

Holding Companies (Overweight)

Focus: Securing an ownership stake in a holding company

Method of transition: Spin-off, then tender offer

Currently, several companies (e.g., Hankook Tire, Aekyung Petrochemical, Kolmar Korea) are pursuing transitions into holding companies. They are doing so to prepare for ownership succession, or to increase the ownership stake of their respective controlling shareholders. These companies are opting for the same conversion process: tendering offers after spinning off subsidiaries. This method of transition is the most popular among companies switching to a holding company structure, as it allows controlling shareholders to increase their stakes in both the holding company and its subsidiaries. LG, SK, CJ, and Nongshim Holdings used this process to complete their transitions into holding companies.

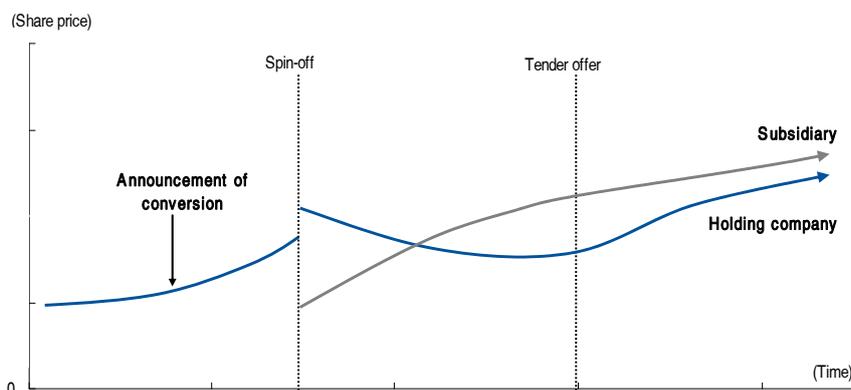
Securing a stable ownership stake (in the holding company) is key

When a company converts to a holding structure, securing a stable ownership stake in the holding company is the most important consideration for controlling shareholders. Controlling shareholders do not need to hold stakes in subsidiaries, as they can control subsidiaries through holding companies. As such, a controlling shareholder exchanges his or her stakes in the subsidiary for newly issued shares of the holding company, increasing his or her stake in the holding company, while maintaining control of the subsidiary through the holding company. Some major groups have adopted a cross-shareholding structure in which a controlling shareholder with stakes in flagship affiliates controls the entire group. If these groups opt to convert to a holding structure because of policy changes (e.g., a ban on cross-shareholding), their preferred method of conversion will likely follow the pattern outlined above.

Recommended holding company investment strategy

We believe investors can benefit when a company switches to a holding structure. We advise investors to invest in subsidiaries during the conversion process (announcement of conversion - spin-off - tender offer). However, when a holding company acquires a subsidiary's shares via a tender offer, we recommend investors buy the holding company's shares, as they have the potential to rise on their valuation merits (relative to asset value).

Share performances of a holding company and a subsidiary after conversion to a holding structure



Source: KDB Daewoo Securities Research

Analysts who prepared this report are registered as research analysts in Korea but not in any other jurisdiction, including the U.S.

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1. Method of transition: Spin-off, then tender offer

A spin-off, followed by a tender offer, is the preferred method for transitioning into a holding company

Currently, several companies (e.g., Hankook Tire, Aekyung Petrochemical, Kolmar Korea) are pursuing transitions into holding companies. They are doing so to prepare for ownership succession, or to increase the ownership stake of their respective controlling shareholders. These companies are opting for the same conversion process: tendering offers after spinning off subsidiaries. In other words, once a company is split into a holding company and a subsidiary, the holding company would acquire stakes in the subsidiary via a tender offer to meet regulatory qualifications (a 20% stake in listed subsidiaries and a 40% stake in non-listed subsidiaries). Then, shareholders would receive new shares of the holding company via a rights offering in return for their shares in the subsidiary.

This method of transition is the most popular among companies switching to a holding company structure, as it allows a controlling shareholder to increase his or her stakes in both the holding company and its subsidiaries. Acquiring a stake in an affiliate in the open market would require a substantial amount of funds, whereas a tender offer followed by a rights offering would enable a holding company to easily gain stakes in its subsidiaries without having to invest sizable funds. Simply put, controlling shareholders can assert their ownership in a holding company at little expense, and holding companies can meet the regulatory requirements for ownership in subsidiaries. LG, SK, CJ, and Nongshim Holdings used this process to complete their transitions into holding companies.

Table 1. Companies currently pushing to adopt holding structures

Holding company	Key subsidiary	Announcement date	Split ratio (holding company : subsidiary)	Relisting date
Kolmar Korea Holdings	Kolmar Korea	6/4/2012	0.325 : 0.675	10/19/2012
AK Holdings	Aekyung Petrochemical	4/24/2012	0.64 : 0.36	9/17/2012
Hankook Tire Worldwide	Hankook Tire	4/25/2012	0.19 : 0.81	10/4/2012
Samyang Holdings	Samyang Corp.	8/10/2012	0.57 : 0.43	12/5/2011

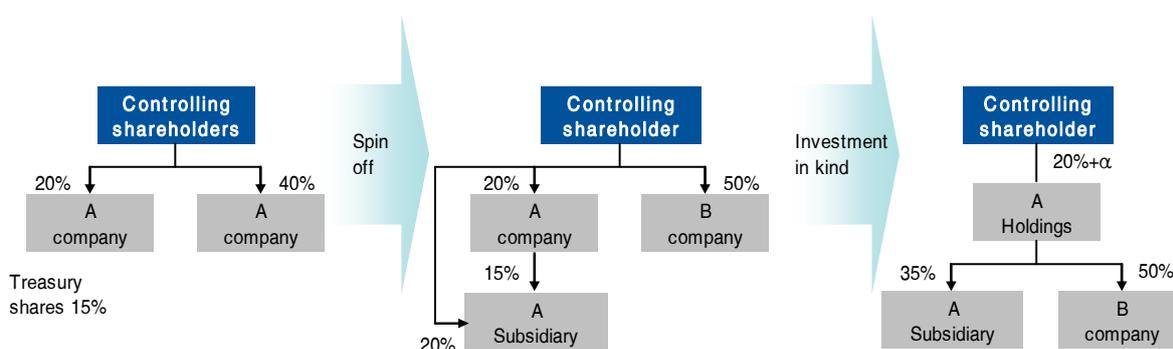
Source: KDB Daewoo Securities Research

Table 2. Types of holding structure conversions

Conversion type	Holdings	
Spin-off	Tender offer	SK, LG, GS, CJ, Amorepacific, Hanjin Heavy Industries & Construction, Nongshim, Daesang, HCN, Daewoong, Pyung Hwa, Neowiz Holdings
	Secondary offering	Daekyo, KPX, ISU, DPI, KEC Holdings
	Spin-off	Se Ah Holdings
Split-off	Nexon, Dongwha, Pulmuone, Korea Computer Holdings	

Source: KDB Daewoo Securities Research

Figure 1. Process of converting to a holding structure



Source: KDB Daewoo Securities Research

2. Securing a stable ownership stake (in the holding company) is key

Some major groups have adopted a cross-shareholding structure in which a controlling shareholder with stakes in flagship affiliates controls the entire group. If these groups opt to convert to a holding structure because of policy changes (e.g., a ban on cross-shareholding), their preferred method of conversion will likely follow the pattern outlined above.

When a company converts to a holding structure, securing a stable ownership stake in the holding company is the most important consideration for the controlling shareholder. Controlling shareholders do not need to hold stakes in subsidiaries, as they can control the subsidiaries through the holding company. As such, a controlling shareholder exchanges his or her stakes in the subsidiary for newly issued shares of the holding company, increasing his or her stake in the holding company, while maintaining control of the subsidiary through the holding company.

On the other hand, there is little incentive for minority shareholders to own stakes in holding companies from an investment or management perspective. Rather, minority shareholders prefer directly investing in operating subsidiaries, which explains why they seldom participate in tender offers related to holding company conversions. As a result, when a company adopts a holding structure, the increase in the controlling shareholder's stake in the holding company tends to be larger than the increase in the holding company's stake in its subsidiary.

Table 3. Changes in controlling shareholders' stakes before and after tender offers (% , %p)

Holding company	Controlling shareholder's stake before tender offer	Controlling shareholder's stake after tender offer	Increase
Woongjin Holdings	36.4	87.2	50.8
LGEI	33.8	78.3	44.5
Daesang Holdings	33.5	67.4	33.9
Hanjin Heavy Industries & Construction	16.9	50.1	33.2
Amorepacific	31.7	62.6	30.9
CJ	20.2	50.1	29.9
LGCI	12.7	41.6	28.9
Nongshim Holdings	36.4	61.3	24.9
Daewoong	55	76.9	21.9
JW Holdings	33.5	54.4	20.9
Neowiz	41.5	60.7	19.2
KEC Holdings	29.6	48	18.4
SK	15.7	29.6	13.9
DPI Holdings	33	45.5	12.5
KPX Holdings	48.5	56.7	8.2
Pyung Hwa Holdings	33.6	39.1	5.5

Source: KDB Daewoo Securities Research

3. Recommended holding company investment strategy

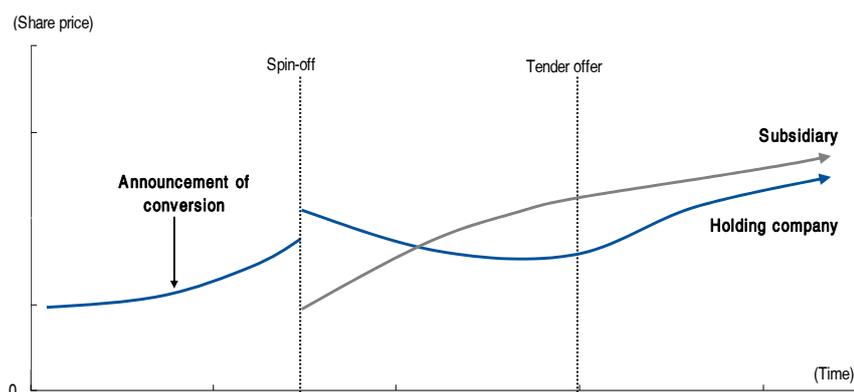
Pre-tender offer, invest in the subsidiary; Post-tender offer, invest in the holding company

We believe investors can benefit when a company switches to a holding structure. We advise investors to invest in subsidiaries during the conversion process (announcement of conversion - spin-off - tender offer). However, when the holding company acquires a subsidiary's shares via a tender offer, we recommend investors buy the holding company's shares, as they have the potential to rise on their valuation merits (relative to asset value).

It should be noted that the controlling shareholder is likely to attempt to increase the value of a subsidiary before making a tender offer, because higher share prices (for the subsidiary) should enable the shareholder to secure a larger stake in the holding company during the share swap. As for the holding company, once a share-swap ratio is set following a tender offer, uncertainties over new share issues should ease.

In this context, we believe investors should closely follow Hankook Tire, which was relisted on October 4th after being split into Hankook Tire Worldwide (holding company) and Hankook Tire (subsidiary).

Figure 2. Share performances of a holding company and a subsidiary after conversion to a holding structure



Source: KDB Daewoo Securities Research

Table 4. Amorepacific Group's conversion to a holding structure (W)

	Date	Amorepacific Group		Amorepacific	
		Share price	Performance	Share price	Performance
Announcement of conversion	3/15/2006	365,000	-	-	-
Suspension of share trading	5/25~6/29/2006	320,000	-12.3%	-	-
Spin-off and listing	6/29/2006	183,000	-	385,000	-
Announcement of tender offer and rights offering	10/9/2006	127,000	-30.6%	455,500	18.3%
Disclosure of issue price	11/14/2006	139,000	9.4%	509,000	11.7%
Peak of the holding company's share price	12/26/2006	171,000	23.0%	563,000	10.6%

Source: KDB Daewoo Securities Research

Table 5. SK Group's conversion to a holding structure (W)

	Date	SK Holdings		SK Energy	
		Share price	Performance	Share price	Performance
Announcement of conversion	4/11/07	93,000	-	-	-
Suspension of share trading	6/28~7/24/07	134,000	44.1%	-	-
Spin-off and listing	7/25/07	205,000	-	169,500	-
Announcement of tender offer and rights offering	9/17/07	182,500	-11.0%	157,000	-7.4%
Disclosure of issue price	9/21/07	178,000	-2.5%	151,000	-3.8%
Peak of the holding company's share price	11/24/07	285,500	60.4%	200,000	32.5%

Source: KDB Daewoo Securities Research

Table 6. Hankook Tire's conversion to holding company structure: Relisting after split off (Shares, Wbn, W)

	Hankook Tire (old)	Hankook Tire Worldwide	Hankook Tire (new)	Note
Authorized shares	250,000,000	250,000,000	250,000,000	
Outstanding shares	152,189,929	28,314,860	123,875,069	
Split ratio	1.00	0.19	0.81	Based on net assets
Market cap.	6,331	1,167	5,165	Market capitalization is split the day before trading is halted
Split ratio of market cap		0.18	0.82	Based on fair value of treasury stock
Base value		41,200	41,750	Split-off market cap/number of shares
Upper limit of opening price		82,400	83,500	200% of base price
Lower limit of opening price		20,600	20,900	50% of base price
Upper limit				Opening price up 15%
Lower limit				Opening price down 15%

Source: KDB Daewoo Securities Research

Table 7. Shares and stakes of controlling shareholders (Shares)

Name	Hankook Tire (old)		Hankook Tire Worldwide		Hankook Tire (new)	
	Shares	Stake	Shares	Stake	Shares	Stake
Yang-rae Cho	24,335,507	15.99%	4,527,546	15.99%	19,807,624	15.99%
Hyun-bum Cho	10,798,251	7.10%	2,010,355	7.10%	8,795,130	7.10%
Hyun-sik Cho	8,817,786	5.79%	1,639,430	5.79%	7,172,366	5.79%
Affiliated individuals	5,431,804	3.57%	1,010,841	3.57%	7,928,004	3.57%
ShinYang Development	1,443,157	0.95%	268,991	0.95%	1,176,813	0.95%
Subtotal	55,138,135	36.23%	10,258,474	36.23%	44,879,712	36.23%
Grand total	152,189,929	100.00%	28,314,860	100.00%	123,875,069	100.00%

Source: KDB Daewoo Securities Research

Table 8. Acquiring stakes in the subsidiary via a tender offer (shares, x)

Hankook Tire Worldwide's shares in Hankook Tire (1)	5,697,654
Total shares of Hankook Tire (2)	123,875,069
Hankook Tire Worldwide's stake in Hankook Tire (1)/(2)	4.6%
Requirements of a holding company (listed subsidiaries)	20.0%
Required stakes (3)	15.4%
Shares of tender offer (2) x (3)	19,077,360
Controlling shareholders' stakes (4)	28.9%
Shares exchangeable by controlling shareholders (2) x (4)	35,775,120

Source: KDB Daewoo Securities Research

Table 9. Change in controlling shareholders' stake before and after tender offer (shares)

Exchange ratio				
Hankook Tire Worldwide: W37,000; Hankook Tire: W60,000, Exchange ratio: 60,000/37,000 = 1.62				
	Before tender offer	New share issues	Total	After tender offer
1) In case of company chairman Yang-rae Cho's participation				
Yang-rae Cho	16.0%	32,120,471	36,648,017	42.5%
Hyun-bum Cho	7.1%	14,262,373	16,272,728	18.8%
Hyun-sik Cho	5.8%	11,630,865	13,270,295	15.4%
2) In case of company chairman Yang-rae Cho's non-participation				
Yang-rae Cho	16.0%	0	4,527,546	8.4%
Hyun-bum Cho	7.1%	14,262,373	16,272,728	30.0%
Hyun-sik Cho	5.8%	11,630,865	13,270,295	24.5%

Source: KDB Daewoo Securities Research

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