

Tobacco (Neutral/Maintain)

Investment Playbook: Focusing on Profitability and Value Amid Headwinds

Report summary

The dynamics of the Indonesian tobacco market

The Indonesian tobacco market, deeply ingrained in the culture, is known for its widespread acceptance of smoking, particularly kretek cigarettes, in our view. Preferred by about 85% of smokers, these kretek cigarettes are a blend of tobacco, cloves, and other flavors. The market offers diverse products like consistent machine-rolled cigarettes (SKM), popular white kretek cigarettes (SPM), and affordable hand-rolled cigarettes (SKT). With an average price of USD\$1.4 per pack, due to domestic sourcing and low labor costs, cigarettes are accessible to a wide range of smokers, catering to various preferences and budgets.

Downtrading still exist, SKT's demand growth still positive

Effective January 1, 2024, Indonesia's Ministry of Finance has introduced a new retail price for cigarettes, along with a 10% YoY increase in excise tax compared to 2023. We anticipate that this regulation will steer middle to lower-income smokers towards cheaper or illegal cigarette options, primarily due to the modest rise in the minimum wage for 2024. The hike in excise tax is likely to influence consumer behavior towards more affordable choices such as Sigaret Kretek Tangan (SKT) and tier 2 Sigaret Kretek Mesin (SKM), benefiting companies like HMSP and WIIM (both Not Rated), in our view. In contrast, GGRM experienced a sales decline in 2023 and is expected to prioritize maintaining profitability, with a projected 9% decrease in sales volume for 2024F.

Simplification of layers could yield benefits for higher-level producers

We believe that simplification of HJE still benefits GGRM and HMSP, going forward. The Ministry of Finance is streamlining tiers from 19 in 2009 to 8 in 2022. Machine-made kretek cigarettes have volume-based taxes, while hand-rolled ones follow a tiered structure. These aim to balance health and revenue but face challenges like tax arbitrage and require ongoing reforms.

Stagnant growth and persistent challenges in e-cigarette innovation

Going forward, we believe that Indonesia's e-cigarette market is booming, becoming one of the world's largest. It offers a less harmful alternative to traditional smoking, thanks to new legislation. However, there are health concerns and stricter regulations than traditional cigarettes, including a 15% tax for e-cigarettes from January 2024. IQOS HEETS, a popular e-cigarette, is costly and caters mainly to higher-income smokers. The industry's future depends on navigating these challenges and adapting to changing regulations.

Maintain Neutral for the sector

Our Neutral stance remains unchanged amidst expectations for an improved economy in 2024F because: 1) the phenomenon of downtrading continues, leading smokers to shift to more affordable segments like SKT and tier-2 SKM; 2) the increase in excise tax for SKT is smaller compared to other segments; and 3) the UMP increase is not proportional to the excise tax hike. Therefore, any better-than-expected sales volume or margin improvement could reverse the stock price trend. We maintain a Trading Buy for GGRM with an unchanged target price of IDR24,500, in light of the subpar results observed in 9M23, we have taken proactive measures to revise our forecast accordingly.

Key investment metrics

Company	Ticker	Market cap * (IDRbn)	Rating	Last price* Target price		Upside (%)	P/B (x)		Div yield (%)		ROE (%)	
				(IDR)	(IDR)		2023F	2024F	2023F	2024F	2023F	2024F
Gudang Garam	GGRM	40,454	Trading Buy	21,025	24,500	16.5	0.8	0.8	4.6	9.8	10.1	10.2

Note: *Data as of January 3, 2024

Source: Company data, Mirae Asset Sekuritas Indonesia Research

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Sector at a glance

The dynamics of the Indonesian tobacco market

The Indonesian tobacco market, deeply rooted in the country's culture, is characterized by the widespread acceptance and prevalence of smoking, particularly kretek cigarettes, in our view. These cigarettes, a unique blend of tobacco, cloves, and other flavors, are a defining feature of the Indonesian smoking culture. Kretek cigarettes are preferred by about 85% of smokers in Indonesia, illustrating the strong cultural connection to this specific cigarette type, in our view.

The affordability and accessibility of cigarettes in Indonesia are key factors contributing to the high consumption rates. With the average cost of a cigarette pack around USD\$1.4, smoking remains an accessible habit for many Indonesians. This affordability is supported by the domestic sourcing of raw materials and the relatively low labor costs in the country, which keep production expenses minimal and prices consumer friendly.

In terms of product categories, the Indonesian tobacco market is diverse. It includes machine-rolled cigarettes (SKM/Sigaret Kretek Mesin), which offer consistency and convenience, white cigarettes (kreteks) (SPM/Sigaret Putih Mesin), which are particularly popular due to their distinctive flavor from cloves, and hand-rolled cigarettes (SKT/Sigaret Kretek Tangan), which are often more affordable and cater to a different consumer segment. This variety caters to a broad range of preferences and economic capabilities within the smoking population.

Cigarette packaging in Indonesia represents different types of cigarettes, each distinguished by their manufacturing process and composition, as follows.

1. SKM (Sigaret Kretek Mesin): This stands for Machine-Rolled Clove Cigarettes. These cigarettes are made using machines and typically include a mixture of tobacco and cloves, or their parts, regardless of the proportion. The manufacturing process covers everything from rolling, filter installation, to retail packaging and tax stamp application. Common brands using SKM include Sampoerna Filter, Classmild, and Surya Gudang Garam.
2. SPM (Sigaret Putih Mesin): This refers to Machine-Rolled White Cigarettes, which are made without the addition of cloves, kelembak, or kemenyan. Like SKM, the entire manufacturing process, from rolling to tax stamp application, is mechanized. Brands like Camel and Marlboro fall under this category.
3. SKT (Sigaret Kretek Tangan): Hand-Rolled Clove Cigarettes. These cigarettes are also made with a mixture of tobacco and cloves, but the production process, including rolling, filter installation, and packaging, is done manually, without machines. Examples of products in this category include Dji Sam Soe Premium and Sampoerna Kretek.
4. SPT (Sigaret Putih Tangan): Hand-Rolled White Cigarettes. These are similar to SKT but made without the addition of cloves, kelembak, or kemenyan. The entire process is manual, and examples include the Ardath brand.

Regulatory challenges and cultural dynamics in Indonesia's tobacco industry

We believe the regulatory environment is an essential aspect of the market. The Indonesian government plans to increase excise tax rates by 10% annually in 2023 and 2024, aiming to reduce smoking prevalence, especially among younger demographics. This regulatory shift is expected to impact the market dynamics, balancing the need to preserve cultural practices with public health objectives.

Despite potential regulatory challenges, we see that the tobacco market in Indonesia continues to remain buoyant, supported by strong domestic demand and cultural acceptance, although downtrading has been present in the last two years. The market's resilience is underpinned by its unique position in Indonesian society, where smoking is not just a habit but a part of the cultural fabric.

However, there are health implications associated with this high prevalence of smoking. The Indonesian government, recognizing the health risks, is actively working on strategies to reduce smoking rates, particularly among youth. This includes the anticipated increase in excise taxes and public health campaigns aimed at raising awareness about the dangers of smoking.

The future of the Indonesian tobacco market may see shifts in consumer behavior and product offerings. Companies are likely to innovate in response to changing regulatory landscapes and consumer preferences, potentially introducing new products that align with health consciousness or different flavor profiles to maintain market interest.

Overall, the Indonesian tobacco market presents a complex interplay of cultural norms, economic factors, and regulatory environments. We think its future trajectory will likely be shaped by how effectively it can adapt to these changing dynamics while retaining its cultural significance in Indonesian society.

Contribution cigarette tax remain high for state revenue

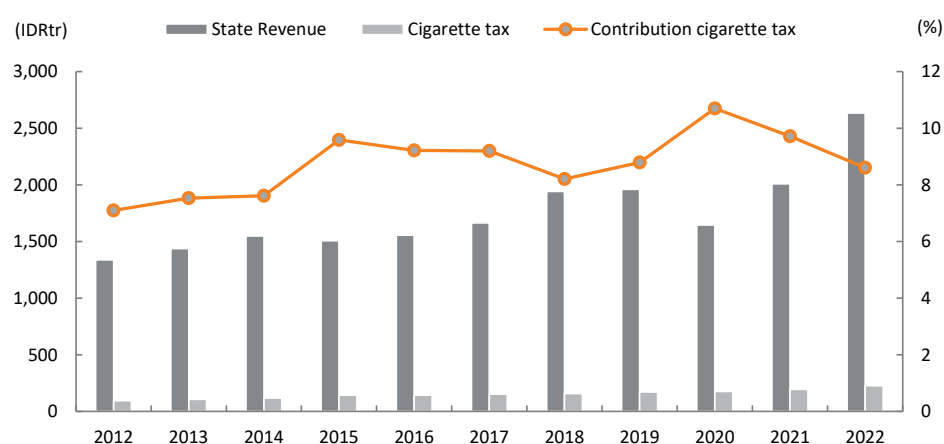
We believe the tobacco industry is expected to continue making significant contributions to Indonesia's state revenue, despite a decline in contributions in 2021 and 2022 due to downtrading, particularly among products from tier-1 manufacturers. Before the pandemic, tobacco excise revenues stood at IDR143.66tr, accounting for 95.5% of all excise revenues, which is a critical source for the state, in our view. From 2012 to 2022, the average contribution from cigarette tax was about 8.8%, with the highest contribution in 2020 at 10.7%.

In addition to its financial contributions, the tobacco industry is a significant employer in Indonesia, employing approximately 1.7mn people in the production of tobacco leaves and cloves. However, we also think it's important to weigh these economic benefits against the health and economic costs associated with smoking, which incur billions in expenses annually due to smoking-related health issues. The Indonesian government has been implementing regulations to mitigate these impacts while trying to maintain the economic benefits. For instance, the government decided to increase tobacco excise by 12% in 2022 and 10% in 2023 & 2024, aiming to boost state revenue and control cigarette consumption, especially among children and teenagers. We think the excise tax increase not only aims to increase state revenue but also to control cigarette consumption, which has proven detrimental to health. The decline in consumption rate is expected to lead to a decrease in production rate, consistent with the government's mission to reduce smoking prevalence, particularly among those under 18 years of age.

The complexity of Indonesia's tobacco taxation system is also notable. Until recently, cigarette tax rates were divided based on product type, volume, and price, aimed to protect smaller manufacturers and local jobs. Effective January 1, 2022, the number of tax tiers was reduced from 10 to 8, as part of the reform to counter rising healthcare costs caused by increasing smoking prevalence and to reduce smoking rates among adolescents.

All in all, we view the tobacco industry in Indonesia plays a significant role in the country's economy, both in terms of revenue generation and employment. However, the government's balancing act between economic benefits and public health costs continues to evolve, with recent measures aimed at reducing smoking rates while maintaining state revenue.

Figure 1. Contribution cigarette tax to state revenue



Source: Ministry of Finance, Mirae Asset Sekuritas Indonesia Research

Major players and market dynamics in Indonesia's tobacco industry

The tobacco industry in Indonesia is a dynamic and influential sector, with several key players shaping its landscape. These companies not only contribute significantly to the market share but also reflect the unique tobacco culture in Indonesia.

HM Sampoerna (HMSP/Not rated) stands as the largest tobacco company in Indonesia, controlling about 28.0% of the market in 2022. Acquired by the global cigarette and tobacco giant Philip Morris in 2005, HM Sampoerna is renowned for distributing the world's best-selling cigarette brand, Marlboro, in Indonesia. In addition to international brands, it offers local favorites like Sampoerna Hijau, Sampoerna A Mild, and the iconic "King of Kretek" Dji Sam Soe. HM Sampoerna is a prominent entity on the Indonesia Stock Exchange (IDX) in terms of market capitalization.

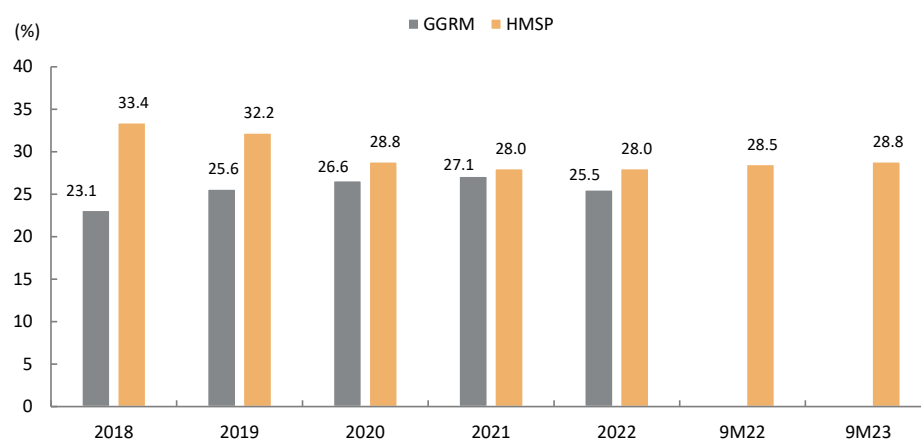
Gudang Garam (GGRM), the second-largest tobacco company, holds around 25.5% of the market in 2022. Known for its significant role in the Indonesian tobacco industry, Gudang Garam has maintained its position as a major player over the years.

Other important cigarette manufacturers include Wismilak Inti Makmur (WIIM/Not Rated) and Bentoel Internasional Investama (RMBA/Not Rated). Additionally, Djarum and Nojorono, although not listed, play a significant role in the industry. Together, these six companies dominate the tobacco market in Indonesia, each contributing to its growth and evolution.

The Indonesian tobacco market is characterized by the widespread popularity of kretek cigarettes, preferred by about 85% of smokers in the country. Kretek cigarettes, a blend of tobacco and cloves, are a trademark of Indonesia and contribute significantly to the market's dynamics. Machine-rolled kretek cigarettes account for around 75% of the total cigarette supply in the country, while hand-rolled cigarettes make up nearly 20%. The tobacco industry in Indonesia benefits from the domestic sourcing of raw materials and low labor costs, which keep production costs low.

With the Indonesian government's focus on reducing smoking prevalence, especially among the younger generation, by planning to increase excise tax rates on cigarettes by 10% annually in 2023 and 2024, the industry is facing evolving challenges. Despite this, the key players continue to adapt and innovate, ensuring their strong presence in the market.

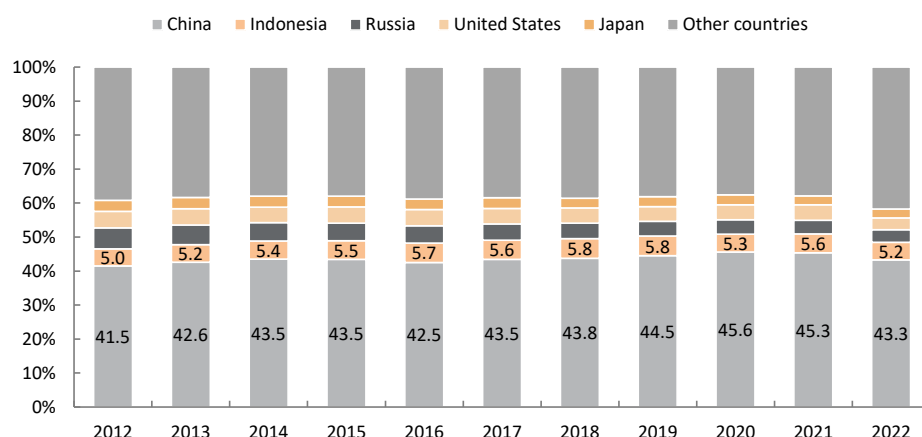
Figure 2. GGRM and HMSP market share



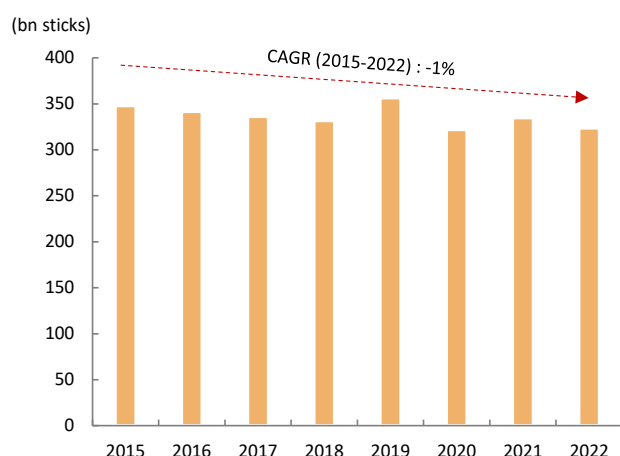
Source: PMI, Statista, Company data, Mirae Asset Sekuritas Indonesia Research

Declining trends in Indonesia's cigarette industry

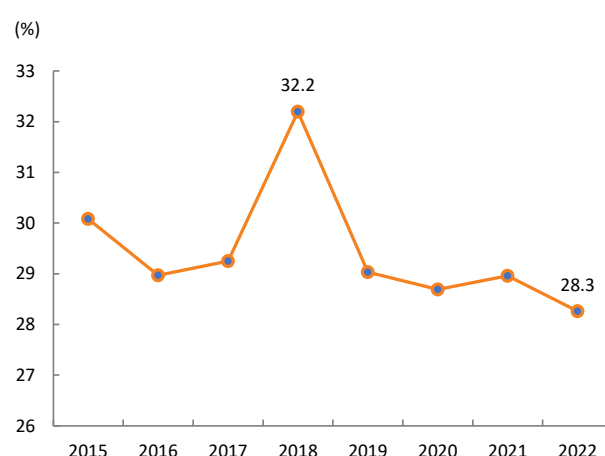
From a business cycle perspective, we observe that the cigarette industry in Indonesia is increasingly entering the sunset phase, despite the presence of new innovations such as e-cigarettes. This is evident from the decline in cigarette production since 2015, with a CAGR (2015-2022) of -1%. Additionally, in line with the government's objectives, the smoking prevalence among the population aged 15 years and above has been decreasing year by year. The percentage share of the population aged 15 years and above was 28.3% in 2022 (compared to 32.2% in 2018).

Figure 3. Indonesia cigarettes' market share is declining in global market

Source: Tobacco Merchants Association, Mirae Asset Sekuritas Indonesia Research

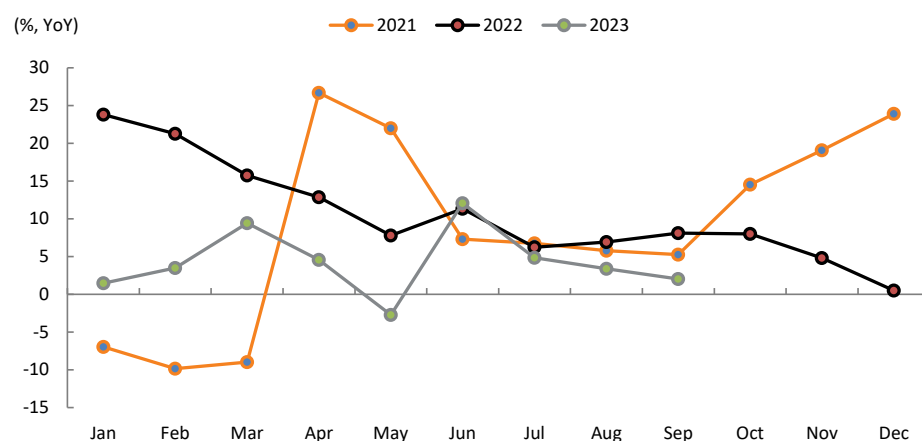
Figure 4. Cigarette production in Indonesia

Source: Ministry of Finance, Mirae Asset Sekuritas Indonesia Research

Figure 5. Smoking prevalence share of the population aged 15 years and above

Source: Statista, Mirae Asset Sekuritas Indonesia Research

Furthermore, we also see relatively high inflation following the fuel price increase in September 2022, triggering a rather stagnant growth for the tobacco sector, particularly in terms of downtrading in the premium segment going forward.

Figure 6. Real sales index: Food, Beverages, and Tobacco (in YoY growth)

Source: Bank Indonesia, Mirae Asset Sekuritas Indonesia Research

Investment Playbook

Downtrading still exist, SKT's demand growth still positive

The Indonesian Ministry of Finance has implemented a new Government retail price (HJE/Harga Jual Eceran) effective from January 1, 2024. These regulations include an adjustment to the excise tax per cigarette stick in 2024, maintaining the same 10% year-on-year increase as in 2023. We believe that this year's rise in excise tax will continue to drive downtrading, especially among middle to lower-income smokers.

We think this trend is further compounded by the modest increase in the 2024 forecast minimum wage, which is set at half of the 2023 increase, around 3.4% YoY. This increase falls below Bank Indonesia's GDP growth forecast for 2024F, projected between 4.7%-5.5% YoY. In our view, these factors could potentially lead smokers to switch to cheaper or illegal cigarettes going forward.

In terms of consumer behavior, which is highly sensitive to price, the higher excise tax on traditional cigarettes in 2024 is expected to cause several market shifts. We anticipate that lower-income smokers will likely shift towards more affordable options such as Sigaret Kretek Tangan (SKT) or tier 2 Sigaret Kretek Mesin (SKM).

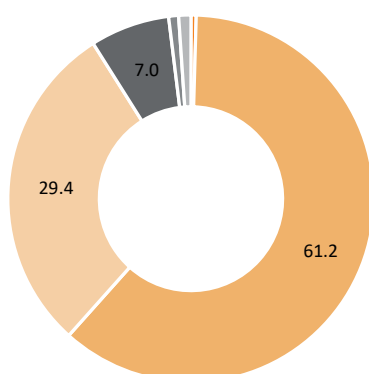
We foresee that this situation will continue to benefit HMSP, which has a SKT market contribution of around 29.4%, and Wismilak Inti Makmur (WIIM). As a tier 2 industry player, WIIM has strategically chosen to keep its SKM production within tier 2 (<3bn sticks annually). As tobacco companies strive to maintain margins, we expect all players will eventually pass on the cost increases to customers.

On the flip side, GGRM experienced a decrease in sales in both the third quarter and first nine months of 2023, in contrast to HMSP's growth during the same periods. This reduction is attributed to a 25% YoY decrease in sales volume due to downtrading. We believe that GGRM will continue to focus on maintaining profitability while bolstering its sales efforts. GGRM's sales volume is expected to contract by about 9% in 2024F.

Figure 7. HMSP's revenue breakdown in 9M23

(%)

- Export
- SKM
- SKT
- SPM
- SPT
- Others

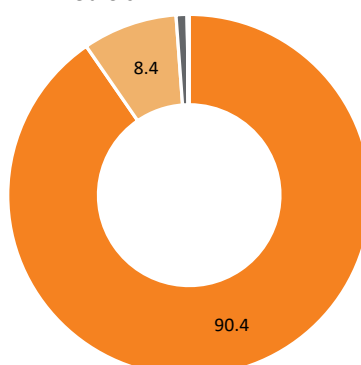


Source: Company data, Mirae Asset Sekuritas Indonesia Research

Figure 8. GGRM's revenue breakdown in 9M23

(%)

- SKM
- SKT
- Paperboard
- Klobot
- Others

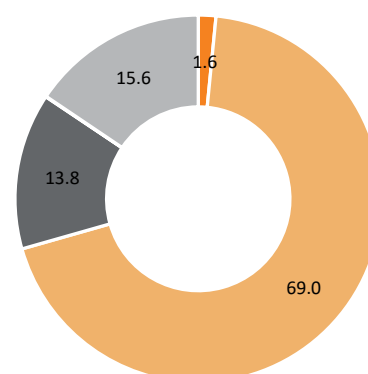


Source: Company data, Mirae Asset Sekuritas Indonesia Research

Figure 9. WIIM's revenue breakdown in 9M23

(%)

- Export
- SKM
- SKT
- Cigar
- Others



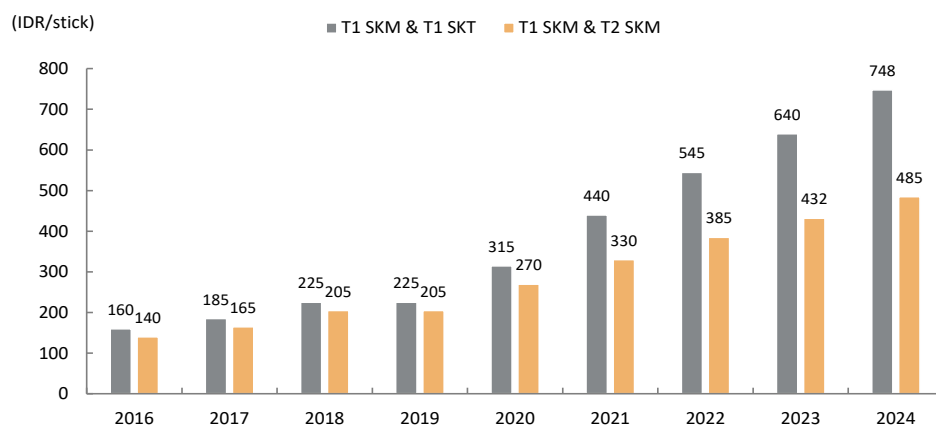
Source: Company data, Mirae Asset Sekuritas Indonesia Research

Figure 10. Yearly excise tax per stick growth

Type of cigarettes	Group	Production group	Gov't retail price (HJE) - 2024	Banderol Tier	2016	2017	2018	2019	2020	2021	2022	2023	2024
					(PMK 198/2015)	(PMK 147/2016)	(PMK 010/2017)	(PMK 010/2018)	(PMK 010/2019)	(PMK 010/2020)	(PMK 010/2021)	(PMK 010/2022)	(PMK 010/2022)
		(sticks)	(IDR/stick)										
Machine rolled	I	>3bn	Minimum 2,260	A	15.7%	10.4%	11.3%	0.0%	25.4%	16.9%	13.9%	11.8%	11.8%
				B									
	II	Not more than 3bn	Minimum 1,380	A	11.5%	7.4%	5.5%	0.0%	22.1%	13.8%	12.1%	11.5%	11.5%
				B	13.2%	11.7%	10.4%	0.0%	23.0%	15.4%	14.3%		
White cigarettes	I	>3bn	Minimum 2,380	A	16.5%	12.1%	12.6%	0.0%	26.4%	18.4%	13.9%	12.0%	12.0%
				B									
	II	Not more than 3bn	Minimum 1,465	A	13.0%	8.2%	12.1%	0.0%	31.1%	16.5%	12.4%	11.8%	11.8%
				B	15.9%	13.7%	22.4%	0.0%	32.4%	18.1%	14.4%		
Hand rolled	I	>2bn	More than 1,375 1,375-1,980	A	10.3%	7.8%	5.8%	0.0%	16.4%	0.0%	3.5%	4.8%	4.8%
				B	11.4%	7.8%	9.4%	0.0%	13.8%	0.0%	4.5%	4.6%	4.7%
	II	>500mn but not more than 2bn sticks	Minimum 865	A	10.7%	6.5%	9.1%	0.0%	11.1%	0.0%	2.5%	4.4%	4.2%
				B	12.0%	10.7%							
	III	Not more than 500mn	Minimum 725	A	5.9%	11.1%	0.0%	0.0%	10.0%	0.0%	4.5%	2.6%	3.4%
				B	0.0%	0.0%							

Source: PMK, Mirae Asset Sekuritas Indonesia Research

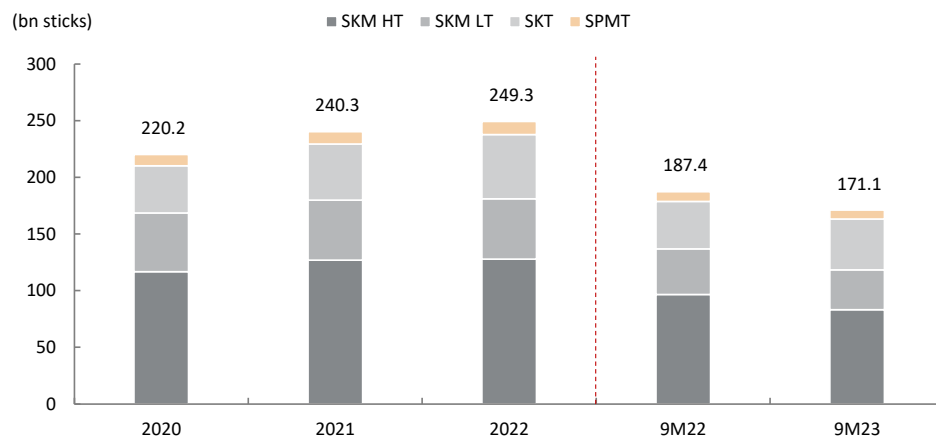
Figure 11. Excise tax between SKM tier-1, SKM tier-2, and SKT tier-1



Note: T1=Tier-1, T2=Tier-2

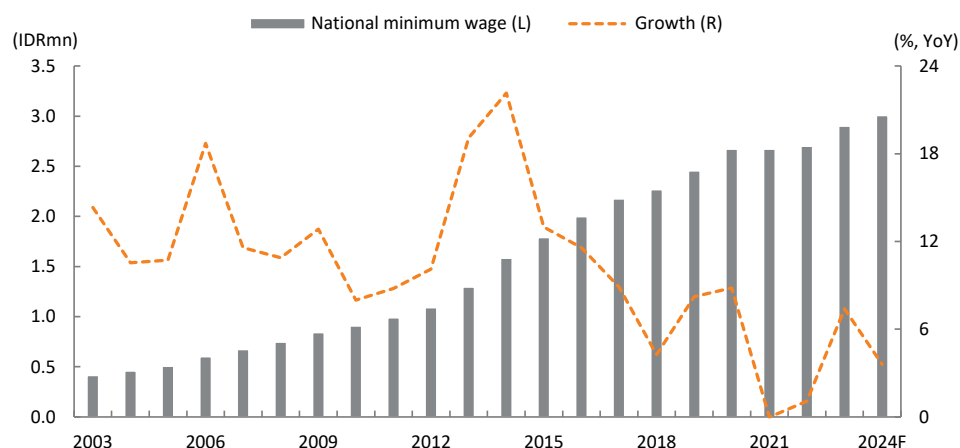
Source: PMK, Mirae Asset Sekuritas Indonesia Research

Figure 12. Industry volume of SKM HT, SKM LT, SKT, and SPMT declined 9% YoY in 9M23



Note: HT=High Tar, LT=Low Tar

Source: Nielsen, Mirae Asset Sekuritas Indonesia Research

Figure 13. Indonesia's minimum wage trajectory

Source: Statistics Indonesia, Mirae Asset Sekuritas Indonesia

Continuing to confront headwinds and stringent regulations

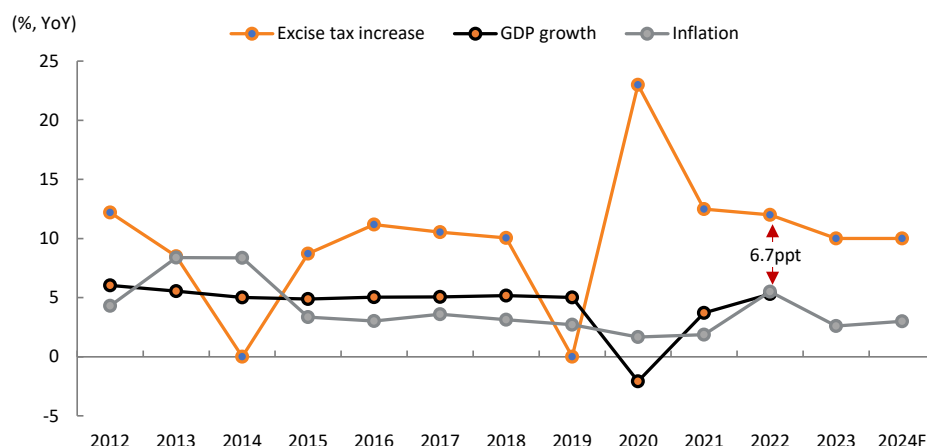
The government has decided to implement a 10% increase in tobacco excise taxes for cigarettes in both 2023 and 2024. The extent of this excise rate increase will vary depending on the type of cigarettes, which includes machine-made kretek (SKM), machine-made white (SPM), and machine-made white kretek (SPM).

Moreover, there will be a 15% increase in excise taxes for electronic cigarettes and a 6% rise for other tobacco products (HPTL). These annual increments will persist for the following five years. Additionally, the government's objective is to reduce the smoking prevalence among individuals aged 10 to 18%, as specified in the National Medium-Term Development Plan (RPJMN) for 2020-2024, to 8.7%.

It's important to note that this tax increase primarily targets machine-made cigarettes (SKM), while hand-rolled cigarettes (SKT) are exempt due to their labor-intensive nature. However, raising excise taxes on SKT could potentially lead to job cuts and a reduction in the workforce.

Nielsen data for the entire tobacco industry shows that sales growth slowed down in 2022, reaching only 3.7%, compared to the 9.1% recovery experienced in 2021. This deceleration in sales volume growth, driven by ongoing economic pressures, has continued to impact the pricing power of tobacco producers. This impact is particularly pronounced due to intense competition for market share.

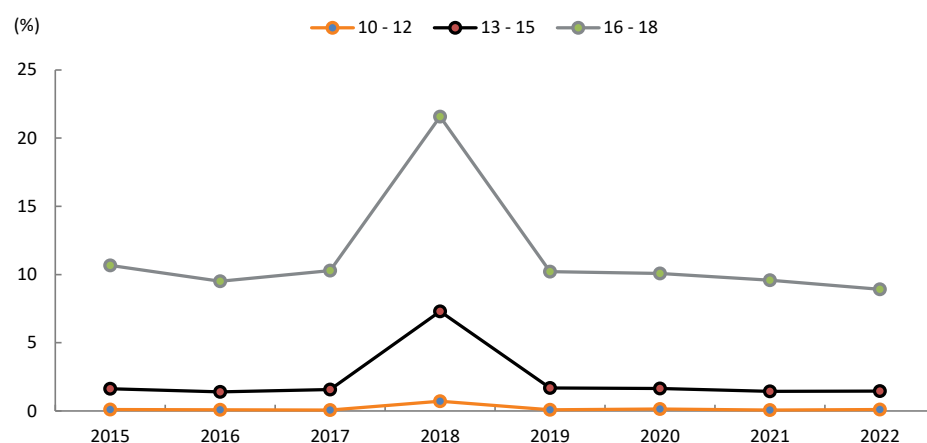
The price adjustments implemented have not kept pace with the increasing excise duty, which encompasses VAT and cigarette tax. To enhance profitability, it is advisable to consider further price increases. Ideally, these increases should align with the recovery of consumer purchasing power and the overall economic improvement in Indonesia.

Figure 14. Excise tax growth exceeds inflation and GDP growth

Source: Ministry of Finance, Statistics Indonesia, Mirae Asset Sekuritas Indonesia Research

In addition to considering cigarette consumption and tax revenue, the Indonesian government also takes into account factors like smoking prevalence among children, employment impact, and the prevalence of illegal cigarettes when determining cigarette excise tax increases.

According to data from Statistics Indonesia (BPS), the prevalence of smoking among individuals aged 10-18 has exhibited a declining trend, reducing from 3.73% in 2015 to 3.44% in 2022. Considering these patterns, we hold an optimistic perspective that forthcoming increases in cigarette excise taxes in Indonesia are likely to be more moderate.

Figure 15. Smoking percentage in population aged ≤ 18 years by age group

Source: Statistics Indonesia, Mirae Asset Sekuritas Indonesia Research

Simplification of layers could yield benefits for higher-level producers

Nonetheless, with the simplification of the price structure for HJE (minimum retail price), we anticipate that both GGRM and HMSP could benefit due to the reduced differentiation and classes for HJE changes moving forward.

The tobacco excise system in Indonesia is quite complex, involving multiple tiers and rates based on various factors such as the type and production volume of tobacco products. As of recent updates, the Indonesian government plans to raise tobacco excise rates by 10% in 2023 and 2024 for hand-rolled cigarettes, with the maximum increase capped at 5% per year. Excise rates for electric cigarettes and other tobacco products will also see increases in the coming years.

The Ministry of Finance has attempted to simplify the tobacco tax tiers, reducing them from 19 tiers in 2009 to 8 tiers in 2022. This simplification is part of a broader strategy to streamline the tax system while still addressing public health concerns and revenue generation.

For example, machine-made kretek cigarettes (a mixture of tobacco and clove) are taxed at two different rates based on production volume. If a tier-1 manufacturer produces more than 3bn cigarettes, the tax is IDR1,231 per stick, whereas for production less than 3bn cigarettes, the tax is IDR 600 per stick. Hand-rolled kretek cigarettes follow a similar tiered structure based on production volumes, with taxes ranging from IDR 115 to IDR 440 per stick, depending on the production scale.

This tiered structure aims to address both public health concerns by discouraging tobacco use and revenue generation for the government. However, it also presents challenges, such as the risk of tax arbitrage and the need for ongoing reforms to further simplify the tax system and make it more efficient.

Figure 16. Yearly excise tax per stick

Type of cigarettes	Group	Production group	Gov't retail price (HJE) - 2024	Banderol Tier	2016	2017	2018	2019	2020	2021	2022	2023	2024
					(PMK 198/2015)	(PMK 147/2016)	(PMK 010/2017)	(PMK 010/2018)	(PMK 010/2019)	(PMK 198/2020)	(PMK 010/2021)	(PMK 010/2022)	(PMK 010/2022)
		(sticks)	(IDR/stick)		IDR	IDR	IDR	IDR	IDR	IDR	IDR	IDR	IDR
Machine rolled	I	>3bn	Minimum 2,260	A	480	530	590	590	740	865	985	1,101	1,231
				B									
	II	Not more than 3bn	Minimum 1,380	A	340	365	385	385	470	535	600	669	746
				B	300	335	370	370	455	525	600		
White cigarettes	I	>3bn	Minimum 2,380	A	495	555	625	625	790	935	1065	1,193	1,336
				B									
	II	Not more than 3bn	Minimum 1,465	A	305	330	370	370	485	565	635	710	794
				B	255	290	355	355	470	555	635		
Hand rolled	I	>2bn	More than 1,375	A	320	345	365	365	425	425	440	461	483
			1,375-1,980	B	245	265	290	290	330	330	345	361	378
	II	>500mn but not more than 2bn sticks	Minimum 865	A	155	165	180	180	200	200	205	214	223
				B	140	155							
	III	Not more than 500mn	Minimum 725	A	90	100	100	100	110	110	115	118	122
				B	80	80							
No of layers					12	12	10	10	10	10	10	8	8

Source: PMK, Mirae Asset Sekuritas Indonesia Research

Figure 17. Government's retail price

Type of cigarettes	Group	Government's retail price (HJE) (IDR/stick)					(% YoY)
		2020	2021	2022	2023	2024	
Machine rolled	I	1,700	1,700	1,905	2,055	2260	10.0
	II	1,275	1,275	1,140	1,255	1,380	10.0
	III	1,020-1,275	1,020-1,275	1,140			
White cigarettes	I	1,790	1,790	2,005	2,165	2380	9.9
	II	1,485	1,485	1,135	1,295	1,465	13.1
	III	1,015-1,485	1,015-1,485	1,135			
Hand rolled	I	1,460	1,460	1,635	1,800	1980	10.0
		1,015-1,460	1,015-1,460	1,135	1,250-1,800	1,375-1,980	10.0
	II	535	535	600	720	865	20.1
	III	450	450	505	605	725	19.8

Source: PMK, Mirae Asset Sekuritas Indonesia Research

Stagnant growth and persistent challenges in e-cigarette innovation

One of the innovations of tobacco sector in Indonesia is e-cigarette. The e-cigarette market in Indonesia has recently experienced substantial growth, positioning it as one of the largest global markets in terms of size. This significant expansion indicates a shift towards vaping as an alternative to traditional tobacco smoking. However, we think this sector faces its unique challenges and controversies.

E-cigarettes are seen as a less harmful alternative for smokers looking to reduce or quit traditional tobacco use. This perspective has been bolstered by the Indonesian Parliament's enactment of Health Law No. 17 of 2023, which legalizes e-cigarettes as addictive substances. Such legal inclusion allows industry participants to operate within a structured framework and provides smokers with less harmful alternatives.

Despite being considered less harmful, e-cigarettes still pose health risks, particularly with long-term use. Their addictive nature necessitates careful regulation to manage potential public health impacts. The regulatory environment for e-cigarettes in Indonesia is becoming more stringent, with the government planning to impose a new tax from January 1, 2024. This tax adds a 15% additional burden on the excise tariff for electronic cigarettes. Furthermore, there is an active public debate in Indonesia regarding vaping products, with opinions divided between banning and regulating them.

The introduction of a 57% excise tax in 2018 on essences used for e-cigarettes, combined with the new taxation policy, may impact the affordability and market penetration of these products. Producers and customers have criticized the swift implementation and lack of consultation regarding these tax changes.

One of the well-known e-cigarettes or Heated Tobacco Units in Indonesia is IQOS HEETS. We believe that IQOS HEETS will become a popular alternative among higher-income smokers who are shifting towards smoke-free options like IQOS. However, we think its usage remains limited due to the relatively high cost of the device, ranging from IDR 475,000 to IDR 649,990 as of January 2024. In our view, this price point will continue to make it a choice for only a select group of smokers, especially considering the ongoing phenomenon of downtrading.

All in all, we think while e-cigarettes offer a viable alternative to traditional smoking and have seen growing market penetration in Indonesia, they face significant challenges, including health concerns, regulatory changes, and a complex taxation environment. The future of the e-cigarette market in Indonesia will likely be shaped by the industry's ability to navigate these challenges and adapt to the evolving regulatory landscape.

Figure 18. E-cigarette market exhibits flat growth in revenue and per capita earnings

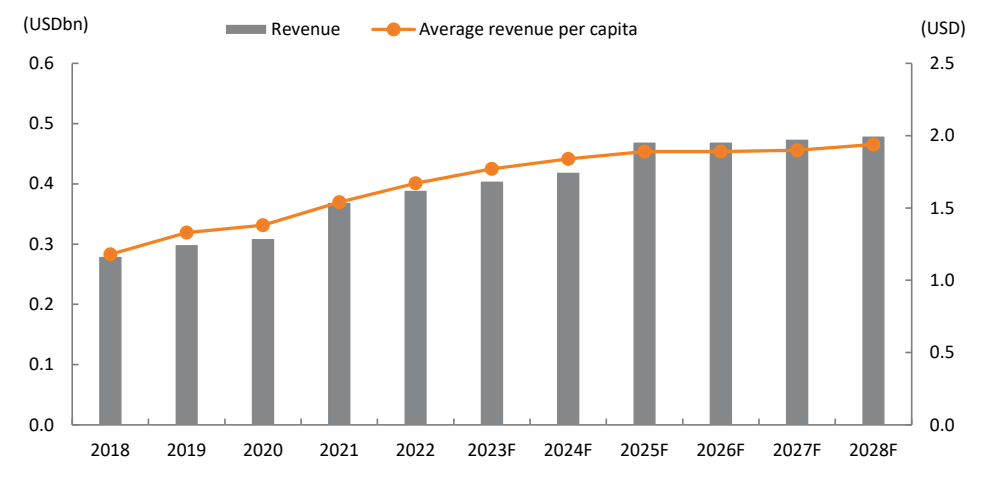


Figure 19. IQOS HEETS



Valuation & Recommendation

Maintain Neutral for the sector

We anticipate that 2024 will continue to present challenges, particularly for tier-1 manufacturers with smaller contributions from Sigaret Kretek Tangan (SKT), due to a larger increase in excise tax relative to the UMP (Minimum Wage). This situation may perpetuate ongoing downtrading. Moreover, we expect that the SKT segment and tier-2 manufacturers will still benefit from the comparatively smaller excise tax hike. This aligns with the two consecutive years of a 10% increase in the average excise tax during 2023-24. Although this increase is lower than the pandemic levels of 12.5% in 2021 and 12.0% in 2022, we believe the widening gap between the UMP increases across provinces and the growth in excise tax is a significant contributing factor.

Looking ahead, we maintain that the simplification of the excise tax structure will positively impact major players like GGRM and HMSP. This change is also expected to narrow the price gap for cigarette players moving forward.

Our Neutral stance remains unchanged amidst expectations for an improved economy in 2024F because: 1) the phenomenon of downtrading continues, leading smokers to shift to more affordable segments like SKT and tier-2 SKM; 2) the increase in excise tax for SKT is smaller compared to other segments; and 3) the UMP increase is not proportional to the excise tax hike. Therefore, any better-than-expected sales volume or margin improvement could reverse the stock price trend.

However, we believe that consumers' preference for trading down to lower-priced brands will persist in 2024F. The simplification of the tax layer is expected to provide a minor buffer against further downtrading to cheaper cigarettes. We maintain a Trading Buy for GGRM with an unchanged target price of IDR24,500, in light of the subpar results observed in 9M23, we have taken proactive measures to revise our forecast accordingly..

Figure 20. GGRM's forward P/E band



Source: Mirae Asset Sekuritas Indonesia Research

GGRM IJ • Tobacco

Gudang Garam

Braving persistent headwinds

(Maintain)
Trading Buy

Target price
IDR24,500

Upside
16.5%

Current price (1/3/24)
IDR21,025

JCI Index	7,279	Market cap (IDRbn)	40,454	Shares outstanding (mn)	1,924	Free Float (%)	23.8
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Report summary

Earnings meet expectation; Hindered SKM sales volume continues

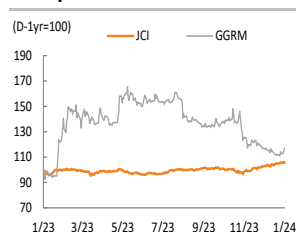
In 3Q23, GGRM's earnings saw impressive YoY growth of 115.9%, reaching IDR1,169bn. However, on a QoQ basis, there was an 11.8% decline. Cumulatively, GGRM's earnings surged to IDR4,457bn, marking a substantial 198% YoY increase. We attribute this growth to several factors, including the low base effect in 9M22, an increase in ASP, and a gradual improvement in efficiency.

Top-line wise, GGRM experienced a sluggish 3Q23, even lower than 2Q23, with revenue amounting to IDR25,897bn (-19.7% QoQ, -0.9% YoY). Cumulatively, GGRM reported negative top-line growth of 13.0% YoY, reaching IDR81,749bn in 9M23. This figure falls short of both our and consensus' estimates at 70% and 66%, respectively. Nevertheless, we cautiously anticipate higher sales in 4Q23 due to higher ASP, considering that 3Q sales were relatively poor. We believe the negative top-line growth in 3Q23 is due to ongoing downtrading, particularly because GGRM's ASP products have nearly reached their maximum price for consumers, with a minimal price increase in 3Q.

We have revised our earnings projections for GGRM downward due to lower-than-expected SKM sales in 3Q23 and downtrading effect. This adjustment is made despite improvements in terms of margins. However, we maintain our Trading Buy recommendation with a lower TP at IDR24,500. Our target price implies a 7.8x 2024F P/E, which is near -2SD of the 5-year mean P/E, derived by the discounted cash flow (DCF) model.

Key data

Price performance



(%)	1M	6M	12M
Absolute	0.0	-23.7	16.8
Relative	-2.6	-31.4	11.1

Earnings and valuation metrics

(FY Dec. 31)	2021	2022	2023F	2024F	2025F
Revenue (IDRbn)	124,881	124,683	108,716	103,131	100,168
Gross Profit (IDRbn)	14,273	11,096	14,730	14,610	13,634
Operating Profit (IDRbn)	7,113	3,771	7,925	8,045	7,172
Net profit (IDRbn)	5,605	2,780	5,942	6,006	5,366
EPS (IDR)	2,913	1,445	3,088	3,121	2,789
BPS (IDR)	30,814	30,069	31,958	32,608	32,994
P/B (x)	0.7	0.7	0.7	0.6	0.6
P/E (x)	7.2	14.6	6.8	6.7	7.5
ROE (%)	9.5	4.8	9.7	9.6	8.5
ROA (%)	6.2	3.1	6.6	6.6	5.9

Notes: NP is attributable to owners of the parent

Source: Company data, Mirae Asset Sekuritas Indonesia Research estimates

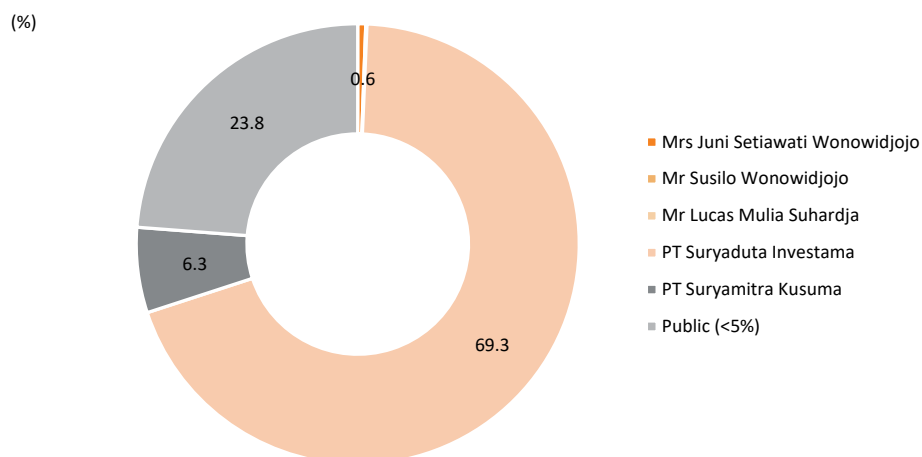
Company at a glance

Leading in full-flavored cigarettes

Gudang Garam (GGRM IJ) is a prominent producer of kretek cigarettes, a type of clove cigarette closely associated with Indonesia and the dominant category in the cigarette market. GGRM is particularly renowned for its SKM FF (full-flavored or high-tar cigarettes), featuring flagship brands like Gudang Garam International and Gudang Garam Signature. According to Nielsen, the company held a significant market share of 25.5%, second only to HM Sampoerna (HMSP IJ) with a 28.0% market share in 2022.

The company was founded by the Wonowidjojo family in 1971. In addition to their personally held shares, the Wonowidjojo family also holds shares through PT Suryaduta Investama, amounting to 69.3%.

Figure 21. Shareholder's composition



Source: Company data, Mirae Asset Sekuritas Indonesia Research

The company presently maintains manufacturing facilities at two principal sites, each dedicated to its primary and secondary kretek production processes. The initial site, located in Kediri, where the company was originally established, also serves as Gudang Garam's headquarters and functions as a vibrant regional trade hub with a population exceeding 290,000. The second site is positioned in Gempol, East Java, roughly 50km from Surabaya. These two strategic locations are aptly situated to fulfill forthcoming market demands.

Gudang Garam manufactures a diverse array of kretek cigarettes, encompassing low-tar (LT) variations alongside traditional hand-rolled kretek. Alongside its core manufacturing operations, the company maintains an internal printing facility and supervises seven subsidiary firms involved in a variety of commercial endeavors.

Table 1. GGRM's subsidiaries

Subsidiaries	Description
PT Surya Pamenang	Producing paperboard for Gudang Garam packaging
PT Surya Madistrindo	Sole distributor of the Company's products
PT Surya Air, Galaxy Prime Ltd, and Prime Galaxy Ltd	Providing non-scheduled air transport services
PT Graha Surya Media	Engaged in entertainment services
PT Surya Inti Tembakau	Engaged in tobacco processing

Source: Company data, Mirae Asset Sekuritas Indonesia Research

Key brand families

GGRM manufactures an extensive assortment of kretek cigarettes, encompassing low-tar-low-nicotine variations, recognized for their light and mild characteristics, as well as traditional hand-rolled kretek cigarettes (SKT). The company distinguishes itself with its Full-Flavored machine-rolled brand (SKM FF).

Table 2. GGRM's product portfolio

Types of cigarettes	Brands			
Hand Made & Klobot <i>Sigaret Kretek Tangan (SKT) & Klobot</i>				
	Gudang Garam Merah 10/12/16	Gudang Garam Djaja 12	Gudang Garam Patra 12	
Machine Made High Tar (Full Flavored – FF) <i>Sigaret Kretek Mesin (SKM) Tinggi Tar</i>				
	Gudang Garam International 12/50	Gudang Garam Signature 12	GG Move 12	
Machine Made Low Tar <i>Sigaret Kretek Mesin (SKM) Rendah Tar</i>				
	Gudang Garam Signature Mild 12/16	GG Mild 16	GG Shiver 16	
				
	Gudang Garam De Luxe 16	Sriwedari 12	Sriwedari Biru Lurik 12	Gudang Garam Klobot 6/12

Table 2. GGRM's product portfolio

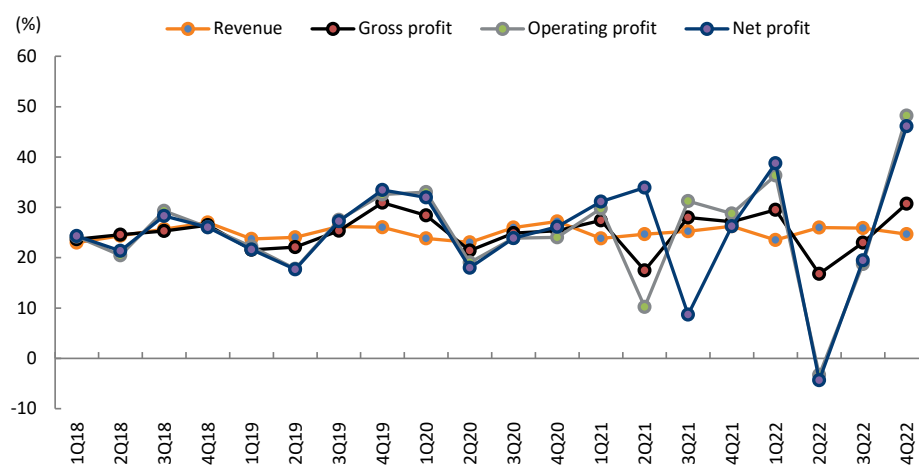
Types of cigarettes	Brands
	   
	Surya 12/16/50 Surya Merah 12 Surya Professional 16 Surya Exclusive 16
	
	Surya Professional Mild 16

Source: Company data, Mirae Asset Sekuritas Indonesia Research

Seasonality

Typically, GGRM's 2H revenue and gross profit make a more substantial contribution to the full-year figures than the 1H results, reaching their peak in the 4Q. This trend is largely a response to the customary announcement of tobacco excise tax adjustments during the 4Q, which prompts the company to pre-emptively raise the Average Selling Prices (ASP) to offset the impending tax increase. We expect this pattern to persist as a result of the planned two-year excise tax hike until 2024F.

Figure 22. Contribution each quarter to full year



Source: Company data, Mirae Asset Sekuritas Indonesia Research

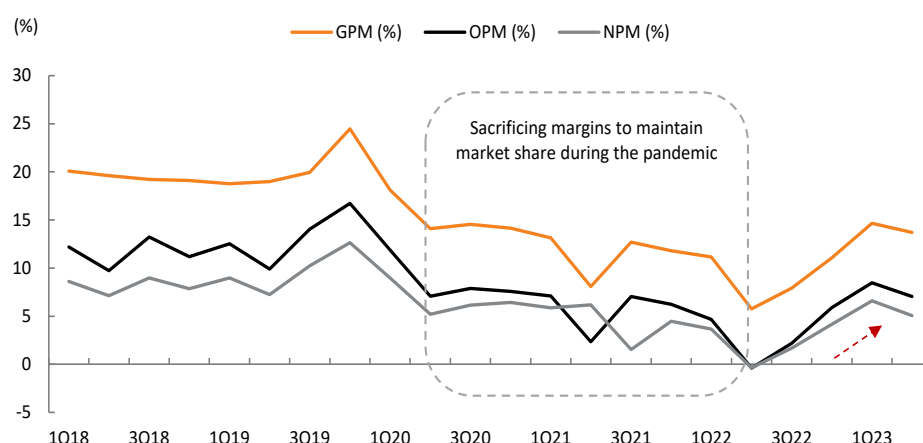
Investment Playbook

Improving margins while grappling with downtrading

During the COVID-19 pandemic, spanning from 2Q20 to 3Q22, GGRM experienced significant margin pressure. This was the result of GGRM's deliberate decision to prioritize market share maintenance over profitability during the pandemic. Despite its popularity among consumers with limited disposable incomes, GGRM was not immune to consumer downgrading, as evidenced by a 9.4% YoY volume decline in 2022, while the industry saw a 4.5% YoY growth in volumes.

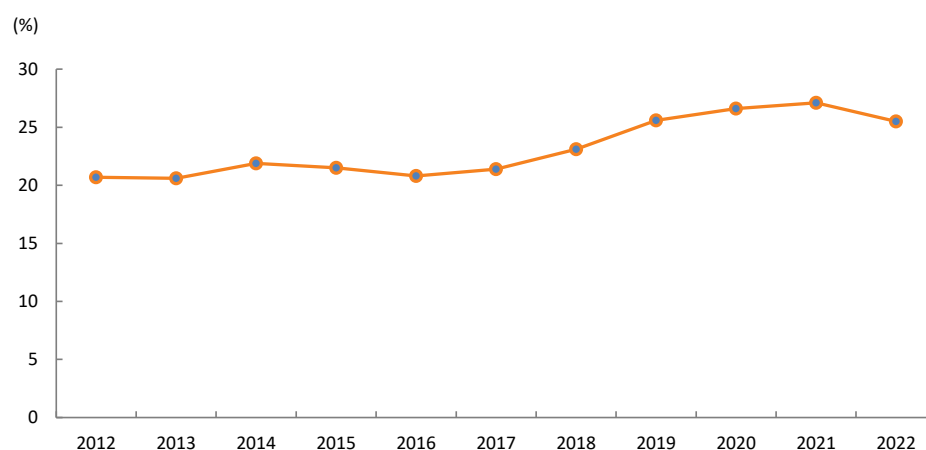
Following a net loss in 2Q22, GGRM appears to be implementing a new strategy centered on margin enhancement. We believe that competitors are also adopting a similar approach in response to consecutive excise tax increases over the past two years. With adjustments made to Average Selling Prices (ASP) and an emphasis on profitability, we anticipate that GGRM could continue its turnaround into 2024 and beyond.

Figure 23. Margins decreased due to the effort to maintain market share, but started improving after the adjustment of ASP



Source: Company data, Mirae Asset Sekuritas Indonesia Research

Figure 24. GGRM's market share in Indonesia cigarette industry



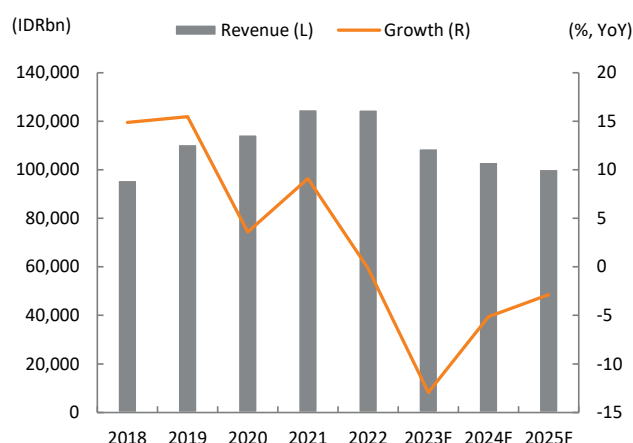
Source: Nielsen, Mirae Asset Sekuritas Indonesia Research

Anticipated modest growth amidst the headwinds

We believe the company has already absorbed the excise tax increase, as evidenced by the improvement in its Gross Profit Margin (GPM). GGRM's GPM increased by more than approximately 5.8ppt in 9M23, reaching 14.0% (compared to 8.2% in 9M22 and 8.9% in FY22). We anticipate that GGRM's EBIT and net profit will continue to improve within 2024F, driven by efficiency measures in areas such as A&P expenses and salaries. However, new excise tax regulations may hamper their top-line growth starting 2Q24. We still believe the company will benefit from the upcoming election and is expected to achieve topline growth in 1Q24.

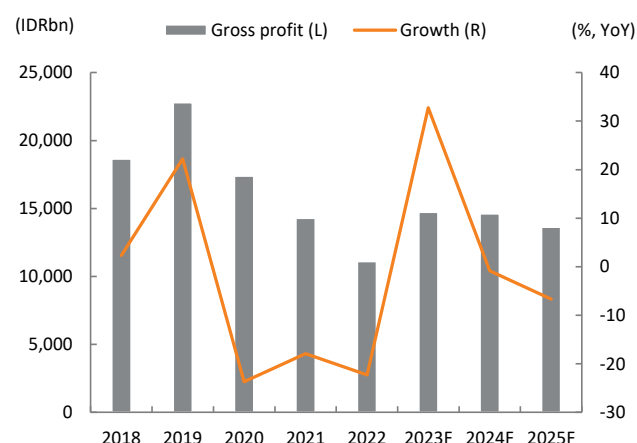
Looking ahead, we project that GGRM's EBIT and net profit will grow with a CAGR (2022-2028F) of 4% and 5%, respectively, while revenue growth will remain low at -5%. Our topline growth projection is based on the assumption of price adjustments and a decline in cigarette volume, particularly for SKM, which is expected to contract by around 15% in 2024F. Meanwhile, sales volume for the SKT segment is expected to remain stable.

Figure 25. Revenue trajectory



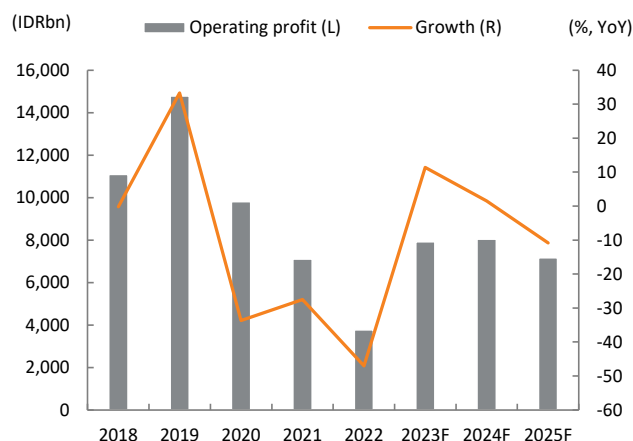
Source: Company data, Mirae Asset Sekuritas Indonesia Research estimates

Figure 26. Gross profit trajectory



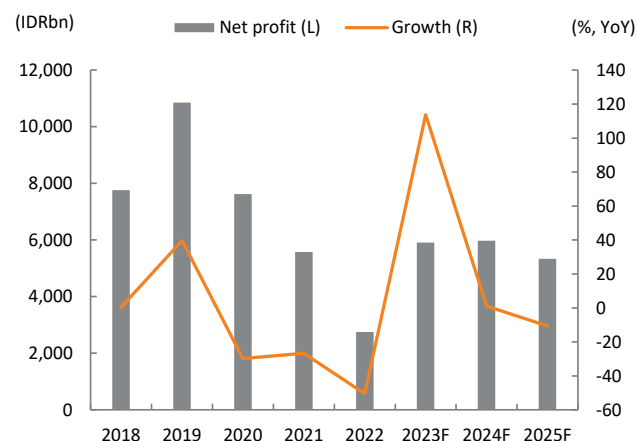
Source: Company data, Mirae Asset Sekuritas Indonesia Research estimates

Figure 27. Operating profit trajectory



Source: Company data, Mirae Asset Sekuritas Indonesia Research estimates

Figure 28. Net profit trajectory



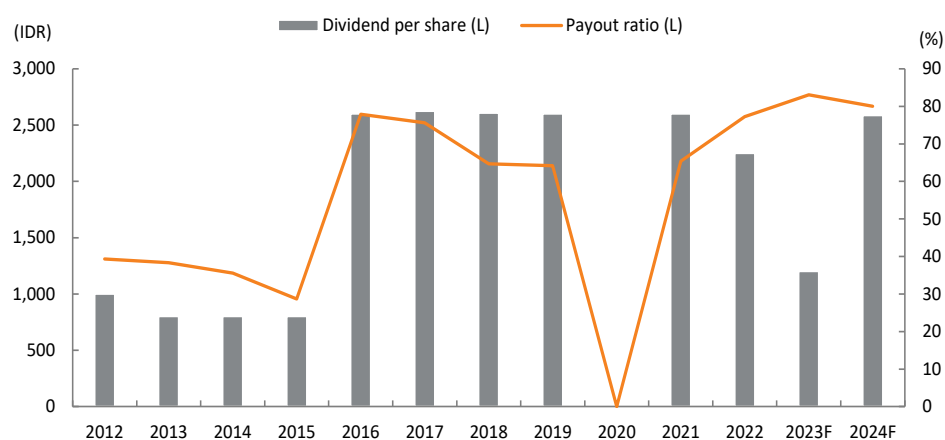
Source: Company data, Mirae Asset Sekuritas Indonesia Research estimates

Lucrative dividend awaits

GGRM often present attractive dividend yields owing to their robust operational cash flow and minimal capital expenditure. With the exception of the year 2020, the company has consistently been inclined towards a generous dividend policy, maintaining a relatively high payout ratio averaging 71% over the period from 2016 to 2019.

We anticipate that, as the company's operational performance continues to strengthen, GGRM will persist in its practice of distributing dividends in the foreseeable future. In the first half of 2023, the company has already disbursed a total of IDR2.3tr, equivalent to IDR1,200 per share, to its investors. Looking ahead, we project a dividend of IDR5tr in 2024F, which could translate into an estimated dividend yield of approximately c.10%.

Figure 29. Dividend per share trajectory



Source: Company data, Mirae Asset Sekuritas Indonesia Research estimates

Recent financial and operational performance

Earnings result as expected, but top line remains sluggish

In 3Q23, GGRM's earnings saw impressive YoY growth of 115.9%, reaching IDR1,169bn. However, on a QoQ basis, there was an 11.8% decline. Cumulatively, GGRM's earnings surged to IDR4,457bn, marking a substantial 198% YoY increase. This aligns with our and consensus' estimates, with run rates of 72% and 71%, respectively. We attribute this growth to several factors, including the low base effect in 9M22, an increase in ASP, and a gradual improvement in efficiency.

Top-line wise, the company experienced a sluggish 3Q23, even lower than 2Q23, with revenue amounting to IDR25,897bn (-19.7% QoQ, -0.9% YoY). Cumulatively, GGRM reported negative top-line growth of 13.0% YoY, reaching IDR81,749bn in 9M23. This figure falls short of both our and consensus' estimates at 70% and 66%, respectively. Typically, 3Q sales are higher 2Q as the company prepares for an excise tax increase. However, the government's consecutive excise tax increases over the past two years have disrupted this pattern. Nevertheless, we cautiously anticipate higher sales in 4Q23 due to higher ASP, considering that 3Q23 sales were relatively poor.

We believe the negative top-line growth in 3Q23 is due to ongoing downtrading, particularly since GGRM's ASP products have nearly reached their maximum price for consumers, with a minimal price increase in 3Q. This is evident from the total sales of SKM (down by 21.4% YoY and 2.4% QoQ to IDR23,150bn), which remain under pressure at IDR73,900bn (-14.1% YoY) in 9M23. We believe sales volume in the SKM segment was more than 20% YoY. In contrast, the SKT segment, which experienced the smallest HJE increase, still showed growth in the third quarter, reaching IDR2,489bn (+4.4% YoY, +15.0% QoQ), translating into cumulative growth by 5.1% YoY in 9M23 to IDR6,898bn. It is worth noting that the SKM segment contributed 90.4% to the company's top line in 9M23.

GGRM's cigarette sales volume lags behind industry growth

We believe that GGRM's cigarette sales volume growth lags behind the industry's growth or declined by 25% YoY in 9M23. Domestic cigarette sales volumes grew on a QoQ basis, with a slight contraction on a YoY basis in the third quarter of 2023, reaching approximately 77.9bn sticks (+8.2% QoQ, -3.9% YoY). However, cumulatively, cigarette industry sales volume (for all cigarette categories) was still down by about 5% YoY, reaching 219.1mn sticks in 9M23.

Improving margins trends

Regarding margins, GGRM noted year-on-year improvements but saw a decline on a quarter-on-quarter basis. In the first nine months of 2023 (9M23), GGRM reported an increase in margins, with Gross Profit Margin (GPM) growing to 14.0%, Operating Profit Margin (OPM) to 7.3%, and Net Profit Margin (NPM) to 5.5%, compared to 8.2%, 2.1%, and 1.6%, respectively, in the same period of 2022 (9M22). We attribute these margin improvements to a combination of factors including lower excise duty, Value Added Tax (VAT), and cigarette taxes, which were influenced by a reduced sales volume of Sigaret Kretek Mesin (SKM) and decreased operational expenses (opex).

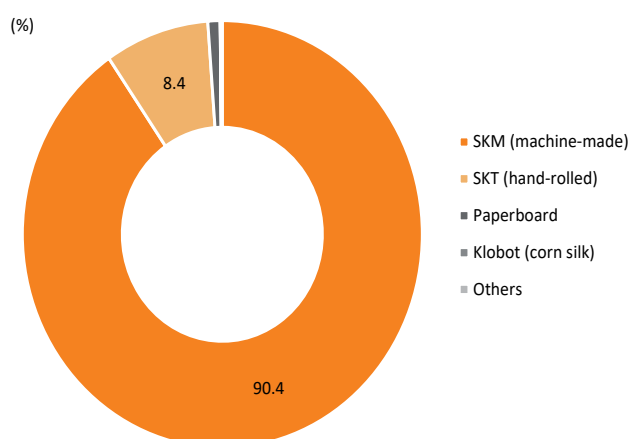
Table 3. GGRM's quarterly earnings results

	3Q22	2Q23	3Q23	YoY (%)	QoQ (%)	9M22	9M23	YoY (%)	Mirae Asset 2023PF	9M23/ Mirae Asset	Cons*	9M23/ Mirae Asset
Revenue	32,247	26,120	25,897	-19.7	-0.9	93,919	81,749	-13.0	116,797	70%	124,498	66%
Cost of sales	29,694	22,543	22,413	-24.5	-0.6	86,230	70,331	-18.4				
Gross profit	2,553	3,577	3,485	36.5	-2.6	7,689	11,418	48.5	15,622	73%	16,891	68%
Operating expenses	1,846	1,739	1,868	1.1	7.4	5,736	5,439	-5.2				
Operating profit	707	1,839	1,617	128.8	-12.1	1,953	5,979	206.1	8,443	71%	8,373	71%
Interest expense	-39	-163	-126	221.0	-22.3	-205	-446	117.4				
Forex gain/loss	12	3	14	21.6	310.1	28	18	-34.2				
Others income	36	34	36	1.3	6.2	171	204	19.4				
Other expenses	-1	-1	-1	10.2	4.9	-3	-3	14.1				
Pre-tax profit	714	1,713	1,540	115.7	-10.1	1,944	5,752	195.9				
Income tax expense	-172	-388	-371	115.1	-4.3	-446	-1,295	190.2				
Net profit	541	1,325	1,169	115.9	-11.8	1,498	4,457	197.6	6,217	72%	6,263	71%
GPM (%)	7.9	13.7	13.5	5.5 pts	-0.2 pts	8.2	14.0	5.8 pts				
OPM (%)	2.2	7.0	6.2	4.1 pts	-0.8 pts	2.1	7.3	5.2 pts				
NPM (%)	1.7	5.1	4.5	2.8 pts	-0.6 pts	1.6	5.5	3.9 pts				

Note: *Data as of October 30, 2023, PF: Previous Forecast

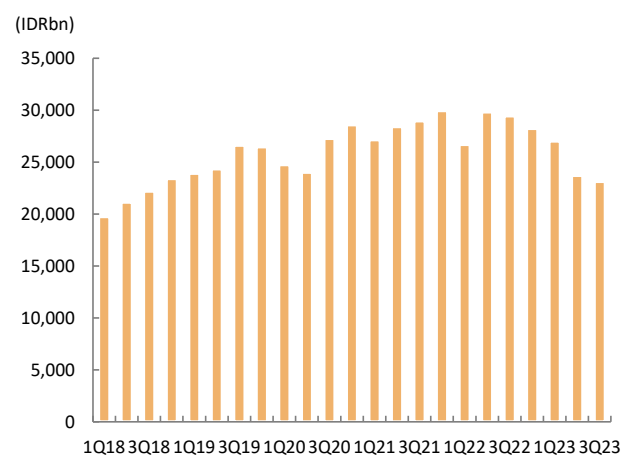
Source: Company data, Mirae Asset Sekuritas Indonesia Research estimates

Figure 30. Revenue breakdown in 9M23



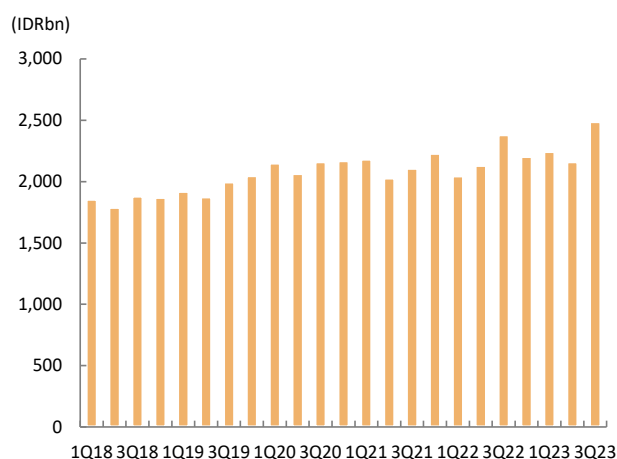
Source: Company data, Mirae Asset Sekuritas Indonesia Research

Figure 31. SKM revenue



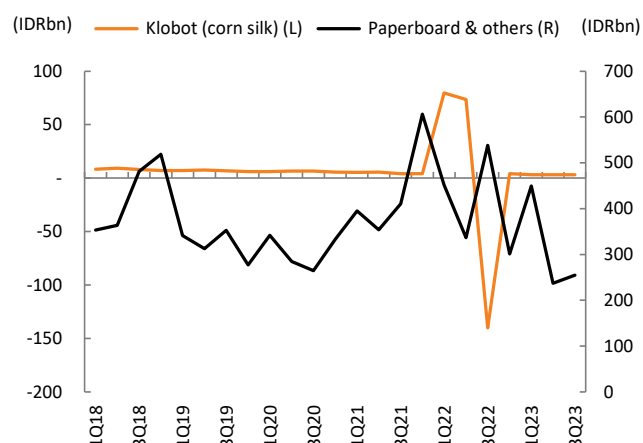
Source: Company data, Mirae Asset Sekuritas Indonesia Research

Figure 32. SKT revenue



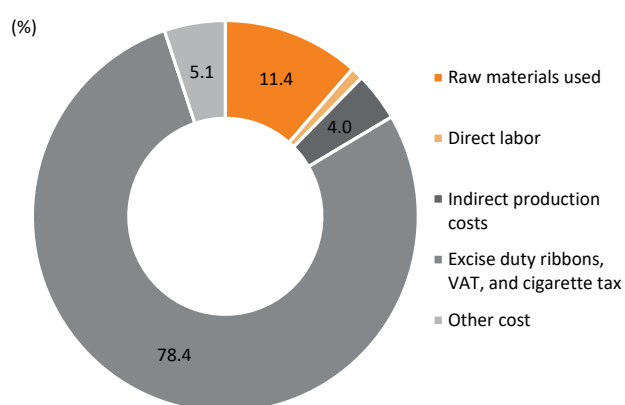
Source: Company data, Mirae Asset Sekuritas Indonesia Research

Figure 33. Klobot, paperboard, and others revenue



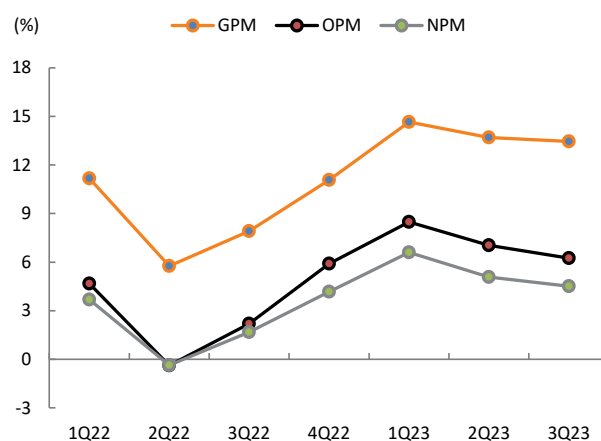
Source: Company data, Mirae Asset Sekuritas Indonesia Research

Figure 34. COGS breakdown in 9M23



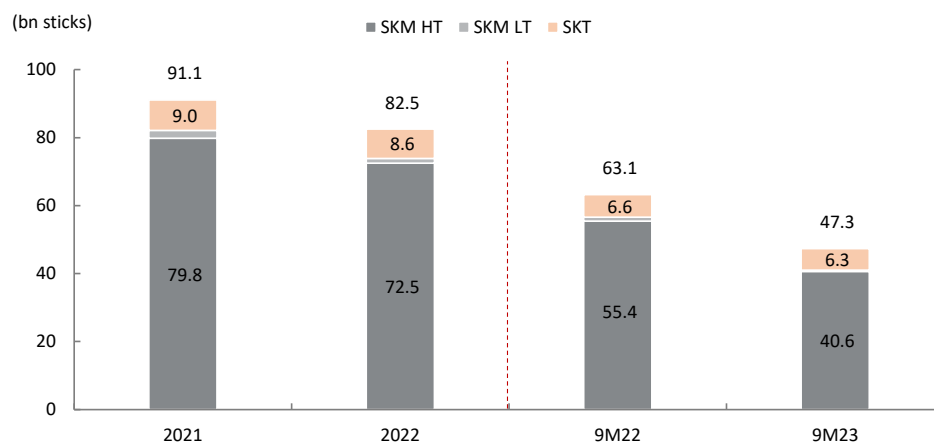
Source: Company data, Mirae Asset Sekuritas Indonesia Research

Figure 35. Quarterly margins



Source: Company data, Mirae Asset Sekuritas Indonesia Research

Figure 36. GGRM's sales volume decline 25% YoY in 9M23



Source: Company data, Mirae Asset Sekuritas Indonesia Research

Fine-tune our forecast mainly in SKM sales volume

Due to a recent performance update, we have adjusted our forecast. We expect lower SKM sales volume than initially anticipated. We have reduced our sales volume assumptions for the SKT segment while maintaining its profitability in line with the company's improvements.

Furthermore, although we expect another increase in ASP for 4Q23 due to the alignment with the new excise tax for 2024, we still anticipate a continued downtrading effect. This is also supported by the ongoing weakness in the cigarette industry sales volume, which was down approximately -5% YoY, reaching 219.1mn sticks in 9M23. It's worth noting that the SKM segment contributes about 90% to GGRM's top line.

Furthermore, we anticipate the possibility of an increase in inflation rates in the coming quarters, as the government may raise interest rates to stabilize the future exchange rate of the Rupiah. We believe this could also have an impact on GGRM's sales volume, as we predict people's purchasing power to decrease, especially for the SKM segment going forward.

Overall, our changes to sales volume have lowered our revenue projections for GGRM in 2023 and 2024. However, moving forward, we still believe the company can maintain improved profitability margins to offset the effects of the declining sales volume.

Table 4. Changes in forecasts (IDRbn)

	Previous forecasts		Current forecasts		Change (%)	
	FY23F	FY24F	FY23F	FY24F	FY23F	FY24F
Revenue	116,797	116,968	108,716	103,131	-6.9	-11.8
Gross profit	15,622	16,049	14,730	14,610	-5.7	-9.0
Operating profit	8,443	8,813	7,925	8,045	-6.1	-8.7
Net profit	6,217	6,466	5,942	6,006	-4.4	-7.1
GPM (%)	13.4	13.7	13.5	14.2	0.2 pts	0.4 pts
OPM (%)	7.2	7.5	7.3	7.8	0.1 pts	0.3 pts
NPM (%)	5.3	5.5	5.5	5.8	0.1 pts	0.3 pts

Source: Mirae Asset Sekuritas Indonesia Research estimates

Valuation and recommendation

Maintain Trading Buy recommendations

We have revised our earnings projections for GGRM downward. This adjustment is due to lower-than-expected SKM sales in 3Q23, despite improvements in margins. Consequently, we have lowered our target price for GGRM to IDR24,500 per share (previously IDR30,000 per share) and maintained our Trading Buy recommendation. Our target price implies a 7.8x 2024F P/E, which is near -2SD of the 5-year mean P/E, derived from the discounted cash flow (DCF) model. Nevertheless, we are still maintaining our dividend payout ratio for 2024F at 80%.

Risks to our recommendation include: 1) worse-than-expected margin and earnings growth, and 2) unfavorable corporate actions and government regulation that could raise concerns about corporate governance and reduce dividend payouts.

Figure 37. GGRM's forward P/E band

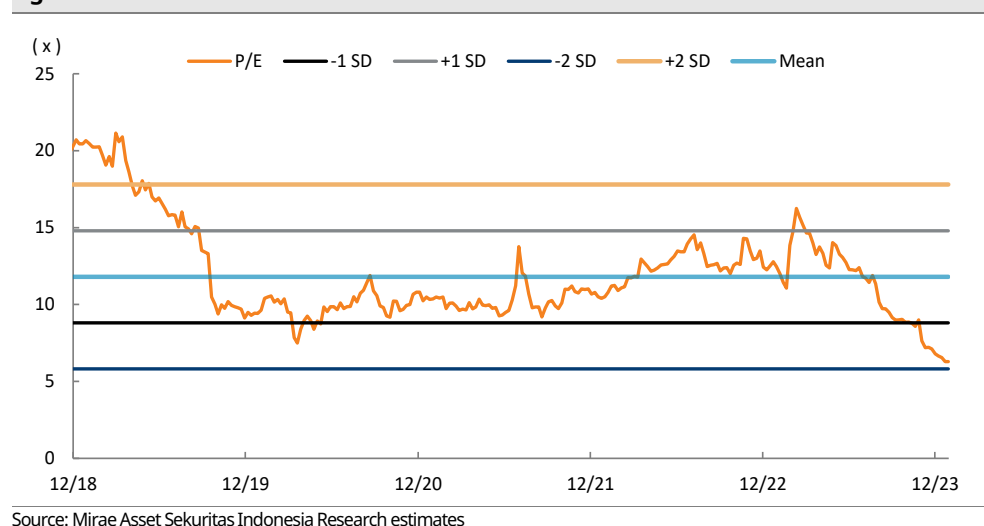


Table 5. Peer valuation comparison

Company name	Market cap (USDmn)	Current P/E	Current P/B	Current EV/EBITDA	Fwd. P/E		Fwd. EV/EBITDA	
					2023F	2024F	2023F	2024F
Hanjaya Mandala Sampoerna Tbk PT	6,615	13.4	3.7	10.7	12.4	11.1	9.2	8.1
Wismilak Inti Makmur Tbk PT	239	7.0	2.1	1.7	N/A	N/A	N/A	N/A
VST Industries Ltd	748	19.1	5.3	12.2	N/A	N/A	N/A	N/A
Japan Tobacco Inc	50,801	13.5	1.7	5.7	13.8	13.5	9.1	8.9
Godfrey Phillips India Ltd	1,362	16.4	3.2	11.9	N/A	N/A	N/A	N/A
British American Tobacco Malaysia Bhd	565	12.5	6.7	9.2	12.6	11.6	10.3	9.7
Ceylon Tobacco Co PLC	576	7.3	18.6	2.8	N/A	N/A	N/A	N/A
ITC Ltd	71,486	30.8	8.6	18.0	28.5	25.6	21.1	18.8
KT&G Corp	9,179	14.1	1.1	6.0	12.2	11.6	7.9	7.5
Average	14,417	14.1	5.2	8.4	14.4	13.3	10.3	9.5
Median	1,981	13.4	3.4	7.6	12.5	11.6	9.1	8.5
Gudang Garam Tbk PT	2,600	7.0	0.7	5.9	6.8	6.7	3.5	3.3

Note: Data as of January 3, 2024

Source: Bloomberg, Mirae Asset Sekuritas Indonesia Research

Gudang Garam (GGRM IJ)

Income statement (Summarized)

(IDRbn)	2022	2023F	2024F	2025F
Revenue	124,683	108,716	103,131	100,168
COGS	113,587	93,986	88,521	86,534
Gross profit	11,096	14,730	14,610	13,634
Opex	7,325	6,806	6,565	6,462
Operating profit	3,771	7,925	8,045	7,172
Other income (expenses)	138	260	248	260
Interest income	0	0	0	0
Interest expense	-262	-366	-285	-277
Profit before income tax	3,647	7,819	8,008	7,155
Income tax expenses	-867	-1,876	-2,002	-1,789
Non-controlling interest	0	0	0	0
Net profit	2,780	5,942	6,006	5,366
EBITDA	6,743	10,861	11,190	10,520

Margin (%)	2022	2023F	2024F	2025F
Gross profit	8.9	13.5	14.2	13.6
Operating profit	3.0	7.3	7.8	7.2
EBITDA	5.4	10.0	10.9	10.5
Net profit	2.2	5.5	5.8	5.4

Growth (% YoY)	2022	2023F	2024F	2025F
Revenue	-0.2	-12.9	-5.1	-2.9
Gross profit	-47.0	11.4	1.5	-10.9
Operating profit	-32.6	8.5	3.0	-6.0
Net profit	-50.4	113.8	1.1	-10.6

Cash flow statement (Summarized)

(IDRbn)	2022	2023F	2024F	2025F
Cash Flows from Op. Activities	9,505	13,436	11,643	9,811
Net profit	2,780	5,942	6,006	5,366
Depreciation/amortization	2,691	2,937	3,145	3,348
Change in working capital	-489	251	46	-96
Others	9,505	13,436	11,643	9,811
Cash Flows from Inv. Activities	-5,338	-4,892	-4,641	-4,508
Capex	-5,338	-4,892	-4,641	-4,508
Others	0	0	0	0
Cash Flows from Fin. Activities	-3,930	-4,344	-4,971	-4,825
Change in liabilities	33	-1,783	-264	-246
Change in equity	0	0	0	0
Dividends paid	366	-252	46	45
Others	-3,930	-4,344	-4,971	-4,825
Increase (decrease) in cash	237	4,200	2,031	479
Beginning balance	4,170	4,407	8,607	10,638
Ending balance	4,407	8,607	10,638	11,116

Note: Net profit refers to net profit attributable to controlling interests

Source: Company data, Mirae Asset Sekuritas Indonesia Research estimates

Balance sheet (Summarized)

(IDRbn)	2022	2023F	2024F	2025F
Current assets				
Cash & equivalents	4,407	8,607	10,638	11,116
Receivables	2,181	2,416	2,292	2,226
Inventories	47,640	42,545	40,057	39,028
Others	1,217	1,397	1,461	1,328
Total current assets	55,445	54,965	54,447	53,698
Non-current assets				
Fixed assets	32,426	34,382	35,878	37,037
Others	691	931	966	976
Total non-current assets	33,117	35,313	36,844	38,013
Total assets	88,563	90,278	91,290	91,711
Current liabilities				
ST bank loans	10,136	8,354	8,090	7,844
Account payables	1,309	1,175	1,107	1,082
Other current liabilities	17,745	17,107	17,165	17,189
Total current liabilities	29,125	26,532	26,285	26,059
Non-current liabilities				
LT bank loans	65	103	77	57
Deferred tax liabilities	328	710	758	677
Others non-current liabilities	1,188	1,443	1,429	1,435
Total non-current liabilities	1,582	2,256	2,264	2,169
Total liabilities	30,707	28,788	28,549	28,227
Shareholders' equity	57,856	61,489	62,741	63,483
Non-controlling interests	0	0	0	0
Total liabilities and equity	88,563	90,278	91,290	91,711

Key valuation metrics/ratios (Summarized)

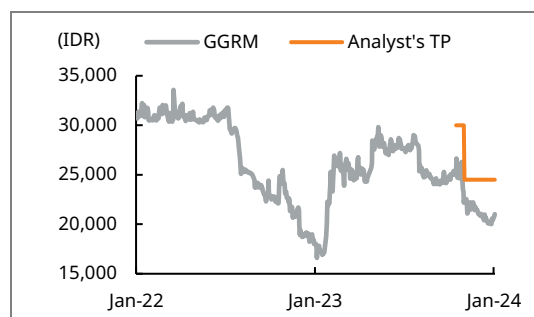
	2022	2023F	2024F	2025F
P/E (x)	14.6	6.8	6.7	7.5
P/B (x)	0.7	0.7	0.6	0.6
EV/EBITDA (x)	5.9	3.5	3.3	3.3
EPS (IDR)	1,445	3,088	3,121	2,789
BPS (IDR)	30,069	31,958	32,608	32,994
DPS (IDR)	2,250	1,200	2,471	2,404
Payout ratio (%)	77	83	80	77
Dividend yield (%)	10.7	5.7	11.8	11.4
Accounts receivable turnover (x)	57	45	45	45
Inventory turnover (x)	0.4	0.4	0.4	0.4
Accounts payable turnover (x)	86	80	80	80
ROA (%)	3.1	6.6	6.6	5.9
ROE (%)	4.8	9.7	9.6	8.5
Current ratio (x)	1.9	2.1	2.1	2.1
Net gearing (x)	0.1	0.0	0.0	-0.1
Interest coverage ratio (x)	-0.5	-0.7	-0.9	-0.9

Appendix 1

Important disclosures and disclaimers

Two-year rating and TP history

Company	Date	Rating	TP (IDR)
Gudang Garam (GGRM JJ)	1/4/2024	Trading Buy	24,500
	11/2/2023	Trading Buy	24,500
	10/16/2023	Trading Buy	30,000
	1/9/2023	Hold	16,500
	11/2/2022	Sell	18,000
	8/1/2022	Sell	20,000
	5/8/2022	Hold	32,300
	1/3/2022	Trading Buy	35,400
	10/29/2021	Hold	33,000



Stock ratings

Buy	Expected 12-month performance: +20% or greater
Trading Buy	Expected 12-month performance: +10% to +20%
Hold	Expected 12-month performance: -10% to +10%
Sell	Expected 12-month performance: -10% or worse

Sector ratings

Overweight	Expected to outperform the market over 12 months
Neutral	Expected to perform in line with the market over 12 months
Underweight	Expected to underperform the market over 12 months

Rating and TP history: Share price (—), TP (—), Not Rated (■), Buy (▲), Trading Buy (■), Hold (●), Sell (◆)

* Our investment rating is a guide to the expected return of the stock over the next 12 months.

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* The TP was determined by the research analyst through valuation methods discussed in this report, in part based on estimates of future earnings.

* TP achievement may be impeded by risks related to the subject securities and companies, as well as general market and economic conditions.

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