

Gudang Garam Tbk (GGRM)

Potential Surprises of 2019's Performance

Company Report | Nov 14, 2018

Buy

Dec 2019 TP (IDR) 100,000

Consensus Price (IDR)	86,915
TP to Consensus Price	+15.1%
vs. Last Price	+32.1%

Shares data

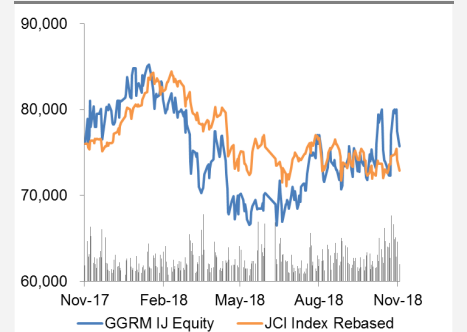
Last Price (IDR)	75,700
Price date as of	Nov 12, 2018
52 wk range (Hi/Lo)	85,275 / 66,525
Free float (%)	23.8
Outstanding sh.(mn)	1,924
Market Cap (IDR bn)	148,299
Market Cap (USD mn)	9,976
Avg. Trd Vol - 3M (mn)	1.02
Avg. Trd Val - 3M (bn)	76.09
Foreign Ownership	8.0%

Consumer Staples

Cigarette

Bloomberg	GGRM IJ
Reuters	GGRM.JK

Share Price Performance



	YTD	1M	3M	12M
Abs. Ret.	-7.1%	1.9%	-1.7%	-0.4%
Rel. Ret.	1.8%	1.6%	3.3%	3.7%

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Double-Digit Growth in Sales

GGRM's sales buoyed 15.5% from IDR21.2 trillion in 3Q17 to IDR24.5 trillion in 3Q18 thanks to **the machine-made clove cigarette (SKM) segment**—contributing 91% to the total sales—posting the surge of 16% in sales from IDR19.1 trillion in 3Q17 to IDR22.2 trillion in 3Q18.

Slowdown Margin in 3Q18

The net profit slightly snapped lower 3.8% from IDR2.29 trillion in 3Q17 to IDR2.2 trillion in 3Q18, albeit the double-digit growth in sales. The slowdown was attributable to the gross margin contraction from 22% in 3Q17 to 19.2% in 3Q18. Of note, the decline in gross margin was driven by **the soaring ratio of excise expenses to sales** from 54% in 3Q17 to 69% in 3Q18.

Postponement of Hike in Excises Rates on Cigarettes

The Indonesian government finally postponed the hike in the 2019 excises rates on cigarettes. On condition excises rates on tier 1 SKM are fixed at IDR590/cigarette, we estimate GGRM to enjoy the middle-single-digit growth in sales. **It is likely to prove a boon for GGRM to adjust to its cigarette selling prices** pursuant to inflation level and prevailing competition in markets. Besides, **its net profit margin is possible to buoy** from the prior estimate of 9.7% to 10%.

Target Price of IDR100,000

We use an estimate of the forward P/E of 17.0x (the 3-year average) as the basis of the valuation method for obtaining the target price. The target price implies a 2019E P/E of 19.5x. Now, GGRM is traded at a 2018E P/E of 18.7x.

Gudang Garam Tbk | Summary (IDR bn)

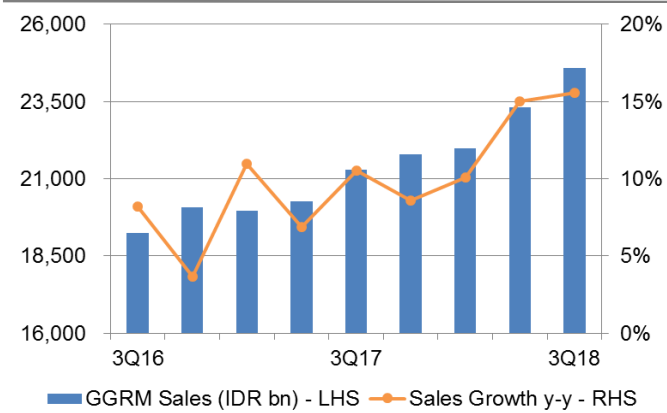
	2017	2018E	2019F	2020F
Sales	83,306	93,141	98,399	104,076
<i>Sales growth</i>	9.2%	11.8%	5.6%	5.8%
EBITDA	13,122	13,385	16,078	18,246
Net Profit	7,754	7,806	9,845	11,346
EPS (IDR)	4,030	4,057	5,117	5,897
<i>EPS growth</i>	16.1%	0.7%	26.1%	15.2%
BVPS (IDR)	21,926	23,373	25,890	29,187
EBITDA margin	15.8%	14.4%	16.3%	17.5%
NPM	9.3%	8.4%	10.0%	10.9%
ROE	18.4%	17.4%	19.8%	20.2%
ROA	11.6%	11.6%	14.2%	16.0%
ROIC	13.3%	13.0%	15.8%	17.6%
P/E	20.8x	18.7x	14.8x	12.8x
P/BV	3.8x	3.2x	2.9x	2.6x
EV/EBITDA	13.7x	12.1x	9.8x	8.4x
DPS (IDR)	2,600	2,600	2,600	2,600
<i>Dividend yield</i>	3.1%	3.4%	3.4%	3.4%

Source: Company Data, Bloomberg, NHKS Research

Please consider the rating criteria & important disclaimer

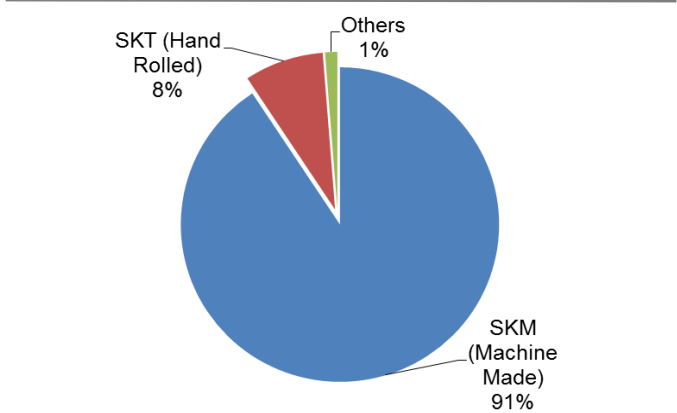
Performance Highlights

GGRM Quarterly Sales | 3Q16 - 3Q18



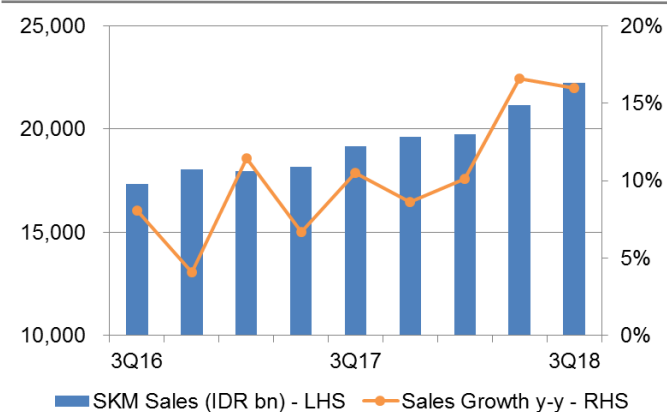
Source: Company, NHKS Research

GGRM Sales Breakdown | FY2018E



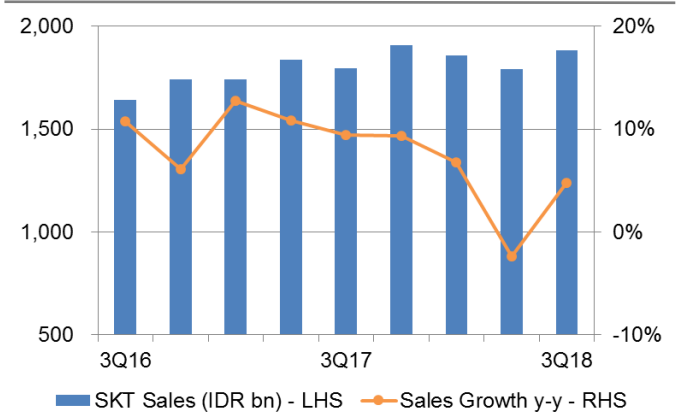
Source: Company, NHKS Research

SKM (Machine Made) Sales Trend | 3Q16 - 3Q18



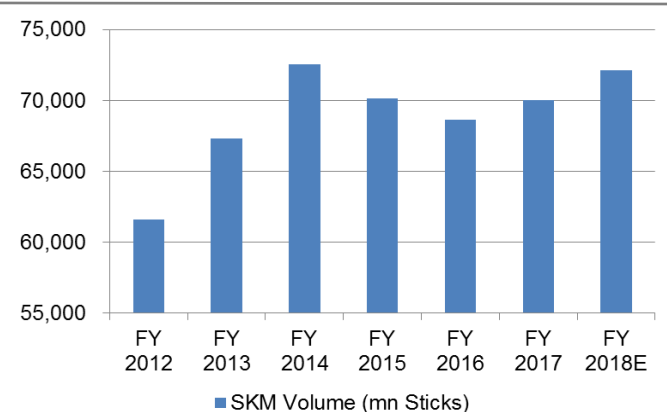
Source: Company, NHKS Research

SKT (Hand Made) Sales Trend | 3Q16 - 3Q18



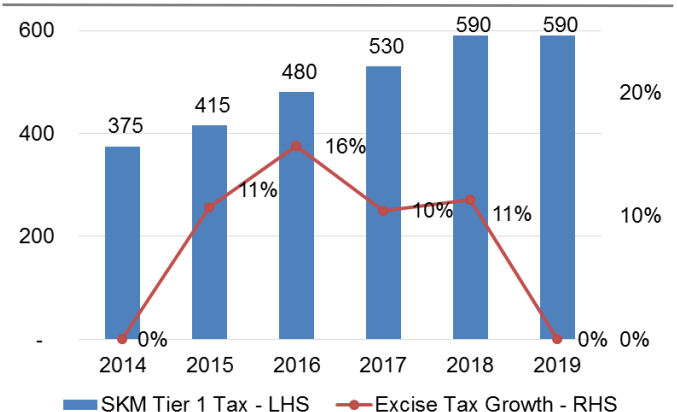
Source: Company, NHKS Research

GGRM SKM Volume (mn sticks) | FY2012 - FY2018E



Source: Company, NHKS Research

SKM Tier 1 Excise Tax (IDR) | 2014 - 2019



Source: Ministry of Finance, NHKS Research

3Q18 review (IDR bn)

	3Q17	4Q17	1Q18	2Q18	3Q18					4Q18E
					Actual	Estimate	y-y	q-q	surprise	
Sales	21,278	21,783	21,981	23,324	24,584	22,769	15.5%	5.4%	8.0%	23,252
Gross Profit	4,692	5,103	4,413	4,576	4,722	5,032	0.6%	3.2%	-6.2%	4,587
<i>Gross Margin</i>	22.0%	23.4%	20.1%	19.6%	19.2%	22.1%	-2.8%	-0.4%	-2.9%	19.7%
EBIT	3,281	3,384	2,723	2,286	3,173	3,658	-3.3%	38.8%	-13.2%	2,902
<i>EBIT Margin</i>	15.4%	15.5%	12.4%	9.8%	12.9%	16.1%	-2.5%	3.1%	-3.2%	12.5%
EBITDA	3,833	4,019	3,260	2,831	3,723	3,892	-2.9%	31.5%	-4.3%	3,571
<i>EBITDA Margin</i>	18.0%	18.4%	14.8%	12.1%	15.1%	17.1%	-2.9%	3.0%	-2.0%	15.4%
Net Profit	2,293	2,336	1,892	1,663	2,206	2,594	-3.8%	32.7%	-14.9%	2,045
<i>Net Margin</i>	10.8%	10.7%	8.6%	7.1%	9.0%	11.4%	-1.8%	1.8%	-2.4%	8.8%

Source: Bloomberg, NHKS research

Earnings revision (IDR bn)

		2018E	2019F	2020F
Sales	-Revised	93,141	98,399	104,076
	-Previous	91,075	99,626	109,033
	-Change	2.3%	-1.2%	-4.5%
Gross Profit	-Revised	18,297	21,157	23,477
	-Previous	19,403	21,220	23,224
	-Change	-5.7%	-0.3%	1.1%
Gross Margin	-Revised	19.6%	21.5%	22.6%
	-Previous	21.3%	21.3%	21.3%
EBIT	-Revised	11,085	13,656	15,543
	-Previous	12,434	13,626	14,912
	-Change	-10.9%	0.2%	4.2%
EBIT Margin	-Revised	11.9%	13.9%	14.9%
	-Previous	13.7%	13.7%	13.7%
EBITDA	-Revised	14,381	15,934	17,448
	-Previous	14,222	15,817	17,392
	-Change	1.1%	0.7%	0.3%
EBITDA Margin	-Revised	15.4%	16.2%	16.8%
	-Previous	15.6%	15.9%	16.0%
Net Profit	-Revised	7,806	9,845	11,346
	-Previous	8,736	9,662	10,641
	-Change	-10.6%	1.9%	6.6%
Net Margin	-Revised	8.4%	10.0%	10.9%
	-Previous	9.6%	9.7%	9.8%

Source: NHKS research

GGRM at A Glance

GGRM is the leading producer of clove cigarettes (*kretek*) identical with Indonesia. As the world's fourth most populous nations inhabited by around 250 million people, Indonesia is home to the biggest and most varied consumers markets with the significant adult smoker percentage—67% of Indonesian adult men are smokers. GGRM dominates 20.8% domestic market shares with its well-known products; and has 67 area offices with 279 distribution points across Indonesia as well as 7,000 vehicles as sale units, including motorcycles to serve its markets.

Its two *kretek* factories are located in Kediri and Gempol. Home to 249,000 inhabitants, Kediri is the regional trade heartland and the location of GGRM's headquarters. Meanwhile, its second *kretek* factory situated in Gempol, East Java, is only 50 km from Surabaya. The two factories prove a boon to responding to the demand for cigarettes.

GGRM's Competitiveness in the Asia Pacific (Emerging Market)

Categorized into cigarette company with topping 9-billion market capitalization, GGRM has the second cheapest P/E after KT&G Corp. However, it has a steep higher profit growth of 8.05%. In addition, its ROE of 20%, similar to that of ITC LTD; its relatively cheap valuation, virtually half of that of ITC make GGRM as top pick stocks for investors, with "growth" orientation.

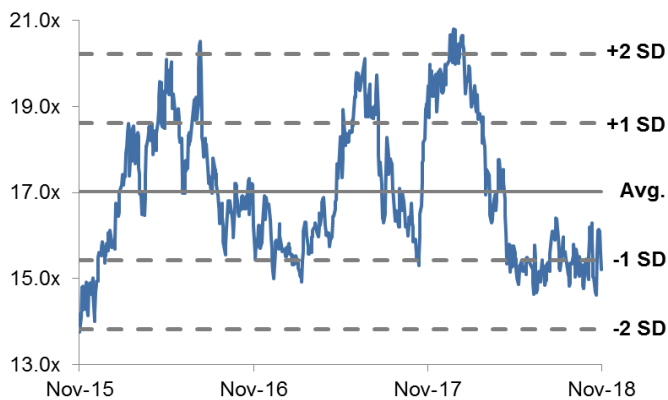
Asia Pacific Cigarette Company

Company	Market Cap (USD mn)	Asset (USD mn)	Sales LTM (USD mn)	Net Profit LTM (USD mn)	Net Profit Growth LTM	Net Margin	ROE LTM	P/E LTM	P/BV
Indonesia									
Gudang Garam	9,988	4,913	6,591	582	8.05%	8.8%	19.6%	18.3x	3.5x
HM Sampoerna	25,876	3,175	7,501	936	0.03%	12.5%	41.8%	29.5x	12.2x
India									
ITC Ltd	46,490	9,869	6,689	1,748	9.54%	26.1%	22.8%	29.8x	6.4x
VST Industries Ltd	638	163	147	28	20.04%	19.2%	32.5%	25.5x	8.0x
Godfrey Phillips India Ltd	593	379	355	25	15.94%	6.9%	9.2%	27.1x	2.4x
Kothari Products Ltd	41	547	976	9	-26.90%	0.9%	5.6%	5.4x	0.3x
Malaysia									
British American Tobacco	2,520	257	683	107	-38.20%	15.7%	102.2%	24.4x	25.1x
Pakistan									
Pakistan Tobacco Co Ltd	4,409	291	462	106	36.93%	22.9%	82.7%	48.4x	32.3x
Philippines									
PTFC Redevelopment Corp	19	8	3	1	16.49%	34.0%	16.5%	17.7x	3.2x
South Korea									
KT&G CORP	12,226	9,346	4,035	1,026	-8.52%	25.4%	15.8%	10.9x	1.7x
Sri Lanka									
Ceylon Tobacco Co Plc	1,515	162	370	104	34.49%	28.0%	256.9%	16.4x	37.7x
Vietnam									
CAT LOI JSC	38	34	84	6	6.74%	6.6%	22.6%	7.6x	1.4x
NGAN SON JSC	8	20	28	1	-13.79%	2.3%	9.1%	12.8x	1.1x

Source: Bloomberg

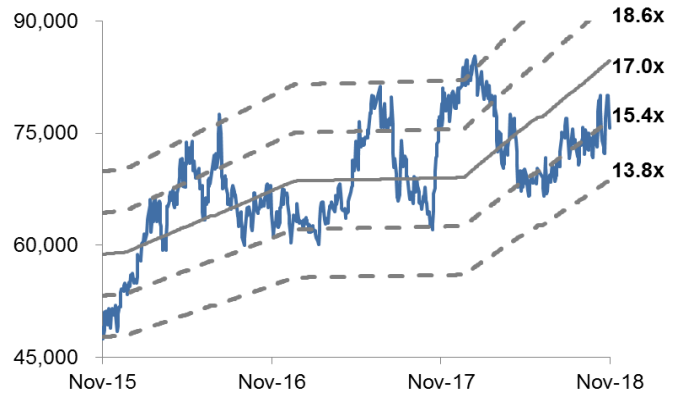
Multiple Valuation

Forward P/E band | Last 3 years



Source: NHKS research

Dynamic Forward P/E band | Last 3 years



Source: NHKS research

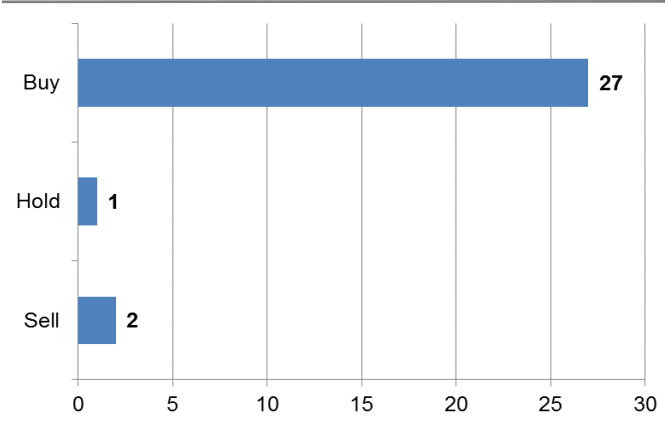
Rating and Target Price Update

Target Price Revision

Date	Rating	Target Price	Last Price	Consensus	vs Last Price	vs Consensus
04/13/2018	Buy	88,650 (Dec 2018)	74,200	88,527	+19.5%	+0.1%
07/11/2018	Buy	88,650 (Dec 2018)	70,975	85,741	+24.9%	+3.4%
09/18/2018	Buy	88,650 (Dec 2019)	74,400	84,866	+19.2%	+4.5%
11/14/2018	Buy	100,000 (Dec 2019)	75,700	86,915	+32.1%	+15.1%

Source: NHKS research, Bloomberg

Analyst Coverage Rating



Source: Bloomberg

Closing and Target Price



Source: NHKS research

NH Korindo Sekuritas Indonesia (NHKS) stock ratings

1. Period: End of year target price
2. Rating system based on a stock's absolute return from the date of publication
 - Buy : Greater than +15%
 - Hold : -15% to +15%
 - Sell : Less than -15%

Summary of Financials

INCOME STATEMENT				
(IDR bn)	2017/12A	2018/12E	2019/12E	2020/12E
Sales	83,306	93,141	98,399	104,076
<i>Growth</i>	9.2%	11.8%	5.6%	5.8%
COGS	(65,084)	(74,844)	(77,243)	(80,599)
Gross Profit	18,222	18,297	21,157	23,477
<i>Gross Margin</i>	21.9%	19.6%	21.5%	22.6%
Operating Expenses	(6,970)	(7,212)	(7,501)	(7,934)
EBIT	11,252	11,085	13,656	15,543
<i>EBIT Margin</i>	13.5%	11.9%	13.9%	14.9%
Depreciation	1,870	2,300	2,422	2,702
EBITDA	13,122	13,385	16,078	18,246
<i>EBITDA Margin</i>	15.8%	14.4%	16.3%	17.5%
Interest Expenses	(801)	(652)	(583)	(473)
EBT	10,437	10,487	13,129	15,131
Income Tax	(2,681)	(2,680)	(3,282)	(3,783)
Minority Interest	(2)	(1)	(2)	(2)
Net Profit	7,754	7,806	9,845	11,346
<i>Growth</i>	16.1%	0.7%	26.1%	15.2%
<i>Net Profit Margin</i>	9.3%	8.4%	10.0%	10.9%

PROFITABILITY & STABILITY				
	2017/12A	2018/12E	2019/12E	2020/12E
ROE	18.4%	17.4%	19.8%	20.2%
ROA	11.6%	11.6%	14.2%	16.0%
ROIC	13.3%	13.0%	15.8%	17.6%
Cash Dividend (IDR bn)	5,003	5,003	5,003	5,003
Dividend Yield	3.1%	3.4%	3.4%	3.4%
Payout Ratio	74.9%	64.5%	64.1%	50.8%
DER	48.8%	41.0%	30.0%	18.0%
Net Gearing	48.9%	41.0%	30.0%	18.0%
LT Debt to Equity	0.0%	0.0%	0.0%	0.0%
Capitalization Ratio	32.8%	29.1%	23.1%	15.3%
Equity Ratio	63.2%	66.6%	72.0%	79.3%
Debt Ratio	30.9%	27.3%	21.6%	14.3%
Financial Leverage	154.0%	153.2%	142.6%	130.6%
Current Ratio	193.6%	207.5%	237.8%	311.4%
Par Value (IDR)	500	500	500	500
Total Shares (mn)	1,924	1,924	1,924	1,924
Share Price (IDR)	83,800	75,700	75,700	75,700
Market Cap (IDR tn)	161.2	145.7	145.7	145.7

BALANCE SHEET				
(IDR bn)	2017/12A	2018/12E	2019/12E	2020/12E
Cash	2,329	2,470	2,781	2,974
Receivables	2,229	2,492	2,633	2,785
Inventories	37,920	36,946	34,533	32,280
Total Current Assets	43,764	42,928	41,100	39,125
Net Fixed Assets	21,409	22,476	25,958	29,500
Other Non Current Asset	1,587	2,159	2,159	2,159
Total Assets	66,760	67,564	69,217	70,784
Payables	1,214	1,396	1,440	1,503
ST Bank Loan	20,600	18,439	14,944	10,109
LT Debt	-	-	-	-
Total Liabilities	24,572	22,592	19,403	14,626
Capital Stock	1,016	1,016	1,016	1,016
Retained Earnings	41,187	43,990	48,833	55,176
Shareholders' Equity	42,188	44,972	49,815	56,159

VALUATION INDEX				
	2017/12A	2018/12E	2019/12E	2020/12E
Price /Earnings	20.8x	18.7x	14.8x	12.8x
Price /Book Value	3.8x	3.2x	2.9x	2.6x
Price/Sales	1.9x	1.6x	1.5x	1.4x
PE/EPS Growth	1.3x	27.7x	0.6x	0.8x
EV/EBITDA	13.7x	12.1x	9.8x	8.4x
EV/EBIT	16.0x	14.6x	11.6x	9.8x
EV (IDR bn)	179,495	161,589	157,783	152,755
Sales CAGR (3-Yr)	8.5%	9.8%	8.9%	7.7%
EPS CAGR (3-Yr)	12.8%	6.6%	13.8%	13.5%
Basic EPS (IDR)	4,030	4,057	5,117	5,897
Diluted EPS (IDR)	4,030	4,057	5,117	5,897
BVPS (IDR)	21,926	23,373	25,890	29,187
Sales PS (IDR)	43,296	48,408	51,141	54,091
DPS (IDR)	2,600	2,600	2,600	2,600

CASH FLOW STATEMENT				
(IDR bn)	2017/12A	2018/12E	2019/12E	2020/12E
Operating Cash Flow	8,205	11,319	14,500	16,331
Investing Cash Flow	(3,240)	(3,940)	(5,692)	(6,300)
Financing Cash Flow	(4,232)	(7,182)	(8,497)	(9,839)
Net Changes in Cash	733	197	311	193

OWNERSHIP		
By Geography	% Shareholders	%
Indonesia	92.0	Suryaduta Investama 69.3
United States	2.9	Suryamitra Kusuma 6.3
Luxembourg	2.1	Fil Limited 1.5
Ireland	0.6	Vanguard Group 0.8

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