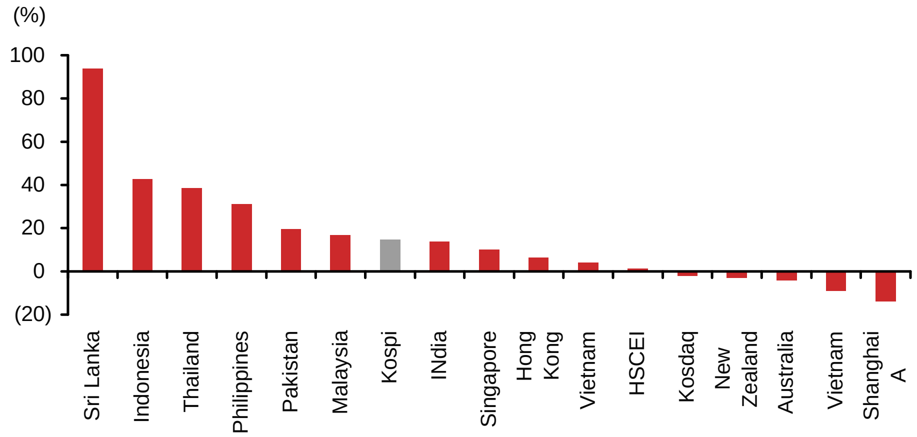
"We expect 2010 to be a year of rebalancing for both the global economy and financial markets. While G7 members will need further time to heal, Asia and emerging markets are expected to grow above trend. At a time when the focus of the global economy is moving to emerging economies, Korea stands out thanks to its high export exposure to these emerging markets — its own intermediary position may also be underscored by likely promotion into developed ranks in global indices. With higher consumption alongside a robust credit cycle in the emerging markets, Korea should be one of the biggest regional beneficiaries of an unfolding capex cycle. We expect favourable liquidity conditions driven by a record BoP surplus and an extended loose monetary policy to support share prices in 2010. High savings at corporates are likely to be transmitted into capex, and confidence in the economy should spread to SMEs, boosting the Kosdaq. In our Korea universe, our conviction BUY calls are Kia Motors, LG Display, POSCO and Samsung Electronics, while we have a REDUCE on Honam Petrochemical."

At the beginning of 2010, investors were concerned about growth. Rather than a double-dip, investors were encouraged by upbeat economic data and looked for normalising of extremely loose monetary policy in the G3. However, as soon as balance sheet expansions by major central banks halted, liquidity conditions deteriorated quickly, leading to the second round of QE by Fed.

In 2010, Korean equities have seen much higher volatility due to European sovereign debt crisis causing the Korean won to depreciate and triggering a risk appetite to reverse. However, as overall global economies continued to recover from the aftermath of the financial crisis Korean equities were able to post a 15% gain in local currency terms. On a relative basis, the returns were subdued as small economies such as those in ASEAN have stolen spotlight, rising 30 to 40% (in local currency terms). But on a risk-adjusted basis, the Korean market appeared better off than more comparable peers, such as Taiwan and others in Northeast Asia.

Exhibit 89. Asia Pacific: Equity markets performance (local currency, YTD)

Korean equities have risen by 15% in local currency terms…

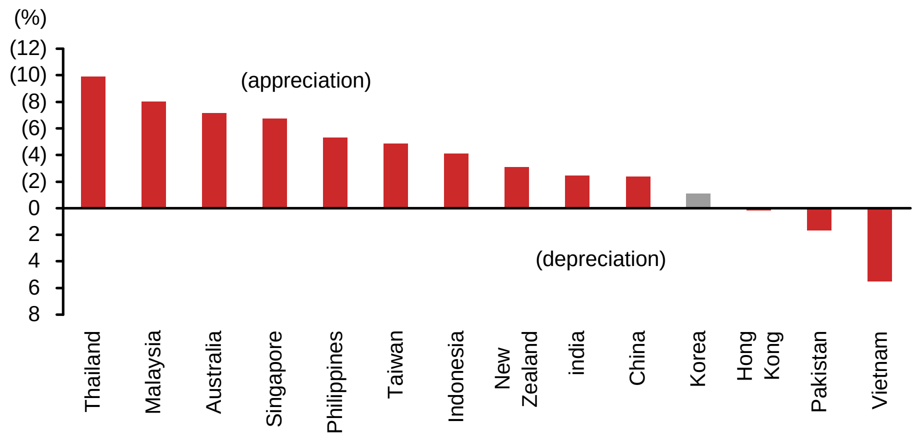


Note: as of 1 Dec 2010.

Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

…while Korean won appreciation has supported total returns in US dollar terms

Exhibit 90. Asia Pacific: currencies (change against US$, YTD)



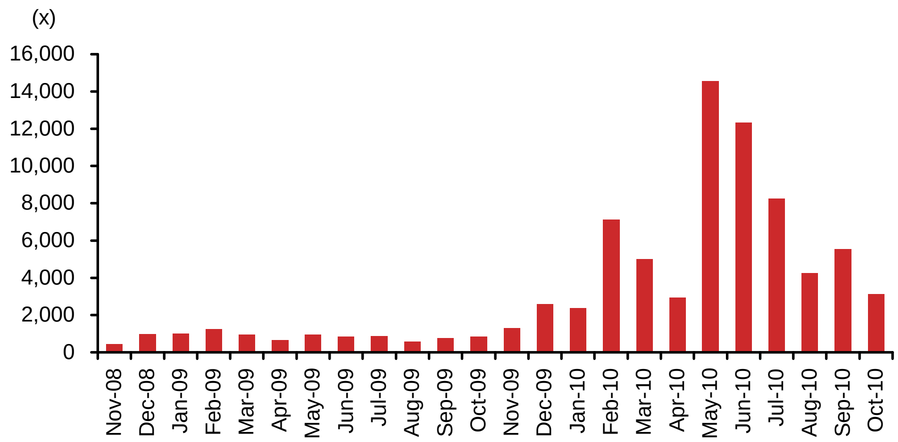
Note: as of 1 Dec 2010.

Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

The Korean equity market started 2010 with investor sentiment exuberance and risk appetite stretched on the back of a dramatic recovery in the economy during the previous year. In the first quarter, the market experienced consolidation with risk appetite normalising but earnings remaining robust. Due to robust earnings forecasts supporting the equity market, even a series of serious confrontations between the two Koreas didn't affect sentiment. However, like other markets, Korean equities were hit by the European sovereign solvency crisis in May. As the US dollar rallied, the reversal in risk appetite caused the equity market to drop.

Looking back at the global market in equity market in 2010, investors' attention was gripped by the European sovereign debt crisis…

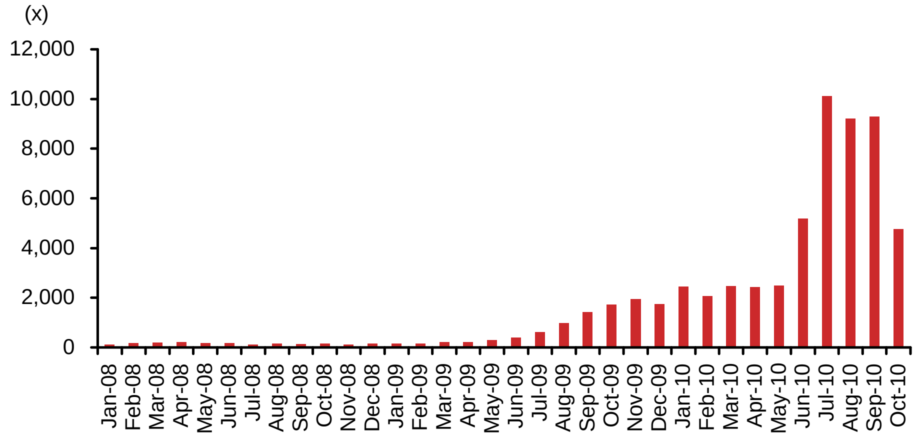
Exhibit 91. Number of times the words "sovereign debt" appear in the press



Source: Factiva, Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 92. Number of times the words "double dip" appear in the press

...and then concerns over a double dip

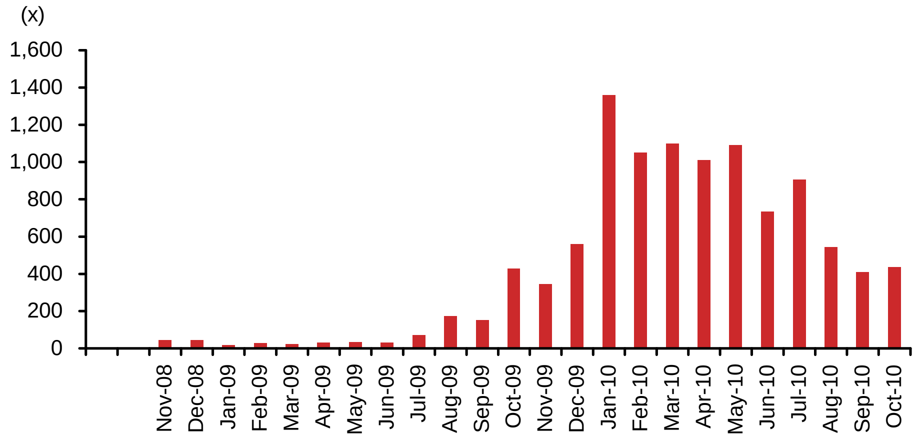


Source: Factiva, Nomura International (Hong Kong) Limited – Investment Strategy

From 2H10, concerns over European sovereign solvency receded while investor sentiment soured on fears that the global economy would fall into a double-dip. The Fed' announcement of the second round of QE triggered a liquidity driven rally in the later part of this year. Meanwhile, companies' earnings reached a record high in 3Q10 helped by strong base effects.

Exhibit 93. Number of times the words "policy tightening" appear in the press

In 2010, calls for policy tightening were pushed back amid a weaker economic growth outlook

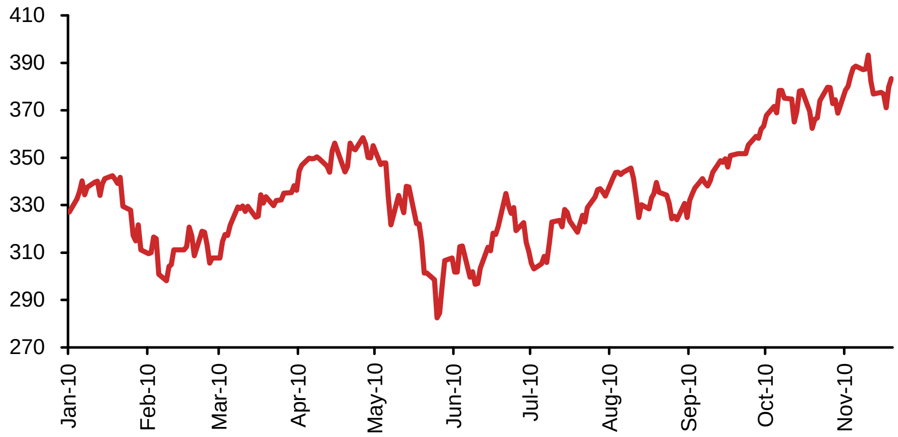


Source: Factiva, Nomura International (Hong Kong) Limited – Investment Strategy

Throughout 2010, local interest rates were kept low despite two policy rate hikes and with the Korean won being undervalued, this provided favourable conditions for exporters. While overall liquidity conditions as well as earnings momentum was supportive to equities, local retail investors haven't returned to the equity market yet; a depressed housing market has hampered any sharp upturn in investor sentiment.

Exhibit 94. MSCI Korea US$ in 2010

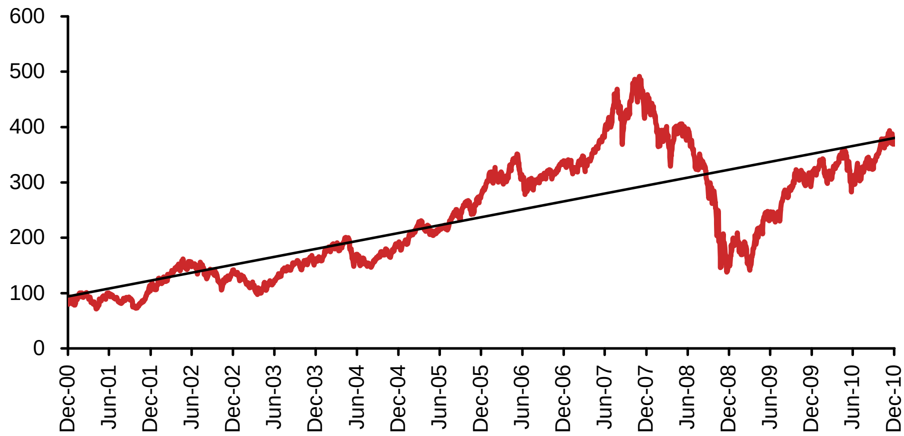
The performance in 2010 was supported by a strong rally in 3Q-4Q amid the announcement of QE2



Source: Thomson Reuters Datastream, Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 95. MSCI Korea US$ (over the past 10 years)

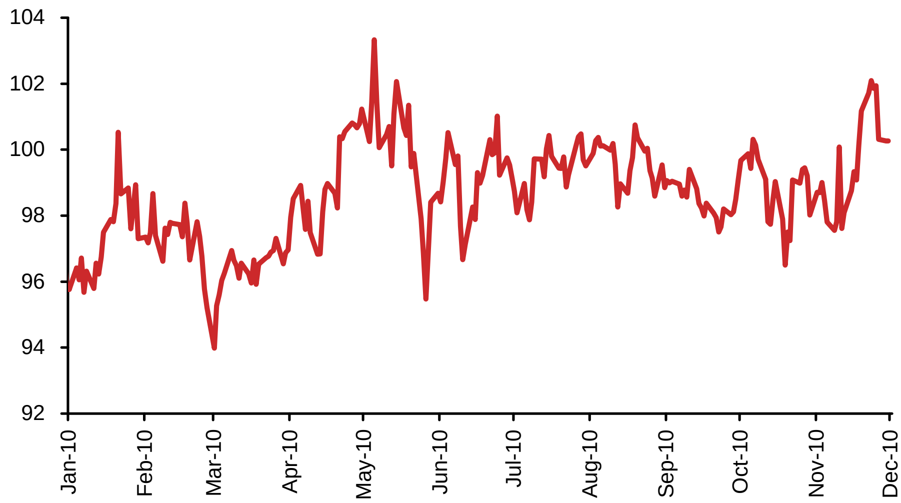
The Korean equity market continued to grow, returning to its long-term trend line…



Source: Nomura International (Hong Kong) Limited – Investment Strategy

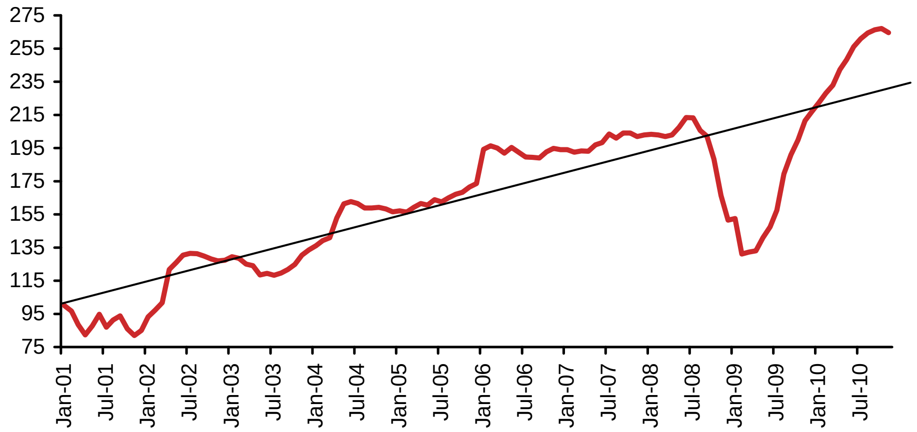
Exhibit 96. MSCI Korea US$ vs MSCI AP ex JP (over the past one year)

…but on a relative measure, the performance has not been so superior…



Source: Nomura International (Hong Kong) Limited – Investment Strategy

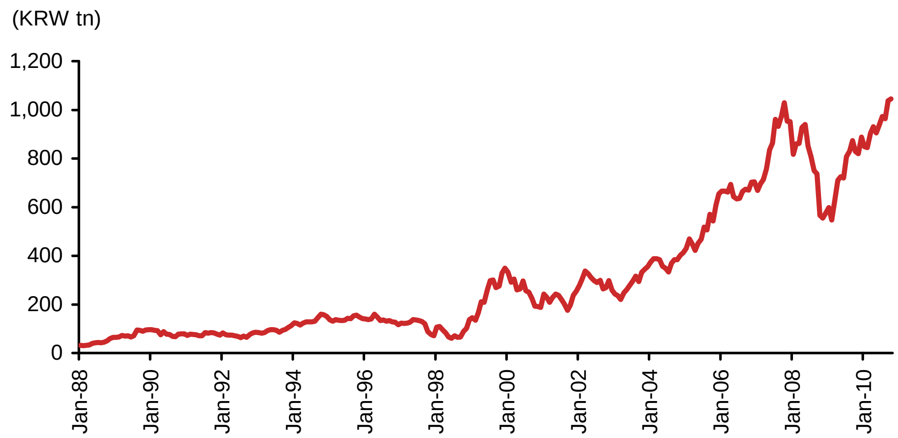
Exhibit 97. MSCI Korea – 12-month forward earnings



Source: Nomura International (Hong Kong) Limited – Investment Strategy

…especially given that companies' earnings have reached a record high

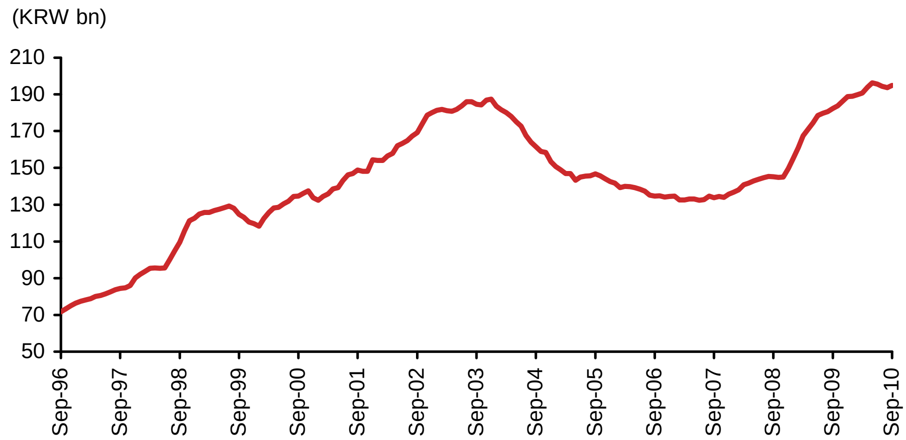
Exhibit 98. Korea: Kospi market cap (Wbn)



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

In terms of market capitalisation, the equity market has fully recovered to the 2007 pre-crisis level…

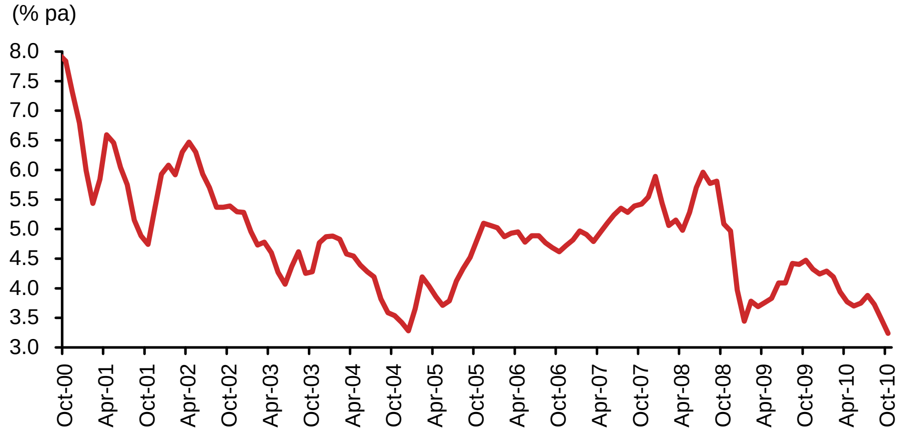
Exhibit 99. Korea: Corporate bonds outstanding



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

...while investors' attentions trend to the bond market…

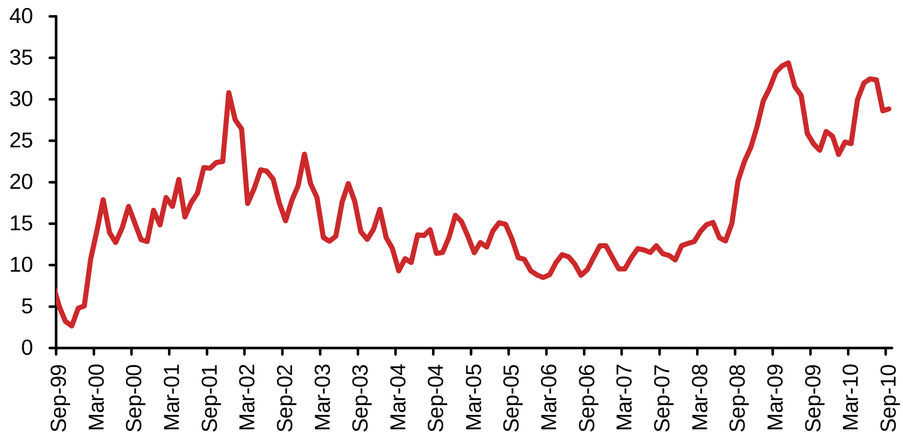
Exhibit 100. Korea: 3-year Treasury bond yield (%)



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

…as treasury bonds have rallied…

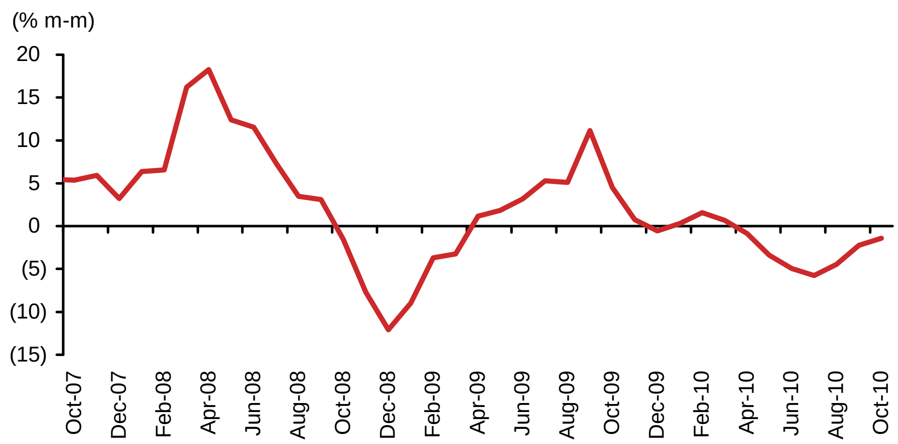
Exhibit 101. Korea: capital raised by corporate bond issuance (Wtn)



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

…and primary markets were stronger as companies took advantage of low interest rates…

Exhibit 102. Korea: Seoul metropolitan area housing price changes

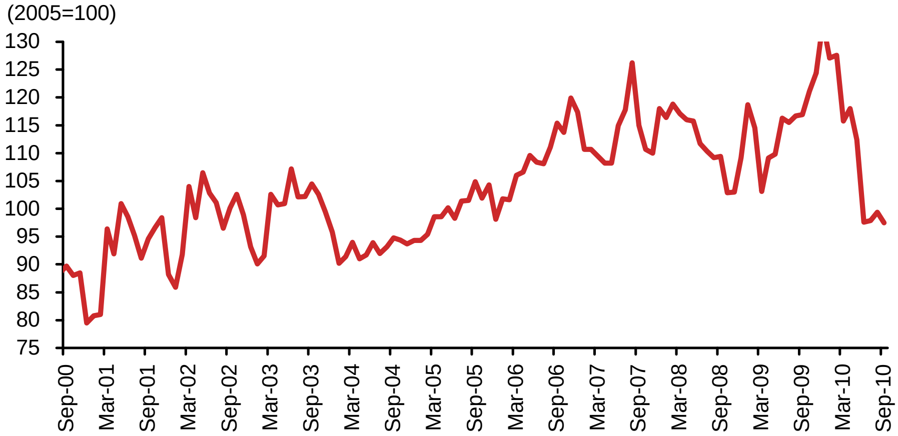


Note: %m-m, annualised

Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

One of the worst performers in asset classes in 2010 was clearly property…

Exhibit 103. Korea: real estate activity



Source: CEIC, Nomura International (Hong Kong) Limited – Investment Strategy

…and activity was at the lowest since 2005

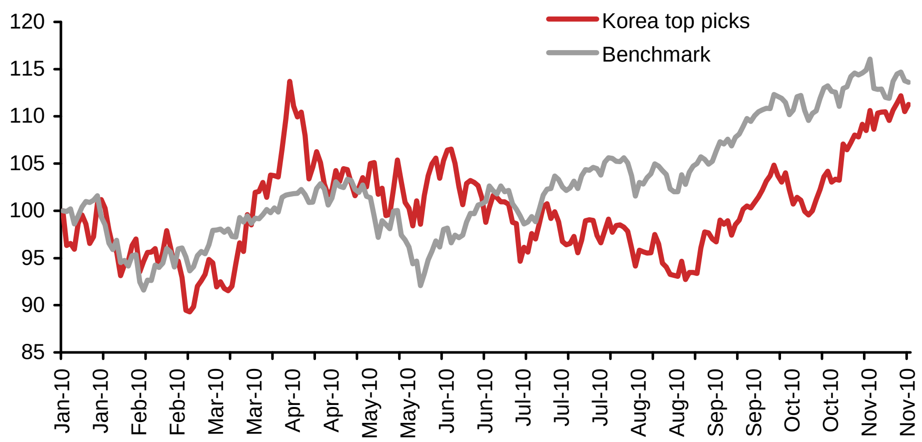
Korea top picks performance and Sector performance in 2010

Nomura Korea Research Team

In our 2010 Outlook, we recommended five top conviction BUY and one REDUCE idea given companies' fundamentals and analyst recommendations. Given the volatile market conditions, we have revised our earnings and recommendations. As a result, we closed our REDUCE position on Honam Petrochemicals on 6 July, 2010, and BUY position on LG Display on 24 August, 2010. The basket has produced absolute positive returns while largely moving in line with the benchmark, Kospi. The performance and constituents are highlighted below:

Our Korean top picks were largely in line with the benchmark

Exhibit 104. Korea 2010 Top Picks



Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 105. 2010 Top Picks: absolute price performance

		Absolute price changes (%)				
Company	**Bloomberg**	**1 week**	**1m**	**3m**	**6m**	**YTD**
Kia Motors	000270 KS	3.17	1.81	2.02	58.31	68.05
LG Display	034220 KS	1.14	(4.53)	4.71	20.30	(10.21)
POSCO	005490 KS	0.55	0.66	(1.61)	(5.48)	(0.65)
SEC	005930 KS	(0.73)	(3.64)	9.77	9.04	6.77
Honam Petrochemical	011170 KS	5.95	7.50	(0.39)	37.23	108.06

Note: as of 1 December, 2010;

Top BUY – Kia Motors, LG Display, Posco and SEC; Top REDUCE – Honam Petrochemical as at 8 Jan 2010

During 2010, we have closed Honam Petrochemicals and LG Display following our analysts' rating changes from REDUCE to NEUTRAL on 6 July, 2010, and BUY to NEUTRAL on 24 August, 2010, respectively

Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 106. 2010 Top Picks: absolute price performance

		P/E (x)		EPS growth (%)		EV/EBITDA (x)		PBR (x)		ROE (%)	
Company	**Bloomberg**	**FY10F**	**FY11F**	**FY10F**	**FY11F**	**FY10F**	**FY11F**	**FY10F**	**FY11F**	**FY10F**	**FY11F**
Kia Motors	000270 KS	8.6	7.5	49.9	14.6	5.2	4.4	2.1	1.7	27.2	24.8
LG Display	034220 KS	12.1	15.3	14.9	(20.8)	3.9	4.0	1.3	1.2	11.2	8.2
POSCO	005490 KS	7.9	6.9	58.4	15.2	5.2	4.4	1.1	1.0	15.3	15.6
SEC	005930 KS	8.8	9.3	65.1	(5.3)	3.9	3.5	1.4	1.3	20.6	16.6
Honam Petrochemical	011170 KS	10.0	8.3	2.9	21.5	6.8	5.7	1.8	1.5	19.9	20.0

Note: as of 1 December, 2010

Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 107. Korea: sector performance in 2010

Sector	Analyst comments on key events/news/sentiment

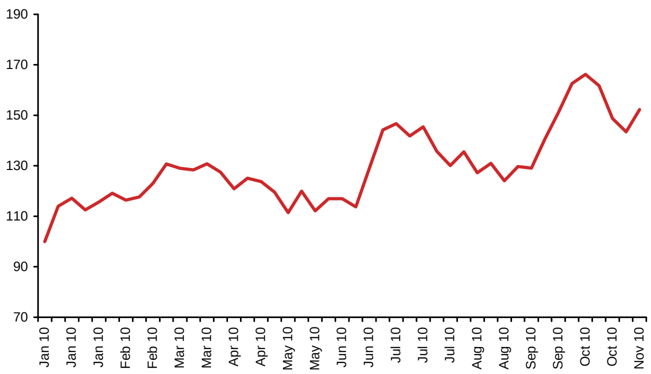
Construction

1H10: Continuing overseas (Gulf) plant orders momentum, further signs of domestic housing market recovery.
2H10: Watch for further signs of housing market recovery.

Power

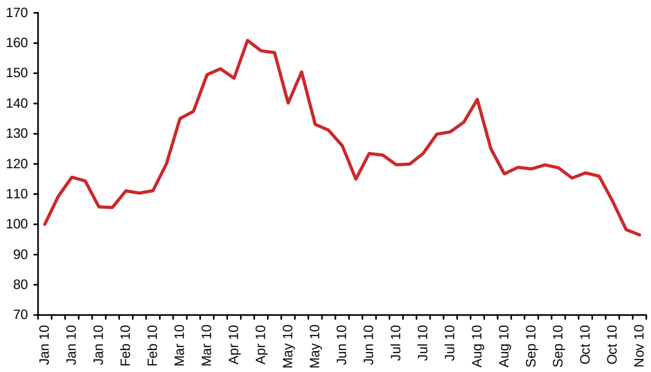
1H10: Anticipation of fuel cost escalation tariff scheme to implement in July.
2H10: Actual implementation of fuel cost scheme starts.

Container shipping



1Q10 - 2Q10 highlighted recovery in global trade activities leading to container shipping share prices outperforming Kospi.
Sharp increase in container shipping share price during June 10 given (1) 80-90% of TSA's proposed increase in annual transpacific contract negotiation (US$800/FEU for Westcoast and US$1,000/FEU for Eastcoast) were successfully implemented implying marginally profitable transpacific routes and (2) potential peak season surcharges on Asia-Europe routes.
With container shipping share price correlates with container freight rates, we continue to see improvement in container freight rates during 3Q due to container shipping peak season. Indeed, container freight rates peaked in 3Q10 due to (1) implementation of peak season surcharges on transpacific and Asia-Europe routes and (2) implementation of surcharges from box shortage. Hence, container shipping carriers announced profitable 3Q earnings and we believe earnings have peaked.

Bulk shipping



Improving bulk shipping share price from Mar10 due to increasing BDIY from 3,005 at the beginning of year to 4,209 in May 10 (peak of 2010).
Chinese steel mills were temporarily slowing production in June (due to negative cash margins with the aim to restore steel prices), leading to declining BDIY and hence bulk share price during 3Q10.
Despite 4Q being the peak season for drybulk shipping sector, the BDIY continued to fall (below our and the market's expectation); hence, leading to pressure in drybulk share prices.

Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

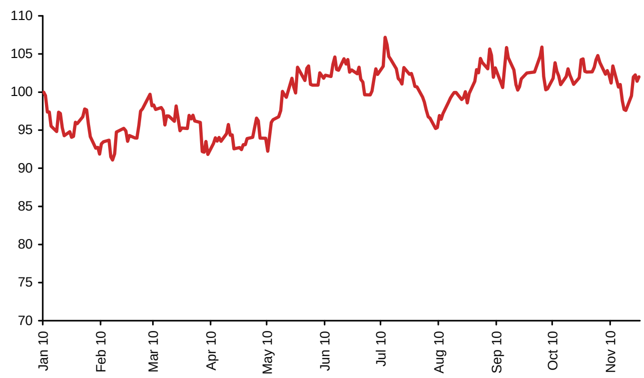
Hardware

- 1Q10: overall demand for IT products was higher than market expectation. In particular, LED was the key growth driver for Korean IT hardware names given rapid penetration of LED in LCD-TVs, leading to hardware stocks outperforming the market.
- 2Q-3Q10: However, actual demand for LED-TV was much slower than market expectation due to high price premium, resulting in oversupply of LED-TV sets and LED-related components. Moreover, not only was LED-TV demand sluggish, but demand for LCD-TV and PC s turned out lacklustre as well. We believe this is attributable to change of consumers taste toward smartphone and tablet PCs.
- 4Q10: except for beneficiaries of the smartphone boom including SEMCO, most IT hardware companies will likely see a significant drop in earnings due to still-slow demand.

Telco

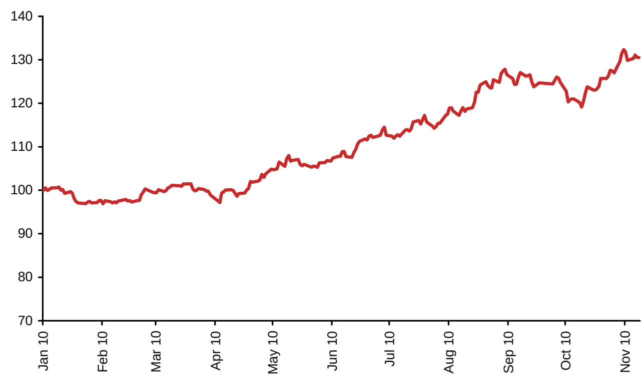
Share-price strength in 1Q10 on the expectation of smartphone-driven fundamental improvement in wireless sector. However, share price lost momentum in mid 2010 due to surging MNP and less effective marketing costs regulation.
After 3Q10 earnings results, positive sentiment was rebuilt for the sector on dividend merit and a stabilising marketing environment. The smartphone ARPU growth story remains intact.

Internet



Korean Internet sector's strong share-price momentum was largely driven by gaming sector performance. The huge success of Korean games in China boosted earnings momentum and sentiment of Korean online gaming sector throughout the year. Meanwhile, Internet portal sector performance was more volatile and driven by company-specific issue.

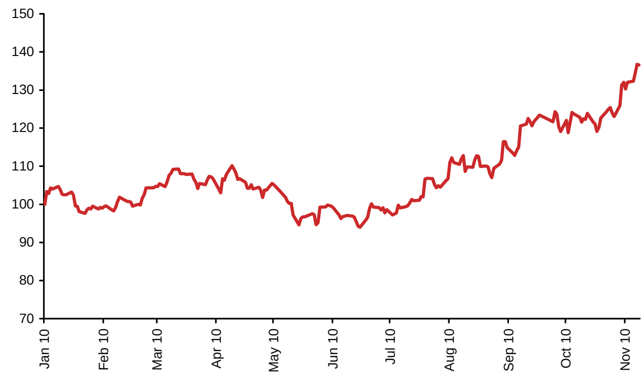
Petrochemical



- 1H10: Strong price trends
- 3Q10: LG Chem signs battery contract with Ford for 2011 Ford Focus (EV) in July.
- 3Q10: Honam Petrochemical acquires Titan Chemical, Malaysia's largest polyolefin producer, for US$1.25bn in July.
- 3Q10: Hanwha Chemical acquires 49.9% of Solarfun Power Holdings, a Nasdaq-listed solar module company, for W434bn in August.
- 4Q10: GM's Chevy Volt (equipped with LG Chem's lithium-ion battery pack) launched in November
- 4Q10: Hanwha Chemical plans to lift capacity to 1GW by FY12F and to 3GW by FY15F (current capacity: 30MW).

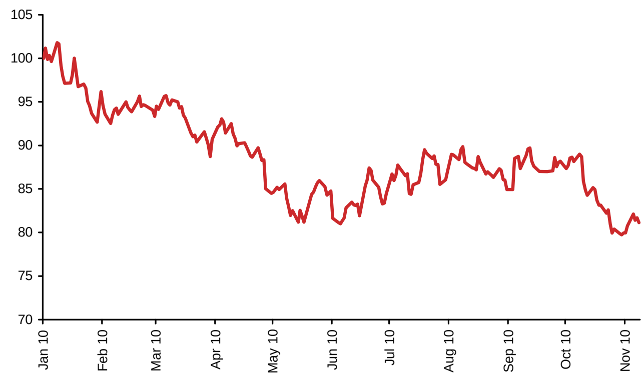
Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

Refining



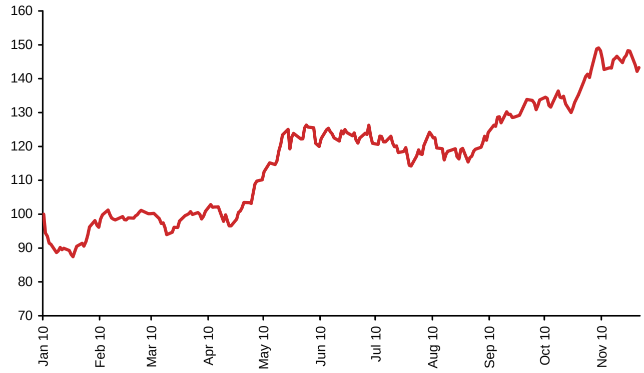
- 1Q10: Crack spreads increased led by gasoline/fuel oil spread (+67% q-q, +3% y-y)
- 2Q10: SK Energy announces restructuring plans to spin-off its refining and petrochemical divisions as 100%-owned subsidiaries in 2011.
- 2Q10: GS Retail (65.8%-owned subsidiary of GS Holdings) sells its department store and discount store divisions to Lotte Shopping for W1.34tn.
- 3Q10: SK Energy signs battery contract with Hyundai and Kia Motors.
- 4Q10: SK Energy announces 2nd oil discovery at Vietnam. Company expects daily production volume to reach 75 k bpd by end-2010.

Steel



- 1Q10: Hyundai Steel began operation of blast furnace #1 in January.
- 1Q10: Concerns about higher raw material costs as the miners demand price increase.
- 2Q10: POSCO bids for Daewoo International
- 3Q10: Korea steel makers shift to quarterly pricing system for raw materials (tracking previous quarter's spot price)
- 3Q10: POSCO acquires Daewoo International
- 4Q10: Hyundai Steel expected to begin operation of blast furnace #2 in November.
- 4Q10: POSCO to keep domestic product prices flat in 4Q
- 4Q10: POSCO guides for lower 4Q10 earnings

Autos & Auto parts



- 1Q10: Investors taking profit and concerns on won appreciation.
- 2Q10: Domestic sales fuelled by success of Kia's K5. Strong US sales for HMC from YF Sonata.
- 4Q10: Stronger than expected 3Q results as well as robust sales of HMC's newly launched models

FINANCIALS – BANKS

Sentiment

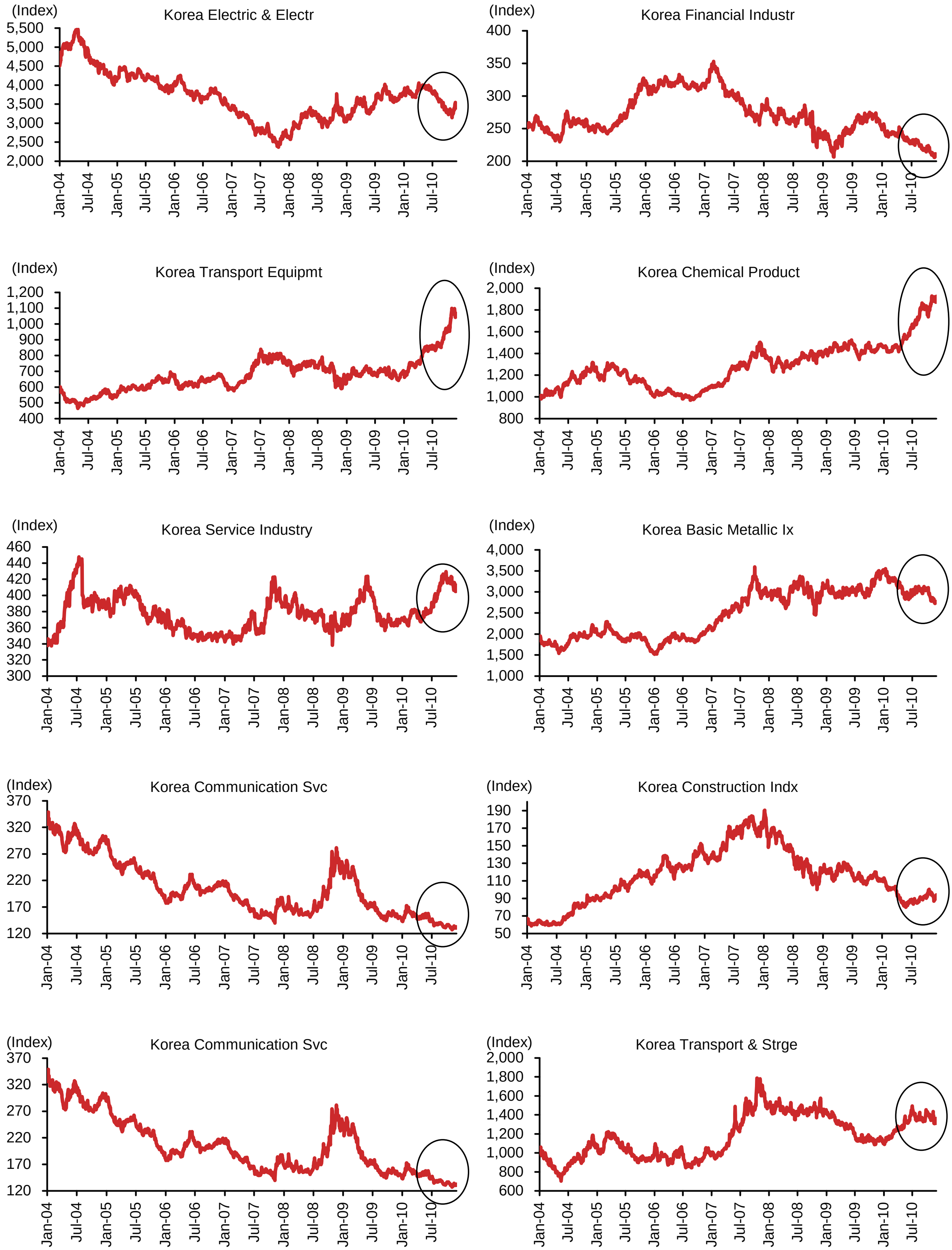
- Share prices of Korean banks underperformed the KOSPI by 17% YTD largely due to delayed recovery of the credit cycle (ie, asset quality recovery and loan growth), despite the strong macro trend in 2010.

Key Events / News

- Apr: Expectations of better than expected 1Q10 earnings
- Jun: Key concerns on asset quality of Korean banks (PF related). Announce results of 3rd round construction sector corporate restructuring
- Jul : BoK announce 25 bps rate hike to 2.25%
- Sep-Oct: Shinhan Financial Group management issue. President Shin suspended and Chairman Ra steps down.
- Oct: Temasek sells shareholding of Hana Financial Group

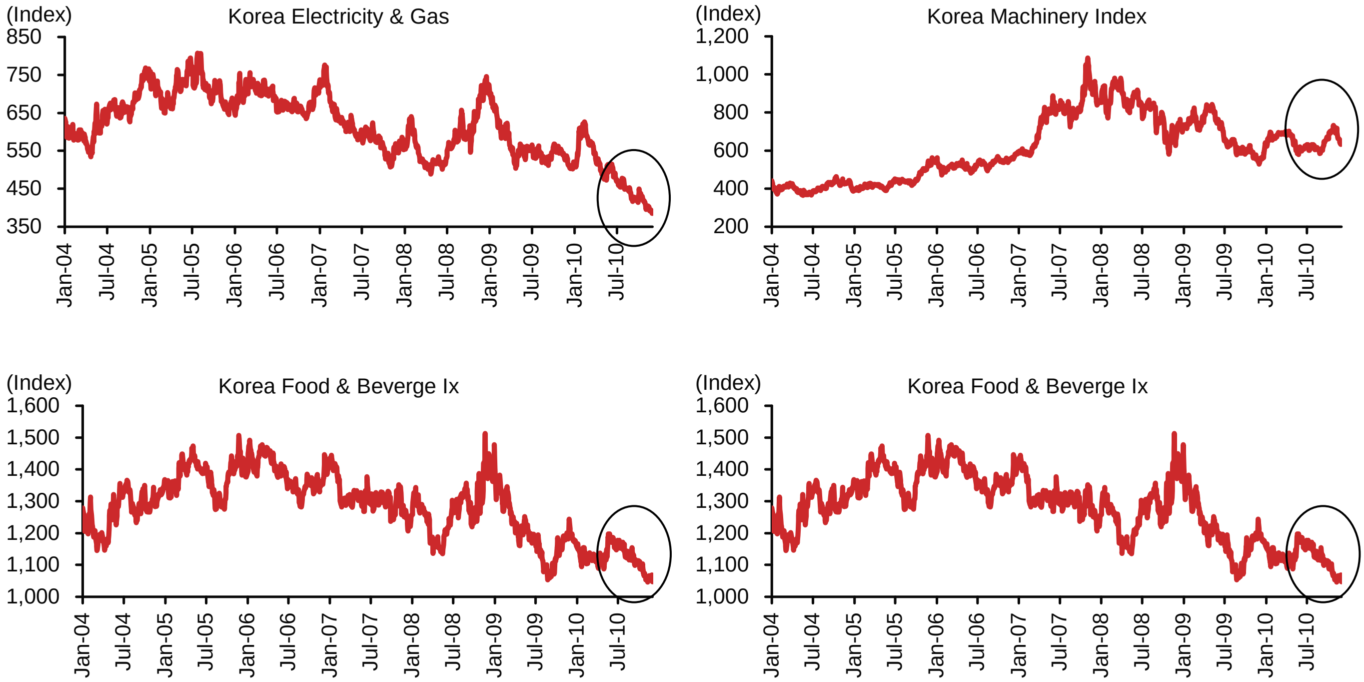
Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 108. Korea: sector performance relative to Kospi



Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

Exhibit 109. Korea: sector performance relative to Kospi (Cont'd)



Source: Bloomberg; Nomura International (Hong Kong) Limited – Investment Strategy

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Sector summaries

Autos & auto parts

BULLISH

Action

We reiterate our Bullish view on Korea autos and auto parts sector. We expect Korean auto makers to continue to expand their global market share, on aggressive new model launches, improving product quality, and brand equity. Although we expect further won appreciation in 2011, the negative impact would be negligible. Valuations are still attractive to provide downside protection. Our top pick is HMC.

Catalysts

We expect solid 4Q10 results to be announced in late January/early February, which should lead to continuous earnings upgrades.

Anchor themes

The Korean auto industry is in the middle of a re-rating process where its valuation discount to global peers is narrowing. Despite unfavourable currency movements, market share gains should continue, backed by aggressive launches of new models with improved quality.

Stocks for action

Our top pick is Hyundai Motor Company, which we think has a stronger new model launch schedule and more stable earnings flow even on a consolidated basis.

Stock	Rating	Price	Price target
Hyundai Motor (005380 KS)	BUY	179,000	210,000
Kia Motors (000270 KS)	BUY	50,500	60,000
Hyundai Mobis (012330 KS)	BUY	288,500	330,000
Mando Corp (060980 KS)	BUY	131,500	177,000
Hankook Tire (000240 KS)	NEUTRAL	32,000	34,000
Halla Climate Control (018880 KS)	NEUTRAL	18,950	22,800

Prices as of 1 Dec 2010

Outstanding drivers

① Sales growth and market share gain to continue

We forecast global auto demand to improve by 8% y-y in 2011F (from +7% y-y in 2010). Key emerging markets, notably China and India, should maintain double-digit growth on low car ownership and strong economic growth. Established markets, US and Europe, should show modest growth (+9%, +4% y-y) in 2011F, while the domestic market should stay healthy. We expect Korean auto makers to expand market share on aggressive new model launches and their focus on small to mid-sized sedans, which are popular in high-growth developing markets.

② Improving brand equity translating into more earnings

Korean auto makers have shown fast improvement in their brand equity. Their residual values have shown the steepest increases in the industry, with some of the recently launched models being ranked as the top in their respective segments. Resultantly, Hyundai and Kia have cut down their incentive offerings and the marketing expenses significantly, without any negative impact on their market share trend. This has been the key positive earnings surprise factor, through massive increase in the equity earnings from overseas subsidiaries.

③ Limited *impact* from won appreciation

While we expect won to appreciate further in FY11F, which may pose concerns for some investors, we believe the negative impact for Korean auto makers should be negligible. Their earnings sensitivity to forex movement has declined with their aggressive overseas capacity expansions and increasing foreign currency borrowing portion. Also, new model launches at higher selling prices should have a stronger positive impact on profit margins, more than offsetting the currency impact.

④ Still attractive valuation

Despite impressive outperformance in 2010, Korean auto companies still trade at over 30% discount to global peers. We believe Korean auto industry is in the middle of a re-rating process, to eliminate the valuation gap in the long term. Our top pick is HMC, based on its strong new model launch schedule and stable earnings flow.

Analyst

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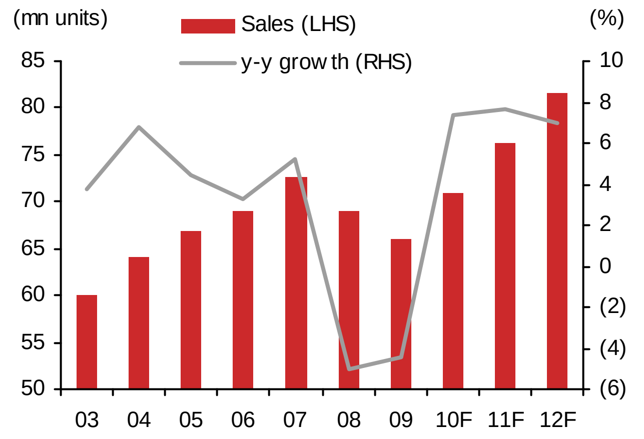
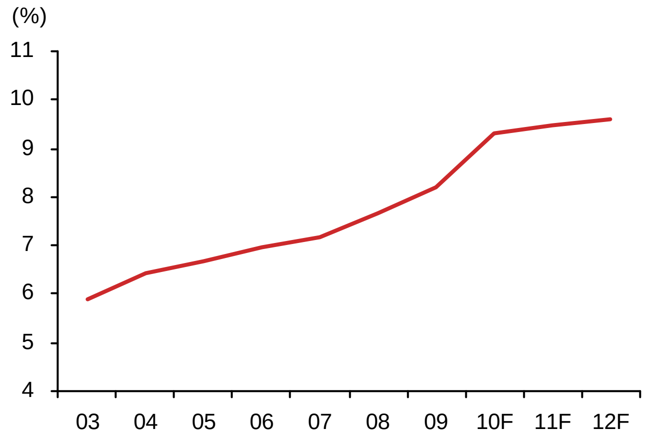
Exhibit 110. Global auto sales trend



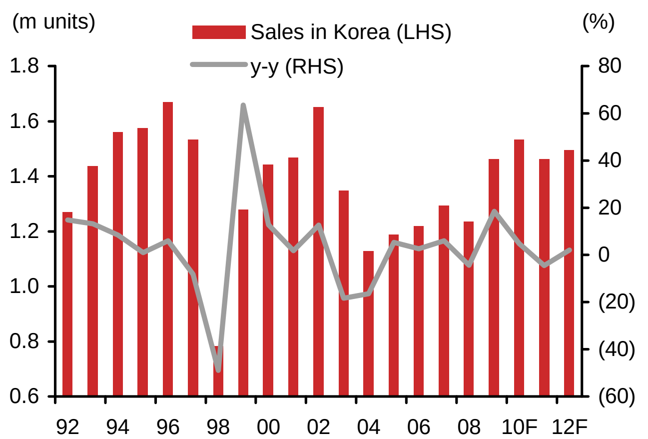
Source: KAMA, Nomura estimates

Exhibit 111. Korean OEMs: global market share trend



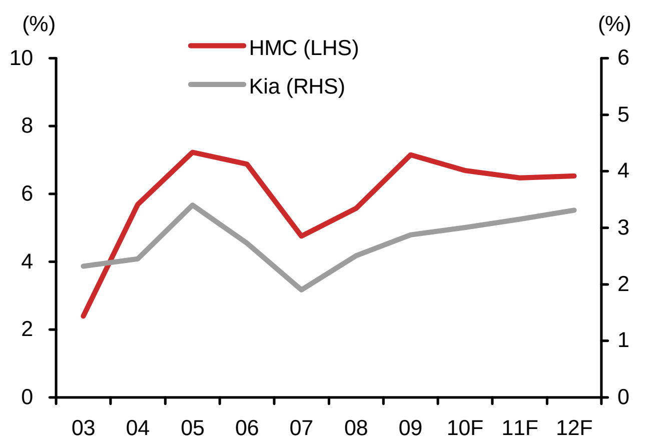
Source: KAMA, Nomura estimates

Exhibit 112. Korea: auto sales volume trend



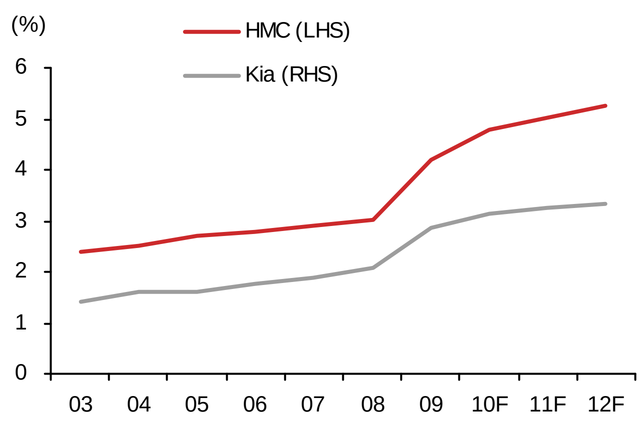
Source: KAMA, Nomura research

Exhibit 113. China: Hyundai/Kia market share trend



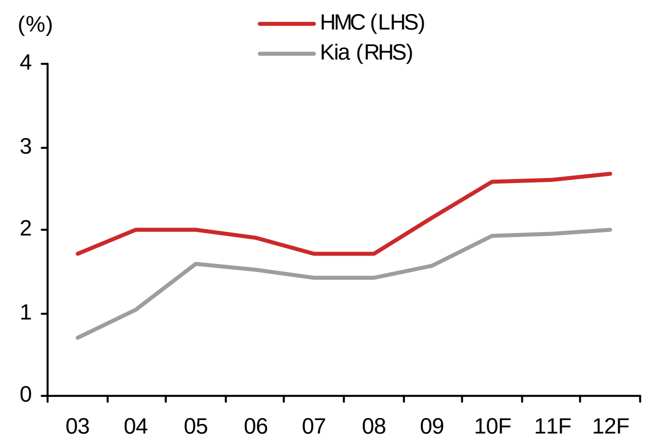
Source: Bank of Korea, KAMA, Nomura research

Exhibit 114. US: auto sales volume trend



Source: Autodata, Nomura estimates

Exhibit 115. US: Hyundai/Kia market share trend



Source: Autodata, Nomura estimates

Exhibit 116. HMC: New model launch schedule

Region	Launch date	Model name	Category	Engine size	Note
	Jan-11	HG	Large sedan	2.0-3.3	Grandeur replacement (Azera)
	1Q11	Veloster	Compact coupe	1.6	Based on Avante (140HP engine)
	2H11	Sonata hybrid	Mid sedan	2.4	212HP, 17km/L mileage
	3Q11	i30	Hatchback	1.5-2.0	Revamped model with new powertrain & design
	2H11	Santa Fe	SUV		Santa Fe replacement
	2H11	VF	Mid sedan		European sedan (new model)
China	1H11	YF Sonata	Mid sedan	2.0/2.4	New Sonata
US	Dec-10	MD	Mid sedan	2.0	Avante replacement (Elantra)
	1H11	Veloster	Compact coupe	1.6	Based on Avante (140HP engine)
	1H11	RC	Small sedan	1.3-1.5	Accent replacement
Europe	1Q11	Veloster (FS)	CUV	1.6	Based on Avante (140HP engine)
	2Q11	VF	Mid Sedan	2.0/2.4	Same platform as Sonata
	4Q11	GD	hatchback	1.5-2.0	New i30

Source: Company data, Nomura research

Exhibit 117. Kia: New model launch schedule

Region	Launch date	Model name	Category	Engine size	Note
Korea	Jan-11	TA / Morning	Compact sedan	+/- 1.0	Morning replacement
	May-11	K5 hybrid	Mid sedan	2.4	
	Aug-11	UB / Pride	Small sedan	+/- 1.0	Pride replacement
	4Q11	UA (New model)	CUV	1.0	new model
	2012	K3	Mid sedan	1.6/2.0/2.4	Forte replacement
	2012	CH (K9)	Large sedan	2.7-3.7	Opirus replacement
	2012	Carens	RV	2.0	Carens replacement
China	Feb-11	K5	Mid sedan	2.0	Lotze replacement
	Aug-11	UB / Pride	Small sedan	+/- 1.0	Pride replacement
US	Jan-11	K5	Mid sedan	2.0/2.4	Lotze(dubbed Optima in the US) replacement
	1Q11	Forte Hatchback	Hatchback	2.0/2.4	5-door model, 3rd Forte version
	Apr-11	K7	Large sedan	2.4/2.7/3.5	
	1H11	K5 hybrid	Mid sedan	2.4	
	Jul-11	UB / Pride	Small sedan	+/- 1.0	Pride replacement
Europe	Feb-11	TA / Morning	Compact sedan	+/- 1.0	Morning replacement
	Apr-11	K5	Mid sedan	2.0	Lotze replacement
	May-11	UB / Pride	Small sedan	+/- 1.0	Pride replacement

Source: Company data, Nomura research

Banks

BULLISH

Action

We see only marginal risk of construction/project finance-related provisioning beyond 2H10F, and regulatory support is likely to back a property-market recovery. These bode well for asset quality and bolster our projections for a NIM turnaround in 2H10F. While we caution that 2H10 earnings could again disappoint broadly, due to provisioning and margin pressure, we think long-term investors should move into position now. KBFG is our top pick among Nomura's universe of Korean banks.

Catalysts

Earnings recovery led by: 1) normalisation of credit costs; 2) loan growth in line with macro growth and 3) higher interest rates.

Anchor themes

Moderating de-leveraging forces and regulatory support to the undersupplied property market have set the stage for a benign credit cycle for Korean banks. We also expect normalisation of monetary policy, once asset prices recover.

Stocks for action

Top Buy – KB Financial Group

Stock	Rating	Price	Price target
KB Financial (105560 KS)	BUY	54,100	70,000
Shinhan (055550 KS)	BUY	44,800	60,000
Woori (053000 KS)	BUY	14,250	18,000
Hana (086790 KS)	Neutral	37,950	39,000
IBK (024110 KS)	BUY	16,150	20,000
KEB (004940 KS)	BUY	11,300	17,500
Daegu (005270 KS)	BUY	13,650	20,000
Busan (005280 KS)	Neutral	14,500	14,000
KB Financial (105560 KS)	BUY	54,100	70,000
Shinhan (055550 KS)	BUY	44,800	60,000

Prices as of 1 Dec 2010

Full cyclical

① Reflecting a more positive view on Korean banks

Our projections for a NIM turnaround from 2H10F are intact for Korean banks. We also look for asset quality to recover and loan growth to evolve amid a more benign credit cycle after earnings pressure in 2H10F. The unprecedented disassociation of the credit cycle from the economic cycle, which we think has hindered bank share performance, is likely to end. Accordingly, in our 30 September, 2010 Korea banks report, *Full Cyclical,* we raised our FY11F earnings forecasts by an average 10% and lifted our PT for KBFG to W70,000 and upgraded WFH a notch to BUY. We maintained our BUY rating and price target for IBK but changed our recommended top pick to KBFG, followed by SFG.

② Benign credit cycle lies just ahead

We expect the property-market centric credit cycle of Korean banks to bottom out in 2H10, upholding asset quality and loan growth. Our review of Korea's top 114 construction players shows only marginal credit risks related to construction/ project finance loans remain beyond 3Q10. Regulatory support should also contribute to the recovery of the property market, cutting credit costs and boosting loan growth at the Korean banks. This, in turn, should lead to normalisation of monetary policy and higher interest rates. Accordingly, we project average EPS growth of 48% y-y for the Korean banks on 6.5% y-y loan growth, and credit costs of 71bps over average loans and NIM expansion of 8bps y-y for FY11F.

③ M&A: options, obstacles and opportunities

Various scenarios are under discussion for privatisation of WFH and Lone Star's KEB stake sale. In any case, we maintain our Neutral stance on M&A given that regulatory constraints on minority shareholder treatment and financial leverage have made acquisition more expensive and less value accretive. Yet, we do not rule out possible value unlocking for KEB and WFH's regional bank subsidiary.

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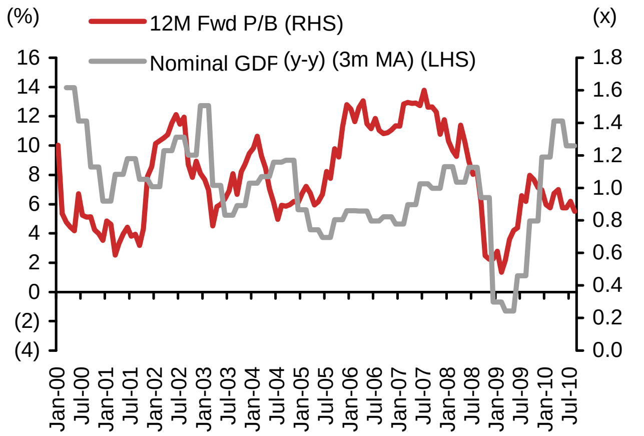
Key share price drivers for Korean banks

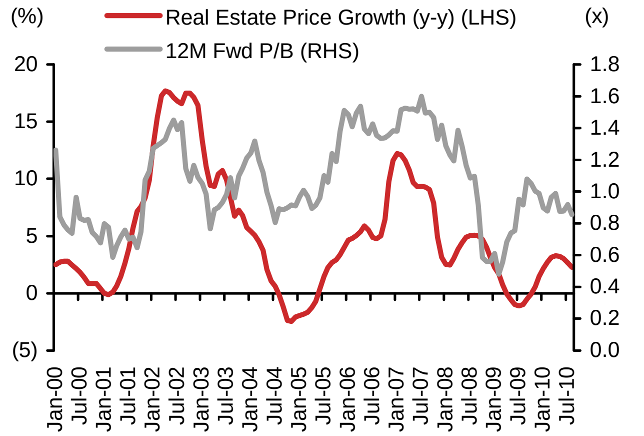
Key share price catalysts

Exhibit 118. Korea Banks: Agg. P/B vs Nominal GDP



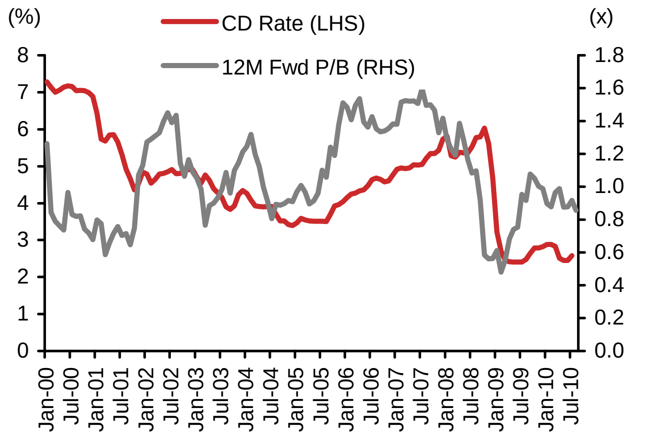
Source: Company reports, Nomura research

Exhibit 119. Korea Banks: Agg. vs Housing price



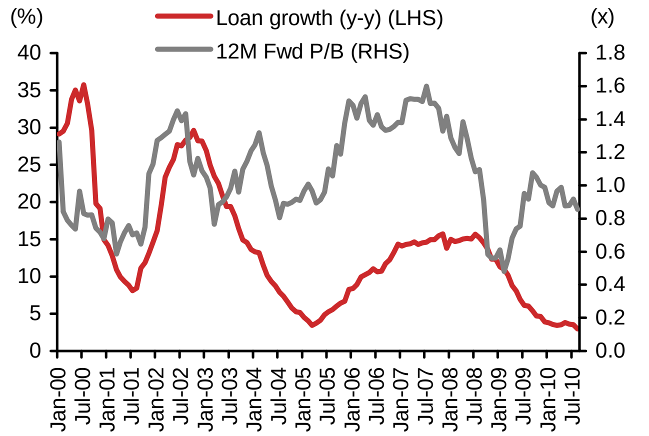
Source: Company reports, FSS, and, Nomura research

Exhibit 120. Korea Banks: Agg. vs 3M CD Rate



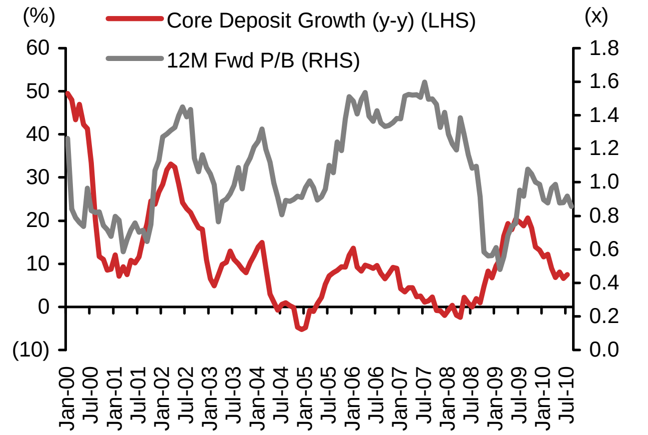
Source: Company reports, FSS, and, Nomura research

Exhibit 121. Korea Banks: Agg. vs Loan growth



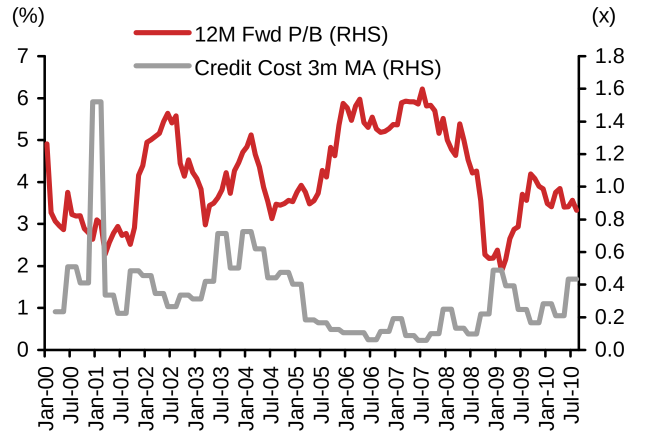
Source: Company reports, FSS, and, Nomura research

Exhibit 122. Korea Banks: Agg. P/B vs Core deposit growth



Source: Company reports, Nomura research

Exhibit 123. Korea Banks: Agg. P/B vs Credit costs (over avg. loans)



Source: Company reports, Nomura research

Chemical

BULLISH

Action

Rising consumption growth and slowing capacity additions globally will likely lead to the "Golden Age" of petrochemical industry. We recommend investors to own a basket of chemical names in Korea, combining both structural and cyclical benefits. The cyclical upturn should last into 2012F.

Catalysts

Positive catalysts could emerge from further evidence of rising Chinese demand and stronger product margins next year.

Anchor themes

We believe the chemical sector is poised to enter a Golden Age, benefiting from rising demand and restrained capacity additions over the next two years. We believe the sector's rerating will be underpinned by expectations of an ethylene upcycle, receding fears of oversupply and upward revisions in street estimates.

Stocks for action

LG Chem is our top BUY for its diverse and competitive product mix.

Stock	Rating	Price	Price target
LG Chem (051910 KS)	BUY	W395,500	W500,000
Honam PC (011170 KS)	BUY	W258,000	W330,000
Hanwha Chem (009830 KS)	BUY	W33,350	W40,000

Prices as of 1 Dec 2010

A Golden Age

① China's structural demand growth

We believe that rising consumption growth in China, brought about by favourable government policies (direct subsidies for goods, minimum wage hikes), structural factors (urbanisation, rising middle-class population), and the 12th Fifth Year Plan (consumption-driven growth, development of Central & Western China), are likely to result in strengthening chemical demand growth. In our 30 November, 2010 regional Anchor Report, *A Golden Age,* we raised our global demand forecast for key products by 0.4-2% pa over the 2010-12F period.

② Global capex cycle is coming to an end

With global capacity additions entering a lull in the 2011-12F period (a legacy of the 2008 financial crisis), we believe margins across a range of key products are likely to rise further in that period. Since we raised our margin forecasts for key products, we also revised our projections for diversified producers: we now expect them to generate record profits over 2011-12F – the Golden Age.

③ Ethylene upcycle continuing beyond 2012F

Beyond 2012, we believe sector margins may decline as new capacity (announced and unannounced) could result in a loosening supply/demand balance. However, in the case of ethylene, we forecast a steady upcycle from end-2011 through 2015. An ethylene 'supercycle' could take place if crude prices remain benign and annual demand grows uninterruptedly at 5% pa throughout the period.

④ Stock picks – LG Chem is our top BUY

Our top BUY is LG Chem for its diversified product mix and new business potential. Investors, we reckon, should focus on the positive trend of the petrochemical business, start of automotive battery shipments and recovery of the electronic materials from early FY11F. We believe LGC will be a direct beneficiary of the petrochemical upturn we expect in 2011-12F.

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Exhibit 124. Global ethylene supply & demand (annualised capacity)

(mn t)	02	03	04	05	06	07	08	09F	10F	11F	12F	13F	14F	15F
Capacity	109.8	110.8	111.4	115.8	120.3	125.1	129.7	130.4	138.8	146.1	147.5	153.0	156.4	158.6
Demand	95.6	98.4	104.1	104.4	109.0	114.8	109.5	114.3	119.4	124.9	131.0	135.9	141.3	147.0
Operating rate (%)	87.1	88.9	93.5	90.1	90.6	91.8	84.4	87.6	86.0	85.5	88.8	88.8	90.4	92.7
Capacity growth (%)	5.3	0.9	0.6	4.0	3.9	4.0	3.7	0.6	6.4	5.3	1.0	2.9	2.2	1.4
Demand growth (%)	4.2	2.9	5.8	0.2	4.5	5.3	(4.6)	4.4	4.4	4.7	4.8	4.0	4.0	4.0
Capacity growth (mn t)	5.5	1.0	0.6	4.4	4.5	4.8	4.6	0.8	8.4	7.3	1.4	4.3	3.4	2.2
Demand growth (mn t)	3.8	2.8	5.7	0.2	4.7	5.7	(5.3)	4.8	5.1	5.6	6.0	5.2	5.4	5.7

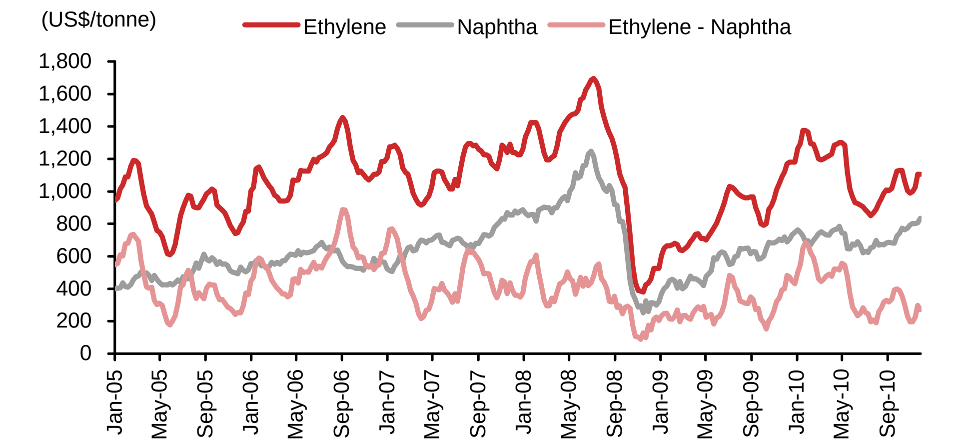
Source: CMAI, Nomura estimates

Exhibit 125. Company product gearing matrix (by revenue, merchant sales of chemicals only)

	Upstream							Mid-stream								Downstream												Fibres		
(%)	Ethylene	Propylene	Butadiene	Benzene	Paraxylene	Orthoxylene	Caustic soda	Acetone	Acrylonitrile	BPA	MEG	Oxo-alcohols	Phenol	PTA	Styrene	Acrylic ester	ABS	ECH	Epoxy resin	MMA	Plasticizer	PC	PE	PP	PS	PVC	SBR/BR	Nylon	Polyester	Rayon
FPC							7		12							13		4		4			25	10		24				
FCFC						7		3					8	25	13		10					7		8	5			8		6
NYP										17	27	7							15		16								19	
LGC							3	3		2	3	5	5			3	19				4		18	6	3	21	4			
Honam			4								25			11	12							2	19	22					5	
Hanwha		16					30					4			5								26			19				
PTT Chem	29	18									10												43							

Source: Company data

Exhibit 126. Ethylene price and margin



Source: Thomson Reuters Datastream

Construction

BULLISH

Action

The outlook for the next two years is strong overseas/domestically, but valuations are below 2007 peaks. Even more than earnings, we think E&C shares will continue to be driven by: 1) new order and backlog growth, 2) domestic and overseas macro conditions (eg, oil price) and 3) domestic deregulation. We remain Bullish.

Catalysts

Korean E&C majors have grown overseas backlog 750% in the past three years, driven by the Gulf's build-out in energy and power plants and market share gains. Overseas backlog continues to mount, now at 4-5x annual sales (vs 1x in FY03). Overseas margins have swung firmly into positive territory for most E&C majors.

Anchor themes

Building domestic apartments is a key long-term focus. E&C majors have a housing backlog of seven years of annual homebuilding sales. A few have a backlog in excess of 10 years of annual housing sales. Housing supply is short.

Stocks for action

SSE, GSEC, DLI are our top BUYs. Valuations are around half of 2007 peaks, even though our BUY-rated E&Cs' share prices are up sharply in the past six months. Consensus price targets have been raised significantly.

Stock	Rating	Price	Price target
SSE (028050 KS)	BUY	197,000	250,000
GSEC (006360 KS)	BUY	105,000	120,000
DLI (000210 KS)	BUY	115,000	120,000

Prices as of 1 Dec 2010

Construction intervention

① Overseas/Gulf: Korean EPCs top market share

Korean E&C/EPC plant engineering majors have grown market share to 40% in the most lucrative of overseas markets, in the Gulf Co-operation Council (GCC) states, where petrodollar recycling has boosted the projects market. Korean majors' overseas backlog and new orders have grown by eight times since 2005. Overseas construction is becoming construction majors' largest earnings source.

② Domestic housing: set for 2011 recovery; general contracts

In Seoul, apartment supply is projected to fall by half in 2011. Rising lease prices also foretell a supply squeeze. Provincial cities, once dubbed "the graveyard for apartment construction", are leading the housing market recovery. Deregulation will also help sales of multi-year building backlogs. Infrastructure and redevelopment should keep E&Cs busy. While still a "pipedream", undersea tunnels to Japan and China are being contemplated more seriously (US$100bn+ each).

③ Nuclear plant engineering (and alternative power)

The US$20bn UAE nuclear power deal heralded a new era for Korean nuclear plant engineering and service firms. The APR1400 reactor model has provided Korea's consortium with a competitive edge in pricing, construction periods, and higher nuclear plant usage. E&Cs are more active in alternative power projects.

④ Valuation; stock selections

Construction Top BUYs: Samsung Engineering, GS E&C, Daelim Industrial, in order of preference. We think growth in new orders and backlog is more important to share prices than earnings. The Kospi E&C sector index gained 100% in 2006-07, despite slow earnings growth. Under these circumstances, our valuation methodology of choice is EV/backlog. On other key valuation metrics, the sector is also well below 2007 peaks. Despite having gained 27% over the past six months, the Kospi construction sector index is at less than half (-53%) of its 2007 peak. Bullish.

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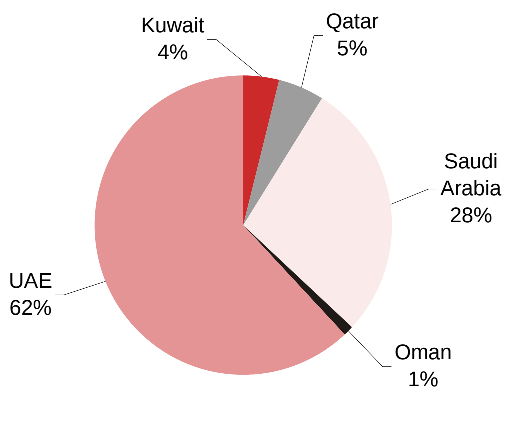
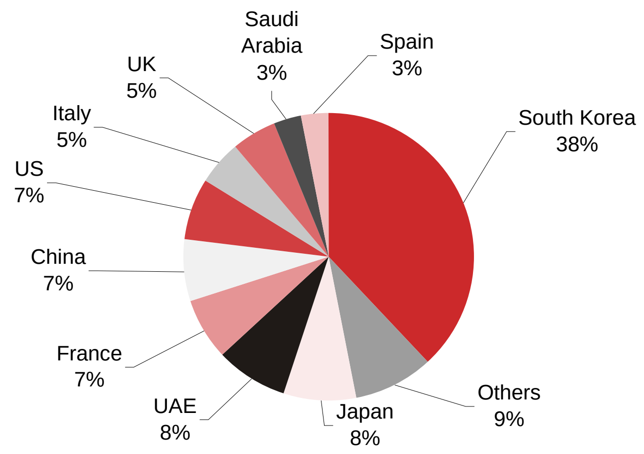
Exhibit 127. GCC contracts by awarding country



Note: % of US$46bn, 2009-10 GCC hydrocarbons plant market

Source: MEED

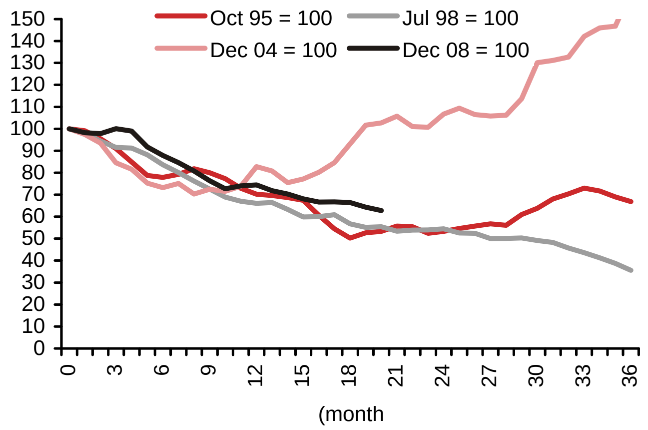
Exhibit 128. EPC awards by contractor nationality



Note: % of US$46bn, 2009-10 GCC hydrocarbons plant market

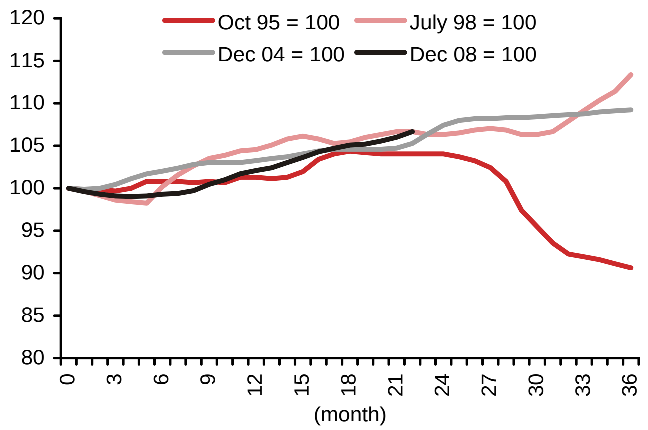
Source: MEED

Exhibit 129. Unsold units: nationwide



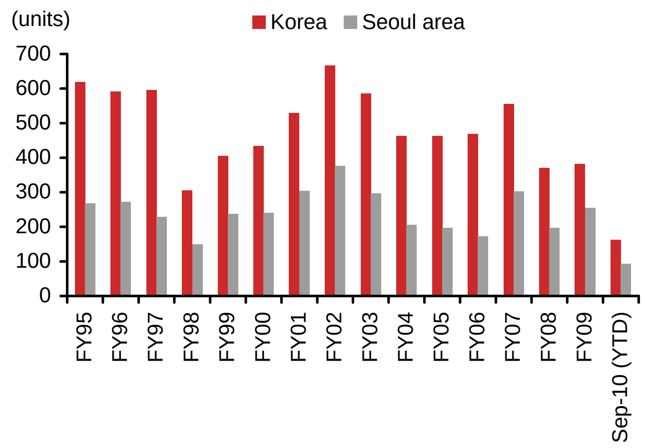
Source: MLTM, Budongsan 114

Exhibit 130. Apartment price: provincial cities



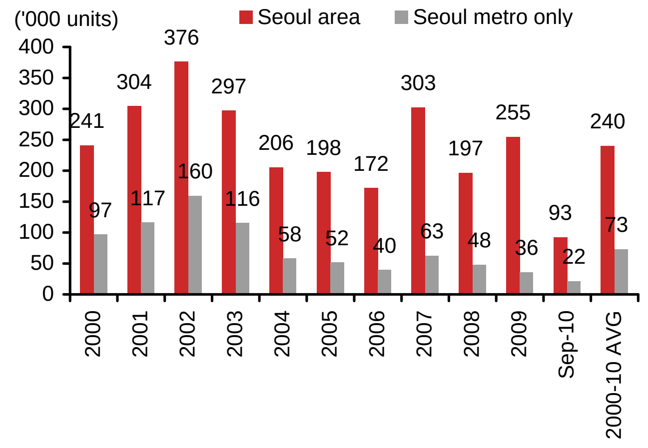
Source: Kookmin Bank

Exhibit 131. Korea housing supply



Source: MLTM, Kookmin Bank

Exhibit 132. Seoul area housing supply



Source: MLTM

Exhibit 133. Progress of upcoming overseas nuclear power plant projects

Country	Status	Date
South Africa	Signed agreement for nuclear business cooperation	8 October 2010
Argentina	Signed MOU for nuclear cooperation	17 September 2010
Turkey	Intergovernmental agreement signing during G-20 (prior to commercial contract in FY11)	11-12 November 2010
	Signed MOU (Memorandum of Understanding) to build two nuclear reactors in Sinop on the Black Sea	16 June 2010
UAE	Signed commercial contract for the construction of 4 nuclear reactors in Ruwais of Abu Dhabi	27 December 2009
Mexico	Planning to sign an MOU on nuclear power generation research and technology	2010 or 2011
Philippines	Planning to sign an MOU for nuclear business cooperation	TBD
India	Agreed with India to start negotiations to help Seoul make inroads into the Indian nuclear energy market.	18 June 2010
China	Korea is also looking into China which is planning to build more than 100 nuclear power plants	TBD

Note: Korea is also currently in talks with Malaysia, Lithuania and Finland for the possible construction of nuclear power plants.

Source: Company data

Consumer related

BULLISH

Action

While we remain positive on general consumption, we prefer TV home shopping to off-line retailers on structural shift to higher-end and recovery in intangible product sales. With either rising raw material or demanding valuation, staples (near staples) will have a weaker performance, in our view. Hyundai Home Shopping (HHS) is our top pick with biggest implied upside.

Catalysts

Subsidiary IPO is an upside catalysts for home shoppers. China performance will be a swing factor for earnings as well as valuation.

Anchor themes

We turn less positive on off-line retail on slower growth on high base and ongoing saturation. With no presence or poor performance in overseas operations, off-line should be less highlighted than TV home shopping, which we believe is the most attractive sector for FY11F.

Stocks for action

We recommend TV home shopping as top sector for FY11F with HHS as our top pick. China plays (Orion and Lock&Lock) should continue to do better backed by stronger earnings momentum from China.

Stock	Rating	Price	Price target
Hyundai Home Shopping (057050 KS)	BUY	95,300	**143,000**
KT&G (033780 KS)	NEUTRAL	64,400	65,000
CJ O Shopping (035760 KS)	BUY	264,900	320,000
GS Home Shopping (028150 KS)	BUY	107,000	154,000
Hyundai Department Store (069960 KS)	NEUTRAL	127,000	130,000
LG H & H (051900 KS)	NEUTRAL	385,500	410,000
Lotte Shopping (023530 KS)	BUY	483,000	570,000
Orion (001800 KS)	BUY	402,000	470,000
Amore Pacific (090430 KS)	NEUTRAL	1,073,000	1,050,000
Shinsegae (004170 KS)	NEUTRAL	578,000	540,000
Seobu Truck Terminal (006730 KS)	BUY	18,350	34,000
Lock & Lock (115390 KS)	BUY	37,650	52,000

Prices as of 1 Dec 2010;

FY11F, year for TV on-line retail

① We remain positive on consumption in general

We remain positive on general consumption given continuous economic growth (increasing wage), the expected recovery in the property market price and strong increase in the number of tourists to Korea. Given a high base in FY10F, FY11F same-store-sales growth across retail formats is likely to be slower y-y. With weaker growth momentum in Korea and poor performance in China, we maintain a NEUTRAL on Shinsegae, while we maintain BUY on Lotte Shopping on relatively attractive valuation and solid earnings growth in Korea with fast selling space growth.

② TV home shopping remains the most attractive

Thanks to a continuing shift to higher-end and apparel in product mix as well as the expected recovery in the tangible product sales growth, TV home shopping should have faster sales revenue and profit growth in FY11F. We like TV home shopping as it seems to have the competitive edge required for success in emerging countries (including China and India) with a superior operating model, lower capital investment required and faster growth in the market size relatively to developed markets. Subsidiaries' IPO scheduled in FY11F (China operation and CATV system operator subsidiaries) could highlight asset value, which is an upside to our forecast. We pick Hyundai Home Shopping as our top pick under the Korea universe on the greatest implied upside.

③ Selective approach to staples on valuation

With rising raw material costs and difficulty in raising product prices given the government's tight price control on rising inflation, we are less positive on food and other staple names. Demanding valuation is another reason why we expect lukewarm share performance. We recommend investors stick to China plays like Orion and Lock&Lock, where we expect stronger earnings growth on faster growing China earnings. We maintain NEUTRAL on KT&G due to structural downturn in volume, continuous market share loss and limited upside from new businesses. Although we are long term positive on fundamentals of cosmetic companies (LGHH and Amorepacific), we consider valuation unattractive.

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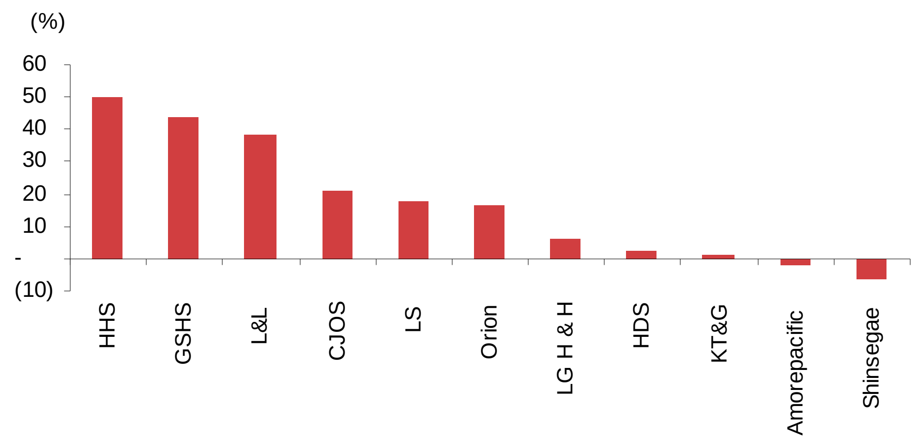
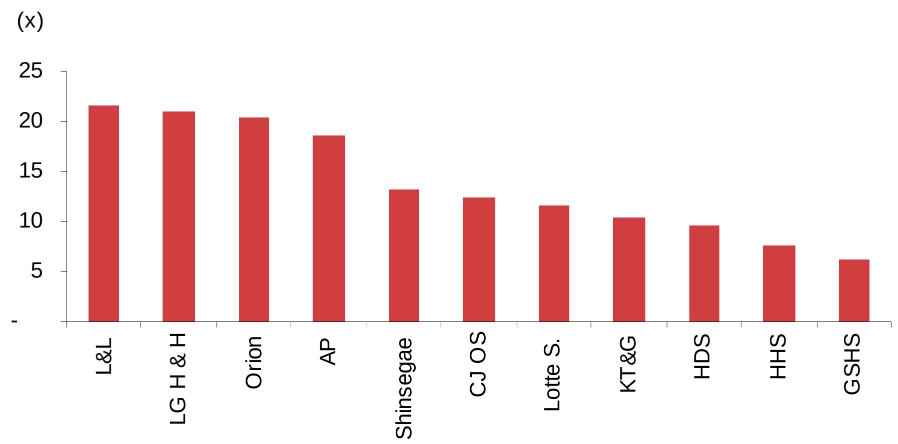
Exhibit 134. Implied upside to our PT



Note: pricing as of 1 December, 2010

Source: Nomura research

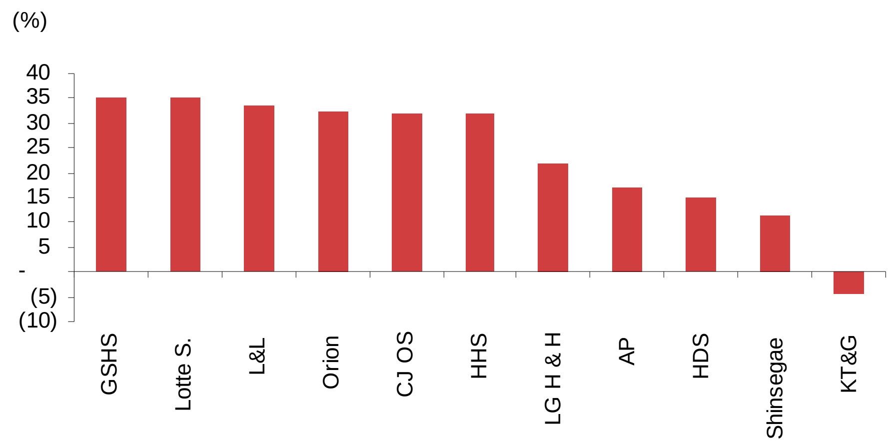
Exhibit 135. FY11F P/E comparison



Note: pricing as of 1 December, 2010

Source: Nomura research

Exhibit 136. FY11F EPS growth comparison



Note: pricing as of 1 December, 2010

Source: Nomura research

Internet

BULLISH

Action

We recommend investors to focus on leading Korean online gaming companies, which are well positioned to see accelerating overseas business momentum going forward. China exposure is the key differentiating factor. Neowiz Games is our top BUY due mainly to its substantial upside on its business momentum in China. We will refocus on new product launch momentum on NCsoft in 2H11.

Catalysts

More visible launch timing for major products remains a share price catalyst for the online gaming sector. For portal sector, further acceleration in online ad revenue and for NHN specifically, potential progress in the Japanese search business could revive the share price momentum, in our view.

Anchor themes

For online gaming sector, overseas growth momentum remains the key to a further re-rating, backed by a resilient domestic growth profile.

Stocks for action

We prefer the online gaming sector over online portal, based mainly on overseas momentum. Our top pick is Neowiz Games which we prefer on a 6 month view. We like NCsoft in the longer term on product launch momentum in late 2011.

Stock	Rating	Price (W)	Price target (W)
NHN (035420 KS)	BUY	193,500	224,000
Daum (035720 KS)	BUY	76,300	98,000
NCsoft (036570 KS)	BUY	255,000	310,000
Neowiz Games (033630 KS)	BUY	47,600	71,000
CJ Internet (037150 KS)	BUY	15,700	20,000
Megastudy (072820 KS)	NEUTRAL	176,600	182,000

Prices as of 1 Dec 2010.

Overseas momentum continues

① Overseas growth momentum; key to online gaming re-rating

We believe increased demand from Chinese publishers for Korean online games should serve as key catalyst for the online gaming sector. As blockbuster games such as Blade&Soul, Guild Wars 2, and Tera are expected to launch in FY11F, we expect lucrative contracts with major Chinese publishers in the near future. Moreover, we anticipate further upside on existing games such as CrossFire and A.V.A. to drive royalty revenue from overseas markets.

② Resilient online ad growth intact in FY11F for Korean portals

We believe the key merit of online portal, defensiveness with resilient growth profile, is still solid investment point. We forecast 4% growth in total ad spend in FY11F and 15% for online ad. Mobile advertising and SNS have surfaced as hot topics of late; however, we believe them to be more of long-term growth drivers for portals.

③ Cautious view on online education sector

Despite recent share price rally due to harder-than-expected K-SAT, we are cautious on the recovery of high-school online business owing to governments' strong stance against private education and limited upside to the penetration rate. We expect the government's next official announcement on next year's K-SAT to be an important swing factor.

④ Prefer online gaming sector to online portal

Compared to online portals, we prefer the online gaming sector on more compelling valuation and robust overseas growth profile. We prefer Neowiz Games on a 6-month view due mainly to its strong earnings momentum and attractive valuations. We like NCsoft in the longer term (12 month view) on new product launch momentum in FY11F.

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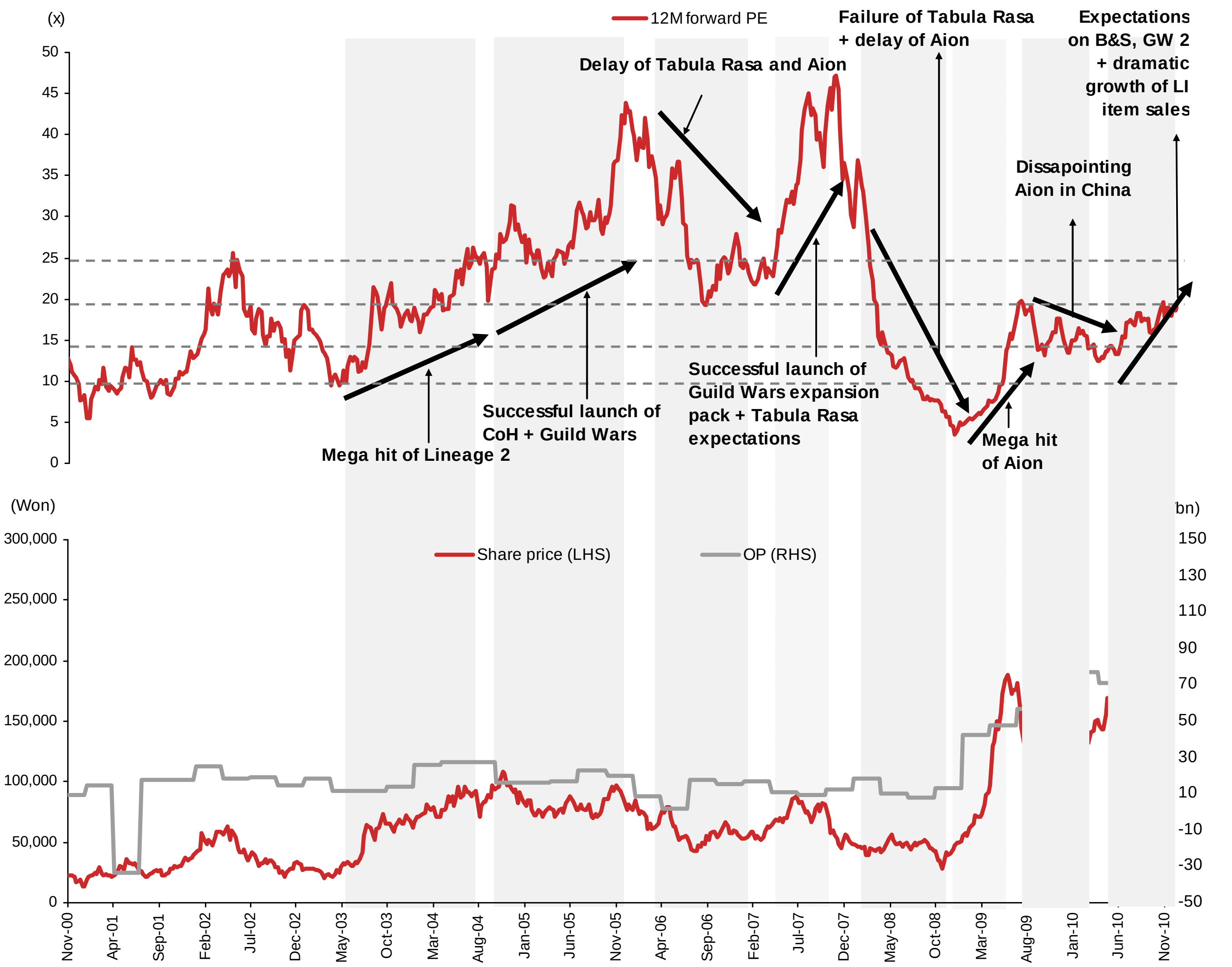
Exhibit 137. Internet peer comparison

	Archeage	Aion	Blade&Soul	Guild Wars 2
Development cost	W30bn (Digital Daily, 5 Sep '10)	W23bn (ET News, 17 Dec '08)	W30bn (HanKook Ilbo, 23 Feb '10)	na
Development period	2006~ present	2004~2008	2006 ~ present	2006 ~ present
Developer	XL Games (founded by Jake Song, creator of Lineage)	Ncsoft	Ncsoft	ArenaNet (US subsidiary of Ncsoft)
Key characteristic	-High level of freedom; aimed to mimic the real society in the virtual world, accentuating interaction between the players	-PvPvE system - Flights plays vital role in travel, combats, quests, etc..	-Relatively fresh theme of oriental martial arts. -PvP and questing 50:50 ratio	- Strengthened RPG factors vs GW 1 - Dynamic event system
Key target market	Asia	Global (tilted towards Asia)	Global (more tailored to Asia, especially China)	US/Europe
CBT/OBT /Commericialization	- 1st CBT : Jul 2010 - 2nd CBT expected in Nov 2010; we expect commercialization in 2H11	- 1st CBT: Oct 2007 - 2nd CBT: Apr 2008 - 3rd CBT: Jul 2008 - OBT: 11 Nov 2008 - Commercialization: 25 Nov 2008	- Demo version likely to be made available at annual G-Star game show in Nov - CBT schedule not set; we expect in 4Q10 or early next year, commercialization in mid 2011	- Demo version revealed at Gamescom in Aug 2010 - CBT schedule not set; we expect in 4Q10 or early next year, commercialization in 2H11

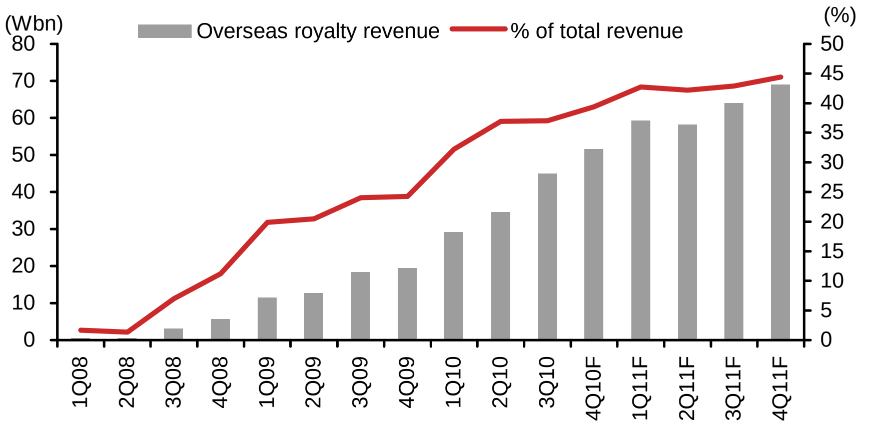
Source: indicated in table, otherwise Nomura estimates, Company data

Exhibit 138. 12M forward /PE multiple trend (upper chart) / share price and OP trend (lower chart)



Source: Company data, Nomura estimates

Exhibit 139. Neowiz Games: overseas royalty revenue trend



Source: Company data, Nomura estimates

Exhibit 140. Korea advertising market trend

(Wbn)	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010F	2011F	2012F
TV	2,069	1,954	2,439	2,367	2,235	2,149	2,184	2,108	1,900	1,671			
Radio	250	237	278	275	265	268	280	281	277	223			
Newspaper	2,121	1,750	2,020	1,890	1,744	1,647	1,701	1,780	1,658	1,501			
Magazine	163	156	181	501	426	437	459	484	480	439			
Display Ad (on bldg)	723	776	872	917	703	736	774	679	640	625			
Cable/Satellite TV	174	165	235	298	403	487	672	830	860	779			
Ad production/Others	217	547	595	364	582	736	785	808	766	737			
Online Ad	**136.0**	**128.0**	**224.3**	**355.9**	**483.2**	**662.5**	**890.7**	**1,136.4**	**1,285.9**	**1,297.8**	**1,644.7**	**1,891.4**	**2,080.5**
- display	136	162	174	236	267	322	402	458	479	449	584	671	738
- search	-	-	50	120	216	340	489	678	807	849	1,061	1,220	1,342
Total Ad	**5,853.4**	**5,712.9**	**6,844.2**	**6,967.0**	**6,840.0**	**7,122.5**	**7,745.6**	**8,105.9**	**7,866.8**	**7,272.3**	**8,145.0**	**8,470.8**	**8,809.6**
GDP (mn$)	**578,665**	**622,123**	**684,264**	**724,675**	**779,381**	**810,516**	**848,045**	**901,189**	**928,711**	**872,988**	**916,638**	**955,053**	**993,542**
% of GDP (%)	1.0	0.92	1.00	0.96	0.88	0.88	0.91	0.90	0.85	0.83	0.89	0.89	0.89
Total ad growth (%)	26.7	(2.4)	19.8	1.8	-1.8	4.1	8.7	4.7	(2.9)	(7.6)	12.0	4.0	4.0
Online ad growth (%)	67.5	-5.9	75.2	58.7	35.8	37.1	34.4	27.6	13.2	0.9	26.7	15.0	10.0
- display (%)		19.1	7.6	35.3	13.3	20.6	24.6	14.2	4.4	(6.2)	30.0	15.0	10.0
- search (%)				140.0	80.0	57.5	43.8	38.6	19.1	5.2	25.0	15.0	10.0
% of online ad / total ad (%)	**2.3**	**2.2**	**3.3**	**5.1**	**7.1**	**9.3**	**11.5**	**14.0**	**16.3**	**17.8**	**20.2**	**22.3**	**23.6**

Source: Cheil Communications. online ad forecast from Internet Marketing Council of Korea, otherwise Nomura estimates

IT Hardware

NEUTRAL

Action

We maintain our negative view on the LCD industry. According to our channel checks, demand for LCD TV is still weak and inventory issue persists in the US market. As such, we think a further TV panel price fall is foreseeable, leading to negative operating profit for panel makers in 4Q10F and 1Q11F. Meanwhile, we recommend investors to look closely at smartphone beneficiaries.

Catalysts

We consider early 2011 the right time for investors to revisit the LCD industry, as we believe inventory issues, stemming from lower utilisation at panel makers, will likely be resolved in 1Q11F.

Anchor themes

We believe the slowdown in the LCD industry should impact component prices from 4Q10 on pricing pressure from panel makers and easing component shortage. We remain cautious on LCD-related components.

Stocks for action

We maintain our NEUTRAL view on the LCD industry. We believe the industry needs more time to resolve inventory issues, while panel makers will likely post losses in 4Q10F and 1Q11F. We maintain our NEUTRAL rating on LGD. We have BUY on SEMCO as it is a potential beneficiary of the smartphone boom.

Stock	Rating	Price	Price target
SEMCO (009150 KS)	BUY	W126,000	W144,000
LG Display (034220 KS)	NEUTRAL	W40,000	W36,000

Prices as of 1 Dec 2010

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Bottom in 1Q11F

① Consumers buying smartphones and tablet PCs, but not LCD TVs

While the LCD industry is still suffering from sluggish demand and inventory issue, demand growth in smartphones and tablet PCs is strong. According to our analysis, consumers' interest in IT products has moved toward smartphones and tablet PCs (see following exhibits). Our concern is that this trend could linger at least until 1H11. From LCD panel makers' point of view, this trend could result in serious changes for their business in the short and medium term.

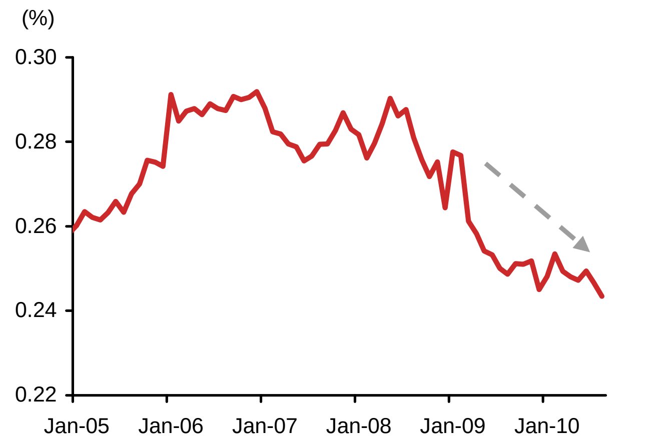
② BUY smartphone beneficiaries

Due to slowdown in LCD TV demand, Korean IT stocks underperformed for the last three months. However, we recommend investors to look closely at smartphone beneficiaries. We believe SEMCO is one of the beneficiaries of increased demand for smartphones and tablet PCs, as it is the most competitive manufacturers in ultra-small with high capacitance MLCCs, which is the key component for smartphones and table PCs. We believe growth momentum at the MLCC business, aided by the smartphone boom, has not yet been priced in.

③ LCD & TV – Tight supply to come in the second half

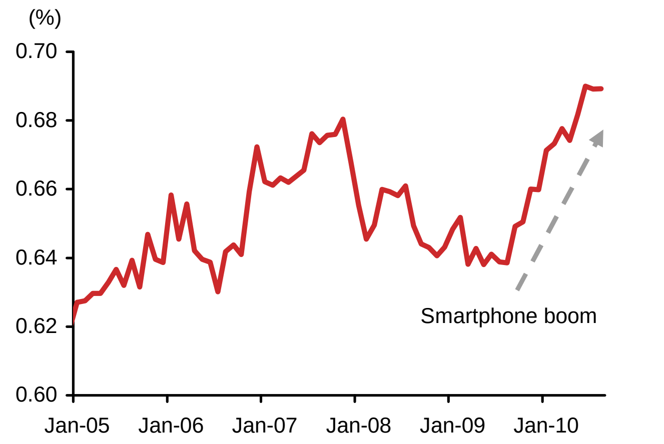
We believe the LCD sector will bottom in 1Q11F and supply will tighten through 2H11F. TV, as well, is likely to bottom in 1Q11F, yet shipment growth will be moderate compared to 2010F (17% y-y in 2011F, vs 28% y-y in 2010F), in our view. We expect penetration of LED into LCD to grow to 55% by 2011F-end, from 23% at end-2010F. However, we are cautious on LED component names as LED chips should be in severe oversupply throughout the year. We maintain our NEUTRAL view on LGD. We think investors should revisit the LCD industry and LGD when the industry finds the bottom in 1Q11F. We have a REDUCE rating on Seoul Semi. As a standalone LED company, we believe Seoul Semi's earnings growth will be impacted significantly by the massive LED price cut and intensified competition due to oversupply.

Exhibit 141. US TV spending as percentage of total consumer spending



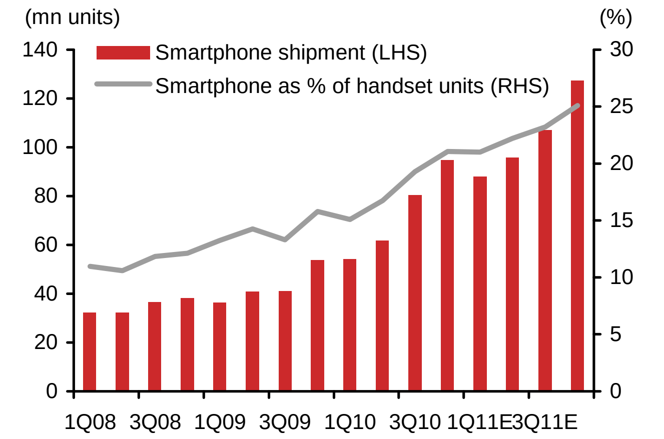
Source: CEIC

Exhibit 142. US mobile device spending as percentage of total consumer spending



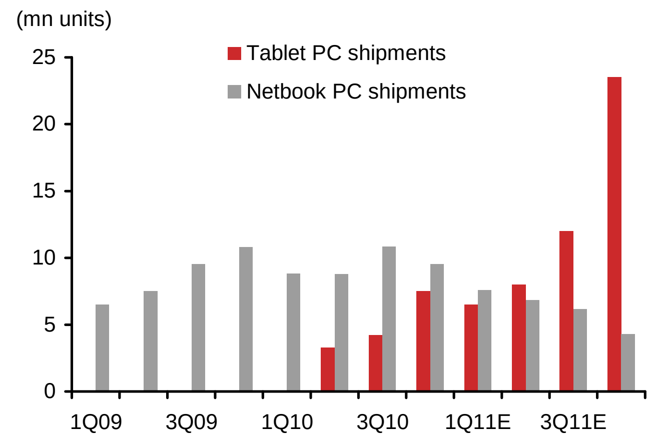
Source: CEIC

Exhibit 143. Smartphone shipment forecast



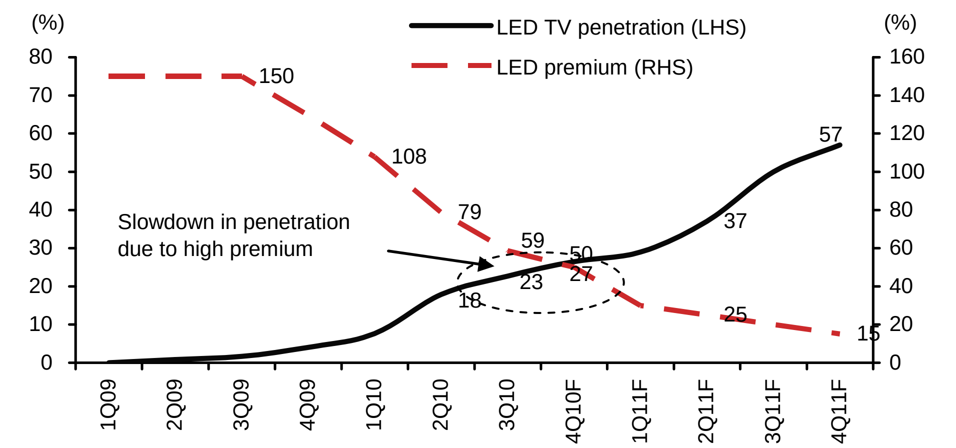
Source: Nomura estimates

Exhibit 144. Tablet PC shipment forecast



Source: Nomura estimates

Exhibit 145. LED penetration forecast



Source: Display Search, Nomura estimates

Memory

BULLISH

Action

We advise investors to be mindful that the bottom is not far away, rather than still focusing on margin deterioration. Given that the price recovery is likely to come at the cost of the 2nd-tiers, we are Buy on only 1st-tier names — Samsung and Hynix.

Catalysts

Faster-than-expected DRAM price drop should lead to both demand recovery and supply slow down. This should result in earlier DRAM price recovery.

Anchor themes

A stark differentiation between those with sheer exposure to specialty DRAM and NAND vs those without, is highly likely. The former are likely to make a soft-landing during the correction, while the latter will make a hard-landing, we believe.

Stocks for action

Owing to the exposure to specialty DRAM and technology leadership, the gap between the top and second-tier names should continue to widen. We favor SEC and like Hynix and advise to take any weaknesses as an opportunity to accumulate.

Stock	Rating	Price	Price target
SEC (005930 KS)	BUY	820,000	1,050,000
Hynix (000660 KS)	BUY	23,400	33,000

Prices as of 1 Dec 2010
Source: Bloomberg; Nomura

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Only 1st-tiers can stand against the headwind

① DRAM – A soft landing likely only for 1st-tier players

Due to lower PC demand, faster-than-expected cannibalisation of tablet & smartphones into traditional PCs, and acceleration of supply growth, PC DRAM prices have rapidly fallen to US$1.4/Gb and are forecast to fall further to around US$1.0/Gb in early 1Q11, below 2nd-tiers' cash costs on 5xnm or 6xnm technology.

Post 1Q11, we expect PC DRAM prices should bottom as (a) memory content per box is likely to recover on low PC DRAM prices and (b) memory players are rapidly shifting their production from PC DRAMs to specialty DRAMs. We forecast only 1st-tier DRAM players, with exposure to both NAND and specialty DRAMs, will see a soft-landing in earnings.

② NAND – A much better outlook than DRAM

Smartphones and tablet PCs should drive strong demand growth for embedded flash. Plus, the demand for solid state drive (SSD) is likely to pick up in earnest from 2011F, as we expect per-Gb costs to come below US$1.0 by 2H11F. In spite of y-y NAND capex increase and likely seasonal weakness during 1Q11, we forecast 2011F NAND demand will outgrow the supply, presenting a stable top line growth to all NAND players.

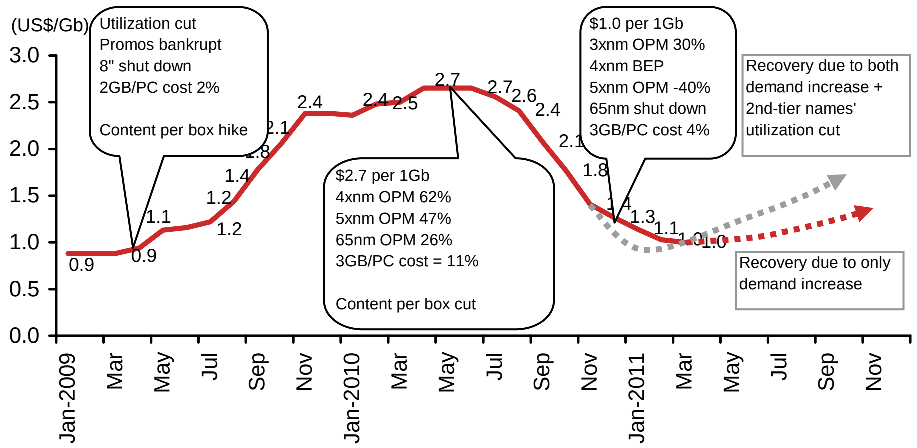
③ Nomura call — by 1Q11F, bottom fish only first-tier players

While current share prices of 1st-tier memory names reflect a hard-landing case, we anticipate a soft-landing scenario. We advise to accumulate only 1st-tier names — Samsung and Hynix — on any weaknesses ahead.

For Samsung, we see a widening gap vs 2nd-tiers, in terms of both production costs and market share. Also, the improvement of set businesses should help defend its overall profitability.

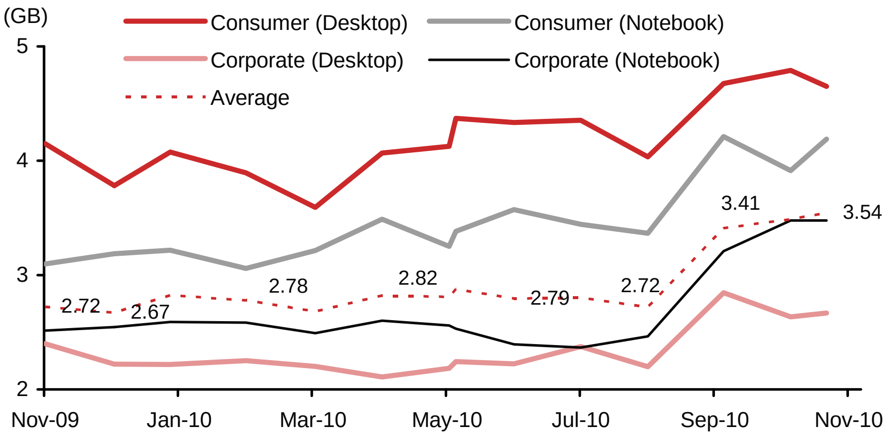
For Hynix, the share price already reflects a hard-landing story. We advise to bottom fish, while the share is trading at the lower end of the box range.

Exhibit 146. DRAM price trend and our forecast



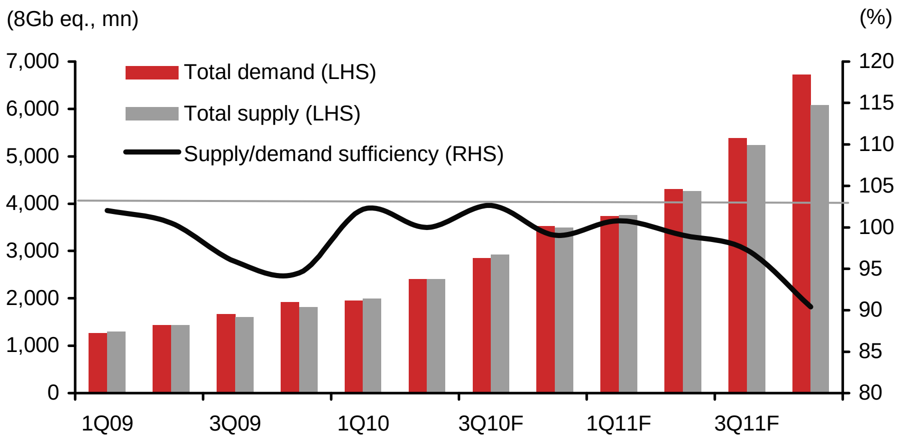
Source: DRAMeXchange, Nomura estimates

Exhibit 147. Recent memory content per box trend



Source: Dell

Exhibit 148. NAND supply-demand outlook



Source: Nomura estimates

Power

BULLISH

Action

Albeit long in the making, the government is proposing a fuel cost escalation scheme for tariffs to be implemented in July 2011, which would link electricity rates to fuel input prices on a regular basis. A tighter tariff scheme should move valuation up from the current low ranges of 0.4-0.5x P/BV.

Catalysts

Catalysts that would move KEPCO stock towards PT: 1) a tighter tariff scheme linked to fuel prices and currency and 2) in longer term, won currency strength.

Anchor themes

Earnings are affected by movements in the won:US$ rates, international fuel commodity prices, CPI, and interest rates. As well, KEPCO leads Korea's consortia that bid for various nuclear power projects overseas. Also see Anchor Report: Asia Pacific Nuclear Power - Asia starts global nuclear chain reaction, 25 January, 2010.

Stocks for action

We cover Kepco in the power sector with a BUY rating on the anticipation of fuel cost escalation tariff scheme in FY11.

Stock	Rating	Price	Price target
Kepco	BUY	28,350	43,000

Prices as of 1 Dec 2010

20-year wait nearing an end?

① 20-year wait for a more guaranteed tariff scheme

Politics have had some major negative ramifications for KEPCO's tariff adjustments throughout its history. As a result, CPI inflation since 1990 has totalled 120%, compared to a 60% gain in KEPCO's tariffs since 1990. Regaining full government control of KEPCO's electricity tariffs is a key reason behind re-merging of the gencos and KEPCO. Albeit long in the making, the government is proposing a fuel cost escalation scheme for tariffs, to be implemented in July 2011, which would link electricity rates to fuel input prices on a regular basis. According to the government, a partial revamping of KEPCO's irregular tariff scheme will enable KEPCO to meet a 6% rate of return target (on electric utility assets) in two-three years. KEPCO's rate-of-return formula, heretofore a loose guideline for determining tariffs, has seen only a 4% average rate-of-return on net power plant in service since the Asian crisis years (1997-98), with RORs meeting the minimum 6% target only in two of the 12 years since the Asian crisis.

② Impact of currency, interest rates, fuel prices and inflation

We estimate that every 1% won depreciation versus the US dollar would pare KEPCO's earnings by 3%, as won-translated fuel costs rise. Essentially all of KEPCO's earnings are denominated in won, while almost all of its fuel costs are in US dollars, exposing earnings to the volatility of the forex markets. Implementation of a fuel cost escalation scheme could smooth out such forex-linked earnings volatility.

③ Positive view on KEPCO

A tighter tariff scheme should move KEPCO's valuation up from the current low ranges of 0.4-0.5x P/BV. KEPCO is by far the cheapest valued major Asian power utility on this basis (see Nomura's daily *Asia Power Lunch* for comparative valuation). We think the low valuation stems from: 1) a loose tariff scheme influenced by the government's political and economic agenda, and 2) KEPCO's defencelessness against volatile won:US$ currency movements. A tighter tariff scheme would re-rate KEPCO's valuations, in our view.

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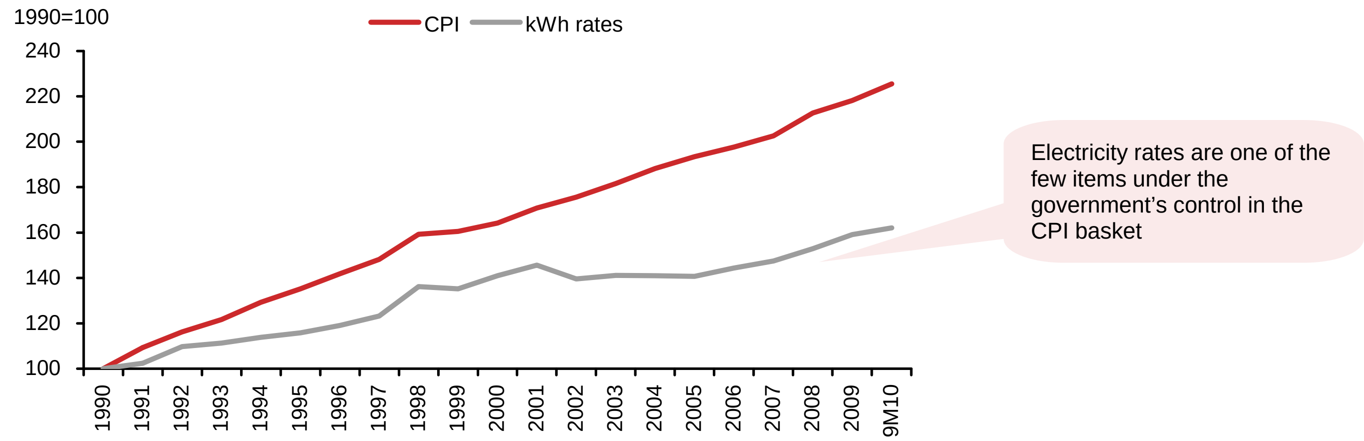
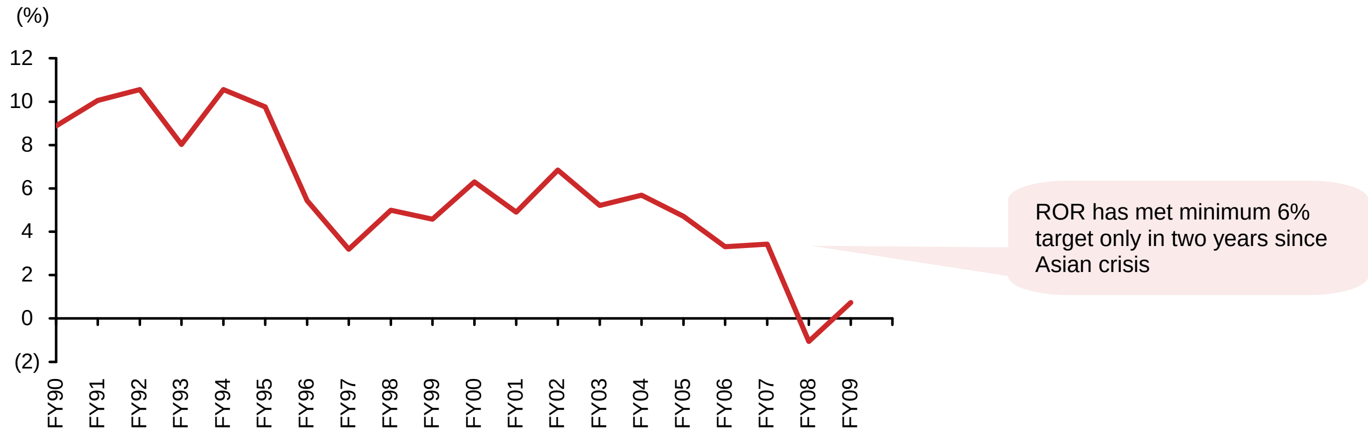
Exhibit 149. KEPCO: CPI versus average power tariff adjustments



Source: Company data, Nomura research.

Exhibit 150. KEPCO: rate of return (on net generating assets)



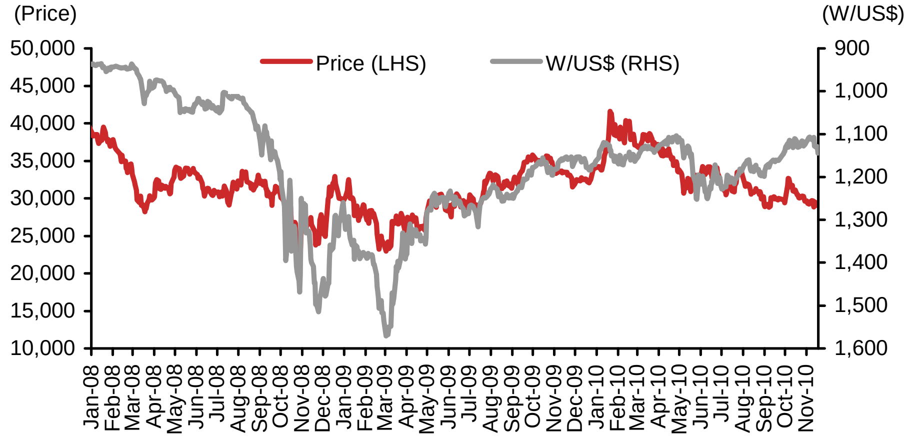
Source: Company data, Nomura research.

Exhibit 151. KEPCO: power tariff hikes vs share price performance

			Share price									W:US$							
			% chg pre tariff				%chg post tariff adjustment					% chg pre-tariff adjustment				% chg post tariff			
Date of tariff chg	Tariff % chg	Price (W)	Vs 1m	3m	6m	12m	vs1m	3m	6m	12m	W:US$ rate	Vs 1m	3m	6m	12m	vs1m	3m	6m	12m
01/Jul/97	5.9	26,400	(4)	2	2	(6)	(2)	(23)	(41)	(41)	888	0	1	(5)	(9)	(0)	(3)	(45)	(35)
01/Jan/98	6.5	16,300	21	(16)	(40)	(34)	41	17	(5)	83	1,600	(28)	(43)	(45)	(47)	5	13	18	33
05/Nov/99	5.3	40,900	4	(0)	6	64	11	(12)	(25)	(36)	1,187	2	1	0	11	3	5	7	5
15/Nov/00	4.0	27,600	5	(18)	(13)	(34)	(17)	(3)	(17)	(15)	1,137	(1)	(2)	(2)	4	(6)	(9)	(13)	(12)
01/Jun/02	(0.1)	24,800	1	13	8	2	(13)	(15)	(21)	(20)	1,222	6	8	4	5	1	2	1	1
01/Mar/04	(1.5)	21,150	5	(17)	10	18	(4)	(12)	(4)	30	1,177	(0)	2	0	1	3	1	2	17
28/Dec/05	2.8	37,600	8	9	19	36	10	7	(6)	13	1,013	3	2	1	3	4	4	5	9
15/Jan/07	2.1	42,100	3	14	22	4	(3)	(7)	10	(10)	939	(2)	2	2	5	0	1	2	0
13/Nov/08	4.5	27,450	3	(15)	(18)	(29)	10	2	8	22	1,391	(11)	(25)	(25)	(34)	1	(1)	11	20
27/Jun/09	3.9	29,500	4	11	(2)	(5)	12	20	11	13	1,284	(1)	5	1	(19)	4	8	9	6
1/Aug/10	3.5	33,200	6	(2)	(13)	(0)	(13)	(11)	(13)	(13)	1,183	4	(6)	(2)	4	(0)	5	4	4
Average	4.3	29,727	5	(2)	(4)	(0)	5	(1)	(8)	2	1,184	(4)	(7)	(8)	(9)	1	3	(0)	3

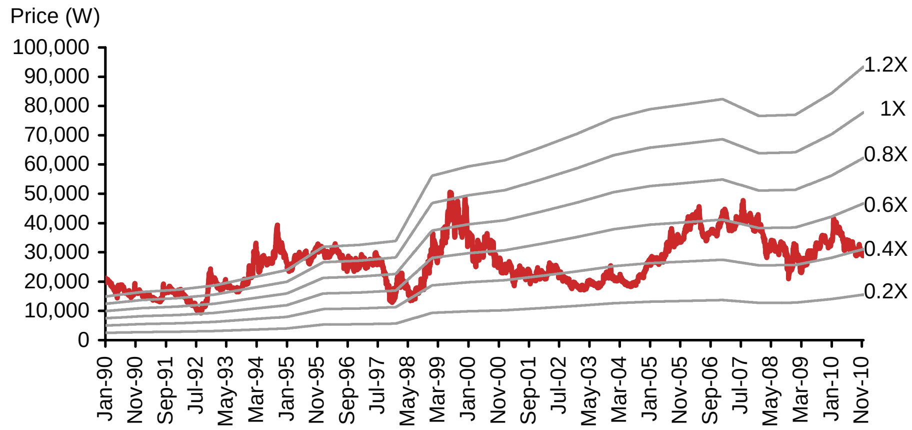
Source: Company data, Nomura research

Exhibit 152. KEPCO: share price performance vs W:US$



Source: Bloomberg, Nomura research

Exhibit 153. KEPCO: Price-to-book ratio



Source: Bloomberg, Company data, Nomura research

Refining

BULLISH

Action

Asian and Korean refining margins are poised for another year of modest gains in 2011F, on slowing capacity additions and a tightening diesel balance. Diesel shortage in China and tight paraxylene supply should underpin refining margin and boost 4Q10 earnings for Korean refiners.

Catalysts

Positive catalysts could emerge from: 1) sustainable margin improvement; 2) delays to new plant start-ups and 3) strengthening oil demand.

Anchor themes

With sector valuations at mid-cycle levels, we are selectively Bullish on Asian refiners with stock-specific catalysts or high gearing towards aromatics, which should enjoy improving margins.

Stocks for action

Our top BUY is SK Energy. Our price target is higher than the Street possibly because we ascribe higher multiples reflecting potential value creation from spin-off and new businesses.

Stock	Rating	Price	Price target
SK Energy (096770 KS)	BUY	W172,500	W190,000
GS Holdings (078930 KS)	BUY	W67,500	W68,000
S-Oil (010950 KS)	BUY	W86,600	W85,000

Prices as of 1 Dec 2010

The bumpy ascent

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① Sustainably stronger 2011F refining margins

We believe Asian refining margins are poised for another year of modest gains in 2011F, on slowing capacity additions and a tightening diesel balance. We forecast Singapore complex margins of US$4.20/bbl and US$5.00/bbl for 2010F and 2011F, respectively (from US$4.00/bbl and US$4.70/bbl previously). Margins in 2011F are likely to peak in the 2009-14F period, unless demand growth surpasses our expectations or new projects see significant delays.

② Aromatics margins on the mend

Paraxylene (PX) margins have disappointed this year, owing to large new capacity additions and higher refinery run rates. We believe PX margins bottomed in 3Q10 and are likely to gain considerable strength from 2H11F as large new PTA expansions boost demand. We also forecast more stable benzene margins over the next few years as the peak expansion period appears to be over.

③ Diesel shortage may persist

Shortage of diesel in China has become more widespread, caused by hoarding in anticipation of future price increases, and to a lesser extent, increasing usage of diesel generators. Although we believe that both the shortage of diesel in China and PX tightness could ease by end-2010, this introduces upside risks to our earnings forecasts for sector stocks in 4Q10.

④ Stock picks – SK Energy is our top BUY

We see further potential upside to SKE's share price despite recent outperformance. The business spin-off, approved at the 26 October EGM, could accelerate positive strategic moves for refining and petrochemical units. E&P production may reach 75,000 bpd in early 2011F (3Q10: 66.8 k bpd). Brazil's Wahoo field and other potential M&As may bring an additional 3,000-5,000bpd by 2013F. Potential deals related to the Incheon refining plant may boost the share price.

Exhibit 154. Global CDU addition and deletion

(kb/d)	2009	2010F	2011F	2012F	2013F	2014F
Gross additions						
North America	21	180	94	415	54	0
Europe	20	130	124	150	0	0
Asia	1,403	914	450	625	1,180	1,000
Middle East	236	20	0	90	32	474
FSU	80	130	140	60	0	0
South America	0	0	115	0	280	150
Africa	100	0	97	100	33	0
Total	**1,860**	**1,374**	**1,020**	**1,440**	**1,579**	**1,624**
Total idled/closed	**946**	**925**	**(60)**	**0**	**0**	**0**
Net additions	**914**	**449**	**1,080**	**1,440**	**1,579**	**1,624**
Demand	(1,300)	1,900	1,300	1,200	1,100	1,000
Supply less demand	**2,214**	**(1,451)**	**(220)**	**240**	**479**	**624**

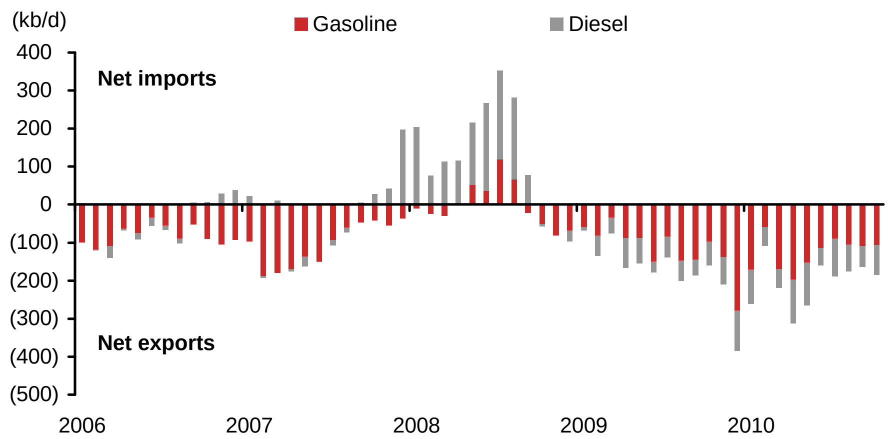
Source: Nomura estimates

Exhibit 155. Singapore refining margin

US$/bbl	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010F	2011F	2012F
Gasoline	7.6	6.1	4.5	7.7	15.7	15.2	13.5	17.0	13.7	12.5	10.8	10.2	9.5
Jet	8.3	5.6	4.3	6.0	13.5	17.4	18.4	18.5	27.7	8.2	11.0	13.0	12.0
Diesel	6.4	4.7	3.7	5.4	11.6	14.2	15.3	16.7	25.9	7.3	11.5	13.5	12.5
Fuel oil	(1.2)	(1.8)	(1.8)	(1.0)	(3.8)	(6.2)	(11.2)	(8.3)	(14.7)	(7.5)	(7.0)	(5.0)	(6.0)
Naphtha	2.2	1.3	1.1	2.5	7.0	2.2	0.8	6.2	(4.2)	(1.6)	0.5	0.5	1.0
LPG	1.4	(0.2)	(1.8)	0.2	0.0	(7.6)	(14.6)	(14.0)	(27.2)	(15.3)	(14.0)	(14.0)	(14.0)
Singapore complex	**3.2**	**2.1**	**1.6**	**3.4**	**6.7**	**6.9**	**5.5**	**7.6**	**6.2**	**3.7**	**4.2**	**5.0**	**4.4**
Singapore simple	**1.2**	**0.2**	**0.2**	**1.4**	**2.1**	**1.8**	**(0.3)**	**1.7**	**0.4**	**0.7**	**0.8**	**1.0**	**0.7**

Source: Bloomberg, Thomson Reuters, Nomura research

Exhibit 156. China gasoline and diesel trade



Source: China Customs Statistics

Shipping

NEUTRAL

Action

We have NEUTRAL ratings on Hanjin and Korea Line, but REDUCE on Hyundai Merchant Marine due to expensive valuation (trading at premium to sector). We are Bullish on drybulk shipping as demand remains robust, however signs are emerging of supply concerns. For container shipping, we are BEARISH as we estimate earnings peaked from lower rates and higher oil prices.

Catalysts

Upcoming catalysts include a higher and stronger rebound in dry bulk freight rates and a continued decline in container freight rates.

Anchor themes

We are Bearish on container shipping as we believe container freight rates have peaked and will decline in 2011F, leading to weaker earnings. We are Bullish on drybulk shipping (for now) given seasonally stronger 4Q and forecast for earnings improvement in 2011F. However, drybulk supply becoming an increasing concern.

Stocks for action

Amongst the Korean shipping companies under our coverage, we have NEUTRAL ratings for Hanjin Shipping and Korea Line. We have REDUCE rating on Hyundai Merchant Marine due to expensive valuation.

Stock	Rating	Price	Price target
Korea Line (005880 KS)	NEUTRAL	38,550	63,000
Hanjin Shipping (117930 KS)	NEUTRAL	35,000	30,000
Hyundai Merchant Marine (011200 KS)	REDUCE	43,400	26,000

Prices as of 1 Dec 2010

Supply concerns increasing

① Container shipping outlook - BEARISH

With quarterly container earnings peaking in 3Q10, we have a Bearish view on the Asian container shipping sector as we estimate sector ROE to decline to 6% in 2011 from 14% in 2010 with supply outpacing demand growth. Container freight rates have begun to decline and we expect this trend to continue into1H11. Also, margins are likely to erode further owing to high oil prices given we expect average Brent oil price to increase 14% to US$95/bbl in 2011. The pace of global economic growth is the key driver as Asia Europe and Asia US routes account for 21% and 41% of sector revenues. Further, carrier's capacity and pricing discipline is also important but we believe idle capacity is likely to be lower than early 2010 levels given the sector remains profitable in 2011.

② Drybulk shipping outlook – BULLISH for now

We are currently Bullish on the drybulk shipping sector as we estimate drybulk demand remains strong primarily driven by global steel demand, especially from China. For example, China accounts for 45% of global steel production during 9M10 and Nomura have a Bullish view on the China steel sector. However, the drybulk newbuilding orderbook is becoming an increasing concern, in our view, as greenfield shipyards begin to deliver newbuildings (we had previously assumed delivery execution problems at greenfield shipyards). With this trend continuing, it may lead to supply becoming a problem in 2011 and 2012. However, we believe port congestion could become an issue in 2011, which would cap the effective capacity. For 2011, we expect drybulk freight rates to be volatile due to port congestion problems during peak demand periods.

③ Korean shipping - stock picks

Amongst the Korean Shipping companies under coverage, we have NEUTRAL ratings on Hanjin and Korea Line. We have REDUCE rating on Hyundai Merchant Marine (HMM) due to expensive valuation as the stock is trading at 2.3x 2011 P/B, and is at a premium to sector average of 1.4x. This is unjustified given we estimate HMM's ROE to decline to 2% in 2011 from 14% in 2010. We have a BUY rating on STX Pan Ocean, a Singapore-listed entity, with a S$18.5 target price, which is equivalent to W15,281/share.

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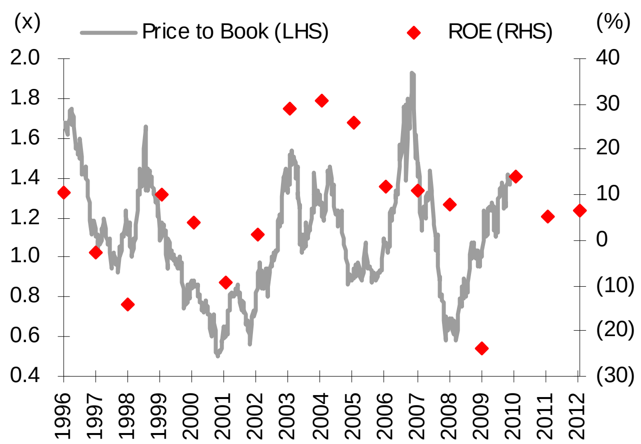
Exhibit 157. Korean shipping – valuation comparison table

Stock	Listing currency	Ticker	Rating	Current price	Price target	Potential upside/ (downside) (%)	Market cap (US$mn)	Avg daily t/o (US$mn)
Korea Line	W	005880 KS	NEUTRAL	38,550	63,000	63.4	402	6.8
Hanjin Shipping	W	117930 KS	NEUTRAL	35,000	30,000	(14.3)	2,344	39.5
Hyundai Merchant Marine	W	011200 KS	REDUCE	43,400	26,000	(40.1)	4,550	19.5
					EV/EBITDA (x)			
Stock	Target EV/Fleet (x)	Current EV/Fleet (x)	Net debt/ equity (%)	Current ratio (x)	2009	2010F	2011F	2012F
Korea Line	0.7	0.6	192.5	1.3	n.m.	9.4	9.3	8.4
Hanjin Shipping	1.5	1.6	225.5	1.0	n.m.	8.7	10.8	8.9
HMM	1.6	2.0	211.4	1.5	n.m.	12.0	19.3	17.5
	Pre-exceptional P/E (x)				Dividend yield (%)			
Stock	2009	2010F	2011F	2012F	2009	2010F	2011F	2012F
Korea Line	n.m.	97.5	152.2	15.5	0.0	0.0	0.0	0.0
Hanjin Shipping	n.m.	17.4	51.8	20.3	0.0	0.0	0.0	0.0
HMM	n.m.	17.0	101.5	55.4	0.0	1.5	0.2	0.5
	P/BV (x)				Pre-exceptional ROE (%)			
Stock	2009	2010F	2011F	2012F	2009	2010F	2011F	2012F
Korea Line	0.7	0.7	0.7	0.7	(81.1)	0.7	0.5	4.3
Hanjin Shipping	1.4	1.3	1.2	1.2	(4.9)	7.4	2.4	5.8
HMM	2.2	2.3	2.3	2.3	(35.3)	13.6	2.3	4.1

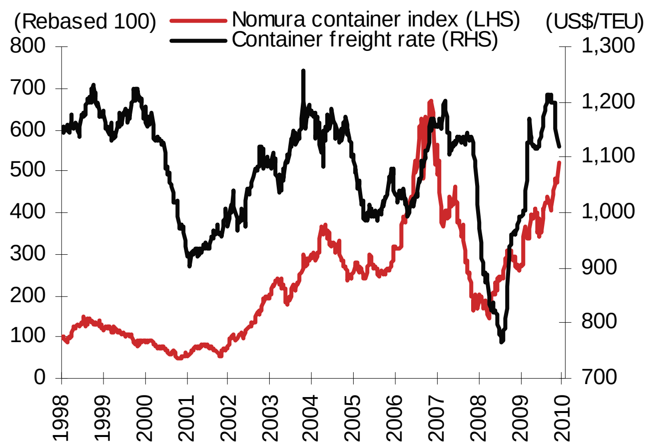
Source: Company data, Nomura estimates

Exhibit 158. Container shipping P/BV and ROE – bearish sector view as ROE declining in 2011



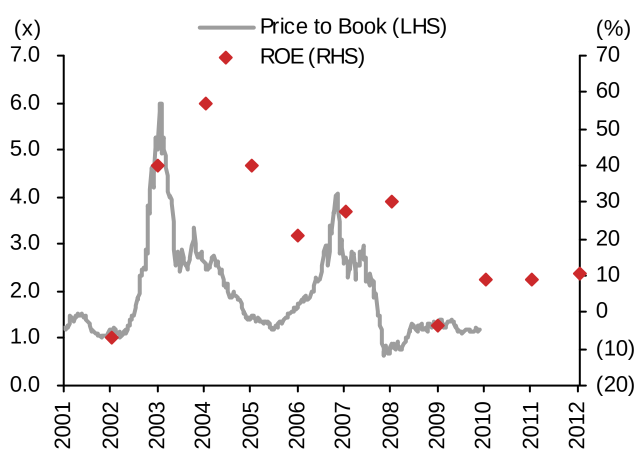
Source: Datastream, Nomura estimates

Exhibit 159. Container shipping index and overall container freight rates



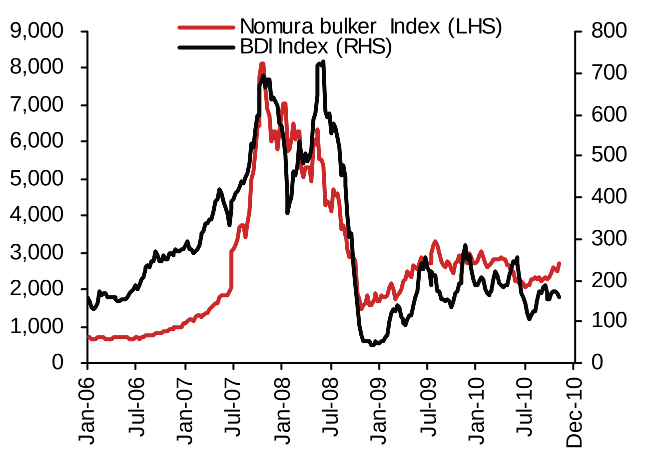
Source: Datastream, Nomura estimates

Exhibit 160. Drybulk shipping P/BV and ROE



Source: Datastream, Nomura estimates

Exhibit 161. Drybulk shipping index and BDI



Source: Datastream, Nomura estimates

Steel

BULLISH

Action

We sense that competition may intensify in Korea when Hyundai Steel's No.3 blast furnace becomes a reality and POSCO announces further expansion plans. Industry signs are mixed at this point, with crude steel production headed down in October, steel prices showing marginal increase and end-demand industries without robust catalysts. However, downside risks for steel look limited, in our view.

Catalysts

Steel price hike, lower raw material costs from 1Q11 (leading to likely earnings improvement in 1Q11F) and visibility in auto steel development.

Anchor themes

Rising raw material costs are driving the global theme of vertical integration, which affects margin and share performance. Equally important are industry consolidation, economies of scale, product mix and technology development.

Stocks for action

We flag Hyundai Steel and POSCO as our preferred exposure. Dongkuk Steel is less attractive on the fundamentals, but the stock looks oversold.

Stock	Rating	Price	Price target
Hyundai Steel	BUY	109,000	125,000
POSCO	BUY	457,000	700,000
Dongkuk Steel	BUY	29,050	33,000

Prices as of 1 Dec, 2010

Searching for an inflection point

① Searching for an inflection point

The Korean steel industry is showing mixed signs. Positive signs are that: 1) spot market prices for iron ore, scrap, and steel have been rising; 2) steel export from China is slowing down and 3) China's long steel inventory has been declining. In contrast, global crude steel production growth has slowed significantly up to September, as has China's apparent steel consumption. Korea's end-demand industries are holding up, although the overall growth rate is slowing down. We think the steel industry may bottom in 1H11F before showing a visible recovery in 2H11F.

② Growth and integration

For Korea where real consumption growth will likely be capped owing to mature end-industries, a key differentiating point for steel companies should be either 1) degree of scale expansion or 2) the level of vertical integration. We would rate Hyundai Steel high on the former criteria, while POSCO ranks high on the latter. As part of achieving 40mn tonne crude steel capacity in Korea, POSCO will be completing steel plate expansions (+4mn tonne) by end-2010F and be adding cold-rolled steel lines by end- 2012F. Its overseas strategy has been narrowed to India and Indonesia. In India, POSCO now has three plants in the pipeline.

③ Stock picks – upside in auto steel - Hyundai Steel

HS is in the nascent stage of an automotive steel development with marked upside potential owing to the relationship with Hyundai Motor Group. We rate HS as our sector top pick, based on strong sales volume growth (25% pa in FY09-11F), product mix shifting to flat steel (flat to represent 43% of volume in FY11F; 27% in FY08) and undemanding valuation.

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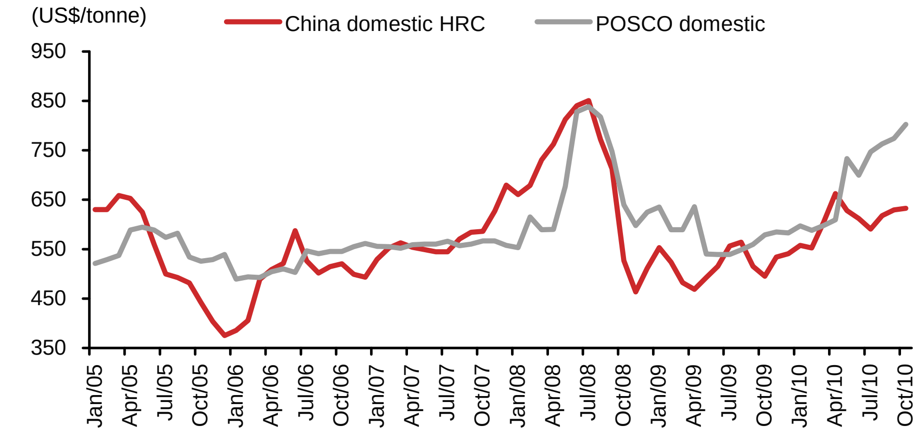
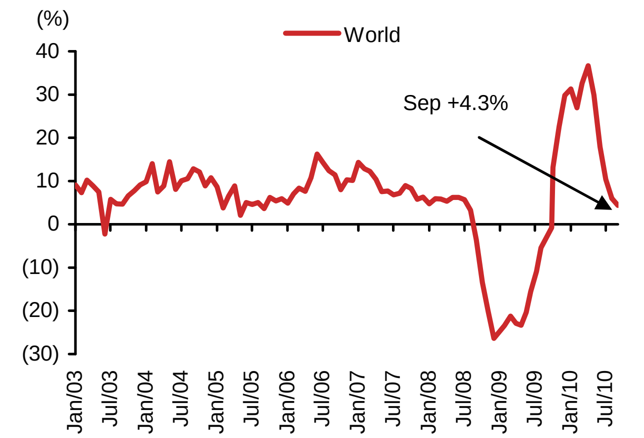
Exhibit 162. Hot-rolled coil price: POSCO versus import



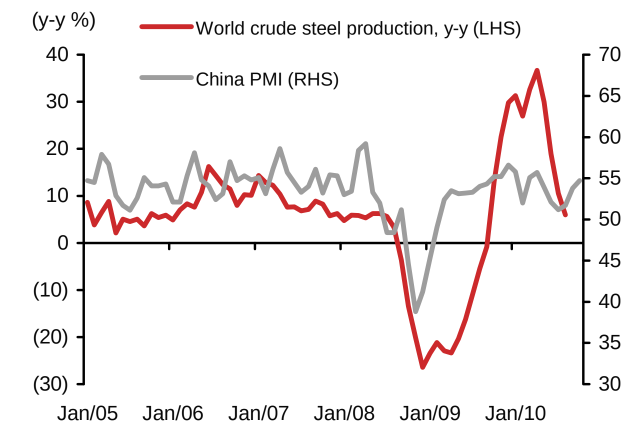
Source: Company data, Metal Bulletin

Exhibit 163. Global crude steel production



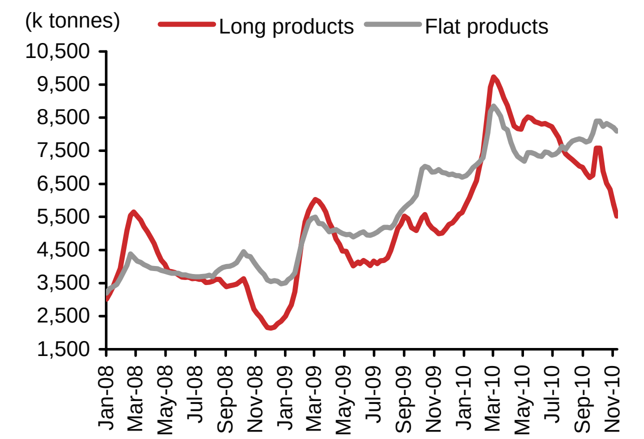
Source: World Steel Association

Exhibit 164. China: PMI



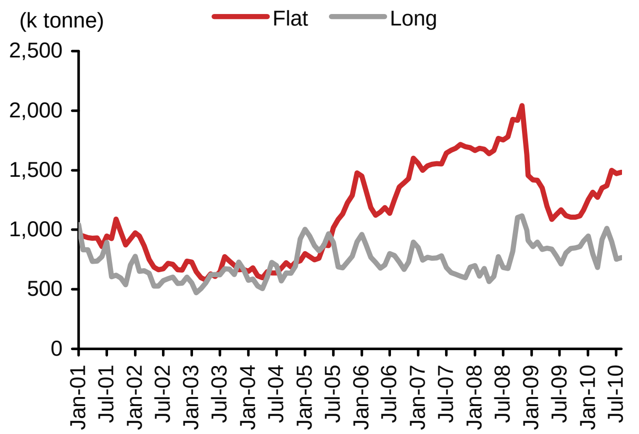
Source: Bloomberg, World Steel Association

Exhibit 165. China: inventory



Source: Mysteel

Exhibit 166. Korea steel inventory



Source: Korea Steel Association

Telecom services

BULLISH

Action

ARPU, marketing costs and capex control remain the key share price drivers for Korea telcos going forward amid the boom of smartphone. We expect SKT and KT to see profitable growth in 2011 on resilient ARPU growth and reasonable marketing/capex costs control going forward.

Catalysts

Moving onto mass-market penetration in 2011F, the longevity of the ARPU uplift, coupled with effective capex control, remain key catalysts in the longer term.

Anchor themes

We are bullish that smartphone-driven data revenue growth will accelerate over the next two years, with a rapid shift into smartphone mass-market penetration. As we see it, Korea's telco sector is well set to be re-rated, riding the smartphone tide.

Stocks for action

SKT and KT remain key beneficiaries of rapid penetration of smartphone in Korea. We are NEUTRAL on LG Uplus. Our key REDUCE is SK Broadband

Stock	Rating	Price	Price target
SK Telecom (017670 KS)	BUY	W171,500	W223,000
KT Corp (030200 KS)	BUY	W46,150	W58,000
LG Uplus (032640 KS)	NEUTRAL	W7,120	W7,400
SK Broadband (033630 KS)	REDUCE	W5,380	W4,600

Prices as of 1 Dec 2010

Profitable growth outlook

① We expect ARPU uplift and well-controlled marketing cost

We are confident that the smartphone impact will accelerate in FY11F with continuing positive trend from smartphone ARPU driving top line and well-controlled marketing costs (as witnessed recently with stabilising MNP numbers amid iPhone 4 launch) resulting in robust earnings.

② Korea smartphone case more bullish than regional peers

For FY11F, we argue that Korea telcos, relative to regional peers, are better positioned to capitalise on increasing smartphone penetration, on: 1) Korean consumers' intense pent-up demand for high-quality wireless data service at a reasonable price; 2) the massive adoption of unlimited data offering (>W55,000 per month) and 3) no smartphone 'subsidy shock', with operators applying higher tariff discounts (special plan), under KCC's marketing costs cap regulation.

③ Positive smartphone economics

Our subsidy payback and cashflow NPV analyses suggest increasing smartphone penetration will ensure profitable growth for Korea telcos owing to its much more favourable return profile (huge incremental ARPU vs limited incremental handset subsidy).

④ SKT/KT the best smartphone plays

Our top BUY is SKT which we believe is better positioned from the perspective of lower subsidies for Android handsets/superior 3G data capacity/pure wireless play, while KT has greater wireless ARPU uplift potential owing to base effect.

Analysts

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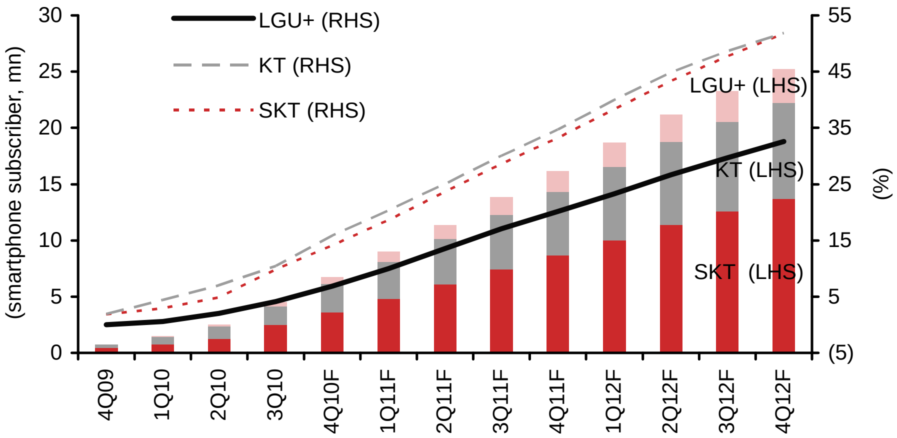
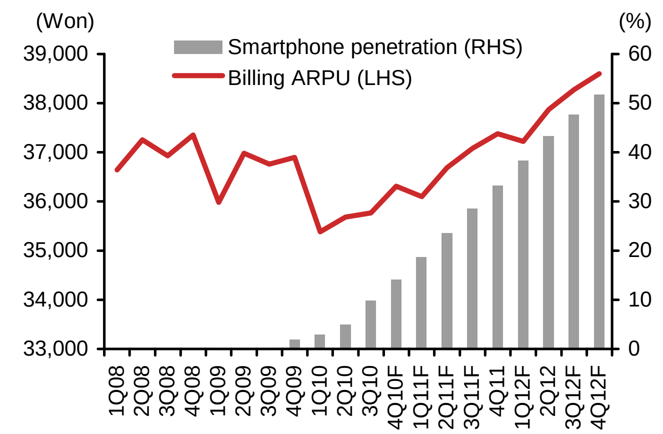
Exhibit 167. Korean smartphone subscriber/penetration trend



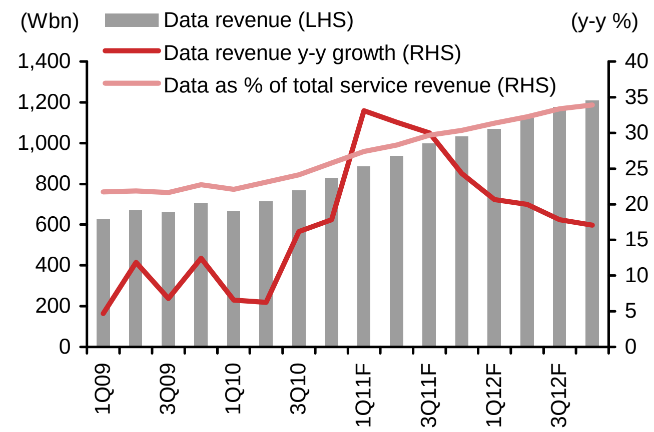
Source: Company data, Nomura estimates

Exhibit 168. SKT billing ARPU/penetration trend



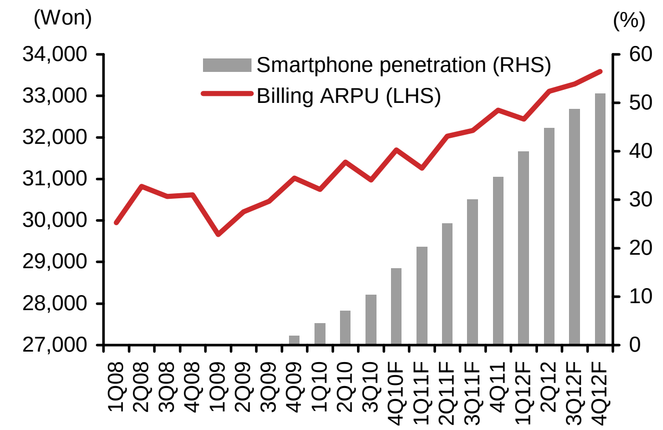
Source: Nomura estimates

Exhibit 169. SKT — Data revenue trend



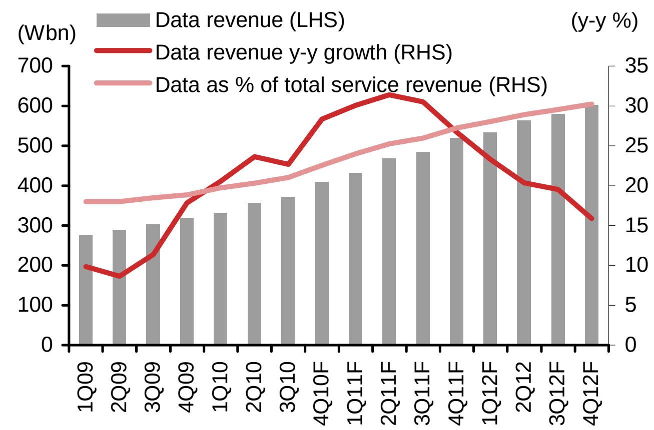
Source: Nomura estimates

Exhibit 170. KT ARPU/penetration trend



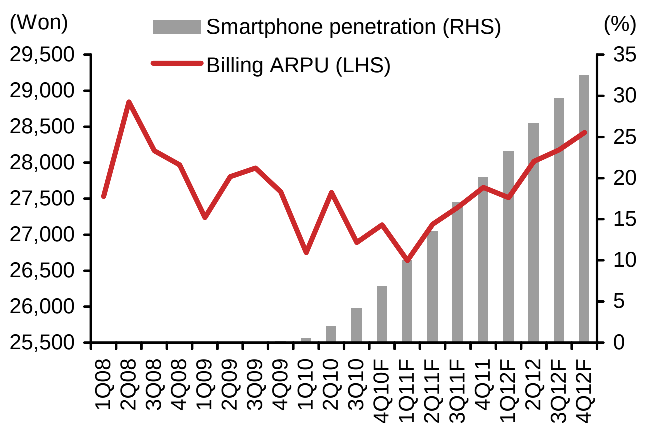
Source: Nomura estimates

Exhibit 171. KT – Data revenue trend



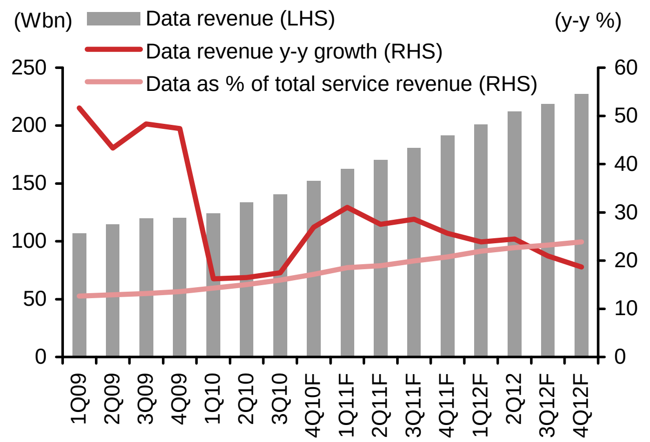
Source: Nomura estimates

Exhibit 172. LGU+ ARPU/penetration trend



Source: Nomura estimates

Exhibit 173. LGU+ - Data revenue trend



Source: Nomura estimates

Exhibit 174. Marketing costs trend

(Wbn)	1Q09	2Q09	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10F	1Q11F	2Q11F	3Q11F	4Q11F
SKT												
Service revenue	2,876	3,068	3,057	3,100	3,018	3,089	3,181	3,222	3,235	3,315	3,360	3,400
Marketing cost	661	950	834	807	846	888	849	801	798	880	826	845
q-q (%)	(4.6)	43.7	(12.2)	(3.2)	4.8	5.0	(4.4)	(5.7)	(0.3)	10.2	(6.1)	2.3
y-y (%)	(13.8)	8.4	14.6	16.5	28.0	(6.5)	1.8	(0.8)	(5.6)	(0.9)	(2.7)	5.6
% of service revenue	23.0	31.0	27.3	26.0	28.0	28.8	26.7	24.8	24.7	26.6	24.6	24.9
KT												
Service revenue	3,788	3,888	3,865	3,893	3,836	3,992	3,999	4,021	3,963	4,017	4,025	4,076
Marketing cost	565	706	810	669	714	687	740	678	676	719	688	692
q-q (%)	(6.4)	24.8	14.8	(17.4)	6.7	(3.8)	7.7	(8.5)	(0.3)	6.4	(4.3)	0.5
y-y (%)	(22.5)	(19.5)	33.8	10.8	26.3	(2.6)	(8.6)	1.3	(5.4)	4.6	(7.1)	2.0
% of service revenue	14.9	18.1	21.0	17.2	18.6	17.2	18.5	16.9	17.1	17.9	17.1	17.0

Source: Company data, Nomura estimates

Exhibit 175. Subsidy payback comparison

	SKT			KT	
(W)	Non-smartphone average	Smartphone (Standard)	Smartphone (Special)	Non-smartphone average	iPhone
Billing ARPU	36,000	57,500	50,000	30,500	54,000
24-month accumulated ARPU	864,000	1,380,000	1,200,000	732,000	1,296,000
Subsidy	180,000	220,000	160,000	160,000	338,000
Payback multiple	4.8	6.3	7.5	4.6	3.8
Payback period (months)	5.0	3.8	3.2	5.2	6.3

Note: payback multiple = 24month accumulated ARPU/ subsidy / payback period = subsidy/Billing ARPU

Source: Company data

Stock picks

GS E & C 006360 KS

INDUSTRIALS/ENGINEERING & CONSTRUCTION | SOUTH KOREA

Maintained

BUY

NOMURA

NOMURA FINANCIAL INVESTMENT (KOREA) CO LTD

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Action

GSEC's position as a top Gulf EPC firm and domestic builder has been overshadowed recently by concern over its unsold housing inventory and PF liabilities. In the event, these worries should subside, thanks to GSEC's own successful restructuring efforts. We also note GSEC's Vietnam business, a catalyst that once drove the share price to all-time highs but has been neglected recently.

Catalysts

Long-term catalysts are overseas construction and a recovery in its domestic housing business.

Anchor themes

We see long-term growth for GSEC, driven by global oil, gas and petrochemical plant build-outs centred in the Middle East, where it has become a major EPC force. GSEC has also established first-mover status in Vietnam's construction market.

Closing price on 1 Dec	W105,000
Price target	**W120,000**
	(set on 4 Feb 10)
Upside/downside	14.3%
Difference from consensus	**5.7%**
FY11F net profit (Wbn)	502
Difference from consensus	**4.7%**

Source: Nomura

Nomura vs consensus

Our price target is slightly above consensus, due to our EV/backlog-based valuation methodology. Our earnings forecast is broadly in line with consensus.

GSEC: underappreciated no more

① Domestic businesses looking better

GS Engineering & Construction (GSEC) has reduced its unsold apartment inventory by 70% from the peak of early 2009. Accordingly, PF liabilities have also declined by over a third. GS and LG group orders are looking up on increasing plant capex from affiliates. GSEC has invested in profitable domestic PFI projects (privately funded infrastructure) and stands to gain from building contracts and capital gains on these investments.

② Gulf EPC business still underestimated

GSEC's overseas plant engineering backlog has multiplied by five times since 2005. GSEC ranked number one in a recent MEED (Middle East Economic Digest) survey of EPC contractors in the Gulf. US$10bn worth of bids are in for a multi-billion dollar refinery project in Saudi Arabia and petrochemicals plant projects in the UAE.

③ Vietnam a potential catalyst, again

GSEC's status as a major developer and builder in Vietnam could be a new catalyst, once the economy there and currency recover. Land has been secured for a major satellite city development in Ho Chi Minh City. Vietnam as a theme has arguably been forgotten for a few years, but GSEC's prospects there drove the stock price up to all-time highs (2007).

④ PT maintained at W120,000/share

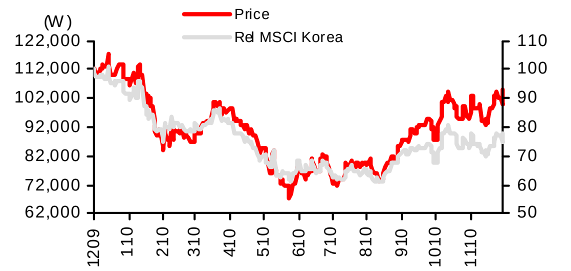
Our price target of W120,000 is derived from the second quintile (0.185x) of GSEC's five-year EV/backlog range (valuation methodology unchanged). At the price target, the stock would trade at well below the 2007 peak P/E and P/BV valuations.

Key financials & valuations

31 Dec (Wbn)	FY09	FY10F	FY11F	FY12F
Revenue	7,377	7,460	7,578	8,572
Reported net profit	383	445	502	573
Normalised net profit	383	445	502	573
Normalised EPS (W)	7,506	8,731	9,838	11,232
Norm. EPS growth (%)	0.3	16.3	12.7	14.2
Norm. P/E (x)	14.0	12.0	10.7	9.3
EV/EBITDA (x)	8.2	7.8	6.0	4.6
Price/book (x)	1.6	1.5	1.3	1.3
Dividend yield (%)	0.9	1.2	1.4	1.6
ROE (%)	12.1	12.8	13.1	14.3
Net debt/equity (%)	net cash	net cash	net cash	net cash
Earnings revisions				
Previous norm. net profit		445	502	573
Change from previous (%)		-	-	-
Previous norm. EPS (W)		8,731	9,838	11,232

Source: Company, Nomura estimates

Share price relative to MSCI Korea

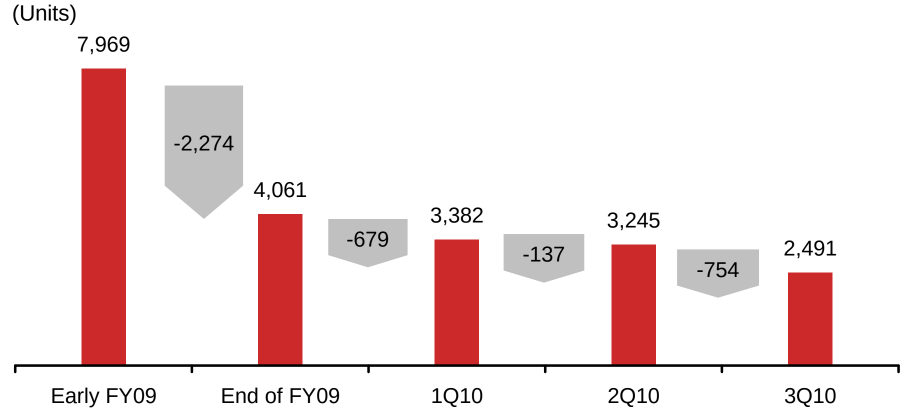


	1m	3m	6m
Absolute (W)	10.2	21.0	34.4
Absolute (US$)	7.0	24.3	44.3
Relative to Index	7.5	11.2	17.6
Market cap (US$mn)			4,654
Estimated free float (%)			69.6
52-week range (W)			117,500/67,300
3-mth avg daily turnover (US$mn)			29.09
Stock borrowability			Easy
Major shareholders (%)			
Huh Chang Soo			12.2
Huh Jin Soo			5.8

Source: Company, Nomura estimates

Per GSEC management, FY10F unsold apartments reduction target: -1,920 units

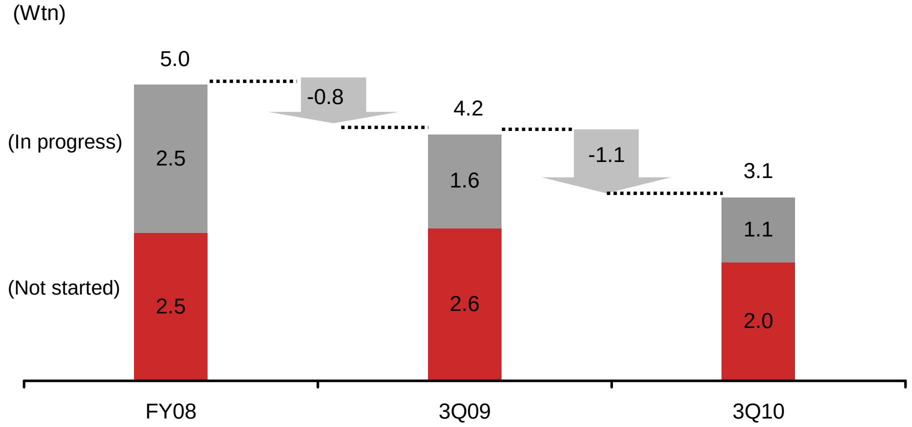
Exhibit 176. GSEC: successful unsold apartment reduction plan



Source: Company data

PF reduction targets W1.5tn level by end-FY11F

Exhibit 177. GSEC: PF liabilities reduction plan



Source: Company data

Valuation methodology and risk

Our price target of W120,000 is derived from the second quintile (0.185x) of GSEC's five-year EV/backlog range (valuation methodology unchanged). The intrinsic value indicated by our DCF analysis is W108,000, but given market risks and the sector's de-rating on the Kospi, we think the stock's EV/backlog band is a better gauge, reflecting the E&C sector's still mixed business conditions. In terms of risks to our BUY rating, we note: 1) on the domestic front, the key risk is a persistent drop in take-up for new apartments; and 2) oil price falls which could force GCC (Gulf Cooperation Council: Saudi Arabia, Kuwait, United Arab Emirates, Oman, Qatar and Bahrain) clients to cut spending plans for the next few years.

Financial statements

Income statement (Wbn)					
Year-end 31 Dec	FY08	FY09	FY10F	FY11F	FY12F
Revenue	6,866	7,377	7,460	7,578	8,572
Cost of goods sold	(5,953)	(6,422)	(6,470)	(6,523)	(7,367)
Gross profit	**913**	**955**	**990**	**1,055**	**1,205**
SG&A	(435)	(387)	(485)	(455)	(493)
Employee share expense					
Operating profit	**478**	**568**	**505**	**600**	**712**
EBITDA	**568**	**598**	**535**	**631**	**747**
Depreciation	(83)	(23)	(23)	(24)	(28)
Amortisation	(7)	(7)	(7)	(7)	(7)
EBIT	**478**	**568**	**505**	**600**	**712**
Net interest expense	33	16	22	33	37
Associates & JCEs					
Other income	37	(75)	55	27	20
Earnings before tax	**549**	**508**	**582**	**660**	**769**
Income tax	(167)	(125)	(137)	(158)	(196)
Net profit after tax	**382**	**383**	**445**	**502**	**573**
Minority interests					
Other items					
Preferred dividends					
Normalised NPAT	**382**	**383**	**445**	**502**	**573**
Extraordinary items	-	-	-	-	-
Reported NPAT	**382**	**383**	**445**	**502**	**573**
Dividends	(82)	(25)	(33)	(38)	(43)
Transfer to reserves	**299**	**358**	**412**	**463**	**529**
Valuation and ratio analysis					
FD normalised P/E (x)	14.0	14.0	12.0	10.7	9.3
FD normalised P/E at price target (x)	16.0	16.0	13.7	12.2	10.7
Reported P/E (x)	14.0	14.0	12.0	10.7	9.3
Dividend yield (%)	0.5	0.9	1.2	1.4	1.6
Price/cashflow (x)	8.6	9.7	5.0	7.2	4.8
Price/book (x)	1.8	1.6	1.5	1.3	1.3
EV/EBITDA (x)	9.4	8.2	7.8	6.0	4.6
EV/EBIT (x)	11.2	8.6	8.3	6.3	4.8
Gross margin (%)	13.3	12.9	13.3	13.9	14.1
EBITDA margin (%)	8.3	8.1	7.2	8.3	8.7
EBIT margin (%)	7.0	7.7	6.8	7.9	8.3
Net margin (%)	5.6	5.2	6.0	6.6	6.7
Effective tax rate (%)	30.5	24.7	23.5	24.0	25.5
Dividend payout (%)	21.6	6.5	7.4	7.6	7.6
Capex to sales (%)	5.1	0.5	2.1	2.1	2.1
Capex to depreciation (x)	4.2	1.6	6.8	6.6	6.3
ROE (%)	14.7	12.1	12.8	13.1	14.3
ROA (pretax %)	7.5	7.6	6.7	7.8	9.0
Growth (%)					
Revenue	14.2	7.4	1.1	1.6	13.1
EBITDA	19.1	5.2	(10.5)	17.8	18.3
EBIT	8.2	18.7	(11.1)	18.8	18.6
Normalised EPS	(4.4)	0.3	16.3	12.7	14.2
Normalised FDEPS	(4.4)	0.3	16.3	12.7	14.2
Per share					
Reported EPS (W)	7,481	7,506	8,731	9,838	11,232
Norm EPS (W)	7,481	7,506	8,731	9,838	11,232
Fully diluted norm EPS (W)	7,481	7,506	8,731	9,838	11,232
Book value per share (W)	59,510	64,686	71,906	78,377	78,397
DPS (W)	485	970	1,300	1,500	1,700

Source: Nomura estimates

Target FY11F P/E significantly below peak P/E (25x) registered in FY07

Cashflow (Wbn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
EBITDA	568	598	535	631	747
Change in working capital	190	34	490	88	370
Other operating cashflow	(139)	(81)	38	20	(10)
Cashflow from operations	**619**	**551**	**1,063**	**739**	**1,107**
Capital expenditure	(353)	(37)	(158)	(157)	(176)
Free cashflow	**267**	**514**	**905**	**582**	**931**
Reduction in investments	(951)	211	(120)	19	(33)
Net acquisitions					
Reduction in other LT assets	0	0	-	-	-
Addition in other LT liabilities	261	(16)	3	4	34
Adjustments					
Cashflow after investing acts	**(423)**	**709**	**788**	**605**	**931**
Cash dividends	(82)	(25)	(33)	(38)	(43)
Equity issue					
Debt issue	309	201	(173)	(71)	(390)
Convertible debt issue					
Others	573	(200)	(44)	(157)	(240)
Cashflow from financial acts	**799**	**(24)**	**(250)**	**(267)**	**(673)**
Net cashflow	**376**	**685**	**538**	**338**	**258**
Beginning cash	384	760	1,445	1,982	2,321
Ending cash	760	1,445	1,982	2,321	2,579
Ending net debt	12	(472)	(1,183)	(1,592)	(1,929)

Source: Nomura estimates

Balance sheet (Wbn)					
As at 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Cash & equivalents	760	1,445	1,982	2,321	2,579
Marketable securities	-	-	-	-	-
Accounts receivable	2,436	2,709	2,740	2,783	3,148
Inventories	457	429	424	424	403
Other current assets	1,275	1,311	1,213	1,306	1,194
Total current assets	**4,928**	**5,894**	**6,359**	**6,834**	**7,324**
LT investments	1,839	1,628	1,747	1,729	1,762
Fixed assets	1,412	1,422	1,452	1,483	1,518
Goodwill					
Other intangible assets					
Other LT assets	3	3	3	3	3
Total assets	**8,182**	**8,946**	**9,562**	**10,048**	**10,606**
Short-term debt	260	350	346	341	301
Accounts payable	1,804	1,496	1,513	1,537	1,739
Other current liabilities	1,725	2,348	2,748	2,948	3,348
Total current liabilities	**3,789**	**4,194**	**4,607**	**4,826**	**5,388**
Long-term debt	512	622	454	387	349
Convertible debt					
Other LT liabilities	847	831	834	838	871
Total liabilities	**5,147**	**5,647**	**5,894**	**6,051**	**6,608**
Minority interest					
Preferred stock					
Common stock	255	255	255	255	255
Retained earnings	1,783	2,141	2,408	2,709	3,053
Proposed dividends	82	25	33	38	43
Other equity and reserves	915	879	971	995	647
Total shareholders' equity	**3,035**	**3,299**	**3,667**	**3,997**	**3,998**
Total equity & liabilities	**8,182**	**8,946**	**9,562**	**10,048**	**10,606**
Liquidity (x)					
Current ratio	1.30	1.41	1.38	1.42	1.36
Interest cover	na	na	na	na	na
Leverage					
Net debt/EBITDA (x)	0.02	net cash	net cash	net cash	net cash
Net debt/equity (%)	0.4	net cash	net cash	net cash	net cash
Activity (days)					
Days receivable	127.6	127.3	133.3	133.0	126.6
Days inventory	27.1	25.2	24.1	23.7	20.5
Days payable	103.3	93.8	84.9	85.3	81.4
Cash cycle	51.4	58.7	72.5	71.4	65.8

Debt peaked in 3Q08

Source: Nomura estimates

Hyundai Motor 005380 KS

INDUSTRIALS/AUTOS & AUTO PARTS | SOUTH KOREA

Maintained

BUY

NOMURA

NOMURA FINANCIAL INVESTMENT (KOREA) CO LTD

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Action

Although HMC has outperformed the KOSPI by 37% YTD, we expect the re-rating of the company to continue on: 1) improved brand equity, 2) enhanced position in the global market and 3) a strong earnings outlook. HMC still trades at a 40% discount to global peers. We reiterate our BUY rating; HMC remains our top pick in the Korea auto space.

Catalysts

New launch of Accent in November and Grandeur in 1Q11 should support strong growth in 1H11. Strong 4Q10 results expected to be announced in late January.

Anchor themes

The Korean auto industry is still in the middle of re-rating process, to eliminate the valuation discount to the global peers. Market share gains should continue despite the unfavourable currency movement, but thanks to aggressive launches of new models with improved quality.

Closing price on 1 Dec	W179,000
Price target	**W210,000**
	(set on 26 Oct 10)
Upside/downside	17.3%
Difference from consensus	**4.0%**
FY11F net profit (Wbn)	5,612
Difference from consensus	**6.1%**

Source: Nomura

Nomura vs consensus

We expect consensus to be raised continuously, to reflect growing earnings from Kia and the overseas subsidiaries.

Re-rating to continue

① Quality improvement

We believe HMC is in the middle of a re-rating process in the equity market, to catch up its improvement in brand equity in the global auto market where it is now viewed as an "okay car" to "good car" from a "cheap car" five to ten years ago. The improvement has been shown through the market share gains and strong earnings flow, but not yet fully in the share price, in our view.

② Market share gains to continue

We believe HMC will continue to gain market share, thanks to the aggressive new model launch efforts, better product quality and enhanced brand image. Also, its strenuous efforts to meet local customers' taste should strengthen its pricing power while reducing marketing costs. We expect the currency impact to be more than offset by increasing overseas production and new model launches.

③ 12% EPS growth in 2011F

We expect HMC to post 12% y-y EPS growth in 2011F after 69% growth in 2010. We expect OP margin to improve to 10% in 2011F (vs 7% in 2009) owing to new model launches at higher prices, strong volume growth and rising utilization rates. Meanwhile, Hyundai E&C is unlikely to be a major concern for HMC, in case it is acquired by HMC as expected by local press reports, given Hyundai E&C's clean balance sheet and high ROEs.

④ Valuation still attractive

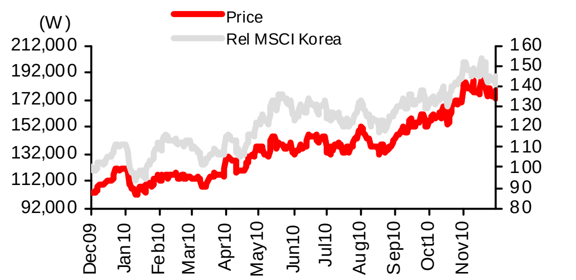
HMC is currently trading at 7x FY11 PER, which at is over 40% discount to the global peer average, based on our and consensus estimates. Our PT of W210,000 is based on 9x FY11 PER, a three-year average discount of 30% to global peers. Downside risks are steeper-than-expected sales declines in Korea and slower market-share gains in key regions.

Key financials & valuations

31 Dec (Wbn)	FY09	FY10F	FY11F	FY12F
Revenue	31,859	36,505	37,502	38,651
Reported net profit	2,962	5,014	5,612	6,135
Normalised net profit	2,962	5,014	5,612	6,135
Normalised EPS (W)	13,445	22,763	25,476	27,852
Norm. EPS growth (%)	104.2	69.3	11.9	9.3
Norm. P/E (x)	13.3	7.9	7.0	6.4
EV/EBITDA (x)	10.8	6.2	5.4	4.9
Price/book (x)	1.8	1.5	1.3	1.1
Dividend yield (%)	0.8	2.3	2.6	2.8
ROE (%)	14.2	20.6	19.3	18.0
Net debt/equity (%)	net cash	net cash	net cash	net cash
Earnings revisions				
Previous norm. net profit		5,014	5,612	6,135
Change from previous (%)		-	-	-
Previous norm. EPS (W)		22,763	25,476	27,852

Source: Company, Nomura estimates

Share price relative to MSCI Korea

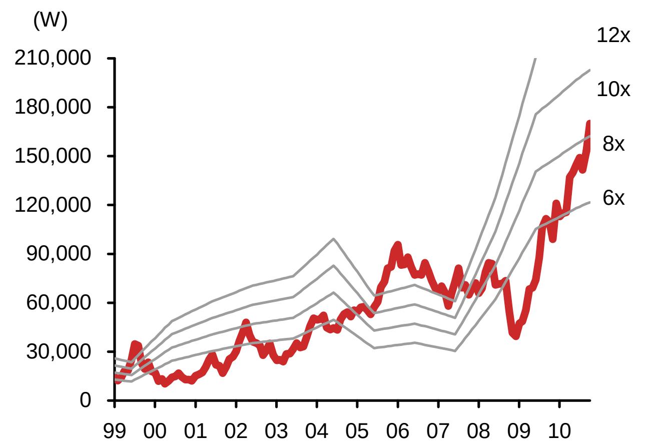


	1m	3m	6m
Absolute (W)	(0.8)	24.3	35.1
Absolute (US$)	(3.7)	27.8	45.0
Relative to Index	(3.2)	14.6	18.3

Market cap (US$mn)	34,272
Estimated free float (%)	70.9
52-week range (W)	188,000/101,500
3-mth avg daily turnover (US$mn)	131.8
Stock borrowability	Easy
Major shareholders (%)	
Hyundai Mobis	20.8
Mirae Asset	5.9

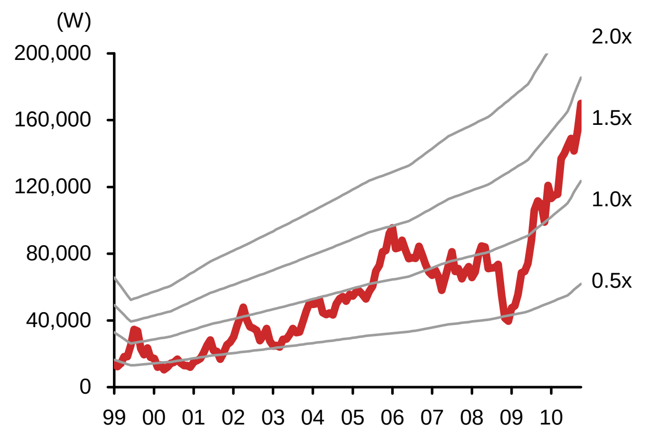
Source: Company, Nomura estimates

Exhibit 178. HMC: P/E band



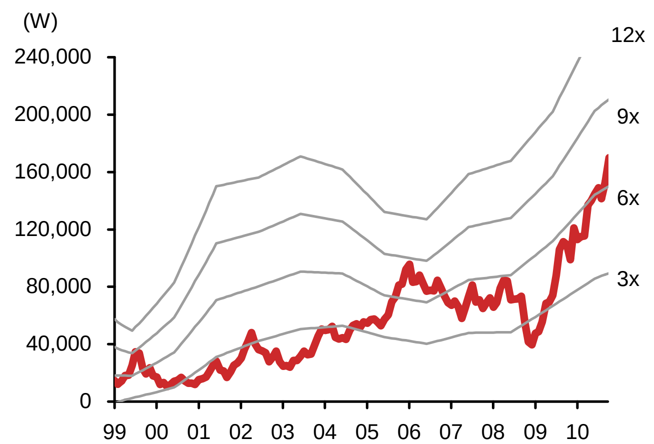
Source: Company data, Nomura estimates

Exhibit 179. HMC: P/B band



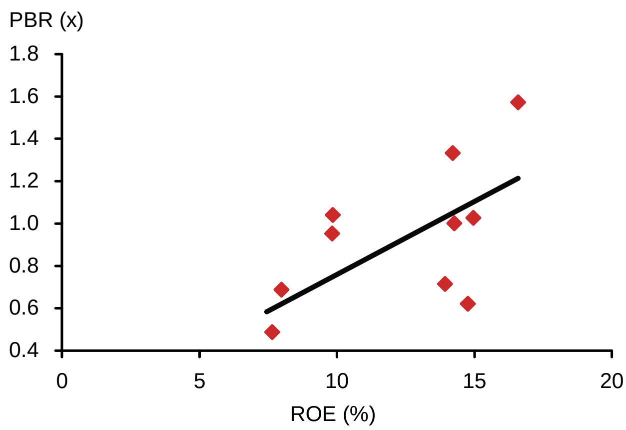
Source: Company data, Nomura estimates

Exhibit 180. HMC: EV/EBITDA band



Source: Company data, Nomura estimates

Exhibit 181. HMC: PB-ROE



Source: Company data, Nomura research

Financial statements

Income statement (Wbn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Revenue	32,190	31,859	36,505	37,502	38,651
Cost of goods sold	(25,059)	(24,885)	(26,729)	(27,083)	(27,642)
Gross profit	**7,131**	**6,975**	**9,776**	**10,419**	**11,009**
SG&A	(5,254)	(4,740)	(6,556)	(6,720)	(6,911)
Employee share expense					
Operating profit	**1,877**	**2,235**	**3,220**	**3,699**	**4,098**
EBITDA	**1,949**	**2,316**	**3,302**	**3,783**	**4,183**
Depreciation	(72)	(81)	(83)	(84)	(86)
Amortisation					
EBIT	**1,877**	**2,235**	**3,220**	**3,699**	**4,098**
Net interest expense	203	84	222	243	265
Associates & JCEs	21	1,337	2,875	3,113	3,345
Other income	(306)	125	85	110	126
Earnings before tax	**1,795**	**3,781**	**6,402**	**7,165**	**7,834**
Income tax	(347)	(820)	(1,388)	(1,553)	(1,698)
Net profit after tax	**1,448**	**2,962**	**5,014**	**5,612**	**6,135**
Minority interests					
Other items					
Preferred dividends					
Normalised NPAT	**1,448**	**2,962**	**5,014**	**5,612**	**6,135**
Extraordinary items					
Reported NPAT	**1,448**	**2,962**	**5,014**	**5,612**	**6,135**
Dividends	(236)	(317)	(892)	(1,006)	(1,091)
Transfer to reserves	**1,212**	**2,644**	**4,123**	**4,606**	**5,044**
Valuation and ratio analysis					
FD normalised P/E (x)	27.2	13.3	7.9	7.0	6.4
FD normalised P/E at price target (x)	31.9	15.6	9.2	8.2	7.5
Reported P/E (x)	27.2	13.3	7.9	7.0	6.4
Dividend yield (%)	0.6	0.8	2.3	2.6	2.8
Price/cashflow (x)	20.3	6.7	4.6	4.4	4.6
Price/book (x)	2.0	1.8	1.5	1.3	1.1
EV/EBITDA (x)	20.6	10.8	6.2	5.4	4.9
EV/EBIT (x)	21.4	11.0	6.3	5.5	5.0
Gross margin (%)	22.2	21.9	26.8	27.8	28.5
EBITDA margin (%)	6.1	7.3	9.0	10.1	10.8
EBIT margin (%)	5.8	7.0	8.8	9.9	10.6
Net margin (%)	4.5	9.3	13.7	15.0	15.9
Effective tax rate (%)	19.3	21.7	21.7	21.7	21.7
Dividend payout (%)	16.3	10.7	17.8	17.9	17.8
Capex to sales (%)	2.5	2.5	2.4	2.6	2.7
Capex to depreciation (x)	11.3	10.0	10.7	11.5	12.3
ROE (%)	7.6	14.2	20.6	19.3	18.0
ROA (pretax %)	6.5	11.2	17.5	17.7	17.4
Growth (%)					
Revenue	5.6	(1.0)	14.6	2.7	3.1
EBITDA	3.4	18.8	42.6	14.6	10.6
EBIT	3.4	19.1	44.1	14.9	10.8
Normalised EPS	(14.1)	104.2	69.3	11.9	9.3
Normalised FDEPS	(14.1)	104.2	69.3	11.9	9.3
Per share					
Reported EPS (W)	6,584	13,445	22,763	25,476	27,852
Norm EPS (W)	6,584	13,445	22,763	25,476	27,852
Fully diluted norm EPS (W)	6,584	13,445	22,763	25,476	27,852
Book value per share (W)	89,216	100,006	121,329	142,757	166,044
DPS (W)	1,070	1,440	4,047	4,566	4,954

Source: Nomura estimates

Snowballing earnings from overseas subsidiaries

Cashflow (Wbn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
EBITDA	1,949	2,316	3,302	3,783	4,183
Change in working capital	(1,062)	2,796	(874)	(113)	(439)
Other operating cashflow	1,052	733	6,189	5,351	4,890
Cashflow from operations	**1,940**	**5,845**	**8,618**	**9,021**	**8,635**
Capital expenditure	(814)	(808)	(885)	(966)	(1,053)
Free cashflow	**1,126**	**5,037**	**7,733**	**8,055**	**7,582**
Reduction in investments	(1,201)	(3,389)	(2,347)	(3,272)	(3,861)
Net acquisitions	(352)	(228)	(1,924)	(1,426)	(1,246)
Reduction in other LT assets	-	-	-	-	-
Addition in other LT liabilities	221	(208)	126	116	99
Adjustments	(285)	371	(2,125)	(1,622)	(1,170)
Cashflow after investing acts	**(491)**	**1,582**	**1,462**	**1,850**	**1,404**
Cash dividends	(276)	(236)	(317)	(892)	(1,006)
Equity issue	-	-	-	-	-
Debt issue	1,066	(820)	46	45	13
Convertible debt issue					
Others	11	(23)	(24)	(25)	(27)
Cashflow from financial acts	**801**	**(1,079)**	**(296)**	**(872)**	**(1,020)**
Net cashflow	**310**	**504**	**1,167**	**978**	**384**
Beginning cash	1,446	1,757	2,260	3,427	4,405
Ending cash	1,756	2,260	3,426	4,405	4,790
Ending net debt	1,197	(138)	(1,260)	(2,193)	(2,565)

Source: Nomura estimates

Balance sheet (Wbn)					
As at 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Cash & equivalents	1,757	2,260	3,427	4,405	4,790
Marketable securities	3,260	5,102	5,357	5,611	5,864
Accounts receivable	2,520	2,165	2,506	2,600	2,679
Inventories	1,809	1,384	1,502	1,537	1,569
Other current assets	956	881	1,000	1,017	1,038
Total current assets	**10,301**	**11,792**	**13,791**	**15,170**	**15,940**
LT investments	10,077	11,624	13,717	16,734	20,342
Fixed assets	9,754	9,726	9,907	10,090	10,274
Goodwill					
Other intangible assets	2,036	2,303	2,602	2,937	3,310
Other LT assets					
Total assets	**32,168**	**35,446**	**40,017**	**44,931**	**49,866**
Short-term debt	1,688	754	731	712	694
Accounts payable	2,444	3,847	3,742	3,792	3,483
Other current liabilities	3,784	4,323	4,130	4,114	4,116
Total current liabilities	**7,915**	**8,924**	**8,604**	**8,617**	**8,294**
Long-term debt	1,266	1,367	1,436	1,500	1,530
Convertible debt					
Other LT liabilities	3,334	3,126	3,252	3,367	3,467
Total liabilities	**12,515**	**13,417**	**13,291**	**13,485**	**13,291**
Minority interest					
Preferred stock					
Common stock	1,489	1,489	1,489	1,489	1,489
Retained earnings	12,419	14,991	19,688	24,408	29,538
Proposed dividends					
Other equity and reserves	5,744	5,549	5,549	5,549	5,549
Total shareholders' equity	**19,652**	**22,029**	**26,726**	**31,446**	**36,576**
Total equity & liabilities	**32,168**	**35,446**	**40,017**	**44,931**	**49,866**
Liquidity (x)					
Current ratio	1.30	1.32	1.60	1.76	1.92
Interest cover	na	na	na	na	na
Leverage					
Net debt/EBITDA (x)	0.61	net cash	net cash	net cash	net cash
Net debt/equity (%)	6.1	net cash	net cash	net cash	net cash
Activity (days)					
Days receivable	26.9	26.8	23.4	24.8	25.0
Days inventory	23.8	23.4	19.7	20.5	20.6
Days payable	39.3	46.1	51.8	50.8	48.2
Cash cycle	11.3	4.1	(8.8)	(5.4)	(2.6)

Source: Nomura estimates

Strong earnings growth leading to solid cash position

LG Chem 051910 KS

OIL & GAS/CHEMICALS | SOUTH KOREA

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Maintained

BUY

Action

Due to weaker earnings prospects in 4Q10, LG Chem's share price has underperformed its Korean chemical peers in the past three months. Investors, we believe, should focus on the positive trend of the petrochemical business, the start of automotive battery shipments and the recovery of electronic materials from early FY11F. LGC will likely be a direct beneficiary of the petrochemical upturn we expect in 2011-12F. BUY.

Catalysts

We see: 1) resilient petrochemical earnings, 2) an increase in car battery shipment, and; 3) positive progress of the LCD glass business as catalysts.

Anchor themes

We believe the chemical sector is poised to enter the Golden Ages, benefiting from rising demand and restrained capacity additions in the next two years. We believe the sector's rerating will be underpinned by expectations of an ethylene upcycle, receding fears of oversupply and upwards revisions in street estimates.

Closing price on 1 Dec	W395,500
Price target	W500,000
	(set on 3 Nov 10)
Upside/downside	26.4%
Difference from consensus	19.0%
FY11F net profit (Wbn)	2,706
Difference from consensus	26.1%

Source: Nomura

Nomura vs consensus

Our higher-than-the-street estimates may stem from a more bullish view of petrochemical division earnings

Valuing the uncharted future (II)

① Maintain BUY, PT of W500,000

We maintain BUY on LG Chem (LGC) with a price target of W500,000 based on a sum-of-the-parts methodology. Our PT reflects a more positive view of petrochemical and car battery business units. We value auto battery and LCD glass at W25,000/share and W28,000/share.

② Petrochemicals – bull cycle has come

For LGC, olefins/PE/PP contribute 31% of FY10F petrochemicals revenue, while products with more resilient fundamentals make up the remainder. We estimate that in 1H10F, acrylates and plasticizers (including ox-alcohol) posted a 20%-plus operating margin for LGC, while PVC and ABS/PS likely posted single-digit margins.

③ Polarizer film and IT batteries – expanding capacities

Polarizer film and IT batteries will likely expand capacities further in 2011-12F owing to market-share gains and increasing orders from existing customers, in our view. LGC maintains the lead in the global polarizer film market, while it is vying for the No.1 or 2 position in the IT battery market (currently No. 3). LGC's efforts to widen its lead over peers in terms of volume and cost structure should help to re-rate earnings and the share price, in our view.

④ Automotive batteries – Chevy Volt as the barometer

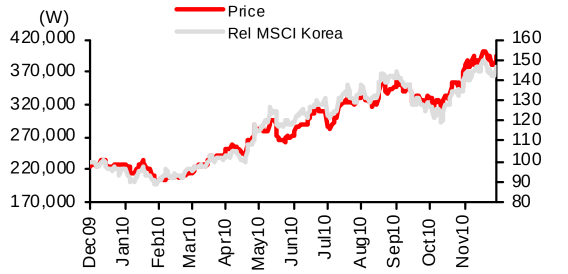
LGC is on track to make the first shipment for GM's Chevy Volt, which is slated for launch in November 2010. The retail price is expected to be US$33,500 (Nissan's competing all-electric LEAF is out for US$25,280) taking the US$7,500 federal tax credit into account. We expect automotive batteries to represent 9% of LGC's FY15F overall sales and OP.

Key financials & valuations

31 Dec (Wbn)	FY09	FY10F	FY11F	FY12F
Revenue	15,521	19,449	21,480	24,776
Reported net profit	1,533	2,200	2,706	2,995
Normalised net profit	1,533	2,200	2,706	2,995
Normalised EPS (W)	23,129	33,197	40,829	45,196
Norm. EPS growth (%)	74.4	43.5	23.0	10.7
Norm. P/E (x)	17.1	11.9	9.7	8.8
EV/EBITDA (x)	10.2	7.8	6.3	5.6
Price/book (x)	4.4	3.6	3.0	2.5
Dividend yield (%)	0.8	1.0	1.1	1.3
ROE (%)	28.1	33.6	33.8	31.2
Net debt/equity (%)	22.0	9.5	2.6	net cash
Earnings revisions				
Previous norm. net profit		2,200	2,706	2,995
Change from previous (%)		-	-	-
Previous norm. EPS (W)		33,197	40,829	45,196

Source: Company, Nomura estimates

Share price relative to MSCI Korea



	1m	3m	6m
Absolute (W)	6.9	14.3	45.4
Absolute (US$)	3.8	17.5	56.1
Relative to Index	4.3	4.3	29.4

Market cap (US$mn)	22,782
Estimated free float (%)	69.9
52-week range (W)	402,000/200,000
3-mth avg daily turnover (US$mn)	118.3
Stock borrowability	Easy
Major shareholders (%)	
LG Corp	30.1
Mirae Asset	8.5

Source: Company, Nomura estimates

Earnings preview

Valuing the uncharted future (II)

Our price target of W500,000 is based on a sum-of-the-parts (SOTP) methodology, where we forecast the enterprise value of the petrochemicals and electronic material (EM) businesses by applying different target multiples. For the EM division, we apply 10.0x, which represents a 20% premium to the Korea tech sector average (we include material, component and growth companies such as Samsung SDI, SEMCO, Samsung Techwin, Jusung Engineering and Technosemichem). For the petrochemicals division, we apply 6.9x, which represents the stock's historical peak cycle multiple (average of FY05-09). We assess the enterprise value of the LCD glass and automotive battery businesses at W2.3tn and W2.1tn, respectively.

Downside risks could stem from worse-than-expected petrochemicals and LCD cycles, which could dampen the company's FY10-11F earnings. Execution risk from car battery production could also de-rate the share price.

Exhibit 182. LG Chem: SOTP valuation

(Wbn)		Remark
Electronic material EV (a)	**11,938**	
EBITDA	1,194	2011F
Multiple (x)	10.0	20% premium to Korea tech average; unchanged
Petrochemical EV (b)	**17,627**	
EBITDA	2,540	2011F
Multiple (x)	6.9	LGC's peak cycle multiple (2005-09)
LCD glass EV (c)	**2,306**	
Auto battery EV (d)	**2,139**	
EV (a)+(b)+(c)+(d)	**34,010**	
(-) Net debt	232	2011F
Market cap	**33,777**	
(-) preferred share market cap	1,014	Market cap Nov 1
Fair market cap	**32,697**	
# of shares (mn)	66.3	Common share
LGC fair value (W/share)	**493,386**	

Source: Nomura estimates

Exhibit 183. LG Chem: quarterly estimate (2010: IFRS based)

(Wbn)	1Q09	2Q09	3Q09	4Q09	2009	1Q10	2Q10	3Q10	4Q10F	2010F
Sales	3,350	3,830	4,295	4,046	15,521	4,423	5,028	5,021	4,977	19,449
Petrochemical	2,554	2,805	3,010	2,914	11,284	3,248	3,705	3,712	3,605	14,270
Electronic material	796	1,025	1,285	1,132	4,237	1,175	1,323	1,309	1,372	5,179
Operating profit	485	629	697	287	2,098	652	828	779	578	2,837
Margin (%)	*14.5*	*16.4*	*16.2*	*7.1*	*13.5*	*14.8*	*16.5*	*15.5*	*11.6*	*14.6*
Petrochemical	380	511	491	226	1,608	486	624	621	397	2,127
Electronic material	105	118	206	61	490	167	204	158	181	709
Recurring profit	433	621	704		2,021	649	822	791	560	2,821
Margin (%)	*12.9*	*16.2*	*16.4*		*13.0*	*14.7*	*16.3*	*15.7*	*11.2*	*14.5*
Net profit	299	475	542		1,533	518	646	599	438	2,200
Margin (%)	*8.9*	*12.4*	*12.6*		*9.9*	*11.7*	*12.8*	*11.9*	*8.8*	*11.3*

Note: 2009 is based on "Korea GAPP consolidated", not IFRS. Full FY09 P&L on consolidated basis is not available

Source: Company data, Nomura estimates

Financial statements

Income statement (Wbn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Revenue	14,555	15,521	19,449	21,480	24,776
Cost of goods sold	(12,300)	(12,390)	(15,492)	(16,807)	(19,664)
Gross profit	**2,255**	**3,131**	**3,958**	**4,674**	**5,112**
SG&A	(934)	(1,034)	(1,121)	(1,187)	(1,271)
Employee share expense					
Operating profit	**1,321**	**2,098**	**2,837**	**3,486**	**3,841**
EBITDA	**1,912**	**2,706**	**3,444**	**4,181**	**4,637**
Depreciation	(567)	(586)	(585)	(672)	(773)
Amortisation	(25)	(22)	(22)	(23)	(23)
EBIT	**1,321**	**2,098**	**2,837**	**3,486**	**3,841**
Net interest expense	(92)	(40)	29	35	52
Associates & JCEs	4	2	-	-	-
Other income	20	(37)	(45)	(52)	(54)
Earnings before tax	**1,254**	**2,021**	**2,821**	**3,469**	**3,840**
Income tax	(267)	(489)	(621)	(763)	(845)
Net profit after tax	**987**	**1,533**	**2,200**	**2,706**	**2,995**
Minority interests					
Other items					
Preferred dividends					
Normalised NPAT	**987**	**1,533**	**2,200**	**2,706**	**2,995**
Extraordinary items					
Reported NPAT	**987**	**1,533**	**2,200**	**2,706**	**2,995**
Dividends	(167)	(209)	(269)	(296)	(333)
Transfer to reserves	**820**	**1,324**	**1,931**	**2,410**	**2,662**
Valuation and ratio analysis					
FD normalised P/E (x)	29.8	17.1	11.9	9.7	8.8
FD normalised P/E at price target (x)	37.7	21.6	15.1	12.2	11.1
Reported P/E (x)	29.8	17.1	11.9	9.7	8.8
Dividend yield (%)	0.6	0.8	1.0	1.1	1.3
Price/cashflow (x)	29.9	10.8	8.9	8.1	7.2
Price/book (x)	5.8	4.4	3.6	3.0	2.5
EV/EBITDA (x)	14.8	10.2	7.8	6.3	5.6
EV/EBIT (x)	21.5	13.1	9.5	7.6	6.8
Gross margin (%)	15.5	20.2	20.3	21.8	20.6
EBITDA margin (%)	13.1	17.4	17.7	19.5	18.7
EBIT margin (%)	9.1	13.5	14.6	16.2	15.5
Net margin (%)	6.8	9.9	11.3	12.6	12.1
Effective tax rate (%)	21.3	24.2	22.0	22.0	22.0
Dividend payout (%)	16.9	13.6	12.2	10.9	11.1
Capex to sales (%)	6.5	7.0	6.2	7.0	6.9
Capex to depreciation (x)	1.7	1.9	2.1	2.2	2.2
ROE (%)	21.9	28.1	33.6	33.8	31.2
ROA (pretax %)	15.4	22.5	28.5	31.2	30.2
Growth (%)					
Revenue	27.5	6.6	25.3	10.4	15.3
EBITDA	13.3	41.5	27.2	21.4	10.9
EBIT	24.0	58.8	35.2	22.9	10.2
Normalised EPS	13.1	74.4	43.5	23.0	10.7
Normalised FDEPS	13.1	74.4	43.5	23.0	10.7
Per share					
Reported EPS (W)	13,262	23,129	33,197	40,829	45,196
Norm EPS (W)	13,262	23,129	33,197	40,829	45,196
Fully diluted norm EPS (W)	13,262	23,129	33,197	40,829	45,196
Book value per share (W)	67,912	89,431	109,565	133,047	158,019
DPS (W)	2,245	3,157	4,067	4,466	5,024

Source: Nomura estimates

This includes automotive battery revenue of W232bn

Cashflow (Wbn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
EBITDA	1,912	2,706	3,444	4,181	4,637
Change in working capital	(756)	(96)	(79)	(217)	(241)
Other operating cashflow	(171)	(183)	(422)	(727)	(769)
Cashflow from operations	**984**	**2,427**	**2,943**	**3,237**	**3,627**
Capital expenditure	(948)	(1,092)	(1,200)	(1,500)	(1,700)
Free cashflow	**36**	**1,335**	**1,743**	**1,737**	**1,927**
Reduction in investments	(79)	(83)	(79)	(173)	(519)
Net acquisitions	(11)	(2)	-	-	-
Reduction in other LT assets	(20)	115			
Addition in other LT liabilities	24	(58)	4	4	5
Adjustments	168	85	(586)	(598)	(524)
Cashflow after investing acts	**119**	**1,391**	**1,083**	**970**	**889**
Cash dividends	(167)	(209)	(268)	(296)	(333)
Equity issue	-	(50)	-	-	-
Debt issue	(323)	(361)	(424)	(419)	(157)
Convertible debt issue					
Others	295	(178)	(198)	(218)	(240)
Cashflow from financial acts	**(195)**	**(799)**	**(891)**	**(932)**	**(729)**
Net cashflow	**(76)**	**592**	**192**	**37**	**160**
Beginning cash	591	514	1,107	1,298	1,336
Ending cash	515	1,106	1,298	1,336	1,495
Ending net debt	2,228	1,304	688	232	(84)

Source: Nomura estimates

Balance sheet (Wbn)					
As at 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Cash & equivalents	514	1,107	1,298	1,336	1,495
Marketable securities	-	-	-	-	-
Accounts receivable	1,552	2,455	2,917	3,222	3,593
Inventories	1,848	1,598	1,549	1,681	1,966
Other current assets	364	118	141	156	180
Total current assets	**4,277**	**5,277**	**5,906**	**6,394**	**7,234**
LT investments	179	262	288	346	519
Fixed assets	5,186	4,775	5,391	6,219	7,146
Goodwill					
Other intangible assets	(75)	162	164	165	167
Other LT assets	169	54	54	54	54
Total assets	**9,736**	**10,531**	**11,803**	**13,179**	**15,120**
Short-term debt	1,508	1,833	1,466	1,100	990
Accounts payable	676	1,785	2,169	2,353	2,753
Other current liabilities	1,087	289	264	313	352
Total current liabilities	**3,271**	**3,907**	**3,899**	**3,766**	**4,094**
Long-term debt	1,234	578	520	468	421
Convertible debt					
Other LT liabilities	177	119	123	128	132
Total liabilities	**4,683**	**4,604**	**4,542**	**4,361**	**4,648**
Minority interest					
Preferred stock	43	43	43	43	43
Common stock	376	376	376	376	376
Retained earnings	3,037	4,836	6,090	7,650	9,281
Proposed dividends					
Other equity and reserves	1,596	671	752	748	772
Total shareholders' equity	**5,053**	**5,927**	**7,261**	**8,817**	**10,472**
Total equity & liabilities	**9,736**	**10,531**	**11,803**	**13,179**	**15,120**
Liquidity (x)					
Current ratio	1.31	1.35	1.51	1.70	1.77
Interest cover	14.4	51.8	na	na	na
Leverage					
Net debt/EBITDA (x)	1.17	0.48	0.20	0.06	net cash
Net debt/equity (%)	44.1	22.0	9.5	2.6	net cash
Activity (days)					
Days receivable	37.6	47.1	50.4	52.2	50.3
Days inventory	49.5	50.7	37.1	35.1	33.9
Days payable	25.0	36.3	46.6	49.1	47.5
Cash cycle	62.1	61.6	40.9	38.1	36.8

Source: Nomura estimates

Samsung Electronics 005930 KS

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Maintained

BUY

NOMURA
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Action

We anticipate Samsung's (SEC) earnings will bottom out in 1Q11F, driven by all its operations. The stock is trading at a 15% discount to the market average P/E, and we expect earnings to recover from a bottom in 1Q11F. We advise accumulating the stock before an anticipated inflection point from 1Q11F. SEC remains on our Conviction List as a BUY.

Catalysts

With LCD taking the lead, we believe major segments that are now muddling through hardships will bottom out one by one from 1Q11F.

Anchor themes

In our view, SEC is best prepared among its peers for "rising technology", such as OLED display, specialty DRAM, NAND and smartphones. With its proven competitiveness in the above spaces, Samsung should recover from the current downcycle ahead of its peers, in our view.

Closing price on 1 Dec	W820,000
Price target	W1,050,000
	(set on 1 Nov 10)
Upside/downside	28.0%
Difference from consensus	3.1%
FY11F net profit (Wbn)	14,976
Difference from consensus	-0.3%

Source: Nomura

Nomura vs consensus

We are more positive than the street on Samsung's ability to differentiate itself from peers in terms of cost competitiveness and market share.

Soft-landing then rerating

① Earnings to bottom in 1Q11F

Having posted record-high results in the first half of 2010, SEC's earnings have been trending down since 3Q10. We anticipate a bottoming out in 1Q11F across all its operations.

② Memory – margins to pick up in 1Q11F

We believe the current downtrend should not last long given that: 1) the technology gap between the 1st tier and the 2nd tier has widened to an extent we have not seen so far; and 2) 2nd-tier players' financial standing has deteriorated. We forecast industry supply growth will begin to slow while demand will pick up in 1Q11F, resulting in margin improvement. As for NAND, we believe the popularity of smartphones, tablet PCs and SSD should directly benefit NAND demand. We forecast the NAND market will experience a persistent upcycle after seasonal weakness in 1Q11F.

③ Panels – differentiated and constant growth ahead

Similar to DRAM, we forecast the panel cycle will bottom out in 1Q11F and recover thereafter. Given its ahead-of-peers status in AMOLED technology, we think SEC is likely to present a differentiated and constant growth story in flat panels.

④ Handsets – to benefit from wider roll-out of Android

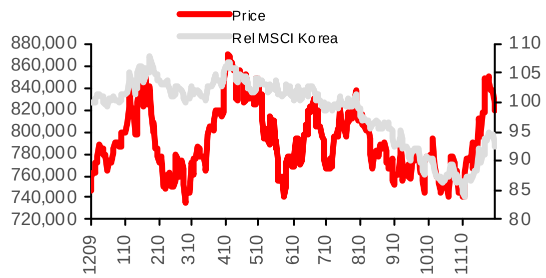
We believe SEC's Android smartphone offerings have successfully settled in the market. In our view, 2011 will be a pivotal point where the number of Android smartphones will begin to surpass the iPhone series and the OS eco-system, which has been regarded as an Achilles' heel, will improve in earnest. We estimate SEC will ship 70mn smartphones and Galaxy Tabs, collectively, in 2011F, up 140% y-y.

Key financials & valuations

31 Dec (Wbn)	FY09	FY10F	FY11F	FY12F
Revenue	136,323	152,843	154,026	169,769
Reported net profit	9,572	15,819	14,976	18,018
Normalised net profit	9,572	15,819	14,976	18,018
Normalised EPS (W)	64,618	106,695	101,013	121,533
Norm. EPS growth (%)	71.8	65.1	(5.3)	20.3
Norm. P/E (x)	14.6	8.8	9.3	7.7
EV/EBITDA (x)	5.1	3.9	3.5	2.7
Price/book (x)	1.7	1.4	1.3	1.1
Dividend yield (%)	1.0	1.6	1.7	1.8
ROE (%)	15.0	20.6	16.6	17.3
Net debt/equity (%)	net cash	net cash	net cash	net cash
Earnings revisions				
Previous norm. net profit		15,819	14,976	18,018
Change from previous (%)		-	-	-
Previous norm. EPS (W)		106,695	101,013	121,533

Source: Company, Nomura estimates

Share price relative to MSCI Korea



	1m	3m	6m
Absolute (W)	9.8	9.0	6.8
Absolute (US$)	7.0	12.5	15.0
Relative to Index	8.3	0.3	(10.6)
Market cap (US$mn)			105,356
Estimated free float (%)			82.0
52-week range (W)			870,000/736,000
3-mth avg daily turnover (US$mn)			276.8
Stock borrowability			Easy
Major shareholders (%)			
Samsung Life Insurance			7.5
Samsung Corp.			5.6

Source: Company, Nomura estimates

Digital Media – margins to normalise throughout 2011F

For TVs, weaker-than-expected demand growth and severe price competition has led to margin contraction. TV inventory adjustment, which we believe is likely to at end-2010, should further weigh on profitability, in our view. Yet, we forecast margin normalisation for the company's TV set operations throughout 2011F thanks to the absence of inventory adjustment. In the home appliances segment, SEC's aggressive investment has pressured profitability. We believe this is temporary in nature and forecast margin improvement as well as market share growth in 2011F.

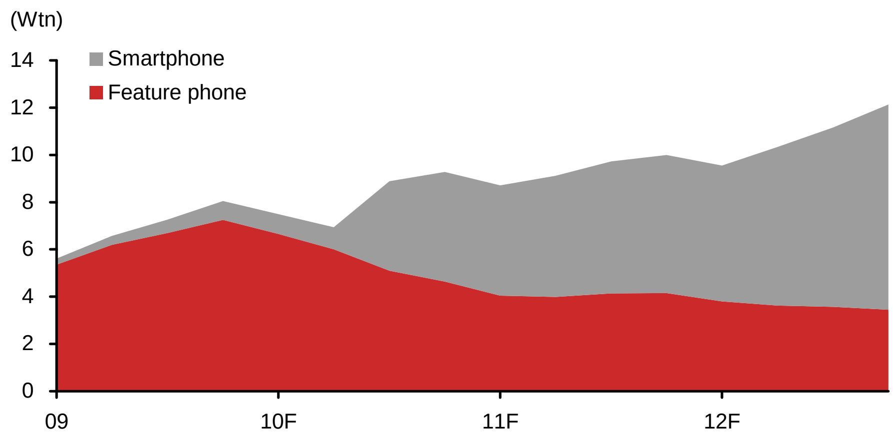
Maintain BUY with PT of W1,050,000

We reaffirm our BUY call and price target of W1,050,000. In spite of weakened earnings momentum from 3Q10 to 1Q11F, which we believe will be only temporary, we believe the company is widening the technology gap in memory, panel, and TV, against its competitors. In smartphones, where SEC has lagged, it appears to be sharpening its edge, we think.

Valuation and investment risks

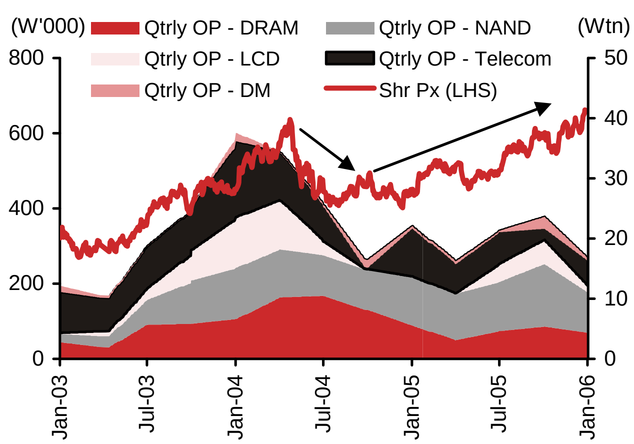
In determining our price target for SEC, we apply a target P/BV of 1.6x (on FY11F ROE of 16.6%) at an FY11F BVPS of W652,087 (method unchanged). As for risks to our call, should the won strengthen at a faster pace than expected, cost reduction impact (in won) would slow and won-translated profits could come in below our estimates.

Exhibit 184. SEC: handset revenue forecast



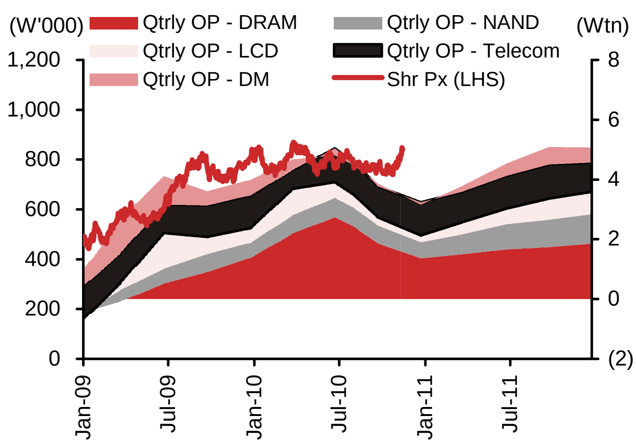
Source: Nomura estimates

Exhibit 185. SEC: OP and share price (FY03-06)



Source: Bloomberg, Nomura research

Exhibit 186. SEC: OP and share price (FY09 - present)



Source: Bloomberg, Nomura estimates

Financial statements

Income statement (Wbn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Revenue	121,294	136,323	152,843	154,026	169,769
Cost of goods sold	(89,762)	(94,593)	(99,975)	(101,169)	(109,253)
Gross profit	**31,532**	**41,730**	**52,868**	**52,857**	**60,515**
SG&A	(25,500)	(30,747)	(36,005)	(36,551)	(40,151)
Employee share expense	-	(80)	902	400	400
Operating profit	**6,032**	**10,903**	**17,765**	**16,706**	**20,765**
EBITDA	**16,127**	**22,063**	**29,098**	**30,982**	**38,033**
Depreciation	(9,856)	(10,911)	(10,850)	(13,780)	(16,760)
Amortisation	(240)	(248)	(483)	(495)	(508)
EBIT	**6,032**	**10,903**	**17,765**	**16,706**	**20,765**
Net interest expense	(56)	(203)	(50)	203	344
Associates & JCEs	838	1,713	2,073	2,189	2,311
Other income	(236)	(222)	(163)	(98)	(98)
Earnings before tax	**6,578**	**12,191**	**19,625**	**19,000**	**23,322**
Income tax	(688)	(2,431)	(3,688)	(3,771)	(4,898)
Net profit after tax	**5,890**	**9,760**	**15,937**	**15,229**	**18,424**
Minority interests	(364)	(188)	(118)	(253)	(406)
Other items					
Preferred dividends					
Normalised NPAT	**5,526**	**9,572**	**15,819**	**14,976**	**18,018**
Extraordinary items					
Reported NPAT	**5,526**	**9,572**	**15,819**	**14,976**	**18,018**
Dividends	(809)	(1,186)	(1,839)	(1,987)	(2,136)
Transfer to reserves	**4,717**	**8,386**	**13,980**	**12,989**	**15,883**
Valuation and ratio analysis					
FD normalised P/E (x)	25.2	14.6	8.8	9.3	7.7
FD normalised P/E at price target (x)	32.3	18.7	11.3	11.9	9.9
Reported P/E (x)	21.8	12.7	7.7	8.1	6.7
Dividend yield (%)	0.7	1.0	1.6	1.7	1.8
Price/cashflow (x)	9.0	6.3	5.4	4.1	3.4
Price/book (x)	2.1	1.7	1.4	1.3	1.1
EV/EBITDA (x)	7.6	5.1	3.9	3.5	2.7
EV/EBIT (x)	18.8	9.5	6.1	6.2	4.7
Gross margin (%)	26.0	30.6	34.6	34.3	35.6
EBITDA margin (%)	13.3	16.2	19.0	20.1	22.4
EBIT margin (%)	5.0	8.0	11.6	10.8	12.2
Net margin (%)	4.6	7.0	10.3	9.7	10.6
Effective tax rate (%)	10.5	19.9	18.8	19.8	21.0
Dividend payout (%)	14.6	12.4	11.6	13.3	11.9
Capex to sales (%)	11.8	6.3	13.7	15.3	15.1
Capex to depreciation (x)	1.5	0.8	1.9	1.7	1.5
ROE (%)	10.1	15.0	20.6	16.6	17.3
ROA (pretax %)	7.5	12.7	17.6	14.5	16.3
Growth (%)					
Revenue	23.1	12.4	12.1	0.8	10.2
EBITDA	(7.7)	36.8	31.9	6.5	22.8
EBIT	(32.8)	80.8	62.9	(6.0)	24.3
Normalised EPS	(25.8)	71.8	65.1	(5.3)	20.3
Normalised FDEPS	(25.5)	73.2	65.3	(5.3)	20.3
Per share					
Reported EPS (W)	37,619	64,618	106,695	101,013	121,533
Norm EPS (W)	37,619	64,618	106,695	101,013	121,533
Fully diluted norm EPS (W)	32,480	56,260	92,978	88,027	105,908
Book value per share (W)	395,651	471,453	567,642	652,087	755,654
DPS (W)	5,500	8,000	13,000	14,000	15,000

Source: Nomura estimates

We find the stock is trading at a 15% discount to the KOSPI's average P/E

Cashflow (Wbn)					
Year-end 31 Dec	FY08	FY09	FY10F	FY11F	FY12F
EBITDA	16,127	22,063	29,098	30,982	38,033
Change in working capital	(3,935)	7,265	353	5,459	6,511
Other operating cashflow	1,168	(10,142)	(6,875)	(7,110)	(8,975)
Cashflow from operations	**13,360**	**19,186**	**22,576**	**29,331**	**35,569**
Capital expenditure	(14,302)	(8,525)	(20,910)	(23,594)	(25,573)
Free cashflow	**(942)**	**10,660**	**1,666**	**5,737**	**9,996**
Reduction in investments	1,830	(3,768)	(3,732)	(2,426)	(2,568)
Net acquisitions					
Reduction in other LT assets	1,936	(6,283)	(1,212)	(237)	(257)
Addition in other LT liabilities	2,773	(3,078)	3,420	(3,507)	(2,322)
Adjustments	(5,365)	7,230	1,008	5,934	4,890
Cashflow after investing acts	**232**	**4,762**	**1,150**	**5,500**	**9,739**
Cash dividends	(1,315)	(871)	(617)	(1,839)	(1,987)
Equity issue	166	331	42	-	-
Debt issue	2,773	(3,078)	3,420	(3,507)	(2,322)
Convertible debt issue					
Others	1,128	192	(3,206)	60	60
Cashflow from financial acts	**2,751**	**(3,427)**	**(361)**	**(5,286)**	**(4,249)**
Net cashflow	**2,983**	**1,335**	**789**	**213**	**5,490**
Beginning cash	5,832	8,815	10,149	10,938	11,151
Ending cash	8,815	10,149	10,938	11,151	16,641
Ending net debt	8,640	(530)	(414)	(4,134)	(11,946)

Source: Nomura estimates

We forecast FY11F capex of W23.5tn

Balance sheet (Wbn)					
As at 31 Dec	FY08	FY09	FY10F	FY11F	FY12F
Cash & equivalents	8,815	10,149	10,938	11,151	16,641
Marketable securities	4,573	10,734	11,418	11,418	11,418
Accounts receivable	12,044	17,818	19,671	21,292	23,047
Inventories	9,493	9,839	14,682	14,802	14,922
Other current assets	14,044	5,671	5,432	1,218	(4,074)
Total current assets	**48,969**	**54,211**	**62,141**	**59,881**	**61,955**
LT investments	11,378	8,985	12,033	14,459	17,027
Fixed assets	42,496	43,560	53,300	65,205	76,792
Goodwill					
Other intangible assets	787	1,256	2,842	2,958	3,078
Other LT assets	1,671	4,168	4,426	4,791	5,186
Total assets	**105,301**	**112,180**	**134,742**	**147,293**	**164,036**
Short-term debt	11,290	5,946	9,279	6,200	4,159
Accounts payable	5,587	8,235	10,175	11,013	11,921
Other current liabilities	15,330	17,694	22,565	24,712	26,900
Total current liabilities	**32,207**	**31,876**	**42,019**	**41,925**	**42,979**
Long-term debt	6,165	3,673	1,245	817	536
Convertible debt					
Other LT liabilities	4,005	3,587	3,581	3,665	3,752
Total liabilities	**42,377**	**39,135**	**46,845**	**46,407**	**47,267**
Minority interest	4,807	3,211	3,738	4,208	4,736
Preferred stock	119	119	119	119	119
Common stock	778	778	778	778	778
Retained earnings	55,420	65,181	83,931	96,920	112,803
Proposed dividends					
Other equity and reserves	1,800	3,756	(670)	(1,139)	(1,667)
Total shareholders' equity	**58,117**	**69,834**	**84,159**	**96,678**	**112,033**
Total equity & liabilities	**105,301**	**112,180**	**134,742**	**147,293**	**164,036**
Liquidity (x)					
Current ratio	1.52	1.70	1.48	1.43	1.44
Interest cover	107.6	53.7	358.6	na	na
Leverage					
Net debt/EBITDA (x)	0.54	net cash	net cash	net cash	net cash
Net debt/equity (%)	14.9	net cash	net cash	net cash	net cash
Activity (days)					
Days receivable	35.0	40.0	44.8	48.5	47.8
Days inventory	35.6	37.3	44.8	53.2	49.8
Days payable	23.7	26.7	33.6	38.2	38.4
Cash cycle	46.9	50.6	55.9	63.5	59.2

Source: Nomura estimates

Samsung Engineering 028050 KS

INDUSTRIALS/ENGINEERING & CONSTRUCTION | SOUTH KOREA

Maintained

BUY

NOMURA
NOMURA FINANCIAL INVESTMENT (KOREA) CO LTD

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Action

SSE recently presented a bullish new order target for FY11F which would see the order backlog grow by 25%. We recently revised up FY11F earnings to reflect improving order momentum in EPC plant projects out of the Gulf and at home. Our target EV/backlog multiple also moved up, but only to the median of the historical range. BUY and PT of W250,000 reaffirmed.

Catalysts

We anticipate continued robust project activity in the Gulf, SSE's key market, in the coming months as a result of firm oil prices. Domestic plant orders are growing strongly off the highest technology plant capex levels since 2005-06.

Anchor themes

Within the broader construction sector, key longer-term focus areas are overseas construction and domestic homebuilding. Refer to our report on SSE, *Company visit: climbing a wall of worry quickly*, 28 September, 2010.

Closing price on 1 Dec	W197,000
Price target	**W250,000**
	(set on 16 Nov 10)
Upside/downside	26.9%
Difference from consensus	**29.8%**
FY11F net profit (Wbn)	512
Difference from consensus	**6.1%**

Source: Nomura

Nomura vs consensus

We have higher-than-consensus estimates on a growing order backlog for FY11F. Guidance is for sales to double by FY12F from FY10 levels.

Accelerating prospects

① Confident of achieving new order targets

Samsung Engineering (SSE) management has robust targets for FY11-12F revenue, new orders and backlogs. Its targets call for revenue and order backlogs to double by FY12F from FY10. Gulf hydrocarbon plant orders continue to come SSE's way, thanks to its good on-time plant completion record since 2005, while domestic plant orders are rising off the highest technology plant capex since 2005-06.

② Engineering capacity set for next EPC boom

Engineering staff numbers have increased by 330% since 2005, but sales per employee are up only 42% over the same period. As a result of economies of scale, the SG&A cost ratio peaked in FY07 and has stabilised below 10%. With its ample staff, SSE looks set to benefit from the next plant EPC boom, we believe.

③ M&A worries over-done

Concern has persisted over two key issues that we addressed in our 11 May, 2010 report, *Company visit: recent concerns exaggerated*. On market interest in the possibility of M&A regarding Samsung C&T, SSE management has strongly denied any merger plans. On currency, we estimate the euro would have to depreciate sharply for European EPC majors to outcompete Korean players on price alone.

④ Price target of W250,000

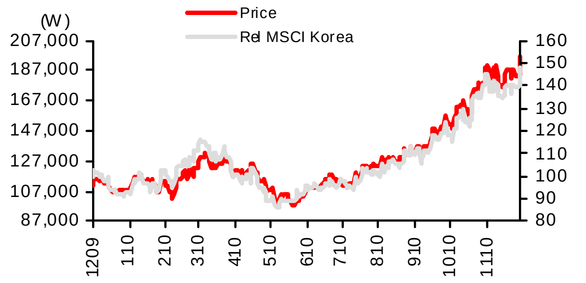
We recently raised our target EV/backlog multiple to the mid-point of the stock's five-year average, on SSE's better prospects for backlog growth and growing cash assets. Our forecast for FY12F calls for 30%-plus EPS growth. We find the stock is trading at only 15x FY11F earnings and 11x FY12F earnings – less than a third of its all-time high P/E valuation (FY07). Meanwhile, its cash pile is mounting thanks to project advances and ROE is well above 30%.

Key financials & valuations

31 Dec (Wbn)	FY09	FY10F	FY11F	FY12F
Revenue	4,035	5,107	8,471	10,772
Reported net profit	247	320	512	702
Normalised net profit	247	320	512	702
Normalised EPS (W)	6,179	8,007	12,799	17,555
Norm. EPS growth (%)	23.0	29.6	59.9	37.2
Norm. P/E (x)	31.9	24.6	15.4	11.2
EV/EBITDA (x)	19.6	14.3	7.9	5.4
Price/book (x)	10.1	7.2	4.9	3.4
Dividend yield (%)	1.0	1.2	1.9	2.5
ROE (%)	36.9	34.2	37.8	35.8
Net debt/equity (%)	net cash	net cash	net cash	net cash
Earnings revisions				
Previous norm. net profit		320	512	702
Change from previous (%)		-	-	-
Previous norm. EPS (W)		8,007	12,799	17,555

Source: Company, Nomura estimates

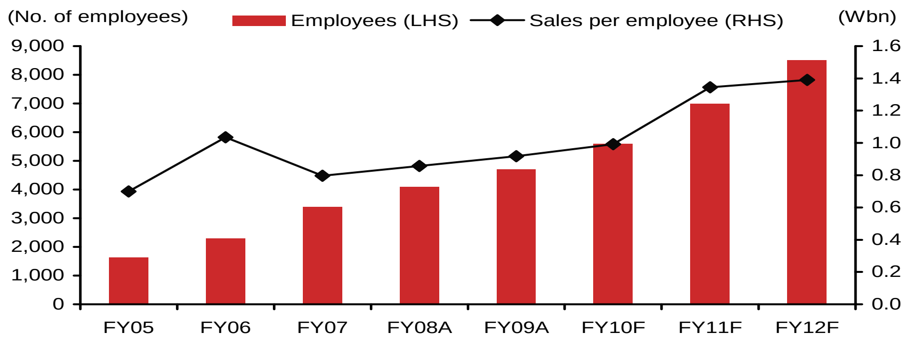
Share price relative to MSCI Korea



	1m	3m	6m
Absolute (W)	4.2	48.7	82.4
Absolute (US$)	1.3	52.8	95.8
Relative to Index	1.7	39.7	69.1
Market cap (US$mn)			6,849
Estimated free float (%)			81.8
52-week range (W)			197,000/97,900
3-mth avg daily turnover (US$mn)			25.20
Stock borrowability			Easy
Major shareholders (%)			
Cheil Industries			13.1
Samsung SDI			5.1

Source: Company, Nomura estimates

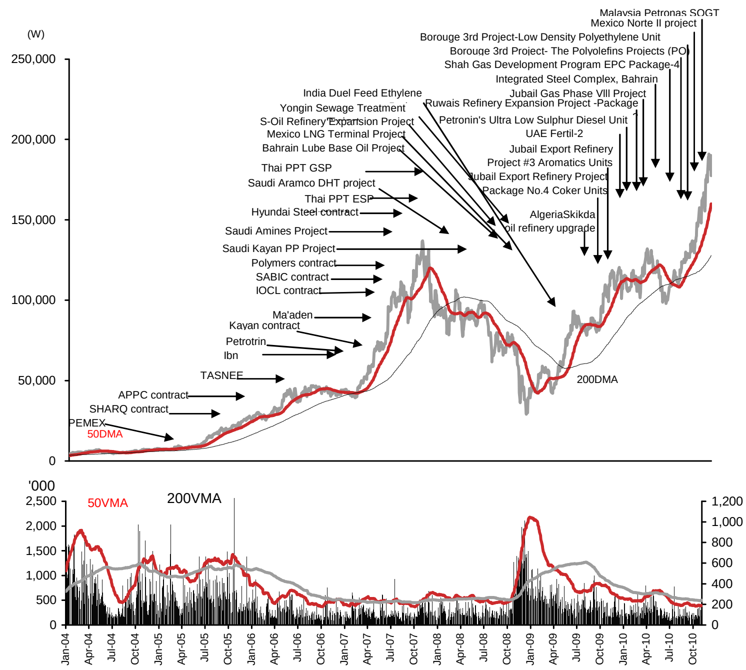
Exhibit 187. SSE: employee numbers and per employee sales



Source: Company data, Nomura research

Exhibit 188. SSE: share price performance vs contract announcements

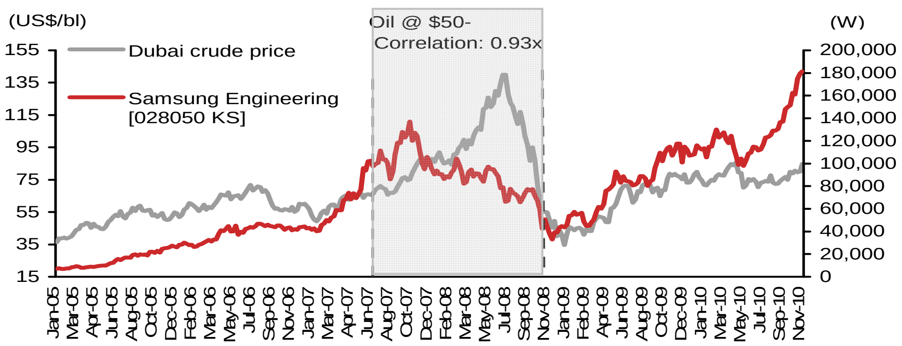
Correlation between project awards and share price in the long run



Source: Bloomberg, Nomura research

Exhibit 189. Oil price vs SSE share price

SSE shares' correlation with oil price in 2009-10 a relatively high 0.85x



Source: Bloomberg, Nomura research

Valuation methodology and risks

Key risks: lower project pricing and a sliding oil price

Our PT of W250,000 assumes a 0.32x target EV/backlog multiple. In terms of downside risks to our price target, we note: 1) possible margin deterioration from a decline in project pricing for the Middle East construction projects; and 2) oil price declines, which could force GCC clients to cut back on spending plans and delay projects in the next few years.

Financial statements

Income statement (Wbn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Revenue	3,215	4,035	5,107	8,471	10,772
Cost of goods sold	(2,751)	(3,419)	(4,234)	(7,075)	(8,951)
Gross profit	**464**	**617**	**873**	**1,395**	**1,821**
SG&A	(285)	(292)	(449)	(703)	(883)
Employee share expense					
Operating profit	**179**	**325**	**423**	**692**	**938**
EBITDA	**199**	**340**	**443**	**713**	**958**
Depreciation	(20)	(14)	(19)	(20)	(20)
Amortisation	-	-	-	-	-
EBIT	**179**	**325**	**423**	**692**	**938**
Net interest expense	36	31	60	80	95
Associates & JCEs					
Other income	52	(21)	(59)	(66)	(64)
Earnings before tax	**267**	**335**	**424**	**706**	**969**
Income tax	(66)	(88)	(104)	(194)	(266)
Net profit after tax	**201**	**247**	**320**	**512**	**702**
Minority interests					
Other items					
Preferred dividends					
Normalised NPAT	**201**	**247**	**320**	**512**	**702**
Extraordinary items	-	-	-	-	-
Reported NPAT	**201**	**247**	**320**	**512**	**702**
Dividends	(46)	(57)	(68)	(108)	(139)
Transfer to reserves	**154**	**190**	**252**	**404**	**563**
Valuation and ratio analysis					
FD normalised P/E (x)	39.2	31.9	24.6	15.4	11.2
FD normalised P/E at price target (x)	49.8	40.5	31.2	19.5	14.2
Reported P/E (x)	39.2	31.9	24.6	15.4	11.2
Dividend yield (%)	0.8	1.0	1.2	1.9	2.5
Price/cashflow (x)	74.3	8.5	11.9	7.9	9.4
Price/book (x)	14.0	10.1	7.2	4.9	3.4
EV/EBITDA (x)	37.0	19.6	14.3	7.9	5.4
EV/EBIT (x)	41.2	20.5	15.0	8.1	5.5
Gross margin (%)	14.4	15.3	17.1	16.5	16.9
EBITDA margin (%)	6.2	8.4	8.7	8.4	8.9
EBIT margin (%)	5.6	8.1	8.3	8.2	8.7
Net margin (%)	6.2	6.1	6.3	6.0	6.5
Effective tax rate (%)	24.8	26.2	24.5	27.5	27.5
Dividend payout (%)	23.1	23.0	21.3	21.1	19.8
Capex to sales (%)	1.0	2.9	5.0	1.5	1.4
Capex to depreciation (x)	1.6	8.3	13.2	6.2	7.6
ROE (%)	37.4	36.9	34.2	37.8	35.8
ROA (pretax %)	18.6	27.1	29.1	37.6	40.7
Growth (%)					
Revenue	41.7	25.5	26.6	65.9	27.2
EBITDA	24.6	70.7	30.3	61.0	34.4
EBIT	20.4	81.8	30.1	63.6	35.4
Normalised EPS	28.9	23.0	29.6	59.9	37.2
Normalised FDEPS	28.9	23.0	29.6	59.9	37.2
Per share					
Reported EPS (W)	5,023	6,179	8,007	12,799	17,555
Norm EPS (W)	5,023	6,179	8,007	12,799	17,555
Fully diluted norm EPS (W)	5,023	6,179	8,007	12,799	17,555
Book value per share (W)	14,045	19,417	27,423	40,222	57,777
DPS (W)	1,500	2,000	2,400	3,800	4,900

Source: Nomura estimates

P/E at only a third of 2007 peak on improving outlook for new orders and earnings

Cashflow (Wbn)					
Year-end 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
EBITDA	199	340	443	713	958
Change in working capital	(93)	583	217	282	(123)
Other operating cashflow					
Cashflow from operations	**106**	**922**	**660**	**995**	**835**
Capital expenditure	(33)	(118)	(255)	(127)	(155)
Free cashflow	**74**	**805**	**405**	**868**	**680**
Reduction in investments	(51)	5	-	-	-
Net acquisitions	43	-	-	-	-
Reduction in other LT assets	6	(3)	13	-	-
Addition in other LT liabilities	18	8	9	27	18
Adjustments					
Cashflow after investing acts	**90**	**816**	**426**	**895**	**698**
Cash dividends	(32)	(46)	(57)	(68)	(108)
Equity issue					
Debt issue	-	-	-	-	-
Convertible debt issue					
Others	(165)	(64)	(46)	(112)	(127)
Cashflow from financial acts	**(197)**	**(111)**	**(103)**	**(180)**	**(235)**
Net cashflow	**(107)**	**705**	**323**	**715**	**463**
Beginning cash	620	512	1,218	1,541	2,256
Ending cash	512	1,218	1,541	2,256	2,718
Ending net debt	(512)	(1,218)	(1,541)	(2,256)	(2,718)

Source: Nomura estimates

Balance sheet (Wbn)					
As at 31 Dec	**FY08**	**FY09**	**FY10F**	**FY11F**	**FY12F**
Cash & equivalents	512	1,218	1,541	2,256	2,718
Marketable securities	-	-	-	-	-
Accounts receivable	610	766	969	1,608	2,045
Inventories	-	-	13	13	13
Other current assets	174	(15)	(15)	(429)	(408)
Total current assets	**1,296**	**1,968**	**2,508**	**3,448**	**4,368**
LT investments	186	181	181	181	181
Fixed assets	183	286	521	628	762
Goodwill					
Other intangible assets					
Other LT assets	15	18	5	5	5
Total assets	**1,680**	**2,452**	**3,215**	**4,261**	**5,316**
Short-term debt	-	-	-	-	-
Accounts payable	473	610	756	1,263	1,598
Other current liabilities	541	954	1,242	1,242	1,242
Total current liabilities	**1,015**	**1,564**	**1,998**	**2,505**	**2,840**
Long-term debt	-	-	-	-	-
Convertible debt					
Other LT liabilities	103	112	120	147	165
Total liabilities	**1,118**	**1,676**	**2,118**	**2,652**	**3,005**
Minority interest					
Preferred stock					
Common stock	200	200	200	200	200
Retained earnings	447	648	969	1,480	2,183
Proposed dividends					
Other equity and reserves	(85)	(72)	(72)	(72)	(72)
Total shareholders' equity	**562**	**777**	**1,097**	**1,609**	**2,311**
Total equity & liabilities	**1,680**	**2,452**	**3,215**	**4,261**	**5,316**
Liquidity (x)					
Current ratio	1.28	1.26	1.26	1.38	1.54
Interest cover	na	na	na	na	na
Leverage					
Net debt/EBITDA (x)	net cash	net cash	net cash	net cash	net cash
Net debt/equity (%)	net cash	net cash	net cash	net cash	net cash
Activity (days)					
Days receivable	56.1	62.2	62.0	55.5	62.0
Days inventory	-	-	0.6	0.7	0.5
Days payable	53.8	57.9	58.9	52.1	58.5
Cash cycle	2.3	4.4	3.7	4.1	4.1

Source: Nomura estimates

Cash piling up on advances from fast-growing Gulf project awards

Valuation and risks

Valuation and risks

Company	Valuation basis	Investment risk
Amore Pacific	Our PT of W1,050,000 is based on a P/E multiple of 19.6x using 12-month-forward EPS shifted earnings base of June 2011.	Woongjin Coway's aggressive expansion in the domestic D2D channel is a downside risk, although we see only a slight probability of this happening.
Busan Bank	Our 12-month price target of W14,000 is based on the Gordon Growth Model (target P/BV = (sustainable ROE – long-term growth)/(costs of equity – long-term growth), assuming a cost of equity of 12.3% and a sustainable ROE of 12.0% and a long-term growth rate of 4.3%. Based on our FY10F estimates, this implies a target P/E and P/BV of 7.3x and 0.9x.	1) Unexpected bankruptcy of large companies could negatively impact our assumptions or could see our W14,000 price target prove to be quite conservative. 2) Overpayment for M&A could negatively impact our price target. 3) Further deterioration of the domestic economy could also have a negative impact on our price target. 4) Stability or NIM expansion would have a positive impact, in our view.
Cheil Industries	Our PT of W93,000 is based on the sum-of-the parts (SOTP) valuation.	Upside risks to our PT include: 1) TV PF approval from Samsung Electronics (SEC); and 2) visible revenue from LED LGP (1% of EM sales) and semiconductor materials. Downside risks include: 1) macro concerns weakening petrochemical pricing, and 2) slower-than-expected domestic consumption recovery, which could negatively impact the apparel division.
CJ Internet	Our price target of W20,000 is based on 5.0x FY10F EBITDA, at a 30% discount to its historical average of one-year forward EV/EBITDA multiple, plus FY10F net cash balance on lowered OP growth of 16.2% in 2010 vs FY07 and FY08 average OP growth of 39.8%.	Downside risks include: 1) further regulatory issues with the government, which could exert pressure on web board game revenue and 2) the potential risk of overpricing related to its M&A strategies.
CJ O Shopping	Our PT W320,000 is based on the SOTP valuation multiple and an EV/EBITDA multiple of 5x for SO (a 20% discount to global peers vs previous multiple of 4x, which offered a 35% discount to global peers), which is at the low-end of the expected HCN IPO price band (4.8-5.7x FY11F EV/EBITDA).	Any new regulatory change other than the 6th TV home shopping channel and new general service line is a downside risk. Stronger recovery in the insurance sales is an upside risk.
Daegu Bank	Our 12-month price target of W20,000, which is based on a Gordon Growth model (target P/B = (sustainable ROE – long-term growth)/(costs of equity-long-term growth), assuming a cost of equity of 12.1% and sustainable ROE of 13.1% and long-term growth of 4.3%. Based on our FY10F estimates, this implies a target P/E and P/BV of 7.4x and 1.1x, respectively.	1) Following the introduction of new benchmark rate mortgage loans, we cannot rule out the possibility of further regulatory changes on loan pricing. This could result in downward adjustment to loan yield assumptions. 2) Unexpected bankruptcy cases of large corporates/conglomerates could lead to deterioration in the earnings of Korean banks/FHCs by increasing credit costs. 3) Further deterioration of the domestic economy could have a negative impact on our assumptions and price target.
Daelim Industrial	Given DLI's fast recovery from the depths of its troubles related to PF liabilities and unsold housing inventory in FY08-09, we think a higher target multiple, at the median of DLI's FY05-10 (0.22x) EV/backlog range, is warranted, which yields a new price target of W120,000 (vs previous W100,000).	1) Oil price trends, which could determine GCC project spending; 2) a potential decline or recovery in the sales of new apartments in the domestic market, and 3) the health of Korea's banks and financial markets, which can influence DLI's and its affiliates' ability to roll-over debt and PF liabilities.
Daewoo E&C	Out target price is W8,500 on our enterprise value/backlog (EV/backlog) valuation methodology for E&C companies. We target DWEC's EV/backlog multiple (0.16x) at the second quartile of the 2005-11F EV/backlog band.	Upside risks centre on a possible fast reduction in unsold apartments, overseas margin expansion, and smoother-than-expected non-core asset sales. Downside risks focus on: 1) margin deterioration overseas and in domestic housing and 2) slower-than-expected asset sales and hence persistent balance sheet deterioration.
Daum Corp.	Our DCF-driven PT of W98,000 applies a terminal growth rate of 3.5% from FY15F and 10.9% WACC.	The key risks to our view include slower-than-expected top-line growth and further downside risk to Overture's PPC in 2011F.
Dongkuk Steel	Our PT of W33,000 is based on FY10F P/BV of 0.8x, which represents the mid-cycle multiple.	For DKS, the direction of the shipbuilding cycle could be a risk factor.
GS Eng & Construction	Our price target of W120,000 is derived from the second quintile (0.185x) of GSEC's five-year EV/backlog range (valuation methodology unchanged).	1) on the domestic front, the key risk is a persistent drop in take-up for new apartments; and 2) oil price falls which could force GCC (Gulf Cooperation Council: Saudi Arabia, Kuwait, United Arab Emirates, Oman, Qatar and Bahrain) clients to cut spending plans for the next few years.
GS Holdings	Our PT of W68,000 is based on 1.4x FY11F P/BV, which is the peak-cycle average of FY04-09.	Risks to our estimates for potential net profit and share price target may be associated with accounting and tax issues. GSH may be obligated to pay higher taxes than our assumptions, in which case EPS would be lower. Also, the structure of listing (new share issuance, stake sell-off, etc) could provide upside and downside risks to our figures.
GS Home Shopping	Our PT W154,000 is based on 8.8x P/E (5-year historical average) applied to 12-month rolling EPS of W17,504.	GSHS's JV with a solid partner overseas, potential benefits from restructuring and cost cutting, and a higher-than-expected dividend are upside risks. Ineffective use of available cash through investment in non-core businesses would be a downside risk.
Halla Climate Control	Our price target of W22,800 is based on 11.0x (global auto parts peer average) FY11F EPS.	Risks to our forecasts are significant appreciation/depreciation of the won against the Euro/US dollar (both upside/downside risks).

Company	Valuation basis	Investment risk
Hana Financial Group	Our PT of W39,000 is based on our Gordon Growth model (target P/BV = (sustainable ROE – long-term growth)/(costs of equity-long-term growth), assuming a cost of equity of 11.3%, sustainable ROE of 9.8%, and long-term growth rate of 4.3%.	1) If the global economy enters a double-dip recession, it would have a negative impact on the Korean economy. Considering that the Korean economy is highly dependent on exports, deterioration in global demand could result in further job losses and bankruptcies of SME exporters. 2) Unexpected bankruptcy of large companies/conglomerates could lead to deterioration in the earnings of Korean banks/FHCs as such events could increase credit costs. 3) In the event of deregulation on financial leverages at Korean bank-FHCs, capital constrains would be lifted, expanding flexibilities of further M&A. 4) Greater-than-expected loan growth should have positive impact on our earnings estimates and price targets.3
Hanjin Shipping	Our target price is based on a sum-of-the-parts methodology: we value the shipping business using the midpoint between mid and trough P/B multiples for container stocks (0.9x) and apply 1.5x multiple to its port business.	Key company upside risk include better-than-expected container earnings recovery, downside risk include sharper than expected decline in container freight rates.
Hankook Tire	Our PT of W34,000 is based on 10.5x (the average mid-cycle multiple over the past five years) our FY11F EPS estimate.	Downside risks include further demand slowdown in Europe and the US. Upside risk is lower-than-forecast raw material prices.
Hanwha Chemical	Our price target of W40,000 is based on a sum-of-the parts (SOTP) valuation model, which incorporates investment assets.	Downside risks may come from; 1) petrochemical price weaknesses; 2) execution risks of new businesses; and 3) acquisition or investment of value destructive business.
Honam Petrochemical	Our price target is based on the sum-of-the parts (SOTP) valuation model, which incorporates investment assets.	Downside risks may come from; 1) petrochemical price weaknesses; 2) HPC buying assets at unattractive prices and 3) input cost volatility may cause unexpected margin squeeze. As some lost capacities are restarting (eg, Formosa Petrochemical's No.1 700,000 tpa naphtha cracker), we may see supply loosening for ethylene. This may dampen the price outlook of polymer in the near term.
Hynix	Our price target is based on 2011F EPS of W4,164 and a target multiple of 10x with a 20% discount to account for the tax deduction that Hynix is presently, though temporarily, enjoying.	The share price may not move ahead of DRAM turns as it has in the past and the DRAM market may simply be weaker than we foresee.
Hyundai Department Store	Our revised PT of W130,000 is based on P/E multiple of 9.6x to our EPS base of W13,109.	Any delay in the new store opening is a downside risk to our earnings forecast. The acquisition of more stakes in Hanmoo Shopping (HS, a 46%-owned subsidiary, unlisted) could be either downside or upside depending on the acquisition price.
Hyundai Development	We target only the average (0.185x) of HDC's five-year EV/backlog range, yielding a price target of W41,000.	1) effects of housing market regulation for the Seoul region, which could affect take-up rates for HDC's mammoth Suwon Gwonseon own-project; 2) continued tight home lending criteria at Korean banks; and 3) uncertainty over negotiations between Seoul and Gyeonggido province over the fast rail system (consortium leader: HDC) could hit glitches over the next six to 12 months.
Hyundai E&C	HDEC's target EV/backlog multiple is 0.18x, only at the average multiple for HDEC's five-year EV/backlog bands, which we believe reflects the company's rapid backlog and new order growth.	1) oil price falls, which could force Gulf clients to cut back spending plans; 2) a potential drop in take-up for new apartments on the domestic front; and 3) possible delays in HDEC's plans for M&A and pre-M&A share disposals by creditor banks (HDEC's de facto owners' group).
Hyundai Home Shopping	Our PT of W143,000 is based on SOTP valuation, assuming 11x P/E on 12m forward EPS, the same multiple we apply for CJOS, to value the Korean home shopping operations.	We believe a successful subsidiary IPO, faster-than-expected profit generation from the newly established joint venture in China, and faster-than-expected recovery in insurance are upside risks to our view. Any negative regulatory change such as bundling of home shopping channels, stricter standards for advertisement of insurance products, etc. would be a downside risk.
Hyundai Merchant Marine	Our target price of W20,200 is based on mid-cycle P/B of 1.7x in 2010.	Hyundai Merchant Marine, company-specific risks include continued M&A risks (source: Lloydslist, March 19, 2007) of a takeover by Hyundai Heavy Industries (HHI) (009540 KS, REDUCE) and those shareholders friendly to HHI.
Hyundai Mobis	Our 12-month price target of W330,000 is based on 11x FY11F P/E, the average of global auto parts companies.	Downside risks to our forecasts include a slowdown in sales volume of HMC and Kia and sharp depreciation in the US dollar.
Hyundai Motor	Our PT of W210,000 is based on 9x FY11F P/E, a 3-year average discount of 30% to global peers.	Downside risks are steeper sales declines in Korea and slower market share gains in key regions.
Hyundai Steel	Our price target of W125,000 is based on an FY10F P/BV of 1.5x.	For HS, successful launch of blast furnace No.2 in January 2011 and quality approval for its automotive steel from the Korean players should be important.
IBK	Our 12-month price target of W20,000, based on a Gordon Growth Model (target P/B = (sustainable ROE – long-term growth)/(costs of equity-long-term growth). Our price target assumes a cost of equity of 12.2% and sustainable ROE of 13.3% and long-term growth rate of 4.3%. Based on our FY10 estimates, this implies a target P/E and P/B of 6.9x and 1.0x, respectively.	1) Sale of non-core investment securities (ie, KT&G and Shinsegae) could result in upward adjustment of earnings estimates and price target. 2) Unexpected bankruptcy cases of large corporations/conglomerates could lead to earnings deterioration for Korean banks/FHCs by increasing their credit costs. Indirectly, the failure of a large corporation could also roil the domestic economy. This could negatively impact the asset quality of retail loans and credit card receivables. 3) Further deterioration of the domestic economy could have a negative impact on our earnings assumptions and price target.
Jusung Engineering	Our PT of 23,000 is on 2011F BPS of W7,500 and target multiple of 3.0x.	If the company fails to prove its technological prowess to Chinese solar customers with existing orders or the government delays the introduction of more favourable policies on the BIPV market, upside on Jusung's solar operation could be capped.

Company	Valuation basis	Investment risk
KB Financial Group	Our 12-month price target at W70,000. Our PT is based on the Gordon Growth Model (target P/BV = (sustainable ROE – long-term growth)/(costs of equity-long-term growth), assuming a cost of equity of 10.3%, sustainable ROE of 12.2%, and long-term growth rate of 4.3%. Based on our FY11F estimates, this implies a target P/E and P/BV of 9.1x and 1.2x, respectively.	1) In the event of the global economy experiencing a double dip, KBFG could experience deterioration of asset quality. 2) Unforeseen dilutive M&A could have a negative impact on our price target and earnings estimates. On the flip side, in the event that KBFG pays a higher-than-expected dividend, our PT estimate would be positively impacted. 3) Delay in recovery of the property market or unfavourable regulatory change could have a negative impact on our earnings estimates and price target. 4) If interest rate hikes are further delayed, our NIM assumptions may be lowered, given that rate hikes are a key driver of NIM. 5) Unexpected bankruptcy cases of large corporations/conglomerates could lead to a deterioration in the earnings of Korean banks/FHCs.
KEB	Our 12-month price target of W17,500 is based on the Gordon Growth model (target P/BV = (sustainable ROE – long-term growth)/(costs of equity-long-term growth), assuming a cost of equity of 10.5% and a sustainable ROE of 12.7% and long-term growth rate of 4.3%. Based on our FY10F numbers, this implies a target P/E of 10.2x and a P/BV of 1.2x.	1) In case the global economy enters a double dip, KEB may experience deterioration of asset quality. 2) A delay in property market recovery, or unfavourable regulatory change, may have a negative impact on our earnings estimates and target price. 3) If the interest rate hike in Korea is further delayed, our NIM assumptions may be lowered, given that an interest rate hike is a key driver for NIM. 4) Unexpected bankruptcy cases of large corporations/conglomerates could lead to a deterioration in the earnings of Korean banks/FHCs.
KEPCO	Our price target of W43,000 is based on an EV/MW target (valuation methodology unchanged) of US$850,000, near the median of KEPCO's post-IPO 20-year EV/MW capacity range.	1) essentially all of KEPCO's earnings are denominated in Korean won, while almost all of its fuel costs are in US dollars, exposing earnings to the volatility of the forex and energy markets, and 2) changes in the government's electricity tariff policy and the macro backdrop can also have a large impact on KEPCO's earnings.
Kia Motors	Our 12-month PT of W60,000 is based on 9x FY11F P/E, which we derive using the 3-year average discount to global peers of 30%.	Downside risks include sharp US dollar depreciation and unsuccessful new model launches.
KOGAS	We derived our price target of W52,000 using the some-of-the-parts methodology.	Risk: 1) Government policies, 2) interest expenses and 3) execution risk. We currently assume the cost pass-on mechanism to be resumed in January 2011, which may be delayed again. 90% of KOGAS' debts are at fixed rate, but the other 10% is subject to interest rate changes. The contribution from its overseas E&P projects is contingent on smooth execution.
KOPEC	Our target price is W130,000, based on KEC's estimated DCF value. We think KEC's predictable long-term cash flows make DCF valuation an especially suitable methodology to value KEC's shares.	KEC's ambition to expand its business domain into the EPC market is viewed as a risk, due to: 1) market competition; and 2) macro factors such as oil price and currency trends, and geopolitics.
Korea Line Corp	Our price target of W63,000 is based on mid-cycle P/B of 1.2x in FY10F, which is equivalent to a target EV/fleet of 0.7x, as we maintain our positive view on the bulk shipping industry.	A reduction in fleet size, especially in the chartered fleet.
Korean Air	Our PT of W92,000 is based on a target P/B of 1.6x (mid-point of historical average and peak) applied to FY11F BVPS.	Risks include won volatility, oil prices, and increasing leverage.
KPS	Our price target is W88,000, based on KPS' DCF value. We think KPS's predictable long-term cash flows make DCF valuation a suitable methodology.	1)The opening up of the market is of little threat to the market leader, we believe, but could bring gradual market share erosion, and 2) with losses at Kepco persisting, concerns are growing over a potential decrease in maintenance contract prices. However, we note that maintenance costs are set based on the government's cost-compensation system, which guarantees compensation of fixed labour costs, regardless of Kepco's performance.
KT Corp	Our DCF-based price target of W58,000 follows from a WACC of 9.0% and a terminal growth rate of 0% after FY15.	Risks to our call include: 1) a steeper-than-expected decline in telephony revenue, and; 2) higher-than-expected marketing costs.
KT&G	Our price target of W65,000 is based on 10.5x P/E (historical average low) applied to FY11F EPS of W6,223.	Upside risks to our price target include a turnaround in market share after management's new marketing strategy and earlier-than-expected tax hike. Downside risks include continued market share decline despite a new marketing strategy.
LG Chem	Our price target of W500,000 is based on a sum-of-the-parts (SOTP) methodology, where we forecast the enterprise value of the petrochemicals and electronic material (EM) businesses by applying different target multiples.	Downside risks could stem from worse-than-expected petrochemicals and LCD cycles, which could dampen the company's FY10-11F earnings. Execution risk from car battery production could also de-rate the share price.
LG Display	We derive our price target of W36,000 by applying 1.1x FY10F P/BV to the median book value between 2010F and 2011F.	The concern about oversupply issue may arise if the industry landscape changes again.
LG Electronics Inc.	Our price target of W98,000 is based on the SOTP valuation. For each business segment we use the peer average EV/EBITDA.	Weaker end demand for handsets and TVs may hurt the company's earnings; a strong Korean won may deteriorate profitability.
LG H & H	Our price target is derived using FY11E earnings and a P/E multiple of 21x, which is the historical average for the past five years.	Effective and sizeable new M&A and better-than-expected earnings growth from The Face Shop are upside risks. Downside risks include lower-than-expected margin growth in the household goods segment due to continued price pressure from hypermarkets. Weaker-than-expected earnings growth in the beverage segment due to lower scale in non-carbonated new-beverage sales is a downside risk. Any delay in M&A would also lead to negative sentiment on the shares, although it would not impact our earnings estimates as we do not reflect any M&A in our forecasts.

Company	Valuation basis	Investment risk
LG Innotek	Our price target of W142,000 is based on 1.7x FY11F BVPS of W83,336 considering its ROE of 15% on average over at least the next three years.	Oversupply of LEDs and faster-than-expected ASP declines would cause negative investor sentiment, as it would lead to margin erosion.
LG Uplus	Our price target of W7,400 is based on DCF valuation, assuming 9.4% WACC and 0% terminal growth after FY15F.	Greater-than-expected negative impact from tariff discount/cannibalisation could pose downside risks for LG Uplus. On the flip side, potential take-up of the bundled product could provide an upside risk.
Lock & Lock	Given our stronger view on the company, we now give a 25x P/E (up from 21x) to 12M fwd EPS of W2,069, three months shifted further to March 2012F.	New capacity expansions to be announced by LnL in the future will be upside risks to our forecast. Also, faster emerging market growth and a bigger-than-expected benefit from the Taobao contract are upside risks. A faster-than-expected appreciation of the Korean won against other foreign currencies will provide a downside risk. Also, slower than-expected new city increase in China is a downside risk.
Lotte Shopping	Our PT of W570,000 is based on 13x P/E multiple (its historical high P/E under IFRS basis, unchanged) and a 12-month rolling FY11 F EPS of W42,492.	Better-than-expected performance of its overseas subsidiaries and further increases in discount store margins are upside risks. Faster-than-expected expansion overseas or ineffective M&A are downside risks.
Mando	Our PT of W177,000 is based on 11x FY11F P/E (global peer average).	Sharp appreciation of the won against the US dollar and a slowdown in global auto demand could present downside risks.
MegaStudy	Our PT of W182,000 is based on DCF valuation, where we apply a 9.7% WACC and a 3% terminal growth rate after FY29F.	Upside risks to our call would be faster than expected take-up of overseas business in China. Worse-than-expected EBSi impact is the downside risk to our call.
NC Soft	Our price target of W310,000 is derived by setting a target one-year forward P/E multiple at 24.5x, a 10% premium over the historical average of 22.2x over the past five years, on major launches of anticipated blockbuster games in 2H11.	A faster-than-expected decline of Aion, both in the domestic and overseas markets, remains the key risk factor, in our view.
Neowiz Games	We set our target one-year forward P/E at 12.8x, a 20% discount to that of the regional peer average of 15.9x (Asia ex-Japan) to derive our TP of W71,000. The 20% discount reflects company's relatively lower margin/ROE.	Key risks to our price target include a potential delay in new products and weaker-than-expected traffic for current franchise games.
NHN Corp.	We derived our W224,000 price target using a SOTP valuation methodology, based on the following assumptions: 1) W162,400 per share value for the Naver portal (a 9.8% WACC and a 5% terminal growth rate after FY11F); 2) W47,600 per share value for the Hangame portal (an 11% WACC and a 2% terminal growth rate after FY11F); 3) W6,800 per share value for its overseas gaming platforms (NHN Japan/Our game China), and; 4) W7,200 per share value of net cash.	Risks to our price target include slower-than-expected recovery in the economy and ad spending, and heightened regulatory risks for web-board games.
OCI Materials	Our PT of W150,000 is based on 4.2x FY11F BVPS of W34,840.	If 'bigger than our baseline' capacity additions for NF3 materialises, the recovery in NF3 selling prices may be short lived.
Orion	We use SOTP valuation methodology with earnings base to March FY12F.	The development of land in Yongsan and Dokok at market price after rise in plot-to build ratio in FY11F is an upside risk as the size of potential gain from the development is W315bn, which is also as big as 20% of market cap presently. Greater-than-expected short-term marketing cost increase is a downside risk. Faster than-expected raw material cost increase is also a downside risk.
POSCO	Our PT of W700,000 is based on FY11F P/BV of 1.5x, which represents the average peak-cycle multiple for 2003-09.	The main risks to our sector and stock view are be associated with the level of price changes that POSCO will be implementing in the coming months relative to raw material price adjustments. Top-down macro risks should provide upside/downside for the steel sector as a whole. For POSCO, excessive capital allocation to non-steel businesses may de-rate the share multiple, in our view.
Samsung Corporation	We derive our price target of W85,000, using an EV/backlog-based SOTP valuation methodology. Given an expected pick-up in new construction orders, we use the mid-point (0.37x) of SSCT's five-year historical EV/backlog range. On this basis, we value the construction business at W51,000/share. We leave intact our conservative SOTP assessment of investment securities assets, valuing them at only 70% of market value or W34,000/share.	1) Oil price trends, which could shape Gulf Co-operation Council (Saudi Arabia, Kuwait, United Arab Emirates, Oman, Qatar and Bahrain) project spending plans; and 2) potential changes in domestic take-up of new apartments.
Samsung Electronics	Our PT ofW1,050,000 is based on 1.6x our FY11F BPS forecast (excluding treasury shares) of W652,087, taking into consideration our FY11F ROE estimate of 16%.	Whether Samsung can successfully position itself in the smartphone space, and whether it can adopt an effective strategy for TV markets in emerging economies are still to be seen.
Samsung Engineering	Our PT of W250,000 assumes a 0.32x target EV/backlog multiple (previously 0.25x for FY10F).	1) possible margin deterioration from a decline in project pricing for the Middle East construction projects; and 2) oil price declines, which could force GCC clients to cut back on spending plans and delay projects in the next few years.
Samsung SDI	Price target of W152,000 is based on 1.4x FY10F P/BV target, which applies 20% discount to the historical high multiple of 1.8x since FY93.	Possible delays for the company's car battery business earnings contribution pose a downside risk.
Samsung Techwin	Price target of W130,000 is based on a SOTP valuation to reflect the changes in its business structure.	Margin pressure on its CCTV business; possible end-demand contraction in the semiconductor market.
SEMCO	Price target of W144,000 is based on EV/EBITDA SOTP to incorporate diverse earnings sources.	The won/US$ forex rate is the biggest earnings factor for SEMCO, meaning higher earnings volatility both to the upside and downside.

Company	Valuation basis	Investment risk
Seobu Truck Terminal	Our 12-month price target of W34,000 consists of DCF value for Yeonsu (39%) and book value for Shinjeong and Yongsan (61%).	Delay in the approval is a downside risk.
Seoul Semiconductor	Price target of W34,000 is based on 3.0 FY11F BVPS of W11,493 considering 19% average ROE for the next three years.	Oversupply of LEDs and faster-than-expected ASP declines would cause negative investor sentiment, as it would lead to margin erosion.
Shinhan Financial Group	Our 12-month price target of W60,000 is based on the Gordon Growth model (target P/B = (sustainable ROE – long-term growth)/(costs of equity-long-term growth), assuming a cost of equity of 10.9%, a sustainable ROE of 14.8% and a long-term growth rate of 4.3%. Based on our FY10 estimates, this implies a target P/E and P/B of 9.1x and 1.4x, respectively.	1) In case the global economy enters a double dip, SFG may experience deterioration of asset quality. 2) A delay in property market recovery or unfavourable regulatory change may have a negative impact on our earnings estimates and target price. 3) If interest rate hikes in Korea are further delayed, our NIM assumptions may be lowered, given that interest rate hikes are a key driver for NIM. 4) Unexpected bankruptcy cases of large corporations/conglomerates could lead to a deterioration in the earnings of Korean banks/FHCs.
Shinsegae	Our price target of W540,000 is derived by applying a FY12F P/E multiple of 12.6x to our 12m fwd EPS of W44,524.	Effective M&A, using the proceeds from its Samsung Life (SL) stake sale presents an upside risk. Bigger-than expected losses from its China operations poses a downside risk.
SK Broadband	Our price target of W4,600 is based on DCF valuation with a WACC of 8.5% (earlier: 8.32%) and a terminal growth rate of 1%.	KT's reinforced post-merger marketing strategy in the fixed line sector remains a short-term risk factor that could result in better-than-expected performance.
SK Energy	Our price target of W190,000 is based on an FY11F P/BV of 1.7x, which is the mid-to-peak cycle multiple over FY07-09.	Risks to our investment view include crude prices and volatile refining margins which may be dictated by the degree of consumption and trade flow of China. Material progress on the new businesses may provide upside risks to our target price.
SK Telecom	Our price target of W223,000 is based on SOTP methodology (unchanged), for which we use a DCF approach to value the parent company with 10.9% WACC and 0% terminal growth after FY15F.	Risks to our price target include less effective marketing cost regulations, coupled with the financial burden associated with turning around SK Broadband and SK Communications.
S-Oil	Our PT of W85,000 is based on FY11F P/BV of 2.4x, the peak-cycle multiple over FY07-09.	Risks include 1) volatile crude prices; 2) volatile refining margins; 3) uncertain aromatic margins; and 4) the uncertain economic outlook.
Ssangyong Motor	Our PT of W1,170 is based on 3.6x (median of the trough multiple over the past five years) FY10F OCFPS.	Upside risks include normalisation of business and changes in consumer demand toward SUVs
STX Pan Ocean	STX Pan Ocean Our price target of S$18.50 is based on mid-cycle P/B of 1.2x in FY10F, which is equivalent to a target EV/fleet of 1.3x	Aggressive fleet expansion plans and potential expansion into other non-core businesses
Technosemichem	Our price target of W37,000 is based on 2011F BPS of W18,300 and a target multiple of 2.0x.	Though we believe revenue growth will be sufficient to lead to continued OP growth despite the margin pressure, less-than-expected shipment, due to further utilisation cuts by Korean panel customers, might be a hurdle for OP growth in 2011F.
Woori Financial Group	Our 12-month PT of 18,000 is based on the Gordon Growth Model (target P/B = (sustainable ROE – long-term growth) / (costs of equity-long-term growth), assuming costs of equity of 11.9% and sustainable ROE of 11.9% and a long-term growth rate of 4.3%. Based on our FY10F estimates, this implies a target P/E and P/BV of 7.0x and 0.9x.	1) If the global economy enters a double dip, WFH may experience deterioration of asset quality. 2) Delay in the recovery of the property market or unfavourable regulatory changes may have a negative impact on our earnings estimates and price target. 3) If the interest rate hike is delayed further, our NIM assumptions may be lowered, given that interest rate hikes are a key driver for NIM. 4) Unexpected bankruptcy of large corporations/conglomerates could lead to deterioration in the earnings of Korean banks/FHCs.

Source: Company data, Nomura estimates

ANALYST CERTIFICATIONS

We, James Kim, Young Sun Kwon, Amy Lee, Gil Hyung Kim, Keith Nam, Cara Song, Stanley Yang, CW Chung, Cindy Park, Andrew Kam Wing Lee, Cecilia Chan, Justin Lee, Young Kwon Kim, Chris Chang, Sabine Park, Stacey Kim, Eric Minuh Cha, Greg Kang and Marcello Seongsoo Ahn, hereby certify (1) that the views expressed in this Research report accurately reflect our personal views about any or all of the subject securities or issuers referred to in this Research report, (2) no part of our compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this Research report and (3) no part of our compensation is tied to any specific investment banking transactions performed by Nomura Securities International, Inc., Nomura International plc or any other Nomura Group company.

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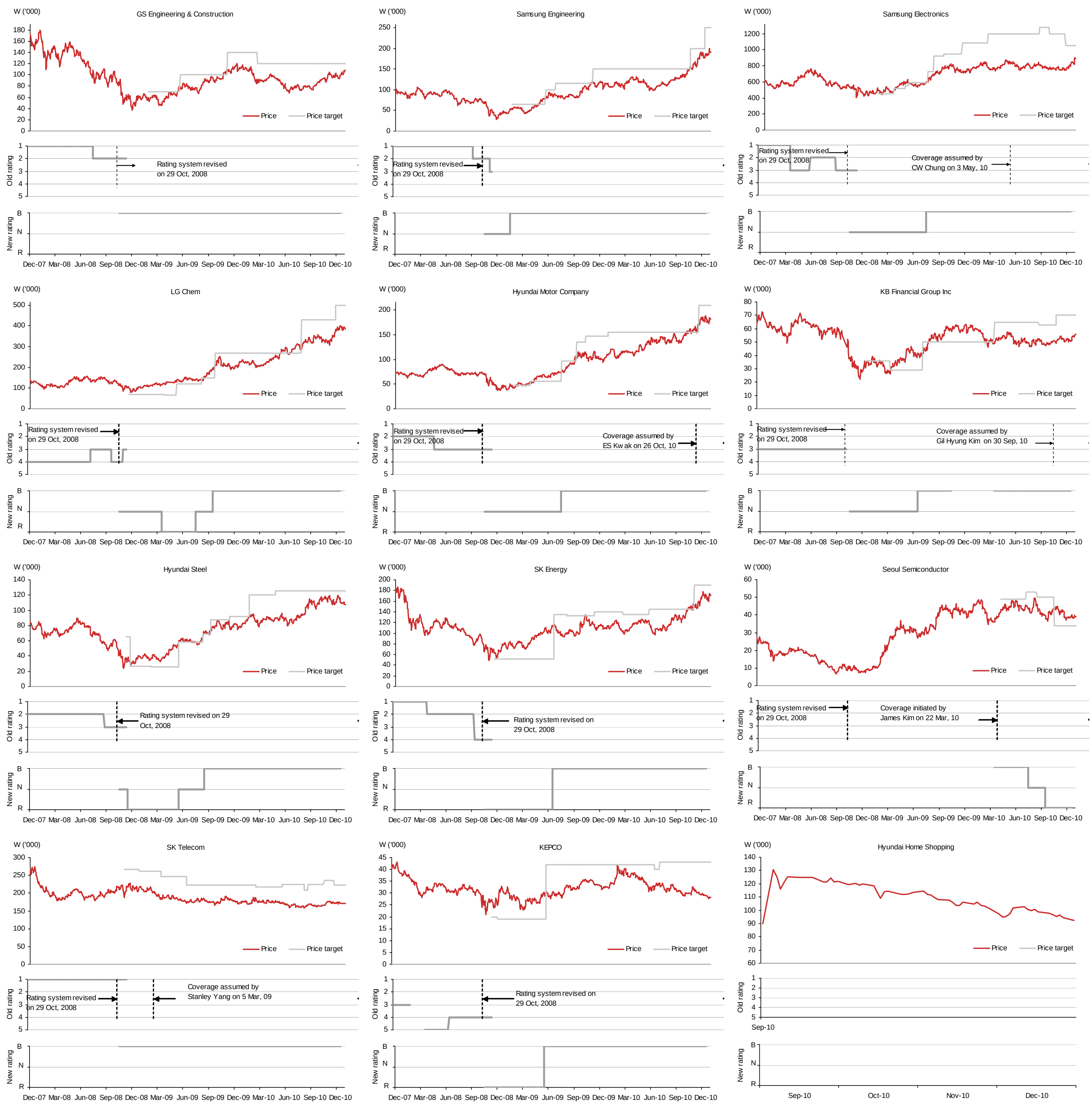
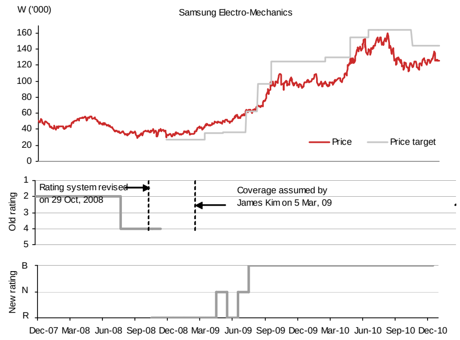
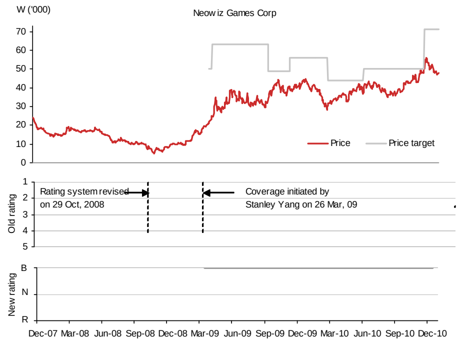
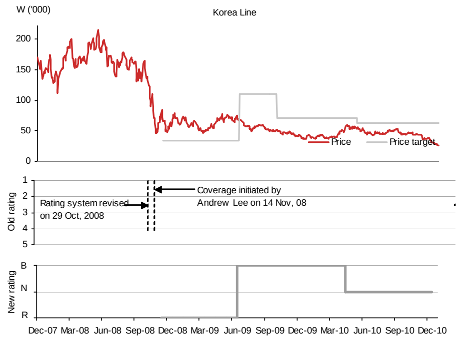
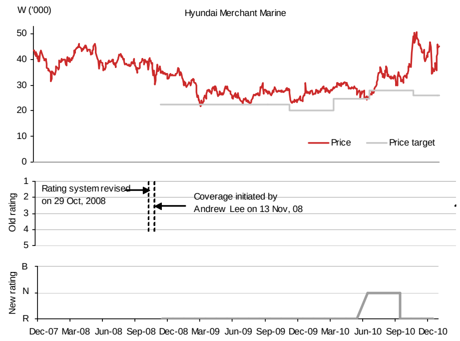
Three-year stock price and rating history

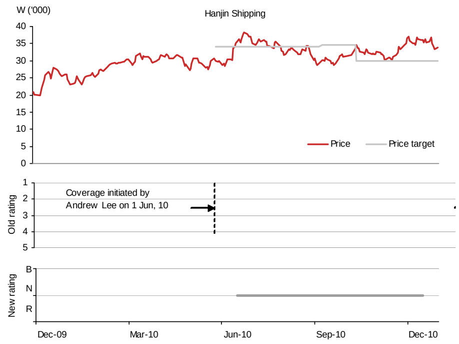












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Explanation of Nomura's equity research rating system in Europe, Middle East and Africa, US and Latin America for ratings published from 27 October 2008

The rating system is a relative system indicating expected performance against a specific benchmark identified for each individual stock. Analysts may also indicate absolute upside to price target defined as (fair value - current price)/current price, subject to limited management discretion. In most cases, the fair value will equal the analyst's assessment of the current intrinsic fair value of the stock using an appropriate valuation methodology such as discounted cash flow or multiple analysis, etc.

STOCKS

A rating of '**Buy'**, indicates that the analyst expects the stock to outperform the Benchmark over the next 12 months.
A rating of '**Neutral'**, indicates that the analyst expects the stock to perform in line with the Benchmark over the next 12 months.
A rating of '**Reduce'**, indicates that the analyst expects the stock to underperform the Benchmark over the next 12 months.
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Benchmarks are as follows: **United States/Europe**: Please see valuation methodologies for explanations of relevant benchmarks for stocks (accessible through the left hand side of the Nomura Disclosure web page: http://www.nomura.com/research);**Global Emerging Markets (ex-Asia):** MSCI Emerging Markets ex-Asia, unless otherwise stated in the valuation methodology.

SECTORS

A '**Bullish'** stance, indicates that the analyst expects the sector to outperform the Benchmark during the next 12 months.
A '**Neutral'** stance, indicates that the analyst expects the sector to perform in line with the Benchmark during the next 12 months.
A '**Bearish'** stance, indicates that the analyst expects the sector to underperform the Benchmark during the next 12 months.
Benchmarks are as follows: **United States**: S&P 500; **Europe**: Dow Jones STOXX 600; **Global Emerging Markets (ex-Asia)**: MSCI Emerging Markets ex-Asia.

Explanation of Nomura's equity research rating system for Asian companies under coverage ex Japan published from 30 October 2008 and in Japan from 6 January 2009

STOCKS

Stock recommendations are based on absolute valuation upside (downside), which is defined as (Price Target - Current Price) / Current Price, subject to limited management discretion. In most cases, the Price Target will equal the analyst's 12-month intrinsic valuation of the stock, based on an appropriate valuation methodology such as discounted cash flow, multiple analysis, etc.
A '**Buy'** recommendation indicates that potential upside is 15% or more.
A '**Neutral'** recommendation indicates that potential upside is less than 15% or downside is less than 5%.
A '**Reduce'** recommendation indicates that potential downside is 5% or more.
A rating of '**RS'** or '**Rating Suspended'** indicates that the rating and target price have been suspended temporarily to comply with applicable regulations and/or firm policies in certain circumstances including when Nomura is acting in an advisory capacity in a merger or strategic transaction involving the subject company.
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A '**Neutral'** rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a neutral absolute recommendation.
A '**Bearish'** rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a negative absolute recommendation.

Explanation of Nomura's equity research rating system in Japan published prior to 6 January 2009 (and ratings in Europe, Middle East and Africa, US and Latin America published prior to 27 October 2008)

STOCKS

A rating of '1' or '**Strong buy'**, indicates that the analyst expects the stock to outperform the Benchmark by 15% or more over the next six months.
A rating of '2' or '**Buy'**, indicates that the analyst expects the stock to outperform the Benchmark by 5% or more but less than 15% over the next six months.
A rating of '3' or '**Neutral'**, indicates that the analyst expects the stock to either outperform or underperform the Benchmark by less than 5% over the next six months.
A rating of '4' or '**Reduce'**, indicates that the analyst expects the stock to underperform the Benchmark by 5% or more but less than 15% over the next six months.
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Stocks labeled '**Not rated'** or shown as '**No rating'** are not in Nomura's regular research coverage. Nomura might not publish additional research reports concerning this company, and it undertakes no obligation to update the analysis, estimates, projections, conclusions or other information contained herein.

SECTORS

A '**Bullish'** stance, indicates that the analyst expects the sector to outperform the Benchmark during the next six months.
A '**Neutral'** stance, indicates that the analyst expects the sector to perform in line with the Benchmark during the next six months.
A '**Bearish'** stance, indicates that the analyst expects the sector to underperform the Benchmark during the next six months.
Benchmarks are as follows: **Japan**: TOPIX; **United States**: S&P 500, MSCI World Technology Hardware & Equipment; **Europe**, by sector - *Hardware/Semiconductors*: FTSE W Europe IT Hardware; *Telecoms*: FTSE W Europe Business Services; *Business Services*: FTSE W Europe; *Auto & Components*: FTSE W Europe Auto & Parts; *Communications equipment*: FTSE W Europe IT Hardware; **Ecology Focus**: Bloomberg World Energy Alternate Sources; **Global Emerging Markets**: MSCI Emerging Markets ex-Asia.

Explanation of Nomura's equity research rating system for Asian companies under coverage ex Japan published prior to 30 October 2008

STOCKS

Stock recommendations are based on absolute valuation upside (downside), which is defined as (Fair Value - Current Price)/Current Price, subject to limited management discretion. In most cases, the Fair Value will equal the analyst's assessment of the current intrinsic fair value of the stock using an appropriate valuation methodology such as Discounted Cash Flow or Multiple analysis etc. However, if the analyst doesn't think the market will revalue the stock over the specified time horizon due to a lack of events or catalysts, then the fair value may differ from the intrinsic fair value. In most cases, therefore, our recommendation is an assessment of the difference between current market price and our estimate of current intrinsic fair value. Recommendations are set with a 6-12 month horizon unless specified otherwise. Accordingly, within this horizon, price volatility may cause the actual upside or downside based on the prevailing market price to differ from the upside or downside implied by the recommendation.

A '**Strong buy'** recommendation indicates that upside is more than 20%.
A '**Buy'** recommendation indicates that upside is between 10% and 20%.
A '**Neutral'** recommendation indicates that upside or downside is less than 10%.
A '**Reduce'** recommendation indicates that downside is between 10% and 20%.
A '**Sell'** recommendation indicates that downside is more than 20%.

SECTORS

A '**Bullish'** rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a positive absolute recommendation.
A '**Neutral'** rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a neutral absolute recommendation.
A '**Bearish'** rating means most stocks in the sector have (or the weighted average recommendation of the stocks under coverage is) a negative absolute recommendation.

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