INDOPREMIER

Premier Insight

17 November 2017

Economic Update

7DRRR & Key takeaway from BI's investors discussion: A confident decision

- **BI decided to maintain the 4.25% rate after a good set of outcomes.**
- **...which came on top of better economic management & performance.**
- **Some foreign developments support decision tonight and going forward.**
- **Indonesian bond market remains interesting from investors perspective.**

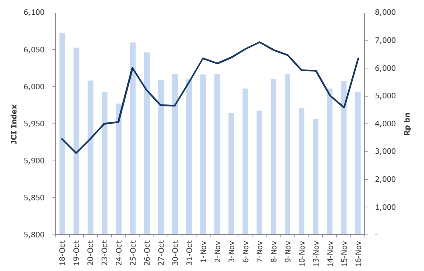
Rate held at 4.25%. We believe BI's decision to hold the reference rate at 4.25% and the maintenance of lending and deposit facility rates, each at 5% and 3.5%, was expected and much anticipated given variables under BI's surveillance have all shown positive outcomes. *First*, there was low domestic inflation at with 3.6% yoy rate by Oct17 and 3.1% core inflation (BI expects inflation to be 3-3.5% FY17). *Second*, USD/IDR exchange rate, which despite recent USD appreciation, remains within the expectation ban and supported by ample foreign reserves (US$126.5bn). *Third*, improvement in the CAD (-1.65% of GDP in 3Q17) and capital & financial account, which grew on both FDI and portfolio investments and with FDI substantially larger than the portfolio investments, had sufficiently minimised the impact of capital reversal that took place in part of the 3Q.

Continued economic recovery. The decision should came with confidence especially as some other recent developments such as the investment-supported economic growth along with better budget management as well as foreign catalysts had given good reviews of the overall performance this year. In the financing, the fiscal authority has managed to improve both revenue and expenditure from last year (71% and 72% of target, respectively by Oct17), keeping deficit safe at the 2.2% of GDP at time where it has also stored up to Rp72tn for 2018's cash management. From our last meeting with the Ministry of Finance (MoF), the minister seems to emphasise 2018's budget on the credibility theme, implying responsible (or quality) expenditures will be central in next year's budget execution which will attempt to provide more social assistance – we expect this should translate to better household consumption next year. The external catalysts include global economic recovery as seen in developed economies such as the United States, Japan, and China, which should uphold Indonesia's external balance position that has already been in positive territory.

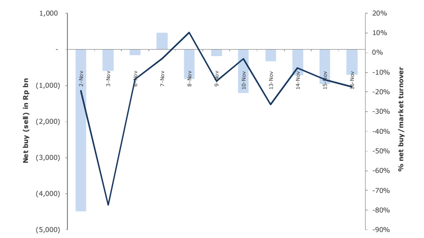
Foreign market developments. On top of the domestic ones, foreign market developments also support the decision. There is currently more than 90% expectation looking for the third-time Federal Funds Rate increase to come this Dec17. The Federal Reserve will also see the appointment of Jerome Powell for chairman next year, which is expected to stay course with normalisation and tightening plan brought by current chair Jannet Yellen. Akin with that, the ECB also plans to halve the amount of bond-buying to EU€30bn starting next year until Sep18, which should reduce liquidity to global market including emerging ones, although leaving the timeline for its quantitative easing program open ended. Also recently, the Bank of England rose its rate for the first time in a decade, embarking on its gradual tightening process. We believe these considerations and the global recovery, which serve as substantial issues that underline them, play, for the major part, important factors in BI's decision; not only in this meeting, but also quite potentially throughout 2018.

Investors' appetite on Indonesian sovereign bond market. With the above factors in mind, we think there remains high interest in Indonesian market implied from investors inquiries and as shown by data. Foreign ownership now stands ~39% of total sovereign bonds with capital inflow recorded Rp145tn ytd (already +35% higher than 2016's full year position). This year, every bond auction week sees approximately 2.4x bid-to-offer ratio, in comparison to last year's 1.9x. Due to this higher interest and absorption, the government intends to cut down 2/3 remaining auctions this year – by the 1W of Nov17 it had satisfied 99% of its target. Indonesian bond market should remain an interesting investors destination, in our view, notably in the face of regional competition among countries with BBB rating, and that the new set of development would still invite more funds despite potential actions from global market participants.

JCI Index



Foreign net buy (sell)



Key Indexes

Index	Closing	1 day	1 year	YTD
JCI	6,038	1.1%	16.3%	14.0%
LQ45	1,007	1.6%	15.7%	13.9%
DJI	23,458	0.8%	24.1%	18.7%
SET	1,691	0.1%	14.8%	9.6%
HSI	29,019	0.6%	30.3%	31.9%
NKY	22,351	1.5%	25.1%	18.8%
FTSE	7,387	0.2%	8.7%	3.4%
FSSTI	3,369	-0.9%	19.7%	16.0%
EIDO	27	1.9%	12.9%	11.6%

Commodity price

Commodities	Last price	Ret 1 day	Ret 1 year
(in USD)			
Oil/barrel (WTI)	55.1	-0.3%	21.0%
CPO/tonne	656.0	0.2%	-4.1%
Soy/bushel	9.4	-0.4%	-2.9%
Rubber/kg	1.6	-0.6%	-20.3%
Nickel/tonne	11,294	-2.9%	0.1%
Tins/tonne	19,432	0.1%	-3.1%
Copper/tonne	6,703	-0.5%	23.6%
Gold/try.oz (Spot)	1,279	0.0%	5.1%
Coal/tonne	96.8	-0.8%	-7.8%
Corn/bushel	3.1	1.3%	-3.1%
Wheat/bushel (usd)	421.5	0.4%	6.2%

Source : Bloomberg

Nippon Indosari (ROTI IJ; Hold)

The caveat on optimism

- **Revenue growth slows as consumer spending weakens.**
- **Expects flat GPM but lower OPM and NPM.**
- **Expansion is the leading indicator of sales growth catalyst.**
- **We lower our gross sales by 3%/12% in FY17/18F. HOLD reaffirmed.**

Waning revenue growth. We highlighted frail 3Q17 gross sales which grew at only 3% yoy (vs. avg5Y: 26%) and view this year sales volume will grow at 6% (vs. avg5Y: 26%) due to slowing household consumption on ROTI's targeted customer segment, a similar trend experienced by other consumer companies. The other issue is higher sales return (FY17F: 19% vs. avg5Y: 12%) triggered by spillover of the unprecedented 4Q16 boycott effect this year This results into decelerating net sales growth of only 1% in FY17F. Nevertheless, we expect normalization in sales return to 16%/14% level in FY18/19F. This brings our net sales forecast to Rp2,7tn in FY18F reviving from our FY17F low-base.

Margins diverge. The company benefits from low wheat price since early 2016 (wheat contributes about c.24% of its cost structure) on which we believe the gross margin will exhibit a slight improvement to around c.52% level in FY17F-FY19F (vs. FY16F: 51%). But, the company is facing two problems. First, high sales return increases defective inventory expense. Second, the expansion plan requires additional headcount which upsurges salaries expense. These two problems result to higher operating expense (FY17F: 42% vs. avg5Y: 33%). This brought lower operating and net income margins to 9.1% and 5.6% in FY17F, respectively.

The future story post rights issuance. Fresh capital injection raised from right issuance amounting to Rp1.4tn should enable deleveraging and expansion into new markets. Right issuance causes lower financial leverage ratio. Our visit noted that company tries to expand its presence in the ex-Java market to unleash sales growth catalyst by building additional 4-6 factories in Java/Sumatera/Kalimantan adding total production capacity about 60%-80% over the five-year time span on which the management expects this will bring effects on sales in the respective period.

Stay HOLD with lower TP of Rp1,200. Gross sales growth in the 3Q17 has shown an anemic growth vis-à-vis the past five-year trend. We thus trimmed our gross sales forecast by 3%/12%/18% for FY17/FY18/FY19 and slashed our TP to Rp1,200 (from Rp1,400) to account for our downgrade. Our TP reflects FY17F P/E of 45.8x. As a market leader in the national bread industry, we believe in ROTI's capability to capitalize ex-Java market potential despite concern on possible shrinking market pie due to the sluggish middle-income class consumption and increasing industry competition.

Year To 31 Dec	2015A	2016A	2017F	2018F	2019F
Revenue (RpBn)	2,209	2,522	2,496	2,783	3,154
EBITDA (RpBn)	557	478	366	441	478
EBITDA Growth (%)	56.6	(14.2)	(23.5)	20.5	8.3
Net Profit (RpBn)	306	282	140	240	281
EPS (Rp)	60	56	27	45	53
EPS Growth (%)	58.5	(7.7)	(51.7)	66.9	16.9
Net Gearing (%)	(43.4)	(42.3)	(66.8)	(65.0)	(30.9)
PER (x)	21.5	23.2	48.1	28.8	24.7
PBV (x)	5.5	4.5	2.3	2.2	2.0
Dividend Yield (%)	0.4	0.5	0.4	0.2	0.3
EV/EBITDA (x)	12.7	15.0	24.3	20.4	16.7

Source : ROTI, IndoPremier *Share Price Closing as of : 15-November-2017*

News & Analysis

Corporates

WIKA: Wijaya karya (WIKA IJ; Rp1,970; Buy) targets earnings growth of 27-30% and new contract growth of 24% in 2018. Company stated the delay in 9M17 financial statement was caused by issuance komodo bonds with ratings of AA which will take place within this year. On separate news, Bank Mandiri (BMRI IJ; Rp7,100; Buy) and Bank Tabungan Negara (BBTN IJ; Rp2,940; Hold) have lent Rp894bn to WIKA in order to help land acquisition of Serang – Panimbang project. (Investor Daily, Bisnis Indonesia).

Comment: WIKA's FY18 earnings estimate is inline with our estimates. Maintain BUY at Rp2,900/share. WIKA is currently trading at 14.3x PER FY17 on Bloomberg consensus.

KIJA: Kawasan Industri Jababeka (KIJA IJ; Rp306; Not Rated) through its subsidiary, Jababeka International B.V. (JIBV) will issue notes worth US$111mn for refinancing purposes. The notes will have 6.5% interest with maturity in 2023. The fund gained will be used for repayment of all outstanding balance from US$260mn old bonds, with 7.5% interest which will mature in 2019. (Bisnis Indonesia).

Markets & Sector

IPO: WIKA Gedung will strengthen its modular technology unit by developing new factory with Prime Modular (Joint Venture) in Cikampek, Karawang in addition to the current factory in Tambun, Bekasi. Modular construction is a pre-engineered building units that are delivered to site and assembled as large components of a building. The method is claimed to be able to save construction time by 40%. Its current factory in Tambun only has the capacity of 10 units per day, and only limited to bathroom construction. WIKA gedung targets new contract for modular construction of Rp100bn in 2018, and Rp200bn in 2019. (Investor daily & Kontan).

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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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