

Perusahaan Gas Negara Tbk (PGAS IJ)

Distribution Volume Potentially Down this Year

Revenue performance of PGAS in 1Q20 was stagnant with a decrease in net profit by 26.6% YoY due to forex loss of USD63 million. We predict that distribution volume will still decrease at around 8-10% MoM in May-June period due to Covid-19 pandemic. PGAS may potentially experience margin reduction in 2020, but we estimate that distribution volume increase by 4%-6% in 2021 will support the performance. We initiate to BUY with target price of IDR1,400.

Stagnant Revenue Performance

In 1Q20, PGAS's revenue performance was quite stagnant at USD874 million (-0.3 YoY). The performance was supported by income increase from gas distribution (+2.4% YoY) and gas transmission (+13% YoY) which balanced out decrease in oil and gas upstream (-18.1 YoY). Gas volume distribution in March was down due to the pandemic so volume was booked under 900 BBTUD but gas ASP still rose. Forex loss of USD63 million made the net profit amount to USD48 million (-26.6 YoY). Revenue and net profit in 1Q20 have reached 28% and 48% of our 2020F target.

Pandemic Hampers Gas Distribution

The pandemic condition through February-April had an impact on the decrease of PGAS gas distribution volume. The volume on April was booked at 804 BBTUD (including Pertagas). We estimate it will drop lower for the May and June period at around 8-10% MoM considering business activity is still falling compared to last year, with the obstruction on expansion process such as construction of pipeline infrastructure.

Impact of New Regulation

According to Ministerial Decree (Kepmen) No. 83, 2020, the government set the price of natural gas for industry in the range of USD6/MMBTU which will be applied by PGAS through LoA. We see that the impact of the regulation will reduce PGAS margins but we remain optimistic that distribution volume will increase significantly at 4-6% in 2021.

Initiate to BUY with Target Price of IDR1,400

We initiate to BUY with blended target price of IDR1,400 considering: 1) potentials of gas network business will still be one of the government's priority; 2) internal efficiency by cutting opex at around 15-35% and the delay of exploration by Saka Energi; 3) business portfolio innovation on the petrochemical industry. Blended target price based on DCF Valuation with WACC of 5.5% and forward P/E methodology of 23.2x (5-year historical mean).

Perusahaan Gas Negara Tbk | Summary

	2019A	2020F	2021F	2022F
Revenue (USD mn)	3,849	3,090	3,439	3,620
Growth (%)	-0.6	-19.7	11.3	5.3
EBITDA (USD mn)	1,040	1,191	1,485	1,704
Net Profit (USD mn)	68	97	134	154
EPS (IDR)	39	59	80	90
Growth (%)	-80.1	50.1	35.7	12.3
P/E (x)	55.0	29.1	21.4	19.1
P/BV (x)	1.2	0.9	0.9	0.8
EV/EBITDA (x)	6.7	5.0	4.2	3.7
ROE (%)	2.1	3.0	4.0	4.4
DER (%)	128.0	140.5	160.5	155.0
Net Debt (USD mn)	1,710	1,880	2,044	2,103

Source: Company Data, Bloomberg, NHKSI Research

Please consider the rating criteria & important disclaimer

Initiation Report | Jul 16, 2020

Buy

Target Price (IDR)	1,400
Consensus Price (IDR)	1,112
TP to Consensus Price (%)	+25.9
vs. Last Price (%)	+21.2

Shares Data

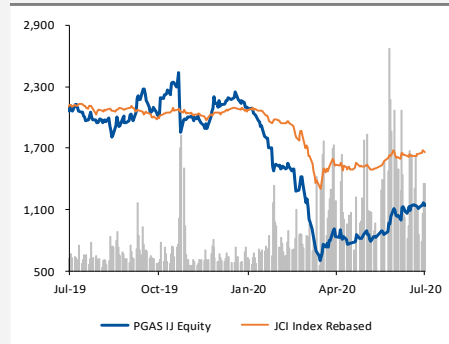
Last Price (IDR)	1,155
Price Date as of	Jul 15, 2020
52 wk Range (Hi/Lo)	2,460/605
Free Float (%)	43.0
Outstanding Shares (mn)	24,242
Market Cap (IDR bn)	27,514
Market Cap (USD mn)	1,903
Avg. Trd Vol - 3M (mn)	187.9
Avg. Trd Val - 3M (bn)	185.6
Foreign Ownership (%)	14.7

Utilities

Energy

Bloomberg	PGAS IJ
Reuters	PGAS.JK

Share Price Performance



	YTD	1M	3M	12M
Abs. Ret.	-47.5%	9.1%	35.9%	-46.5%
Rel. Ret.	-27.0%	6.9%	27.7%	-24.9%



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Industry Overview

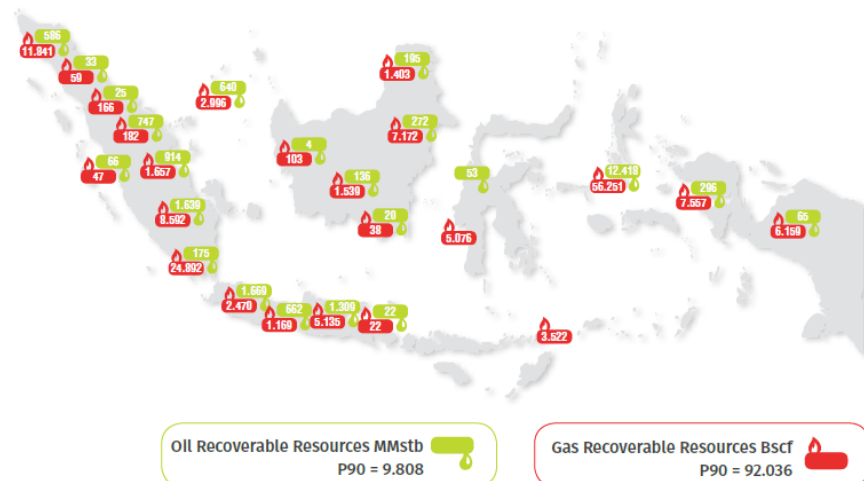
Gas reserves & gas associations in 2018 reach 50 trillion TCF with resources reaching 92,036 BSCF

Large Oil and Gas Reserves

As of 2018, Indonesia has an oil and condensate of 2.5 billion BTSTB and gas reserves and associate of 50 trillion TCF. The data is also supported by the newest geology and geophysics that Indonesia has oil resources amounting to 9,808 MMTSB and gas of 92,036 BSCF. As for the Reserves Replacemen Ratio (RRR) for oil and gas in Indonesia on 2019, reached 353.7% with the addition of 2,634 million barrels reserves.

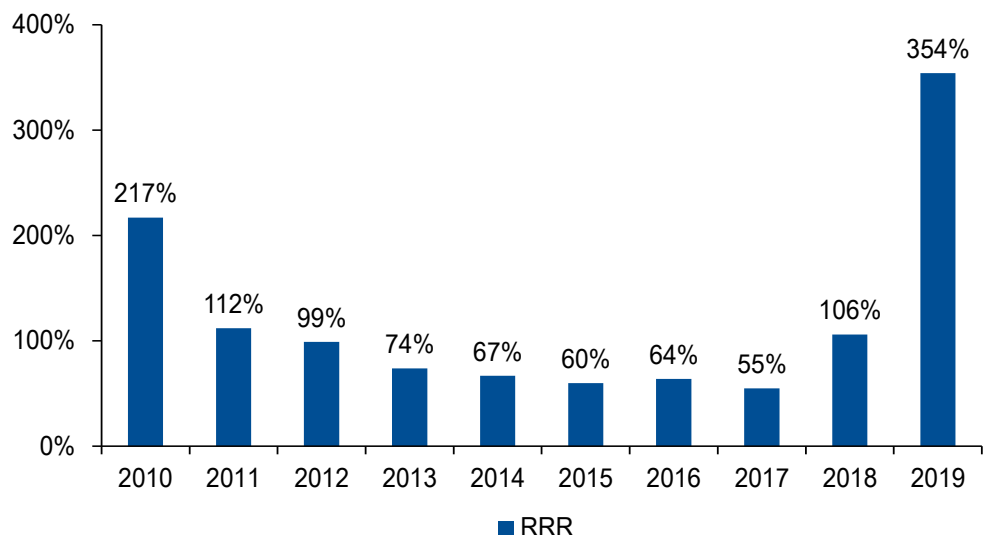
Indonesia's RRR performance in 2019 was the highest in the last decade. The RRR data on 2013-2017 period is around 55%-74%, then the increased performance of 2019 has reached 354%. It shows that the national oil and gas resources is still massive and we predict to give income boost for Indonesia in the next couple of years. The large amount of reserves is supported by an investment increase in the oil and gas upstream sector reaching up to USD12.2 billion or increasing by 11% compared to 2018 realization.

Figure 1: Indonesia's Oil & Gas Resources and Reserves Map



Source: Special Task Force for Upstream Oil & Gas Business

Figure 2: Indonesia's Reserves Replacement Ratio



Source: Special Task Force for Upstream Oil & Gas Business, NHKSI Research

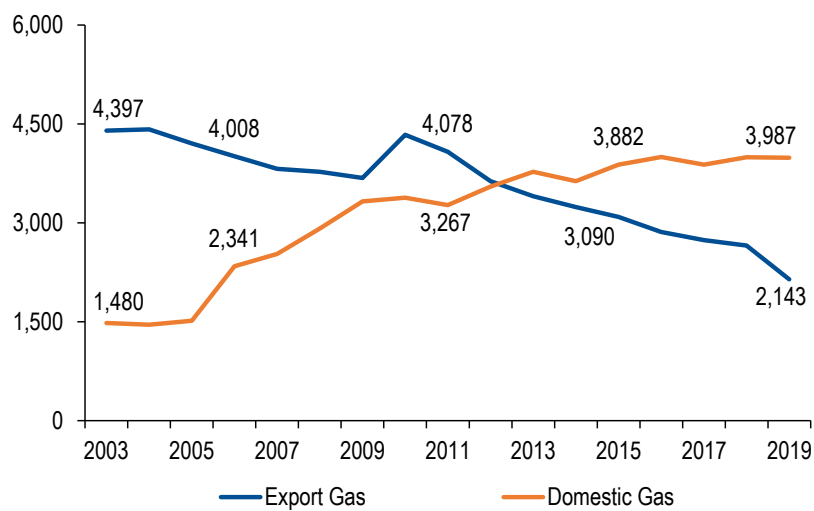
Gas consumption in Indonesia is mostly by the industrial sector, electricity, and fertilizer factories

Domestic Gas Allocation Keeps Rising

In 2013-2019, the gas distribution for Indonesian people’s needs keep rising. Gas consumption in 2019 is 65% of the national total distribution that reached around 3,987 BBTUD with the addition of 2,413 export volume. The biggest allocation for domestic gas consumption comes from the industrial sector, electricity, and fertilizer factories, which in total amounts to 94.3%.

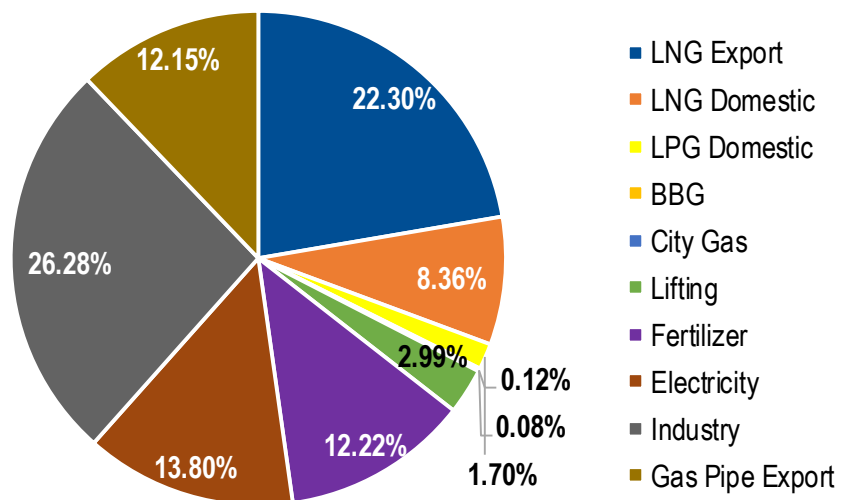
Currently, the government will still continue the monetization of natural gas through gas pipeline infrastructure optimization which is mostly done by PT Perusahaan Gas Negara Tbk (PGAS), in addition to mini LNG and CNG distribution to reach end user. As for lifting gas, LNG in 2019 managed to reach 701.9 BTU and the consumption keeps rising every year. LNG is mostly consumed by the electricity sector with total allocation of 95% and the rest is for manufacture industry and misc.

Figure 3: National Gas Allocation



Source: Special Task Force for Upstream Oil & Gas Business, NHKSI Research

Figure 4: Composition of Gas Consumption



Source: Special Task Force for Upstream Oil & Gas Business, NHKSI Research

Company Overview

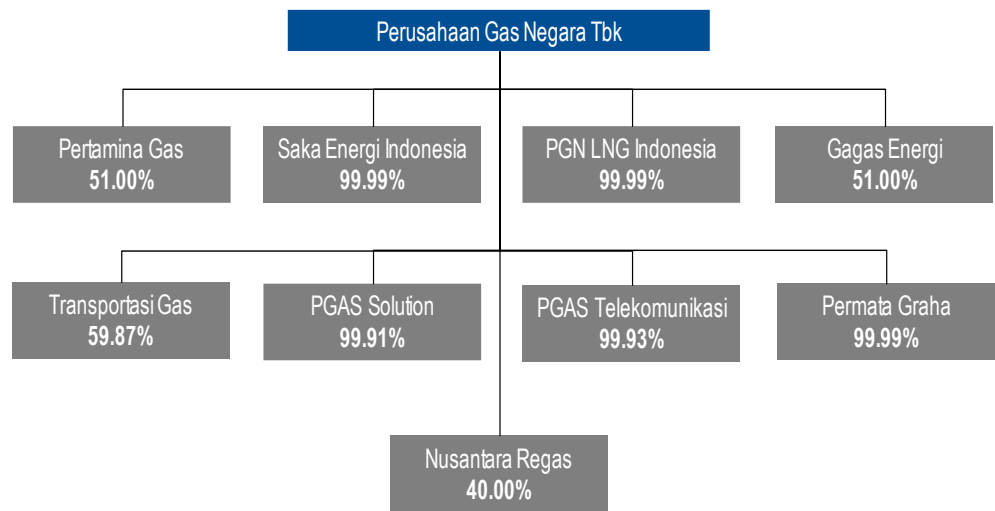
PGAS has managed 96% of the existing downstream infrastructure of natural gas in Indonesia

Natural Gas Infrastructure Management Company in Indonesia

PT Perusahaan Gas Negara Tbk (PGAS) as Subholding Gas, integrates natural gas infrastructure in Indonesia and seeks to increase energy access in Indonesian by using both pipeline and non-pipeline infrastructure. At present, PGAS has operated in 66 districts/cities, in 17 provinces in Indonesia and continues to expand. The natural gas end user segment that receives PGN natural gas energy services range from households, transportation (SPBG), small customers, commercial, industrial and power plants.

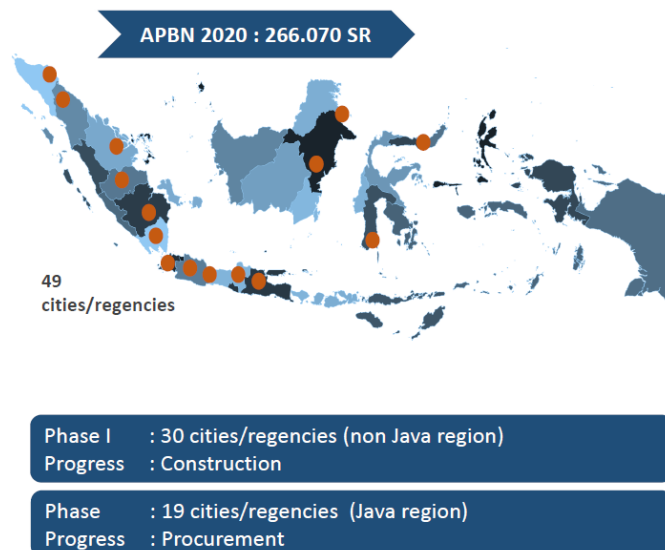
The PGAS downstream natural gas infrastructure management portfolio until 2019 includes 96% of the natural gas downstream infrastructure that has been built and is operating. As for the management of household natural gas network and small customers, follows the Government and the Sayang Ibu Program covering 49 regencies/cities throughout Indonesia with around 3,000 km long Jargas pipeline.

Figure 5: Business Structure



Source: Company Data, NHKSI Research

Figure 6: City Gas Project



Source: Company Data

SEI and Pertagas are vital subsidiaries for overall PGAS business.

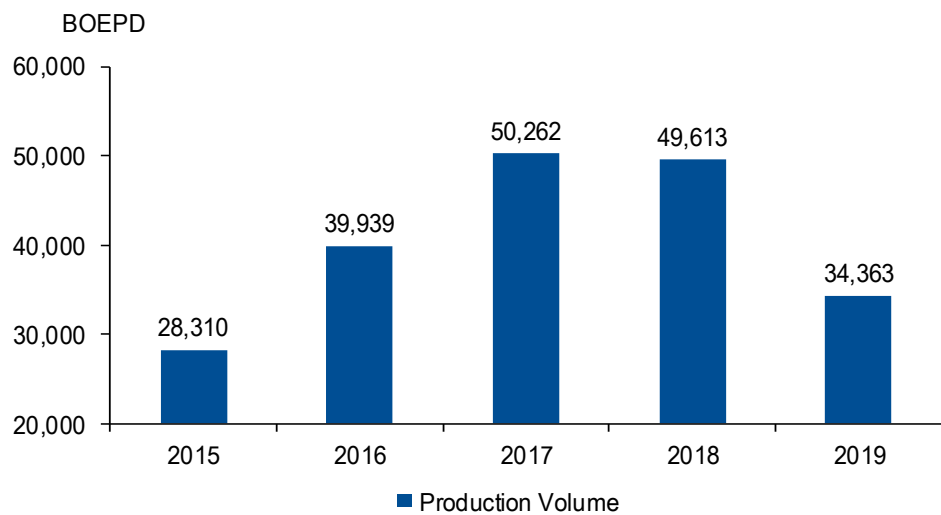
Saka Energi Indonesia

In 2019, Saka Energi Indonesia (SEI) produced a total lifting of 10.32 MMBOE with the volume of each commodity namely oil at 4.82 BPD, gas at 84 BBTUD, LPG at 68 MTPD and LNG at 48 BBTUD. When compared to 2019, the total lifting produced decreased by 38% due to the expiration of SEI ownership in the South East Sumatra block and the Sanga-Sanga block in 2018.

Pertamina Gas

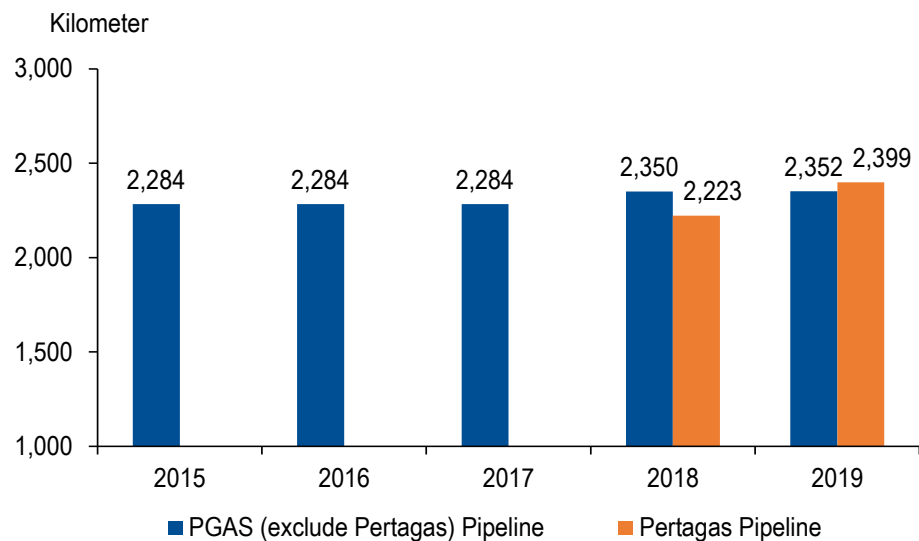
The Pertamina Gas (Pertagas) working area is divided into 6 operational areas, with 5 operating areas handling natural gas pipelines, and 1 operating area handling oil pipelines. For gas transportation, Pertagas successfully distributed 519,483 MMSCF of natural gas in 2019, rising by 1.41% YoY. The realization of natural gas trading volume in 2019 reached 45,266 BBTU, down 3% YoY due to reduced natural gas allocation from KEIL for the East Java region.

Figure 7: SEI Volume Production



Source: Company Data, NHKSI Research

Figure 8: Length of Pertagas Pipeline



Source: Company Data, NHKSI Research

Performance & Outlook

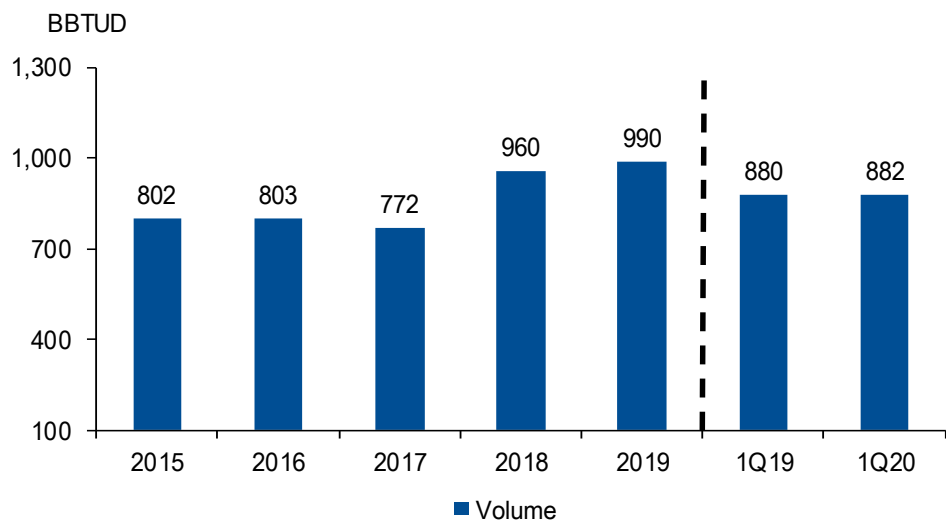
The 2Q20 distribution volume will decline due to low consumption of the industrial sector

Gas Distribution and Sales Segment

The distribution and sales segment of natural gas distribute it to end users for commercial customers and manufacturing industries, power plants, MSMEs, and households using various modes, such as pipelines and non-pipelines. This business segment is managed by PGAS directly and its subsidiary, Gagas Energi Indonesia (GEI). PGAS distribution areas and business operations are spread across several cities / districts in Indonesia and are classified into three Regional Distributions (RD).

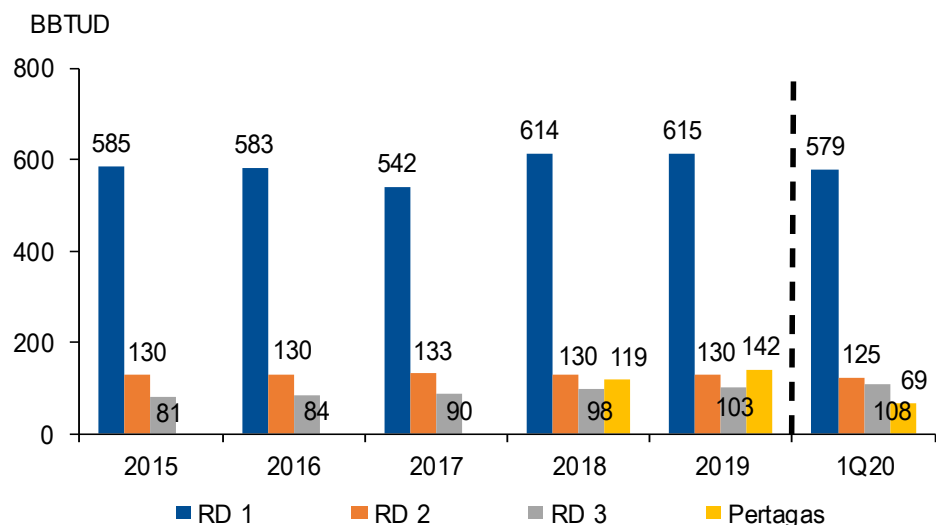
In 1Q20, the consolidated distribution volume was relatively stable on an annual basis even though consumption was slightly lower than non-electricity customers. The impact of Covid-19 started to be seen in January-March. We estimate this pandemic will still impact on 2Q20 performance which potentially record a decline. The estimation takes into account; 1) low consumption from the industrial sector; 2) the distribution process is hampered when user experiences an increase.

Figure 9: Distribution Volume



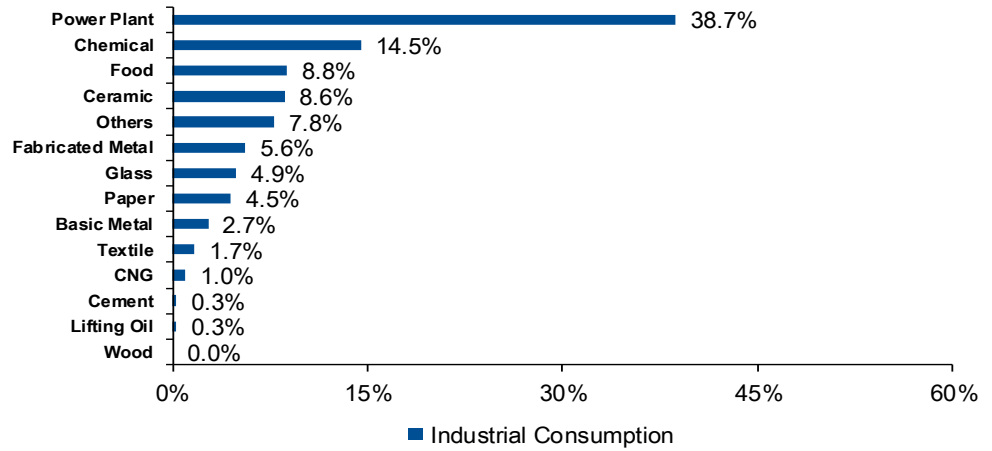
Source: Company Data, NHKSI Research

Figure 10: Distribution Volume Per Regional



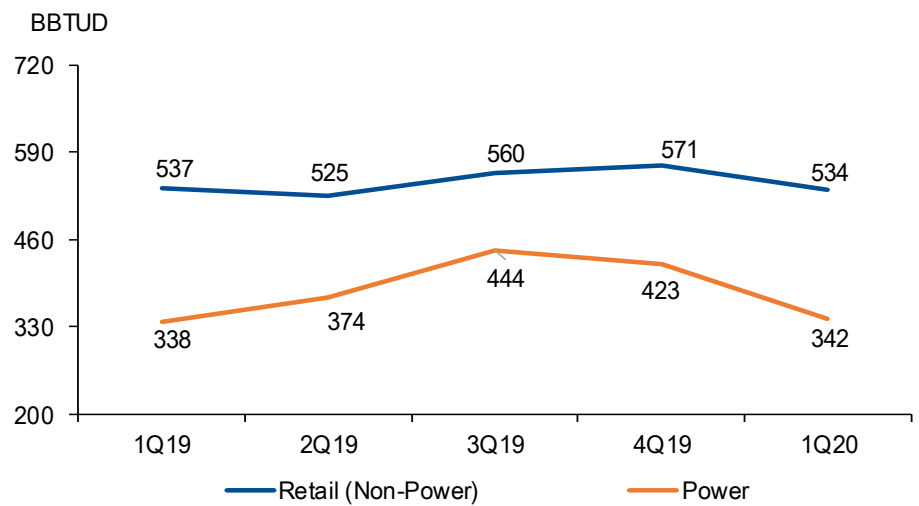
Source: Company Data, NHKSI Research

Figure 11: Industrial Consumption to Total Sales Volume



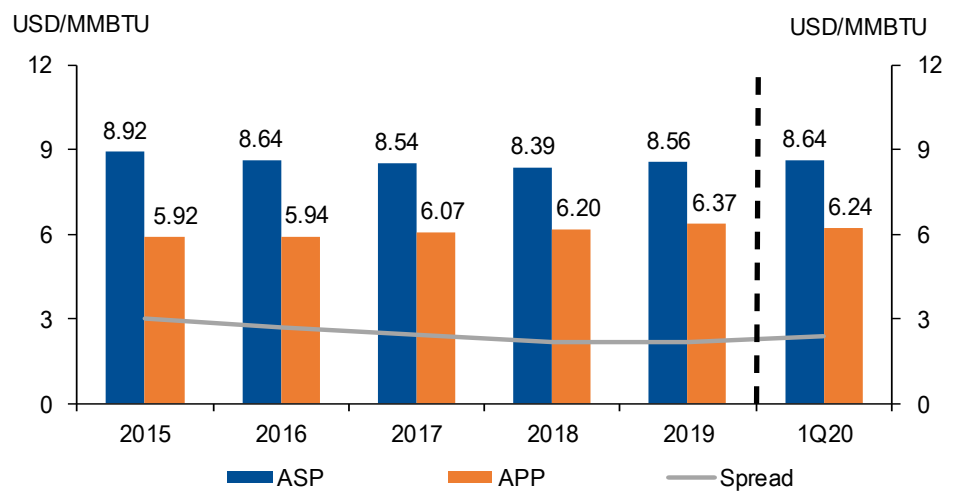
Source: Company Data, NHKSI Research

Figure 12: Trend of Industrial Consumption



Source: Company Data, NHKSI Research

Figure 13: Segment Pricing



Source: Company Data, NHKSI Research

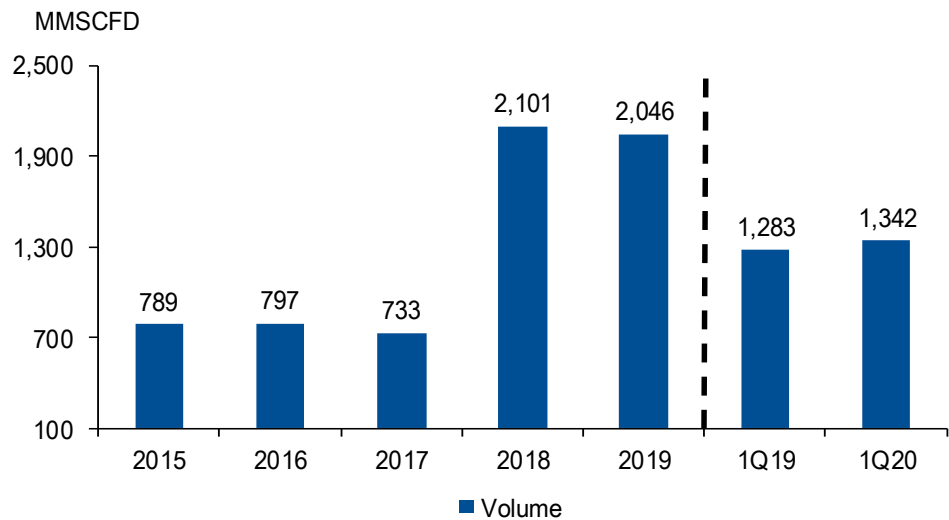
In 1Q20, Pertagas managed to record an increase in transmission volume of 8% YoY

Gas Transmission Segment

PGAS distributes gas products through transmission pipeline infrastructure to end users with the help of cost calculations based on downstream oil business regulations and agreements with BPH Migas. Prices are affected by the channel cost agreement and PGAS facilitates several suppliers to distribute natural gas. The majority of natural gas transmission line targets owned by PGAS are used for electricity needs.

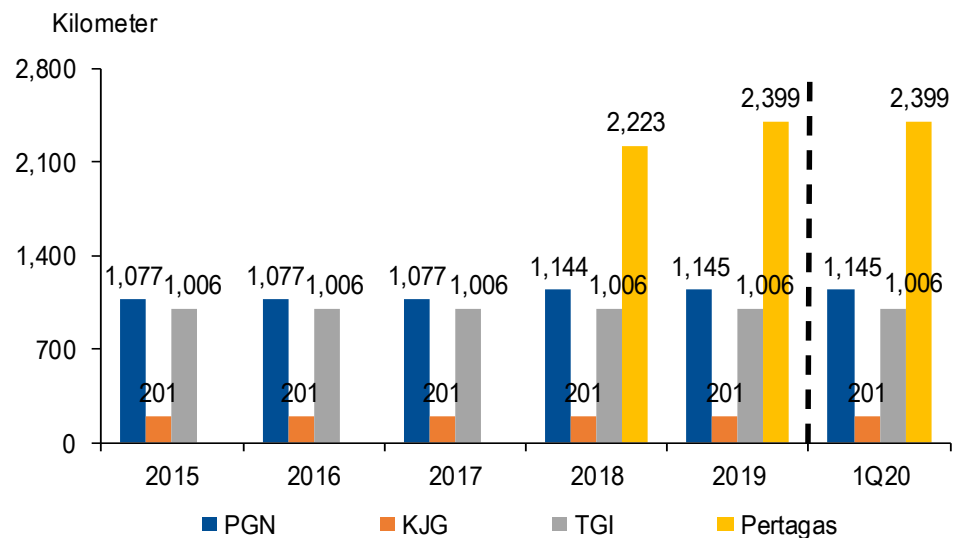
In 1Q20, PGAS owns 4,751 km long transmission pipe which includes 2,399 km operated by Pertagas. Besides, Transgasindo (TGI) operates 1,066 long pipe, and Kalimantan Jawa Gas (KJG) owns 201 km. The performance of the gas transmission business operated by Pertagas was the largest contributor to PGAS's volume of 1,334 MMSCFD, up 8% YoY. For 2020, we estimate that transmission transmission will continue to decline annually, considering; 1) the effect of no contribution from the Muriah Block in 1Q20 so that it will have an impact on PGAS performance; 2) pandemic conditions in 1H20.

Figure 14: Transmission Volume



Source: Company Data, NHKSI Research

Figure 15: Length of Transmission Pipeline



Source: Company Data, NHKSI Research

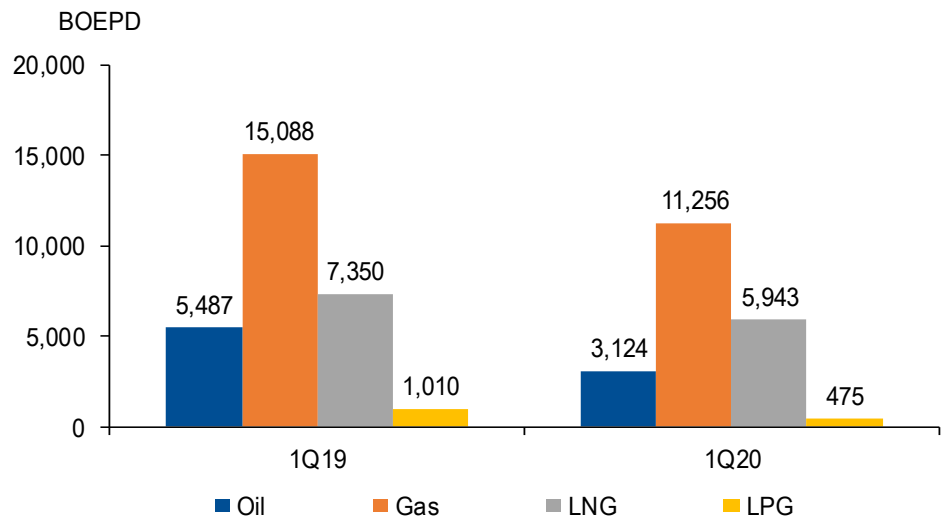
Upstream segment will still be depressed in 2020 after the SEI expansion delay this year

Upstream Segment

SEI is a subsidiary of PGAS which controls and operates the upstream segment and after PGAS entered the Pertamina group, it made it easy for SEI to participate in the oil and gas PSC in Indonesia. Currently, SEI participates in 12 PSCs with PSCs in charge of production in Muara Bakau, Fasken, Muriah, Pangkah, Bangkanai, and Ketapang. From the 12 PSC assets, SEI could produce a total of 28,294 BOEPD of oil, gas, LNG and LPG lifting in 2019.

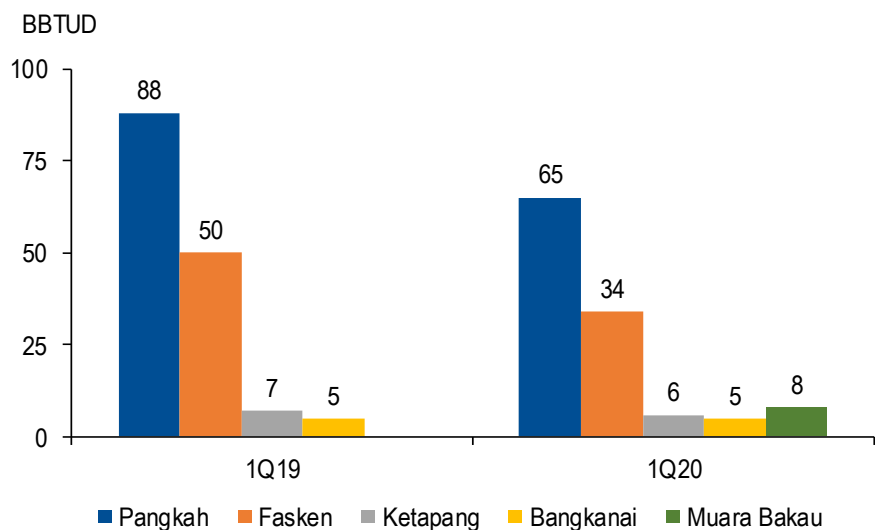
In 1Q20, SEI experienced a decrease in the amount of lifting to 20,798 BOEPD or a 28% YoY decrease due to falling world oil prices coupled with pandemic conditions which resulted in lower production activities. For 2020, we will still see the upstream segment producing lower total lifting of around 23,000 BOEPD-24,000 BOEPD. Our estimation considers; 1) certainty that there will be no expansion for SEI in 2020; 2) the average global oil price for the WTI benchmark is in the range of USD30/barrel-USD40/barrel.

Figure 16: Oil & Gas Lifting



Source: Company Data, NHKSI Research

Figure 17: Gas Production by Location



Source: Company Data, NHKSI Research

LNG terminal project in Teluk Lamong can increase PGAS's gas supply up to 30 BBTUD

Potential Project

PGAS has a potential project which is the construction of LNG terminal in Teluk Lamong, East Java, which is estimated to operate starting in 2020. This project is predicted to spend USD20 million, and hoped to increase the PGAS's gas supply. The LNG terminal construction will be done in three phases.

Phase 1 is the construction of Floating Storage Unit (FSU), Onshore Receiving Facility (ORF), and cryogenic and gas distribution pipeline. Phase 2 is the construction of LNG filling station. Phase 3 is the last step where the LNG storage tank (offshore) is built. Until 1Q20, phase 1 and 2 has reached 91% of construction, while studies are still being conducted for phase 3 project.

Figure 18: LNG Infrastructure in Teluk Lamong



Source: Company Data

Valuation & Recommendation

Initiate to BUY with Target Price at IDR1,400

We initiate to BUY with blended target price at IDR1,400 and our valuation is based on DCF Valuation and forward PE methodology with a 55% weightage to DCF in accordance to its enterprise value and 45% is based on 23.2x forward P/E. For DCF, we used WACC of 5.5% with constant growth of 4% so get the terminal value of USD30,095 million. As for forward P/E, we use P/E with a 5-year historical mean period.

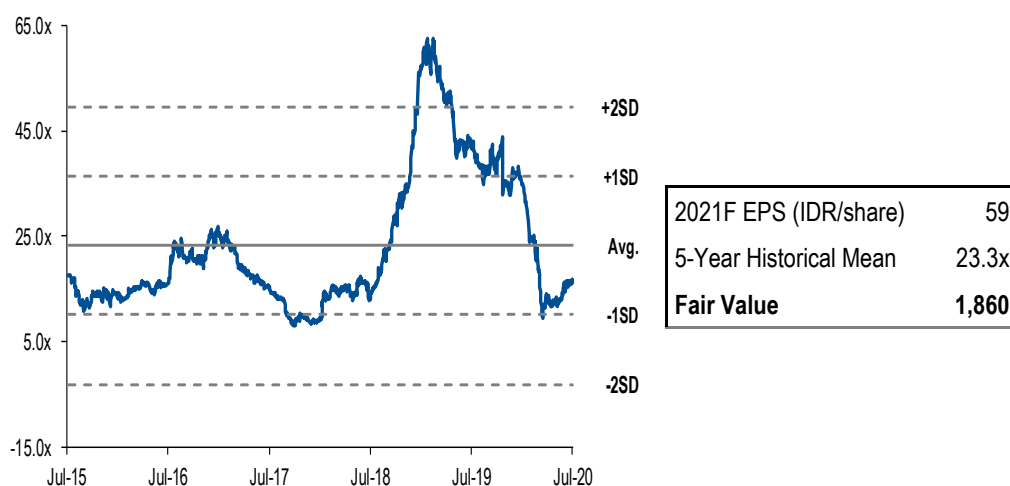
Table 1: DCF Valuation

Assumptions	2019	PV of Terminal Value	24,299
Beta	1.91	EV	26,513
Risk Market Premium	3.0%	LT Employee Benefits	148
Risk Free Rate	4.2%	Non-Controlling Interest	673
Cost of Equity	9.9%	Fair Value	1,060
Cost of Debt	0.2%		
Tax Rate	22%		
Weight of Equity	54%		
Weight of Debt	46%		
WACC	5.5%		

DCF (USD mn)	2019	2020	2021	2022	2023
EBIT (1-Tax)	518	539	561	583	606
Depreciation	458	807	1,022	1,175	1,234
Δ NWC	-216	-198	-433	-88	-92
Capex	241	405	392	359	343
Free Cash Flow	952	1,140	1,623	1,487	1,589

Source: Company Data, NHKSI Research

Figure 19: 5-Year Forward P/E Band



Source: Company Data, NHKSI Research

Sensitivity Analysis

We conduct a sensitivity analysis for each change in WACC on the target price. Each change value always varies, in the WACC range of 4.9% to 6.1% will result in a target price in the range of IDR1,325 to IDR1,500 with a beta range of 1.75 to 2.05.

Table 2: Impact of Changes WACC

Beta Sensitivity	WACC	Changes to TP (IDR)	Change in TP
1.75	4.9%	1,500	-6.6%
1.80	5.1%	1,450	-3.4%
1.85	5.3%	1,425	-1.7%
1.91	5.5%	1,400	
1.95	5.7%	1,375	1.8%
2.00	5.9%	1,350	3.7%
2.05	6.1%	1,325	5.6%

Source: Company Data, NHKSI Research

Financial Review

Quarterly Review

	1Q19	2Q19	3Q19	4Q19	1Q20					2Q20E
					Actual	Estimate	YoY %	QoQ %	Surprise %	
Income Statement										
Revenue	876	929	1,022	1,021	874		-0.3	-14.4		655
Gross Profit	285	295	307	340	287		0.7	-15.7		191
EBIT	155	86	136	107	155		0.2	44.9		66
EBITDA	182	263	247	250	184		0.9	-26.4		319
Net Profit	65	33	75	-70	48		-26.6	-168.1		14
Margin										
Gross Margin	32.5	31.7	30.0	33.3	32.9		0.3	-0.5		29.1
EBIT Margin	17.7	9.2	13.3	10.5	17.8		0.1	7.3		10.1
EBITDA Margin	20.8	28.3	24.2	24.5	21.1		0.2	-3.4		48.8
Net Profit Margin	7.4	3.6	7.3	-6.9	5.5		-2.0	12.3		2.2

Unit: USD mn, %

Source: Company Data, NHKSI Research

Earnings Revision

		2020F	2021F	2022F
Income Statement				
Revenue	-New	3,090	3,439	3,620
	-Previous	-	-	-
	-Change %	0.0	0.0	0.0
	-Consensus	3,178	3,367	3,424
Gross Profit	-New	936	1,082	1,178
	-Previous	-	-	-
	-Change %	0.0	0.0	0.0
	-Consensus	981	1,055	1,076
EBIT	-New	383	463	529
	-Previous	-	-	-
	-Change %	0.0	0.0	0.0
	-Consensus	337	365	405
EBITDA	-New	1,191	1,485	1,704
	-Previous	-	-	-
	-Change %	0.0	0.0	0.0
	-Consensus	777	826	894
Net Profit	-New	97	134	154
	-Previous	-	-	-
	-Change %	0.0	0.0	0.0
	-Consensus	85	149	176
Margin				
Gross Margin	-New	30.3	31.5	32.6
	-Previous	-	-	-
EBIT Margin	-New	12.4	13.5	14.6
	-Previous	-	-	-
EBITDA Margin	-New	38.5	43.2	47.1
	-Previous	-	-	-
Net Profit Margin	-New	3.1	3.9	4.3
	-Previous	-	-	-

Unit: USD mn, %

Source: Company Data, NHKSI Research

Financial Summary

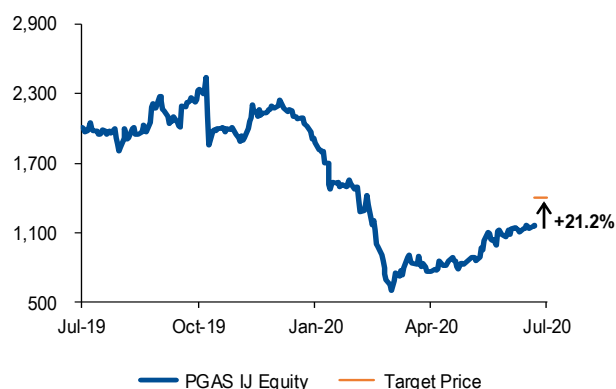
INCOME STATEMENT					PROFITABILITY & STABILITY				
(USD mn)	2019/12A	2020/12F	2021/12F	2022/12F		2019/12A	2020/12F	2021/12F	2022/12F
Revenue	3,849	3,090	3,439	3,620	ROE	2.1%	3.0%	4.0%	4.4%
<i>Growth</i>	-0.6%	-19.7%	11.3%	5.3%	ROA	0.9%	1.3%	1.6%	1.7%
COGS	(2,621)	(2,154)	(2,357)	(2,441)	ROIC	3.5%	3.5%	4.6%	5.0%
Gross Profit	1,227	936	1,082	1,178	Cash Dividend (USDmn)	97	100	107	134
<i>Gross Margin</i>	31.9%	30.3%	31.5%	32.6%	Dividend Yield	2.6%	3.4%	3.6%	4.5%
Operating Expenses	(709)	(553)	(619)	(650)	Payout Ratio	144.1%	102.9%	79.5%	87.2%
EBIT	518	383	463	529	DER	128.0%	140.5%	160.5%	155.0%
<i>EBIT Margin</i>	13.5%	12.4%	13.5%	14.6%	Net Gearing	90%	108%	134%	140%
Depreciation	522	807	1,022	1,175	LT Debt to Equity	78.2%	89.6%	105.3%	103.9%
EBITDA	1,040	1,191	1,485	1,704	Capitalization Ratio	46.0%	49.8%	53.6%	53.4%
<i>EBITDA Margin</i>	27.0%	38.5%	43.2%	47.1%	Equity Ratio	43.9%	41.6%	38.4%	39.2%
Interest Expenses	(210)	(165)	(173)	(182)	Debt Ratio	37.3%	41.3%	44.3%	44.9%
EBT	280	229	359	420	Financial Leverage	234.4%	250.6%	257.7%	255.0%
Income Tax	(167)	(90)	(101)	(118)	Current Ratio	196.6%	202.5%	223.3%	231.9%
Minority Interest	(45)	(42)	(124)	(148)	Par Value (IDR)	100	100	100	100
Net Profit	68	97	134	154	Total Shares (bn)	24,242	24,242	24,242	24,242
<i>Growth</i>	-80.0%	43.8%	38.4%	14.6%	Share Price (IDR)	2,170	1,720	1,720	1,720
<i>Net Profit Margin</i>	1.8%	3.1%	3.9%	4.3%	Market Cap (IDR tn)	52.6	41.7	41.7	41.7

BALANCE SHEET					VALUATION INDEX				
(USD mn)	2019/12A	2020/12F	2021/12F	2022/12F		2019/12A	2020/12F	2021/12F	2022/12F
Cash	1,040	1,438	1,845	1,993	Price/Earnings	55.0x	29.1x	21.4x	19.1x
Receivables	510	523	626	564	Price/Book Value	1.2x	0.9x	0.9x	0.8x
Inventories	71	74	93	94	Price/Sales	1.0x	1.0x	0.9x	0.8x
Total Current Assets	2,209	2,536	3,108	3,172	PE/EPS Growth	-0.7x	0.7x	0.6x	1.3x
Net Fixed Assets	4,250	4,581	4,732	5,005	EV/EBITDA	6.7x	5.0x	4.2x	3.7x
Other Non Current Asset	915	921	928	938	EV/EBIT	13.4x	15.7x	13.4x	11.8x
Total Assets	7,374	8,038	8,768	9,115	EV (IDR bn)	6,926	5,999	6,203	6,262
Payables	260	271	336	306	Sales CAGR (3-Yr)	9.5%	-4.7%	-3.9%	-2.0%
ST Bank Loan	221	322	345	381	EPS CAGR (3-Yr)	-41.0%	-17.9%	-26.0%	31.8%
LT Debt	2,529	2,995	3,543	3,715	Basic EPS (IDR)	39	59	80	90
Total Liabilities	4,139	4,696	5,403	5,541	Diluted EPS (IDR)	39	59	80	90
Capital Stock + APIC	344	344	344	344	BVPS (IDR)	1,868	1,930	1,943	2,064
Retained Earnings	2,729	2,726	2,551	2,571	Sales PS (IDR)	2,223	1,785	1,986	2,090
Total Equity	3,234	3,342	3,365	3,574	DPS (IDR)	56	58	62	78

CASH FLOW STATEMENT					TOP OWNERSHIP		
(USD mn)	2019/12A	2020/12F	2021/12F	2022/12F	By Geography	% Shareholders	%
Operating Cash Flow	893	951	1,107	1,354	Indonesia	85.3	Pertamina 60.0
Investing Cash Flow	(1,736)	(647)	(1,363)	(1,468)	United States	7.1	Norges Bank 1.8
Financing Cash Flow	762	(112)	662	262	Norway	2.7	Vanguard Group 1.6
Net Changes in Cash	(81)	191	407	148	Luxembourg	1.6	FMR 1.3

Source: Company Data, NHKSI Research

Closing & Target Price Update



Source: Bloomberg, NHKSI Research

Rating & Target Price Update

Date	Rating	Target Price	Consensus
2016.12.16	Buy	IDR2,900	IDR3,058
2018.09.10	Buy	IDR2,600	IDR2,438
2020.07.16	Buy	IDR1,400	IDR1,112

Source: NHKSI Research

NHKSI Stock Ratings

- Based on a stock's forecasted absolute return over a period of 12 months from the date of publication.
- Buy: greater than +15%, Hold: -15% to +15%, Sell: less than -15%.
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