



July 15, 2009

Hyundai Heavy Industries

Shipbuilding

Reuters Code 009540.KS

Bloomberg Code 009540 KS

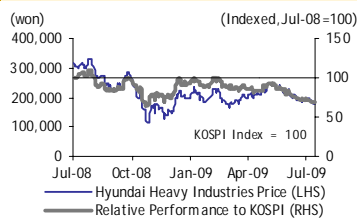
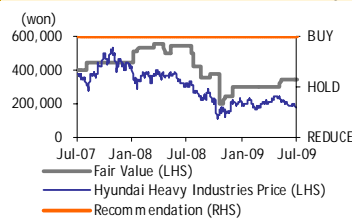
BUY

Price (Jul. 14) W179,500

Fair Value W260,000

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KOSPI :	1,385.56p
KOSDAQ :	476.25p
Market Cap. :	W13,642.0bn/ US\$11,966.7mn
Par Value :	W5,000
Outstanding Shares :	76.0mn
Free Floating Shares :	43.7mn (57.5%)
52-Week High/Low :	W333,000/ W115,500
60-Day Avg. Trading Volume :	472,723shrs
60-Day Avg. Trading T/O :	W101,777mn
Foreign Ownership :	16.69%
Major Shareholders :	MJ Jung 21.32%
	KCC 8.15%
Absolute Performance	3M -15.3%
	6M -16.1%
	12M -43.4%
Relative Performance to KOSPI	3M -18.0%
	6M -28.4%
	12M -36.3%

Share Price Performance**Fair Value & Recommendation History****Staying on top of the game**

2H09 order receipts to increase vs. 1H09, but the pace to slow Hyundai Heavy Industries' newbuilding orders amounted to US\$850mn in May, extending a steady monthly order intake trend. E&E (electric and electronic) system and offshore plant orders increased 16.2% YoY and 20.7% YoY, respectively, in the year to May, while the shipbuilding division booked nothing. The shipbuilding unit had an order backlog of 303 vessels, worth US\$20bn, which is equivalent to 34 months of work. Shipbuilding market conditions are expected to improve in 2H09 after a deep slump in 1H09. Still, on a YoY basis, sluggish market conditions should continue throughout the year.

World's No. 1 in shipbuilding, a reason to remain optimistic Hyundai Heavy Industries posted US\$2.71bn worth of new orders (-83.1% YoY) in the year to May across the divisions, a sharp decline from a year earlier. The target-to-current ratio also remained at a slow 12.8%. The shipbuilding division has not been too aggressive about winning new orders. First, the global shipbuilding market is still in its downturn with order volume contracting. Second, prices will fall further if Hyundai Heavy, the world's biggest shipbuilder, goes on the offensive. This is a good strategy for a short-term cash flow, but the company's future earnings value will decline and a price order in the global shipbuilding market, led by Korean companies, could collapse. All in all, the company is expected to remain cautious in 2H09 until the market regains stability.

Earnings growth momentum intact in 2Q09 The company is estimated to have achieved an operating profit of W456bn (-16.6% YoY) on sales of W5.446tr (+15.6% YoY) with a pre-tax profit of W681bn (-24.5% YoY) in 2Q09. Sales growth will likely slow amid delays in deliveries. Operating profit and pre-tax profit will also feel the squeeze from slowing sales growth.

BUY for a fair value of W260,000 We revise down Hyundai Heavy's fair value by 23.5% to W260,000 (operating value of W215,102 and non-operating value of W46,610) for the following reasons. First, investors will focus on the drought of new orders rather than the company's ability to stay on top of the game as the world's best and biggest shipbuilder. Second, we revise down 2009 full-year profit estimate. Third, we downgrade our target P/E (8.5x) for the shipbuilding sector.

Year to Dec.	Sales (W bn)	OP (W bn)	Pre-tax (W bn)	NP (W bn)	EPS (Won)	Growth (%)	PER (x)	EV/EBITDA (x)	PBR (x)	ROE (%)	Net Debt Ratio (%)	Div. Yield (%)
2007	15,533.0	1,750.7	2,394.4	1,736.1	22,843	143.5	13.7	9.5	4.3	35.4	(62.3)	2.4
2008	19,957.1	2,206.2	2,949.6	2,256.7	29,693	30.0	9.9	7.6	4.0	40.7	(44.2)	1.7
2009E	23,997.0	2,331.0	2,866.1	2,192.8	28,852	(2.8)	6.2	3.9	1.8	33.5	(29.6)	2.8
2010E	28,728.2	2,853.1	3,389.6	2,593.3	34,122	18.3	5.3	3.5	1.4	30.0	(14.4)	2.8
2011E	32,803.1	2,727.3	3,244.6	2,482.3	32,662	(4.3)	5.5	3.6	1.1	22.8	(9.4)	2.8

Order receipts are weak, but no-order strategy is helpful

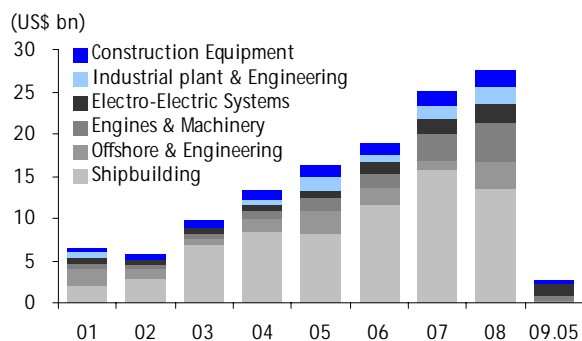
Monthly order trend sustained in all segments except shipbuilding

Hyundai Heavy Industries' newbuilding orders amounted to US\$850mn in May, extending a steady monthly order intake trend. E&E (electric and electronic) system and offshore plant orders increased 16.2% YoY and 20.7% YoY, respectively, in the year to May, while the shipbuilding division booked nothing. The shipbuilding unit had an order backlog of 303 vessels, worth US\$20bn, which is equivalent to 34 months of work. Shipbuilding market conditions are expected to improve in 2H09 after a deep slump in 1H09. Still, on a YoY basis, sluggish market conditions should continue throughout the year.

Order intake momentum sharply weaker than previous years

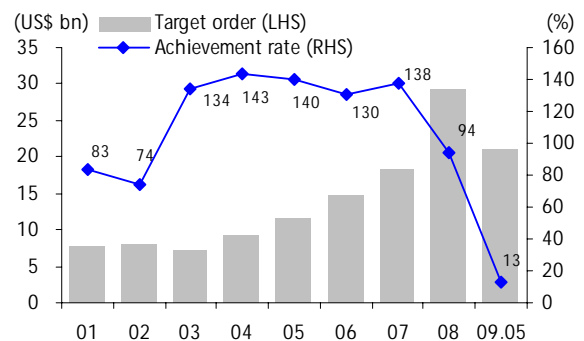
Hyundai Heavy Industries surpassed its order target every year during the past five years from 2003 to 2008. However, in the first five months of this year, the company posted US\$2.71bn worth of new orders (-83.1% YoY) across the divisions, a sharp decline from a year earlier. The target-to-current ratio also remained at a slow 12.8%. The shipbuilding division has not been too aggressive about winning new orders. First, the global shipbuilding market is still in its downturn with order volume contracting. Second, prices will fall further if Hyundai Heavy, the world's biggest shipbuilder, goes on the offensive. This is a good strategy for a short-term cash flow, but the company's future earnings value will decline and a price order in the global shipbuilding market, led by Korean companies, could collapse. All in all, the company is expected to remain cautious in 2H09 until the market regains stability.

Annual new orders by biz unit (amount based)



Source: Clarksons, Goodmorningshinhan securities

Target order amount and achievement rate trend



Source: HHI, Goodmorningshinhan securities

Company-wide sales stood at W9.042tr (+20.9% YoY) for the year to May

Company-wide sales stood at W9.042tr (+20.9% YoY) for the year to May, accounting for 39.5% of the 2009 order target (W22.009tr). Despite weak order receipts, the company is making decent progress, which is attributable to its stable order backlog. By segment, shipbuilding and construction equipment sales showed the weakest growth of 8.1% and -51.2%, respectively. Other business divisions are showing robust growth.

2009 monthly sales by biz unit						
(W bn)	Jan.	Feb.	Mar.	Apr.	May	Cumulated
Sales	1,730	1,829	1,935	1,820	1,728	9,042
Shipbuilding	762	752	898	835	700	3,947
Offshore & Engineering	326	408	355	319	286	1,694
Engines & Machinery	215	243	222	209	254	1,143
Electro-Electric Systems	218	233	259	216	219	1,145
Industrial plant & Engineering	118	106	118	151	121	,614
Construction Equipment	78	74	69	78	137	436
Others	13	13	14	12	11	63
(Growth, %)						
Total sales	22.5	29.8	26.2	15.1	11.8	20.9
Shipbuilding	7.0	8.2	19.3	13.3	(7.2)	8.1
Offshore & Engineering	103.8	155.0	89.8	42.4	56.3	85.3
Engines & Machinery	66.7	72.3	29.1	25.9	47.7	46.5
Electro-Electric Systems	56.8	70.1	73.8	46.9	28.1	54.1
Industrial plant & Engineering	53.2	7.1	61.6	48.0	42.4	40.8
Construction Equipment	(57.4)	(55.4)	(63.1)	(58.9)	(18.0)	(51.2)
Shipbuilding	8.3	18.2	16.7	(20.0)	(21.4)	(1.6)

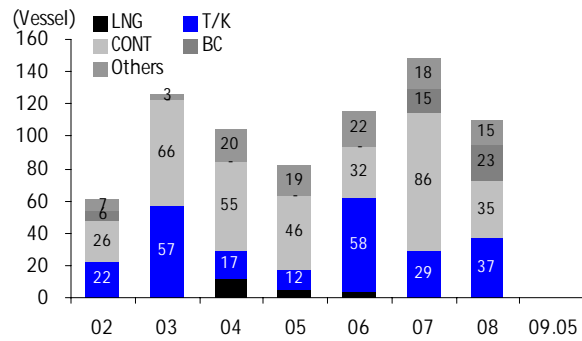
Source: Goodmorningshinhan securities

Order backlog and quarterly earnings forecasts

Order backlog is equivalent to 2 years and 10 months of inventory

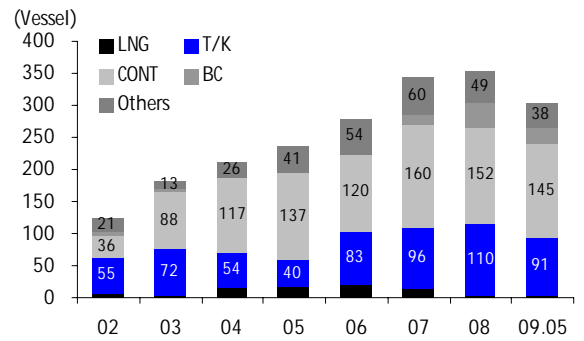
The shipbuilding unit didn't book a single order in the year to May. The order backlog stands at 303 vessels worth US\$29bn, big enough to keep the company busy until 1Q12, or even longer if delivery postponement requests from some clients are considered. On the other hand, the company can pick up the pace if shipbuilding demand recovers. All in all, the current workload is estimated at 2 years and 10 months.

New order (vessel based)



Source: HHI, Goodmorningshinhan securities

backlog (vessel based)



Source: HHI, Goodmorningshinhan securities

2Q09 sales estimated at W5,446bn (+15.6% YoY)

The company is estimated to have achieved an operating profit of W456bn (-16.6% YoY) on sales of W5.446tr (+15.6% YoY) with a pre-tax profit of W681bn (-24.5% YoY) in 2Q09. Sales growth will likely slow amid delays in deliveries. Operating profit and pre-tax profit will also feel the squeeze from slowing sales growth. Declines in heavy plate prices will not likely translate into margin gains until 2H09 due to an input time lag.

HHI's quarterly earnings summary

(W bn)	1Q08	2Q08	3Q08	4Q08	1Q09	2Q09F	3Q09F	4Q09F	1Q10F	2Q10F	3Q10F	4Q10F
Sales	4,354	4,709	4,843	6,051	5,494	5,446	5,766	7,292	6,863	7,120	7,659	9,069
OP	640	548	344	675	471	456	450	953	605	903	1,040	1,174
RP	651	903	406	991	633	681	670	882	778	1,136	1,263	1,092
NP	442	655	292	867	498	521	512	661	595	869	967	836
(%)												
OPM	14.7	11.6	7.1	11.2	8.6	8.4	7.8	13.1	8.8	12.7	13.6	12.9
RPM	14.9	19.2	8.4	16.4	11.5	12.5	11.6	12.1	11.3	16.0	16.5	12.0
(growth, %)												
Sales	18.4	21.5	29.9	42.3	26.2	15.6	19.0	20.5	24.9	30.7	32.8	24.4
OP	58.9	48.4	(18.7)	21.4	(26.3)	(16.6)	30.7	41.2	28.3	97.9	131.1	23.2
RP	28.1	59.0	(31.5)	36.3	(2.7)	(24.5)	65.2	(11.0)	22.9	66.7	88.6	23.9
NP	19.2	56.9	(32.9)	69.1	12.7	(20.4)	75.6	(23.8)	19.5	66.7	88.6	26.5

Source: wisefn, Goodmorningshinhan securities estimates



• GMSH Rating Classifications (As of 10 Feb. 2003) : BUY; Over +15%, HOLD; -15% to +15%, REDUCE; -15% or More

Balance Sheet

Year to Dec. (W bn)	2007	2008	2009E	2010E	2011E
Total Assets	16,824.1	25,280.4	27,547.1	31,022.1	34,084.6
Current Assets	8,499.5	12,617.6	12,808.2	14,197.6	15,229.2
Cash & Cash Equivalents	953.8	667.5	619.7	422.2	34.7
St. Investment Assets	2,657.5	1,808.9	1,899.3	1,994.3	2,094.0
Accounts Receivable	2,740.7	4,498.9	4,352.5	5,210.6	5,949.8
Inventory	1,119.2	2,263.3	2,033.6	2,434.6	2,779.9
Others	1,028.4	3,379.1	3,903.2	4,135.9	4,370.8
Non-current Assets	8,324.6	12,662.8	14,738.9	16,824.5	18,855.4
Investment Assets	2,971.8	3,224.4	3,963.7	4,775.6	5,606.1
Tangible Assets	4,968.8	6,190.0	7,370.1	8,480.9	9,525.7
Intangible Assets	236.0	262.3	269.6	275.8	266.8
Total Liabilities	11,332.6	19,685.2	20,058.8	21,240.1	22,120.0
Current Liabilities	10,887.6	16,473.9	16,478.2	16,886.8	17,990.3
Accounts Payable	1,495.2	2,337.3	2,810.4	3,364.5	3,841.7
St. Debt	0.0	0.0	0.0	0.0	0.0
Current Portion of Lt. Debt	187.3	0.0	0.0	0.0	300.0
Others	9,205.1	14,136.6	13,667.9	13,522.3	13,848.6
Non-current Liabilities	444.9	3,211.3	3,580.6	4,353.3	4,129.7
Bonds	0.0	0.0	300.0	1,000.0	700.0
Lt. Debt	1.6	3.3	3.3	3.3	3.3
Others	443.3	3,208.0	3,277.3	3,350.0	3,426.4
Total Stockholders Equity	5,491.5	5,595.2	7,488.3	9,781.9	11,964.6
Paid-in Capital	380.0	380.0	380.0	380.0	380.0
Capital Surplus	2,771.4	2,818.6	2,818.6	2,818.6	2,818.6
Capital Adjustment	(696.7)	(1,762.0)	(1,762.0)	(1,762.0)	(1,762.0)
Other Accumulated Earnings	169.8	(498.5)	(498.5)	(498.5)	(498.5)
Retained Earnings	2,867.1	4,657.1	6,550.2	8,843.9	11,026.5
Total Debt	189.0	3.3	303.3	1,003.3	1,003.3
Net Debt(Cash)	(3,422.3)	(2,473.0)	(2,215.6)	(1,413.1)	(1,125.4)

Cash Flow

Year to Dec. (W bn)	2007	2008	2009E	2010E	2011E
Cash Flows from Operating	4,116.0	2,382.7	1,767.4	1,239.5	1,771.7
Net Profit	1,736.1	2,256.7	2,192.8	2,593.3	2,482.3
Depreciation	351.7	347.3	535.7	621.9	704.8
Amortization	40.2	43.5	45.8	47.0	48.1
Equity Method Loss(Gain)	(482.5)	(619.9)	(350.8)	(375.3)	(383.5)
Investment Asset Disp Loss(Gain)	(7.0)	(23.6)	(23.6)	(23.6)	(23.6)
Tangible Asset Disp Loss(Gain)	26.6	8.8	9.2	9.7	10.2
Changes in Working Capital	2,461.3	(1,235.0)	251.5	(1,102.4)	(837.8)
Others	(10.3)	1,605.0	(893.2)	(531.1)	(228.8)
Cash Flows from Investing	(3,476.0)	(1,183.7)	(1,815.5)	(1,837.3)	(1,859.5)
St. Investment Assets Dec.(Inc.)	(2,165.5)	870.3	(90.4)	(95.0)	(99.7)
Investment Securities Dec.(Inc.)	(356.1)	(271.0)	0.0	0.0	0.0
Tangible Assets Dec.(Inc.)	(891.9)	(1,708.0)	(1,725.1)	(1,742.3)	(1,759.8)
Others	(62.4)	(75.0)	0.0	0.0	0.0
Free Cash Flow	640.0	1,199.0	(48.2)	(597.8)	(87.8)
Cash Flows from Financing	(506.2)	(1,485.3)	0.3	400.3	(299.7)
St. Debt Inc.(Dec.)	0.0	0.0	0.0	0.0	0.0
Cur. Por. of Lt. Debt Inc.(Dec.)	0.0	(187.6)	0.0	0.0	300.0
Bonds Inc.(Dec.)	0.0	0.0	300.0	700.0	(300.0)
Lt. Debt Inc.(Dec.)	0.3	1.7	0.0	0.0	0.0
Share Capital Inc.(Dec.)	0.0	0.0	0.0	0.0	0.0
Dividend Paid	(161.2)	(466.6)	(299.7)	(299.7)	(299.7)
Others	(345.2)	(832.7)	0.0	0.0	0.0
Change in Cash	133.8	(286.3)	(47.8)	(197.5)	(387.5)
Beginning Cash	819.9	953.8	667.5	619.7	422.2
Ending Cash	953.8	667.5	619.7	422.2	34.7
Capex/ Sales (%)	5.7	8.6	7.2	6.1	5.4
Depreciation/ Sales (%)	2.3	1.7	2.2	2.2	2.1
Depreciation/ Capex (%)	39.4	20.3	31.1	35.7	40.0

Source: Company data, GMSH estimates

Profit and Loss

Year to Dec. (W bn)	2007	2008	2009E	2010E	2011E
Net Sales	15,533.0	19,957.1	23,997.0	28,728.2	32,803.1
Growth (%)	23.7	28.5	20.2	19.7	14.2
Export ratio (%)	88.5	90.0	91.3	92.2	92.7
Cost of Sales	12,976.1	16,812.0	20,618.6	24,719.6	28,833.8
Growth (%)	18.3	29.6	22.6	19.9	16.6
Gross Profit	2,556.9	3,145.1	3,378.5	4,008.5	3,969.4
Gross Margin (%)	16.5	15.8	14.1	14.0	12.1
SG&A Expenses	806.2	938.9	1,047.5	1,155.4	1,242.1
Growth (%)	14.8	16.5	11.6	10.3	7.5
Operating Profit	1,750.7	2,206.2	2,331.0	2,853.1	2,727.3
Growth (%)	99.2	26.0	5.7	22.4	(4.4)
Operating Margin (%)	11.3	11.1	9.7	9.9	8.3
Non-Operating Inc (Exp)	643.7	743.5	535.1	536.5	517.4
Interest Income	199.7	279.9	230.3	227.9	210.4
Interest Expenses	11.4	6.5	10.3	44.0	67.5
Net F/X	14.4	55.5	52.4	49.2	45.9
Net Asset Disposal	(19.5)	14.8	14.4	13.9	13.5
Net Equity Method	482.5	619.9	350.8	375.3	383.5
Net Other non-operating	(22.0)	(220.2)	(102.5)	(85.9)	(68.4)
Pre-tax Profit from Cont. Op	2,394.4	2,949.6	2,866.1	3,389.6	3,244.6
Income Taxes	658.3	693.0	673.3	796.3	762.3
Profit from Cont. Op	1,736.1	2,256.7	2,192.8	2,593.3	2,482.3
Profit from Discont. Op	0.0	0.0	0.0	0.0	0.0
Net Profit	1,736.1	2,256.7	2,192.8	2,593.3	2,482.3
Growth (%)	143.5	30.0	(2.8)	18.3	(4.3)
Net Margin (%)	11.2	11.3	9.1	9.0	7.6
EBITDA	2,142.6	2,597.0	2,912.5	3,522.0	3,480.1
Growth (%)	70.4	21.2	12.1	20.9	(1.2)
Dividend Payout (%)	26.9	13.3	13.7	11.6	12.1

Key Ratios

Year to Dec.	2007	2008	2009E	2010E	2011E
EPS (won)	22,843	29,693	28,852	34,122	32,662
Adj. EPS (won)	23,100	29,498	28,663	33,939	32,485
BPS (won)	72,257	73,621	98,530	128,710	157,429
DPS (won)	7,500	5,000	5,000	5,000	5,000
PER (x)	13.7	9.9	6.2	5.3	5.5
Adj. PER (x)	13.5	10.0	6.3	5.3	5.5
PBR (x)	4.3	4.0	1.8	1.4	1.1
PCR (x)	14.3	6.2	9.0	5.8	5.2
EV/ EBITDA (x)	9.5	7.6	3.9	3.5	3.6
PEG (x)	1.0	3.0	(0.5)	na	na
Dividend Yield (%)	2.4	1.7	2.8	2.8	2.8
Profitability					
Operating Margin (%)	11.3	11.1	9.7	9.9	8.3
EBITDA Margin (%)	13.8	13.0	12.1	12.3	10.6
Pre-tax Profit Margin (%)	15.4	14.8	11.9	11.8	9.9
Net Margin (%)	11.2	11.3	9.1	9.0	7.6
ROA (%)	11.6	10.7	8.3	8.9	7.6
ROE (%)	35.4	40.7	33.5	30.0	22.8
ROIC (%)	67.8	53.7	33.7	29.9	22.1
Stability					
Debt Ratio (%)	206.4	351.8	267.9	217.1	184.9
Net Debt Ratio (%)	(62.3)	(44.2)	(29.6)	(14.4)	(9.4)
Interest Coverage (x)	153.5	340.9	225.8	64.9	40.4
Activity					
Asset Turnover (x)	1.0	0.9	0.9	1.0	1.0
Receivables Turnover (x)	5.6	5.3	5.2	5.8	5.7
Inventory Turnover (x)	13.8	11.8	11.2	12.9	12.6
Payables Turnover (x)	11.6	10.4	9.3	9.3	9.1
Working Capital Turnover (x)	(5.3)	(5.2)	(5.4)	(7.8)	(11.7)

Source: Company data, GMSH estimates

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