SECTOR UPDATE

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Industrial Team

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▶ AT A GLANCE

LIG Nex1 (079550 KS, 383,000)		
Target price	KRW595,000	55.4%
BUY		
Hanwha Aerospace (012450 KS, 886,000)		
Target price	KRW1,300,000	35.3%
BUY		
Hyundai Rotem (064350 KS, 183,000)		
Target price	KRW280,000	50.2%
BUY		
Korea Aerospace Industries (047810 KS, 113,000)		
Target price	KRW130,000	12.9%
BUY		

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Defense

Structural improvement, beyond a one-off

- The upturn in Korea's defense industry reflects a structural shift that extends beyond a typical cyclical upswing.
- Korean defense companies, supported by strong profit growth, should be able to navigate concerns over post-war demand normalization as well as valuation pressure stemming from the derating of European peers. It remains too early to turn cautious.

WHAT'S THE STORY?

(§The Korean version of this report was published on Dec 15)

Korea's defense sector is cyclical: The defense sector is often described as cyclical. As part of the broader industrials universe, earnings tend to rise and fall over long cycles due to the time required to adjust capacity. However, defense demand is primarily driven by long-term government procurement plans, which limits the risk of the classic industrials pattern of excess supply or shortages. Instead, the sector follows a development-to-mass-production cycle, with profitability peaking during mass-production. Many Korean defense companies rely on a small number of flagship items for the majority of revenue, meaning consolidated earnings can fluctuate depending on whether core products are in the development phase or in mass-production.

Implication of export expansion: Defense companies typically re-enter the development phase for next-generation programs once mass-production and deployment of a core product are completed. Successful exports, however, have an effect similar to extending the mass-production phase. Export contracts are usually executed after early mass-production risks and defects have been largely eliminated. In addition, export ASPs are generally higher than domestic ASPs, and export margins are materially superior to those achieved in the domestic mass-production stage. The recent surge in Korean defense companies' earnings has been driven primarily by exports.

Prolonged boom—Structural change: We view the recent rise of Korea's defense industry as a structural shift rather than a simple cyclical upturn, for three reasons. First, the export environment remains favorable. Ongoing geopolitical tensions continue to push defense spending higher across major countries, a trend likely to persist even after the Russia-Ukraine war ends. On the supply side, capacity expansion by global defense majors—particularly in the US—has remained limited.

(Continued on the next page)

Second, the industry is benefiting from the establishment of operating track records and the emergence of maintenance, repair, and overhaul (MRO) demand. Defense procurement is inherently conservative, but once a supplier is adopted, incremental sales become easier. Securing initial reference contracts in new markets during the Russia-Ukraine war represents a structural inflection point for Korean defense companies. Moreover, delivered equipment generates long-duration MRO revenue, enhancing revenue.

Third, the sector is underpinned by large backlogs and forward-looking investment. Order backlogs at major Korean defense companies already equate to roughly four years of revenue, with additional contracts still under negotiation. Companies are also reinvesting cash generated during the upturn into future growth areas, which should help extend the growth runway.

Conclusion—Not time to worry, but stay positive: From a fundamental perspective, industry risks remain contained. From a market perspective, the recent derating of European defense peers represents a near-term headwind. However, valuation pressure from cross-border comparisons can be absorbed, given the Korean defense sector's strong earnings growth and the premium typically accorded to industrial companies in the domestic equity market. We believe a constructive stance toward the Korean defense sector remains appropriate.

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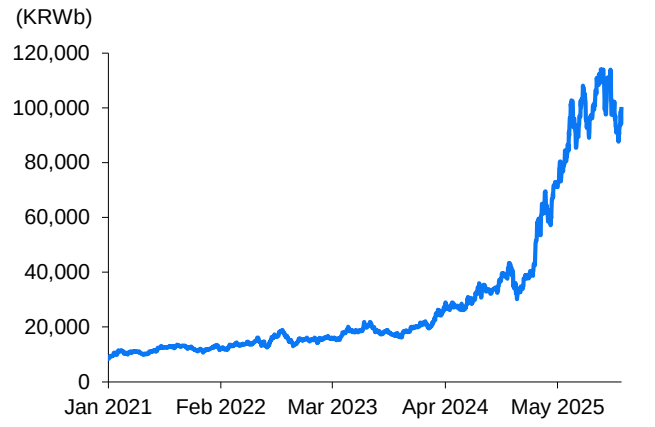
Recent share-price weakness: Sustainability of boom in question

Another year-end pullback triggered by momentum exhaustion

Major Korean defense stocks are down 13% q-q in 4Q to date—a correction ostensibly triggered by a lack of near-term momentum. Momentum typically fades in 4Q because: 1) domestic defense projects tend to be awarded toward year-end as budget execution accelerates; 2) some companies set aside provisioning for low-margin domestic development projects in 4Q; and 3) one-off costs—such as performance bonuses and development cost amortization—are often booked in 4Q, particularly in periods of improving earnings. While 3Q results were not weak, major defense stocks corrected immediately after the earnings season, reflecting low expectations for 4Q results. Historically, defense stocks have tended to soften in 4Q.

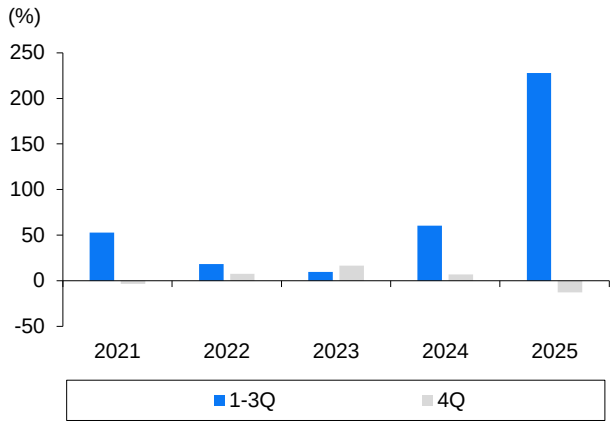
In addition, with major diplomatic events largely concluded for the year, expectations for new export contracts have faded. Media reports suggesting a possible end to the Ukraine war have also weighed on investor sentiment. Profit-taking has intensified following the sector's strong ytd performance across share prices, order intake, and earnings.

Korean defense firms*: Combined market cap



Note: *KAI, LIG Nex1, Hanwha Systems, Hanwha Aerospace, and Hyundai Rotem
Source: Samsung Securities

Korean defense firms'* share performance: 1Q-3Q vs 4Q



Note: * KAI, LIG Nex1, Hanwha Systems, Hanwha Aerospace, Hyundai Rotem
Source: Samsung Securities

Concern centered on sustainability of the cycle

As noted above, year-end share-price weakness is a recurring seasonal pattern. Nevertheless, few investors appear to dismiss this year's correction as inconsequential. In investor meetings, anxiety is noticeably higher than in prior years. The scale of the year-end weakness is also different this time. From 2022 to 2024—following the outbreak of the Russia-Ukraine war and the acceleration of Korea's export order momentum—domestic defense stocks were relatively weaker in 4Q than over 1Q-3Q, but this reflected a deceleration in gains rather than the outright declines seen this year.

We believe the recent correction reflects more than short-term momentum fatigue. In particular, the market is questioning whether a potential end to the Russia-Ukraine war could undermine sentiment toward defense equities—an anxiety reinforced by the recent pullback in European defense stocks. Korea's defense industry is not immune to these concerns, given that it is generating unprecedented profits from Poland-related projects contracted immediately after the Russia-Ukraine war began, and that the re-rating of European peers had previously helped alleviate valuation concerns for Korean names.

In short, the current year-end weakness appears to reflect a broader question: whether the rally in Korean defense stocks and the earnings improvement of the past three years represent a sustainable shift or a one-off, war-driven phenomenon. Put differently, the recent correction is fundamentally about whether the cycle is peaking. Addressing this requires a clearer understanding of the specific dynamics of the Korean defense industry cycle.

Korea's defense sector is cyclical

How does the Korean defense industry's cycle differ from that of conventional industrials?

Industrials are typically cyclical, with profits rising and falling over repeated periods and with long, pronounced swings between booms and busts. This reflects the time required to adjust capacity. Like other manufacturers, industrial companies tend to invest aggressively during upturns, often driven by optimistic forecasts. The problem is that capacity expansion continues even as the cycle nears its peak. Investments committed at the top of the cycle are completed with a lag—often after demand has already begun to wane—resulting in significant oversupply. Conversely, capacity reductions through restructuring are usually pursued during downturns, but these measures cannot be implemented quickly. As a result, restructuring initiated near the trough constrains capacity in the subsequent recovery, amplifying the next boom.

The defense sector also requires substantial capital and long lead times to expand capacity, and capacity reductions are similarly difficult to execute in the short term. However, defense cycles are not generated by the same dynamics as those of conventional industrials. Most importantly, the industry structure makes irrational oversupply unlikely. Demand is shaped by government budgets and long-term procurement plans, resulting in high visibility and predictability. In addition, Korea's defense sector is highly concentrated, often with a single supplier for each major item, which limits competitive intensity. Moreover, even during severe downturns, government support tends to ensure industry survival, reducing the likelihood of extreme, industry-wide restructuring. As a result, both oversupply and supply shortages are rare.

Korea's defense cycle alternates between development and mass-production

Because demand is determined by government procurement plans, the defense sector should, in theory, exhibit less of a conventional industrial cycle. In practice, however, Korean defense companies' earnings have historically risen and fallen in discernible cycles, indicating that a cycle does exist—albeit one driven by different dynamics.

Traditionally, Korea's defense cycle consists of two phases: development and mass-production. Development refers to the creation of a new weapons system. During this phase, companies recognize revenue because the effective "owner" of the program is the government rather than the contractor. Firms provide development services to the government, and intellectual property rights typically reside with the state. Once development is completed, the system transitions into mass-production and deployment. In principle, the developer and the mass-production contractor can differ, as the government selects the production supplier. In practice, however, it is generally most efficient for the developer to undertake mass-production, so the same company usually plays both roles.

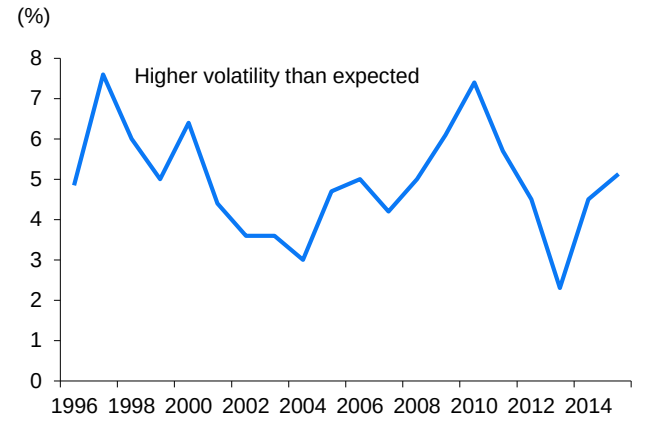
Profitability is higher in mass-production than in development

Defense companies' profitability is structurally stronger in the mass-production phase. From a utilization perspective, development is typically associated with low production facility utilization. Given the security-sensitive nature of defense manufacturing and the rigidity of Korea's labor market, fixed-cost burdens tend to rise during development. By contrast, utilization increases meaningfully during mass-production, improving margins through operating leverage.

The difference is also explained by risk asymmetry. Development projects are prone to cost overruns and, in extreme cases, failure-related costs. Importantly, it is often unclear whether the government will fully compensate these unexpected expenses, and disputes over cost responsibility can arise.

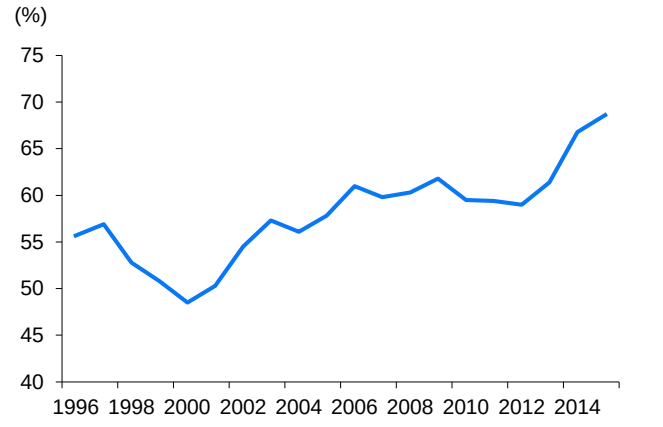
Mass-production, by contrast, begins after key development issues have been resolved. Since it involves scaling an already developed system, the risk of unforeseen costs is lower. Moreover, production is typically governed by contracts, incentivizing for productivity gains and margin expansion.

Korean defense firms: OPM before prior boom



Source: Ministry of Data and Statistics

Korean defense firms: Utilization rate before prior boom



Source: Ministry of Data and Statistics

Why the development-mass-production cycle forms

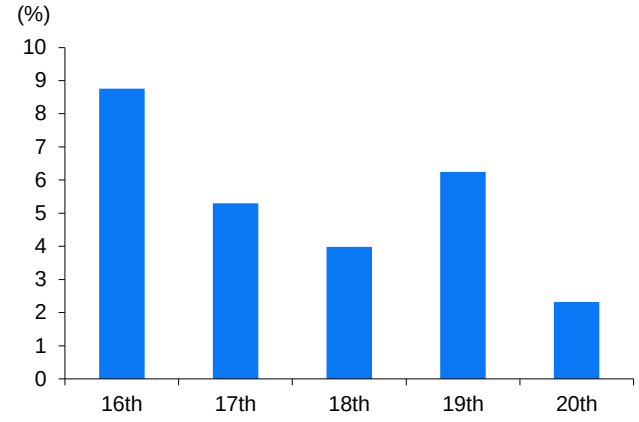
Korea's defense cycle is evident not only at the individual product level but also at the company earnings level. This reflects the fact that most Korean defense companies depend heavily on a small number of flagship products for the bulk of revenue. When a core product enters the development phase, consolidated earnings tend to soften; when it transitions into mass-production, earnings improve.

Korea's domestic defense market is relatively small, and the industry has largely been nurtured under government leadership. The market is not deep enough for companies to independently fund advanced weapons development and fully recoup development costs through sales. As a result, the government must bear a portion of these costs directly or indirectly through the national budget. Given fiscal constraints, it is inefficient to cultivate multiple suppliers for a single platform to promote competition. Consequently, most Korean defense companies have evolved to specialize around specific products.

Even when companies diversify their flagship products, heavy reliance on domestic sales can still result in cyclical earnings. For Korean defense companies with high domestic exposure, operating performance is strongly influenced by the national defense budget and procurement policy. Korea's defense budget is shaped not only by external security threats but also by each administration's policy priorities. While strengthening defense capabilities is broadly bipartisan given the peninsula's geopolitical context, the policy approach can differ materially. One administration may emphasize domestic development, while another may favor imports of advanced foreign systems. In the latter case, even if the overall defense budget expands, the direct benefit to domestic defense companies may be limited.

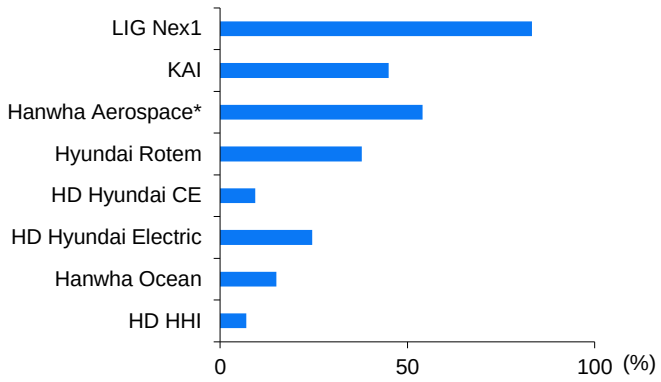
Policy uncertainty persists even when domestic development is prioritized. If the government raises the defense budget but initiates more development programs than the incremental funding can support, companies may face greater difficulty in securing compensation for development failures or cost overruns. Around election cycles, the risk of policy shifts can therefore act as an additional source of uncertainty for defense stocks.

Korea: Defense budget CAGR, by administration



Source: Ministry of Defense

Major industrial companies: Domestic portion of sales



Note: As of end-3Q25;
*Hanwha Ocean excluded from consolidated figures
Source: Samsung Securities

Significance of export expansion in Korea's defense cycle

Growing exports, soaring share prices

The most meaningful change in Korea's defense industry over the past five years has been the surge in export orders. During the previous boom (2013-2015), average annual defense exports amounted to just USD3.5b. Export orders rose to USD7.3b in 2021 and then surged to USD17.3b in 2022 following the outbreak of the Russia-Ukraine war. Over 2023 and 2024, orders declined y-y due to a high base, delays in the timing of several large contracts, and rising political uncertainty in Korea. Even so, the two-year average remained USD11.5b, well above historical levels. Defense equities reacted sharply: the combined market cap of Korean defense companies has risen 629% since end-2021. Investor response was strong because exports were viewed as a catalyst for structural change in the industry.

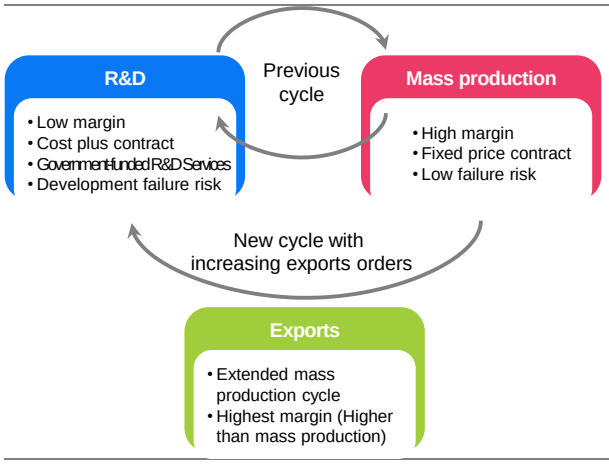
Exports extend the mass-production cycle

Rising exports enhance profitability and improve earnings visibility. As discussed earlier, profitability is structurally higher in mass-production than in development. Once mass-production and deployment of a flagship product are completed, companies typically transition to next-generation development, which weighs on earnings. If export orders are secured at this stage, however, the effect is similar to extending the mass-production phase.

Export projects are also generally more profitable than domestic mass-production. Most exported systems are already in (or have completed) mass-production, meaning exports are executed after early production risks have largely been eliminated. When exports overlap with ongoing domestic production, utilization can increase further, maximizing operating leverage. In addition, export ASPs are typically higher than domestic ASPs. In the domestic market, the government is both the dominant customer and the sponsor of development-stage programs, which limits contractors' bargaining power. This dynamic does not apply to overseas customers, and during periods of supply constraint, suppliers are better positioned to command higher prices.

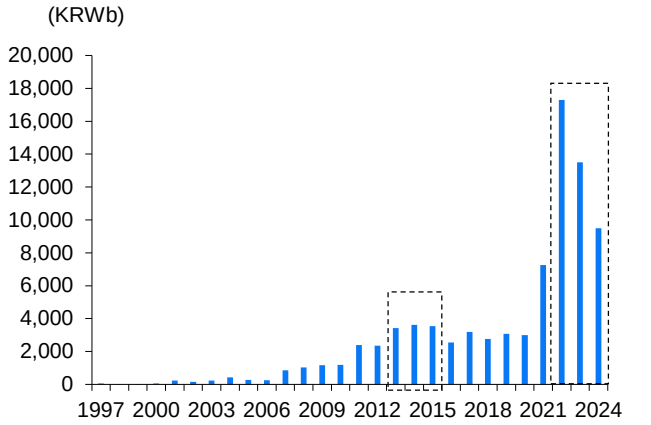
Finally, export expansion improves earnings stability and predictability by diversifying customers and end markets, reducing exposure to domestic policy uncertainty inherent in democracies with regular election cycles.

Korea's defense industry: How exports alter the cycle



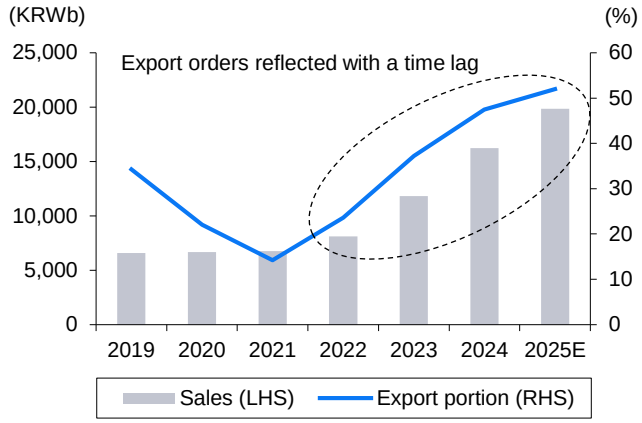
Source: Samsung Securities

Korea's defense industry: Exports orders



Source: DAPA, press released

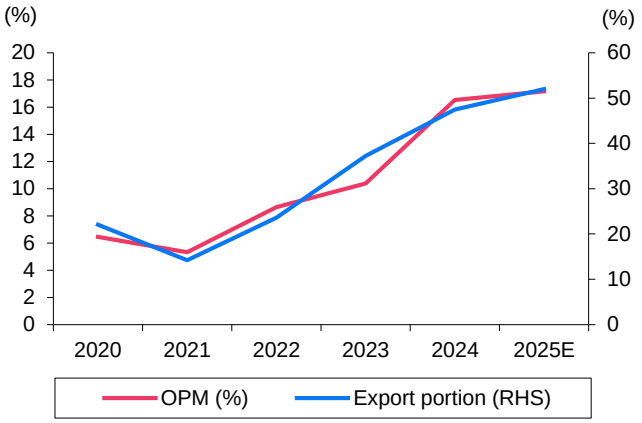
Korean defense sales*: Absolute and export portion



Note: Sum of Hanwha Aerospace's land defense division, KAI, LIG Nex1, and Hyundai Rotem's defense division

Source: Company data, Samsung Securities estimates

Korean defense majors*: Exports vs operating margin



Note: Hanwha Aerospace's land defense division, KAI, LIG Nex1, and Hyundai Rotem's defense division

Source: Company data, Samsung Securities estimates

Prolongation of the boom as a structural change

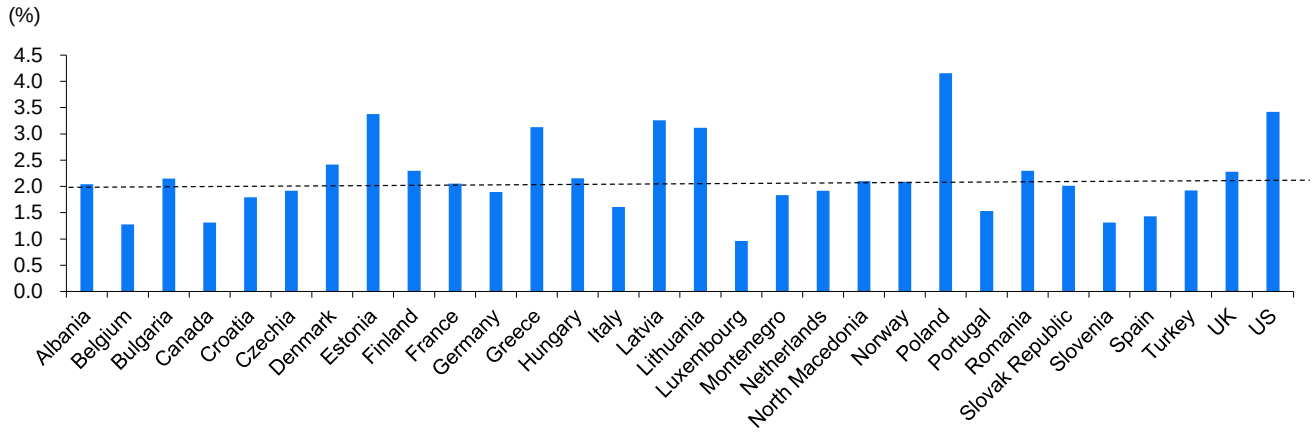
Case 1. Export environment remains favorable: Demand strong, supply tight supply

We view the recent improvement in profitability across Korea's defense industry not as a simple cyclical upswing, but as a structural shift. The first reason is that export conditions remain supportive. Korea's defense export expansion has been fundamentally driven by a combination of rising global demand for weapons and constrained supply—and this imbalance remains.

On the demand side, global defense spending exhibits a structural upward bias. While the war in Ukraine was a decisive catalyst for recent budget increases and will not last indefinitely, higher defense spending is likely to persist even after the war ends. European countries—and particularly those in Eastern Europe, which face a continued Russian threat—have little incentive to materially reduce defense budgets. Middle Eastern nations are also increasing spending in response to regional rearmament. Notably, many of Korea's recent export customers are countries adjacent to conflict zones rather than direct belligerents.

From an institutional perspective, the risk of defense spending cuts also appears limited. NATO has agreed to raise its defense spending guideline to 5% of GDP by 2035, announced ahead of its leaders' summit in Jun 2025. The previous benchmark of 2% of GDP has not been met by roughly 30% of member states. If the higher target is implemented, defense spending should continue to trend upward. Saudi Arabia, a key Middle Eastern customer, is also expected to increase defense outlays. To achieve its goal of localizing 50% of defense procurement by 2030, Saudi Arabia will require cooperation with foreign defense companies, including technology transfer and local investment. To incentivize such cooperation, continued procurement from partner defense suppliers is likely.

NATO member countries: Defense spending as portion of GDP (2024)



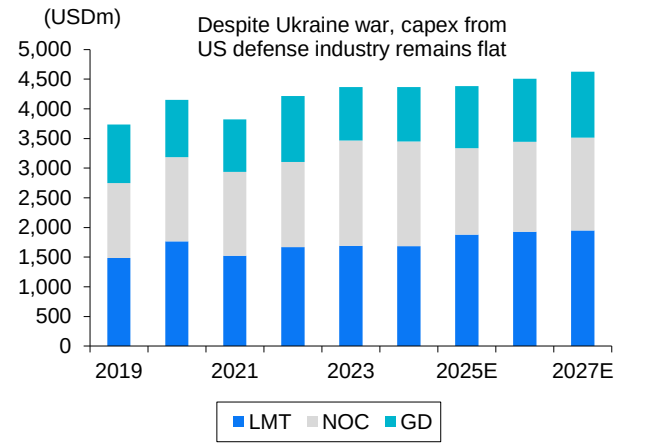
Source: NATO

It is also important to note that recent conflicts have involved the actual consumption of weapons rather than purely symbolic arms races, as was often the case in the past. Weapons are expensive, long-life assets that require ongoing maintenance and life-extension, and replacement demand typically emerges only gradually. For munitions and missiles in particular, replacement demand is limited unless inventories are physically depleted. Recent conflicts have materially drawn down stockpiles, creating immediate replacement demand. As a result, the market today reflects both structural growth in demand growth and inventory rebuilding.

The current environment is particularly favorable for Korean suppliers. While conflicts are increasing, the US is avoiding direct intervention and instead encouraging greater burden-sharing among allies. Korea is unlikely to sell meaningfully into the US market itself given US technological leadership. Consequently, increased defense spending by US allies is more supportive for Korean exporters than higher spending by the US alone.

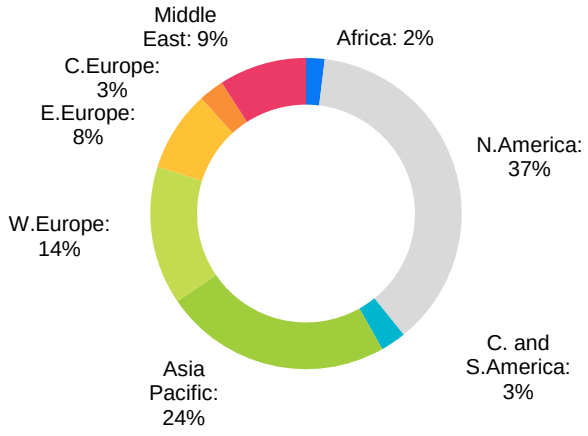
On the supply side, global defense capacity has not expanded meaningfully despite rising demand. Large global defense contractors have operated in stable and predictable markets for decades, limiting incentives to maintain excess capacity. As with other industrial sectors, defense manufacturing capacity cannot be expanded quickly. US defense companies, in particular, have limited motivation to pursue aggressive capacity expansion given uncertainty around the long-term trajectory of US defense budgets. Despite their scale, US contractors remain highly dependent on domestic demand, which is natural given that North America accounts for 37% of global defense spending. Unless US policy on burden-sharing shifts materially, uncertainty will persist from their perspective, constraining large-scale investment in capacity. As a result, the global defense market remains supply-constrained. Countries capable of large-scale production while maintaining full interoperability with Western systems are still limited, and when price competitiveness is considered, Korean weapon systems remain among the most compelling alternatives for many buyers.

US defense companies: Capex



Source: Bloomberg

Global defense expenditure, by region



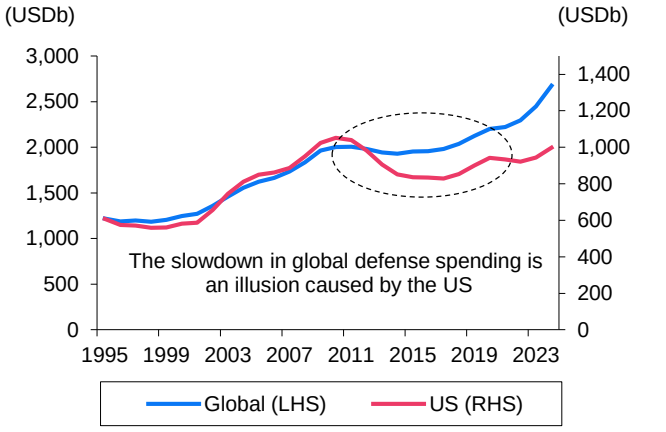
Source: SIPRI

Case 2. Export track record and MRO demand from delivered systems

Korea's meaningful entry into overseas defense markets can itself be viewed as a source of structural growth. Defense procurement is inherently conservative and characterized by high entry barriers, as buyers are reluctant to adopt unproven systems given the national security implications. Conversely, once a supplier is accepted, it can become relatively insulated from competition.

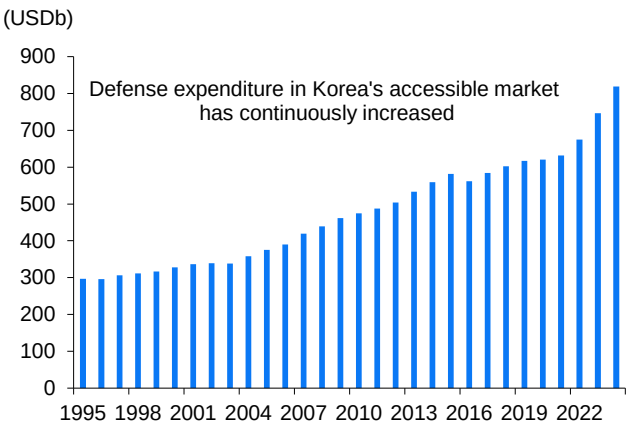
Defense spending in the "rest of world" segment—often regarded as Korea's core addressable market—had been rising steadily even prior to the Russia-Ukraine war. The slowdown in global defense spending growth over 2011-2017, including outright declines over 2012-2014, was driven mainly by US budget cuts following the end of the Afghanistan war and efforts to address US fiscal deficits. Excluding the US and Western Europe, where Korea faces significant technology gaps, and China and Russia, where exports are constrained by technical and political factors, the "others" segment recorded a CAGR of 3% even during that period (*ie*, 2011-2017). Annual growth in this segment accelerated to average 10% over 2022-2024, which spans the key phases of the war in Ukraine, or 9% even excluding Ukraine.

Defense budgets: Global vs US



Source: SIPRI

Defense expenditure in Korea's accessible market*

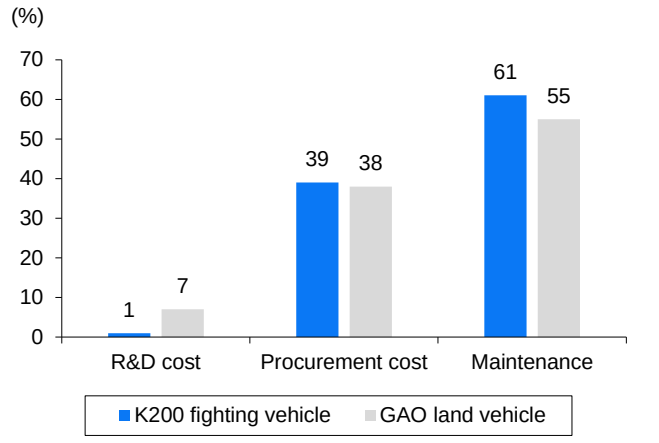


Note: *Global figure excluding North America, Europe, Russia, and China
Source: SIPRI

Despite steady demand growth in accessible markets, Korea was unable to scale exports meaningfully prior to the Russia-Ukraine war due to the conservative nature of buyers. Today, following the onset of the war, Korean defense companies have established track records in new markets, which we view as a structural inflection point. In defense markets, once a system is validated and adopted by one country, subsequent validation and sales to other countries become easier, as the platform has been proven in operational service. As the number of user countries increases, suppliers can also achieve economies of scale and enhance price competitiveness, creating a virtuous circle.

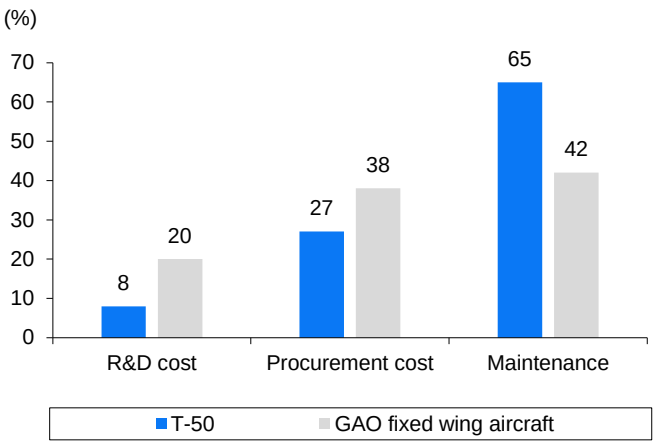
Equally important is the presence of long-duration follow-on revenue. Weapons systems have long service lives, and the market for support services—maintenance, overhaul, and management—can exceed the value of the initial sale. We estimate that initial procurement typically accounts for less than half of total lifecycle cost, implying that once a system is delivered, defense companies can generate incremental revenue over an extended period. This materially lengthens the business cycle for Korean defense companies that have successfully expanded overseas. For reference, in the case of the FA-50 (a successful Korean defense export), the Korea Institute for Defense Analyses (KIDA) estimates that operating and maintenance costs account for 75% of total lifecycle costs based on current prices. For land-based weapons systems, maintenance costs are estimated at approximately 61% of lifecycle cost.

Land-based weapons: Breakdown of lifecycle costs



Source: Korea Institute of Military Science and Technology

Aircraft: Breakdown of lifecycle costs



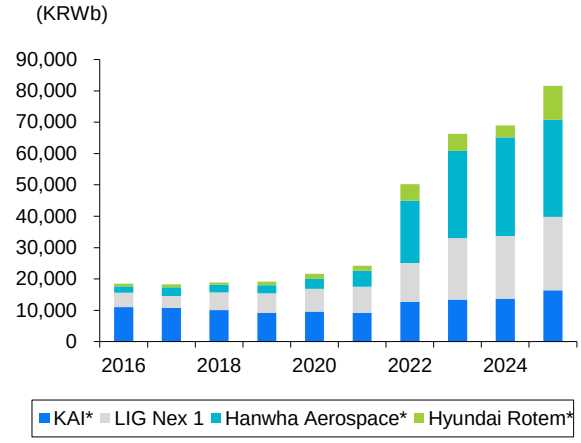
Source: Korea Institute of Military Science and Technology

Case 3. Massive backlogs and investments in future growth

Even based solely on currently secured backlogs, concerns about a near-term peak appear premature. Hanwha Aerospace's land defense backlog stands at KRW31t; Hyundai Rotem's defense backlog at KRW11t; Korea Aerospace Industries' (KAI) backlog at KRW14t excluding airframe parts; and LIG Nex1's total backlog at KRW23t. These figures are 3.4x higher than at end-2021 (prior to the Russia-Ukraine war) and correspond to an average of 4.3 years of expected revenue based on this 2025 estimates.

On backlog alone, continued earnings growth over the next two to three years appears reasonable. Moreover, as the backlog expansion has been driven largely by export orders, margins embedded in the existing backlog should remain favorable. It is also premature to argue that Poland-related projects are nearing exhaustion. Based on company disclosures, Hanwha Aerospace's first execution contracts in Poland run through Sep 2026 for the K9 and Nov 2027 for the Chunmoo, while second execution contracts signed over 2023-2024 extend to 2031 for the K9 and 2029 for the Chunmoo. Hyundai Rotem's first K2 execution contract runs through Dec 2027, with the second extending to 2033. KAI's FA-50 deliveries are scheduled to run through Sep 2028. While contract end dates and revenue recognition timing may differ, even allowing for these factors, Poland-related projects should remain meaningful earnings contributors for Korean defense companies for an extended period.

Korean defense majors: Orderbook



Note: *Defense divisions only for KAI and Hyundai Rotem, and land defense division only for Hanwha Aerospace

Source: Company data, Samsung Securities

Korean defense majors: Orderbook-to-sales ratio (estimates)

(KRWb)	Orderbook (A)	2025E sales (B)	Orderbook-to-sales (A/B) (x)
KAI*	16,344	2,885	5.67
LIG Nex1	23,427	4,034	5.81
Hanwha Aerospace*	31,000	8,463	3.66
Hyundai Rotem*	10,790	3,457	3.12
Total	81,561	18,840	4.33

Note: *Defense divisions only for KAI and Hyundai Rotem, and land defense division only for Hanwha Aerospace

Source: Company data, Samsung Securities

Poland projects: Timelines

Project	Item	Disclosure date	Timeline (disclosed)		Size	
			Start	End	(Volume)	(KRWb)
1st execution contract	K-9 propelled gun	Aug 29, 2022	Aug 26, 2022	Sep 30, 2026	212	3,204
	Chunmoo	Nov 4, 2022	Nov 4, 2022	Nov 15, 2027	218	5,048
	K2 tank	Aug 29, 2022	n/a	Dec 31, 2027	180	4,499
	FA-50	Sep 19, 2022	Nov 30, 2022	Sep 30, 2028	48	2,165
2nd execution contract	K-9 propelled gun	Dec 4, 2023	Dec 1, 2023	Nov 29, 2031	152	3,447
	Chunmoo	Apr 25, 2024	Apr 25, 2025	Oct 30, 2029	72	2,253
	K2 tank	Aug 4, 2025	Aug 1, 2025	Dec 31, 2033	180	8,981

Note: Based on public disclosures

Source: Company data

Beyond secured orders, the export pipeline remains sizeable. In the Middle East, potential opportunities span both land and air systems, with Saudi Arabia pursuing ground force reinforcement and Iraq seeking to replace aging tank fleets. Interest in Korean fighter aircraft is also elevated, supported by shorter lead times and fewer procurement constraints. The Middle East is a familiar market for Korean suppliers given prior sales and operating experience. In Africa, Egypt's large-scale trainer replacement program has prompted KAI to declare its participation. Southeast Asia also shows interest across Korean platforms, including aircraft and missile systems, particularly in Malaysia and the Philippines. In South America, Peru is actively pursuing Korean systems, and Korean companies are building cooperative relationships with a view to using Peru as a regional bridgehead. In Europe, despite local capacity expansion and EU support for intra-regional defense production, additional exports to countries such as Norway, Sweden, and Estonia continue to be cited in media reports. There is also potential, albeit limited, for exports to the US, the world's largest defense market. KAI plans to participate with Lockheed Martin in a US Navy advanced trainer program, while LIG Nex1's Bigung (Poniard, a 2.75-inch guided rocket) has been added to the US list of acquisition candidates. Most of these pipeline opportunities will require time to reach contract, face intense competition, and remain opaque given the nature of defense procurement. However, the frequency of reported export discussions despite limited disclosure suggests that the actual scale of export pursuits may exceed market expectations.

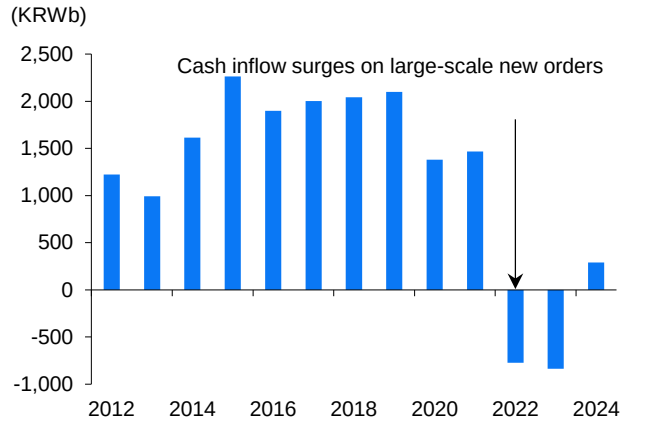
Potential weapon export orders, as reported in the media

Company	Country	Item	Summary of local media reports
Hanwha Aerospace	Chile	TIGON	Proposed TIGON system for Chile's armored vehicle modernization
	Saudi Arabia	Chunmoo, K9, Redback, Hyunmoo	Saudi Arabia considering land force modernization; additional Chunmoo sales under negotiation
	Spain	K9	Spain considering the purchase of 214 artillery units
	Estonia	Chunmoo	Due to delays in HIMARS delivery, Estonia may deploy both Chunmoo and HiMARS
	Norway	Chunmoo	Chunmoo competing with HIMARS
Hyundai Rotem	Sweden	K2	Germany won the next-generation tank program; Rotem to bid for the replacement program
	Peru	K2, Wheeled armored vehicle	Peru's land forces modernization program (K2 purchases from Korea through 2028, followed by local production over 2029-2040)
	Romania	K2	Competing with the US and Germany in Phase 2, after Phase 1 was awarded to the US
	Iraq	K2	Replacement program for an aging Abrams tank fleet
KAI	US	T-50/FA-50	Competing with Boeing for the UJTS program
	Egypt	FA-50	Competing with France and China in an aging training jet replacement program
	Iraq	KUH	Negotiations underway with Iraq's Ministry of Defense
	UAE	KF-21, Surion	UAE general participated in a KF-21 test flight; KUH export under negotiation
	Slovakia	FA-50	Interest expressed in an air force modernization program
	Peru	KF-21, FA-50	Replacement of an aging fleet; Korea proposing a combined FA-50/KF-21 package
	Malaysia	KF-21, FA-50	Additional FA-50 purchases under consideration; interest expressed in KF-21
LIG Nex1	Poland	M-SAM	Due to delays in PAC-3 deliveries from the US, KR M-SAM has emerged as an alternative
	Philippines	K-SAAM	Potential for additional naval combat system sales
	US	LOGIR	Passed Foreign Comparative Testing in Jul 2024
	Malaysia	M-SAM II	Competing with NASAMS

Source: Domestic press

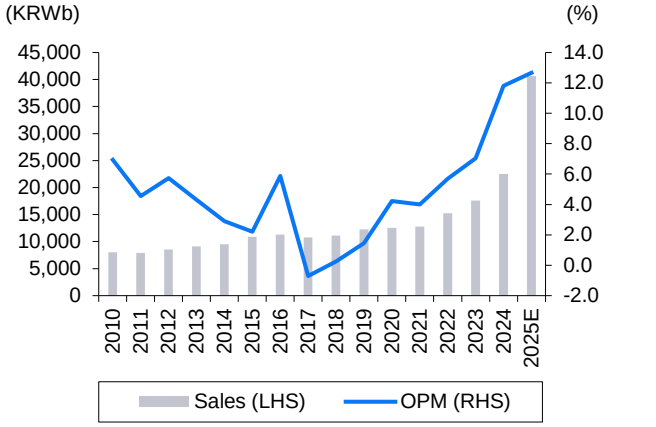
Investment activity by major Korean defense companies should also support longer-term growth. As in other order-based industries, large contracts typically involve substantial advance payments. Supported by repeated earnings strength and upfront cash inflows, balance sheets and cash generation have continued to improve. Companies are using this cash for investments, including capacity expansion and development spending to enter new markets. If executed successfully, these investments can enhance competitive positioning, diversify revenue streams, and help defend profitability through future industry downturns.

Korean defense majors*: Net debt



Note: Hanwha Aerospace (parent basis), Hyundai Rotem, LIG Nex1, and KAI
Source: Company data

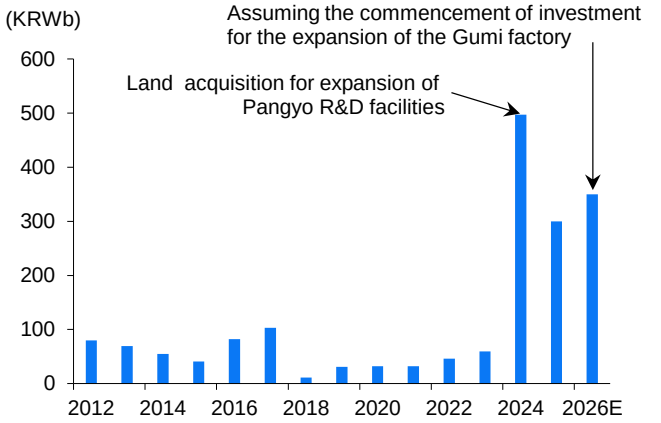
Korean defense majors: Sales and operating profit



Note: Hanwha Aerospace (parent basis), Hyundai Rotem, LIG Nex1, and KAI
Source: Company data

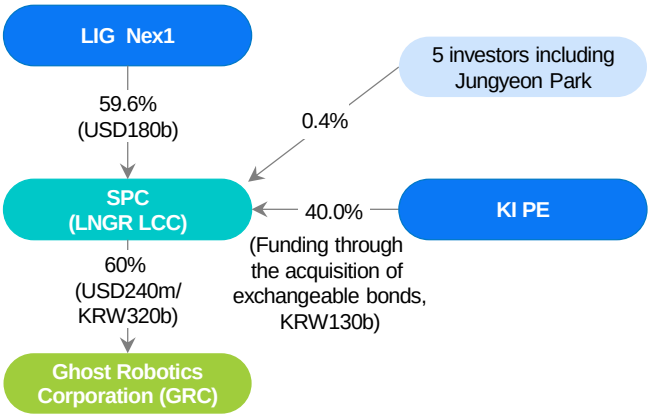
By company, LIG Nex1 executed a major investment program in 2024. The company acquired the Seongnam Sejong Research Institute site to build a new R&D facility, with total investment—including land acquisition—amounting to KRW385.3b. For capacity expansion, it is expected to begin capex next year for the LG Electronics plant acquired in 2024; recent disclosures indicate planned investment of KRW374b through 2029. Beyond expansion of existing operations, 2024 also marked a turning point in M&A activity, with acquisitions of Korea Investment PE and Ghost Robotics.

LIG Nex1: Capex



Source: Company data, Samsung Securities estimates

Ghost Robotics acquisition structure

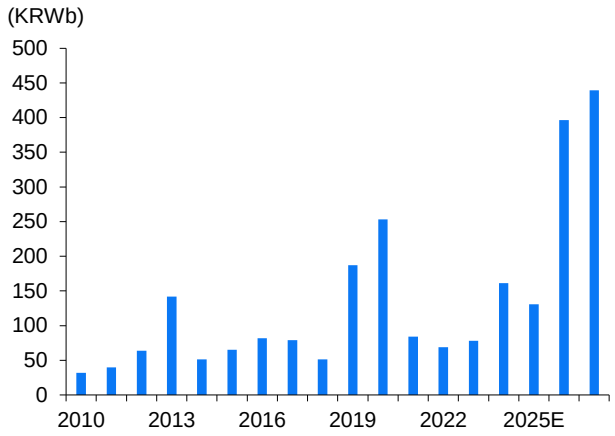


Source: Press released

KAI is pursuing large-scale capacity expansion. According to its 3Q23 report, the company has KRW966.9b of planned capex for 2025-2027, equivalent to roughly KRW320b per year. For comparison, its tangible asset investment averaged KRW110b per year over the past decade. The planned capex is expected to be used to convert existing plants into smart factories and to expand manufacturing capacity for finished aircraft exports and the KF-21.

In addition, the company has outlined substantial investment in future technology development. Under its long-term vision (announced in 2023), KAI plans to invest KRW1.5t in R&D through 2027, followed by an additional KRW3t over 2028-2033.

KAI: Capex



Note: 2025-2027 figures are estimates based on investment plans disclosed in quarterly reports
Source: Company data

KAI's 2050 vision: R&D investment plans

Period	Industry	Capex (KRWb)
2023-2027	Product development (KF-21, FA-50, *etc*)	710
	New platforms (AAV, eco-friendly aircraft, *etc*)	460
	New tech (AI, unmanned autonomous vehicles, *etc*)	330
	Total	1,500
2028-2033		3,000

Note: Announced in 2023
Source: Company data

We believe Hyundai Rotem has scope to roughly double K2 tank production capacity, considering delivery requirements implied by its backlog and capex trends among key suppliers. According to its annual report, the company plans to invest approximately KRW630b to expand domestic capacity expansion over 2025-2027. Planned investment for 2026 is KRW230b and 2027 KRW260b—well above the five-year annual average of KRW50b in tangible asset investment.

Hanwha Aerospace has been the most aggressive in expansion. Unlike its peers, its investments span both defense and non-defense businesses. On the M&A front, the company, together with group affiliates, acquired shipbuilder Hanwha Ocean in 2023 and participated in its capital increase, with total spending of KRW1.3t. It subsequently acquired a Singapore-based offshore structures company. Even excluding its stake purchase in Australian shipbuilder Austal, cumulative M&A spending over 2022-2025 amounts to KRW3.9t. The company is also investing proactively in core defense operations, including KRW194.9b to build a facility in Australia and KRW667.3b to expand propellant production. Media reports suggest it is also reviewing construction of a propellant plant in the US. According to its corporate value enhancement plan disclosed in 2025, Hanwha Aerospace plans to execute total investments of KRW17t over 2025-2028.

Hanwha Aerospace: Acquisitions over 2022-2025

Time	Target	(KRWb)
Dec 2022	Hanwha Defense	852
May 2023	Hanwha Ocean	1,000
Nov 2023	Hanwha Ocean capital raise	313
Mar 2024	Hanwha Semitech capital raise	237
June 2024	Hanwha Futureproof	656
Jan 2025	NextDecade	180
Mar 2025	Dyna-Mac	635
Total		3,873

Note: *Excluding investments in Austal
Source: Company data, Samsung Securities

Hanwha Aerospace: Investment plan

(KRWb)	2025E	2026E	2027E	2028E	Total
Overseas investment	728	3,162	1,770	605	6,265
Defense	606	2,261	1,694	605	5,165
Shipbuilding/Offshore/Energy	122	901	76		1,100
R&D for new-market entry	368	483	386	322	1,559
Land defense infrastructure	859	892	347	194	2,292
Aerospace infrastructure	310	255	231	158	954
Total	2,992	7,954	4,506	1,884	17,336

Note: Based on “value-up” plan
Source: Company data

Conclusion: Still constructive on Korea's defense sector

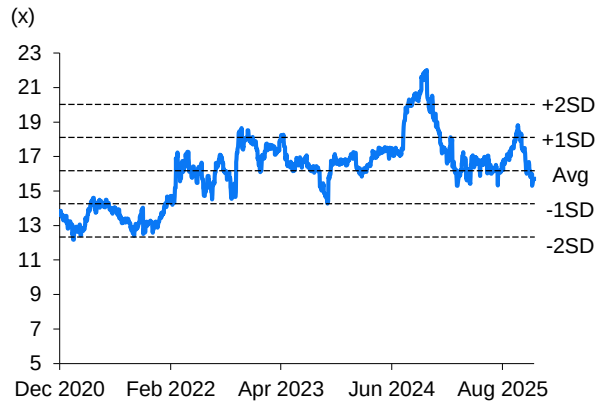
Valuation from a financial market perspective remains a risk

As discussed above, an end to the war in Ukraine is unlikely to materially undermine the operating outlook for Korean defense companies. Global defense budgets should continue to trend higher, driven by rearmament among countries adjacent to regions of geopolitical tension, while the pool of suppliers capable of delivering required systems remains limited. It is unrealistic to assume that the end of the Russia-Ukraine war would immediately usher in global stability. Concerns over fundamentals therefore appear premature.

From a share price and valuation perspective, however, the impact of a potential end of the war cannot be dismissed entirely. The recent pullback in European defense stocks, driven by speculation around a possible end to the conflict, represents a headwind. European defense names have rallied sharply this year on the back of surging weapons demand related to the war, as well as expectations of EU policy support for the bloc's defense industry. This rerating in Europe had positive spillover effects for Korean defense stocks, as European valuations diverged from those of US defense peers, where concerns over the defense budget had weighed on multiples.

Historically, one of the most frequently cited bear arguments against Korean defense stocks centered on valuation comparisons with major US defense contractors. Some investors were uncomfortable with Korean defense names trading at a premium to world-leading US defense large caps. However, as European defense valuations moved into premium territory relative to US peers—and as markets increasingly accepted a structural divergence between US and non-US defense valuations—these valuation concerns receded. As a result, elevated valuations for Korean defense companies became easier to justify than in the past.

Lockheed Martin: 1-year-forward P/E



Source: Bloomberg

Rheinmetall: 1-year-forward P/E

Source: Bloomberg

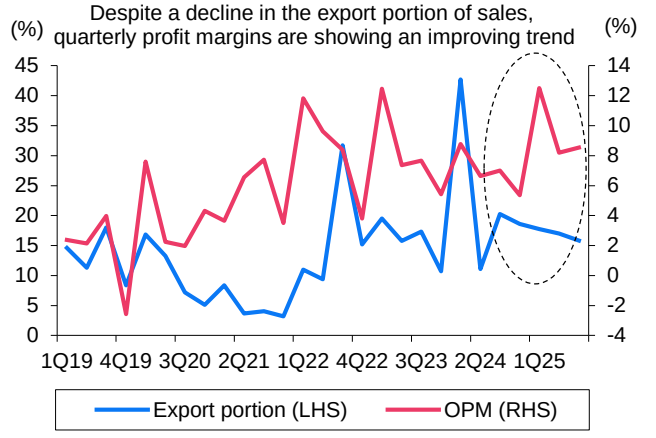
Why we remain upbeat despite valuation concerns

With European defense companies delivering strong profit growth, the market shifting its valuation basis to 2026, and share prices correcting, questions have emerged around the valuation of Korean defense firms. Nevertheless, we find two reasons to remain constructive on Korean defense stocks, believing valuation concerns can be addressed.

First, Korean defense companies retain strong growth potential. Massive backlogs and ongoing capacity expansion programs should support above-industry growth. It is also important to note that Korean defense companies remain relatively small players in the global market: even modest gains in market share can translate into a meaningful expansion of the profit pool. More broadly, during industry booms, followers often grow faster than leaders. Ultimately, valuation is a function of earnings growth. Within Europe, valuation dispersion among peers is largely explained by differences in growth expectations. Rheinmetall—now widely viewed as a symbol of high valuation—trades at a premium to its European peers on expectations of faster growth within Europe, underpinned by large-scale capex and limited exposure to the US defense budget.

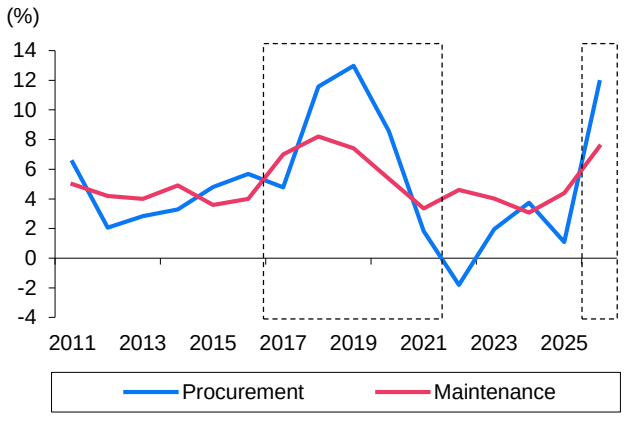
Improving profitability in domestic projects is another supportive factor. Export-led top-line growth is easing the fixed-cost burden associated with the Korean defense sector's domestic projects. At LIG Nex1, which has relatively high domestic exposure, operating margins have improved recently despite a decline in the export share of sales, indicating better profitability in domestic programs. The defense budget—critical to domestic profitability—is also supportive. The recently finalized defense budget for 2026 includes a 7.5% y-y increase, the largest since 2008, alongside an 11.9% y-y increase in the force improvement program, the largest since 2019, which is primarily allocated to weapons procurement. If budget expansion translates into structurally higher margins for defense contractors, upward revisions to long-term earnings estimates are possible.

LIG Nex1: Export portion of sales vs operating margin



Source: Company data

Defense budget growth



Source: Ministry of Defense

Second, Korea's defense sector has distinct attributes within the domestic equity market. It is one of the few manufacturing subsectors relatively insulated from macroeconomic swings and external geopolitical risks such as US tariffs. The sector also offers high visibility for medium-term sales and earnings growth, supported by large backlogs. One reason defense stocks outperformed in 2025 was that investors seeking to avoid external uncertainties increased exposure to industrials. As a result, investor preference within the domestic market became increasingly concentrated in the industrials sector.

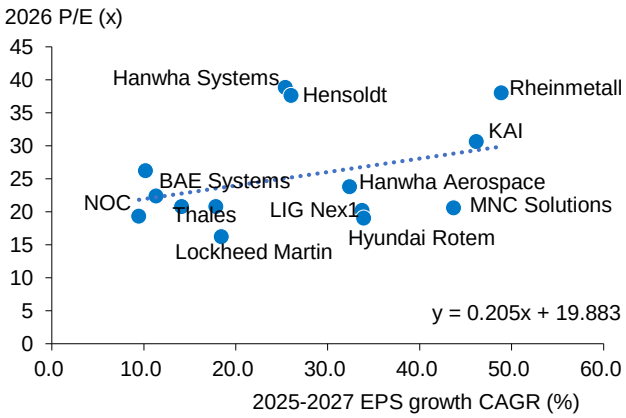
Following the recent correction, defense sector valuations no longer appear excessive relative to Korean industrial large caps. Korean defense stocks are now trading at around 22x 2026 P/E, at a discount to the Kospi 200 Industrials average of 27x and the KRX Machinery & Equipment average of 33x. With external uncertainties unresolved and no clear rationale for major defense companies to trade at a discount within industrials, we believe share prices have already reflected a substantial portion of valuation-related concerns.

Global defense companies: Rankings

Rank	Company	Country	Defense sales (USDb)	Defense portion (%)
1	**Lockheed Martin**	US	68.4	96
2	**Raytheon Technologies**	US	43.5	54
3	**CASIC**	China	38.7	32
4	**Northrop Grumman**	US	36.6	89
5	**General Dynamics**	US	36.5	76
6	**BAE Systems**	UK	32.3	96
7	**Boeing**	US	31.8	48
8	**CSSC**	China	22.4	20
9	**L3Harris Technologies**	US	17.0	80
10	**Thales**	France	15.9	72
…				
18	**Rheinmetall AG**	Germany	8.2	78
22	**Hanwha Group**	Korea	6.8	17
…				
53	**LIG Nex1**	Korea	2.4	100
62	**KAI**	Korea	2.1	21

Note: 2024 figures
Source: Defense News

Global defense names: EPS growth vs P/E multiple



Note: Based on Bloomberg consensus
Source: Bloomberg

Korean industrial sectors: P/E multiples

(x)	Defense	Shipbuilding	Power equipment	Kospi 200 Industrials	KRX Machinery & Equipment	Kospi Machinery & Equipment
2025E	31.6	35.3	43.5	35.1	54.2	58.4
2026E	22.0	22.4	31.1	26.8	33.0	38.1
2027E	17.0	17.8	23.8	20.5	24.6	31.6

Note: Calculating by summing market cap and net profit estimates for defense, shipbuilding, and power equipment sector;
As of Dec 12
Source: Samsung Securities estimates, FnGuide

COMPANY UPDATE

2025. 12. 30

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LIG Nex1 (079550)

Three positives the market is underestimating

- LIG Nex1's share price has been lackluster, reflecting management's conservative forward guidance and leaving the stock trading at a discount to local peers. We believe the current valuation fails to reflect three key positives.
- Specifically, the market is underpricing: 1) a sharp increase in backlogged orders; 2) capacity expansion that improves the conversion of backlog into revenue; and 3) upside to margins on domestic projects, which still account for a meaningful share of sales.

WHAT'S THE STORY?

(§The Korean version of this report was published on Dec 15)

Higher order backlog: LIG Nex1's backlog has risen 17% ytd to KRW23.4t as of end-3Q, representing 2.8x growth versus end-2021 and roughly 6x expected 2025 revenue. Importantly, more than half of the backlog is export-related. Compared with peers, the company has a larger proportion of security-sensitive programs that limit external disclosure, and export contracts typically entail longer lags between order intake and revenue recognition. As a result, the market has yet to fully internalize the scale of backlog expansion and the strength of export momentum.

Domestic project profitability upside: LIG Nex1 maintains a higher domestic revenue mix than peers, and domestic programs have historically delivered lower margins than exports. That said, domestic margins have improved relative to the past, likely reflecting: 1) better project-level economics; and/or 2) a lower fixed-cost burden driven by export-led top-line growth. Under either explanation, the recent improvement appears more structural than temporary—though investor sentiment toward domestic profitability remains cautious. In addition, Korea's steadily rising defense budget—an important determinant of long-term domestic profitability—provides further support.

SUMMARY FINANCIAL DATA

(Continued on the next page)

	2024	2025E	2026E	2027E
Revenue (KRWb)	3,276	4,034	4,813	5,589
Operating profit (KRWb)	230	354	501	644
Net profit (adj) (KRWb)	222	300	418	537
EPS (adj) (KRW)	10,078	13,632	19,006	24,387
EPS (adj) growth (% y-y)	26.7	35.3	39.4	28.3
EBITDA margin (%)	9.4	11.8	13.3	14.1
ROE (%)	19.6	22.5	25.8	26.6
P/E (adj) (x)	38.0	28.1	20.2	15.7
P/B (x)	7.0	5.8	4.7	3.7
EV/EBITDA (x)	26.7	17.3	12.3	9.5
Dividend yield (%)	0.6	0.7	0.9	1.0

Source: Company data, Samsung Securities estimates

AT A GLANCE

BUY

Target price	KRW595,000	55.4%
Current price	KRW383,000	
Market cap	KRW8.4t/USD6.6b	
Shares (float)	22,000,000 (60.9%)	
52-week high/low	KRW631,000/KRW194,500	
Avg daily trading value (60-day)	KRW74.3b/ USD48.5m	

ONE-YEAR PERFORMANCE

	1M	6M	12M
LIG Nex1 (%)	-5.1	-16.7	94.3
Vs Kospi (%pts)	-5.5	-41.7	15.7

KEY CHANGES

(KRW)	New	Old	Diff
Recommend.	BUY	BUY	
Target price	595,000	595,000	0.0%
2025E EPS	13,632	13,632	0.0%
2026E EPS	19,006	19,006	0.0%

SAMSUNG vs THE STREET

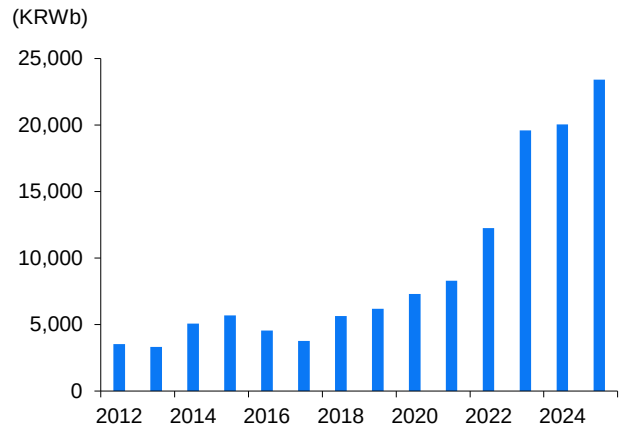
No of estimates	17
Target price	600,412
Recommendation	3.9

※ Rating: 4 < → BUY, 3 = HOLD, 2 > → SELL

Continued capacity expansion: LIG Nex1 is sustaining elevated capex to support future growth. In 2024, it acquired the Seongnam Sejong Research Institute site to develop an R&D facility, with total investment, including land, amounting to KRW385.3b. It has also announced plans to invest KRW374b through 2029 in the Gumi facility it acquired in the same year. By comparison, average annual tangible asset investment over the past decade, including 2024, was below KRW100b. This step-up in capex materially enhances the credibility and visibility of a scenario in which the current backlog translates into sustained medium-term revenue growth.

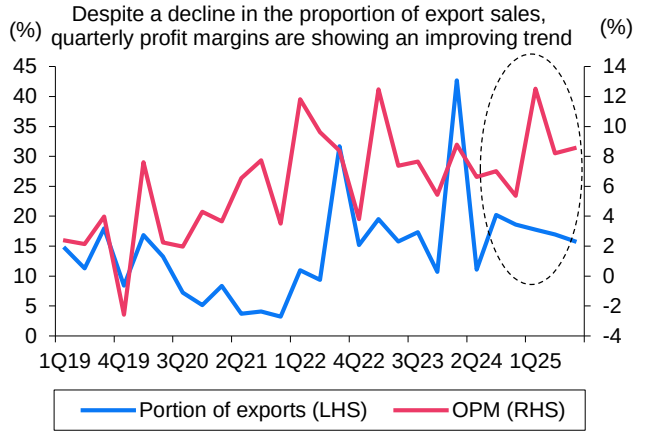
What the market is missing: LIG Nex1's share price fell sharply after the 3Q earnings release, largely due to conservative guidance. In our view, the pullback reflects management caution rather than any deterioration in the company's medium- to long-term growth trajectory. Following the decline, the stock is now trading at a meaningfully wider discount to peers. Given the company's relatively straightforward, defense pure-play business model, a persistent valuation discount is difficult to justify on fundamentals alone. We believe the market has yet to fully reflect the three positives outlined above, largely due to overly cautious guidance.

LIG Nex1: Orderbook



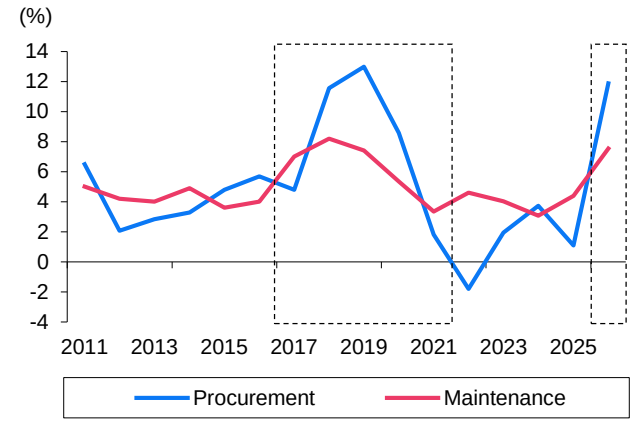
Source: Company data

LIG Nex1: Export portion of revenue vs operating margin



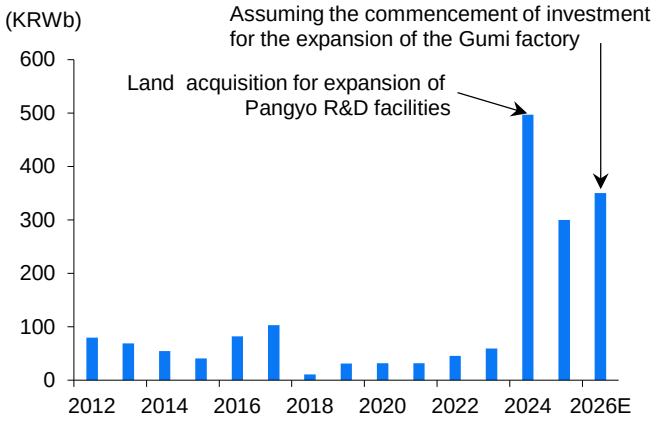
Source: Company data

Defense budget growth



Source: Ministry of National Defense

LIG Nex1: Capex



Source: Company data, Samsung Securities estimates

Income statement

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Sales	**2,309**	**3,276**	**4,034**	**4,813**	**5,589**
Cost of goods sold	1,962	2,824	3,407	3,997	4,590
Gross profit	**347**	**453**	**628**	**816**	**1,000**
Gross margin (%)	15.0	13.8	15.6	16.9	17.9
SG&A expenses	160	223	274	314	356
Operating profit	**186**	**230**	**354**	**501**	**644**
Operating margin (%)	8.1	7.0	8.8	10.4	11.5
Non-operating gains (losses)	**-1**	**-20**	**10**	**28**	**35**
Financial profit	10	28	36	29	37
Financial costs	15	85	16	12	12
Equity-method gains (losses)	0	0	0	0	0
Other	4	36	-10	10	10
Pre-tax profit	**185**	**210**	**364**	**529**	**679**
Taxes	10	-7	73	111	143
Effective tax rate (%)	5.4	-3.3	20.0	21.0	21.0
Profit from continuing operations	175	217	291	418	537
Profit from discontinued operations	0	0	0	0	0
Net profit	**175**	**217**	**291**	**418**	**537**
Net margin (%)	7.6	6.6	7.2	8.7	9.6
Net profit (controlling interests)	175	222	300	418	537
Net profit (non-controlling interests)	0	-5	-9	0	0
EBITDA	255	309	475	640	789
EBITDA margin (%)	11.1	9.4	11.8	13.3	14.1
EPS (parent-based) (KRW)	7,953	10,078	13,632	19,006	24,387
EPS (consolidated) (KRW)	7,953	9,848	13,235	19,006	24,387
Adjusted EPS (KRW)*	7,953	10,078	13,632	19,006	24,387

Balance sheet

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Current assets	**2,536**	**3,895**	**4,712**	**5,912**	**7,318**
Cash & equivalents	445	547	580	899	1,354
Accounts receivable	276	364	475	593	689
Inventories	229	364	332	396	459
Other current assets	1,585	2,620	3,325	4,025	4,815
Fixed assets	**1,280**	**2,231**	**2,222**	**2,231**	**2,236**
Investment assets	59	80	72	73	73
Tangible assets	894	1,371	1,378	1,359	1,335
Intangible assets	188	629	614	641	670
Other long-term assets	139	150	158	158	158
Total assets	**3,816**	**6,125**	**6,934**	**8,143**	**9,554**
Current liabilities	**2,651**	**4,617**	**5,143**	**5,909**	**6,723**
Accounts payable	128	364	448	534	621
Short-term debt	108	163	150	100	60
Other current liabilities	2,415	4,090	4,545	5,274	6,042
Long-term liabilities	**113**	**271**	**313**	**415**	**557**
Bonds & long-term debt	20	188	208	233	313
Other long-term liabilities	93	83	105	182	244
Total liabilities	**2,763**	**4,888**	**5,456**	**6,324**	**7,279**
Owners of parent equity	**1,052**	**1,211**	**1,451**	**1,792**	**2,247**
Capital stock	110	110	110	110	110
Capital surplus	142	142	142	142	142
Retained earnings	678	907	1,148	1,489	1,944
Other	122	51	51	51	51
Non-controlling interests' equity	**0**	**27**	**27**	**27**	**27**
Total equity	**1,052**	**1,237**	**1,478**	**1,819**	**2,274**
Net debt	-263	-176	-201	-541	-947

Cash flow statement

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Cash flow from operations	**467**	**952**	**183**	**485**	**574**
Net profit	175	217	291	418	537
Non-cash profit and expenses	79	130	137	136	144
Depreciation	59	68	74	79	84
Amortization	10	11	37	37	38
Other	10	51	25	21	21
Changes in A/L from operating activities	213	605	-246	-69	-106
Cash flow from investments	**-97**	**-978**	**-80**	**-60**	**-60**
Change in tangible assets	-59	-497	-80	-60	-60
Change in financial assets	1	-4	0	0	0
Other	-39	-477	0	0	0
Cash flow from financing	**-177**	**122**	**-70**	**-106**	**-59**
Change in debt	-68	186	7	-25	40
Change in equity	0	0	0	0	0
Dividends	-42	-52	-59	-77	-81
Other	-66	-12	-18	-4	-18
Change in cash	193	102	33	319	455
Cash at beginning of year	253	445	547	580	899
Cash at end of year	445	547	580	899	1,354
Gross cash flow	**254**	**347**	**428**	**555**	**680**
Free cash flow	**408**	**455**	**103**	**425**	**514**

Financial ratios

Year-end Dec 31	2023	2024	2025E	2026E	2027E
Growth (%)					
Sales	4.0	41.9	23.1	19.3	16.1
Operating profit	4.1	23.3	54.0	41.8	28.4
Net profit	42.3	23.8	34.4	43.6	28.3
Adjusted EPS**	42.3	26.7	35.3	39.4	28.3
Per-share data (KRW)					
EPS (parent-based)	7,953	10,078	13,632	19,006	24,387
EPS (consolidated)	7,953	9,848	13,235	19,006	24,387
Adjusted EPS**	7,953	10,078	13,632	19,006	24,387
BVPS	47,835	55,031	65,963	81,469	102,156
DPS (common)	1,950	2,400	2,700	3,500	3,700
Valuations (x)					
P/E***	48.2	38.0	28.1	20.2	15.7
P/B***	8.0	7.0	5.8	4.7	3.7
EV/EBITDA	32.0	26.7	17.3	12.3	9.5
Ratios (%)					
ROE	17.6	19.6	22.5	25.8	26.6
ROA	5.1	4.5	4.6	5.5	6.1
ROIC	18.5	24.2	23.5	0.0	0.0
Payout ratio	24.5	23.8	19.8	18.4	15.2
Dividend yield (common)	0.5	0.6	0.7	0.9	1.0
Net debt to equity	-25.0	-14.2	-13.6	-29.7	-41.6
Interest coverage (x)	19.3	19.2	22.2	43.3	54.5

Note: *Excluding one-off items;
**Fully diluted, excluding one-off items;
***From companies subject to equity-method valuation

Source: Company data, Samsung Securities estimates

COMPANY UPDATE

2025. 12. 30

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Hanwha Aerospace (012450)

Three pillars supporting sustained growth

- Sharp improvements in share price and operating performance have fueled investor skepticism about the durability of incremental growth.
- We, however, believe the growth runway remains intact, supported by: 1) a virtuous circle driven by an expanding installed base of flagship platforms; 2) a large backlog with a structurally higher export mix; and 3) ongoing capacity expansion focused on the core business.
- Recent equity fundraising has further enhanced Hanwha Aerospace's financial flexibility, improving its leverage metrics and increasing its capacity for additional investments.

WHAT'S THE STORY?

(§The Korean version of this report was published on Dec 15)

Expanding K9 user base—installed-base flywheel aids long-term growth: In 2025, Hanwha Aerospace signed a K9 self-propelled howitzer export contract with Vietnam, increasing the number of operator countries to 11. A broader user base is structurally supportive of long-term growth through three channels.

First, a larger installed base raises the likelihood of repeat orders and supports a longer-duration MRO and aftermarket revenue stream. Second, export volume growth enables economies of scale, reinforcing cost competitiveness and creating a self-reinforcing cycle in future bids. Third, adoption by multiple countries lowers the "validation hurdle" for new export customers, potentially streamlining evaluation processes and accelerating procurement decisions.

(Continued on the next page)

AT A GLANCE

BUY

Target price	KRW1,300,000	35.3%
Current price	KRW961,000	
Market cap	KRW49.6t/USD31.3b	
Shares (float)	51,563,401 (62.6%)	
52-week high/low	KRW1,107,000/KRW300,335	
Avg daily trading value (60-day)	KRW205.0b/ USD131.4m	

ONE-YEAR PERFORMANCE

	1M	6M	12M
Hanwha Aerospace (%)	0.1	0.8	213.3
Vs Kospi (%pts)	-0.3	-29.3	86.6

KEY CHANGES

(KRW)	New	Old	Diff
Recommend.	BUY	BUY	
Target price	1,300,000	1,300,000	0.0%
2025E EPS	26,370	26,370	0.0%
2026E EPS	40,179	40,179	0.0%

SAMSUNG vs THE STREET

No of estimates	19
Target price	1,334,474
Recommendation	4.0

※ Rating: 4 < → BUY, 3 = HOLD, 2 > → SELL

SUMMARY FINANCIAL DATA

(KRWb)	2024	2025E	2026E	2027E
Revenue	11,240	26,764	30,133	32,556
Operating profit	1,732	3,410	4,399	4,916
Net profit (adj)	2,299	1,360	2,072	2,383
EPS (adj) (KRW)	50,436	26,370	40,179	46,219
EPS (adj) growth (% y-y)	212.4	-47.7	52.4	15.0
EBITDA margin (%)	18.4	14.5	16.3	16.7
ROE (%)	53.9	18.5	19.6	19.1
P/E (adj) (x)	19.1	36.4	23.9	20.8
P/B (x)	8.8	5.1	4.3	3.7
EV/EBITDA (x)	30.5	15.3	11.5	9.7
Dividend yield (%)	0.4	0.5	0.6	0.7

Source: Company data, Samsung Securities estimates

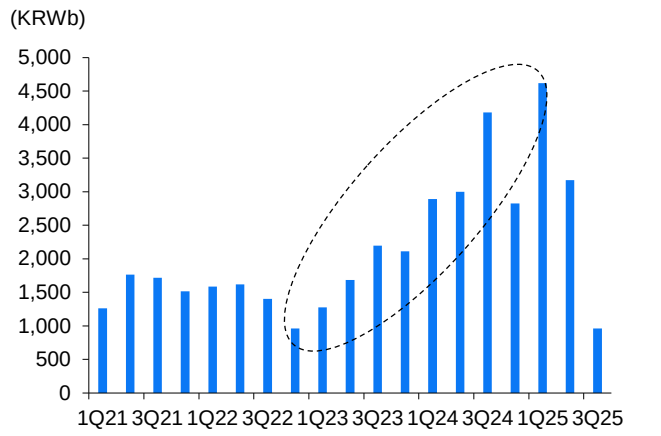
Larger backlog, structurally higher export mix—visibility on growth and profitability: The backlog at Hanwha Aerospace's land systems business has expanded to approximately KRW31t, equivalent to around 3.7x annual revenue. Additional export opportunities (*eg*, to Sweden and Saudi Arabia) remain in progress, implying further upside to top-line growth and supporting the sustainability of the current export revenue mix (around 60%).

Profitability visibility also remains favorable. Poland's Phase 1 execution contracts have not yet been fully completed, and a KRW5.7t Phase 2 execution contract balance remains in backlog. Given the still-substantial remaining volume under the Poland programs, we see scope for the company to sustain its elevated margin profile for longer than the market may assume.

Ongoing capacity expansion focused on the core business: Hanwha Aerospace continues to invest aggressively in capacity expansion, and we note that a meaningful portion of this is directed toward its core defense business rather than broader group initiatives. The company plans KRW670b of investment to expand propellant production capacity, targeting completion in 2026, and media reports suggest it is also reviewing construction of a propellant plant in the US. Manufacturing investments are underway in Australia and Romania, alongside efforts to establish a production JV in Poland with local partner WB Group. Expanding local production footprints should mitigate concerns around Europe's policy emphasis on intra-regional defense suppliers by improving procurement eligibility and competitiveness.

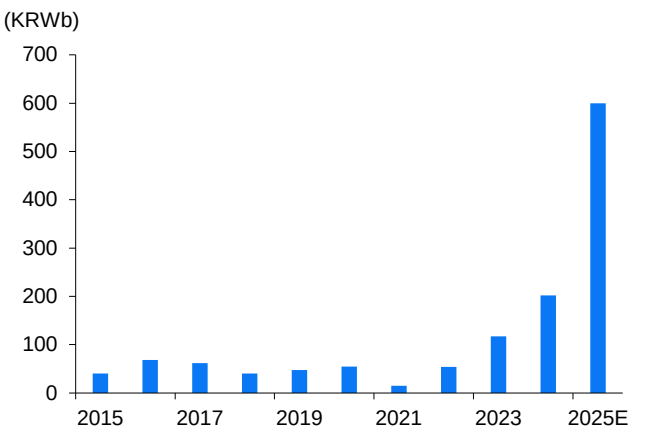
While aggressive investment could pressure financial ratios, a recent equity raise has materially strengthened the balance sheet; net debt (parent basis) fell from KRW4.6t at end-1Q to KRW0.96t, providing greater flexibility for incremental capex while maintaining financial stability.

Hanwha Aerospace: Net debt trends (parent basis)



Source: Company data

Hanwha Aerospace: Capex trends (parent basis)



Source: Company data, Samsung Securities estimates

Income statement

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Sales	**9,359**	**11,240**	**26,764**	**30,133**	**32,556**
Cost of goods sold	7,221	8,370	21,354	23,507	25,232
Gross profit	**2,138**	**2,870**	**5,411**	**6,626**	**7,324**
Gross margin (%)	22.8	25.5	20.2	22.0	22.5
SG&A expenses	1,447	1,138	2,001	2,227	2,407
Operating profit	**691**	**1,732**	**3,410**	**4,399**	**4,916**
Operating margin (%)	7.4	15.4	12.7	14.6	15.1
Non-operating gains (losses)	**524**	**966**	**-768**	**-260**	**-155**
Financial profit	1,145	374	914	552	351
Financial costs	398	495	1,280	770	494
Equity-method gains (losses)	16	105	0	0	0
Other	-239	982	-402	-41	-12
Pre-tax profit	**1,215**	**2,697**	**2,641**	**4,139**	**4,762**
Taxes	238	158	581	952	1,095
Effective tax rate (%)	19.6	5.8	22.0	23.0	23.0
Profit from continuing operations	977	2,511	2,060	3,187	3,666
Profit from discontinued operations	0	29	0	0	0
Net profit	**977**	**2,540**	**2,060**	**3,187**	**3,666**
Net margin (%)	10.4	22.6	7.7	10.6	11.3
Net profit (controlling interests)	818	2,299	1,360	2,072	2,383
Net profit (non-controlling interests)	159	241	700	1,116	1,283
EBITDA	1,030	2,063	3,875	4,907	5,452
EBITDA margin (%)	11.0	18.4	14.5	16.3	16.7
EPS (parent-based) (KRW)	16,147	50,436	26,370	40,179	46,219
EPS (consolidated) (KRW)	19,295	55,722	39,954	61,814	71,105
Adjusted EPS (KRW)*	16,147	50,436	26,370	40,179	46,219

Balance sheet

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Current assets	**9,192**	**22,868**	**26,669**	**31,234**	**36,388**
Cash & equivalents	1,806	2,968	3,995	6,384	9,530
Accounts receivable	2,034	8,509	4,033	4,541	4,906
Inventories	2,869	6,290	7,333	8,256	8,919
Other current assets	2,483	5,101	11,308	12,054	13,033
Fixed assets	**10,351**	**20,469**	**22,513**	**23,899**	**24,736**
Investment assets	3,942	2,416	2,534	2,548	2,561
Tangible assets	3,410	8,320	9,915	10,967	11,481
Intangible assets	2,203	7,744	8,075	8,396	8,706
Other long-term assets	795	1,988	1,988	1,988	1,988
Total assets	**19,543**	**43,337**	**49,183**	**55,133**	**61,124**
Current liabilities	**12,077**	**25,516**	**24,765**	**26,962**	**28,544**
Accounts payable	919	1,708	1,833	2,064	2,230
Short-term debt	1,374	5,153	3,200	3,000	2,800
Other current liabilities	9,784	18,655	19,732	21,898	23,514
Long-term liabilities	**2,782**	**6,456**	**8,339**	**10,330**	**12,691**
Bonds & long-term debt	1,401	4,165	3,975	3,715	3,715
Other long-term liabilities	1,381	2,292	4,364	6,615	8,976
Total liabilities	**14,859**	**31,973**	**33,104**	**37,292**	**41,235**
Owners of parent equity	**3,528**	**4,995**	**9,709**	**11,472**	**13,520**
Capital stock	266	240	270	270	270
Capital surplus	192	207	3,796	3,796	3,796
Retained earnings	2,627	4,747	5,848	7,611	9,659
Other	443	-198	-205	-205	-205
Non-controlling interests' equity	**1,156**	**6,369**	**6,369**	**6,369**	**6,369**
Total equity	**4,684**	**11,364**	**16,079**	**17,841**	**19,889**
Net debt	2,038	6,957	3,503	344	-3,155

Cash flow statement

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Cash flow from operations	**1,390**	**1,393**	**1,470**	**4,410**	**4,292**
Net profit	977	2,540	2,060	3,187	3,666
Non-cash profit and expenses	-49	-244	703	692	700
Depreciation	261	259	311	347	368
Amortization	78	72	154	161	167
Other	-388	-575	238	184	164
Changes in A/L from operating activities	462	-903	-1,294	531	-74
Cash flow from investments	**-3,029**	**-1,367**	**-1,919**	**-1,412**	**-895**
Change in tangible assets	-450	-577	-1,906	-1,398	-882
Change in financial assets	35	-897	-13	-14	-13
Other	-2,614	106	0	-0	0
Cash flow from financing	**368**	**1,066**	**1,476**	**-610**	**-250**
Change in debt	538	6,928	-2,143	-610	-250
Change in equity	-25	-10	3,619	0	0
Dividends	-51	-120	-258	-309	-335
Other	-94	-5,732	258	309	335
Change in cash	-1,263	1,161	1,027	2,389	3,147
Cash at beginning of year	3,070	1,806	2,968	3,995	6,384
Cash at end of year	1,806	2,968	3,995	6,384	9,530
Gross cash flow	**928**	**2,296**	**2,763**	**3,879**	**4,366**
Free cash flow	**937**	**815**	**-438**	**3,010**	**3,408**

Financial ratios

Year-end Dec 31	2023	2024	2025E	2026E	2027E
Growth (%)					
Sales	32.6	20.1	138.1	12.6	8.0
Operating profit	72.6	150.6	96.9	29.0	11.8
Net profit	566.6	160.0	-18.9	54.7	15.0
Adjusted EPS**	318.5	212.4	-47.7	52.4	15.0
Per-share data (KRW)					
EPS (parent-based)	16,147	50,436	26,370	40,179	46,219
EPS (consolidated)	19,295	55,722	39,954	61,814	71,105
Adjusted EPS**	16,147	50,436	26,370	40,179	46,219
BVPS	69,689	109,587	188,301	222,480	262,198
DPS (common)	1,800	3,500	5,000	6,000	6,500
Valuations (x)					
P/E***	59.5	19.1	36.4	23.9	20.8
P/B***	13.8	8.8	5.1	4.3	3.7
EV/EBITDA	51.2	30.5	15.3	11.5	9.7
Ratios (%)					
ROE	25.6	53.9	18.5	19.6	19.1
ROA	4.7	7.3	2.9	4.0	4.1
ROIC	12.9	15.0	13.5	15.3	16.4
Payout ratio	11.1	6.9	19.0	14.9	14.1
Dividend yield (common)	0.2	0.4	0.5	0.6	0.7
Net debt to equity	43.5	61.2	21.8	1.9	-15.9
Interest coverage (x)	4.1	7.1	7.4	12.5	14.8

Note: *Excluding one-off items;
**Fully diluted, excluding one-off items;
***From companies subject to equity-method valuation

Source: Company data, Samsung Securities estimates

COMPANY UPDATE

2025. 12. 30

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Hyundai Rotem (064350)

Multiple businesses but one growth engine

- Hyundai Rotem was previously viewed as a conglomerate due to its three heterogeneous business units. Today, however, investors can increasingly value the company primarily on its defense business.
- We expect robust earnings momentum at the defense unit and earnings stabilization at the non-defense businesses. As a result, the conglomerate discount historically applied to the company should gradually narrow. We reinstate coverage of Hyundai Rotem at BUY.

WHAT'S THE STORY?

(§The Korean version of this report was published on Dec 15)

Diverse operations but a simpler investment case: Hyundai Rotem operates across defense, rail, and plant businesses. Identifying direct comparables—either domestically or globally—with a similar business portfolio is challenging. This heterogeneity has historically been the reason for a conglomerate discount, but that dynamic is now changing. The defense unit has grown to account for the vast majority of consolidated earnings, while profitability at the non-defense units has stabilized. As a result, it is now feasible to estimate enterprise value primarily based on the defense business. We reinstate coverage of Hyundai Rotem with a BUY rating and 12-month target price of KRW280,000 (based on a sum-of-the-parts valuation).

(Continued on the next page)

AT A GLANCE

BUY

Target price	KRW280,000	50.2%
Current price	**KRW186,400**	
Market cap	KRW20.3t/USD13.9b	
Shares (float)	109,142,293 (66.2%)	
52-week high/low	KRW244,500/KRW48,350	
Avg daily trading value (60-day)	KRW158.9b/ USD95.8m	

ONE-YEAR PERFORMANCE

	1M	6M	12M
Hyundai Rotem (%)	-4.8	3.7	275.4
Vs Kospi (%pts)	-5.2	-27.3	123.6

KEY CHANGES

(KRW)	New	Old	Diff
Recommend.	BUY		
Target price	280,000		
2025E EPS	6,964		
2026E EPS	9,788		

SAMSUNG vs THE STREET

No of estimates	17
Target price	296,647
Recommendation	4.0

※ Rating: 4 < → BUY, 3 = HOLD, 2 > → SELL

SUMMARY FINANCIAL DATA

(KRWb)	2024	2025E	2026E	2027E
Revenue	4,377	6,013	6,774	7,247
Operating profit	457	1,015	1,416	1,766
Net profit (controlling)	407	760	1,068	1,363
EPS (adj) (KRW)	3,728	6,964	9,788	12,486
EPS (adj) growth (% y-y)	152.7	86.8	40.6	27.6
EBITDA margin (%)	11.5	17.8	21.9	25.4
ROE (%)	21.8	31.8	33.0	31.3
P/E (adj) (x)	50.0	26.8	19.0	14.9
P/B (x)	9.9	7.4	5.5	4.1
EV/EBITDA (x)	39.5	17.9	12.2	9.2
Dividend yield (%)	0.1	0.3	0.4	0.5

Source: Company data, Samsung Securities estimates

Defense unit—Straightforward growth narrative: The defense business has secured a large order backlog, with more than 80% estimated to come from high-margin projects in Poland. This provides clear visibility on top-line growth and margin expansion as the backlog converts into revenue. The company is also in discussions regarding additional overseas export contracts.

Non-defense units—Earnings stabilizing: The gradual stabilization of profitability at the rail and plant businesses is a meaningful positive. While these units are not major profit contributors, they are unlikely to incur the large-scale losses seen in the past. The incentive to accept low-priced orders has declined materially, given the strong earnings contribution from the defense business. Historically, loss-making orders were often accepted to cover fixed costs or secure advance payments. However, Hyundai Rotem's consolidated earnings and balance sheet have strengthened significantly, reducing such pressures. Competition in the rail industry could ease amid US-led efforts to contain China, whose CRRC is the world's largest rolling stock manufacturer. In the plant business, we believe downsizing of operations and increased revenue contributions from group affiliates helps limit downside.

Summary: Three heterogeneous businesses

Disconnected units

Hyundai Rotem's revenue mix comprises defense (defense solutions; 56%), rail (rail solutions; 35%), and plant (eco plant 9%). Relative to other listed large-cap peers, its business mix is unusually diverse. For comparison, LIG Nex1 generates the bulk of its revenue from defense. Korea Aerospace Industries generates some sales from civil aircraft parts, but aerospace and defense are typically classified as a single sector globally. Hanwha Aerospace owns multiple subsidiaries and functions as an intermediate holding company, but its non-defense businesses are directly or indirectly related to defense and largely structured as subsidiaries, allowing investors to isolate defense value more easily.

By contrast, Hyundai Rotem's rail, defense, and plant businesses differ materially in end markets and cycle characteristics. This structure has historically weighed on valuation, as markets tend to favor simpler business models.

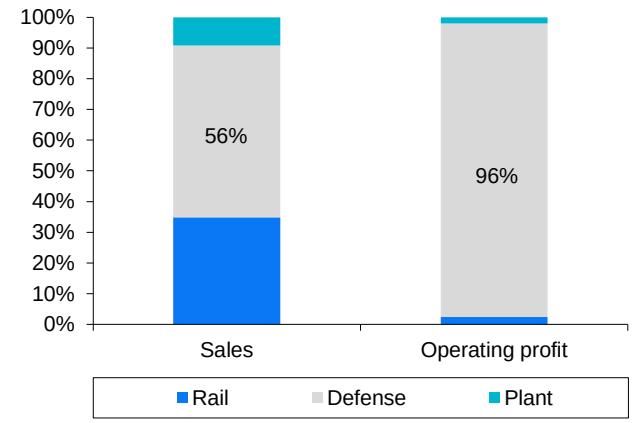
Straightforward growth story and simpler valuation

Hyundai Rotem's growth narrative is becoming simpler amid the defense sector's rerating. Defense revenue accounted for 31% of total revenue in 2021, surpassed rail revenue in 2023, and rose to 54% in 2024.

In 2025, we expect the defense business to account for a massive 96% of operating profit. While the rail and plant businesses are not meaningful profit contributors, they are unlikely to incur the large-scale losses seen in the past. With non-defense segments stabilizing around breakeven, investors can increasingly value Hyundai Rotem primarily on defense earnings, supporting a gradual reduction in the conglomerate discount.

The defense growth story itself is straightforward: 1) the company holds a sizable order backlog; 2) a large portion of the backlog comprises high-margin export projects; and 3) the backlog should drive revenue and profit growth for several years. When viewed in isolation, the defense business is relatively easy to assess, given its limited number of flagship products. Accordingly, the valuation discount historically applied to Hyundai Rotem should gradually be eliminated. We reinstate coverage of Hyundai Rotem with a target price of KRW280,000. Our sum-of-the-parts valuation applies a 21x EV/EBITDA multiple to the defense segment—consistent with the multiple we use for Hanwha Aerospace's land defense business, and broadly in line with European land defense peers. This implies 28.6x 2026 P/E, in line with the average for Korea's industrials sector and at a discount to the machinery sector.

Rotem: Sales and operating profit contributions, by unit



Source: Hyundai Rotem

Valuation

(KRWb)	Calculation	2026E EBITDA	Multiple (x)	EV
Revenue	(A)	1,461		29,542
Defense*		1,361	21.0*	28,585
Rail**		68	9.3**	636
Plant***		32	10.1***	321
Net debt (end-3Q25)	(B)			958
EV	(C=A-B)			30,500
Float ('000)	(D)			109,142
Target price (KRW)	(C/D)			280,000

Note: *Average at which domestic and European peer group are trading;
**Average at which overseas rivals are trading
***Average at which Korean EPC companies are trading
Source: Samsung Securities

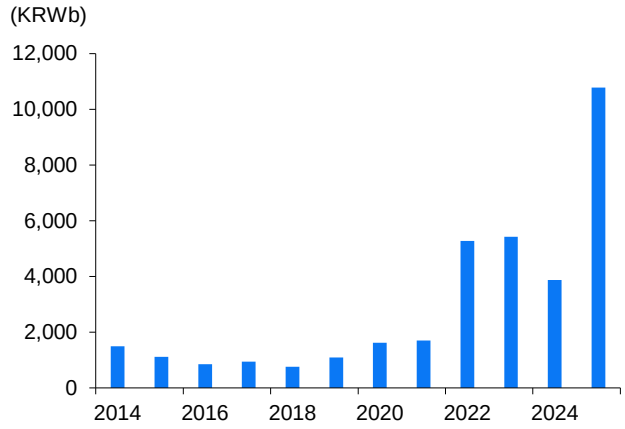
Defense business: Growth narrative straightforward

Expanding order backlog and rising ASP

At end-3Q, Hyundai Rotem's defense order backlog stood at approximately KRW10.8t. The backlog had surged from KRW1.6t in 2021 to KRW5.3t in 2022 following the company's success in securing its first Polish export contract. Subsequent delays to the second Polish contract and the lack of additional large export wins reduced the backlog to around KRW2.5t in 2025. But this trend reversed in Aug 2025, when Hyundai Rotem secured the second Polish export contract, valued at roughly KRW9t—well above prior expectations—driving a sharp rebound in total backlog.

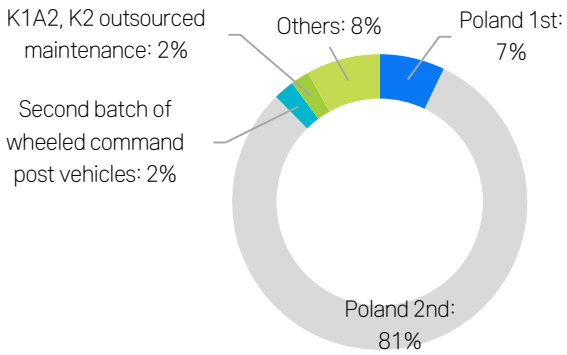
The current backlog is highly concentrated, with around 88% estimated to originate from Polish projects. The second contract alone, which features materially higher unit prices than the first, accounts for roughly 80% of total backlog. Investment to convert backlog into revenue is ongoing. Based on the publicly disclosed delivery schedule for the Polish projects, domestic production volumes, and capacity expansion by key suppliers, K2 tank production capacity will likely need to roughly double over time. With the firm's defense backlog equivalent to around 3x 2025 defense sales and dominated by high-priced export contracts, we see strong visibility for sustained top-line growth and margin expansion.

Defense division: Orderbook



Source: Company data, Samsung Securities estimates

Defense division: Orderbook breakdown



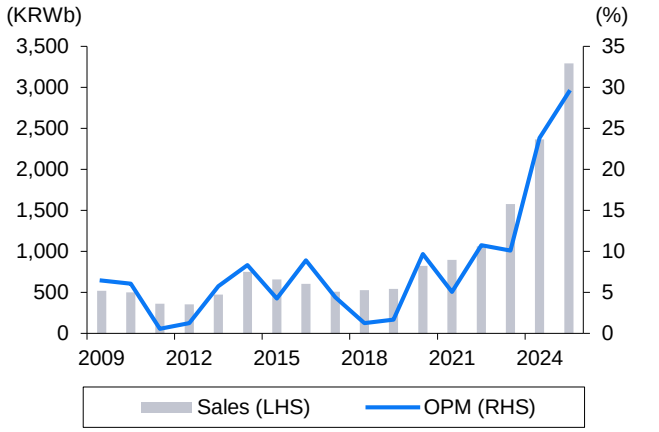
Note: As of end-3Q25
Source: Company data, Samsung Securities estimates

Poland exports and domestic K2 mass-production

	Size		Period	
	(Number)	(KRWb)	Start	End
Poland exports	980	n/a	2022	n/a
1st project	180	4,499	2022	2027
2nd project	180	8,981	2025	2033
Domestic K2 4th mass-production*	150		2024	2028

Note: * No formal contract signed yet but reflecting media reports
Source: Press, company data

Defense division: Sales and operating margin



Source: Company data, Samsung Securities estimates

Ample potential for additional orders

The concentrated product mix—primarily the K2 main battle tank—represents a double-edged sword. If Hyundai Rotem continues to secure high-margin export orders, the simplicity of its backlog is supportive for valuation. If, however, current projects prove to be one-off in nature, valuation upside would be limited. Ultimately, a full removal of the valuation discount to peers requires conviction in the company's ability to secure additional high-profit export orders.

Encouragingly, incremental export opportunities for the K2 appear robust. Most notably, Hyundai Rotem disclosed the signing of an MOU with Peru's Army Arsenal covering tanks and wheeled armored vehicles. According to media reports, Peru plans to procure 54 K2 tanks and 141 wheeled armored vehicles, with execution contracts expected by Jun 2026 and total order value estimated at KRW2.5t-3t. This would mark the K2's first entry into Latin America, diversifying export exposure and alleviating concerns over post-Poland profitability.

Moreover, under the 2022 framework agreement with Poland, total potential demand amounts to 980 tanks. Given that Phase 1 and Phase 2 orders each comprised 180 units, further follow-on orders likely remain.

We acknowledge rising protectionism and local-industry preferences, as illustrated by Norway's selection of Germany's Leopard 2A7 despite the K2's strong performance. That said, the global tank market is characterized by surging demand and constrained supply. Even assuming heightened competition, demand appears to exceed Hyundai Rotem's production capacity. Skepticism around the future relevance of tanks—raised following the emergence of advanced weapons systems—has reversed in the wake of the Russia-Ukraine war. Replacement of aging fleets, new adoption by countries that previously underinvested in armored vehicles and rising demand for high-performance tanks amid the proliferation of anti-tank missiles and drones are occurring simultaneously. Beyond Peru, countries such as Sweden, Romania, and Iraq are pursuing fleet replacement and modernization.

On the supply side, competition remains limited. Among modern tanks currently in production, credible peers are largely confined to Germany's Leopard 2 and the US Abrams SEP v3. While performance differences are not decisively skewed toward any single platform, the K2 is widely regarded as more cost-effective. Although pricing is not officially disclosed, market consensus suggests the K2 is materially cheaper, with some media citing prices more than 50% lower than peers. Its competitiveness is further underpinned by mass-production capability (and resultant shorter lead times). Defense media such as *Defense Romania* estimate Germany's annual tank output at around 60 units, vs Korea's roughly 100 units (with plans to double capacity). For countries seeking to secure large numbers of tanks quickly under budget constraints, the K2 represents one of the most viable options.

Tank comparison

	K2	Leopard 2	Abrams
Weight (tonne)	55	63-67	66-73
Speed (km/h)	70	68	70
Range (km)	450	550	390
Horsepower	1,500	1,500	1,500
Crew	3	4	4
Armament	120 mm 55 Smoothbore gun	120 mm 55 Smoothbore gun	120 mm 55 Smoothbore gun
Diving depth (m)	4.1	With towing equipment, 4m	1.98
Combat method	Auto	Manual	Manual
Completed	2007-2012	2010-2013	2017

Source: Press

Possible export projects (as mentioned in the media)

Country	Item	Media coverage
Sweden	K2 tank	Germany wins next-generation tank project; Challenges to replace aging tanks and secure additional orders
Peru	K2 tank, wheeled armored vehicles	Master agreement signed to supply 54 K2 tanks and 141 wheeled armored vehicles
Romania	K2 tank	US wins project phase 1; competes with US and Germany in phase 2
Iraq	K2 tank	Aged Abrams tank replacement program

Source: Press

Significance of improving profitability in non-defense businesses

Earnings at rail and plant units stabilizing

The gradual stabilization of profitability at the rail and plant businesses is a meaningful positive. The rail division recorded losses almost every year over 2014-2020, except 2016 and 2017. The plant business posted continuous losses from 2014 to 2019.

The root cause was aggressive low-price bidding. In the plant business, design changes drove cost overruns and required large provisioning, as initial contract prices failed to adequately reflect project risks. Contracts secured at low prices are inherently vulnerable to losses, even from minor delays or modest cost overruns. Similarly, losses at the rail business stemmed from: 1) low margins on domestic projects; 2) an aggressive bidding strategy aimed at securing new customers; and 3) intense price competition overseas from rapidly expanding Chinese players. The underlying reason to take such low-priced orders was the need to cover fixed costs amid declining sales.

Profitability at these two units has now begun to stabilize. This improvement reflects the completion of most low-priced orders, an improved cost structure following restructuring during the downturn, and a strategic shift away from high-risk contracts. A key driver of this turnaround is the positive spillover from the strong performance of the defense business. Rapid growth in the defense division has materially improved consolidated earnings and cash flow, reducing pressure from fixed costs and the risk of capital erosion from recurring losses. As cash flow has strengthened, the incentive to accept low-margin orders simply to secure advance payments has also waned.

Change appears sustainable

We do not believe the stabilization in non-defense earnings will prove temporary. Most low-priced contracts have been completed, restructuring during the downturn has enhanced cost structure, and management has taken a disciplined approach to avoiding loss-priced contracts. Notably, the plant business returned to profitability at revenue levels comparable to prior periods. Moreover, at end-2024, the rail business preemptively set aside provisioning for potential future losses. As the current backlog translates into revenue, the likelihood of large-scale losses appears limited.

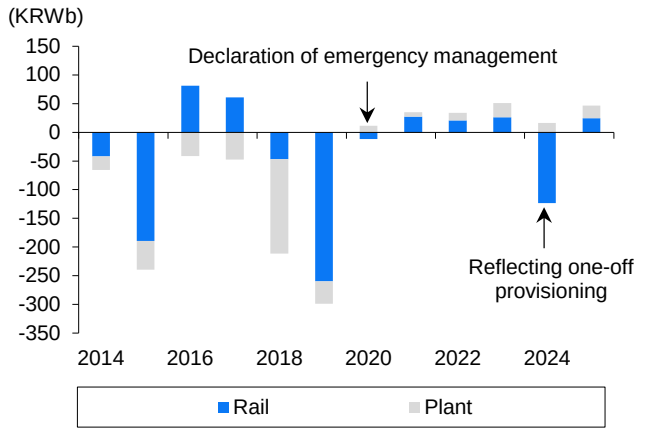
Incentives to pursue new low-margin contracts are also low, given expectations for sustained strength in defense earnings and robust cash flow. The company enjoyed a turn to a net cash position in 2023 and held nearly KRW1t in net cash as of 3Q25, supported by defense earnings and advance payments.

Order momentum and backlog trends are also favorable. Rail order backlog has risen to KRW18t, up 2.4x from end-2022, driven by the signing of large export contracts. Even excluding positive spillover from the defense business, incentives to accept loss-making rail orders appear limited.

Over the longer term, competition in the rail industry could ease amid US-led efforts to contain China. China's CRRC is the world's largest rolling stock manufacturer. In Apr 2025, Israel's Ministry of Finance canceled CRRC's participation in the Jerusalem Light Rail Blue Line project at the final stage, citing the company's inclusion on a US Department of Defense blacklist. Similar dynamics have emerged in other industries, where restrictions on Chinese access to certain markets have benefited Korean suppliers—Korean power equipment makers in North America being a notable example.

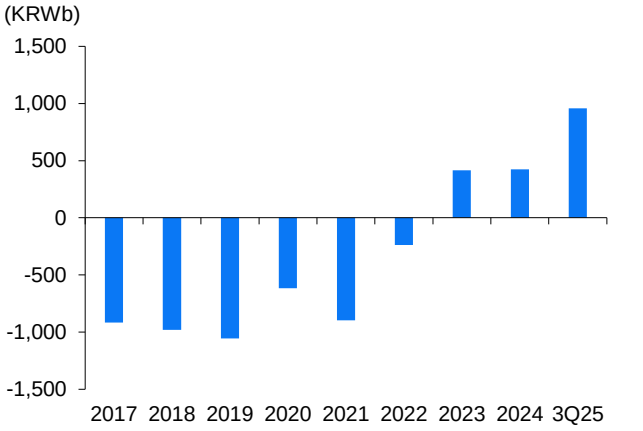
Hyundai Rotem is actively expanding in North America. In 2025, it secured LA Metro EMU and Boston double-deck coach contracts, and it completed construction of a rail electronics facility in California. Meanwhile, the company has been scaling down its plant business, with a growing share of revenue coming from group affiliates—customers that offer higher communication efficiency and execution visibility—thereby reducing the risk of significant losses.

Operating profit at rail and plant divisions



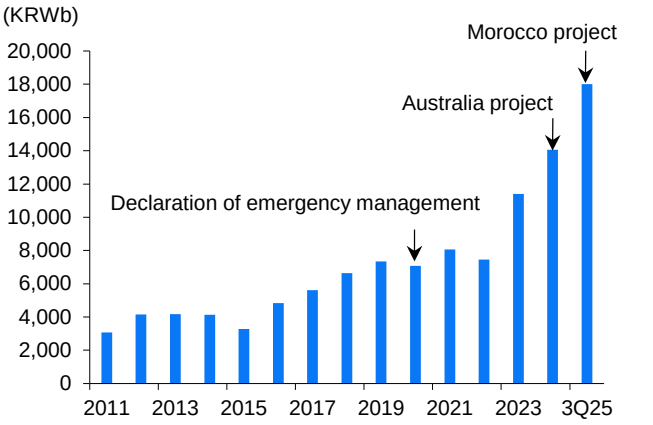
Source: Hyundai Rotem

Hyundai Rotem: Net cash



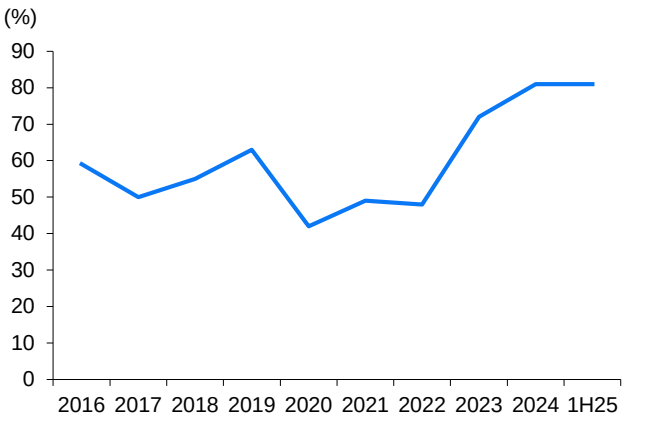
Source: Hyundai Rotem

Rail division: Orderbook



Source: Hyundai Rotem

Plant division: Captive portion of sales



Source: Hyundai Rotem

Income statement

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Sales	**3,587**	**4,377**	**6,013**	**6,774**	**7,247**
Cost of goods sold	3,123	3,548	4,537	4,853	4,946
Gross profit	**464**	**829**	**1,476**	**1,921**	**2,301**
Gross margin (%)	12.9	18.9	24.5	28.4	31.8
SG&A expenses	254	372	461	505	535
Operating profit	**210**	**457**	**1,015**	**1,416**	**1,766**
Operating margin (%)	5.9	10.4	16.9	20.9	24.4
Non-operating gains (losses)	**-29**	**53**	**-15**	**-11**	**27**
Financial profit	48	75	92	71	102
Financial costs	47	52	62	52	49
Equity-method gains (losses)	-0	-0	-0	-0	-0
Other	-29	30	-45	-30	-26
Pre-tax profit	**181**	**510**	**1,000**	**1,406**	**1,793**
Taxes	24	104	240	337	430
Effective tax rate (%)	13.3	20.5	24.0	24.0	24.0
Profit from continuing operations	157	405	760	1,068	1,363
Profit from discontinued operations	0	0	0	0	0
Net profit	**157**	**405**	**760**	**1,068**	**1,363**
Net margin (%)	4.4	9.3	12.6	15.8	18.8
Net profit (controlling interests)	161	407	760	1,068	1,363
Net profit (non-controlling interests)	-4	-2	0	0	0
EBITDA	250	504	1,069	1,482	1,843
EBITDA margin (%)	7.0	11.5	17.8	21.9	25.4
EPS (parent-based) (KRW)	1,475	3,728	6,964	9,788	12,486
EPS (consolidated) (KRW)	1,436	3,713	6,964	9,788	12,486
Adjusted EPS (KRW)*	1,475	3,728	6,964	9,788	12,486

Balance sheet

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Current assets	**3,690**	**3,686**	**4,880**	**6,267**	**7,698**
Cash & equivalents	396	472	1,255	2,249	3,481
Accounts receivable	339	909	1,170	1,318	1,410
Inventories	269	316	379	427	457
Other current assets	2,686	1,989	2,077	2,273	2,351
Fixed assets	**1,551**	**1,599**	**1,714**	**1,916**	**2,125**
Investment assets	54	55	55	55	55
Tangible assets	1,234	1,292	1,386	1,570	1,765
Intangible assets	92	104	125	143	158
Other long-term assets	170	148	148	148	148
Total assets	**5,241**	**5,285**	**6,594**	**8,183**	**9,823**
Current liabilities	**3,205**	**3,020**	**3,480**	**3,868**	**4,038**
Accounts payable	465	432	577	650	695
Short-term debt	83	60	80	100	60
Other current liabilities	2,657	2,527	2,824	3,118	3,283
Long-term liabilities	**390**	**256**	**407**	**627**	**844**
Bonds & long-term debt	246	3	11	18	28
Other long-term liabilities	144	254	397	610	817
Total liabilities	**3,595**	**3,276**	**3,887**	**4,495**	**4,882**
Owners of parent equity	**1,680**	**2,045**	**2,743**	**3,724**	**4,977**
Capital stock	546	546	546	546	546
Capital surplus	520	520	520	520	520
Retained earnings	317	689	1,383	2,364	3,618
Other	297	291	294	294	294
Non-controlling interests' equity	**-33**	**-36**	**-36**	**-36**	**-36**
Total equity	**1,647**	**2,009**	**2,707**	**3,688**	**4,941**
Net debt	-417	-424	-1,190	-2,160	-3,397

Cash flow statement

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Cash flow from operations	**734**	**142**	**927**	**1,233**	**1,551**
Net profit	157	405	760	1,068	1,363
Non-cash profit and expenses	140	278	128	188	203
Depreciation	27	33	38	46	55
Amortization	13	14	16	20	22
Other	100	231	74	122	125
Changes in A/L from operating activities	437	-541	39	-23	-14
Cash flow from investments	**-270**	**233**	**-132**	**-230**	**-250**
Change in tangible assets	-54	-81	-132	-230	-250
Change in financial assets	-204	314	0	0	0
Other	-12	-1	0	0	0
Cash flow from financing	**-576**	**-300**	**-12**	**-8**	**-70**
Change in debt	-561	-244	-12	-8	-70
Change in equity	0	0	0	0	0
Dividends	0	-11	-65	-87	-109
Other	-15	-45	65	87	109
Change in cash	-110	76	783	995	1,231
Cash at beginning of year	506	396	472	1,255	2,249
Cash at end of year	396	472	1,255	2,249	3,481
Gross cash flow	**297**	**684**	**888**	**1,256**	**1,566**
Free cash flow	**680**	**61**	**795**	**1,003**	**1,301**

Financial ratios

Year-end Dec 31	2023	2024	2025E	2026E	2027E
Growth (%)					
Sales	13.4	22.0	37.4	12.7	7.0
Operating profit	42.4	117.4	122.3	39.5	24.7
Net profit	-19.4	158.5	87.5	40.6	27.6
Adjusted EPS**	-18.6	152.7	86.8	40.6	27.6
Per-share data (KRW)					
EPS (parent-based)	1,475	3,728	6,964	9,788	12,486
EPS (consolidated)	1,436	3,713	6,964	9,788	12,486
Adjusted EPS**	1,475	3,728	6,964	9,788	12,486
BVPS	15,391	18,737	25,129	34,117	45,602
DPS (common)	100	200	600	800	1,000
Valuations (x)					
P/E***	126.3	50.0	26.8	19.0	14.9
P/B***	12.1	9.9	7.4	5.5	4.1
EV/EBITDA	79.6	39.5	17.9	12.2	9.2
Ratios (%)					
ROE	10.1	21.8	31.8	33.0	31.3
ROA	3.2	7.7	12.8	14.5	15.1
ROIC	10.8	22.7	41.7	54.4	61.0
Payout ratio	6.8	5.4	8.6	8.2	8.0
Dividend yield (common)	0.1	0.1	0.3	0.4	0.5
Net debt to equity	-25.3	-21.1	-44.0	-58.6	-68.7
Interest coverage (x)	7.3	27.5	86.1	124.1	177.1

Note: *Excluding one-off items;
**Fully diluted, excluding one-off items;
***From companies subject to equity-method valuation

Source: Company data, Samsung Securities estimates

COMPANY UPDATE

2025. 12. 30

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Scan to go to
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Korea Aerospace Industries

(047810)

2026—inflection point finally in sight

- Export orders for finished aircraft have fallen short of plan. However, the deferral of several projects originally expected in 2025 has effectively shifted momentum into 2026. We expect 2026 to mark the start of an earnings recovery at Korea Aerospace Industries (KAI).
- Long-term growth visibility remains high. That said, for investors seeking a new entry point, it would be more prudent to wait for a period when KAI's valuation premium to peers narrows.

AT A GLANCE

BUY

Target price	KRW130,000	12.9%
Current price	**KRW109,600**	
Market cap	KRW10.7t/USD7.4b	
Shares (float)	97,475,107 (72.5%)	
52-week high/low	KRW115,000/KRW49,850	
Avg daily trading value (60-day)	KRW77.8b/ USD48.6m	

ONE-YEAR PERFORMANCE

	1M	6M	12M
Korea Aerospace Industries (%)	7.7	24.7	98.2
Vs Kospi (%pts)	7.6	-11.8	17.8

KEY CHANGES

(KRW)	New	Old	Diff
Recommend.	BUY	BUY	
Target price	130,000	120,000	8.3%
2025E EPS	2,211	2,211	0.0%
2026E EPS	3,832	3,832	0.0%

SAMSUNG vs THE STREET

No of estimates	16
Target price	130,750
Recommendation	3.9

※ Rating: 4 < → BUY, 3 = HOLD, 2 > → SELL

WHAT'S THE STORY?

(§The Korean version of this report was published on Dec 15)

Deferred orders building a richer pipeline: Over 1Q-3Q, Korea Aerospace Industries (KAI) secured KRW1.1t in finished-aircraft export orders. While this exceeds full-year 2024 levels (KRW180b), it represents only 31% of the full-year target set earlier this year, as many projects under discussion—including the Philippines project—have been deferred. The delay in Middle East orders for rotary-wing aircrafts is a particular letdown. Importantly, however, these projects have not been lost to failed bids or cancellations but have simply been rescheduled. As a result, the forward order pipeline is effectively accumulating rather than deteriorating. Looking to 2026, Malaysia is likely to place a second tranche order for the FA-50 light attack aircraft. As this is not expected to go through a competitive tender, there is a high probability of KAI signing the deal. Tender procedures are expected to progress for an Egypt project and commence for the US Navy trainer program. Of course, the Egypt and US projects will be put up for competition , and while these may not lead to contracts within 2026, related news flow should remain supportive for sentiment.

(Continued on the next page)

SUMMARY FINANCIAL DATA

(KRWb)	2024	2025E	2026E	2027E
Revenue	3,634	3,902	5,248	6,267
Operating profit	241	315	496	621
Net profit (adj)	172	216	374	460
EPS (adj) (KRW)	1,765	2,211	3,832	4,724
EPS (adj) growth (% y-y)	-23.2	25.3	73.3	23.3
EBITDA margin (%)	9.5	11.8	13.0	13.0
ROE (%)	10.4	12.1	18.8	20.0
P/E (adj) (x)	65.2	52.0	30.0	24.4
P/B (x)	6.6	6.1	5.3	4.5
EV/EBITDA (x)	35.2	26.3	17.8	14.7
Dividend yield (%)	0.4	0.6	0.9	1.0

Source: Company data, Samsung Securities estimates

Earnings rebound likely from 2026: Earnings rebound likely from 2026: Earnings are also likely to reach an inflection point in 2026. Domestically, LAH deliveries should increase materially, and KF-21 mass production is expected to begin contributing meaningfully to revenue. On the export side, revenue recognition related to the Poland and Malaysia programs is set to accelerate. We expect the sales growth to dilute fixed costs and lift margins. In addition, the commercial aircraft parts business is entering a recovery phase.

Wait for valuation pressure to ease: We raise our target price to KRW130,000, based on the KRX Machinery & Equipment sector's average 2026E P/E of 33x. With order intake and earnings momentum set to resume, KAI has little fundamental justification to trade at a discount to the machinery sector. However, the stock is trading at a meaningful premium to domestic defense peers. This reflects heightened export expectations linked to recent Middle East diplomatic developments, supply-demand distortions in certain peer stocks subject to investment warnings or watchlists, and stronger investor preference for the space sector. Historically, KAI has often commanded a premium given its exposure to advanced weapons, which were viewed as offering superior growth relative to conventional weapons. However, recent conflicts (in which weapons are actually deployed) have prompted a reassessment of growth prospects for conventional defense systems. In addition, the prolonged CEO vacancy adds near-term uncertainty. While KAI's long-term growth potential remains intact, we believe a more prudent approach is to wait for either: 1) a narrowing of the valuation gap versus peers; or 2) greater clarity on long-term strategy under new leadership.

Income statement

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Sales	**3,819**	**3,634**	**3,902**	**5,248**	**6,267**
Cost of goods sold	3,355	3,152	3,279	4,360	5,186
Gross profit	**464**	**481**	**623**	**888**	**1,081**
Gross margin (%)	12.1	13.3	16.0	16.9	17.3
SG&A expenses	216	241	308	392	460
Operating profit	**248**	**241**	**315**	**496**	**621**
Operating margin (%)	6.5	6.6	8.1	9.4	9.9
Non-operating gains (losses)	**21**	**-44**	**-46**	**-11**	**-23**
Financial profit	112	121	144	87	44
Financial costs	88	144	152	96	65
Equity-method gains (losses)	0	-2	-2	-2	-2
Other	-4	-18	-35	-0	0
Pre-tax profit	**269**	**197**	**269**	**485**	**598**
Taxes	47	26	54	112	138
Effective tax rate (%)	17.6	13.3	20.0	23.0	23.0
Profit from continuing operations	221	171	216	374	460
Profit from discontinued operations	0	0	0	0	0
Net profit	**221**	**171**	**216**	**374**	**460**
Net margin (%)	5.8	4.7	5.5	7.1	7.3
Net profit (controlling interests)	224	172	216	374	460
Net profit (non-controlling interests)	-3	-1	0	0	0
EBITDA	369	345	461	683	813
EBITDA margin (%)	9.6	9.5	11.8	13.0	13.0
EPS (parent-based) (KRW)	2,298	1,765	2,211	3,832	4,724
EPS (consolidated) (KRW)	2,271	1,753	2,211	3,832	4,724
Adjusted EPS (KRW)*	2,298	1,765	2,211	3,832	4,724

Balance sheet

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Current assets	**4,681**	**5,439**	**5,854**	**7,857**	**9,546**
Cash & equivalents	658	115	139	164	344
Accounts receivable	347	399	374	503	601
Inventories	1,736	2,359	2,673	3,595	4,293
Other current assets	1,939	2,567	2,668	3,595	4,308
Fixed assets	**2,459**	**2,587**	**2,776**	**3,069**	**3,372**
Investment assets	89	103	101	98	96
Tangible assets	815	913	1,065	1,227	1,380
Intangible assets	804	846	886	1,018	1,171
Other long-term assets	751	725	725	725	725
Total assets	**7,140**	**8,026**	**8,630**	**10,926**	**12,917**
Current liabilities	**4,400**	**4,915**	**5,140**	**6,776**	**7,976**
Accounts payable	353	504	535	719	859
Short-term debt	21	414	400	410	380
Other current liabilities	4,026	3,997	4,206	5,647	6,737
Long-term liabilities	**1,119**	**1,384**	**1,616**	**2,000**	**2,448**
Bonds & long-term debt	208	593	623	673	713
Other long-term liabilities	911	791	993	1,327	1,735
Total liabilities	**5,520**	**6,298**	**6,756**	**8,775**	**10,424**
Owners of parent equity	**1,597**	**1,706**	**1,853**	**2,129**	**2,472**
Capital stock	487	487	487	487	487
Capital surplus	128	128	128	128	128
Retained earnings	1,003	1,111	1,258	1,534	1,878
Other	-21	-21	-21	-21	-21
Non-controlling interests' equity	**23**	**21**	**21**	**21**	**21**
Total equity	**1,620**	**1,727**	**1,874**	**2,150**	**2,494**
Net debt	-156	916	903	929	740

Cash flow statement

Year-end Dec 31 (KRWb)	2023	2024	2025E	2026E	2027E
Cash flow from operations	**-700**	**-728**	**251**	**228**	**433**
Net profit	221	171	216	374	460
Non-cash profit and expenses	296	267	177	197	232
Depreciation	91	82	91	100	110
Amortization	30	22	59	62	71
Other	175	163	27	35	51
Changes in A/L from operating activities	-1,218	-1,166	-142	-343	-260
Cash flow from investments	**-108**	**-189**	**-243**	**-263**	**-263**
Change in tangible assets	-78	-161	-243	-263	-263
Change in financial assets	40	102	0	0	0
Other	-71	-130	0	0	0
Cash flow from financing	**-546**	**369**	**16**	**60**	**10**
Change in debt	-516	436	16	60	10
Change in equity	0	0	0	0	0
Dividends	-24	-49	-68	-97	-117
Other	-6	-18	68	97	117
Change in cash	-1,366	-543	24	25	180
Cash at beginning of year	2,024	658	115	139	164
Cash at end of year	658	115	139	164	344
Gross cash flow	**517**	**438**	**393**	**571**	**693**
Free cash flow	**-778**	**-889**	**8**	**-36**	**170**

Financial ratios

Year-end Dec 31	2023	2024	2025E	2026E	2027E
Growth (%)					
Sales	37.0	-4.9	7.4	34.5	19.4
Operating profit	74.8	-2.7	30.9	57.4	25.2
Net profit	91.0	-22.8	26.1	73.3	23.3
Adjusted EPS**	89.1	-23.2	25.3	73.3	23.3
Per-share data (KRW)					
EPS (parent-based)	2,298	1,765	2,211	3,832	4,724
EPS (consolidated)	2,271	1,753	2,211	3,832	4,724
Adjusted EPS**	2,298	1,765	2,211	3,832	4,724
BVPS	16,388	17,500	19,009	21,841	25,365
DPS (common)	500	500	700	1,000	1,200
Valuations (x)					
P/E***	50.1	65.2	52.0	30.0	24.4
P/B***	7.0	6.6	6.1	5.3	4.5
EV/EBITDA	30.0	35.2	26.3	17.8	14.7
Ratios (%)					
ROE	14.8	10.4	12.1	18.8	20.0
ROA	3.0	2.3	2.6	3.8	3.9
ROIC	15.1	8.2	7.9	10.4	11.2
Payout ratio	21.8	28.3	31.7	26.1	25.4
Dividend yield (common)	0.4	0.4	0.6	0.9	1.0
Net debt to equity	-9.6	53.0	48.2	43.2	29.7
Interest coverage (x)	8.5	7.2	6.6	11.5	13.9

Note: *Excluding one-off items;
**Fully diluted, excluding one-off items;
***From companies subject to equity-method valuation

Source: Company data, Samsung Securities estimates

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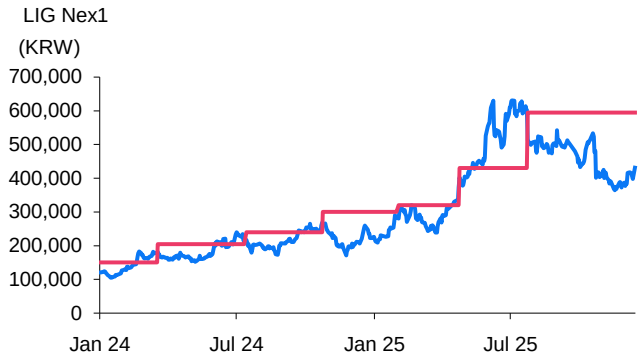
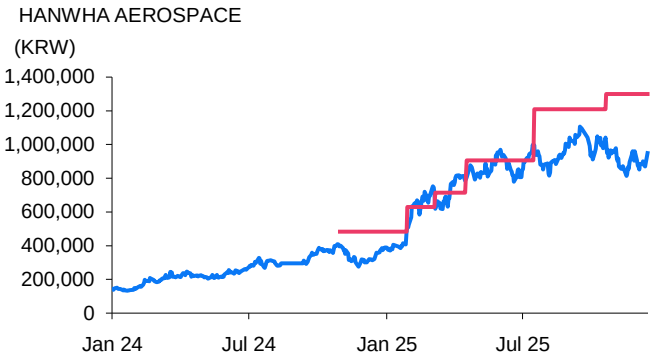
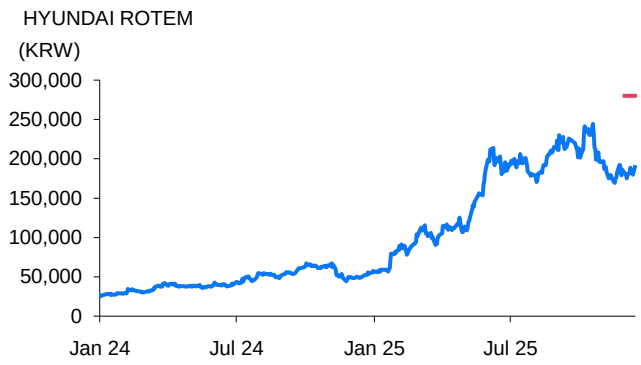
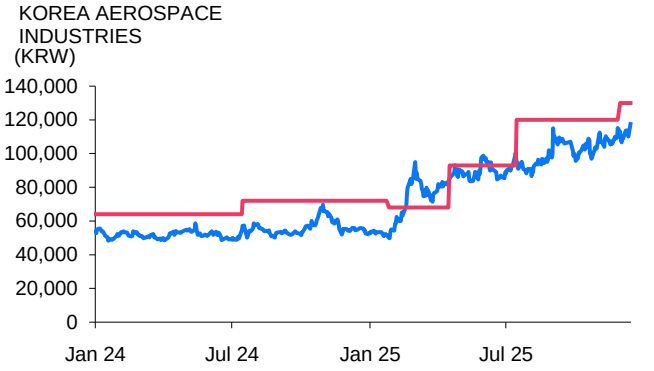
Target price changes in past two years









Rating changes over past two years (adjusted share prices)

LIG Nex1								
Date	2023/12/11	2024/4/2	7/29	11/8	2025/2/17	5/9	8/8	11/7
Recommendation	BUY	BUY	BUY	BUY	BUY	BUY	HOLD	BUY
Target price (KRW)	150000	205000	240000	300000	320000	430000	595000	595000
Gap* (average)	-8.24	-10.44	-9.45	-25.01	-10.10	21.59	-17.12	
(max or min)**	22.20	16.83	12.08	-3.33	16.41	46.74	-8.91	

HANWHA AEROSPACE							
Date	2024/11/14	2025/2/12	3/21	5/2	5/23	7/31	11/4
Recommendation	BUY	BUY	HOLD	BUY	BUY	BUY	BUY
Target price (KRW)	482506	630212	713912	905929	905929	1210000	1300000
Gap* (average)	-26.78	4.57	2.22	-8.44	-2.38	-20.34	
(max or min)**	1.63	19.37	14.48	-3.26	10.16	-8.51	

HYUNDAI ROTEM	
Date	2025/12/15
Recommendation	BUY
Target price (KRW)	280000
Gap* (average)	
(max or min)**	

KOREA AEROSPACE INDUSTRIES						
Date	2023/11/8	2024/7/30	2025/2/10	5/2	7/30	12/15
Recommendation	BUY	BUY	BUY	BUY	BUY	BUY
Target price (KRW)	64000	72000	68000	93000	120000	130000
Gap* (average)	-20.28	-22.50	9.65	-3.39	-15.63	
(max or min)**	-8.44	-3.19	39.71	8.06	-4.08	

Note: * [(average, maximum, or minimum share price over duration of target price minus target price) / target price] x 100%
** Maximum/minimum share price if new target is higher/lower than market close on the business day prior to target price change

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Industry

OVERWEIGHT	Expected to outperform market by 5% or more within 12 months
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BUY(83.5%)·HOLD(16.5%)·SELL(0%)

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