

# Gudang Garam Tbk (GGRM)

## Resilience as Pressures of Tax Are On



Company Report | Sep 24, 2019

### Buy

<b>Dec 2019 TP (IDR)</b>	<b>75,075</b>
Consensus Price (IDR)	79,797
TP to Consensus Price	-5.9%
vs. Last Price	+35.5%

#### Shares data

Last Price (IDR)	55,425
Price date as of	Sep 18, 2019
52 wk range (Hi/Lo)	94,400 / 54,600
Free float (%)	23.8
Outstanding sh.(mn)	1,924
Market Cap (IDR bn)	106,113
Market Cap (USD mn)	7,593
Avg. Trd Vol - 3M (mn)	1.93
Avg. Trd Val - 3M (bn)	135.44
Foreign Ownership	8.0%

#### Consumer Staples

##### Cigarette

Bloomberg	GGRM IJ
Reuters	GGRM.JK

Although the cigarette industry was modest in 1H19, GGRM jostled for posting double-digit growth on grounds of solid sales volume and FY19's unchanged cigarette excise taxes.

#### 1H19 Double Digit Growth

GGRM posted for 1H19 sound performance, given a 16.4% y-y growth to IDR52,7 trillion in revenues; a 20.2% y-y gains to IDR5.7 trillion in operational profits, and double-digit growth or 20.4% y-y increase to IDR4.2 trillion in net profits. In 1H19, double-digit growth in top and bottom line was driven by a 14.7% y-y sales growth to 46.6 billion cigarettes. Full Flavor machine-made clove cigarettes (Sigaret Kretek Mesin Full Flavor, SKM FF) dominating domestic market share strived for sales of 38.3 billion cigarettes or a 15.5% y-y. Then, hand-rolled cigarettes (Sigaret Kretek Tangan, SKT) and machine-made cigarettes with low nicotine and tar contents (Sigaret Kretek Mesin Low Tar and Nicotine, SKM LTN) respectively posting sales of 4.2 billion cigarettes.

#### Pressuring Regulations

After unchanged cigarettes excise taxes during FY19, the Ministry of Finance rolled out the hike of 23% in cigarette taxes and the increase of 35% y-y in retail selling prices (Harga Jual Eceran, HJE) to take into effect on January 1st, 2020. We consider that the hike will narrow revenue margins and operational profits due to decreases in sales volume. The sales volume of SKM in FY19 is estimated to hit ~11% y-y or 85 billion cigarettes, but its FY20 growth is likely to decline to ~9% y-y or 78 billion cigarettes, coupled with the hike in average selling prices. Based on Nielsen research, in 1H19, the cigarette industry weakened by 8.6% y-y lower than that in 1H18; thus, we revise our target price to IDR75,075 or a 29.74%, with the estimated COGS growth of ~8% y-y.

#### Launching New Products

On August 5, 2019, GGRM launched new SKT product, Gudang Garam Patra, given the fact that sales of its SKT products grew by 2.4% y-y in 1H19. We believe that the launch of new products will drive sales up.

#### Maintain Buy with the Price Target of IDR75,075

We maintain BUY recommendation, with the target price of IDR75,075 based on the estimated forward P/E valuation of 22.1x and a 5.9% yield upside potential of the current stock price. Indonesia's second rating after China in Top 10 Consumers of Cigarettes is fundamental to support the cigarette industry outlook, not to mention that benign inflation keeping consumers purchasing power in check is another positive catalyst for the industry outlook. Adding to low inflation is rising retail selling prices having little impact on GGRM as prior to the hike, SKM selling price is affordable for smokers.

#### Gudang Garam Tbk | Summary (IDR bn)

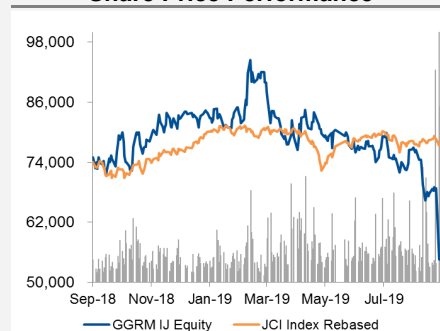
	2018A	2019E	2020F	2021F
Sales	95,708	106,301	112,259	131,124
<i>Sales growth</i>	14.9%	11.1%	5.6%	16.8%
EBITDA	13,374	13,567	11,751	12,852
Net Profit	7,792	7,830	6,541	7,205
EPS (IDR)	4,050	4,070	3,399	3,744
<i>EPS growth</i>	0.5%	0.5%	-16.5%	10.1%
BVPS (IDR)	23,457	24,926	25,726	26,871
EBITDA margin	14.0%	12.8%	10.5%	9.8%
NPM	8.1%	7.4%	5.8%	5.5%
P/E	20.7x	13.6x	16.3x	14.8x
P/BV	3.6x	2.2x	2.2x	2.1x
EV/EBITDA	13.2x	8.3x	9.4x	8.7x
DPS (IDR)	2,600	2,600	2,600	2,600
<i>Dividend yield</i>	3.1%	4.7%	4.7%	4.7%

Source: Company Data, Bloomberg, NHKS Research

Please consider the rating criteria & important disclaimer

NH Korindo Sekuritas Indonesia

#### Share Price Performance



	YTD	1M	3M	12M
Abs. Ret.	-33.9%	-27.7%	-28.3%	-23.2%
Rel. Ret.	-41.1%	-27.3%	-28.6%	-31.2%

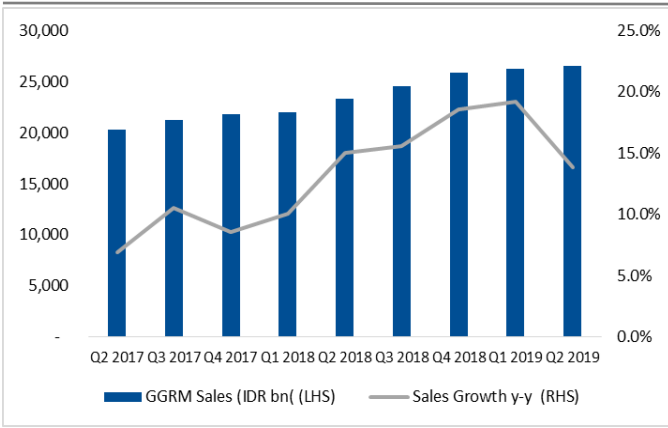
#### Putu Chantika Putri D.

+62 21 797 6202, ext:114

putu.chantika@nhsec.co.id

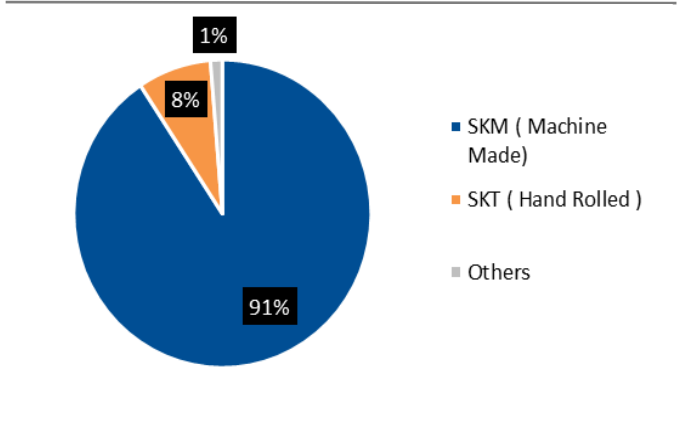
## Performance Highlights

GGRM Quarterly Sales | 2Q17 - 2Q19



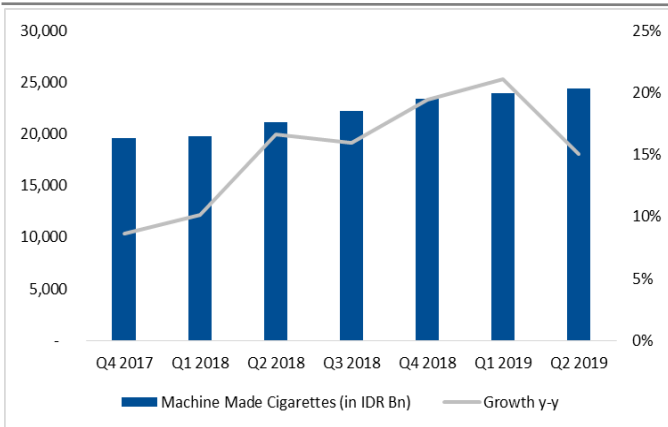
Source: Company, NHKS Research

GGRM Sales Breakdown | FY2019



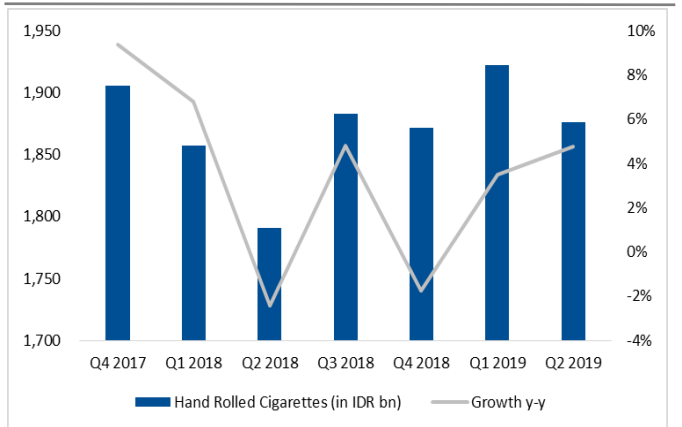
Source: Company, NHKS Research

SKM (Machine Made) Sales Trend | 4Q17 - 2Q19



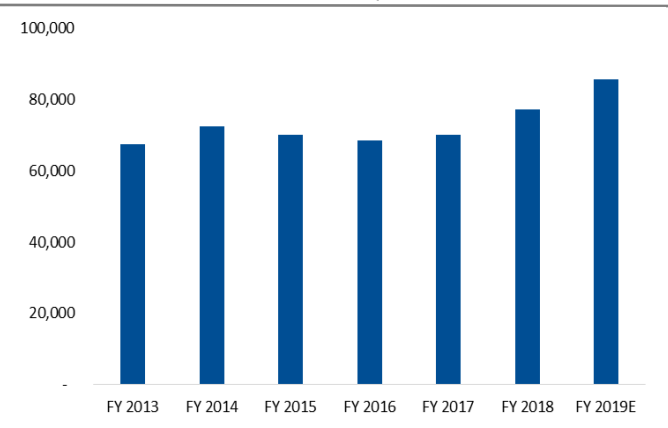
Source: Company, NHKS Research

SKT (Hand Made) Sales Trend | 4Q17 - 2Q19



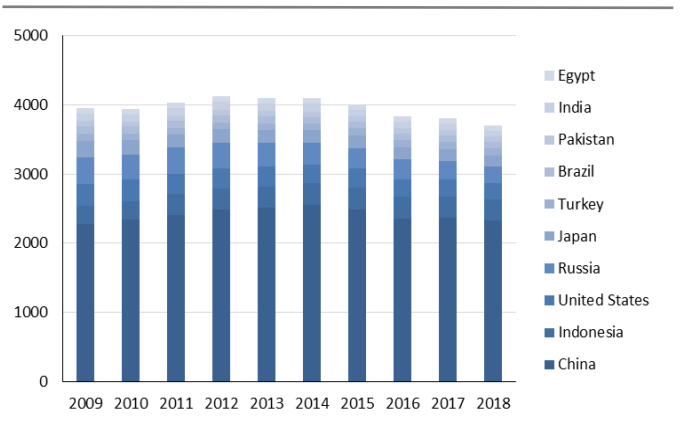
Source: Company, NHKS Research

GGRM SKM Volume (mn sticks) | FY2013 - FY2019E



Source: Company, NHKS Research

Top 10 Consumers of Cigarettes (Sticks Consumed in Bn)



Source: Ministry of Finance, NHKS Research

## 2Q19 review (IDR bn)

	2Q18	3Q18	4Q18	1Q19	2Q19					3Q19E
					Actual	Estimate	y-y	q-q	surprise	
Sales	23,324	24,584	25,818	26,197	24,584		13.8%	1.3%		26,575
Gross Profit	4,576	4,722	4,934	4,919	5,039		10.1%	2.4%		3,402
<i>Gross Margin</i>	19.6%	19.2%	19.1%	18.6%	19.0%		-0.6%	0.2%		12.8%
EBIT	2,286	3,173	2,936	3,326	2,642		15.5%	-20.6%		1,957
<i>EBIT Margin</i>	9.8%	12.9%	11.4%	12.7%	10.0%		0.1%	-2.7%		7.4%
EBITDA	2,827	3,721	3,570	3,911	3,222		14.0%	-17.6%		2,542
<i>EBITDA Margin</i>	12.1%	15.1%	13.8%	14.9%	12.1%		0.0%	-2.8%		9.6%
<b>Net Profit</b>	<b>1,663</b>	<b>2,206</b>	<b>2,031</b>	<b>2,355</b>	<b>1,926</b>		<b>15.8%</b>	<b>-18.2%</b>		<b>1,344</b>
<i>Net Margin</i>	7.1%	9.0%	7.9%	9.0%	7.3%		0.1%	-1.8%		5.1%

Source: Bloomberg, NHKS research

## Earnings revision (IDR bn)

		2019E	2020F	2021F
Sales	-Revised	106,301	112,259	131,124
	-Previous	99,626	109,033	
	-Change	6.7%	3.0%	
Gross Profit	-Revised	18,575	17,627	19,865
	-Previous	21,220	23,224	
	-Change	-12.5%	-24.1%	
Gross Margin	-Revised	17.5%	15.7%	15.1%
	-Previous	21.3%	21.3%	
EBIT	-Revised	11,068	9,069	9,870
	-Previous	13,626	14,912	
	-Change	-18.8%	-39.2%	
EBIT Margin	-Revised	10.4%	8.1%	7.5%
	-Previous	13.7%	13.7%	
EBITDA	-Revised	13,567	11,751	12,852
	-Previous	15,817	17,392	
	-Change	-14.2%	-32.4%	
EBITDA Margin	-Revised	12.8%	10.5%	9.8%
	-Previous	15.9%	16.0%	
<b>Net Profit</b>	-Revised	<b>7,830</b>	<b>6,541</b>	<b>7,205</b>
	-Previous	9,662	10,641	
	-Change	-19.0%	-38.5%	
Net Margin	-Revised	7.4%	5.8%	5.5%
	-Previous	9.7%	9.8%	

Source: NHKS 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.

### Gudang Garam's Market Share

Gudang Garam's total sales volume, including exports hiked to 85.2 billion cigarettes, with a 9.2% increase in domestic sales volume. The hike in cigarette excise tax lowers consumers' spending on cigarettes and drives them to buy more affordable cigarettes; the rising demand for SKM shows the popularity of more affordable products.

### 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
<b>Indonesia</b>									
Gudang Garam	7,536	4,789	7,141	590	4.09%	8.3%	20.0%	12.5x	2.4x
HM Sampoerna	19,414	3,230	7,498	983	11.48%	13.1%	50.5%	19.3x	9.6x
<b>India</b>									
ITC Ltd	40,726	10,357	6,844	1,802	11.72%	26.3%	22.6%	23.0x	4.9x
VST Industries Ltd	769	174	157	32	24.71%	20.6%	36.4%	24.2x	8.3x
Godfrey Phillips India Ltd	702	414	353	37	63.61%	10.6%	13.6%	19.3x	2.5x
Kothari Products Ltd	28	474	N/A	18	123.25%	N/A	11.5%	1.6x	0.2x
<b>Malaysia</b>									
British American Tobacco	1,365	256	671	104	-1.35%	15.4%	115.2%	13.4x	15.6x
<b>Pakistan</b>									
Pakistan Tobacco Co Ltd	3,926	291	405	82	-14.64%	20.1%	59.2%	55.9x	32.1x
<b>Philippines</b>									
PTFC Redevelopment Corp	36	8	3	2	40.25%	44.6%	23.0%	23.2x	5.1x
<b>South Korea</b>									
KT&G CORP	11,789	9,120	4,165	625	-39.36%	15.0%	12.4%	13.2x	1.6x
<b>Sri Lanka</b>									
Ceylon Tobacco Co Plc	1,191	154	191	102	6.84%	53.3%	195.5%	12.2x	22.9x
<b>Vietnam</b>									
CAT LOI JSC	40	44	88	6	25.63%	7.0%	22.0%	6.9x	1.5x
NGAN SON JSC	9	17	30	1	11.69%	2.0%	8.7%	14.4x	1.2x

Source: Bloomberg

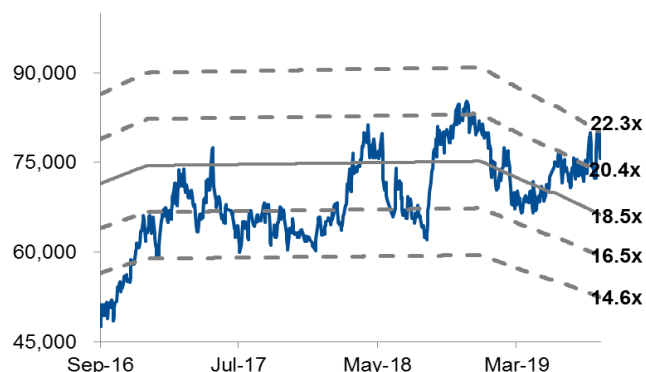
## Multiple Valuation

Forward P/E band | Last 3 years



Source: NHKS research

Dynamic Forward P/E band | Last 3 years



Source: NHKS research

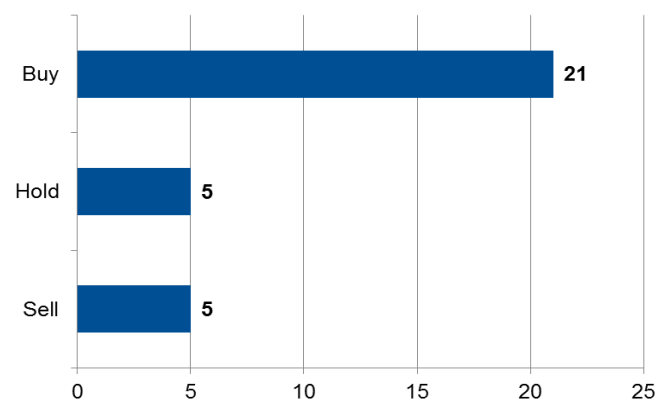
## Rating and Target Price Update

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%
09/24/2019	Buy	77,075 (Dec 2019)	55,425	79,797	+35.5%	-5.9%

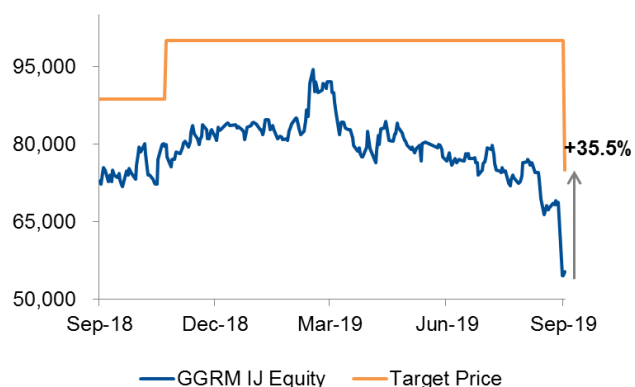
Source: NHKS research, Bloomberg

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)	2018/12A	2019/12E	2020/12E	2021/12E
<b>Sales</b>	<b>95,708</b>	<b>106,301</b>	<b>112,259</b>	<b>131,124</b>
<i>Growth</i>	14.9%	11.1%	5.6%	16.8%
COGS	(77,063)	(87,726)	(94,633)	(111,258)
<b>Gross Profit</b>	<b>18,644</b>	<b>18,575</b>	<b>17,627</b>	<b>19,865</b>
<i>Gross Margin</i>	19.5%	17.5%	15.7%	15.1%
Operating Expenses	(7,526)	(7,507)	(8,558)	(9,996)
<b>EBIT</b>	<b>11,119</b>	<b>11,068</b>	<b>9,069</b>	<b>9,870</b>
<i>EBIT Margin</i>	11.6%	10.4%	8.1%	7.5%
Depreciation	2,255	2,499	2,682	2,982
<b>EBITDA</b>	<b>13,374</b>	<b>13,567</b>	<b>11,751</b>	<b>12,852</b>
<i>EBITDA Margin</i>	14.0%	12.8%	10.5%	9.8%
Interest Expenses	(678)	(612)	(332)	(245)
<b>EBT</b>	<b>10,479</b>	<b>10,441</b>	<b>8,722</b>	<b>9,607</b>
Income Tax	(2,686)	(2,611)	(2,181)	(2,402)
Minority Interest	(1)	0	0	0
<b>Net Profit</b>	<b>7,792</b>	<b>7,830</b>	<b>6,541</b>	<b>7,205</b>
<i>Growth</i>	0.5%	0.5%	-16.5%	10.1%
<i>Net Profit Margin</i>	8.1%	7.4%	5.8%	5.5%

### PROFITABILITY & STABILITY

	2018/12A	2019/12E	2020/12E	2021/12E
ROE	17.3%	16.3%	13.2%	13.9%
ROA	11.3%	10.7%	9.9%	10.5%
ROIC	13.2%	13.2%	11.9%	13.1%
Cash Dividend (IDR bn)	5,003	5,003	5,003	5,003
Dividend Yield	3.1%	4.7%	4.7%	4.7%
Payout Ratio	64.5%	64.2%	63.9%	76.5%
DER	38.4%	19.6%	14.0%	16.0%
Net Gearing	38.4%	19.6%	14.0%	16.0%
LT Debt to Equity	0.0%	0.0%	0.0%	0.0%
Capitalization Ratio	27.7%	16.4%	12.3%	13.8%
Equity Ratio	65.3%	65.6%	74.7%	75.3%
Debt Ratio	25.1%	12.9%	10.5%	12.1%
Financial Leverage	152.9%	148.4%	150.0%	131.0%
Current Ratio	205.8%	202.0%	252.3%	249.0%
Par Value (IDR)	500	500	500	500
Total Shares (mn)	1,924	1,924	1,924	1,924
Share Price (IDR)	83,800	55,425	55,425	55,425
Market Cap (IDR tn)	161.2	106.6	106.6	106.6

### BALANCE SHEET

(IDR bn)	2018/12A	2019/12E	2020/12E	2021/12E
Cash	2,034	3,134	2,693	3,524
Receivables	1,726	2,381	2,024	3,083
Inventories	38,560	39,586	30,802	28,593
<b>Total Current Assets</b>	<b>45,285</b>	<b>46,575</b>	<b>37,141</b>	<b>36,749</b>
Net Fixed Assets	22,759	25,163	27,553	30,495
Other Non Current Asset	1,054	1,344	1,587	1,377
<b>Total Assets</b>	<b>69,097</b>	<b>73,082</b>	<b>66,281</b>	<b>68,621</b>
Payables	1,130	980	1,057	1,243
ST Bank Loan	17,322	9,400	6,930	8,272
LT Debt	-	-	-	-
<b>Total Liabilities</b>	<b>23,964</b>	<b>25,121</b>	<b>16,781</b>	<b>16,918</b>
Capital Stock	1,016	1,016	1,016	1,016
Retained Earnings	44,151	46,978	48,517	50,720
<b>Shareholders' Equity</b>	<b>45,133</b>	<b>47,961</b>	<b>49,499</b>	<b>51,702</b>

### VALUATION INDEX

	2018/12A	2019/12E	2020/12E	2021/12E
Price /Earnings	20.7x	13.6x	16.3x	14.8x
Price /Book Value	3.6x	2.2x	2.2x	2.1x
Price/Sales	1.7x	1.0x	0.9x	0.8x
PE/EPS Growth	42.0x	27.6x	-1.0x	1.5x
EV/EBITDA	13.2x	8.3x	9.4x	8.7x
EV/EBIT	15.9x	10.2x	12.2x	11.3x
EV (IDR bn)	176,493	112,876	110,846	111,358
Sales CAGR (3-Yr)	10.8%	11.7%	10.5%	11.1%
EPS CAGR (3-Yr)	6.6%	5.5%	-5.5%	-2.6%
Basic EPS (IDR)	4,050	4,070	3,399	3,744
Diluted EPS (IDR)	4,050	4,070	3,399	3,744
BVPS (IDR)	23,457	24,926	25,726	26,871
Sales PS (IDR)	49,742	55,247	58,344	68,148
DPS (IDR)	2,600	2,600	2,600	2,600

### CASH FLOW STATEMENT

(IDR bn)	2018/12A	2019/12E	2020/12E	2021/12E
Operating Cash Flow	11,232	19,119	12,348	10,106
Investing Cash Flow	(3,228)	(4,994)	(5,315)	(5,615)
Financing Cash Flow	(8,299)	(12,924)	(7,473)	(3,660)
<b>Net Changes in Cash</b>	<b>(295)</b>	<b>1,201</b>	<b>(441)</b>	<b>831</b>

### 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

### DISCLAIMER

This report and any electronic access hereto are restricted and intended only for the clients and related entity of PT NH Korindo Sekuritas Indonesia. This report is only for information and recipient use. It is not reproduced, copied, or made available for others. Under no circumstances is it considered as a selling offer or solicitation of securities buying. Any recommendation contained herein may not suitable for all investors. Although the information here is obtained from reliable sources, its accuracy and completeness cannot be guaranteed. PT NH Korindo Sekuritas Indonesia, its affiliated companies, respective employees, and agents disclaim any responsibility and liability for claims, proceedings, action, losses, expenses, damages, or costs filed against or suffered by any person as a result of acting pursuant to the contents hereof. Neither is PT NH Korindo Sekuritas Indonesia, its affiliated companies, employees, nor agents liable for errors, omissions, misstatements, negligence, inaccuracy arising herefrom.

All rights reserved by PT NH Korindo Securities Indonesia