April 12, 2010

Asia Tire Sector

Kicking the tires: structural shift in rubber S/D negative

Goldman Sachs

Adding Hankook, Sumitomo Rubber to Sell; bearish on tires

We remain bearish on Asian tire stocks and downgrade Hankook Tire (000240.KS) and Sumitomo Rubber (5110.T) to Sell from Neutral while adding Hankook to our Conviction List. We also **reiterate our Sell ratings (Conviction List) on Bridgestone (5108.T) and Cheng Shin Rubber (2105.TW).**

Rubber near record high, margin deterioration inevitable

Rubber recently broke one of the longest records in commodity history by topping its all-time high of US$3.5/kg after almost 60 years. The upward trend in the natural rubber price is growing more pronounced due to tight supply/demand, with the price rising to US$3.8/kg (up 2.5X yoy) in early April. Rubber supply/demand is likely to remain tight for some time given production concerns in rubber-producing countries and rising demand from China, India, and the rest of emerging Asia, which account for nearly 70% of demand. **We raise our natural rubber price forecasts to US$3.4/kg for 2010 and US$3.6/kg for 2011**, but expect the pass-on to tire prices to be insufficient to offset margin deterioration.

But earnings expectations (and valuations) remain high

Natural rubber accounts for a third of tire materials costs and as such has the largest impact on earnings. Tire makers need to raise prices by 5% to offset the impact of a 10% rise in all materials. But passing on higher costs to consumers may very well prove to be difficult for two reasons: (1) a **slow recovery in developed market replacement tires**, and (2) **vicious competition in emerging markets**. Aggressive hikes could also dampen the demand recovery. In line with this, **we lower our earnings estimates for tire companies**; on average, our estimates are around 20% below consensus. We believe that market expectations are too high; and the sector is not pricing in all the risks.

Rise in rubber prices could be structural

There is a **risk that the rise in rubber prices is more structural** due to competing economics of alternative agribusinesses such as palm oil and changes in demand in India and China. Thus while there could be seasonal decline in rubber prices later in the year, longer term **we expect rubber prices to remain higher than in the past**. Moreover, tire makers may be less able than in the past to pass on these rising costs. The markets could thus come to view the tire sector as more cyclical, and less defensive.

12-MONTH TARGET PRICE AND RATING CHANGES

	Ticker	New Rating	Price 8-Apr-2010	New TP (Local curr.)	Old TP (Local curr.)	Upside/ Downside
Yokohama Rubber	5101.T	**Neutral**	439	**410**	430	-6.6%
Bridgestone	5108.T	**Sell***	1,534	**1,350**	1,430	-12.0%
Sumitomo Rubber	5110.T	**Sell**	827	**730**	750	-11.7%
Hankook Tire	000240.KS	**Sell***	22,250	**17,000**	22,000	-23.6%
Cheng Shin Rubber	2105.TW	**Sell***	68	**55**	55	-18.9%

Note: * Conviction List.
Source: Company data, Goldman Sachs Research estimates.

NATURAL RUBBER HIT NEW RECORD HIGH , RAISING ASSUMPTIONS TO $3.4/KG IN 2010

Rubber price f'casts, US$/kg

	CY2008	CY2009	CY2010	CY2011
New GSE	**2.6**	**1.9**	**3.4**	**3.6**
Old GSE			*3.1*	*3.2*

Source: SICOM.

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Kicking the tires (again); cutting forecasts, target prices, and ratings

Rubber recently broke one of the longest records in commodity history by topping its all-time high price of US$3.5/kg after nearly 60 years. We believe rubber may have entered a new cycle of long-term supply/demand imbalance resulting from structural changes. We do not think tire makers, which account for roughly 80% of rubber demand, will be able to fully pass through higher rubber costs as the replacement demand recovery has been slow in developed economies and competition is heating up in emerging economies. We raise our rubber price assumptions and lower our earnings estimates for tire makers. We maintain our bearish stance on Asian tire stocks, and downgrade Hankook Tire (000240.KS) to Sell (Conviction List) and Sumitomo Rubber (5110.T) to Sell. We reiterate our Sell ratings on Bridgestone (5108.T) and Cheng Shin Rubber (2105.TW) and keep both on our Conviction List.

Downgrade Hankook to Sell (CL), Sumitomo Rubber to Sell; reiterate Sell ratings (CL) on Bridgestone, Cheng Shin Rubber

We see long-term tightness in supply keeping rubber prices at elevated levels and raise our natural rubber price assumptions to US$3.40/kg from US$3.10/kg for 2010 and to US$3.60/kg from US$3.20/kg for 2011. The cost increases are not limited to natural rubber; **other costs – such as synthetic rubber, carbon black and steel tire cords – are all rising quickly.** Based on the upward revisions to our input price assumptions, we lower our tire maker earnings estimates and 12-month target prices.

Our FY2010 earnings estimates are roughly 20% below Bloomberg consensus, on average, leading us to think that the markets have yet to factor in all the cost increases. **Sector valuations are still on the rich side, and as we expect a decline in longer-term returns, we think the shares could decline further.**

Our new price targets imply 23.6% potential downside for Hankook and 11.7% potential downside for Sumitomo Rubber; we downgrade both stocks to Sell from Neutral and add Hankook to our Conviction List. We reiterate our Sell ratings on Bridgestone (12% potential downside) and Cheng Shin Rubber (18.9% potential downside) and keep both on our Conviction List. We revise down our estimates for Yokohama Rubber but maintain our Neutral rating on the stock due to limited downside of 7% to our new target price.

Our valuation methodology (and ratings system) values these stocks relative to each covering analyst's regional coverage group.

Exhibit 1: Downgrade Hankook, Sumitomo Rubber to Sell (Hankook onto CL), reiterate Sell (CL) on Bridgestone and Cheng Shin Rubber

Asia tire subsector 12-month price targets and earnings estimates (new vs. old)

	Ticker	New Rating	Old Rating
Yokohama Rubber	5101.T	**Neutral**	Neutral
Bridgestone	5108.T	**Sell***	Sell*
Sumitomo Rubber	5110.T	**Sell**	Neutral
Hankook Tire	000240.KS	**Sell***	Neutral
Cheng Shin Rubber	2105.TW	**Sell***	Sell*

	Ticker	Price 8-Apr-2010	New TP (Local curr.)	Old TP (Local curr.)	Upside/ Downside	Implied valuation (2010) P/E (X)	Implied valuation (2010) P/B (X)	Current valuation (2010) P/E (X)	Current valuation (2010) P/B (X)
Yokohama Rubber	5101.T	439	**410**	430	-6.6%	**19.1**	**0.88**	20.4	0.94
Bridgestone	5108.T	1,534	**1,350**	1,430	-12.0%	**34.6**	**0.96**	18.4	1.09
Sumitomo Rubber	5110.T	827	**730**	750	-11.7%	**16.2**	**0.98**	12.2	1.11
Hankook Tire	000240.KS	22,250	**17,000**	22,000	-23.6%	**9.3**	**1.13**	9.2	1.48
Cheng Shin Rubber	2105.TW	68	**55**	55	-18.9%	**10.6**	**2.19**	13.1	2.70

Note: * Conviction List. Target price methodologies: P/B-ROE correlation for Cheng Shin Rubber and the three Japanese tire makers; below-mid-cycle P/B multiple for Hankook Tire. Common risks: materials price, tire prices, replacement tire shipments.

Source: Company data, Goldman Sachs Research estimates.

Rubber price hits 60-year high, signaling possible structural change

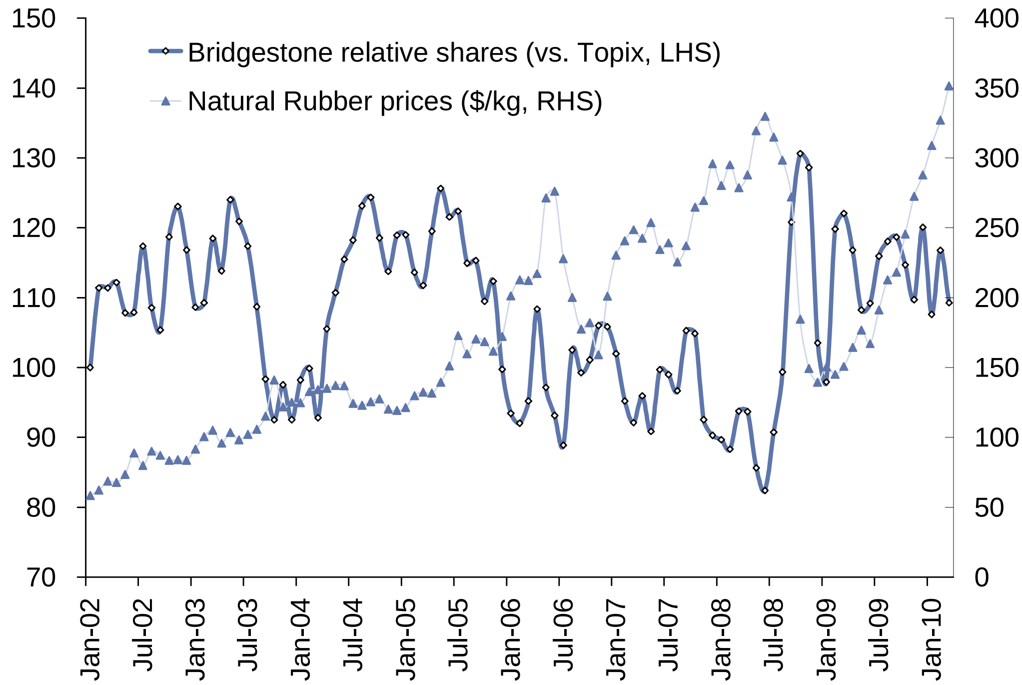
We do not believe this is just a short-term bubble. Several short-term market conditions have worked together to push natural rubber prices to a 60-year high. The natural rubber price appears to be at the start of a long-term, structural upward trend. As a result, we believe the tire subsector could become more of a commodity/cyclical sector affected by higher input prices and resulting deterioration in spreads, and viewed less as a defensive sector buoyed by consistent replacement tire demand.

Natural rubber 30% of tire input costs, so price rises pose significant earnings/share price risk

Natural rubber price spikes erode margins, so they have a major impact not only on tire maker earnings but also on share prices. The **stock market has a strong tendency to price in future changes in price spreads because product price hikes consistently lag input price rises.** Tire stocks significantly outperformed the auto sector and TOPIX in 2H2006 and in 2H2008, when natural rubber prices fell (see Exhibit 2).

Exhibit 2: Since 2005, Bridgestone has far outperformed TOPIX during input price corrections

Natural rubber price and Bridgestone's TOPIX-relative share price performance



Source: Datastream.

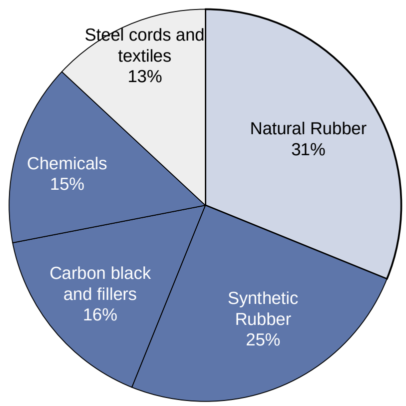
Near-term risks: Supply/demand tightening on production problems, rapidly growing demand in China

Two factors are contributing to the current tightness in rubber supply/demand:

- **Robust demand in China**, which accounts for 35% of global rubber consumption, and
- **Supply not keeping pace with demand due to production problems** (bad weather in Indonesia, drought in China).

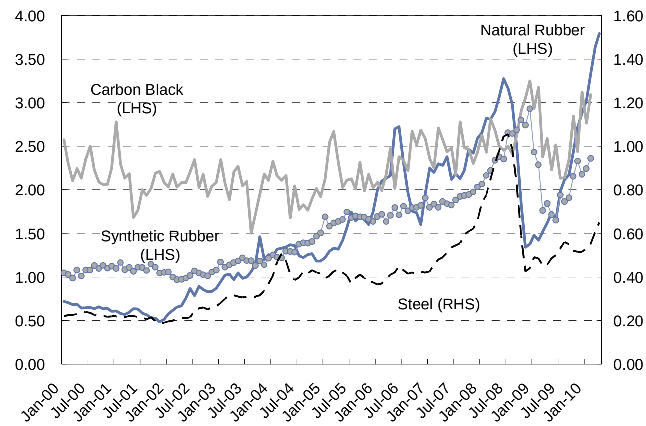
The natural rubber price has surged on tight supply/demand, reaching a new all-time high of US$3.80/kg at the beginning of April. With production poised to decline, it does not appear likely that supply/demand will ease sharply or that the price will correct significantly. We expect the natural rubber price to remain around US$3.40/kg even after the supply/demand balance stabilizes later in 2010. We raise our natural rubber price assumptions to US$3.40/kg from US$3.10/kg for 2010, and to US$3.60/kg from US$3.20/kg for 2011. When we look beyond other materials, commodities overall are strengthening its rising momentum in prices. We believe the hikes in tire materials to widen and pressure earnings (Exhibit 3, 4).

Exhibit 3: Natural rubber accounts for 1/3 of material
Tire raw material breakdown



Source: Michelin.

Exhibit 4: Materials aside from nat rubber also rising
Trends in raw material prices, US$/kg



Source: Datastream, Trade minisitry of Japan

While we expect a rise in prices, the recovery in tire demand in developed markets is proceeding at a slow pace. We believe tire makers have neither the ability nor the willingness to raise prices aggressively as passing higher input costs on into product prices could stifle demand. Instead, we think tire makers will be forced to absorb much of the current input price rise in the form of lower profit margins.

Medium/long-term risks: Growing Asia demand, while supply may fall on attractive alternatives

China, India, and other emerging markets in Asia account for roughly 70% of natural rubber consumption worldwide. That said, nearly half of the tires (the main use of rubber) made in these countries are for export, meaning the US, Europe, and other developed markets still account for over half of final demand.

In 2009, however, demand in China and India picked up markedly, and domestic demand has begun replacing exports as the growth driver. There is a risk that if growth in these countries follows a similar curve to that in developed markets, natural rubber consumption could increase several fold in China and India alone.

While rubber demand continues to show strong growth, major rubber-producing countries (Thailand, Indonesia, Malaysia, etc) are not actively engaged in efforts to increase supply substantially. While rising rubber prices should be a welcome development for rubber-producing countries, with their large agricultural populations, we expect them to adjust production in such a way as to maintain some supply tightness that balances supply growth with price rises.

Structurally, there is also the risk of palm oil, and other attractive alternatives that compete for plantation land, depressing rubber production in these countries. We thus see considerable risk of prolonged supply/demand tightness in rubber.

Bearish on tires. Tire stocks not factoring in margin deterioration

Based on upward revisions to our raw material cost assumptions, we lower our tire company earnings estimates and price targets. We downgrade Hankook Tire and Sumitomo Rubber to Sell from Neutral, and add Hankook to our Conviction List, where it joins Bridgestone and Cheng Shin Rubber. We see the tire subsector growing less defensive and more cyclical. We reiterate our bearish stance on the Asian tire subsector.

Margins to deteriorate given difficulty of offsetting higher input prices via price hikes

We see a very difficult environment continuing for tire makers given downside volume risk chiefly in developed countries and shrinking spreads due to sharply rising input prices and slowness in passing on these higher prices. With signs pointing toward a structural price rise for natural rubber, the core input, we expect profit margins to deteriorate.

Exhibit 5: Average price hikes of 5% or so needed to offset 10% input price rise
Input price and price rise sensitivity, FY2010 estimate basis

	Bridgestone		Sumitomo Rubber		Yokohama Rubber		Hankook Tire		Cheng Shin Rubber	
	5108		5110		5101		000240.KS		2105.TW	
	(mn yen)		(mn yen)		(mn yen)		(mn won)		(mn NT$)	
Rating	Sell*		Sell		Neutral		Sell*		Sell*	
Income statement		%		%		%		%		%
Sales	2,841,000	100%	585,000	100%	470,000	100%	5,161,700	100%	102,823	100%
Sales (mn USD basis)	*31,230*	*100%*	*6,431*	*100%*	*5,059*	*100%*	*4,516*	*100%*	*3,223*	*100%*
Operating profit	81,000	3%	26,400	5%	19,200	4%	611,300	12%	11,978	12%
Operating profit (mn USD basis)	*890*	*3%*	*290*	*5%*	*207*	*4%*	*535*	*12%*	*375*	*12%*
Sensitivity analysis										
Natural rubber consumption, MT	750,000-800,000	-	250,000	-	180,000	-	270,000	-	-	-
Earnings sensitivity (10c), mn USD	80	-	25	-	18	-	27	-	-	-
Earnings sensitivity (10c), %	9%	-	9%	-	9%	-	10%	-	-	-
Price hikes										
1% price hike, mn USD	259	-	53	-	39	-	45	-	32	-
% of hikes needed to offset 10% rise in RM overall	5.0%	-	5.1%	-	6.0%	-	4.6%	-	5.0%	-

Note: *Conviction List.

Source: Company data, Goldman Sachs Research estimates.

We estimate Asian tire makers would need to raise prices around 5% on average to offset the impact of a 10% average rise in input prices. The natural rubber price has risen roughly 30% since the start of the year, and other inputs—synthetic rubber, carbon black, etc.—are up over 10% on average. Raising prices may be difficult however, due to the slow pace of demand recovery in Japan and other developed markets, and price hikes could dampen demand and translate into a decline in volume.

We are below Bloomberg consensus on Hankook Tire and Bridgestone by over 20%. We believe the market's high expectations will be lowered once the outlook for 2Q on becomes clearer.

Exhibit 6: Our earnings are below consensus by over 20% on average
Our earnings forecasts versus consensus, ¥ mn, mn won, mn NT$

	Ticker	EPS (New)		EPS (Old)		Changes	
		FY2010E	FY2011E	FY2010E	FY2011E	FY2010E	FY2011E
Yokohama Rubber	5101.T	**21.5**	**28.9**	22.7	31.0	-5.3%	-6.7%
Bridgestone	5108.T	**39.0**	**61.6**	42.6	66.3	-8.4%	-7.1%
Sumitomo Rubber	5110.T	**45.0**	**63.7**	48.4	69.0	-7.1%	-7.7%
Hankook Tire	000240.KS	**1,831.2**	**1,902.4**	2,116.8	2,141.8	-13.5%	-11.2%
Cheng Shin Rubber	2105.TW	**5.2**	**5.3**	5.2	5.3	0.0%	0.0%
Asia tire average						-6.8%	-6.6%

	Ticker	Op. profit (New)		Op. profit (Old)		Changes	
		FY2010E	FY2011E	FY2010E	FY2011E	FY2010E	FY2011E
Yokohama Rubber	5101.T	**16,600**	**20,700**	17,400	22,300	-4.6%	-7.2%
Bridgestone	5108.T	**81,000**	**109,000**	85,000	115,000	-4.7%	-5.2%
Sumitomo Rubber	5110.T	**26,400**	**34,900**	27,800	37,100	-5.0%	-5.9%
Hankook Tire	000240.KS	**254,946**	**279,976**	300,154	322,699	-15.1%	-13.2%
Cheng Shin Rubber	2105.TW	**11,978**	**12,469**	11,978	12,469	0.0%	0.0%
Asia tire average						-5.9%	-6.3%

	Ticker	Op. profit (GSE)		Op. profit (Consensus)		GSE vs Consensus	
		FY2010E	FY2011E	FY2010E	FY2011E	FY2010E	FY2011E
Yokohama Rubber	5101.T	**16,600**	**20,700**	19,986	26,223	-16.9%	-21.1%
Bridgestone	5108.T	**81,000**	**109,000**	112,618	151,601	-28.1%	-28.1%
Sumitomo Rubber	5110.T	**26,400**	**34,900**	31,206	38,644	-15.4%	-9.7%
Hankook Tire	000240.KS	**254,946**	**279,976**	347,586	393,198	-26.7%	-28.8%
Cheng Shin Rubber	2105.TW	**11,978**	**12,469**	14,103	15,714	-15.1%	-20.7%
Asia tire average						-20.4%	-21.7%

Source: Company data, Bloomberg consensus, Goldman Sachs Research estimates.

Hankook, Sumitomo appear overvalued; downgrading to Sell

We maintain our bearish stance on Asian tire stocks, and downgrade Hankook Tire to Sell (Conviction List) and Sumitomo Rubber to Sell. We also reiterate our Sell ratings (Conviction List) on both Bridgestone and Cheng Shin Rubber.

Asian tire sector valuations are actually slightly lower than those for global peers. However, within our autos sector coverage in each region, valuations are demanding while returns remain low.

Hankook Tire: Sell, add to Conviction List; 23.6% potential downside

We downgrade Hankook Tire to Sell from Neutral, and add the shares to our Conviction List. Our new price target of W17,000 (previously W22,000) suggests 23.6% potential downside. We expect the rise in rubber and other material costs to put pressure on Hankook's margins. We have cut our below-bloomberg consensus estimates further: lowering our FY2010 EPS forecasts by 9%-15%. Our new 2010 EPS estimate is 20% below Bloomberg consensus. We forecast FY2010 operating profit and EPS declines of 27% and 22% yoy, respectively. The company's guidance for 2010 is also based on a natural rubber price of US$2,440/t (vs a current spot price of US$3,800/t). 1Q12/2010 earnings could be boosted by cheap inventories left over from 4Q12/2009, but we think market expectations for earnings will fade from 2Q12/2010 onward as earnings deteriorate.

Sumitomo Rubber: 1Q overshoot priced in, Sell on worsening from 2Q on

We also lower our estimates for Sumitomo Rubber, cutting FY12/10 operating profits to ¥26.4 bn from ¥27.8 bn, and lower our 12-month price target to ¥730 (12% potential downside) from ¥750. Our new target implies the second greatest potential downside in our Japan auto parts/tire coverage after Bridgestone, and on this basis we downgrade the stock to Sell from Neutral. Sales volumes are currently above guidance, especially in the Falken brand, and initial offtake sales in Europe are also robust. We look for very substantial progress in 1Q12/10 toward the company's 1H operating profit guidance of ¥7 bn, and forecast 1Q profits of around ¥6 bn. The share price has risen by around 10% over the past month (compared to sideways movement in Bridgestone's share price) in reaction to steady earnings improvement. We think the company may raise 1H guidance, but we see a full-fledged rise in material prices squeezing profits from 2Q onwards, as at rival companies. We expect full-year earnings to fall short of initial guidance.

Bridgestone: Maintain C-Sell; Downside in material prices/volume

Normally, Bridgestone is comparatively impervious to input prices as it is aggressively moving up the production chain, but this is conversely having a negative impact in FY12/10. We lower our earnings estimates roughly 5% to reflect higher prices for natural rubber, butadiene, and other core inputs. We forecast operating profits of ¥81 bn in FY12/10 and ¥109 bn in FY12/11. We see the company making more rapid progress than it projects toward its 1H operating profit guidance of ¥31 bn, and believe 1Q12/10 operating profits could reach ¥20-¥30 bn. It is very difficult to predict whether the company will raise guidance to reflect the 1Q overshoot or lower guidance to factor in higher input prices from 2Q. Along with our lower forecasts, we lower our 12-month price target to ¥1,350 (12% potential downside) from ¥1,430. We reiterate our Sell rating and keep the stock on our Conviction List.

Yokohama Rubber: Estimates and TPs cut, but limited downside, Maintain Neutral

Reflecting upward revisions to our raw material price assumptions, we cut our FY3/11 op. profit forecast for Yokohama Rubber to ¥16.6 bn from ¥17.4 bn. We lower our 12-month target price, based on P/B-ROE correlation, to ¥410 yen from ¥430, but downside to our new target is relatively limited at 7%. Valuation for Yokohama looks undemanding on a P/B of 0.94X our FY3/10 estimate versus multiples of around 1.1X for BS and Sumitomo, and an Asian coverage average of around 1.4X. We believe the business environment remains tough as Yokohama has relatively high domestic operation exposure, but we remain Neutral due to limited downside.

Exhibit 7: Japanese tires/CSR derived from P/BvsROE, Hankook from fair P/B of 1.2X.
Target price and valuation table at a glance

	Apr 8 (¥, Won, NT$)	Old TP (¥, Won, NT$)	**New TP (¥, Won, NT$)**	**Return potential**
Yokohama Rubber	439	430	410	-6.6%
Bridgestone	1,534	1,430	1,350	-12.0%
Sumitomo Rubber	827	750	730	-11.7%
Hankook Tire	22,250	22,000	17,000	-23.6%
Cheng Shin Rubber	67.8	55.0	55.0	-18.9%

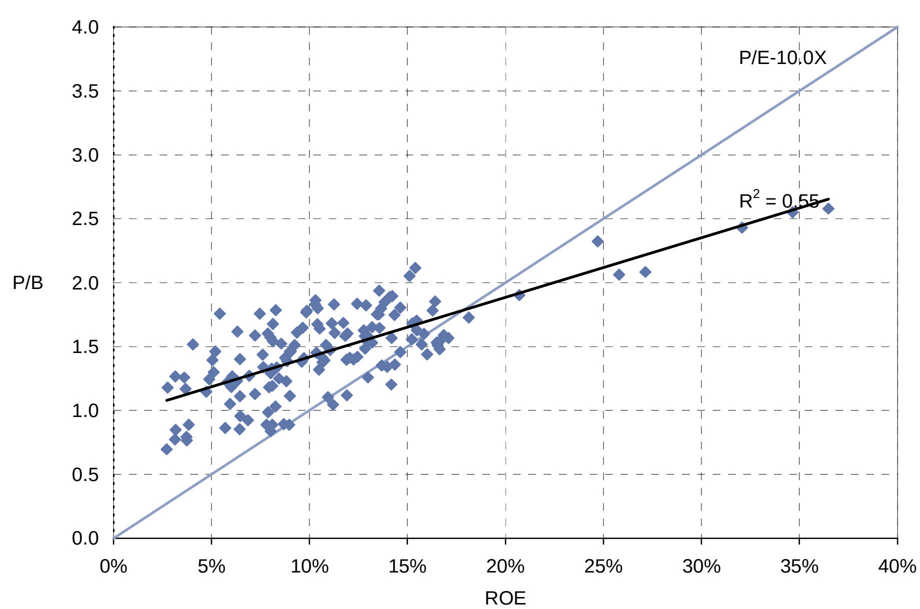
	Target P/B	Hist. avg P/B	Theoretical value (¥, Won, NT$)	Return potential
Yokohama Rubber	0.89	1.09	410	-7%
Bridgestone	0.95	1.35	1,340	-13%
Sumitomo Rubber	0.98	1.38	730	-12%
Hankook Tire	1.20	1.40	17,000	-24%
Cheng Shin Rubber	2.50	1.40	55	-19%

	Valuation		**Implied valuation**	
	P/E (2010E)	P/B (2010E)	P/E (2010E)	P/B (2010E)
Yokohama Rubber	19.4	0.94	18.1	0.88
Bridgestone	36.0	1.09	31.7	0.96
Sumitomo Rubber	17.1	1.11	15.1	0.98
Hankook Tire	12.4	1.51	9.5	1.15
Cheng Shin Rubber	13.1	3.08	10.6	2.50

(¥, Won, NT$, %)	BPS 2010E	EPS 2010E	ROE 2010E
Yokohama Rubber	465	22.7	5.0%
Bridgestone	1,412	42.6	3.0%
Sumitomo Rubber	742	48.4	6.6%
Hankook Tire	14,726	1,798	12.8%
Cheng Shin Rubber	22.0	5.2	22.0%

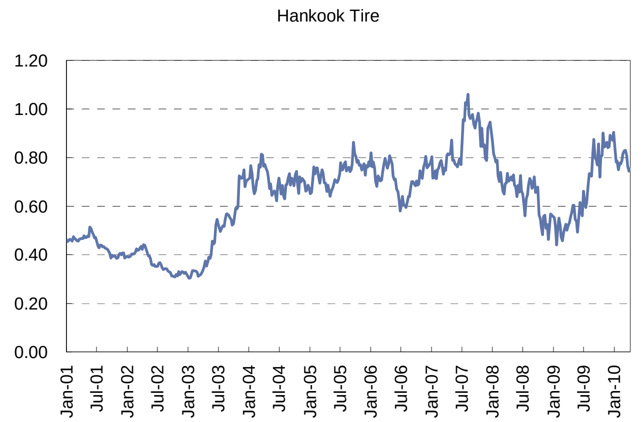
Source:Company data, Goldman Sachs Research.

Exhibit 8: Japanese tire makers' TP derived from P/BvsROE, which show strong explanation historically
P/BvsROE historical scattered chart of Japanese Auto sector



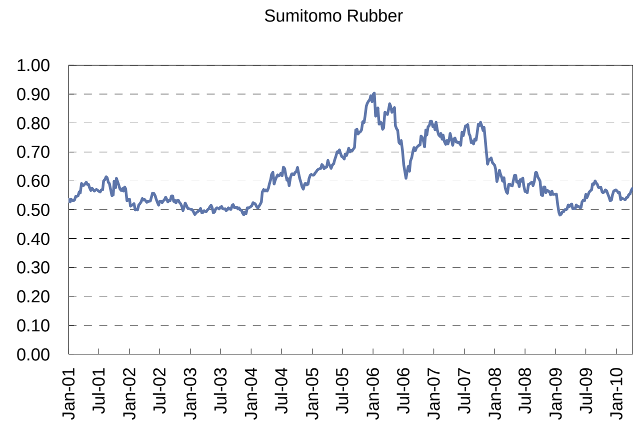
Source: Company data, Datastream, Goldman Sachs Research.

Exhibit 9: Hankook valuations have risen
Trends in EV/GCI (X)



Source: Factset, Goldman Sachs Research estimates.

Exhibit 10: Sumitomo rising as 1Q expectations high
Trends in EV/GCI (X)

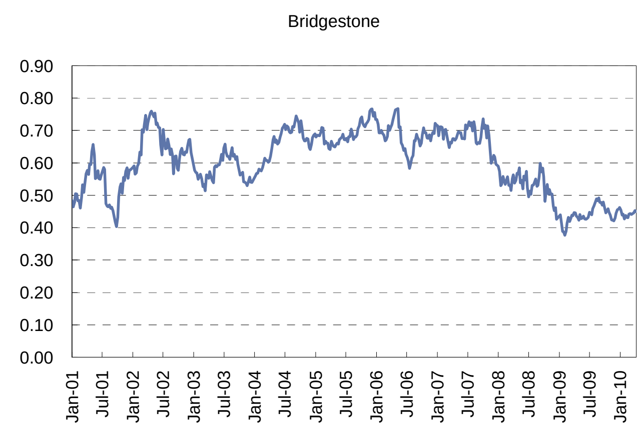


Source: Factset, Goldman Sachs Research estimates.

Exhibit 11: CSR also rising on 1Q expectations
Trends in EV/GCI (X)

Source: Factset, Goldman Sachs Research estimates.

Exhibit 12: Bridgestone relatively low, but appropriate as returns are low
Trends in EV/GCI (X)



Source: Factset, Goldman Sachs Research estimates.

Exhibit 13: Global tire maker valuation comparison

Company	Rating	Apr 08 Price	Market Cap. (in $mn)	Operating Profits 2009E (in $mn)	2010E (in $mn)	2011E (in $mn)	P/E 2009E (x)	2010E (x)	2011E (x)	P/B 2009E (x)	2010E (x)	2011E (x)	2010E P/CF (x)	EV/EBITDA (x)	Div. Yield (%)	ROE (%)
Tires																
Yokohama Rubber	Neutral	439	1,610	206	178	222	15.7	20.4	15.2	0.98	0.94	0.88	4.2	6.5	2.7	4.7%
Bridgestone	Sell*	1,534	13,356	811	867	1,167	1153.4	39.3	24.9	1.11	1.09	1.05	6.1	7.3	1.0	2.8%
Sumitomo Rubber	Sell	827	2,329	308	283	374	23.9	18.4	13.0	1.16	1.11	1.05	4.7	7.4	1.9	6.2%
Hankook	Sell*	22,250	3,019	311	227	250	9.7	12.4	11.9	1.67	1.51	1.37	7.6	0.3	1.6	12.1%
CSR	Sell*	67.8	3,540	516	379	395	9.2	13.1	12.7	3.08	2.70	2.39	8.0	2.0	3.1	22.0%
Asia Average							**14.6**	**20.7**	**15.5**	**1.60**	**1.47**	**1.35**	**6.1**	**4.7**	**2.1**	**9.5%**
Continental	Buy	37.1	9,907	-1,997	1,515	2,076	-3.9	39.4	14.3	1.66	1.48	1.34	3.8	2.8	0.0	9.8%
Michelin	Neutral	53.3	10,498	1,163	1,899	2,272	75.0	11.6	8.2	1.42	1.30	1.16	4.7	2.4	2.8	15.1%
Nokian Tires	Sell	19.0	3,207	136	224	302	40.7	21.2	13.8	3.12	2.89	2.50	13.4	0.7	1.8	19.4%
Pirelli	Neutral	0.5	3,162	290	477	549	107.0	12.8	14.7	1.88	1.73	1.60	5.6	1.8	2.2	11.3%
Goodyear	Buy	12.8	3,098	263	823	1,164	-13.5	21.2	7.9	4.19	3.65	2.55	3.6	2.0	0.0	38.5%
US/EU Average							**74.2**	**21.2**	**11.8**	**2.46**	**2.21**	**1.83**	**6.2**	**2.0**	**1.4**	**18.8%**
Tires Average							**40.2**	**21.0**	**13.7**	**2.03**	**1.84**	**1.59**	**6.2**	**3.3**	**1.7**	**14.2%**

Note: *Conviction List.

Source: Company data, Datastream, Goldman Sachs Research estimates.

Exhibit 14: Yokohama Rubber and Sumitomo Rubber have rallied for the last one month on revision to its FY3/10 guidance and high expectation on 1QFY12/10 respectively

Global tire maker share price performance

Tires		CCY	Price	1wk (%)	1 Month (%)		3 Month (%)		6 Month (%)		1 Year (%)	
KO:KMH	KUMHO	KW	3,590.0	1.4	YOKOHAMA	13.4	KUMHO	16.9	PIRELLI	18.6	COOPER	287
TW:CSI	CSR	TW	68.1	1.0	SUMITOMO	10.5	YOKOHAMA	9.7	YOKOHAMA	10.3	CONTINENTAL	141
D:CON	CONTINENTAL	E	38.0	0.5	PIRELLI	9.1	SUMITOMO	4.9	COOPER	9.0	PIRELLI	112
U:GT	GOODYEAR	U$	13.0	0.2	CSR	4.8	PIRELLI	1.6	SUMITOMO	5.3	CSR	92
J5101	YOKOHAMA	Y	441.0	-0.2	CONTINENTAL	3.7	BRIDGESTONE	-0.6	HANKOOK	5.3	NEXEN	75
KO:HKT	HANKOOK	KW	22,000.0	-0.7	COOPER	3.1	CONTINENTAL	-2.9	CONTINENTAL	5.2	GOODYEAR	71
J5110	SUMITOMO	Y	830.0	-1.3	BRIDGESTONE	2.3	CSR	-4.8	BRIDGESTONE	5.2	MICHELIN	68
J5108	BRIDGESTONE	Y	1,578.0	-1.4	KUMHO	2.0	MICHELIN	-5.6	MICHELIN	3.0	HANKOOK	60
F:MCL	MICHELIN	E	54.0	-1.9	MICHELIN	-2.5	COOPER	-6.0	CSR	-1.3	SUMITOMO	16
I:PCI	PIRELLI	E	0.4	-2.7	GOODYEAR	-5.3	HANKOOK	-7.6	NEXEN	-6.1	BRIDGESTONE	1
KO:WSF	NEXEN	KW	5,200.0	-3.4	NEXEN	-5.5	GOODYEAR	-18.1	GOODYEAR	-20.6	YOKOHAMA	-2
U:CTB	COOPER	U$	19.3	-3.5	HANKOOK	-7.8	NEXEN	-18.9	KUMHO	-37.1	KUMHO	-21

Source: Datastream.

Exhibit 15: Japan tire stocks are not undervalued

Japan Autos valuation comparison

Company	Code	Rating	Apr 08 Price (¥)	Market Cap. (¥bn)	Operating Profits 2009E (¥bn)	Operating Profits 2010E (¥bn)	Operating Profits 2011E (¥bn)	P/E 2009E (x)	P/E 2010E (x)	P/E 2011E (x)	P/B 2009E (x)	P/B 2010E (x)	P/B 2011E (x)	2010E P/CF (x)	2010E EV/EBITDA (x)	2010E Div. Yield (%)	2010E ROE (%)
Assembers																	
Nissan	7201	Neutral	811	3,666	310.0	370.0	470.0	53.3	18.9	14.4	1.23	1.17	1.11	6.6	5.1	1.2	6.3%
Toyota	7203	Neutral	3,690	12,723	-100.0	500.0	740.0	1052.0	19.4	14.7	1.16	1.12	1.06	8.5	7.9	1.6	5.9%
Mazda	7261	Neutral	264	470	7.0	23.0	37.0	592.7	42.9	21.9	0.82	0.92	0.89	5.7	9.2	1.1	2.2%
Daihatsu	7262	Neutral	883	377	36.0	38.0	44.0	19.6	17.3	14.8	1.11	1.05	1.00	4.3	4.3	1.7	6.2%
Honda	7267	Buy*	3,265	5,991	350.0	510.0	620.0	20.7	13.9	11.8	1.40	1.31	1.21	7.9	6.5	2.1	9.7%
Suzuki	7269	Neutral	2,014	1,093	70.0	93.0	113.0	28.6	26.5	21.1	1.01	1.13	1.08	6.3	4.4	1.0	4.3%
Fuji Heavy	7270	Buy	486	380	22.0	38.0	46.0	-23.4	19.6	15.6	1.00	0.97	0.93	5.1	6.5	2.1	5.0%
Yamaha Motor	7272	Neutral	1,280	367	-44.6	20.0	40.0	-1.7	59.0	18.4	1.72	1.69	1.60	7.5	9.0	0.0	2.9%
Assembers Average								**30.6**	**27.2**	**16.6**	**1.18**	**1.17**	**1.11**	**6.5**	**6.6**	**1.4**	**5.3%**
Trucks																	
Isuzu	7202	Neutral	250	424	8.0	31.0	50.0	-325.9	18.9	13.4	1.45	1.35	1.29	7.3	8.9	0.0	7.4%
Hino	7205	Sell	390	224	-1.0	12.0	23.0	-26.0	53.2	17.2	1.27	1.26	1.20	4.3	7.5	1.3	2.4%
Trucks Average								**NM**	**36.0**	**15.3**	**1.36**	**1.31**	**1.25**	**5.8**	**8.2**	**0.6**	**4.9%**
Suppliers																	
Toyota Boshoku	3116	Sell	1,607	302	26.0	34.0	43.0	34.0	18.2	14.9	1.81	1.70	1.57	5.6	4.5	1.9	9.6%
Denso	6902	Neutral	2,731	2,414	120.0	140.0	170.0	27.4	21.4	17.6	1.19	1.15	1.10	7.7	5.9	1.5	5.5%
Aisin Seiki	7259	Buy	2,716	800	80.0	115.0	130.0	162.6	13.0	12.1	1.23	1.15	1.08	3.9	3.3	2.2	9.2%
Nissin Kogyo	7230	Neutral	1,437	94	4.6	10.1	13.4	37.6	13.8	10.2	1.17	1.09	1.01	6.4	4.0	2.2	8.2%
Keihin	7251	Buy*	1,778	132	14.0	22.0	30.0	20.2	10.4	8.0	1.15	1.05	0.93	4.7	2.2	1.3	10.5%
FCC	7296	Buy	1,665	88	5.5	11.5	15.4	33.4	10.9	8.2	1.27	1.16	1.05	5.8	3.7	1.9	11.2%
Stanley Elec.	6923	Neutral	1,751	319	24.7	31.8	38.6	13.2	16.3	13.3	1.54	1.44	1.33	8.1	4.6	1.7	9.1%
Koito Mfg	7276	Neutral	1,354	218	28.8	32.5	36.0	26.9	15.7	13.4	1.48	1.38	1.29	6.1	4.3	2.4	9.1%
Toyoda Gosei	7282	Buy	2,485	323	24.0	37.2	46.9	23.6	14.5	11.2	1.55	1.42	1.29	5.0	3.6	1.4	10.2%
Suppliers Average								**42.1**	**14.9**	**12.1**	**1.38**	**1.28**	**1.18**	**5.9**	**4.0**	**1.8**	**9.2%**
Tires																	
Yokohama Rubber	5101	Neutral	439	150	19.2	16.6	20.7	15.7	20.4	15.2	0.98	0.94	0.88	4.2	6.5	2.7	4.7%
Bridgestone	5108	Sell*	1,534	1,247	75.7	81.0	109.0	1153.4	39.3	24.9	1.11	1.09	1.05	6.1	7.3	1.0	2.8%
Sumitomo Rubber	5110	Sell	827	218	28.7	26.4	34.9	23.9	18.4	13.0	1.16	1.11	1.05	4.7	7.4	1.9	6.2%
Tires Average								**19.8**	**26.0**	**17.7**	**1.08**	**1.05**	**1.00**	**5.0**	**7.0**	**1.9**	**4.6%**

Note: Averages for PER, PCFR, PBR, EV/EBITDA exclude Fuji Heavy Industry. EV calculated based on previous fiscal year's Net debt (FY3/09). Debt excludes sales finance business, but EBITDA is based on company-defined overall capital. Target prices based on historical correlation between P/B and ROE. Risks include forex, US economic trends, and prices of materials such as natural rubber and crude oil. * Conviction List. For important disclosures, see http://www.gs.com/research/hedge.html

Source: Company data, Datastream, Goldman Sachs Research estimates.

Exhibit 16: Global tire maker CROCI (cash return) distribution
Director's Cut: Japan Autos CROCI Quartile destribution

	CROCI											
Name	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009E**	**2010E**	**2011E**
Aisin Seiki	10%	7%	8%	8%	9%	9%	9%	11%	7%	6%	7%	7%
Bridgestone	5%	6%	11%	10%	11%	10%	7%	9%	6%	6%	5%	6%
Daihatsu Motor	8%	5%	5%	7%	8%	6%	9%	9%	7%	6%	5%	5%
Denso	8%	8%	8%	8%	9%	10%	10%	11%	6%	6%	6%	6%
FCC	8%	11%	11%	14%	13%	8%	13%	13%	11%	8%	10%	13%
Fuji Heavy Industries	9%	10%	8%	7%	4%	7%	6%	6%	4%	4%	6%	7%
Hino Motors	10%	4%	4%	7%	6%	6%	6%	6%		3%	4%	5%
Honda Motor	10%	14%	14%	10%	11%	10%	13%	18%	14%	13%	13%	13%
Isuzu Motors	3%			6%	8%	7%	9%	9%			4%	4%
Keihin	5%	10%	12%	14%	12%	10%	11%	13%	9%	10%	13%	15%
Koito Mfg	10%	7%	8%	8%	9%	10%	10%	10%	7%	8%	8%	8%
Mazda Motor	4%	3%	6%	6%	6%	6%	8%	6%				3%
Nissan Motor	8%	8%	12%	12%	6%	7%	12%	10%	10%	8%	9%	10%
Nissin Kogyo	5%	8%	11%	15%	10%	13%	18%	12%	13%	9%	9%	11%
Stanley Electric	11%	7%	12%	13%	14%	14%	16%	16%	11%	12%	11%	9%
Sumitomo Rubber Industries	6%	5%	7%	8%	7%	7%	5%	10%	3%	9%	6%	7%
Suzuki Motor				7%	11%	13%	14%	11%	6%	6%	7%	7%
Toyoda Gosei	9%	8%	9%	10%	8%	9%	11%	13%	9%	9%	12%	13%
Toyota Boshoku	13%	11%	11%	11%	13%	13%	17%	19%	11%	9%	10%	11%
Toyota Motor	9%	9%	11%	11%	12%	15%	18%	17%	9%	7%	9%	10%
Yamaha Motor	6%	7%	10%	9%	9%	19%	12%	12%	4%		5%	6%
Yokohama Rubber				5%	5%	5%	5%	7%	5%	5%	5%	5%

First Quartile
Second Quartile
Third Quartile
Fourth Quartile
Not Meaningful / Missing

Source: Factset, Goldman Sachs Research estimates.

Short-term risks: Production problems and growing China demand vs. difficulty of price pass-through due to slow recovery in DMs

Chinese imports of natural rubber reached a new all-time high near the end of last year, and inquiries are growing even stronger due partly to the impact of a drought in China. At the same time, rubber-producing countries such as Indonesia are encountering production problems due to bad weather, and this is reducing supply. Reflecting the dramatic tightening in the supply/demand balance, the natural rubber price hit its highest level in 60 years. Tire maker focus is shifting to replacement tire price hikes, but we do not think makers will be able to pass on higher input costs sufficiently amid a gradual demand recovery in developed markets. We see margins deteriorating across the board at tire makers this fiscal year.

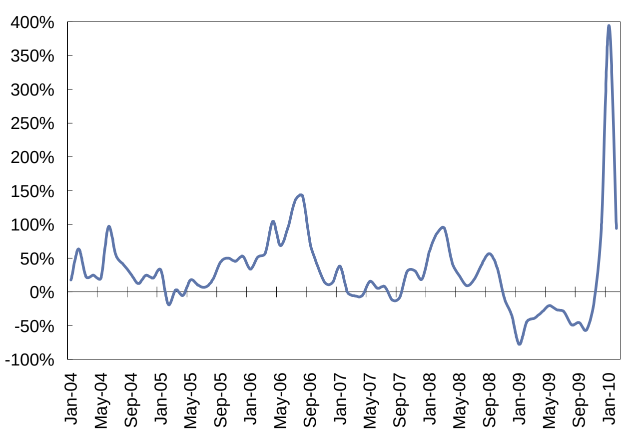
Rubber price surging on robust Chinese demand, supply problems

The natural rubber price hit a new all-time high on March 31 and continued rising after that, climbing to US$3.80/kg on April 7. This marks a rise of nearly 2.5X yoy in one year from the April 2009 average of US$1.50. The rapid price rise is being driven on the demand side by surging imports to China, which accounts for 35% of natural rubber consumption worldwide, due to a drought there, among other factors.

Another factor contributing to near-term supply/demand tightness is that supply is not keeping pace with recovering demand in developed economies. The world's No. 2 natural rubber-producing country, Indonesia, has been plagued by bad weather since the middle of last year, and production continues to run below year-earlier levels as a result (see Exhibits 17-19).

Exhibit 17: Imports rising sharply on drought and other factors

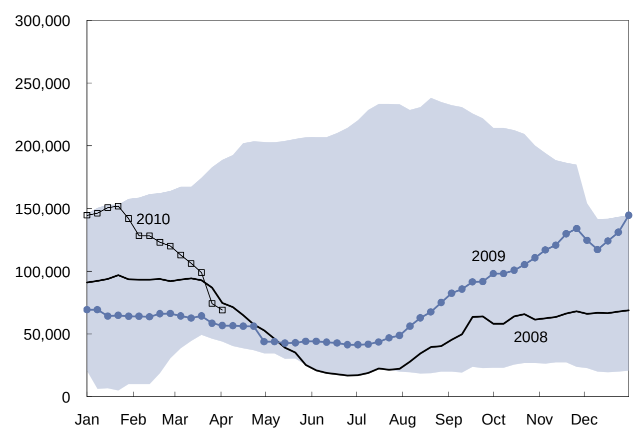
Chinese natural rubber imports (yoy)



Source: Datastream.

Exhibit 18: Shanghai inventory declining sharply due to drought

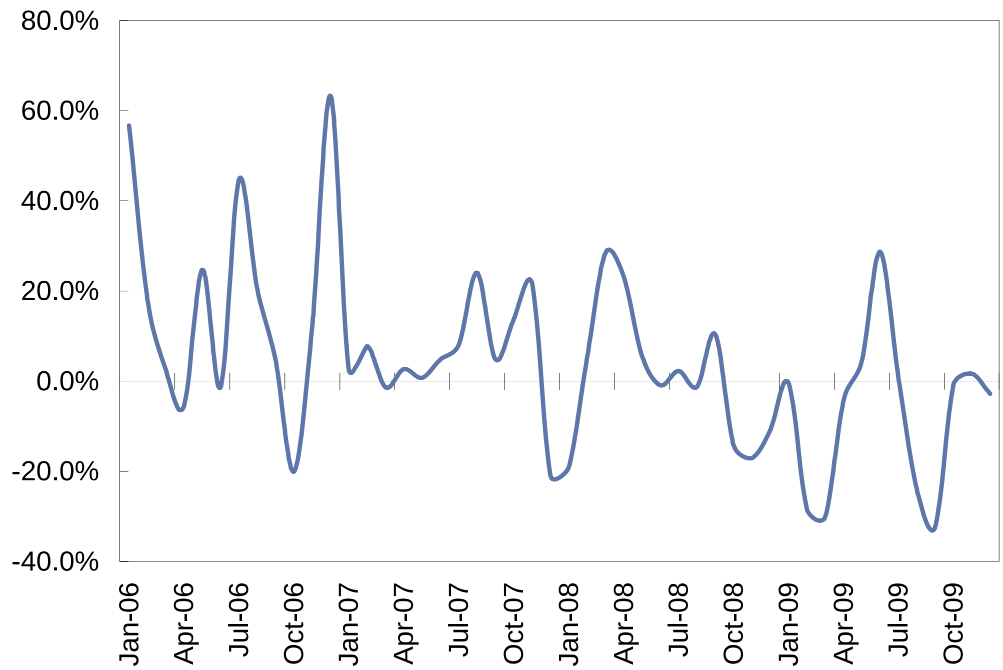
Shanghai natural rubber warehouse inventory (tonnes)



Note: Shaded area show historical min/max range

Source: Datastream.

Exhibit 19: Production running below year-earlier levels since mid-2009
Indonesia natural rubber production (yoy)

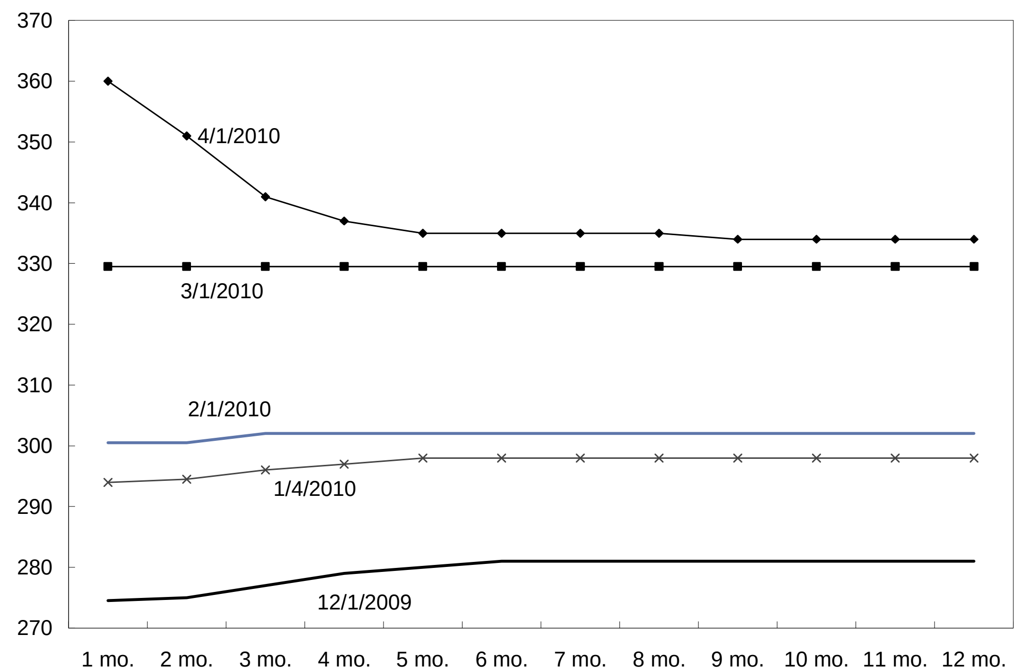


Source: IRSG.

Tight S/D reflected in jump in near futures, high level for far futures

Going back to late-2009 through March 2010, the Singapore SICOM natural rubber (RSS3) futures curve had a mild upward slope (Contango) but in the period through end-March it had inverted sharply with a steep rise in the nearest-delivery contract (Backwardation). We ascribe this shift to the current tightness of supply/demand, not expectations for a fall in price. The 12-month contract is trading at US$3.35/kg, above the pre-financial crisis peak of US$3.31/kg (June 2008). Some correction may occur, but we expect the natural rubber price to stick at high levels (see Exhibit 20).

Exhibit 20: Recent S/D tightening behind sharp rise in nearest-delivery RSS3 futures
Shape of forward curve for natural rubber futures (RSS3) (US cents per kilogram)



Source: SICOM.

Expecting little price pass-through for replacement tires in developed markets

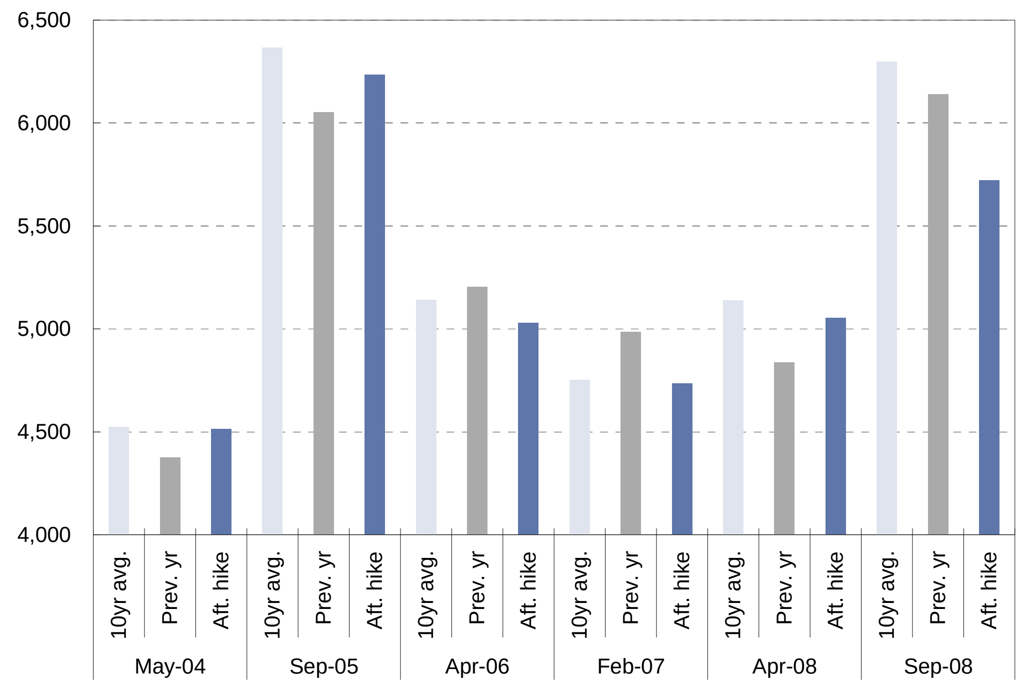
In the current cycle we think it will be difficult for tire makers to push through price hikes in developed markets (i.e., Japan, Europe, and the US) in response to materials cost growth. In Japan's case, demand is no higher than the depressed level of 1Q2009 and we do not see good prospects even assuming that summer tire sales have been delayed by late snowfall.

Our analysis of the impact from price hikes indicates that pass-through would hold back demand recovery at this stage. We looked at (1) average shipments for the month each side of price hikes for Japanese replacement tires, (2) the past 10-year average for the three months on either side, and (3) the average for the corresponding period in the year before hikes. We found that demand fell when prices were increased. Price hikes were a dampener even in the last cycle, when demand was growing, albeit a modest one .

We think tire makers will have to let their profit margin take the weight of materials cost growth in the near term. They posted strong earnings in 4Q2009 and their margins are much larger than they were in the last cycle. At the same time, commodities other than natural rubber are far below their most recent peak, which is not conducive to price hikes (see Exhibits 21-24).

Exhibit 21: When tire prices are hiked, shipment volumes tend to decline yoy or fall below the ten-year average

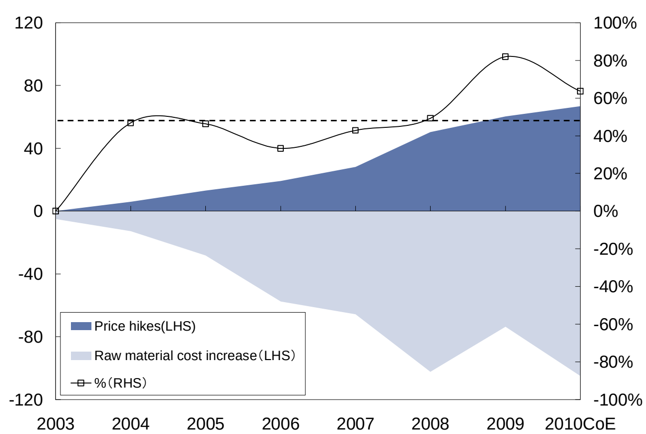
Comparison of shipment volumes in months on either side of domestic price hikes (thousands per month)



Source: JATMA.

Exhibit 22: Cumulative recovery of higher input costs via price hikes improved to over 80% in 2009

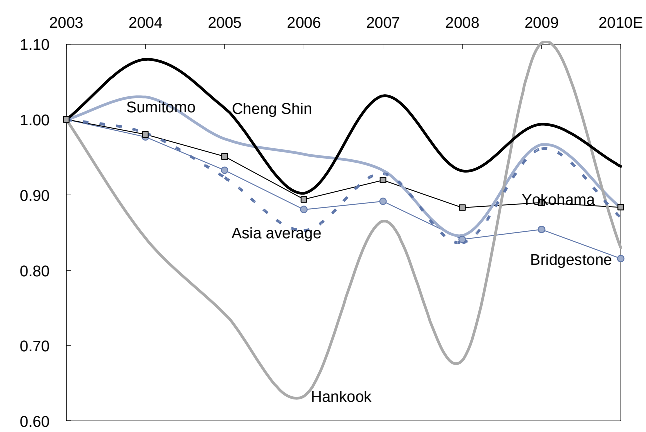
Sumitomo Rubber: OP Impact of input rise increase/price hikes (¥ bn)



Source: Sumitomo Rubber Industries.

Exhibit 23: Gross margins widened in 2009 but we look for margins to narrow again

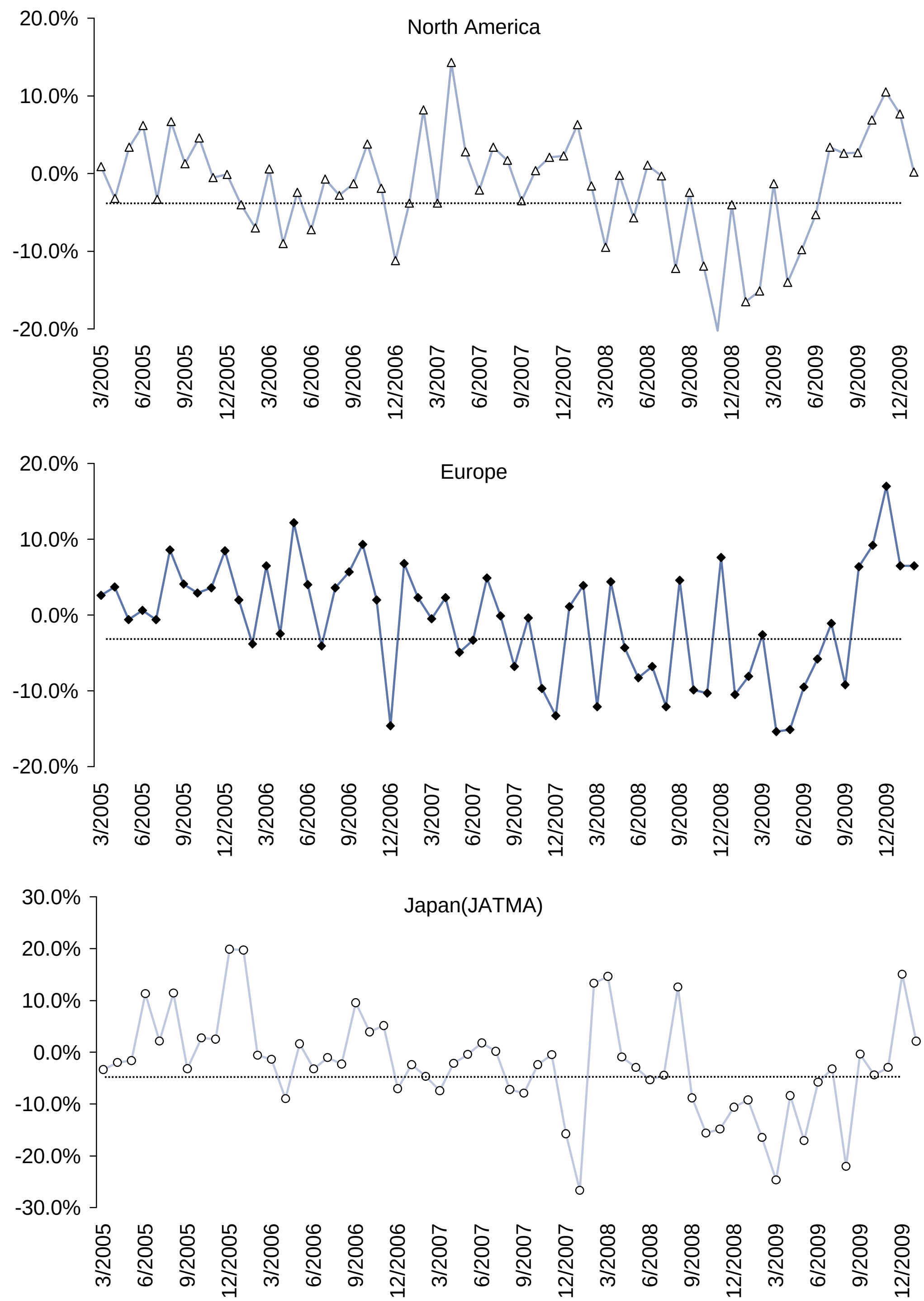
Gross margin trend (2003=1.00)



Source: Company data, Goldman Sachs Research estimates.

Exhibit 24: Despite year earlier weakness, replacement tire demand in developed markets has stayed weak since start-2010

Monthly shipments of tires for passenger cars and light trucks, yoy basis



Source: Michelin, JATMA.

Longer-term risks: Growing Chinese/Indian demand outpacing supply growth, stiffer competition in emerging markets

China, India, and other emerging markets in Asia have procured roughly 70% of natural rubber volumes worldwide and exported many of the tires made from this rubber to developed markets (i.e., the US, Europe, and Japan). In this way, developed market growth has underpinned growth in natural rubber consumption. We now expect rubber consumption volumes to grow sharply since a new growth driver emerged in 2009 - domestic tire demand in China and India. On the supply side, we think natural rubber production may undershoot the expectations of tire makers if rubber growers decide to switch to other cash crops. With natural rubber prices having entered a secular upward trend, we think stiffer competition will constrain tire makers from passing on higher input costs and so will squeeze their margins.

We expect sharp growth in China/India to outpace supply growth

China has absorbed nearly all of the growth in natural rubber consumption volumes over the past ten years. The main driver was export markets but we expect Chinese domestic demand growth to drive future rubber demand. As we see little reason to expect sharp expansion in rubber supply volumes, we look for supply/demand to tighten further. We thus raise our natural rubber price assumptions to US$3.40/kg for 2010 and to US$3.60/kg for 2011 (see Exhibit 25).

Exhibit 25: We see Chinese/Indian demand as drivers; supply/demand tightness unlikely to ease even if rubber-producing nations boost supply
Our natural rubber supply/demand forecasts

Supply vol. (Thou. tonnes)	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010E	2011E
Thailand	2,320	2,615	2,876	2,984	2,937	3,137	3,056	3,090	3,086	3,306	3,593
Indonesia	1,607	1,630	1,792	2,066	2,271	2,637	2,755	2,751	2,535	2,669	2,805
Malaysia	882	890	986	1,169	1,126	1,284	1,200	1,072	856	862	867
Vietnam	313	331	364	419	482	555	602	660	724	841	943
China	478	527	565	573	510	533	600	560	630	736	800
India	632	641	707	743	771	853	811	881	817	850	874
Others	1,101	703	744	804	810	702	702	1,017	955	1,061	1,100
Total	7,332	7,337	8,033	8,758	8,907	9,701	9,726	10,031	9,602	10,324	10,980

Demand vol. (Thou. tonnes)	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010E	2011E
North America	1,105	1,266	1,225	1,290	1,316	1,148	1,157	1,179	790	958	1,008
Japan	729	749	784	815	857	874	887	878	637	673	707
Korea	332	326	333	352	370	364	377	358	330	341	350
W. Europe	253	278	299	319	335	321	374	398	360	383	406
China	1,330	1,395	1,525	2,000	2,150	2,400	2,550	2,924	3,669	3,981	4,372
India	631	680	717	745	789	815	851	881	904	961	1,020
Other Asia	2,258	2,153	2,291	2,334	2,366	2,510	2,735	2,580	2,133	2,367	2,479
South America	415	432	473	526	538	528	565	574	449	467	485
E. Europe/Russia	173	157	180	198	227	250	271	254	186	186	188
Africa	107	116	118	123	121	120	118	127	90	90	92
Total	7,333	7,552	7,944	8,701	9,069	9,329	9,884	10,154	9,547	10,406	11,107

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010E	2011E
S-D Gap (Thou. tonnes)	-1	-215	89	57	-162	372	-158	-123	55	-82	-127
Inventory (Thou. tonnes)	2,193	1,978	2,067	2,124	1,962	2,334	2,177	2,557	2,262	2,180	2,053
Inventory days (day)	109	96	95	89	79	91	80	92	86	76	67

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010E	2011E
Nat rubber price (RSS3, US$/kg)	57	76	107	128	149	208	226	260	192	335	360

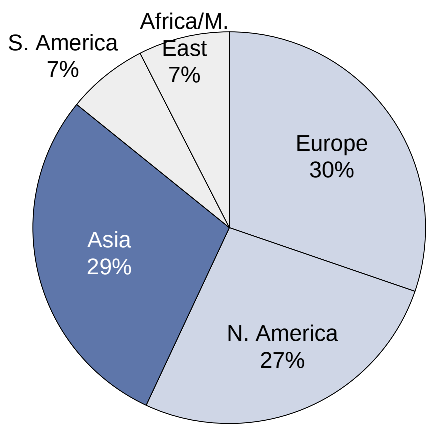
Source: IRSG, Goldman Sachs Research estimates.

Asian EM tire demand replacing DM demand as main rubber driver

Europe and North America account for about 60% of global tire demand compared with roughly 30% for Asian countries but China, India, and the rest of Asia account for 70% of natural rubber consumption. This gap reflects a structure where tire makers export tires made in Asian countries where production costs are low to developed markets.

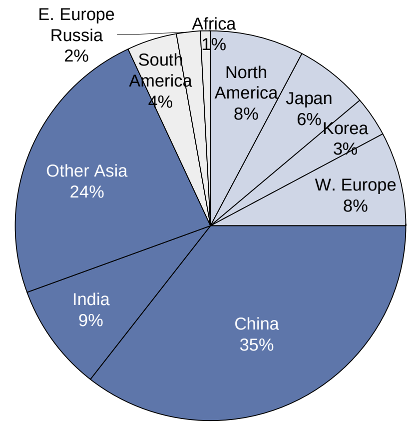
Yet this structure has been evolving. China is the biggest buyer of natural rubber, and the driver of tire demand there has shifted since 2009 from exports to domestic demand. India's tire market has long been driven by domestic demand but its rubber consumption has started to grow sharply in step with the growth of its economy. We expect growth in Asian emerging markets, which account for 70% of global rubber consumption volume, to drive natural rubber demand over the longer term (see Exhibit 26-27).

Exhibit 26: NA/Europe account for 60% of tire demand…
Regional breakdown of OEM/replacement demand (tire volumes, passenger car radials + truck/bus radials)



Source: Michelin.

Exhibit 27: …but less than 25% of natural rubber use
Regional breakdown of natural rubber procurement volumes



Source: IRSG.

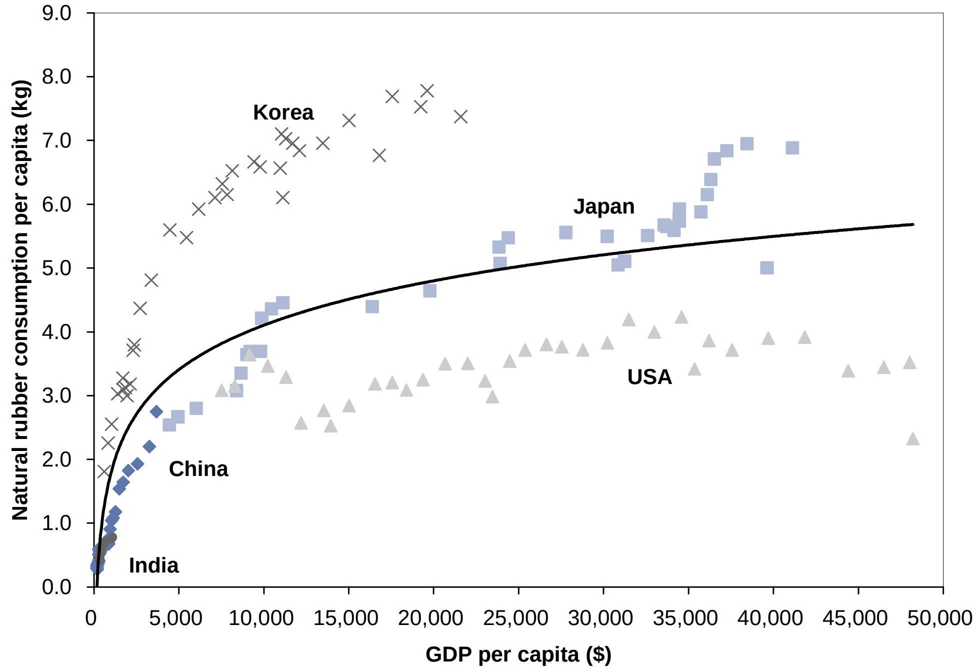
We expect double-digit growth in Chinese/Indian natural rubber consumption

Chinese tire volumes grew robustly in the five years through 2008, with both domestic shipments and exports expanding by roughly 9% per year. China's natural rubber consumption grew on average by 14% over this span. China's tire export ratio went from about 30% in 2002 or so to nearly 50% in 2008, underscoring the role of exports in driving growth. In 2009, however, Chinese auto sales expanded sharply and domestic tire shipment volume grew 14% while tire exports grew only 6%. Despite a smaller tire export ratio, China's consumption of natural rubber grew 25% yoy, showing that domestic demand has emerged as a growth driver.

As the Chinese economy expands, we look for structural growth in its rubber consumption. Assuming China's per-capita rubber consumption grows to a level similar to that of Japan, we estimate it would grow from the current 2.8kg/person to 4kg-5kg/person for growth in the range of 30%-50%. If China's per-capital growth is closer to that of the US (3kg-4kg), we estimate growth in the range of 10%-30%. Along with the advance of motorization and population growth, we expect fundamental changes in per-capita consumption to drive sharp growth in natural rubber consumption.

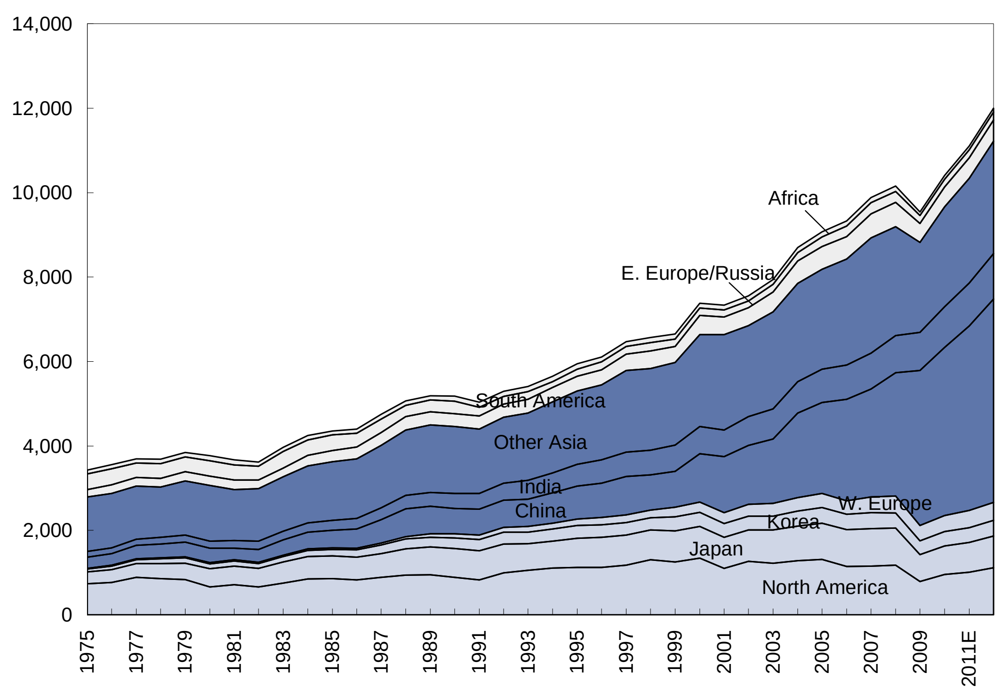
Although India's tire export ratio has stayed low at about 10%, the country is in the early stages of motorization, so its per-capital rubber consumption is still very low compared with that of other countries. Assuming its export ratio stays at 10% and its per-capital consumption grows to a level on par with that of the US, we estimate its total natural rubber consumption would nearly triple in size (see Exhibits 28-29).

Exhibit 28: Ample room for domestic demand-led growth in both China and India
Per-capital GDP and natural rubber consumption (US$ per capita, kg per capita)



Source: IMF, IRSG.

Exhibit 29: China and India are long-term demand drivers
Regional breakdown of natural rubber consumption volume; thousand tonnes per year

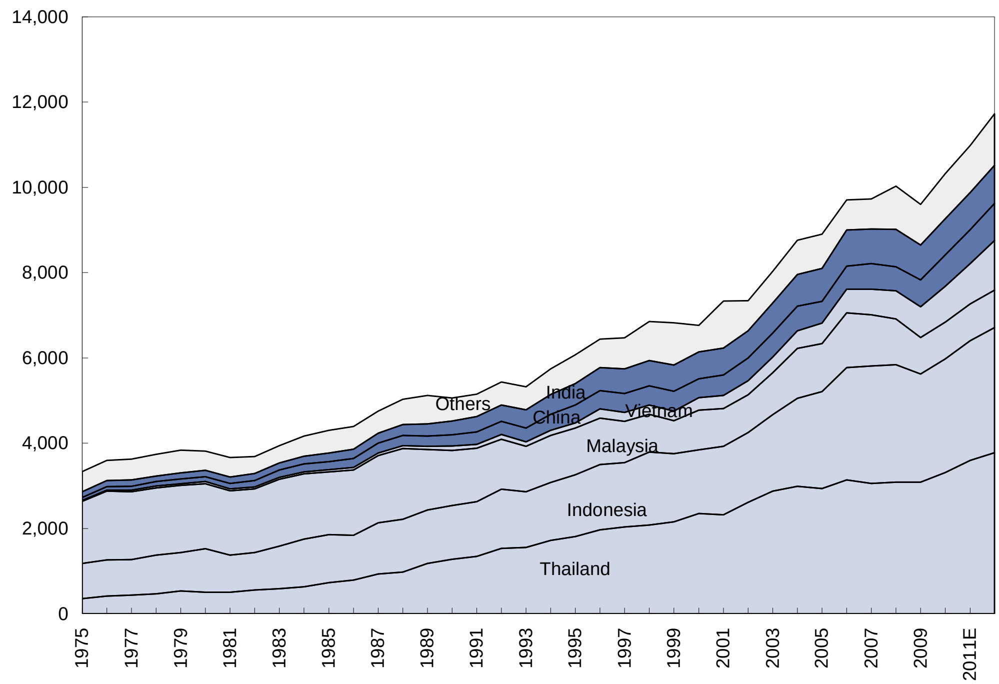


Source: IRSG.

Thailand, Indonesia, and other natural rubber producers are likely to pursue supply growth

Four Southeast Asian countries produce about 75% of the global natural rubber supply: Thailand (3 mn tonnes; 31%), Indonesia (2.5 mn tonnes; 26%), Malaysia (900,000 tonnes; 9%), and Vietnam (700,000 tonnes; 8%). China and India are producers of natural rubber but are also major purchasers. China uses about 3.6 mn tonnes while producing 600,000, and India uses about 900,000 tonnes while producing 800,000, making both countries net importers due to expanding internal demand. In the medium-to-long term, we do not expect the four Southeast Asian countries mentioned above to deviate from the pursuit of supplying the world with natural rubber as demand expands rapidly (see Exhibit 30).

Exhibit 30: Natural rubber supply growth is centered on four Southeast Asian countries
Natural rubber production by country; thousands of tonnes per year



Source: IRSG.

Price risk higher on government intervention in Thailand and other rubber-producing countries; market power may surpass OPEC's

Agriculture is crucial to Thailand, where it contributes over 10% to GDP and approximately half the population works in the sector, and the situation is similar in other rubber-producing countries. Within this vital sector, natural rubber is a core export product and consistently ranks near the top in monetary terms, and for this alone governments of producing countries pay maximum attention to market trends in the product.

Thailand produces the most natural rubber, and ministries and officials there aggressively regulate rubber prices. Since the start of 2009, they have taken the lead in implementing export regulations and transplanting policies. Thai export authorities have recently commented that current price levels are proper and reasonable.

We are projecting that major producers will increase natural rubber volume, but we do not expect so much that demand/supply eases. We have not yet seen a rubber cartel emerge to exert significant influence in the same way as OPEC. However, the risk of that remains considerable as the countries in question dominate the market with an 80% share vs. OPEC's 30%-40% (see Exhibit 31).

Exhibit 31: Agriculture is a core industry for rubber-producing countries
Rubber producer population, agricultural contribution to GDP

	pop.	farm pop.	%	GDP	farm GDP	%
Thailand	63.4	28.1	44.2%	245	28	11.4%
Indonesia	228.9	91.9	40.1%	365	52	14.4%
Malaysia	26.1	3.6	13.8%	187	19	10.2%
Vietnam	86.2	55.9	64.9%	58	13	21.7%

Note: Pop.：millions GDP：nominal bn$

Main agricultural exports	
Thailand	dry nat rubber(23%)・polished rice(16%)・nat rubber(5%)
Indonesia	palm oil(34%)・dry nat rubber(24%)・palm seed oil(5%)・coffee beans(5%)
Malaysia	palm oil(45%)・dry nat rubber(16%)・fatty acid oil(6%)・palm seed oil(4%)
Vietnam	polished rice(17%)・coffee beans（9%)・cashew nuts(6%)・dry nat rubber(6%)

Source: FAO, MOF.

Shift to palm oil production in Malaysia and Indonesia a supply risk

Malaysia's and Indonesia's greatest export in monetary terms is palm oil, surpassing natural rubber. Palm fruit can be harvested after three years, much sooner than natural rubber, which takes five to seven. Palm tree cultivation and transplanting are pursued aggressively as the tree's soil needs are also relatively easier to meet. Palm oil is not well known in Japan, but demand is expected to grow as its use extends beyond tires and into household goods like cooking oil and cosmetics. Uses for palm oil are broad compared to natural rubber, with biodiesel applications also being aggressively pursued.

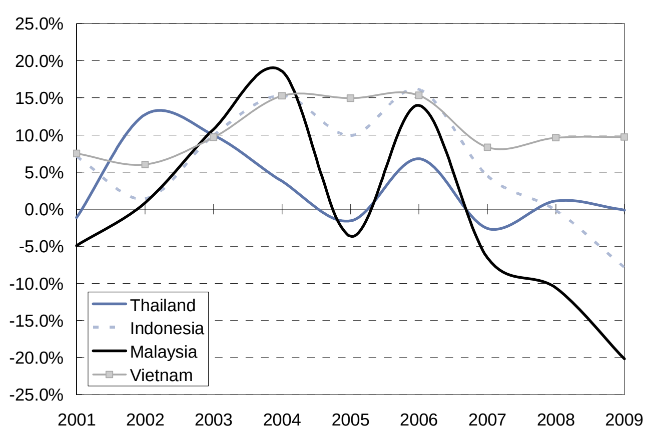
In Malaysia, land suitable for transplanting has largely been converted from natural rubber to palm trees thanks in part to government support and subsidies. Palm oil exports are greater than natural rubber in both volume and monetary terms. A similar situation is unfolding in Indonesia, where new plantation areas may end up as a sea of palm trees. We therefore think natural rubber volume growth may undershoot market expectations (see Exhibits 15-17).

Exhibit 32: Attractive palm oil incentives
Palm oil-related government incentives

Government measures to promote oil palm plantations	
Indonesia	
In Development	Plantations managed under a unified management structure (PIR method). Farmers can borrow funds and own land.
Alternative fuel	Presidential mandate issued in 2006 regarding the supply and use of palm oil as a bio fuel. Aiming to replace 10% of diesel fuel use and 50% of power generation fuel use in 2010.
Attracting foreign investment	New capital investment law: Income tax, import tax, and value-added tax exempted or waived, among others. Also applied to agriculture.
Malaysia	
In Development	Big development structure introduced by the Federal Land Development Authority (FELDA).
Alternative fuel	Permission to produce Envo Diesel bio fuel for the EU market. Diesel combination technology developed under the guidance of the Malaysia Palm Oil Board.

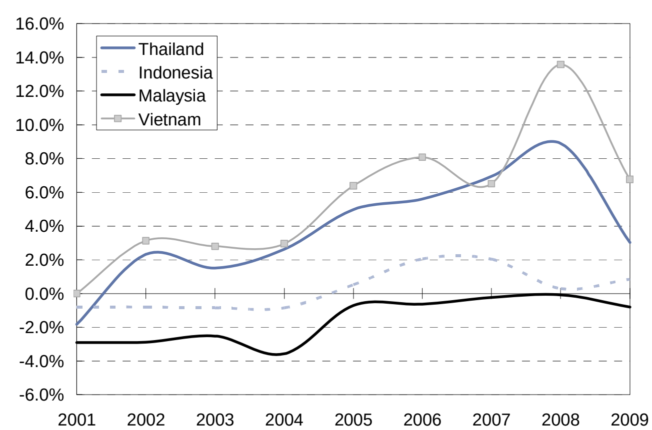
Source: FAO, various governmental bodies.

Exhibit 33: Sharp drop in natural rubber production in Malaysia/Indonesia
Natural rubber production volume (Yoy, %)



Source: IRSG

Exhibit 34: No growth in plantation land area
Ratio of plantation land surface area used for natural rubber cultivation



Source: IRSG

Exhibit 35: Sharp growth in palm oil production in Malaysia/Indonesia in the past five years

Natural rubber/ palm oil supply volumes

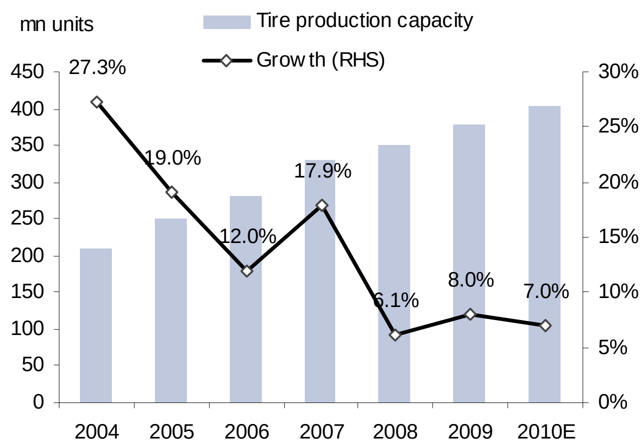
Unit:mn tonne	2005	2006	2007	2008	2009	CAGR 05-09	2010E	2011E
Malaysia								
Crude palm oil	15.20	15.49	15.29	17.57	17.26	2.6%	17.60	18.33
yoy		*1.9%*	*-1.2%*	*14.9%*	*-1.8%*		*2.0%*	*4.1%*
Natural rubber	1.13	1.28	1.20	1.07	0.86	-5.3%	0.86	0.87
yoy		*14.0%*	*-6.5%*	*-10.6%*	*-20.2%*		*0.6%*	*0.6%*
Indonesia								
Crude palm oil	13.54	15.52	16.73	18.88	20.14	8.3%	22.08	24.41
yoy		*14.6%*	*7.8%*	*12.9%*	*6.7%*		*9.6%*	*10.5%*
Natural rubber	2.27	2.64	2.76	2.75	2.53	2.2%	2.67	2.80
yoy		*16.1%*	*4.5%*	*-0.2%*	*-7.9%*		*5.3%*	*5.1%*

Source: Oil World, IRSG, Goldman Sachs Research estimates.

Risk of high rubber prices and stiffer tire competition

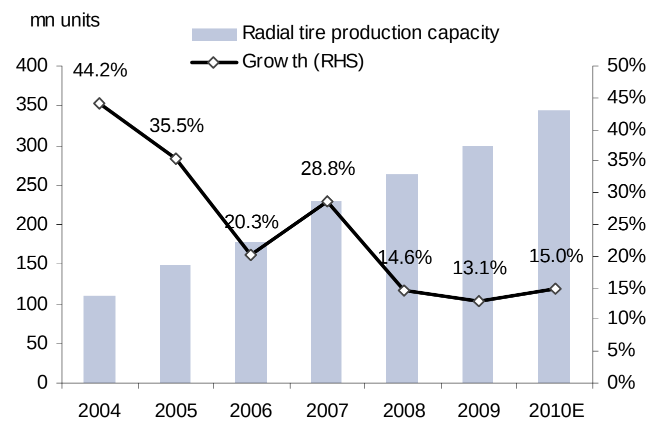
We expect domestic demand to expand sharply in China and India but given the many tire producers in these countries, we think oversupply is a long-term risk to bear in mind. Tire makers are rapidly expanding tire capacity for compact and mid-sized vehicles, where demand is expected to grow fastest, and there are concerns that competition may escalate. Japanese tire makers may need to shift down in their export mix given that their exports to China are in a high price zone (ASP is over ¥7,000). Due in part to the likely emergence of local startups and cut-throat competition, we think a shift down in demand to cheaper tires will probably erode the tire mix and pull down tire ASPs. As a result, we see considerable risk of margins eroding (see Exhibits 36-39).

Exhibit 36: CRIA expects overall Chinese tire capacity to grow about 7% in 2010



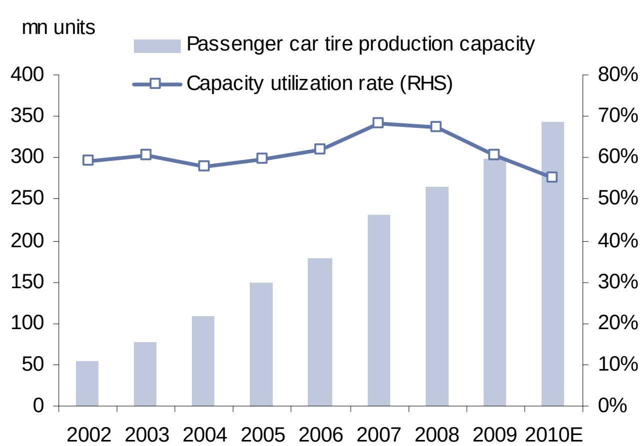
Source: CRIA, 2008-2009.

Exhibit 37: CRIA expects radial tire capacity to grow twice as fast in 2010, at nearly 15%



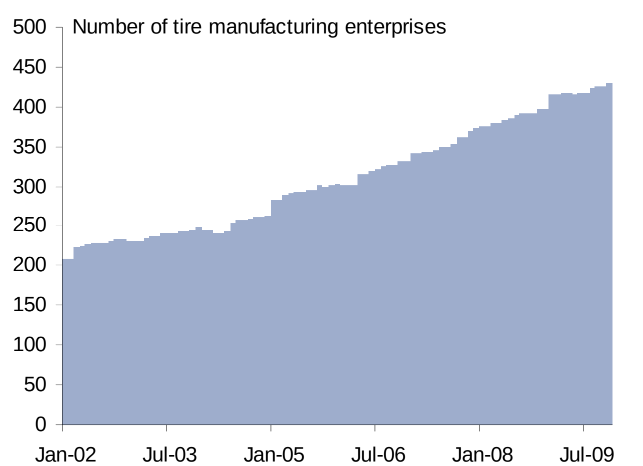
Source: CRIA, 2008-2009.

Exhibit 38: We expect oversupply to lower utilization
China tire capacity for passenger vehicles, utilization rates



Source: CRIA, IRSG, Goldman Sachs Research estimates.

Exhibit 39: Number of Chinese tire makers growing
No signs of consolidation



Source: CEIC.

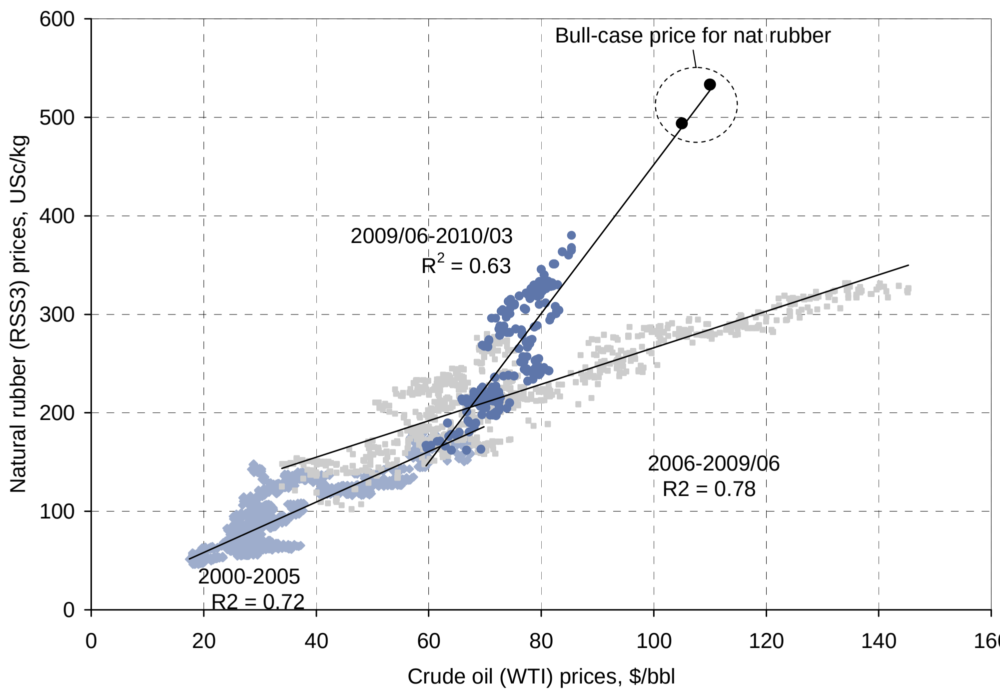
If oil price correlation entered new stage, US$5/kg is possible

Sustainability is unclear; we think a US$5/kg scenario is possible

Recent trends seem to indicate the correlation between natural rubber prices and crude oil prices has broken down. Rather than representing a breakdown, we think the regression line of the correlation has tilted upwards and shifted to the left (suggesting a higher price of rubber vs oil price than before). Supply-demand is an important determinant of price formation for a commodity, but price arbitrage is a constant consideration as the ratio of natural to synthetic rubber can be adjusted by 5% in either direction OK.

Riding strong momentum, natural rubber prices have climbed to new highs since June 2009, supported by tight supply/demand. If the price correlation based on current supply/demand dynamics holds up, it implies a natural rubber price of US$5/kg in 2011-2012 when our global ECS team forecasts oil prices of over US$100 bbl (see Exhibit 40).

Exhibit 40: Our 2011-2012 oil price forecasts imply a natural rubber price of US$5/kg
Correlation between natural rubber price and crude oil prices



Note: Our global equity oil team's oil price forecasts are US$110 bbl for 2011 and US$105 bbl for 2012.

Source: SICOM, NYMEX, Goldman Sachs Research estimates.

ACTION

Sell

Bridgestone (5108.T)

Return Potential: (12%)

Most exposed to input prices, volume shortfall a concern, Sell (CL)

Source of opportunity

Bridgestone has actively moved up the production chain so it is normally more resilient than peers to higher raw material prices. However, its positioning is now working against it due to the surge in core input prices (natural rubber and Butadiene) in FY12/10; we think it assumes a natural rubber price of about US$2.80/kg for FY3/11, and that current price rises are likely to have an adverse impact. Factoring in higher natural rubber/butadiene prices, we cut our operating profit forecast to ¥81.0 bn for FY12/10 and ¥109.0 bn for FY12/11. Our forecasts are about 20% below Bloomberg consensus numbers, which we expect to fall. Along with our forecast cuts, we lower our 12-month target price to ¥1,350 from ¥1,430 (potential downside of 12%). Our We reiterate our Sell rating and keep the stock on our Conviction List.

Catalyst

We estimate 1Q12/10 operating profits of ¥20-¥30 bn, putting it fairly close to 1H guidance for ¥31.0 bn. Yet it is still largely unclear to us whether it will raise guidance to reflect the 1Q overshoot or it will lower to factor in higher input prices from 2Q. We have serious concerns in the near term about its outlook and think it will face even stronger headwinds from a tough competitive climate given its high sales ratio to developed markets relative to peers, so we think it is too soon to re-rate the shares

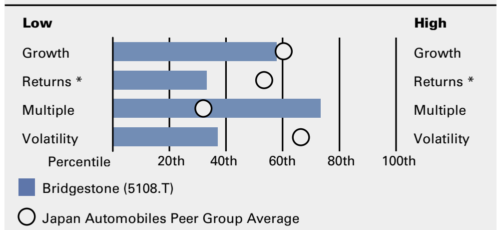
Valuation

Along the cuts to our forecasts, we lower our 12-month target price based on PB-ROE correlation to ¥1,350 from ¥1,430. Our new target implies a 0.96X P/B and a 34.6X P/E on our FY12/10 estimates.

Key risks

A stronger recovery in replacement tire demand in developed markets than we expect, price increases, raw material prices, and forex.

Investment Profile

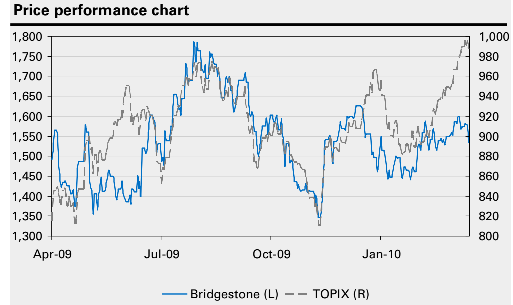


* Returns = Return on Capital. For a complete description of the investment profile measures please refer to the disclosure section of this document.

Key data	Current
Price (¥)	1,534
12 month price target (¥)	1,350
Market cap (¥bn)	1,197.3

Consolidated (¥bn)	12/09	12/10E	12/11E	12/12E
Revenue	2,597.0	2,841.0	3,075.0	3,205.0
yoy % chg.	(19.7)	9.4	8.2	4.2
Revenue CoE	--	2,830.0	--	--
Op. profit	75.7	81.0	109.0	131.0
yoy % chg.	(42.4)	7.0	34.6	20.2
Op. profit CoE	--	94.0	--	--
EPS (¥)	1.3	39.0	61.6	77.5
yoy % chg.	(90.0)	2,833.6	57.8	25.9
EPS CoE (¥)	--	57.4	--	--
P/E (X)	NM	39.3	24.9	19.8
P/B (X)	1.1	1.1	1.1	1.0
EV/EBITDA (X)	6.9	7.1	6.6	6.1

Price performance chart



Share price performance (%)	3 month	6 month	12 month
Absolute	(1.4)	(0.4)	2.9
Rel. to TOPIX	(5.9)	(10.3)	(14.9)

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 4/08/2010 close.

Bridgestone: Summary financials

Profit model (¥bn)	12/09	12/10E	12/11E	12/12E
Revenue	2,597.0	2,841.0	3,075.0	3,205.0
Cost of goods sold	(1,767.0)	(1,978.7)	(2,120.4)	(2,192.6)
Gross profit	**830.1**	**862.3**	**954.6**	**1,012.4**
SG&A and other	(754.3)	(781.3)	(845.6)	(881.4)
Operating profit	**75.7**	**81.0**	**109.0**	**131.0**
Net interest income/(expense)	(19.9)	(21.6)	(23.3)	(23.3)
Equity in earnings of affiliates	0.0	0.0	0.0	0.0
Net other nonoperating inc/(exp)	(1.3)	(3.3)	0.0	0.0
Recurring profit	**54.5**	**56.1**	**85.7**	**107.7**
Extraordinary income	4.1	0.0	0.0	0.0
Extraordinary expense	(23.1)	0.0	0.0	0.0
Pretax profit	**35.4**	**56.1**	**85.7**	**107.7**
Income tax	(29.2)	(20.0)	(30.0)	(38.0)
Minority interest	(5.1)	(5.5)	(7.4)	(8.9)
Net income	**1.0**	**30.6**	**48.3**	**60.8**
Capital expenditures (excl. leases)	--	--	--	--
Capital expenditures (incl. leases)	(191.2)	(210.0)	(230.0)	(240.0)
Depreciation & amortization	(175.7)	(175.0)	(179.0)	(183.0)
EPS (basic) (¥)	**1.3**	**39.0**	**61.6**	**77.5**
EPS (fully diluted) (¥)	**1.3**	**39.0**	**61.6**	**77.5**
BVPS (¥)	1,385.4	1,408.9	1,454.5	1,514.0
DPS (¥)	16.0	16.0	18.0	20.0
Dividend payout ratio (%)	1,203.0	41.0	29.2	25.8

Year-on-year change (%)	12/09	12/10E	12/11E	12/12E
Revenue	(19.7)	9.4	8.2	4.2
Operating profit	(42.4)	7.0	34.6	20.2
Recurring profit	(26.9)	3.0	52.8	25.7
Net income	(90.0)	NM	57.8	25.9
EPS (basic)	(90.0)	2,833.6	57.8	25.9
EPS (fully diluted)	(90.0)	2,833.6	57.8	25.9

Margins (%)	12/09	12/10E	12/11E	12/12E
Operating profit	2.9	2.9	3.5	4.1
EBITDA	9.7	9.0	9.4	9.8
Recurring profit	2.1	2.0	2.8	3.4
Net income	0.0	1.1	1.6	1.9

Cash flow statement (¥bn)	12/09	12/10E	12/11E	12/12E
Net income	1.0	30.6	48.3	60.8
D&A add-back	175.7	175.0	179.0	183.0
Minority interest add-back	5.1	5.5	7.4	8.9
Net (inc)/dec in working capital	116.5	(70.8)	(67.9)	(37.7)
Other operating cash flow	40.3	(7.4)	(4.1)	(4.1)
Cash flow from operations	**338.7**	**132.9**	**162.7**	**210.9**
Capital expenditures (incl. leases)	(191.2)	(210.0)	(230.0)	(240.0)
Purchases of long-term securities	0.0	0.0	0.0	0.0
Sales of long-term securities	0.0	0.0	0.0	0.0
Other investing cash flow	3.0	7.1	7.1	7.1
Cash flow from investments	**(188.3)**	**(202.9)**	**(222.9)**	**(232.9)**
Dividends paid (common & preferred)	(14.9)	(12.5)	(12.5)	(14.1)
Incr./(decr.) in debt	(16.6)	49.8	50.0	0.0
Common stock issuance	0.0	0.0	0.0	0.0
Other financing cash flow	7.0	(0.8)	(0.8)	(0.8)
Cash flow from financing	**(24.5)**	**36.5**	**36.7**	**(14.9)**
Total cash flow	**125.9**	**(33.6)**	**(23.6)**	**(37.0)**

Balance sheet (¥bn)	12/09	12/10E	12/11E	12/12E
Cash & equivalents	242.5	208.9	185.4	148.4
Accounts receivable	484.0	529.4	573.0	597.3
Inventory	435.3	476.2	515.4	537.2
Other current assets	112.7	26.6	12.4	16.1
Total current assets	**1,274.5**	**1,241.1**	**1,286.2**	**1,299.0**
Net PP&E	1,076.6	1,143.9	1,229.2	1,323.1
Net intangibles	38.7	38.7	38.7	38.7
Total investments	214.4	207.3	177.3	127.3
Other long-term assets	204.3	204.3	204.3	204.3
Total assets	**2,808.4**	**2,835.3**	**2,935.7**	**2,992.4**
Accounts payable	165.3	180.8	195.7	204.0
Short-term debt	241.4	241.0	241.0	241.0
Other current liabilities	356.0	277.0	269.4	262.2
Total current liabilities	**762.7**	**698.8**	**706.1**	**707.2**
Long-term debt	538.7	589.0	639.0	639.0
Other long-term liabilities	386.2	403.1	403.1	403.1
Total long-term liabilities	**924.9**	**992.1**	**1,042.1**	**1,042.1**
Total liabilities	**1,687.6**	**1,691.0**	**1,748.2**	**1,749.3**
Minority interest	33.9	39.4	46.8	55.7
Total common equity	**1,086.9**	**1,105.0**	**1,140.7**	**1,187.4**
Total liabilities & equity	**2,808.4**	**2,835.3**	**2,935.7**	**2,992.4**
Net debt	537.7	621.1	694.6	731.6

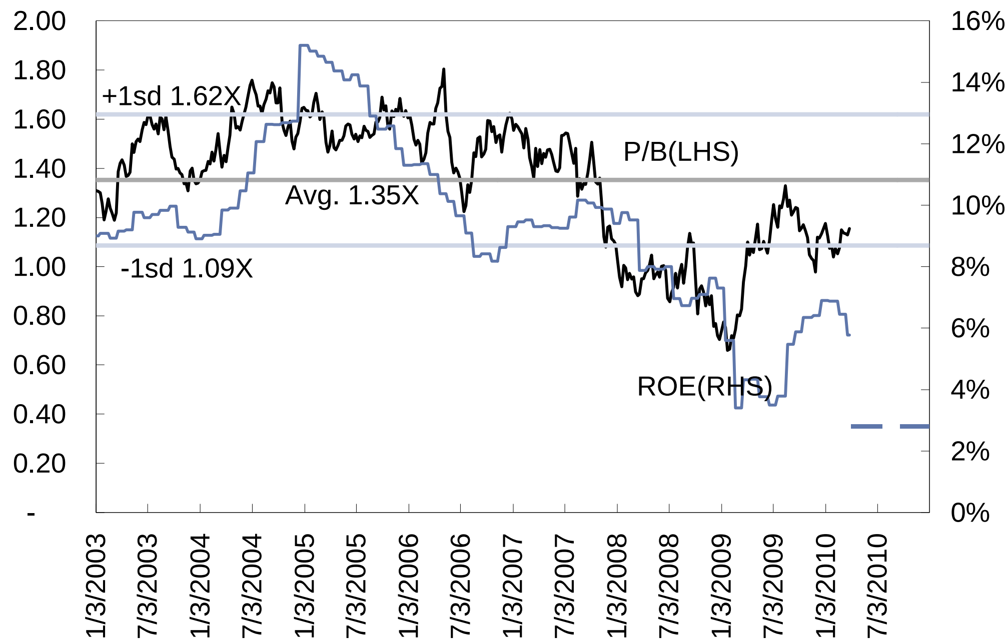
Ratios	12/09	12/10E	12/11E	12/12E
ROE (%)	0.1	2.6	4.6	5.5
ROA (%)	0.0	1.1	1.7	2.1
Net debt/equity (%)	39.2	62.7	63.9	66.2
Interest coverage ratio (X)	2.9	2.9	3.7	4.5

Valuation	12/09	12/10E	12/11E	12/12E
P/E (X)	NM	39.3	24.9	19.8
EV/EBITDA (X)	6.9	7.1	6.6	6.1
P/B (X)	1.1	1.1	1.1	1.0
Dividend yield (%)	1.0	1.0	1.2	1.3
FCF yield (%)	10.6	(8.2)	(7.5)	(4.4)

Note: Last actual year may include reported and estimated data.

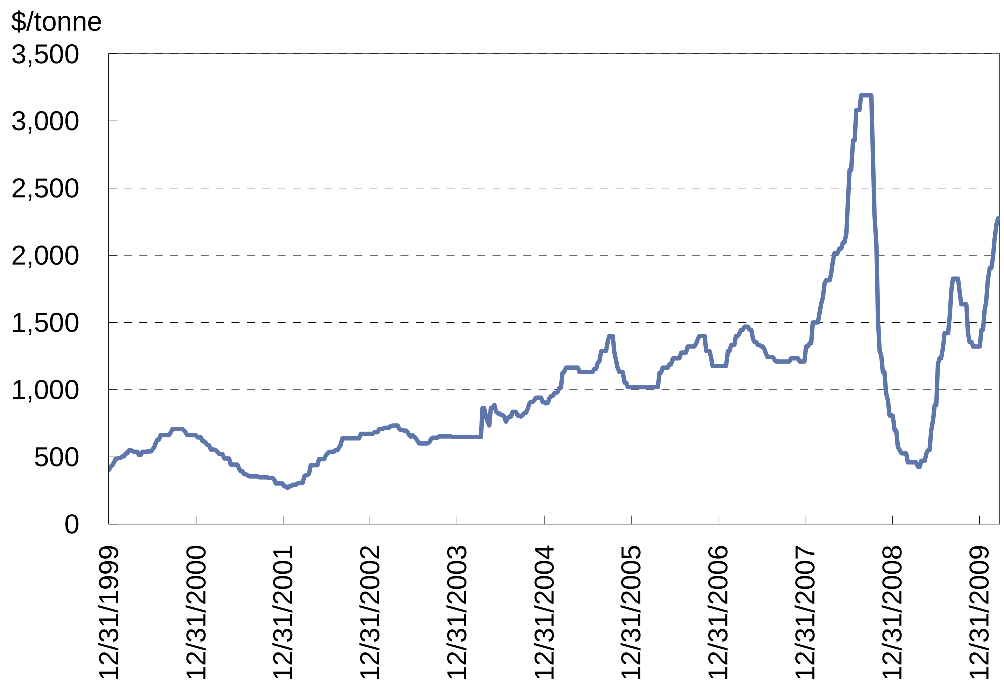
Source: Company data, Goldman Sachs Research estimates.

Exhibit 41: P/B-ROE correlation is an effective share price measure…and it suggests downside
Bridgestone: P/B-ROE correlation, X, %



Source: Datastream, Goldman Sachs Research.

Exhibit 42: Sharp rise in spot prices of buying-position butadiene
North American butadiene spot prices



Source: [Exhibit Source].

ACTION

Sell

Sumitomo Rubber Industries (5110.T)

Return Potential: (12%)

Down to Sell relative to coverage; 1Q potential overshoot priced in

Source of opportunity

We lower our FY12/10 op. profit forecast to ¥26.4 bn from ¥27.8 bn, and our 12-month target price to ¥730 from ¥750 on raised input cost assumptions. Our new target implies the second greatest potential downside (12%) in our Japan auto parts/tire coverage, after Bridgestone; we downgrade to Sell from Neutral. Positive 1Q earnings have led to a share price rise of around 10% in the past month (Bridgestone's shares trended flat). We think a 1H guidance raise is likely but (like peers) earnings will be curbed by rising input costs from 2Q on. We think a miss of full-year initial guidance miss is likely.

Catalyst

Current volumes, centered on the Falken brand, are trending above guidance and European offtake business appears off to a good start. 1H op. profit guidance is ¥7.0 bn, and we think 1Q (Jan.-Mar.) results will show good progress, coming in around ¥5.0 bn-¥7.0 bn. However, we think a 1Q overshoot will represent the end of near-term positive catalysts for Sumitomo Rubber. We do not think that volume growth in Europe and US will be able to fully offset the impact of higher unit costs. We project a gradual erosion of expectations which have trended high until now.

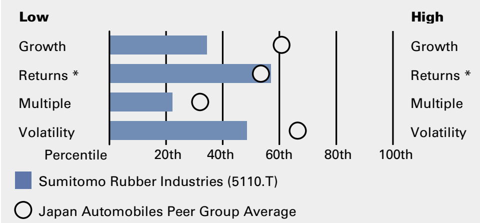
Valuation

Along with our revised estimates we lower our 12-month target price to ¥730 from ¥750. Our target price is based on P/B-ROE correlation and equals a P/B of 0.98X and a P/E of 16.2X on our FY12/10 estimates.

Key risks

Strong aftermarket tire demand recovery in the industrialized countries exceeding our expectations, price hike trends, input cost trends, forex.

Investment Profile

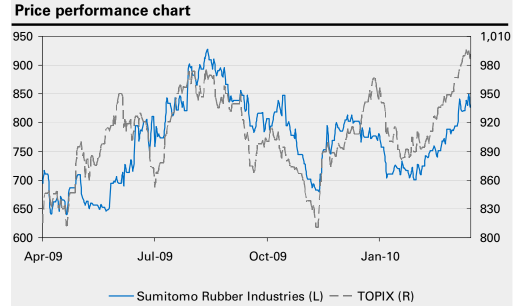


* Returns = Return on Capital For a complete description of the investment profile measures please refer to the disclosure section of this document.

Key data	Current
Price (¥)	827
12 month price target (¥)	730
Market cap (¥bn)	217.0

Consolidated (¥bn)	12/09	12/10E	12/11E	12/12E
Revenue	524.5	585.0	617.0	631.0
yoy % chg.	(13.3)	11.5	5.5	2.3
Revenue CoE	--	580.0	--	--
Op. profit	28.7	26.4	34.9	39.9
yoy % chg.	11.8	(8.1)	32.2	14.3
Op. profit CoE	--	27.0	--	--
EPS (¥)	34.7	45.0	63.7	74.3
yoy % chg.	743.3	29.8	41.5	16.8
EPS CoE (¥)	--	38.1	--	--
P/E (X)	23.9	18.4	13.0	11.1
P/B (X)	1.2	1.1	1.1	1.0
EV/EBITDA (X)	7.1	7.4	6.2	5.7

Price performance chart



Share price performance (%)	3 month	6 month	12 month
Absolute	6.8	2.5	19.2
Rel. to TOPIX	2.0	(7.7)	(1.5)

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 4/08/2010 close.

Sumitomo Rubber Industries: Summary financials

Profit model (¥bn)	12/09	12/10E	12/11E	12/12E
Revenue	524.5	585.0	617.0	631.0
Cost of goods sold	(334.2)	(393.0)	(405.8)	(408.1)
Gross profit	**190.3**	**192.0**	**211.2**	**222.9**
SG&A and other	(161.5)	(165.6)	(176.3)	(183.0)
Operating profit	**28.7**	**26.4**	**34.9**	**39.9**
Net interest income/(expense)	(3.6)	(4.0)	(4.0)	(4.0)
Equity in earnings of affiliates	3.5	0.0	0.0	0.0
Net other nonoperating inc/(exp)	(1.6)	(1.0)	(1.0)	(1.0)
Recurring profit	**20.0**	**21.4**	**29.9**	**34.9**
Extraordinary income	0.0	0.0	0.0	0.0
Extraordinary expense	(2.7)	0.0	0.0	0.0
Pretax profit	**17.3**	**21.4**	**29.9**	**34.9**
Income tax	(6.3)	(7.6)	(11.0)	(13.0)
Minority interest	(1.9)	(2.0)	(2.2)	(2.4)
Net income	**9.1**	**11.8**	**16.7**	**19.5**
Capital expenditures (excl. leases)	--	--	--	--
Capital expenditures (incl. leases)	(30.8)	(36.4)	(40.0)	(40.0)
Depreciation & amortization	(33.2)	(34.2)	(37.0)	(36.0)
EPS (basic) (¥)	**34.7**	**45.0**	**63.7**	**74.3**
EPS (fully diluted) (¥)	**34.7**	**45.0**	**63.7**	**74.3**
BVPS (¥)	712.9	742.2	787.5	842.0
DPS (¥)	18.0	16.0	18.0	20.0
Dividend payout ratio (%)	51.9	35.6	28.3	26.9

Year-on-year change (%)	12/09	12/10E	12/11E	12/12E
Revenue	(13.3)	11.5	5.5	2.3
Operating profit	11.8	(8.1)	32.2	14.3
Recurring profit	34.9	6.8	39.7	16.7
Net income	743.5	29.8	41.5	16.8
EPS (basic)	743.3	29.8	41.5	16.8
EPS (fully diluted)	743.3	29.8	41.5	16.8

Margins (%)	12/09	12/10E	12/11E	12/12E
Operating profit	5.5	4.5	5.7	6.3
EBITDA	11.8	10.4	11.7	12.0
Recurring profit	3.8	3.7	4.8	5.5
Net income	1.7	2.0	2.7	3.1

Cash flow statement (¥bn)	12/09	12/10E	12/11E	12/12E
Net income	9.1	11.8	16.7	19.5
D&A add-back	37.4	34.2	37.0	36.0
Minority interest add-back	1.9	2.0	2.2	2.4
Net (inc)/dec in working capital	(4.8)	(5.7)	(8.0)	(3.5)
Other operating cash flow	20.8	0.0	0.0	0.0
Cash flow from operations	**64.5**	**42.3**	**47.9**	**54.4**
Capital expenditures (incl. leases)	(30.8)	(36.4)	(40.0)	(40.0)
Purchases of long-term securities	0.0	0.0	0.0	0.0
Sales of long-term securities	0.0	0.0	0.0	0.0
Other investing cash flow	(3.5)	0.0	0.0	0.0
Cash flow from investments	**(34.3)**	**(36.4)**	**(40.0)**	**(40.0)**
Dividends paid (common & preferred)	(4.7)	(4.2)	(4.7)	(5.2)
Incr./(decr.) in debt	5.0	0.0	0.0	0.0
Common stock issuance	0.0	0.0	0.0	0.0
Other financing cash flow	(21.5)	(13.2)	5.5	(4.5)
Cash flow from financing	**(21.2)**	**(17.4)**	**0.8**	**(9.7)**
Total cash flow	**9.0**	**(11.5)**	**8.7**	**4.7**

Balance sheet (¥bn)	12/09	12/10E	12/11E	12/12E
Cash & equivalents	28.2	16.8	25.4	30.1
Accounts receivable	126.3	140.9	148.6	152.0
Inventory	74.4	83.0	87.6	89.6
Other current assets	26.4	26.2	26.2	26.2
Total current assets	**255.4**	**266.8**	**287.8**	**297.8**
Net PP&E	234.0	236.2	239.2	243.2
Net intangibles	15.3	15.3	15.3	15.3
Total investments	61.3	0.0	0.0	0.0
Other long-term assets	47.2	102.7	102.6	102.5
Total assets	**613.2**	**621.0**	**645.0**	**658.8**
Accounts payable	60.5	78.0	82.3	84.1
Short-term debt	87.3	63.6	63.6	63.6
Other current liabilities	52.3	46.6	47.2	47.5
Total current liabilities	**200.1**	**188.2**	**193.1**	**195.2**
Long-term debt	172.4	182.4	187.4	182.4
Other long-term liabilities	31.7	31.7	31.7	31.7
Total long-term liabilities	**204.1**	**214.1**	**219.1**	**214.1**
Total liabilities	**404.2**	**402.3**	**412.2**	**409.3**
Minority interest	22.0	24.0	26.2	28.6
Total common equity	**187.0**	**194.7**	**206.6**	**220.9**
Total liabilities & equity	**613.2**	**621.0**	**645.0**	**658.8**
Net debt	221.4	229.2	225.6	215.9

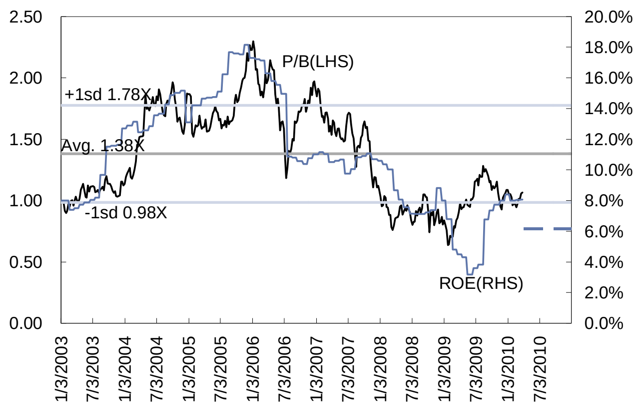
Ratios	12/09	12/10E	12/11E	12/12E
ROE (%)	4.9	6.2	8.3	9.1
ROA (%)	1.5	1.9	2.6	3.0
Net debt/equity (%)	118.4	117.7	109.2	97.7
Interest coverage ratio (X)	6.1	5.3	7.0	8.0

Valuation	12/09	12/10E	12/11E	12/12E
P/E (X)	23.9	18.4	13.0	11.1
EV/EBITDA (X)	7.1	7.4	6.2	5.7
P/B (X)	1.2	1.1	1.1	1.0
Dividend yield (%)	2.2	1.9	2.2	2.4
FCF yield (%)	13.9	0.9	1.8	4.8

Note: Last actual year may include reported and estimated data.

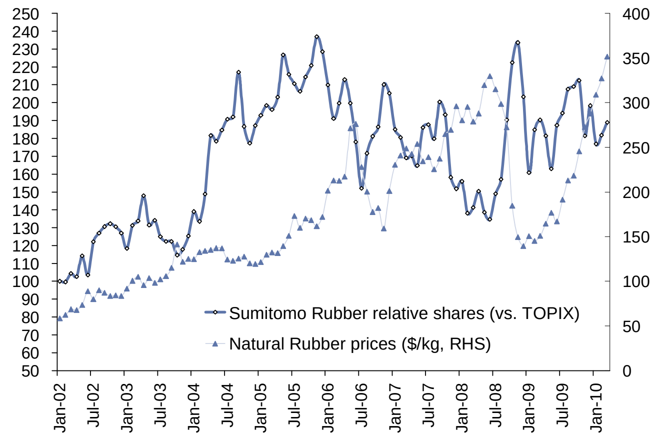
Source: Company data, Goldman Sachs Research estimates.

Exhibit 43: P/B-ROE correlation is an effective share price measure…and it suggests downside
Sumitomo Rubber: P/B-ROE correlation, X, %



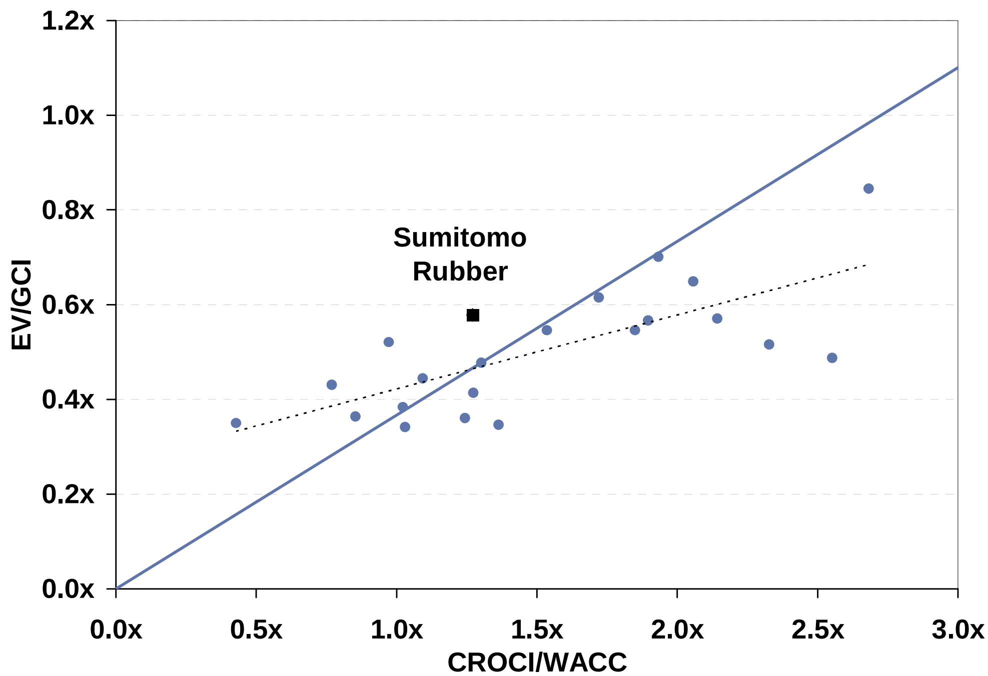
Source: Datastream, Goldman Sachs Research.

Exhibit 44: Natural rubber prices appear to have a big impact on share price
Sumitomo Rubber's relative share price and natural rubber price trend



Source: Datastream, Goldman Sachs Research.

Exhibit 45: Sumitomo Rubber looks unattractive within the Japanese auto sector based on its CF return valuation
Sumitomo Rubber: Director's Cut valuation



Source: [Exhibit Source].

ACTION

Sell

Hankook Tire (000240.KS)

Return Potential: (24%)

D/G to Conviction-Sell on near-term earnings risk, high expectations

Source of opportunity

We are downgrading Hankook Tire to Sell, adding it to our Conviction List and cutting our price target to W17,000 (24% potential downside). We believe that the rise in rubber and other material costs is likely to put pressure on Hankook's margins. While we expect tire companies to raise prices to offset rising costs, the slow recovery from the crisis, coupled with the fact that rubber is at a near 60-year high, will make it hard to completely offset the rising costs. We have cut our below-consensus (Bloomberg) estimates further: our new 2010 EPS estimate is 20% below consensus. We cut our 2010/11/12 EPS estimates by 15%/13%/9%.

Catalyst

We believe that Bloomberg consensus expectations that Hankook's 2010 OP and EPS will remain flat are too optimistic in light of the rising costs. We are expecting OP and EPS to be down 27% and 22% yoy, respectively based on our higher material price assumptions. The company's guidance for 2010 is also based on a natural rubber price of US$2,440/t (vs current price of US$3,800/t; we assume US$3,400/t). While 1Q earnings could be strong (no one-offs like 4Q, and cheaper inventory of rubber), we believe that 2Q could start a sequential drop in earnings.

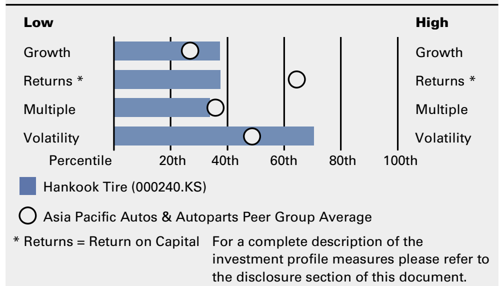
Valuation

Our new 12-month price target of W17,000 values Hankook at 1.2X book, below its mid-cycle multiple of 1.4X. As an efficient, low-cost producer, Hankook generates higher returns than global tire peers. Its strong market position in China, which accounted for 16% of 2009 pre-tax profit, also makes Hankook an attractive structural favorite within the sector. However, we believe that near-term earnings risk, coupled with currently-high expectations, makes the stock quite vulnerable.

Key risks

Rise in tire ASPs, drop in rubber prices, corporate actions, changes in FX, possible spillover from rival Kumho Tire's woes.

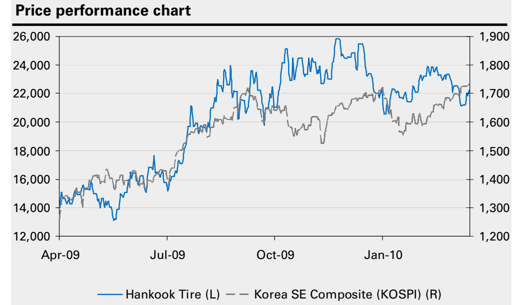
Investment Profile



Key data	Current
Price (W)	22,250
12 month price target (W)	17,000
Market cap (Wbn)	3,386.2

Parent (Wbn)	12/09	12/10E	12/11E	12/12E
Revenue	2,811.9	2,943.2	3,129.7	3,252.6
yoy % chg.	6.3	4.7	6.3	3.9
Revenue CoE	--	--	--	--
Op. profit	348.4	254.9	280.0	332.2
yoy % chg.	35.9	(26.8)	9.8	18.6
Op. profit CoE	--	--	--	--
EPS (W)	2,306	1,798	1,868	2,113
yoy % chg.	1,280.8	(22.0)	3.9	13.1
EPS CoE (W)	--	--	--	--
P/E (X)	9.7	12.4	11.9	10.5
P/B (X)	1.7	1.5	1.4	1.2
EV/EBITDA (X)	6.6	8.2	7.5	6.6

Price performance chart



Share price performance (%)	3 month	6 month	12 month
Absolute	(4.9)	9.1	58.9
Rel. to Korea SE Composite (KOSPI)	(7.0)	1.6	15.7

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 4/08/2010 close.

Hankook Tire: Summary financials

Profit model (W bn)	12/09	12/10E	12/11E	12/12E
Total revenue	**2,811.9**	**2,943.2**	**3,129.7**	**3,252.6**
Cost of goods sold	(1,963.0)	(2,187.9)	(2,317.7)	(2,383.8)
SG&A	(284.7)	(294.3)	(313.0)	(309.0)
R&D	--	--	--	--
Other operating profit/(expense)	(215.7)	(206.0)	(219.1)	(227.7)
EBITDA	**518.6**	**425.6**	**474.4**	**544.7**
Depreciation & amortization	(170.1)	(170.7)	(194.4)	(212.6)
EBIT	**348.4**	**254.9**	**280.0**	**332.2**
Interest income	10.4	17.3	12.2	8.3
Interest expense	(15.0)	(14.4)	(14.4)	(14.4)
Income/(loss) from uncons. subs.	16.0	32.5	33.6	34.4
Others	91.8	69.8	62.8	62.8
Pretax profits	**451.6**	**360.1**	**374.1**	**423.2**
Income tax	(100.7)	(86.4)	(89.8)	(101.6)
Minorities	0.0	0.0	0.0	0.0
Net income pre-preferred dividends	**350.9**	**273.7**	**284.3**	**321.6**
Preferred dividends	0.0	0.0	0.0	0.0
Net income (pre-exceptionals)	**350.9**	**273.7**	**284.3**	**321.6**
Post-tax exceptionals	0.0	0.0	0.0	0.0
Net income	**350.9**	**273.7**	**284.3**	**321.6**
EPS (basic, pre-except) (W)	2,306	1,798	1,868	2,113
EPS (basic, post-except) (W)	2,306	1,798	1,868	2,113
EPS (diluted, post-except) (W)	2,306	1,798	1,868	2,113
DPS (W)	350	360	380	430
Dividend payout ratio (%)	15.2	20.0	20.3	20.3
Free cash flow yield (%)	7.6	2.6	2.3	4.1

Growth & margins (%)	12/09	12/10E	12/11E	12/12E
Sales growth	6.3	4.7	6.3	3.9
EBITDA growth	24.9	(17.9)	11.4	14.8
EBIT growth	35.9	(26.8)	9.8	18.6
Net income growth	NM	(22.0)	3.9	13.1
EPS growth	1,280.8	(22.0)	3.9	13.1
Gross margin	30.2	25.7	25.9	26.7
EBITDA margin	18.4	14.5	15.2	16.7
EBIT margin	12.4	8.7	8.9	10.2

Cash flow statement (W bn)	12/09	12/10E	12/11E	12/12E
Net income pre-preferred dividends	350.9	273.7	284.3	321.6
D&A add-back	170.1	170.7	194.4	212.6
Minorities interests add-back	0.0	0.0	0.0	0.0
Net (inc)/dec working capital	(57.8)	(7.1)	(35.3)	(25.8)
Other operating cash flow	(25.4)	(32.5)	(33.6)	(34.4)
Cash flow from operations	**437.8**	**404.8**	**409.8**	**474.0**
Capital expenditures	(227.9)	(320.0)	(330.0)	(330.0)
Acquisitions	(55.7)	(30.0)	(30.0)	(30.0)
Divestitures	0.0	0.0	0.0	0.0
Others	40.3	(90.0)	(60.0)	(60.0)
Cash flow from investments	**(243.3)**	**(440.0)**	**(420.0)**	**(420.0)**
Dividends paid (common & pref)	(21.8)	(50.8)	(54.7)	(56.9)
Inc/(dec) in debt	(27.4)	0.0	0.0	0.0
Common stock issuance (repurchase)	0.0	0.0	0.0	0.0
Other financing cash flows	0.0	0.0	0.0	0.0
Cash flow from financing	**(49.2)**	**(50.8)**	**(54.7)**	**(56.9)**
Total cash flow	**145.4**	**(86.1)**	**(64.9)**	**(2.9)**

Balance sheet (W bn)	12/09	12/10E	12/11E	12/12E
Cash & equivalents	288.8	202.8	137.9	135.0
Accounts receivable	412.2	431.4	458.8	476.8
Inventory	379.8	397.5	422.7	439.3
Other current assets	172.6	172.6	172.6	172.6
Total current assets	**1,253.3**	**1,204.3**	**1,191.9**	**1,223.6**
Net PP&E	1,261.3	1,440.6	1,606.2	1,753.6
Net intangibles	10.5	10.5	10.5	10.5
Total investments	435.0	557.5	651.1	745.4
Other long-term assets	19.7	19.7	19.7	19.7
Total assets	**2,979.9**	**3,232.6**	**3,479.4**	**3,752.9**
Accounts payable	260.7	290.5	307.8	316.5
Short-term debt	101.9	101.9	101.9	101.9
Other current liabilities	294.7	298.6	300.7	308.2
Total current liabilities	**657.3**	**691.1**	**710.4**	**726.7**
Long-term debt	218.1	218.1	218.1	218.1
Other long-term liabilities	82.2	82.2	82.2	82.2
Total long-term liabilities	300.4	300.4	300.4	300.4
Total liabilities	**957.7**	**991.4**	**1,010.8**	**1,027.0**
Preferred shares	**0.0**	**0.0**	**0.0**	**0.0**
Total common equity	**2,022.2**	**2,241.2**	**2,468.6**	**2,725.9**
Minority interest	0.0	0.0	0.0	0.0
Total liabilities & equity	**2,979.9**	**3,232.6**	**3,479.4**	**3,752.9**
BVPS (W)	**13,287**	**14,726**	**16,221**	**17,911**

Ratios	12/09	12/10E	12/11E	12/12E
ROE (%)	18.7	12.8	12.1	12.4
ROA (%)	12.4	8.8	8.5	8.9
ROACE (%)	17.7	12.3	11.4	11.7
Inventory days	78.2	64.8	64.6	66.0
Receivables days	42.1	52.3	51.9	52.5
Payable days	45.0	46.0	47.1	47.8
Net debt/equity (%)	1.5	5.2	7.4	6.8
Interest cover - EBIT (X)	74.9	NM	125.1	54.2

Valuation	12/09	12/10E	12/11E	12/12E
P/E (analyst) (X)	9.7	12.4	11.9	10.5
P/B (X)	1.7	1.5	1.4	1.2
EV/EBITDA (X)	5.3	8.2	7.5	6.6
Dividend yield (%)	1.6	1.6	1.7	1.9

Note: Last actual year may include reported and estimated data.

Source: Company data, Goldman Sachs Research estimates.

Reg AC

We, Yuichiro Isayama, Rajeev Das and Tommy Wong, hereby certify that all of the views expressed in this report accurately reflect our personal views about the subject company or companies and its or their securities. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

Investment Profile

The Goldman Sachs Investment Profile provides investment context for a security by comparing key attributes of that security to its peer group and market. The four key attributes depicted are: growth, returns, multiple and volatility. Growth, returns and multiple are indexed based on composites of several methodologies to determine the stocks percentile ranking within the region's coverage universe.

The precise calculation of each metric may vary depending on the fiscal year, industry and region but the standard approach is as follows:

Growth is a composite of next year's estimate over current year's estimate, e.g. EPS, EBITDA, Revenue. **Return** is a year one prospective aggregate of various return on capital measures, e.g. CROCI, ROACE, and ROE. **Multiple** is a composite of one-year forward valuation ratios, e.g. P/E, dividend yield, EV/FCF, EV/EBITDA, EV/DACF, Price/Book. **Volatility** is measured as trailing twelve-month volatility adjusted for dividends.

Quantum

Quantum is Goldman Sachs' proprietary database providing access to detailed financial statement histories, forecasts and ratios. It can be used for in-depth analysis of a single company, or to make comparisons between companies in different sectors and markets.

Disclosures

Coverage group(s) of stocks by primary analyst(s)

Yuichiro Isayama: Japan-Automobiles. Rajeev Das: Asia Pacific Autos & Auto Parts, Asia Pacific Steel, Japan-Steel. Tommy Wong: Asia Pacific Autos & Auto Parts, Asia Pacific Infrastructure.

Asia Pacific Autos & Auto Parts: Bajaj Auto, Cheng Shin Rubber, Hankook Tire, Hero Honda Motors, Hyundai Mobis, Hyundai Motor, Kia Motors, Maruti Suzuki India, Taiwan Synthetic Rubber Corporation, Tata Motors.

Asia Pacific Infrastructure: China Communications Construction (H), China Railway Construction (A), China Railway Construction (H), China Railway Group (A), China Railway Group (H), Daqin Railway, Fujian Expressway, Guangshen Railway (A), Guangshen Railway (H), Guangxi Liugong, HAECO, Jiangsu Expressway (A), Jiangsu Expressway (H), Jiangxi Ganyue Expressway, Lonking Holdings, Sany Heavy, Shandong Expressway, Shenzhen Expressway (H), Shenzhen Expressway (A), SIA Engineering, Sichuan Expressway(H), Sichuan Expressway (A), Zhejiang Expressway.

Asia Pacific Steel: Dongkuk Steel Mill, Hyundai Steel, Jindal Steel & Power, JSW Steel, POSCO, POSCO (ADR), Sesa Goa, Steel Authority of India, Tata Steel.

Japan-Automobiles: Aisin Seiki, Bridgestone, Daihatsu Motor, Denso, F.C.C., Fuji Heavy Industries, Hino Motors, Honda Motor, Isuzu Motors, Keihin, Koito Mfg, Mazda Motor, Nissan Motor, Nissin Kogyo, Stanley Electric, Sumitomo Rubber Industries, Suzuki Motor, Toyoda Gosei, Toyota Boshoku, Toyota Motor, Yamaha Motor, Yokohama Rubber.

Japan-Steel: Daido Steel, JFE Holdings, Kobe Steel, Nippon Steel, Sanyo Special Steel, Sumitomo Metal Industries, Tokyo Steel Manufacturing.

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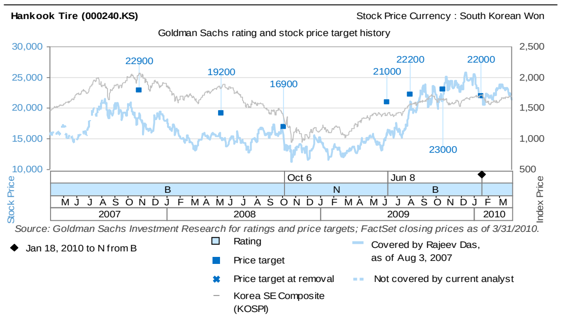
Price target and rating history chart(s)



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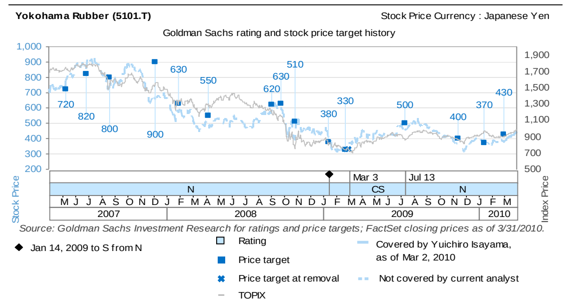

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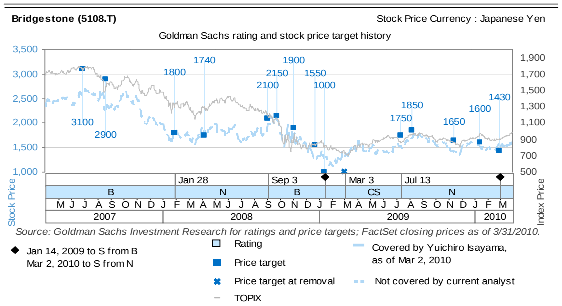

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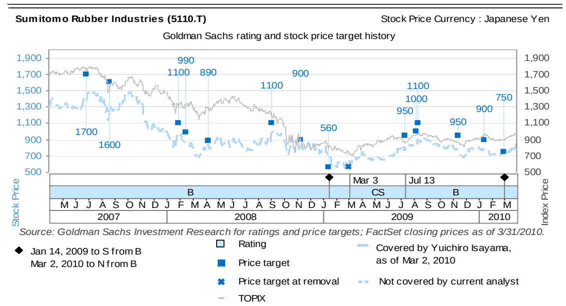

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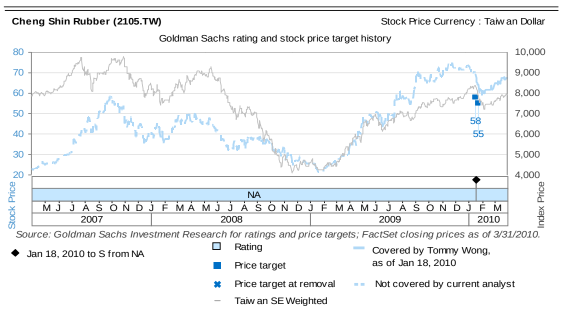

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