

Asahi Kasei

Japan/Chemicals

30 August 2019 – 11:40 pm GMT+1:00

UBS Research

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12-month rating	Buy
12-month price target	¥1,440.00
Prior	¥1,600
Price	¥961.20

Undervalued relative to competitors

- Results were weak, but entering a recovery phase
- OP estimated to decline 6% yoy to ¥198bn
- Separators expected to enter recovery phase
- Valuation: maintain Buy rating

We have lowered our earnings estimates based on analysis of results. Apr-Jun results came in below estimates, mainly for petrochemical related products and separators. We are still not positive on petrochemical prices, but we expect earnings to be relatively firm compared with rivals medium term since the scale of ethylene production is small. For separators, we think a recovery is very likely from Jul-Sep onward. Sustained high growth for Zoll (critical care equipment), for which estimates were revised upward after results, is also attractive. Meanwhile, the current PER premium relative to competitors is near the bottom over the past three years (Figure 2). We think excessive concern is priced in and we think investment appeal has conversely increased.

OP estimated to decline 6% yoy to ¥198bn

We have lowered our FY19 OP forecast from ¥215bn to ¥198bn. This is mainly due to changing our acrylonitrile (AN) spread assumption from \$810/tonne to \$690/tonne and forex from ¥110/\$ to ¥107/\$. We have also lowered estimates for auto related materials and separators (Figure 17). We think the full-year company plan of ¥205bn is very likely to be revised downward at the H1 results stage, mainly for specialty solutions and performance products. In FY20, we estimate profit declines for pharmaceuticals and AN, and we estimate that OP can be kept flat yoy at ¥198bn through separators and growth for Zoll (forex assumption ¥105/\$).

Separators expected to enter recovery phase

Sales volume for separators declined yoy in Apr-Jun due to continued effects from energy storage system (ESS) fires in South Korea as well as inventory adjustments by some customers. However, the inventory adjustments appear to have already ended. With regard to ESS demand, shipments have been rebounding since the South Korean government announced the results of its investigation in June. From Jul-Sep onward, downstream demand is expected to be strong from higher xEV related demand and a recovery in the ESS market (Page 5).

Valuation: maintain Buy rating

We have lowered our PT from ¥1,600 to ¥1,440 together with changes to our earnings estimates. This applies a PER of 12.4X (previously FY19E 12.5X) to FY20E EPS of ¥116 prior to goodwill amortization and is based on SOTP with reference to competitors. We think the shares look strongly undervalued both compared with the historical range and considering the premium relative to competitors.

Trading data and key metrics

52-wk range	¥1,744-909
Market cap.	¥1,334bn/US\$12.5bn
Shares o/s	1,387m (ORD)
Free float	95%
Avg. daily volume ('000)	3,173
Avg. daily value (m)	¥3,369.1
Common s/h equity (03/20E)	¥1,474bn
P/BV (03/20E)	0.9x
Net debt / EBITDA (03/20E)	0.7x
RIC	3407.T
BBG	3407 JP

Sources: UBS, Bloomberg

EPS (reported, basic)

	From	To	% ch	Cons.
03/20E	111.3	103.9	-7	105.0
03/21E	112.9	101.8	-10	106.2
03/22E	119.7	107.0	-11	112.6

Definitions of terms and abbreviations are available in the appendix section of this report, and more extensively on internet at www.ubs.com/glossary

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Asahi Kasei

Company Profile: Asahi Kasei

Asahi Kasei was founded in 1922 and initially produced textiles and chemical fertilisers based on ammonia. The company's businesses are highly diversified relative to other general chemical manufacturers in Japan and are currently categorised into seven sub-segments, chemicals, textiles, housing, construction materials, electronics, pharmaceuticals/medical, and critical care.

Statement of Risk

Our PT is based on PER. Major risks to general chemical manufacturers include: 1) deterioration in the supply and demand balance alongside lower demand for various products and growth in supply, as well as an accompanying decline in prices; 2) deterioration in spreads due to a sharp rise in raw material prices; 3) a decline in competitiveness due to forex volatility; 4) a retreat in de-

mand in the downstream automotive and electronics industries; 5) substitution of existing products as a result of the emergence of new technologies; 6) stiffer competition from new entrants; and 7) the emergence of unexpected side-effects for pharmaceuticals and agrochemicals.

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Highlights (¥bn)	03/17	03/18	03/19	03/20E	03/21E	03/22E	03/23E	03/24E
Revenues	1,883	2,042	2,170	2,227	2,271	2,329	2,393	2,465
Operating profit	159.2	198.5	209.6	198.0	198.0	208.0	219.0	234.0
Recurring profit	160.6	212.5	220.0	206.2	205.9	216.1	227.3	242.5
Net profit (reported)	115.0	170.3	147.5	145.1	142.1	149.4	157.3	168.0
EPS (reported, ¥)	82.3	121.9	105.6	103.9	101.8	107.0	112.5	120.2
Profitability/valuation	03/17	03/18	03/19	03/20E	03/21E	03/22E	03/23E	03/24E
EBIT margin %	8.5	9.7	9.7	8.9	8.7	8.9	9.2	9.5
ROIC (EBIT) %	12.7	15.9	15.7	13.5	12.9	13.0	13.2	13.5
EV/EBITDA x	5.3	6.3	6.8	4.8	4.6	4.4	4.2	4.0
PE (reported) x	10.8	10.7	13.1	9.2	9.4	9.0	8.5	8.0
Net dividend yield %	2.7	2.6	2.5	4.0	4.2	4.4	4.7	5.0

Source: Company accounts, Thomson Reuters, UBS estimates. Metrics marked as (UBS) have had analyst adjustments applied.

Valuations: based on an average share price that year, (E): based on a share price of ¥961.2 on 30 Aug 2019 15:58 JST

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Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

Market Return Assumption (MRA) is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium).

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Terms and Abbreviations

Term / Abbreviation	Description / Definition	Term / Abbreviation	Description / Definition
1H, 2H, etc. or 1H11, 2H11, etc.	First half, second half, etc. or first half 2011, second half 2011, etc.	1Q, 2Q, etc. or 1Q11, 2Q11, etc.	First quarter, second quarter, etc. or first quarter 2011, second quarter 2011, etc.
2011E, 2012E, etc.	2011 estimate, 2012 estimate, etc.	A	actual i.e. 2010A
ADR	American depositary receipt	ARPU	Average Revenue Per User
AUM	Assets under management = total value of own and third-party assets managed	Avg.	average
BCOM	Bloomberg Commodity Index	bn	Billion
bp or bps	Basis point or basis points (100 bps = 1 percentage point)	BVPS	Book value per share = shareholders' equity divided by the number of shares
CAGR	Compound annual growth rate	Cant Inc/Capita	Cantonal income per capita (Switzerland only)
Capex	Capital expenditures	CF	Cash flow
CFO	1) Cash flow from operations, 2) Chief financial officer	COGS	Cost of goods sold
COM	Common shares	Cons.	Consensus
Core Tier 1 Ratio	Tier 1 capital minus tier 1 hybrid securities	Cost/Inc Ratio (%)	Costs as a percentage of income
CPI	Consumer price index	CR	Combined ratio = ratio of claims and expenses as a percentage of premiums (for insurance companies)
CY	Calendar year	DCF	Discounted cash flow
DDM	Dividend discount model	Dividend Yield (%)	Dividend per share divided by price per share
DPS	Dividend per share	E	expected i.e. 2011E
EBIT	Earnings before interest and taxes	EBIT Margin (%)	EBIT divided by revenues
EBITDA	Earnings before interest, taxes, depreciation and amortization	EBITDA Margin (%)	EBITDA divided by revenues
EBITDA/Net Interest	EBITDA divided by net interest expense	EBITDAR	Earnings before interest, taxes, depreciation, amortization and rental expense
EFVR	Estimated fair value range	EIA	Energy Information Administration
EmV	Embedded value = net asset value + present value of forecasted future profits (for life insurers)	EPS	Earnings per share
Equity Ratio (%)	Shareholders' equity divided by total assets	EV	Enterprise value = market value of equity, preferred equity, outstanding net debt and minorities
FCF	Free cash flow = cash a company generates above outlays required to maintain/expand its asset base	FCF Yield (%)	Free cash flow divided by market capitalization
FFO	Funds from operations	FY	Fiscal year / financial year
GDP	Gross domestic product	Gross Margin (%)	Gross profit divided by revenues
H	half year	h/h	Half-year over half-year; half on half
hist av.	Historical average	Interbank Ratio	Interbank deposits due from banks divided by interbank deposits due to banks

Asahi Kasei

Term / Abbreviation	Description / Definition	Term / Abbreviation	Description / Definition
Interest Coverage	Ratio that expresses the number of times interest expenses are covered by earnings	Interest exp	Interest expense
ISIN	International securities identification number	K	One thousand
LLP/Net Int Inc (%)	Loan loss provisions divided by net interest income	LLR/Gross Loans (%)	Loan loss reserves divided by gross loans
LPR	Least Preferred: The stock is expected to both underperform the relevant benchmark and depreciate in absolute terms.	Market cap	Number of all shares of a company (at the end of the quarter) times closing price
m/m	Month-over-month; month on month	mn or m	Million
M and A	Merger and Acquisition	MP	Marketperform: The stocks expected performance is in line with the sector benchmark
MPR	Most Preferred: The stock is expected to both outperform the relevant benchmark and appreciate in absolute terms.	n.a.	Not available or not applicable
NAV	Net asset value	Net Debt	Short- and long-term interest-bearing debt minus cash and cash equivalents
Net DPS	Net dividends per share	NIM or Net Int Margin (%)	Net interest income divided by average interest-bearing assets
Net Margin (%)	Net income dividend by revenues	NV	Neutral View: The stock is expected to neither outperform nor underperform the relevant benchmark nor significantly appreciate or depreciate in absolute terms.
n.m. or NM	Not meaningful	NPL	Non-performing loans
OP	Outperform: The stocks is expected to outperform the sector benchmark	Op Margin (%)	Operating income divided by revenues
p.a.	Per annum (per year)	P/BV	Price to book value
P/E or PE	Price to earnings / Price Earnings Ratio	P/E Relative	P/E relative to the market
P/EmV	Price to embedded value	PEG Ratio	P/E ratio divided by earnings growth
PPI	Producer price index	Prim Bal/Cur Rev (%)	Primary balance divided by current revenue (total revenue minus capital revenue)
Profit Margin (%)	Net income divided by revenues	q/q or QQQ	Quarter-over-quarter; quarter on quarter
R and D	Research and development	ROA (%)	Return on assets
ROAE (%)	Return on average equity	ROCE (%)	Return on capital employed = EBIT divided by difference between total assets & current liabilities
ROE (%)	Return on equity	ROIC (%) or ROI	Return on invested capital
Shares o/s	Shares outstanding	Solvency Ratio (%)	Ratio of shareholders' equity to net premiums written (for insurance companies)
sotp or SOTP	Sum of the parts	Tax Burden Index	Swiss tax index; 100 = average tax burden of all cantons
tgt	Target	Tier 1 Ratio (%)	Tier 1 capital divided by risk-weighted assets; describes a bank's capital adequacy
tn	Trillion	UP	Underperform: The stock is expected to underperform the sector benchmark
Valor	Swiss company identifier	WACC	Weighted average cost of capital
WPIC	World Platinum Investment Council	CIO	UBS WM Chief Investment Office
x	multiple / multiplier	y/y or YOY	Year-over-year; year on year
yr	Year	YTD	Year-to-date

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