

Gudang Garam Tbk (GGRM)

1Q20: A Touch Below Our Estimate, FY Outlook Lowered

GGRM still recorded modest growth in revenue and net profit in 1Q20, supported by advances in all segments such as SKM, SKT and paperboard. However, GPM and EBIT margins still recorded a contraction due to a moderate increase in ASP amid an increase in excise tax rates and downward trend in cigarettes volume sales.

1Q20 Performance Below Expectations

Based on the results of the 1Q20 financial statements, GGRM recorded revenues of IDR27 trillion (+4.1% y-y; -5.4% q-q) and posted a net profit of IDR2.4 trillion (+3.9% y-y; -32.7% q-q). This result is below our expectations due to high base growth throughout FY19. EBIT increased slightly to IDR3.3 trillion (+0.3% y-y; -33.2% q-q), due to a significant decrease in other expenses to IDR1.0 billion and a surge in foreign exchange earnings to IDR26 billion. In terms of margins, GPM recorded a decrease of 60 bps to 18.1% and EBIT margin recorded a decrease of 40 bps to 12.3%. Meanwhile, NPM remains relatively stable at 9%. We believe this contraction is due to a moderate increase in ASP of c.1-3% and has not been able to compensate for the rise in excise tax rates and retail sale prices (HJE) which increased significantly in FY20.

Faster Growth Pace of Hand-Rolled Cigarettes (SKT) Segment

Based on its revenue segment in 1Q20, machine-made clove cigarettes as the key contributor to revenue (c.91%) recorded revenues reaching Rp24 trillion (+3% y-y, -6% q-q), followed by hand-rolled clove cigarettes (c.7%) posted revenues reaching IDR 2.1 trillion (+12% y-y, +5% q-q). The paperboard segment recorded an increase in revenue to Rp317 billion (+23% y-y, +26% q-q), while the corn-silk clove cigarette segment recorded a decrease in revenue to Rp6 billion (-14% y-y, -2% q-q). We cautiously assume faster growth in the SKT segment compared to the SKM segment indicate a high likelihood of consumers shifting to cigarettes at lower prices. In addition, we estimate that the pandemic that has an impact on public consumption will also reduce the volume of cigarette sales. However, we believe GGRM is quite defensive in the face of this pandemic caused by the majority of domestic raw materials so that it is not affected by the fluctuating USD/IDR exchange rate, PMK policy No.30/PMK.04/2020 regarding the postponement of excise payments which helps lessen pressure on net income and still maintaining a strong position in the FF SKM segment (GG internasional and GG Surya).

Maintain BUY with Lower TP Rp59,550/share

We maintain BUY recommendation with the lower target price of FY20 IDR59,550 and a forward PE of 9.2x, with strong fundamentals amid a surge in excise tax rates and an attractive valuation with PE traded at 8.3x and compared to a median average PE of 8.85x. In addition, we assume that GGRM still distributes dividends with the same dividend yields as the previous year. Risks of our target price are 1) Slower purchasing power; 2) lower than expected sales volume in the FF SKM segment; 3) Significant increase in cigarette excise rates, thereby suppressing COGS.

Gudang Garam Tbk | Summary (IDR bn)

	2019A	2020E	2021F	2022F
Sales	110,524	117,334	125,508	133,793
<i>Sales growth</i>	15.5%	6.2%	7.0%	6.6%
EBITDA	17,401	17,685	19,850	21,948
Net Profit	10,881	10,385	12,416	13,884
EPS (IDR)	5,655	5,397	6,453	7,216
<i>EPS growth</i>	39.6%	-4.6%	19.6%	11.8%
EBITDA margin	15.7%	15.1%	15.8%	16.4%
NPM	9.8%	8.9%	9.9%	10.4%
P/E	14.8x	9.1x	7.6x	6.8x
P/BV	3.2x	1.7x	1.5x	1.3x
EV/EBITDA	10.1x	6.1x	5.3x	4.6x
DPS (IDR)	2,600	2,600	2,600	2,600
<i>Dividend yield</i>	3.1%	5.3%	5.3%	5.3%

Source: Company Data, Bloomberg, NHKS Research

Please consider the rating criteria & important disclaimer

Buy

Dec 2020 TP (IDR) **59,550**

Consensus Price (IDR)	55,569
TP to Consensus Price	+7.2%
vs. Last Price	+20.8%

Shares data

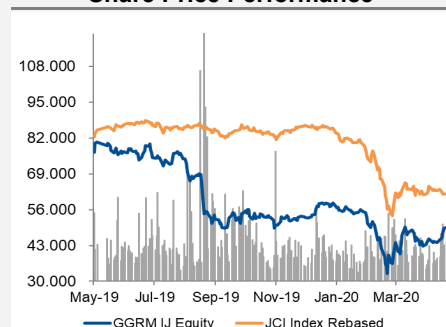
Last Price (IDR)	49,300
Price date as of	May 19, 2020
52 wk range (Hi/Lo)	80,475 / 32,900
Free float (%)	23.8
Outstanding sh.(mn)	1,924
Market Cap (IDR bn)	91,442
Market Cap (USD mn)	6,1442
Avg. Trd Vol - 3M (mn)	1.30
Avg. Trd Val - 3M (bn)	58.86
Foreign Ownership	8.0%

Consumer Staples

Cigarette

Bloomberg	GGRM IJ
Reuters	GGRM.JK

Share Price Performance



	YTD	1M	3M	12M
Abs. Ret.	-7.6%	7.2%	-10.7%	-38.2%
Rel. Ret.	20.0%	9.0%	12.6%	-16.2%

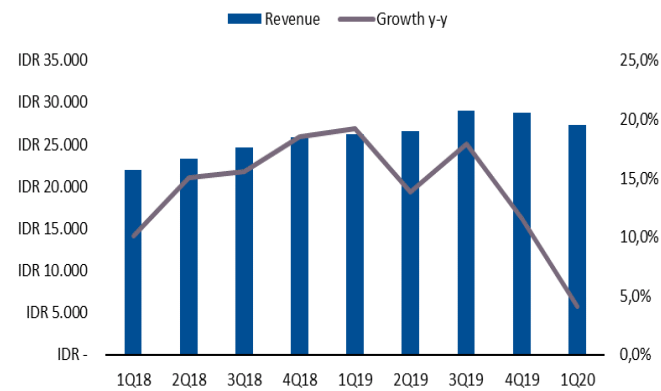
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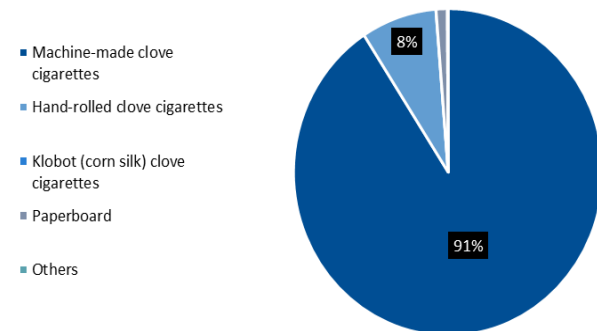
Performance Highlights

GGRM Quarterly Sales | 1Q18 - 1Q20



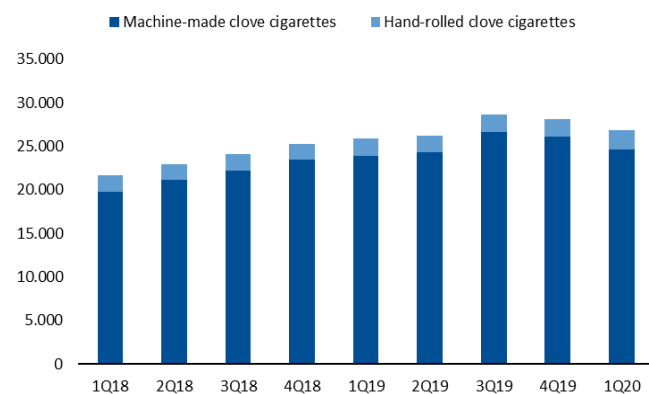
Source: Company Data, NHKSI Research

GGRM Sales Breakdown | 1Q20



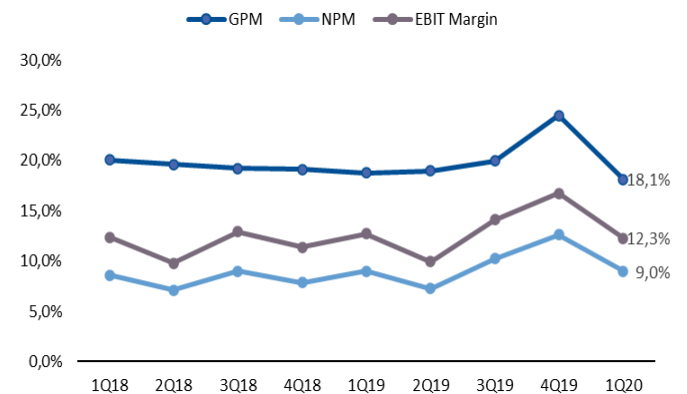
Source: Company Data, NHKSI Research

Machine and Hand Made Sales Trend | 1Q18 - 1Q20



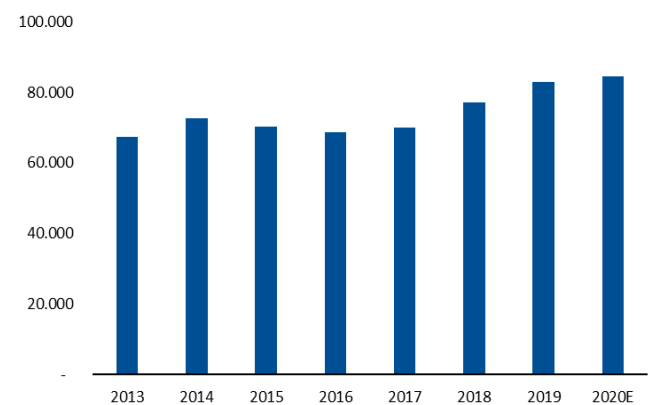
Source: Company Data, NHKSI Research

GGRM Quarterly Margins | 1Q18 - 1Q20



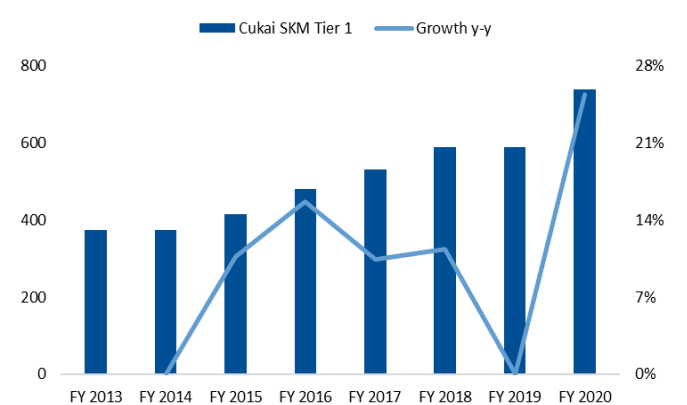
Source: Company Data, NHKSI Research

GGRM SKM Volume (mn sticks) | FY2013 - FY2020E



Source: Company Data, NHKSI Research

Excise Tax for Cigarettes in Indonesia



Source: Various Sources, NHKSI Research

1Q20 review (IDR bn)

	1Q19	2Q19	3Q19	4Q19	1Q20					2Q20E
					Actual	Estimate	y-y	q-q	surprise	
Sales	26,197	26,548	28,976	28,803	27,261	31,071	4.1%	-5.4%	-12.3%	27,909
Gross Profit	4,919	5,039	5,779	7,046	4,942	5,784	0.5%	21.9%	-14.6%	4,399
<i>Gross Margin</i>	18.8%	19.0%	19.9%	24.5%	18.1%	18.6%	-0.6%	4.5%	-0.5%	15,8%
EBIT	3,326	2,642	4,089	4,815	3,341	3,640	0.4%	17.8%	-8.2%	1,961
<i>EBIT Margin</i>	12.7%	10.0%	14.1%	16.7%	12.3%	11.7%	-0.4%	2.6%	0.5%	7,0%
EBITDA	3,911	3,222	4,695	5,573	3,969	4,244	1.5%	18.7%	-6.5%	2,664
<i>EBITDA Margin</i>	14.9%	12.1%	16.2%	19.4%	14.6%	13.7%	-0.4%	3.1%	0.9%	9,5%
Net Profit	2,355	1,926	2,962	3,637	2,447	2,205	3.9%	22.8%	11.0%	1,350
<i>Net Margin</i>	9.0%	7.3%	10.2%	12.6%	9.0%	7.1%	0.0%	2.4%	1.9%	4,8%

Source: Bloomberg, NHKSI research

Earnings revision (IDR bn)

		2020E	2021F	2022F
Sales	-Revised	117,334	125,508	133,793
	-Previous	138,173	163,174	
	-Change	-15.1%	-23.1%	
Gross Profit	-Revised	23,109	26,080	28,729
	-Previous	21,197	24,645	
	-Change	6.0%	5.8%	
Gross Margin	-Revised	19.7%	20.8%	21.5%
	-Previous	15.8%	15.1%	
	-Change			
EBIT	-Revised	14,929	17,231	19,096
	-Previous	11,264	12,206	
	-Change	32.5%	41.2%	
EBIT Margin	-Revised	12.7%	13.7%	14.3%
	-Previous	8.2%	7.5%	
	-Change			
EBITDA	-Revised	17,685	19,850	21,948
	-Previous	13,681	14,901	
	-Change	29.3%	33.2%	
EBITDA Margin	-Revised	15.1%	15.8%	16.4%
	-Previous	9.9%	9.1%	
	-Change			
Net Profit	-Revised	10,385	12,416	13,884
	-Previous	6,541	7,205	
	-Change	58.8%	72.3%	
Net Margin	-Revised	8.9%	9.9%	10.4%
	-Previous	4.7%	4.4%	
	-Change			

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.

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
Indonesia									
Gudang Garam	6,142	5,680	7,881	775	32.91%	9.8%	21.8%	8.3x	1.7x
HM Sampoerna	13,829	3,676	7,482	972	-0.25%	13.0%	35.4%	14.9x	5.3x
India									
ITC Ltd	30,146	10,357	6,844	1,802	11.72%	26.3%	22.6%	18.1x	3.9x
VST Industries Ltd	637	174	193	43	34.05%	22.2%	36.4%	15.9x	7.3x
Godfrey Phillips India Ltd	661	414	353	37	63.61%	10.6%	13.6%	19.3x	2.5x
Malaysia									
British American Tobacco	767	251	569	74	-33.20%	13.0%	84.6%	10.9x	9.5x
Pakistan									
Pakistan Tobacco Co Ltd	2,603	261	347	84	36.26%	24.2%	71.5%	32.4x	22.9x
South Korea									
KT&G CORP	9,082	9,275	4,194	894	14.12%	21.3%	13.0%	9.8x	1.3x
Sri Lanka									
Ceylon Tobacco Co Plc	913	147	198	96	-1.15%	48.2%	190.5%	9.9x	19.8x

Source: Bloomberg

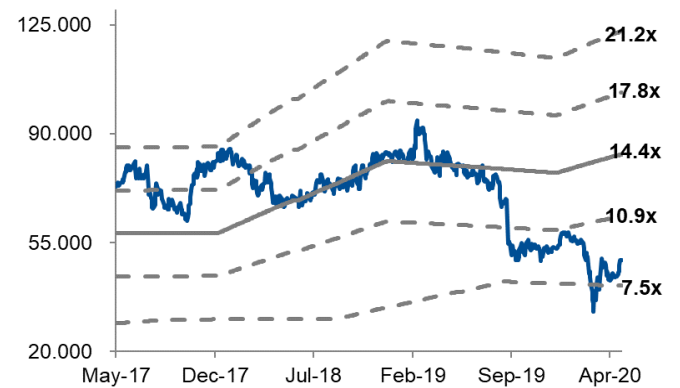
Multiple Valuation

Forward P/E band | Last 3 years



Source: NHKSI research

Dynamic Forward P/E band | Last 3 years



Source: NHKSI research

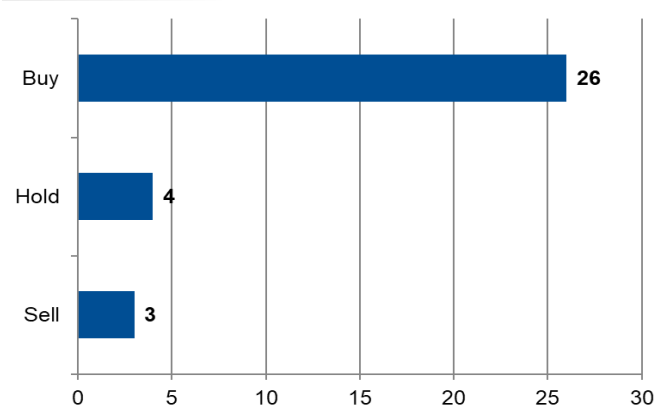
Rating and Target Price Update

Target Price Revision

Date	Rating	Target Price	Last Price	Consensus	vs Last Price	vs Consensus
09/18/2018	Buy	88,650 (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%
12/30/2019	Buy	61,800 (Dec 2020)	52,400	59,865	+17.9%	+3.2%
05/26/2020	Buy	59,550 (Dec 2020)	49,300	55,569	+20.8%	+7.2%

Source: NHKS research, Bloomberg

Analyst Coverage Rating



Source: Bloomberg

Closing and Target Price



Source: NHKSI 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)	2019/12A	2020/12E	2021/12E	2022/12E
Sales	110.524	117.334	125.508	133.793
<i>Growth</i>	15,5%	6,2%	7,0%	6,6%
COGS	(87.741)	(94.224)	(99.429)	(105.064)
Gross Profit	22.783	23.109	26.080	28.729
<i>Gross Margin</i>	20,6%	19,7%	20,8%	21,5%
Operating Expenses	(7.912)	(8.180)	(8.848)	(9.633)
EBIT	14.872	14.929	17.231	19.096
<i>EBIT Margin</i>	13,5%	12,7%	13,7%	14,3%
Depreciation	2.530	2.756	2.619	2.852
EBITDA	17.401	17.685	19.850	21.948
<i>EBITDA Margin</i>	15,7%	15,1%	15,8%	16,4%
Interest Expenses	(599)	(853)	(430)	(321)
EBT	14.488	13.846	16.555	18.513
Income Tax	(3.607)	(3.462)	(4.139)	(4.628)
Minority Interest	0	-	-	-
Net Profit	10.881	10.385	12.416	13.884
<i>Growth</i>	39,6%	-4,6%	19,6%	11,8%
<i>Net Profit Margin</i>	9,8%	8,9%	9,9%	10,4%

PROFITABILITY & STABILITY

	2019/12A	2020/12E	2021/12E	2022/12E
ROE	21,4%	18,4%	19,4%	19,1%
ROA	13,8%	12,7%	14,7%	15,6%
ROIC	16,4%	16,0%	17,5%	18,0%
Cash Dividend (IDR bn)	5.003	5.003	5.003	5.003
Dividend Yield	3,1%	5,3%	5,3%	5,3%
Payout Ratio	64,2%	46,0%	48,2%	40,3%
DER	33,8%	23,8%	15,7%	9,3%
Net Gearing	33,9%	23,8%	15,7%	9,3%
LT Debt to Equity	0,0%	0,0%	0,0%	0,0%
Capitalization Ratio	25,3%	19,2%	13,6%	8,5%
Equity Ratio	64,8%	69,1%	75,9%	81,8%
Debt Ratio	21,9%	16,4%	11,9%	7,6%
Financial Leverage	153,8%	149,4%	137,9%	126,7%
Current Ratio	206,2%	234,2%	303,2%	414,1%
Par Value (IDR)	500	500	500	500
Total Shares (mn)	1.924	1.924	1.924	1.924
Share Price (IDR)	83.800	49.300	49.300	49.300
Market Cap (IDR tn)	161,2	94,9	94,9	94,9

BALANCE SHEET

(IDR bn)	2019/12A	2020/12E	2021/12E	2022/12E
Cash	3.572	3.960	4.638	5.638
Receivables	1.876	2.082	2.227	2.374
Inventories	42.847	46.596	46.445	48.214
Total Current Assets	52.081	53.593	54.246	57.144
Net Fixed Assets	25.374	26.549	28.323	30.154
Other Non Current Asset	1.192	1.643	1.660	1.676
Total Assets	78.647	81.785	84.228	88.974
Payables	1.297	1.265	1.335	1.410
ST Bank Loan	17.236	13.443	10.032	6.768
LT Debt	-	-	-	-
Total Liabilities	27.717	25.303	20.333	16.196
Capital Stock	1.016	1.016	1.016	1.016
Retained Earnings	49.948	55.499	62.913	71.795
Shareholders' Equity	50.931	56.481	63.895	72.777

VALUATION INDEX

	2019/12A	2020/12E	2021/12E	2022/12E
Price /Earnings	14,8x	9,1x	7,6x	6,8x
Price /Book Value	3,2x	1,7x	1,5x	1,3x
Price/Sales	1,5x	0,8x	0,8x	0,7x
PE/EPS Growth	0,4x	-2,0x	0,4x	0,6x
EV/EBITDA	10,1x	6,1x	5,3x	4,6x
EV/EBIT	11,9x	7,3x	6,1x	5,2x
EV (IDR bn)	176.493	108.489	104.307	100.218
Sales CAGR (3-Yr)	10,8%	13,2%	12,1%	9,5%
EPS CAGR (3-Yr)	6,6%	17,7%	10,2%	16,8%
Basic EPS (IDR)	5.655	5.397	6.453	7.216
Diluted EPS (IDR)	5.655	5.397	6.453	7.216
BVPS (IDR)	26.470	29.355	33.208	37.824
Sales PS (IDR)	57.442	60.981	65.230	69.536
DPS (IDR)	2.600	2.600	2.600	2.600

CASH FLOW STATEMENT

(IDR bn)	2019/12A	2020/12E	2021/12E	2022/12E
Operating Cash Flow	10.948	13.608	13.476	14.008
Investing Cash Flow	(4.818)	(4.424)	(4.385)	(4.741)
Financing Cash Flow	(4.606)	(8.796)	(8.414)	(8.266)
Net Changes in Cash	1.524	388	677	1.001

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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