

Nippon Indosari (ROTI IJ)

06 April 2016

Initiating Coverage

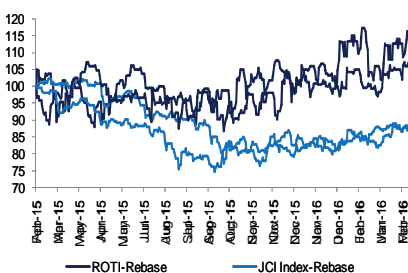
BUY (New)

Stock Data

Target price (Rp)	Rp1,650
Prior TP (Rp)	n/a
Shareprice (Rp)	Rp1,270
Upside/downside (%)	+29.9
Sharesoutstanding (m)	5
Marketcap. (US\$ m)	0
Free float (%)	43.3
Avg. 6m dailyT/O (US\$ m)	0.2

Price Performance

	3M	6M	12M
Absolute (%)	5.8	7.6	15.5
Relative to JCI (%)	-1.0	1.8	25.8
52w high/low (Rp)	1,400 - 1,045		



Major Shareholders

PT. Indoritel Makmur	31.5%
Bonlight Investments, Ltd.	26.5%
Pasco Shikishima Corp.	8.5%

Estimate Change; Vs. Consensus

	2016F	2017F
Latest EPS (Rp)	67	76
Vs. Prior EPS (%)	n/a	n/a
Vs. Consensus (%)	22	14

Source: Bloomberg

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A rapidly growing bread producer

- ROTI is a leading producer in Indonesia's fragmented bakery industry
- Indonesia's low bread consumption will support growth
- Superior earnings growth outlook driven by capacity expansions
- Initiate coverage with BUY at TP of Rp1,650

Market leader in Indonesia. Nippon Indosari (ROTI) is a leading producer in Indonesia's bread industry with 11% market share. The company operates 10 factories located in Java, Sumatera and Sulawesi with capacity of 4.2m pcs/day (4 yr CAGR:20.4%) and is supported by strong product innovation, brand recognition and distribution network of 59,295 points of sales as of Aug 2015. Indonesia's bread industry comprises home/small producers (68% of market); mass producers (20%), of which ROTI dominates 90% of market share, and boutique bakery (12%). We believe the highly fragmented nature of the bread industry offers the company strong growth opportunity as income levels continue to rise.

Low per-capita consumption. Indonesia's bread market grew by 13.3% CAGR in 2010-15, according to Euromonitor. With the country's baked goods consumption per capita of 2.3kg, below ASEAN peers such as Thailand (2.4kg), Malaysia (7.6kg) and Singapore (9.7kg), this should offer scope for strong growth opportunity as Indonesians become more upwardly mobile and require more convenient food to eat such as bread -- as evident from steadily rising per capita bread consumption in Indonesia (6.23% CAGR in 2010-2015) vs. flat rice consumption during the same period.

Superior earnings growth. We forecast ROTI's earnings to grow at 23% CAGR in FY15-18F on the back of its strong, albeit moderating, revenue growth of 20% vs. 29% CAGR of the past five years. Strong growth prospect should also be supported by the company's vigorous expansions, rising promotion and wider distribution coverage, in addition to lifestyle changes towards consumption of baked goods in Indonesia. We expect gross margin to remain at 53% due to low wheat prices and improving sales returns in line with the plan to shift distribution mix towards general trade channel from 25% to 40% by 2020. Company's strong relationship with the Indofood group, which is the dominant player in the flour mill industry in Indonesia, should also support its growth prospect, in our view.

Initiate with BUY. Our DCF-derived target price of Rp1,650(key assumptions: 11.6% WACC, 5% terminal growth) implies target FY17F multiples of 22x P/E and 11x EV/EBITDA, which are well below the valuation of large-cap consumer peers in Indonesia. The stock also currently trades at 2 std below its mean multiples, thus providing a good entry point. We are bullish on ROTI's outlook given its consistency in delivering strong earnings growth in the past five years (22% CAGR). Key risks: economic growth, inflation, wheat flour price.

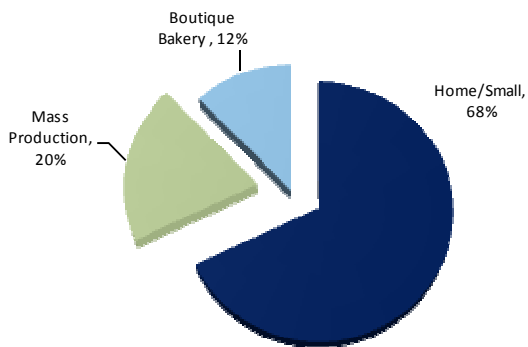
Year To 31 Dec	2014A	2015A	2016F	2017F	2018F
Revenue(RpBn)	1,880	2,175	2,582	3,093	3,741
EBITDA(RpBn)	356	523	633	753	921
EBITDA Growth (%)	30.7	47.0	21.1	19.0	22.3
Net Profit(RpBn)	193	271	338	387	499
EPS (Rp)	38	54	67	76	98
EPS Growth (%)	21.1	40.8	24.7	14.4	28.8
Net Gearing (%)	18.4	(43.4)	5.0	9.8	3.0
PER (x)	33.3	23.7	19.0	16.6	12.9
PBV (x)	6.7	5.4	4.3	3.5	2.8
Dividend Yield (%)	0.2	0.4	0.4	0.5	0.6
EV/EBITDA (x)	17.6	13.3	10.0	8.3	6.9

Source: ROTI, IndoPremier

Share Price Closing as of : April 1, 2016

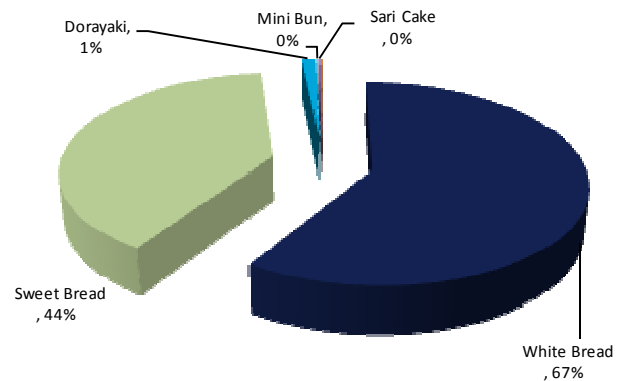
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Fig. 1: Indonesia's Bread Industry Segmentation in 2014



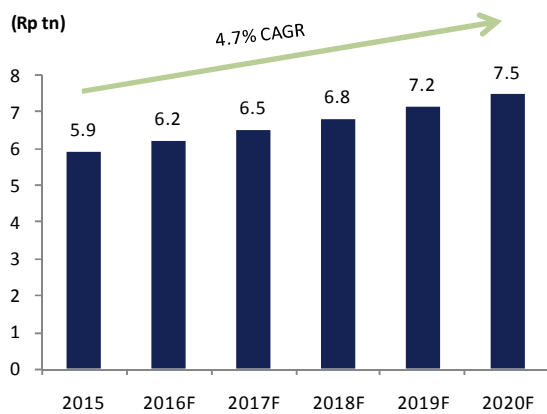
Source: APEBI, Indo Premier

Fig. 2: ROTI's Revenue Breakdown 2015 (% of net sales)



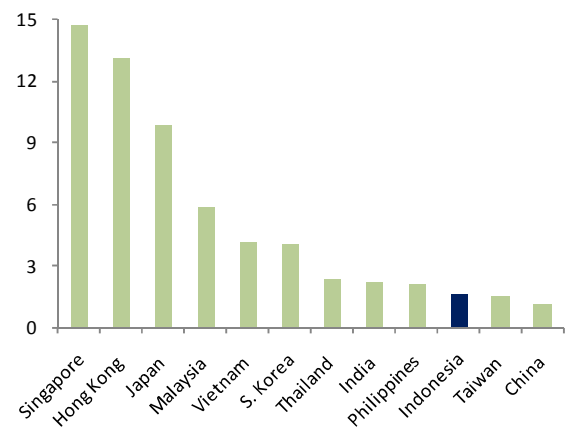
Source: Company, Indo Premier

Fig. 3: Bright outlook for Indonesia's bread industry



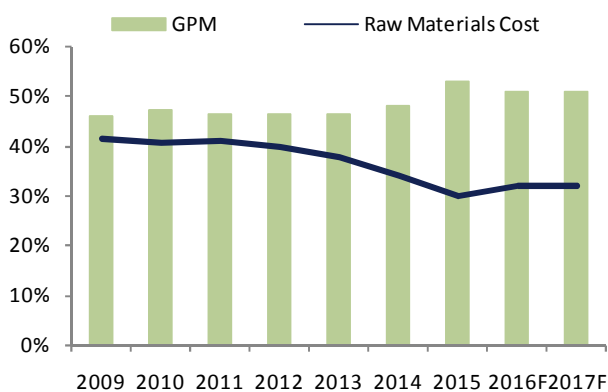
Source: Euromonitor

Fig. 4: Despite Low Baked Goods Per capita Spending



Source: Euromonitor

Fig. 5: Improving GPM on lower raw materials cost



Source: Indo Premier Forecasts

Fig. 6: 1 stdev below its mean, good entry point



Source: Bloomberg

Investment Case

Leading producer in Indonesia's highly fragmented industry

Started in 1996, PT Nippon Indosari is a leading producer in Indonesia's highly fragmented bread industry with 11% market share. The company operates ten factories located in Java (7), Sumatera (2) and Sulawesi (1) with a total capacity of 4.2m pieces a day (CAGR of 20.4% in 2011-2015) and is supported by strong product innovation, brand recognition and extensive distribution network comprising 59,295 points of sale as of August 2015. Indonesia's bread industry has turnover of Rp23tn (US\$1.8bn) in 2015 and comprises three segments: 1) unbranded home/small producers (68% of market); 2) branded large-scale/mass producers (20%), of which ROTI is a dominant player with 90% share, and 3) boutique/franchised bakery (12%). We believe the highly fragmented nature of the bread industry, with large contribution of unbranded products, offers the company strong growth opportunity as income levels continue to rise in Indonesia. In addition, the company has attained various prestigious awards including the best brand award by Top Brand and Forbes Indonesia. In 2015 Top Brand Award, Sari Roti positioned itself at the forefront with a total index of 74. Despite the weaker economic conditions last year, the company has once again been awarded the Best of the Best Award by Forbes Indonesia for three consecutive years, where the evaluation criteria is based on ROE, sales growth, EPS and company's consistency in the past couple of years.

Exposure to high growth Indonesia's bread market

Indonesia's bread market has grown by 13.3% CAGR in 2010-2015, according to Euromonitor. In spite of this, the country's annual baked goods consumption per capita of 2.3kg remained below those of ASEAN peers such as Thailand (2.4kg), Malaysia (7.6kg) and Singapore (9.7kg). In terms of per capita spending, Indonesia stood at US\$8.6 in 2015, which was well below its ASEAN peers, namely: Singapore (US\$51.7), Malaysia (US\$17.3), Thailand (US\$11.4) and Vietnam (US\$9.8). This holds strong growth opportunity as Indonesians become more upwardly mobile and require quicker/more convenient food to eat such as bread and instant noodles. This trend is evident from steadily rising per capita bread consumption in Indonesia (6.23% CAGR in 2010-2015) vs. flat rice consumption during the same period.

Superior growth driven by robust expansion and lower return

We forecast ROTI's earnings to double over the next three years (23% CAGR in FY15-18F) on the back of its strong, albeit moderating, revenue growth of 20% vs. 29% CAGR achieved in the past five years. The strong growth prospect should be supported by the company's vigorous capacity expansions, rising promotion and improving distribution coverage, in addition to population lifestyle changes towards consumption of branded goods in Indonesia. We expect ROTI to sustain its high gross margin of 53% given low commodity (flour wheat) prices and improving sales returns in line with the plan to shift distribution mix towards the more general trade channel from 25% to 40% by 2020 (modern trade: from 75% to 60%). The company's strong relationship with the Indofood group, which is the dominant player in the flour mill industry in Indonesia, should also support its growth prospect, in our view.

Valuation and risks

Our DCF-derived target price of Rp 1,650 (assuming a 11.6% WACC, 5% terminal growth) implies target FY17F multiples of 22x P/E and 11x EV/EBITDA, which are still well below the valuation of large-cap consumer peers in Indonesia. Since its listing in June 2010, ROTI has traded at trailing P/E of 34x on average, more than double that of the JCI Index (14.9x on average since June 2010) and 36.5% premium to its consumer peers in JAKCONS (average at 23.2x). The stock is currently trading 2 std below its mean multiples, thus providing a good entry point. We are bullish on ROTI's outlook given its consistency in delivering strong earnings growth in the past five years (22% CAGR). Some key risk factors to our earnings forecasts and equity valuation include Indonesia's macroeconomic condition, rising competition in bread industries, weakening currency, rising material cost/commodity price and rising cost of capital in the country.

Leading bread producers in Indonesia

Leader in Fragmented Bread Industry in Indonesia

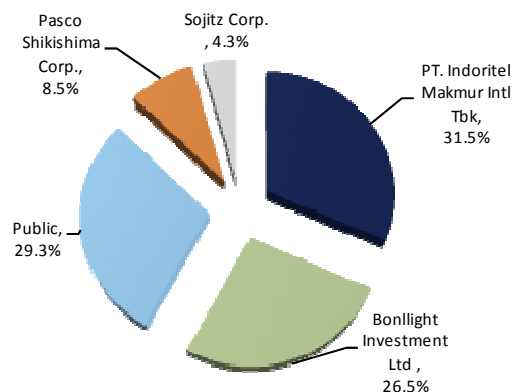
Indonesia's bread industry is considered fragmented market. It is categorized into three main segments, namely home/small industry, mass production and boutique bakery. In the home/small industry, there are estimated of 5,000 players with distribution coverage of 5-20km. It comprises of 68% from the total industry value. Meanwhile, mass production, which comprises 20% of total value, is dominated by few enterprises with wider distribution coverage of 200-300km; while the remaining 12% are in the format of boutique/artisanal bakeries. Boutique/artisanal bakeries are usually dominated by many franchised players which specialized in high quality bread, pastries and cakes at higher price point with different target market. Some examples of boutique bakeries are including Bread Talk, Tous Les Jours, and Paul Patisseries.

We believe PT Nippon Indosari (ROTI) is well-positioned to maintain its leadership as some consumers have started to shift toward mass-produced and boutique bakeries from home/small industry due to health issue as home/small industry's products are considered to be less hygienic. Moreover, we view home/small industry, even with similar price point, will struggle due to raw material price fluctuation, limited production capacity and lacking economic of scale. Overall, we view that consumers tend to be confident about the quality of packaged baked goods which makes packaged bread continued to fare better than unpackaged bread. As evidence, the growth of packaged bread has been higher compared to unpackaged bread (6.8% CAGR vs. 5% CAGR in 2010-2015) and the situation is expected to remain the same in the next 5 years (5.7% CAGR vs. 3.8% CAGR in 2015-2020F). Differ from Vietnam's bakery scene, where unpackaged breads are on average 7.6x reported higher sales compared to packaged bread during 2010-2015.

Started in 1996, ROTI plays an important role as the first and largest mass bread producer in Indonesia. Since it went public in 2010, the company has ramped up its production capacity to meet the rising bakery demand in Indonesia. With its famous tagline "Roti-nya Indonesia", Sari Roti has become one of Indonesia's most successful and recognizable household brands in Indonesia. The company has variety of products including white bread, sweet bread, Sari Cake, and newly launched products such as: Mini Bun and Dorayaki to capture higher target market. Back in 2010, the company only operated 3 factories but managed to add 7 more facilities during 2011-2014. The 10 factories are located in Java, Sumatera and Sulawesi with capacity up to 4mn per day. We view company's robust expansion supports ROTI strong revenue growth of 29% CAGR in 2010-2015 with a compelling average ROAE of 23% during the same period. We believe that the company's strong innovation, robust expansion and distribution capabilities have contributed to its success in achieving 90% of market leaderships in mass bread production in Indonesia.

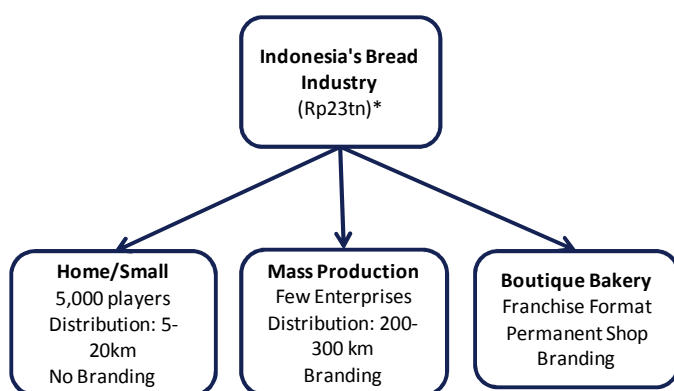
In addition, the company has also achieved various prestigious awards including the best brand award by Top Brand. In 2015, Sari Roti positioned itself at the forefront with a total index of 74%, followed by Bread Talk with 2.8% and Holland Bakery with 2.4%. Despite weak economic conditions in 2015, the company has once again awarded Best of the Best Award by Forbes Indonesia for three consecutive years for three consecutive years, where the evaluation criteria is based on ROE, sales growth, EPS and company's consistency in the past couple of years. ROTI has delivered outstanding performance and consistency in grabbing the market share. We also view ROTI is well-positioned in bright outlook of Indonesia's baked goods.

Fig. 7: ROTI's Shareholder Structure as of 2015



Source: Company

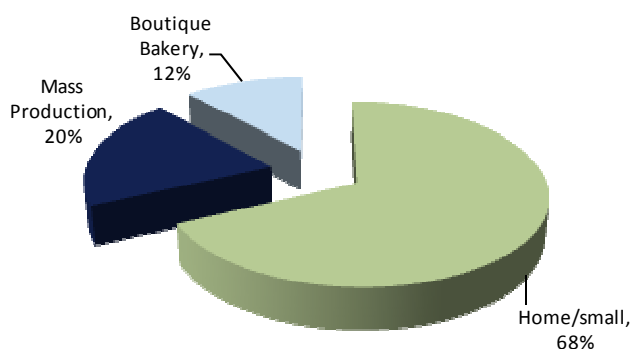
Fig. 8: Three segments of Indonesia's Bread Industry



Source: Company

*)APEBI Oct 24, 2014

Fig. 9: Indonesia's Bread Industry Segmentation in 2014



Source: Company, APEBI

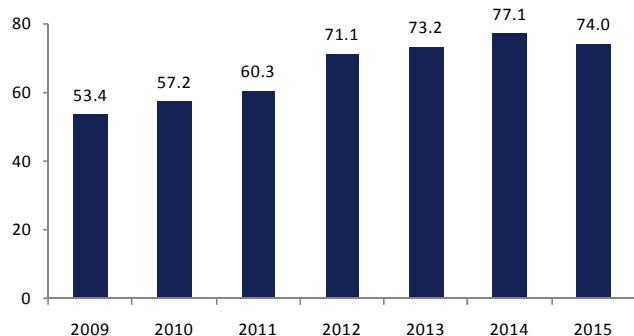
Competition Tightens Up but Still Remains Undeclared

The bright prospect of Indonesia's bakery industry has attracted many players, either local or foreign, to enter the market. For instance, Yamazaki Bakery has entered into mass produced bread market through its JV with Alfamart back in 2013. Although, the product variety and pricing are pretty similar to ROTI's, we view that ROTI has established brand loyalty and equity one step ahead of Yamazaki. We also believe ROTI has limited threat from artisanal bakeries as large industrial producers have the advantage of producing in bulk. In terms of pricing, the unit price of packaged bread is often lower than unpackaged products, as artisanal baked goods tend to be offered at higher price points. Another advantage is that ROTI as a mass bakery producer have more power in building brand awareness given the wider and stronger distribution capability. Therefore, we believe any new entrants should find it challenging to adjust to Indonesia's fragmented bakery market and imitate ROTI's success story.

Supported by its strong track record, production capability and vast distribution network, ROTI has positioned itself as the dominant domestic bread producers in Indonesia. ROTI's market value has gradually increasing from 6.9% in 2011, 9% in 2012, 10% in 2013 and 11% in 2014 as a result of company's robust expansion and vigorous A&P spending. As evidence, ROTI's A&P spending soared for almost 85% to Rp94bn in 2012 from Rp50.8bn in 2011. However, the A&P spending has slowed down to 6.2% of total sales in 2013 and further improving to 4.5% of sales in 2015. We expect during the period, the company have established strong brand loyalty and awareness so that new entrants will have difficulties in grabbing ROTI's market share.

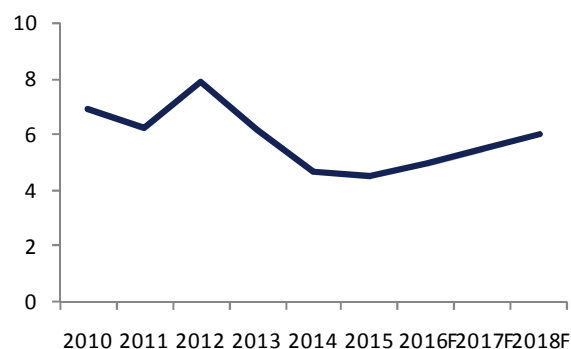
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Fig. 10: Always leading as the Top Brand Award



Source: Top Brand Award

Fig.11: Less Aggressive A&P expense after 2012 (% of sales)



Source: Company, indo Premier Forecast

Fig. 12: Price Comparison

Type	Price (Rp)	
	Sari Roti	Mr. Bread
White Bread	11,500	11,000
Wheat Bread	16,000	12,000
Sweet Bread	5,500	5,000

Source: Indomaret as of January 2016

Exposure to Lucrative Indonesia's bread market

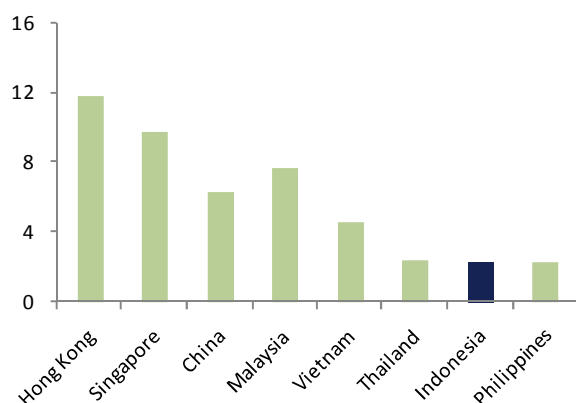
Bright prospects for Indonesia's bakery market

Over the past three years, the Indonesia's bakery industry has grown by 13.5% CAGR. According to Euromonitor, the value of bakery industry is estimated to reach Rp5.9tn in 2015 (+11.6%yoy) and Rp6.2tn in 2016. In spite of the growth, Indonesia's bread consumption per capita is relatively low, of only 2.3kg per annum. It is considerably far below its neighbouring countries such as Thailand, Malaysia, Singapore and Hong Kong with 2.4kg, 7.6kg, 9.7kg and 11.8kg per annum, respectively.

In terms of bread consumption per capita, in 2015 Indonesia reported lowest figure of only US\$8.6 per annum which was also well below its ASEAN peers. As comparison, Hong Kong per capita spending stands at US\$69.2, Singapore at US\$51.7, Malaysia at US\$17.3, and Thailand at US\$11.4 per year. We see this low penetration holds ample room for growth opportunity as income levels continue to rise and Indonesians become more upwardly mobile thus requires quicker and more convenient way to eat such as bread and instant noodle. In addition, unlike cakes and pasties, which tend to be bought only occasionally, purchases of bread are more frequent as it used as a substitute for rice during breakfast or snacks during break time. As a result, rice consumption per capita growth (5-year CAGR: -0.2%) fell behind bread consumption per capita growth of 6.23% CAGR during 2010-2015. At the same time, we view ROTI still has limited exposure to the eastern part of Indonesia, which offers another potential target market to support its robust growth once they tapped into the market.

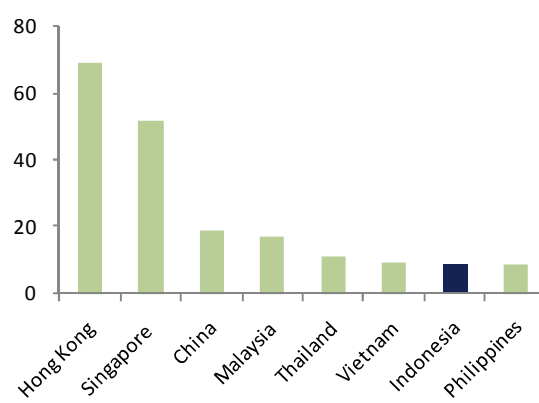
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Fig. 13: Low baked goods consumption per capita (kg/yr)



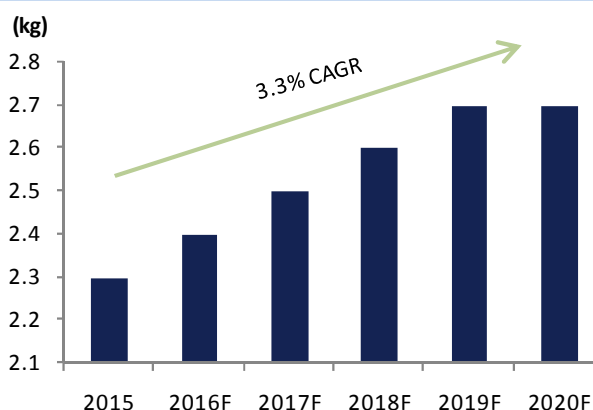
Source: Euromonitor

Fig. 14: Low baked goods consumption per capita (US\$/yr)



Source: Euromonitor

Fig. 15: Rising Indonesia's Baked Goods Consumption (US\$ per capita)



Source: Euromonitor

Benefiting from rising middle income populations and a change in lifestyle

We view Indonesia as a lucrative market for bread industry due to rising middle class, supportive demographics and rising disposable income. The urban population is estimated at 138mn people and is expected to continue growing given Indonesia's large young population and a sustained trend of urbanization. Furthermore, according to McKinsey Research, as many as 90 million Indonesians are estimated to join the consuming class by 2030 with substantial amount of disposable income to spend. By 2030, it is projected that Indonesia's consuming middle class to be tripled to 135mn to become the world's largest middle class after China and India.

Urban Indonesians spend about 31.5% of their food expenditure on prepared F&B vs. rural's 18.2%. This number has been increasing in recent years and trending towards that of high urban population countries, where urban people typically have hectic lifestyles and prefer a quick meal that requires minimal cooking. We therefore believe that the changing lifestyles of consumers are positive for F&B companies such as ROTI.

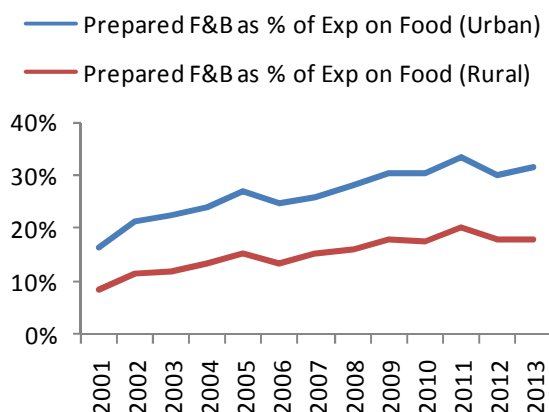
As the number of female civil servants grew by 2.8% CAGR over FY05-15 (vs. 1.9% CAGR of male counterparts), we view packaged breads will also be benefited from growing number of working women who have less time to cook thus they prefer simpler and more practical food such as bread and instant noodle as the substitute for themselves or other members of the family for the married women.

In terms of age structure, Indonesia has a large young population with 66.5% of the total population are within the productive age (15-64 years old). We view this will further support potential growth in consumption of prepared F&B. In addition, the growing number of young working-class has started adjusted to new lifestyle ("urban lifestyle") to seek quick and more convenient meals such as bread and cereals. According to an estimate of Indonesia Bakery Association, bread/cakes consumption surged nearly 60% during 2010-2014. In fact, consumption of wheat in Indonesia has also doubled since 2002. Over the past decade, Indonesia's wheat imports surged 63% to a record 7.7 million metric tons in 2015, while consumption jumped 70% far outpacing a 8% gain in rice demand, U.S. Department of

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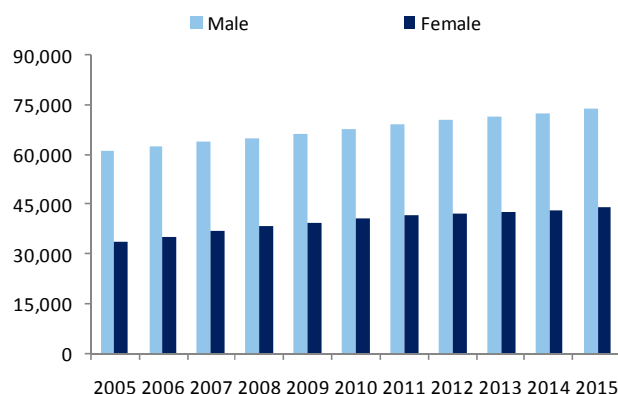
Agriculture data show. In 2016, the wheat import is estimated to continue rising to 8.1 million tons. Thus, we view this will be positive on ROTI's growth going forward given its strong brand equity.

Fig. 16: Urban spends more than rural



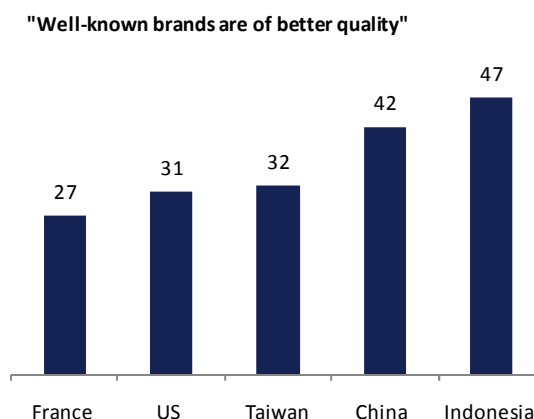
Source: CEIC, Indo Premier

Fig. 17: Growing number of female workers (people)



Source: ILO

Fig. 18: Indonesia consumers place strong faith in brands



Source: McKinsey Chinese consumer studies, 2011; McKinsey Consumer and Shopper Insights Indonesia study, 2011

Supported by nationwide distribution

In order to penetrate Indonesia mass market, one needs scale and extensive distribution networks. The cost of serving consumers is high due to Indonesia's dispersed geography and population, poor infrastructure, and fragmented retail landscape. According to data from Euro monitor (2010), Indonesia's grocery retail sales points of about 2mn are the third most fragmented after India (12.3m) and China (3.7m). Traditional trade accounts for 85.2% of total grocery retail value attained in 2012 vs. 14.8% collected from modern trade, based on Bain & Co research, and it is expected traditional trade to remain dominant over next the 15 years.

ROTI's distribution is considerably vast and highly efficient. The distribution is usually completed within 24 hours as bakery products are having short shelf lives (less than 7 days). As of August 2015, ROTI has covered 59,295 points of sales throughout the nation. ROTI's distribution channel is still dominated with modern trade channel which accounts for 75% from the total points of sale, while general trade only accounts for 25%. ROTI's general trade sales are also underpinned by the number of tricycles vendors who ply their trade in residential areas across Indonesia. As of Dec 2014, there are 3,741 active tricycles, a 4.4% increase from the previous year.

Although, the rapid expansion of modern trade has brought positive impact on ROTI's distribution as it provides high product visibility and availability throughout Indonesia. Going forward, the company plans to shift toward general trade channel to lower sales return, better

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receivable, and ensuring deeper and more direct product penetration for consumers who do not live in big cities.

Fig.19 : Points of sale as of 2015

Points of Sale	Dec-11	Dec-12	Dec-13	Dec-14
Minimarts	11,897	14,563	18,542	20,911
Supermarkets	583	667	797	815
Tricycles	2,470	3,070	3,582	3,741
Warung	14,676	19,639	26,819	30,028
Institutions	48	56	136	511
Total	29,674	37,995	49,876	56,006

Source: Company

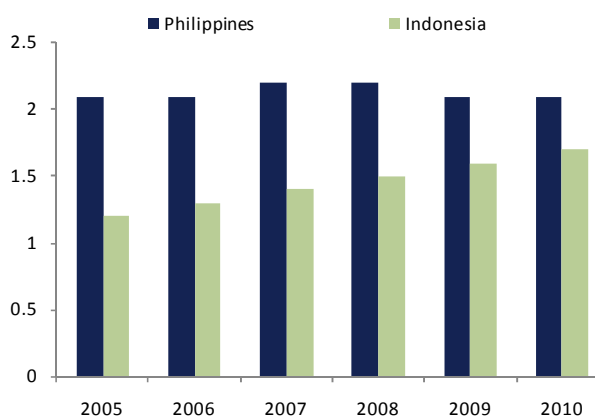
Overseas Expansion

ROTI recently announced its new partnership with Philippine-based food producer and distributor, Monde Nissin Corp (MNC). ROTI injected US\$6.87mn (~Rp90bn) to the joint venture, taking a 55% stake in the enterprise, while MNC contributed the remaining 45% stake. We view MNC to be the suitable partner for ROTI as MNC has over 35 years of presence in the country which allowed it to establish a following among consumers. The bakery industry in Philippines is considered as a very competitive landscape. However MNC has successfully attained 33% value share in Philippines, supported by the company's continuous innovation, differentiated products and wide brand portfolio.

Similar to Indonesia demographic profile, Philippine has a large population of more than 100mn people as of February 2016 and it is characterized by a rapidly expanding middle class segment which constitute a powerful consumer force. In addition, the busy lifestyle of urban dwellers in Philippines assist the growth of baked goods as they switch from rice to bread or pastries for breakfast.

Historically, during 2005-2010, Philippines bread consumption per capita by unit is on average 50% higher compared to Indonesia. In addition, Philippines baked goods spending per capita is estimated at US\$9.1 in 2015 (vs. Indonesia at US\$8.6). Therefore, we view Philippines provides another venue which will support ROTI's robust growth going forward.

Fig. 20: Indonesia vs Philippines Baked Goods Consumption (kg per capita)



Source: Euromonitor 2011

Earnings forecast and assumptions

We forecast ROTI's net profit to rise to Rp338bn in 2016F (+25% yoy), driven by stable margin gross margin at level 53% due to lower commodity price (i.e. wheat price dropped by 23.5% yoy in 2015).

We forecast ROTI's net profit to rise to Rp387bn in 2017F (+14% yoy) and Rp498bn in 2018F (+28% yoy). At the operating level, we forecast ROTI's EBITDA margin to slightly improve to 24.7% from 24.3% in 2015. We expect that operating profit will grow at 16.5% and 19.8% during 2016F and 2017F, respectively, on the back of ROTI's strong revenue growth of 18.7% and 19.8%, respectively, with white bread and sweet bread still become the main revenue contributor.

Fig. 21 : Summary of Our Earnings Forecasts

(Rp bn)	2014	2015F	2016F	2017F	2018F
Revenue	1,880	2,175	2,582	3,093	3,741
Gross Profit	901	1,155	1,368	1,639	1,983
EBITDA	359	528	638	759	928
Operating Profit	263	416	484	580	720
Pre-Tax Profit	257	378	489	579	741
Net Profit	192	271	338	387	499
Ratios (%)					
Gross Margin	47.9	53.1	53.0	53.0	53.0
EBITDA Margin	19.1	24.3	24.7	24.6	24.8
Net Margin	10.2	12.4	13.1	12.5	13.3

Source: IndoPremier Forecasts

Our key earnings forecast assumptions are stated below and in the following table:

- **Revenue.** We assume white bread and sweet bread will still be the main driver. We forecast the revenue to grow at 19.8% CAGR during 2015-2018F (vs. 28.9% CAGR during 2009-2015). We expect the revenue will increase to Rp2.6tn (+18.8% yoy) in 2016F which mainly comes from volume growth as the company will continue rapid expansion to maintain its position and ASP hike of 5%. We view pricing will be less likely to become an issue as historically, ROTI has been able to pass on its raw material price increase by ASP hike.
- **COGS.** We assume cost of direct materials to stay at 47% of sales in 2016F, due to lower cost of raw material (wheat and oil-based products). We expect the material cost to be maintained at 31% of total sales in 2016F and 2017F. Direct labor cost is assumed to be relatively stable at 6% of sales during 2016F-2017F, while manufacturing overhead should slightly decline to 10% of sales during 2016F-2017F from 11% in 2015.
- **Opex.** We assume selling expense to stay at 34.2% of sales in 2016F and 2017F before improving to 33.7% in 2018F. We see A&P spending is crucial to increase brand awareness and maintain its market leader. We assume the A&P expense will be a little higher at 5% of total sales in 2016F and gradually increases to 5.5% in 2017F, while the G&A expense is assumed to be maintained at 9% in 2016F before improving to 8% in 2017F.

Fig. 22: Our Key Earnings Forecast Assumptions

	2014	2015F	2016F	2017F	2018F
Revenue Growth (%yoy)					
- White Bread	110.0	24.2	28.0	28.0	28.0
- Sweet Bread	(15.1)	(0.6)	5.0	5.0	8.0
- Sales return	32.3	6.4	18.2	19.2	26.3
Revenue	24.9	15.6	18.7	19.8	21.0
COGS (% of sales)					
- Direct Material	34.0	29.8	31.0	31.0	31.0
- Direct Labor	6.4	5.7	6.0	6.0	5.0
- Manuf. Overhead	11.6	11.4	10.0	10.0	11.0
Total	52.0	46.9	47.0	47.0	47.0
Gross Margin	47.9	53.1	53.0	53.0	53.0
Operating Cost (% sales)					
- G&A Expenses	8.3	9.0	9.0	8.0	8.0
- Selling Expenses	25.7	25.0	26.0	26.5	26.0
Total	34.0	34.0	35.0	34.5	34.0

Source: Indo Premier Forecasts

Sensitivity Analysis

We performed a sensitivity analysis on our FY16 net profit forecasts to changes in our revenue, cost of goods sold, gross margin and operating cost assumptions. We found ROTI's earnings to be most sensitive to assumptions on gross profit margins, with each one percentage point lower margins versus our assumptions leading to a reduction in our FY16F earnings forecasts by 0.3%. Similarly, for every 1% higher raw material costs than our assumption, our earnings forecasts are impacted by 0.1%. For operating costs, each 1% higher selling expenses have more significant impact on earnings (-0.2%) than G&A expenses (-0.1%). Meanwhile, the impact on earnings from 1% lower revenues than our assumption is more significant for the white bread sales (-0.2%) and sweet bread sales (-0.1%) and improvement of 1% in sales return will increase the net profit by 0.04%.

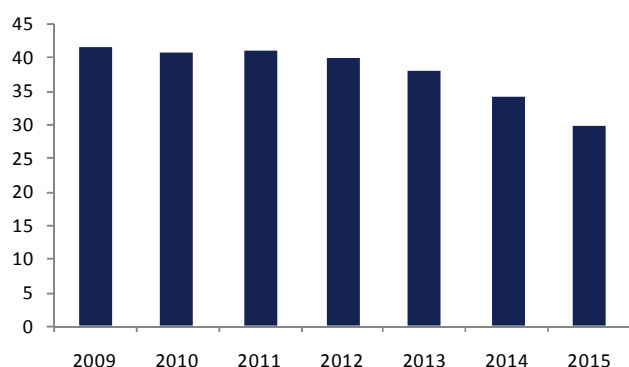
Fig. 23: Earnings Sensitivity Analysis

	Impact on FY16F Net Profit
Revenues	
- White Bread -1%	-0.2%
- Sweet Bread -1%	-0.1%
- Sales return +1%	-0.04%
Cost of Goods Sold	
- Direct Materials +1%	-0.1%
- Direct labor +1%	-0.05%
Gross Margin	
- Gross Margin -1%	-0.3%
Operating Cost	
- G&A Expenses +1%	-0.1%
- Selling Expenses +1%	-0.2%

Source: Indo Premier Forecasts

ROTI Initiating Coverage

Fig. 24: Downward trend of Raw Material (% of sales)...



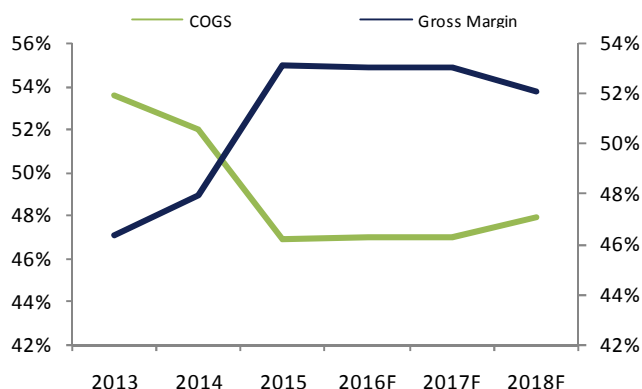
Source: Company, Indo Premier Estimates

Fig. 25: ...due to downtrend in Wheat Price



Source: Bloomberg

Fig. 26: Gross Margin will be stable as COGS stabilizes (% of sales)



Source: Company, Indo Premier Estimates

Valuation, TP Rp1,650

We initiate coverage on ROTI with a BUY rating and target price of Rp1,650. We derive our target price based on DCF valuation with explicit free cash flow forecasts for 2016-2025F, taking into account capex spending, and a terminal value, with the following assumptions: 5% terminal growth rate and 11.5% WACC based on a risk-free rate of 8%, an equity risk premium of 5%, and an asset beta of 0.8 (reflecting low earnings volatility of consumer products' companies in Indonesia). We assume a tax shield of 25% on cost of debt to reflect the company's marginal corporate tax rate.

A summary of our DCF analysis is shown in Fig. 27. The net present value (NPV) of our free cash flow forecasts in the next ten years represents 36.7 % of our Enterprise Value estimate for the company, with the NPV of Terminal Value contributing the remaining 63.3%. Based on our forecast for ROTI's net debt level as of 31 December 2016, we arrive at our DCF-derived fair equity value estimate of around Rp8.3tn for the company. The target price implies FY17F of 22x and FY17F EV/EBITDA of 11x. The valuation is fairly low compared to other FMCG companies such as UNVR (35x P/E 16F based on our estimate). However, we like ROTI better because it is well-positioned in Indonesia's high growing bakery market and possesses a more robust growth outlook, especially with the currently low bread consumption per capita and burgeoning middle income population. We view the current valuation at 1 stdev below its mean provides a good entry point. Since its listing in June 2010, ROTI has traded at 34x PE on average, more than double that of the JCI Index (14.9x on average since June 2010) and at almost a 36.5% premium to its consumer peers in JAKCONS (average at 23.2x). In addition, we view ROTI's lack of presence in eastern part of Indonesia holds another growth opportunity.

ROTI Initiating Coverage

Fig. 27: DCF Valuation Summary

(Rp bn)	2016F	2017F	2018F	2019F	2020F	2021F	2022F	2023F	2024F	2025F
Free Cash Flow										
EBIT	484	580	720	852	995	1,220	1,108	1,269	1,342	1,457
Plus: Depr. & Amort.	149	173	201	238	275	307	338	369	399	428
EBITDA	633	753	921	1,090	1,270	1,526	1,446	1,638	1,741	1,885
Less: Tax Payable	(121)	(145)	(180)	(213)	(249)	(305)	(277)	(317)	(336)	(364)
Plus: Changes in W/C	(80)	(44)	(25)	(28)	18	(12)	(3)	(24)	24	(15)
Less: Capex	(390)	(438)	(586)	(584)	(531)	(528)	(526)	(524)	(521)	(520)
Free Cash Flow	42	126	130	266	508	681	640	773	909	986
Terminal Value										
Terminal Growth	5.0%									
Terminal WACC	11.5%									
Terminal FCF	1,045									
NPV of TV	15,896									
NPV of TV	5,315									
DCF Valuation										
NPV of Forecasts	3,085									
NPV of TV	5,315									
Enterprise Value	8,399									
Less: Net Debt	(56)									
Equity Value	8,343									

Source: Indo Premier Forecasts

Fig. 28: P/E Comparison

Company	B'berg	Country	Mkt Cap (US\$ mn)	P/E (x)		EV/EBITDA (x)		ROE (%)	ROAA (%)
	Code			FY15F	FY16F	FY15F	FY16F	FY14	FY14
Unilever Indonesia	UNVR IJ	Indonesia	25,041.8	54.4	48.8	38.9	34.9	129.6	42.5
Kalbe Farma	KLBF IJ	Indonesia	5,167.3	30.2	26.8	19.7	17.4	23.6	17.4
Indofood CBP	INDF IJ	Indonesia	4,822.2	19.0	14.9	10.1	8.9	16.0	4.8
Indofood SM	ICBP IJ	Indonesia	6,792.9	27.9	25.0	18.8	16.5	19.5	11.3
Mayora Indah	MYOR IJ	Indonesia	2,139.8	23.1	21.7	12.8	11.5	10.3	4.0
President Bakery PCL	PB:TB	Thailand	668.5	16.6	17.0	10.7	10.9	24.0	18.5
S&P Syndicate PCL	SNP:TB	Thailand	397.4	22.8	22.6	13.9	12.3	22.4	13.9
Grupo Bimbo	BIMBOA:MM	Mexico	13,806.2	35.2	27.3	13.7	12.2	7.3	2.3
Panera Bread Co	PNRA:US	USA	4,710.1	31.3	26.4	12.9	11.5	24.2	10.4
Average				28.9	25.6	16.8	15.1	30.8	13.9

Source: Bloomberg

Closing price and foreign exchange rate as of April 1, 2016

UNVR (UNVR IJ; Rp43,175 ; HOLD), KLBF (KLBF IJ; Rp1,450 ;BUY), ICBP (ICBP IJ; Rp15,325; BUY), INDF (INDF;Rp7,225; HOLD) are Indo Premier forecasts, MYOR (MYOR IJ;Rp31,475; Not Rated), President Bakery (PB TB;THB 52.25; Not Rated),S&P Syndicate (SNP TB; THB 28.50; Not Rated), Grupo Bimbo (BIMBOA MM;MXN 51.1; Not Rated), Panera Bread (PNRA US;USD 204.83; Not Rated) are Bloomberg forecasts.

ROTI Initiating Coverage

Fig. 29: Superior to JCI and JAKCONS Index



Source: Bloomberg

Fig. 30: P/E band



Source: Bloomberg

Fig. 31: Sari Roti's Products



Source: Indomaret

Fig. 32: Mr. Bread's Products



Source: Indomaret

Risk to our investment case

1. Fluctuations in the US\$/IDR exchange rate and raw material prices may have negative impact for ROTI.
2. Exposed to macroeconomic risks including economic slowdown, higher than expected inflation, lower purchasing power.
3. Rising material cost/commodity price especially wheat price
4. Tightening competition in bread industries

ROTI Initiating Coverage

Year To 31 Dec (RpBn)	2014A	2015A	2016F	2017F	2018F
Income Statement					
Net Revenue	1,880	2,175	2,582	3,093	3,741
Cost of Sales	(979)	(1,020)	(1,214)	(1,454)	(1,758)
Gross Profit	901	1,155	1,368	1,639	1,983
SG&A Expenses	(639)	(739)	(884)	(1,059)	(1,263)
Operating Profit	263	416	484	580	720
Net Interest	(46)	(75)	(36)	(69)	(59)
Forex Gain (Loss)	4	0	0	0	0
Others-Net	36	39	28	34	41
Pre-Tax Income	257	379	477	545	702
Income Tax	(64)	(108)	(138)	(158)	(204)
Minorities	0	0	0	0	0
Net Income	193	271	338	387	499
Balance Sheet					
Cash & Equivalent	163	516	184	130	139
Receivable	213	251	299	358	432
Inventory	41	43	53	64	77
Other Current Assets	4	4	0	0	0
Total Current Assets	420	814	536	551	648
Fixed Assets - Net	1,680	1,821	2,062	2,327	2,712
Goodwill	0	0	0	0	0
Non Current Assets	36	64	77	62	75
Total Assets	2,136	2,699	2,676	2,940	3,435
ST Loans	48	0	0	155	19
Payable	126	160	0	227	275
Other Payables	134	236	184	176	197
Current Portion of LT Loans	0	0	0	0	0
Total Current Liab.	308	396	374	558	490
Long Term Loans	291	0	258	155	187
Other LT Liab.	584	1,122	565	410	495
Total Liabilities	1,183	1,518	1,197	1,123	1,172
Equity	274	274	274	274	274
Retained Earnings	686	915	1,213	1,553	1,999
Minority Interest	0	0	0	0	0
Total SHE + Minority Int.	960	1,189	1,487	1,827	2,274
Total Liabilities & Equity	2,143	2,707	2,684	2,950	3,445

Source: ROTI, IndoPremier

ROTI Initiating Coverage

Year to 31 Dec	2014A	2015A	2016F	2017F	2018F
Cash Flow					
Net Income (Excl.Extraordinary&Min.Int)	193	271	338	387	499
Depr. & Amortization	93	107	149	173	201
Changes in Working Capital	(96)	76	(65)	(42)	(24)
Others	78	153	21	92	92
Cash Flow From Operating	267	608	443	611	767
Capital Expenditure	(353)	(277)	(403)	(423)	(599)
Others	1	15	16	16	18
Cash Flow From Investing	(352)	(262)	(387)	(406)	(581)
Loans	178	(339)	258	51	(103)
Equity	0	0	0	0	0
Dividends	(16)	(28)	(27)	(34)	(39)
Others	(44)	409	(606)	(260)	(21)
Cash Flow From Financing	119	42	(375)	(243)	(163)
Changes in Cash	34	388	(319)	(38)	22
Financial Ratios					
Gross Margin (%)	47.9	53.1	53.0	53.0	53.0
Operating Margin (%)	14.0	19.1	18.8	18.8	19.3
Pre-Tax Margin (%)	13.7	17.4	18.5	17.6	18.8
Net Margin (%)	10.3	12.5	13.1	12.5	13.3
ROA (%)	9.7	11.2	12.6	13.8	15.6
ROE (%)	22.1	25.3	25.3	23.4	24.3
ROIC (%)	16.9	23.0	22.2	20.0	22.4
Acct. Receivables TO (days)	38.4	38.8	38.6	38.5	38.4
Acct. Receivables - Other TO (days)	0.0	0.2	0.3	0.2	0.2
Inventory TO (days)	25.3	24.3	25.2	24.9	25.0
Payable TO (days)	53.1	51.1	52.5	52.3	52.1
Acct. Payables - Other TO (days)	34.8	36.8	33.4	19.8	16.7
Debt to Equity (%)	35.3	0.0	17.4	16.9	9.1
Interest Coverage Ratio (x)	0.2	0.2	0.1	0.1	0.1
Net Gearing (%)	18.4	(43.4)	5.0	9.8	3.0

Source: ROTI, IndoPremier

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INVESTMENT RATINGS

BUY : Expected total return of 10% or more within a 12-month period
HOLD : Expected total return between -10% and 10% within a 12-month period
SELL : Expected total return of -10% or worse within a 12-month period

ANALYSTS CERTIFICATION.

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