

Gudang Garam Tbk (GGRM)

3Q20 Performance Driven By Robust Top Line Growth

GGRM reported solid revenue growth on the back of decent performance from both segments – hand rolled cloves and machine rolled cloves. Meanwhile, GGRM has declared not to distribute dividend this year and settled short term loan which resulted in improvement of DER.

3Q20 Revenue Beat Our Expectation

Gudang Garam (GGRM) booked 3Q20 revenue of IDR29.7tn (+2.6% YoY, +12.6% QoQ), achieving 73.9% and 74.5% of our and consensus estimate respectively. This revenue was above our expectations, as hand-rolled cloves (SKT) sales growth continued to increase at moderate pace by 8% YoY (vs. 6% in 3Q19). Meanwhile, machine-rolled cloves (SKM) sales was recorded at IDR26.6tn (+0.3% YoY, +12.8% QoQ). We see the demand for this segment was starting to show signs of recovery. Gross profit slumped by 25.2% YoY due to excise tax hike, which caused GPM to shrink by 540bps to 14.5% YoY in 3Q20. On margin side, EBIT margin and NPM declined by 600bps to 8.1% YoY and 410bps to 6.1% YoY respectively. The sharp decline in margins was largely due to higher opex. Thus, net profit in 3Q20 stood at IDR1.8tn (-38.3% YoY, +32.9% QoQ).

Dividend Not Distributed This Year

GGRM had distributed total dividend of IDR5tn (IDR2,600 per share) for four consecutive year. With that track record, AGM's decision to not to distribute dividends this year was unexpected. Based on our previous assumption, GGRM's next DPR will be at 46%, lower than the 4 years (FY16-19) average at 70.3% and still able to generate enough cash flow. In accordance with current circumstances, we have revised our DPR projection to 0%/64% for FY20E/FY21E. Meanwhile, we noticed that the total debt in 3Q20 has decreased significantly by 86% to IDR1.0tn, from IDR8.3tn in 2Q20. As a result, DER has improved to 2.09x in 3Q20 (vs. 15.5x in 2Q20).

Keep an Eye on The Cigarette Excise Tax Announcement

As stated in the 2021 Draft State Budget, the govt' has proposed for tobacco excise revenue increase by 4.8% YoY to IDR172.8tn, which indicates the excise tax is expected to hike next year even though Finance Ministerial Regulation 2021 (PMK/Peraturan Menteri Keuangan) has not been released. Our projection for excise tax growth for machine-rolled in FY21E will be around 10% (vs. ~25% in FY20), as significant increase in excise tax will negatively impact the sector.

Maintain BUY with lower TP Rp49,000/share

At the current share price, GGRM is traded at PE of around 9.6x (-2SD from its 3-year mean P/E). The share price is down by -22.4% YTD and has underperformed by -9.7% than JCI performance. In our view, the company is unlikely to fully pass on the excise tax to the buyers as the company needs to maintain its market share. The company also needs to keep an eye on the announcement of cigarette excise tax. Despite the unfavorable situation, we believe once purchasing power is back to normal, GGRM has ample room to increase ASP. As such, we retained our BUY rating with 18.4% potential upside from current share price and target P/E of 10.9x.

Gudang Garam Tbk | Summary (IDR bn)

	2019A	2020E	2021F	2022F
Sales	110.524	112.785	120.809	129.701
<i>Sales growth</i>	15,5%	2,0%	7,1%	7,4%
EBITDA	17.401	13.534	14.653	15.554
Net Profit	10.881	7.806	8.632	9.105
EPS (IDR)	5.655	4.057	4.486	4.732
<i>EPS growth</i>	39,6%	-28,3%	10,6%	5,5%
EBITDA margin	15,7%	12,0%	12,1%	12,0%
NPM	9,8%	6,9%	7,1%	7,0%
P/E	14,8x	10,2x	9,2x	8,7x
P/BV	3,2x	1,4x	1,3x	1,2x
EV/EBITDA	10,1x	6,9x	5,3x	5,0x
DPS (IDR)	2.600	-	2.600	2.600
<i>Dividend yield</i>	3,1%	0,0%	6,3%	6,3%

Source: Company Data, Bloomberg, NHKS Research

Please consider the rating criteria & important disclaimer

Buy

Target Price (IDR) 49,000

Consensus Price (IDR)	54,355
TP to Consensus Price	-9.9%
vs. Last Price	+18.4%

Shares data

Last Price (IDR)	41,400
Price date as of	Nov 09, 2020
52 wk range (Hi/Lo)	58,325 / 32,900
Free float (%)	23.8
Outstanding sh.(mn)	1,924
Market Cap (IDR bn)	81,581
Market Cap (USD mn)	5,773
Avg. Trd Vol - 3M (mn)	1.897
Avg. Trd Val - 3M (bn)	85.00
Foreign Ownership	8.0%

Consumer Staples

Cigarette

Bloomberg	GGRM IJ
Reuters	GGRM.JK

Share Price Performance



	YTD	1M	3M	12M
Abs. Ret.	-22.4%	-6.4%	-19.3%	-22.6%
Rel. Ret.	-7.6%	-12.4%	-23.1%	-9.3%

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3Q20 review (IDR bn)

	3Q19	4Q19	1Q20	2Q20	3Q20					4Q20E
					Actual	Estimate	y-y	q-q	surprise	
Sales	28.976	28.803	27.261	26.394	29.720	26.405	2,6%	12,6%	12,6%	29.410
Gross Profit	5.779	7.046	4.942	3.719	4.323	4.095	-25,2%	16,2%	5,6%	4.938
<i>Gross Margin</i>	19,9%	24,5%	18,1%	14,1%	14,5%	15,5%	-5,4%	0,5%	-1,0%	16,8%
EBIT	4.089	4.815	3.305	1.894	2.409	2.605	-41,1%	27,2%	-7,5%	3.232
<i>EBIT Margin</i>	14,1%	16,7%	12,1%	7,2%	8,1%	9,9%	-6,0%	0,9%	-1,8%	11,0%
EBITDA	4.695	5.573	3.966	2.559	3.082	3.288	-34,3%	20,4%	-6,3%	3.926
<i>EBITDA Margin</i>	16,2%	19,4%	14,5%	9,7%	10,4%	12,5%	-5,8%	0,7%	-2,1%	13,3%
Net Profit	2.962	3.637	2.447	1.374	1.826	1.773	-38,3%	32,9%	3,0%	2.425
<i>Net Margin</i>	10,2%	12,6%	9,0%	5,2%	6,1%	6,7%	-4,1%	0,9%	-0,6%	8,2%

Source: Bloomberg, NHKSI research

Earnings revision (IDR bn)

		2020E	2021F	2022F
Sales	-Revised	112.785	120.809	129.701
	-Previous	107.151	109.945	116.870
	-Change	5,3%	9,9%	11,0%
Gross Profit	-Revised	17.922	19.186	20.717
	-Previous	17.738	21.263	22.689
	-Change	1,0%	-9,8%	-8,7%
Gross Margin	-Revised	15,9%	15,9%	16,0%
	-Previous	16,6%	19,3%	19,4%
EBIT	-Revised	10.840	11.997	12.675
	-Previous	10.756	13.512	14.274
	-Change	0,8%	-11,2%	-11,2%
EBIT Margin	-Revised	9,6%	9,9%	9,8%
	-Previous	10,0%	12,3%	12,2%
EBITDA	-Revised	13.534	14.653	15.554
	-Previous	13.465	16.140	17.106
	-Change	0,5%	-9,2%	-9,1%
EBITDA Margin	-Revised	12,0%	12,1%	12,0%
	-Previous	12,6%	14,7%	14,6%
Net Profit	-Revised	7.806	8.632	9.105
	-Previous	7.443	9.790	10.417
	-Change	4,9%	-11,8%	-12,6%
Net Margin	-Revised	6,9%	7,1%	7,0%
	-Previous	6,9%	8,9%	8,9%

Source: NHKSI Research

A Glance at GGRM

GGRM is the leading producer of clove cigarettes (kretek) identical with Indonesia. As the world's fourth most populous nations inhabited by around 266 million people, Indonesia is home to the largest and most varied consumers markets with the significant adult smoker percentage—67% of Indonesian adult men are smokers. GGRM dominates 23.1% domestic market shares with its well-known products; and has 66 area offices with 269 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 268,000 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.

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	5.773	5.680	7.752	642	0,12%	8,3%	17,9%	8.8x	1.4x
HM Sampoerna	12.387	3.676	6.986	826	-16,61%	11,8%	43,0%	14.7x	6.6x
India									
ITC Ltd	29.520	10.264	6.911	2.160	21,55%	31,3%	24,6%	14.3x	3.4x
VST Industries Ltd	701	185	175	43	34,05%	24,5%	41,9%	17.1x	6.6x
Godfrey Phillips India Ltd	626	437	402	54	47,85%	13,5%	18,2%	12.1x	2.1x
Malaysia									
British American Tobacco	784	251	550	63	-26,77%	11,5%	72,2%	12.1x	8.9x
Pakistan									
Pakistan Tobacco Co Ltd	2.471	261	369	89	29,17%	24,1%	73,6%	27.6x	19.7x
South Korea									
KT&G CORP	10.380	9.275	4.323	825	-5,73%	19,1%	12,2%	10.9x	1.2x
Sri Lanka									
Ceylon Tobacco Co Plc	980	147	188	87	-13,79%	46,2%	233,8%	11.3x	31.4x

Source: Bloomberg

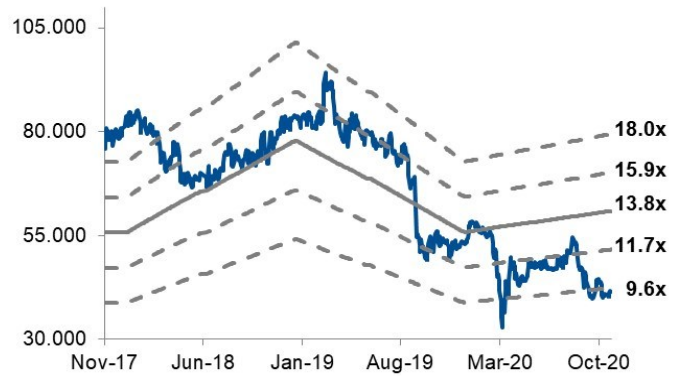
Multiple Valuation

Forward P/E band | Last 3 years



Source: NHKSI research

Dynamic Forward P/E band | Last 3 years



Source: NHKSI research

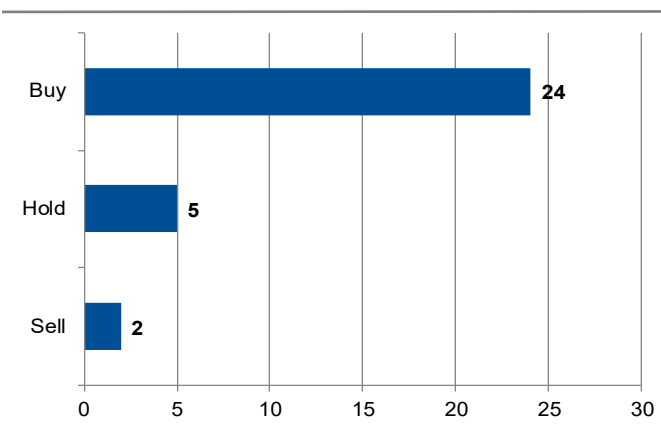
Rating and Target Price Update

Target Price Revision

Date	Rating	Target Price	Last Price	Consensus	vs Last Price	vs Consensus
09/18/2018	Buy	88,650	74,400	84,866	+19.2%	+4.5%
11/14/2018	Buy	100,000	75,700	86,915	+32.1%	+15.1%
09/24/2019	Buy	77,075	55,425	79,797	+35.5%	-5.9%
12/30/2019	Buy	61,800	52,400	59,865	+17.9%	+3.2%
05/26/2020	Buy	59,550	49,300	55,569	+20.8%	+7.2%
11/17/2020	Buy	49,000	41,400	54,355	+18.4%	-9.9%

Source: NHKSI research, Bloomberg

Analyst Coverage Rating



Source: Bloomberg

Closing and Target Price



Source: NHKSI research

Summary of Financials

INCOME STATEMENT

(IDR bn)	2019/12A	2020/12E	2021/12E	2022/12E
Sales	110.524	112.785	120.809	129.701
<i>Growth</i>	15,5%	2,0%	7,1%	7,4%
COGS	(87.741)	(94.864)	(101.623)	(108.984)
Gross Profit	22.783	17.922	19.186	20.717
<i>Gross Margin</i>	20,6%	15,9%	15,9%	16,0%
Operating Expenses	(7.912)	(7.082)	(7.188)	(8.041)
EBIT	14.872	10.840	11.997	12.675
<i>EBIT Margin</i>	13,5%	9,6%	9,9%	9,8%
Depreciation	2.530	2.694	2.655	2.879
EBITDA	17.401	13.534	14.653	15.554
<i>EBITDA Margin</i>	15,7%	12,0%	12,1%	12,0%
Interest Expenses	(599)	(388)	(285)	(320)
EBT	14.488	10.407	11.665	12.304
Income Tax	(3.607)	(2.602)	(3.033)	(3.199)
Minority Interest	0	-	-	-
Net Profit	10.881	7.806	8.632	9.105
<i>Growth</i>	39,6%	-28,3%	10,6%	5,5%
<i>Net Profit Margin</i>	9,8%	6,9%	7,1%	7,0%

PROFITABILITY & STABILITY

	2019/12A	2020/12E	2021/12E	2022/12E
ROE	21,4%	13,2%	13,8%	13,6%
ROA	13,8%	9,7%	10,2%	10,4%
ROIC	16,4%	13,3%	13,7%	13,6%
Cash Dividend (IDR bn)	5.003	-	5.003	5.003
Dividend Yield	3,1%	0,0%	6,3%	6,3%
Payout Ratio	64,2%	0,0%	64,1%	58,0%
DER	33,8%	3,5%	3,7%	3,3%
Net Gearing	33,9%	3,5%	3,7%	3,3%
LT Debt to Equity	0,0%	0,0%	0,0%	0,0%
Capitalization Ratio	25,3%	3,4%	3,6%	3,2%
Equity Ratio	64,8%	73,6%	74,0%	76,4%
Debt Ratio	21,9%	2,6%	2,7%	2,5%
Financial Leverage	153,8%	144,5%	135,5%	132,9%
Current Ratio	206,2%	275,9%	279,8%	308,5%
Par Value (IDR)	500	500	500	500
Total Shares (mn)	1.924	1.924	1.924	1.924
Share Price (IDR)	83.800	41.400	41.400	41.400
Market Cap (IDR tn)	161,2	79,7	79,7	79,7

BALANCE SHEET

(IDR bn)	2019/12A	2020/12E	2021/12E	2022/12E
Cash	3.572	3.913	4.658	5.808
Receivables	1.876	3.245	3.475	3.731
Inventories	42.847	42.754	44.631	44.340
Total Current Assets	52.081	51.414	54.236	55.323
Net Fixed Assets	25.374	27.384	28.957	30.617
Other Non Current Asset	1.192	1.408	1.422	1.436
Total Assets	78.647	80.205	84.615	87.376
Payables	1.297	1.274	1.364	1.463
ST Bank Loan	17.236	2.065	2.317	2.202
LT Debt	-	-	-	-
Total Liabilities	27.717	21.202	21.983	20.641
Capital Stock	1.016	1.016	1.016	1.016
Retained Earnings	49.948	58.020	61.650	65.752
Shareholders' Equity	50.931	59.003	62.632	66.735

VALUATION INDEX

	2019/12A	2020/12E	2021/12E	2022/12E
Price /Earnings	14,8x	10,2x	9,2x	8,7x
Price /Book Value	3,2x	1,4x	1,3x	1,2x
Price/Sales	1,5x	0,7x	0,7x	0,6x
PE/EPS Growth	0,4x	-0,4x	0,9x	1,6x
EV/EBITDA	10,1x	6,9x	5,3x	5,0x
EV/EBIT	11,9x	8,6x	6,5x	6,1x
EV (IDR bn)	176.493	93.288	77.776	77.283
Sales CAGR (3-Yr)	10,8%	13,2%	10,6%	8,1%
EPS CAGR (3-Yr)	6,6%	17,7%	0,2%	3,5%
Basic EPS (IDR)	5.655	4.057	4.486	4.732
Diluted EPS (IDR)	5.655	4.057	4.486	4.732
BVPS (IDR)	26.470	30.665	32.552	34.684
Sales PS (IDR)	57.442	58.617	62.787	67.409
DPS (IDR)	2.600	-	2.600	2.600

CASH FLOW STATEMENT

(IDR bn)	2019/12A	2020/12E	2021/12E	2022/12E
Operating Cash Flow	10.948	20.803	9.712	10.709
Investing Cash Flow	(4.818)	(5.287)	(4.217)	(4.441)
Financing Cash Flow	(4.606)	(15.070)	(4.750)	(5.118)
Net Changes in Cash	1.524	446	745	1.151

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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1. Based on a stock's forecasted absolute return over a period of 12 months from the date of publication.
2. Rating system based on a stock's potential upside from the date of publication
 - Buy : Greater than +15%
 - Overweight : +5% to 15%
 - Hold : -5% to +5%
 - Underweight : -5% to -15%
 - Sell : Less than -15%

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