

12 March 2018

Basic Materials | Coal Mining

Coal Mining

Overweight (Maintained)

Domestic Power Plant Ceiling Coal Price Set

MEMR has issued a ministry decree that regulates the selling prices of coal with CV of 6,322kcal/kg GAR to domestic coal power plants. This sets the ceiling at USD70.00/tonne. To factor in the impact of the decree, we cut FY18F earnings for Adaro Energy by ~14%, Bukit Asam by ~7% and Harum Energy by ~14%. We think this decree only benefits the coal mining contractors, as the ministry now allows coal miners that comply with the decree to increase their original coal production plans by 10%. We also think the recent coal counters sell-off has been overdone, and maintain our OVERWEIGHT call on the on sector.

Stocks Covered: 3
Ratings (Buy/Neutral/Sell): 3 / 0 / 0
Last 12m Earnings Revision Trend: Positive

Top Picks

Adaro Energy (ADRO IJ) – BUY
Bukit Asam (PTBA) – BUY

Target Price

IDR2,800
IDR3,900

Coal price ceiling of USD70.00/tonne for domestic power plants. The Ministry of Energy and Mineral Resources (MEMR) has issued Ministry Decree No. 1395 K/30/MEM/2018. This regulates the selling price of coal with a calorific value (CV) of 6,322kcal/kg gross as received (GAR) to domestic coal power plants at USD70.00/tonne or based on the domestic thermal coal reference prices (HBA) – whichever is lower. The selling price of lower CV and quality of coal is adjusted proportionally, according to the CV of the coal. The ceiling coal price for domestic power plants is valid for 2018-2019, with maximum coal sales volume of 100m tonnes pa. At the end of 2019, the ceiling coal selling price and maximum quota is to be reviewed.

Allowing coal production to increase by ~10% from original coal production plans. MEMR also stated that coal companies, which have fulfilled the minimal domestic market obligation of 25% and ceiling coal selling prices for domestic coal-fired power plants, are allowed to increase coal production by 10% from their original approved production plans.

Coal mining contractors should be beneficiaries of the MEMR decree. The 10% higher coal production from coal mining companies' original approved production plans should be positive for the volume growth of the mining contractors. This includes United Tractor's (UNTR IJ, BUY, TP: IDR43,100) Pamapersada and Delta Dunia's (DOID IJ, BUY, TP: IDR1,300) Bukit Makmur.

Cutting FY18F earnings by between 7-14% due to the USD70.00/tonne ceiling price. We fine-tune our forecasts – to accommodate the ceiling coal price of USD70.00/tonne for domestic market obligations (DMOs) of 25% of total coal production – across all coal companies under our coverage. This results in FY18F earnings being cut by ~14%, ~7% and ~14% for Adaro Energy, Bukit Asam and Harum Energy respectively. This also results in FY19F earnings being cut for Adaro Energy (~7%), Bukit Asam (~5%) and Harum Energy (~12%).

Sell-off overdone, overhang should fade. We think the recent sell-off – due to the uncertainties over DMO coal ceiling prices – has been overdone. The share price overhang of local coal counters should fade, as the clarity over coal ceiling prices has been set by the MEMR decree.

OVERWEIGHT, with Adaro Energy and Bukit Asam as our Top Picks. We maintain our OVERWEIGHT call on the sector. We like Bukit Asam, as we think consensus has still not factored in its decent FY18 earnings growth. Post earnings adjustment for the ceiling coal prices, Bukit Asam is trading at a FY18F P/E of 6.7x on our FY18F EPS. This is undemanding, when considering its sizable FY18F ROE of 30.5%. We like Adaro Energy on the back of its strong cash flows and net cash position. We estimate that the firm is to increase its dividend payout to 40%, which should, in turn, result in a dividend yield of 4.7%. Key risks to our BUY calls include lower-than-expected coal prices, significant increases in oil prices, unfavourable government policies domestically, and unfavourable policies towards coal in China.

Company Name	Rating	Price	Target	% Upside (Downside)	P/E (x) Dec-18F	P/B (x) Dec-18F	Yield (%) Dec-18F
Adaro Energy	BUY	IDR2,170	IDR2,800	29.0	9.7	1.3	4.7
Bukit Asam	BUY	IDR2,890	IDR3,900	34.9	6.7	1.8	4.5
Harum Energy	BUY	IDR2,740	IDR3,300	20.4	9.3	1.4	-

Source: Company data, RHB

Analyst

Hariyanto Wijaya, CFA, CPA, CFTe, CMT
+6221 2970 7061

hariyanto.wijaya@rhbgroup.com



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Figure 1: Changes in earnings post the MEMR's ceiling coal price of USD70.00 per tonne using these assumptions – our FY18F base coal price assumption of USD90.00 per tonne, and all coal miners supplying 25% of their production to domestic coal-fired power plants

Company	FY18 earnings				Target price (IDR)			Revised TP implying FY18 P/E on our revised FY18 EPS
	Prior ceiling	Post ceiling	Changes	Consensus earnings	Prior ceiling	Post ceiling	Changes	
ADRO (USDm)	607	519	-14.5%	579	3,000	2,800	-6.7%	12.6
PTBA (IDRbn)	5,041	4,668	-7.4%	3,957	4,100	3,900	-4.9%	9.0
HRUM (USDm)	66	57	-14.0%	54	3,500	3,300	-5.7%	11.0

Source: RHB

12 March 2018

Basic Materials | Mining

Adaro Energy

Buy (Maintained)

Factoring In The Coal Price Ceiling's Impact

MEMR issued a ministry decree to regulate the selling prices of coal with CV of 6,322kcal/kg GAR to domestic coal power plants, by setting a ceiling of USD70.00/tonne. To factor in the impact of the MEMR regulation, we cut our FY18F-19F earnings for Adaro Energy by 14.5% and 7.3% respectively. We reiterate our BUY call with revised TP of IDR2,800 (from IDR3,000, 29% upside). Our DCF-derived TP of IDR2,800 implies FY18F P/E of 12.6x, which is -0.1SD from its 10-year mean P/E of 13.2x.

Ceiling for coal price of USD70.00/tonne for domestic power plants. On 7 Mar, MEMR issued a Ministry Decree No.1395 K/30/MEM/2018 to regulate the selling prices of coal with CV of 6,322kcal/kg GAR to domestic coal power plants. The ceiling price was set at USD70/tonne or based on the domestic HBA, whichever is lower.

The selling price for coal with lower CV and quality was adjusted proportionally according to the CV of the coal. The ceiling coal price for domestic power plants is valid for 2018-2019, with maximum coal sales volume of 100m tonnes pa. At the end of 2019, the ceiling for coal selling price and maximum quota would be reviewed.

Allowance for an increase in coal production of 10% from original coal production plan. MEMR also stated that coal companies that fulfil the minimum domestic market obligation of 25%, as well as the ceiling coal selling price for domestic coal-fired power plants, would be able to receive a 10% increase in coal production from their original approved production plans.

FY18F-19F earnings cut by 14.5% and 7.3% respectively. We fine-tune our FY18F-19F assumptions to factor in the impact of the ceiling for coal selling price for domestic power plants for 25% of Adaro Energy's coal production, which is higher than its current coal sales to Perusahaan Listrik Negara (PLN) of ~20% of its total coal production.

This has resulted in a cut in our FY18F-19F earnings of 14.5% and 7.3% respectively. We maintain our FY20 assumptions as the ceiling for coal prices is only valid during 2018-2019.

Reiterate BUY call with revised TP of IDR2,800. Our DCF-derived TP of IDR2,800 implies FY18F P/E of 12.6x (-0.1SD from its 10-year mean P/E of 13.2x). We maintain our BUY call on the back of undemanding valuations and high dividend yields. With its strong cash flows and net cash position, we estimate that Adaro Energy would increase its dividend payout to 40%, which would in turn result in a projected dividend yield of 4.7% in FY18F.

Key risks to our BUY call include lower-than-expected coal prices, significant increases in oil prices, unfavourable government policies domestically, and unfavourable policies on coal in China.

Target Price:	IDR2,800
Price:	IDR2,170
Market Cap:	USD5,031m
Bloomberg Ticker:	ADRO IJ

Share Data

Avg Daily Turnover (IDR/USD)	127,659m/9.44m
52-wk Price low/high (IDR)	1,410 - 2,560
Free Float (%)	35
Shares outstanding (m)	31,985
Estimated Return	29%

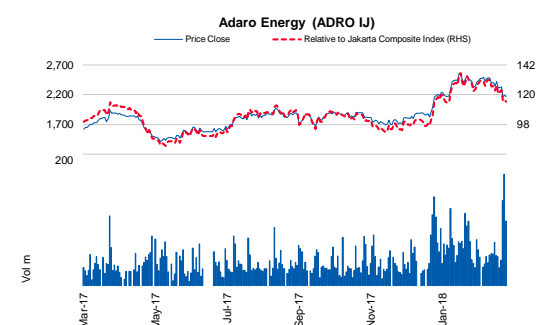
Shareholders (%)

Adaro Strategic Investments	43.9
Garibaldi Thohir	6.2
TP Rachmat	3.3

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	16.7	(6.5)	25.8	15.1	28.8
Relative	15.5	(5.4)	19.1	5.3	9.7

Source: Bloomberg



Source: Bloomberg

Forecasts and Valuations	Dec-16	Dec-17	Dec-18F	Dec-19F	Dec-20F
Total turnover (USDm)	2,524	3,258	3,532	4,065	4,240
Reported net profit (USDm)	335	483	519	566	586
Recurring net profit (USDm)	335	483	519	566	586
Recurring net profit growth (%)	119.5	44.4	7.3	9.1	3.5
Recurring EPS (USD)	0.01	0.02	0.02	0.02	0.02
DPS (USD)	0.003	0.003	0.007	0.008	0.008
Recurring P/E (x)	15.0	10.4	9.7	8.9	8.6
P/B (x)	1.61	1.45	1.31	1.21	1.12
P/CF (x)	8.5	10.8	7.7	5.4	5.2
Dividend Yield (%)	2.0	2.0	4.7	5.0	4.9
EV/EBITDA (x)	7.45	4.95	4.10	3.60	3.33
Return on average equity (%)	11.1	14.7	14.2	14.1	13.5
Net debt to equity (%)	9.4	4.2	12.0	3.0	net cash
Our vs consensus EPS (adjusted) (%)			(9.9)	4.1	7.7

Source: Company data, RHB

Analyst

Hariyanto Wijaya, CFA, CPA, CFTe, CMT
+6221 2970 7061

hariyanto.wijaya@rhbgroup.com



Financial Exhibits

Financial model updated on: 2018-03-11.

Asia	Financial summary	Dec-16	Dec-17	Dec-18F	Dec-19F	Dec-20F
Indonesia	Recurring EPS (USD)	0.01	0.02	0.02	0.02	0.02
Basic Materials	EPS (USD)	0.01	0.02	0.02	0.02	0.02
Adaro Energy	DPS (USD)	0.003	0.003	0.007	0.008	0.008
Bloomberg ADRO IJ	BVPS (USD)	0.10	0.11	0.12	0.13	0.14
Buy	Weighted avg adjusted shares (m)	31,986	31,986	31,986	31,986	31,986
Valuation basis	Valuation metrics	Dec-16	Dec-17	Dec-18F	Dec-19F	Dec-20F
We use DCF as the main valuation method because we want to factor in the impact of long-term sustainable coal prices. We also use P/E as a corroborative valuation.	Recurring P/E (x)	15.0	10.4	9.7	8.9	8.6
	P/E (x)	15.0	10.4	9.7	8.9	8.6
	P/B (x)	1.61	1.45	1.31	1.21	1.12
	FCF Yield (%)	5.9	5.7	(2.5)	8.4	12.3
	Dividend Yield (%)	2.0	2.0	4.7	5.0	4.9
	EV/EBITDA (x)	7.45	4.95	4.10	3.60	3.33
	EV/EBIT (x)	10.2	6.1	5.2	4.8	4.4
Key drivers	Income statement (USDm)	Dec-16	Dec-17	Dec-18F	Dec-19F	Dec-20F
Our TP is mostly sensitive to changes in:	Total turnover	2,524	3,258	3,532	4,065	4,240
i. Coal sales volume;	Gross profit	685	1,142	1,284	1,344	1,264
ii. Coal price;	EBITDA	802	1,167	1,443	1,558	1,533
iii. Oil prices.	Depreciation and amortisation	(215)	(215)	(311)	(379)	(379)
	Operating profit	588	952	1,132	1,179	1,154
	Net interest	(41)	(34)	(57)	(54)	(36)
	Income from associates & JVs	(0)	0	0	0	0
	Pre-tax profit	547	930	1,075	1,125	1,117
	Taxation	(206)	(393)	(479)	(501)	(497)
	Minority interests	(6)	(53)	(78)	(59)	(35)
	Recurring net profit	335	483	519	566	586
Key risks	Cash flow (USDm)	Dec-16	Dec-17	Dec-18F	Dec-19F	Dec-20F
Key risks include:	Change in working capital	42	(211)	(179)	(20)	3
i. A significant drop in coal prices;	Cash flow from operations	591	464	651	925	967
ii. Weaker-than-expected coal demand;	Capex	(293)	(178)	(777)	(500)	(346)
iii. A significant increase in oil prices.	Cash flow from investing activities	(278)	(121)	(649)	(372)	(218)
	Proceeds from issue of shares	7	(43)	0	0	0
	Dividends paid	(87)	(101)	(142)	(242)	(249)
	Cash flow from financing activities	(57)	(325)	(503)	(342)	(559)
	Cash at beginning of period	702	1,077	1,207	705	916
	Net change in cash	256	18	(501)	211	191
	Ending balance cash	959	1,095	705	916	1,107
Company Profile	Balance sheet (USDm)	Dec-16	Dec-17	Dec-18F	Dec-19F	Dec-20F
Adaro Energy is an Indonesian energy group that focuses on integrated coal mining through subsidiaries. Its principal mine location is in South Kalimantan, where subsidiary PT Adaro Indonesia operates the largest single-site coal mine in the southern hemisphere. PT Adaro Indonesia operates under a first-generation coal co-operation agreement (CCA) with the Government that is valid until 2022. Its customers are mostly blue-chip power utilities.	Total cash and equivalents	1,077	1,207	705	916	1,107
	Tangible fixed assets	3,980	3,862	4,200	4,193	4,032
	Intangible assets	794	794	794	794	794
	Total investments	48	46	46	46	46
	Total other assets	109	134	134	134	134
	Total assets	6,522	6,814	6,757	7,024	7,074
	Short-term debt	154	237	200	366	448
	Total long-term debt	1,280	1,140	1,020	690	278
	Other liabilities	16	16	16	16	16
	Total liabilities	2,736	2,723	2,492	2,371	2,064
	Shareholders' equity	3,125	3,464	3,840	4,164	4,501
	Minority interests	639	623	421	484	505
	Total equity	3,786	4,092	4,265	4,653	5,010
	Net debt	357	170	514	139	(382)
	Total liabilities & equity	6,522	6,814	6,757	7,024	7,074
	Key metrics	Dec-16	Dec-17	Dec-18F	Dec-19F	Dec-20F
	Revenue growth (%)	(6.0)	29.1	8.4	15.1	4.3
	Recurrent EPS growth (%)	119.5	44.4	7.3	9.1	3.5
	Gross margin (%)	27.1	35.0	36.4	33.0	29.8
	Operating EBITDA margin (%)	31.8	35.8	40.9	38.3	36.2
	Net profit margin (%)	13.3	14.8	14.7	13.9	13.8
	Dividend payout ratio (%)	30.2	20.9	46.0	44.1	42.4
	Capex/sales (%)	11.6	5.5	22.0	12.3	8.2
	Interest cover (x)	11.8	18.0	15.7	18.7	23.9

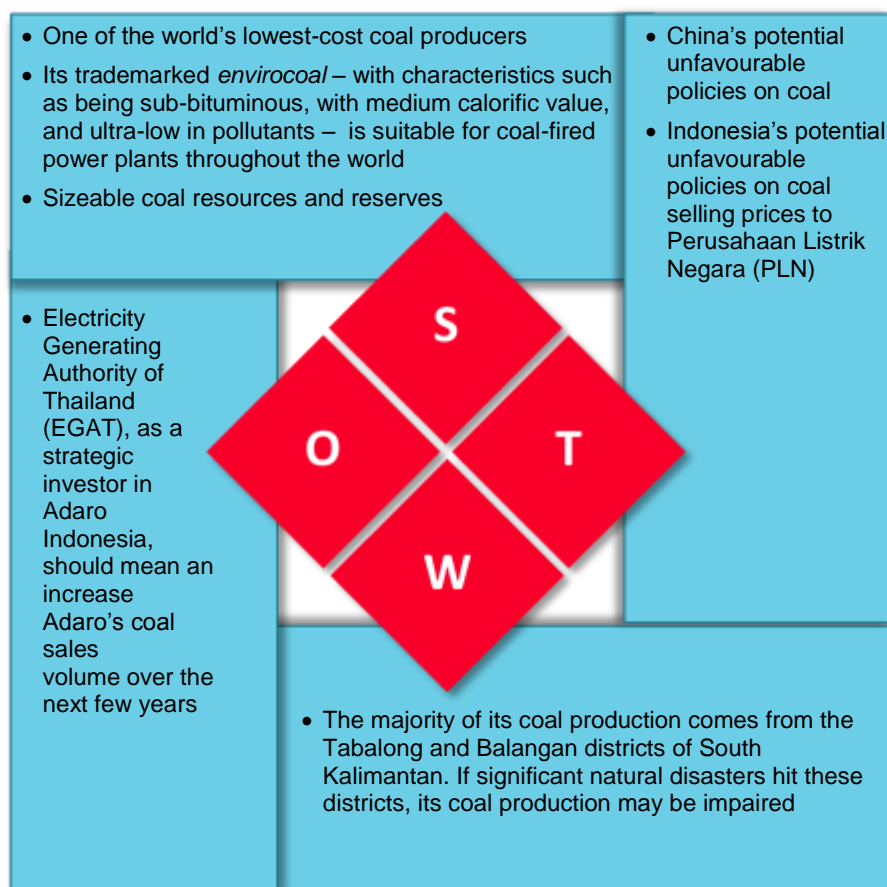
Source: Company data, RHB

Figure 1: Changes in our forecasts

USD m	Previous forecasts			Current forecasts			Changes		
	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F	FY18F	FY19F	FY20F
Average coal price (USD per tonne) (Newcastle. CV of 6,000kcal/kg)	90	85	78	90	85	78	0.0%	0.0%	0.0%
Average oil price (USD per barrel)	64	60	60	64	60	60	0.0%	0.0%	0.0%
Coal production volume (m tonnes)	55	65	69	55	65	69	0.0%	0.0%	0.0%
Purchased coal volume (m tonnes)	0	0	3	0	0	3	0.0%	0.0%	0.0%
Sales coal volume (m tonnes)	55	65	72	55	65	72	0.0%	0.0%	0.0%
Revenue	3,713	4,199	4,240	3,532	4,065	4,240	-4.9%	-3.2%	0.0%
Gross profit	1,440	1,414	1,264	1,284	1,344	1,264	-10.8%	-5.0%	0.0%
Operating profit	1,286	1,248	1,154	1,132	1,179	1,154	-12.0%	-5.5%	0.0%
Net profit (net of minority interests)	607	611	586	519	566	586	-14.5%	-7.3%	0.0%

Source: RHB

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2018-03-07	Buy	3,000	2,160
2018-02-08	Buy	3,100	2,420
2018-01-26	Buy	3,100	2,440
2017-11-01	Buy	2,300	1,910
2017-08-29	Buy	2,300	1,870
2017-02-28	Buy	2,100	1,695
2015-11-04	Not Rated	na	655
2014-11-03	Neutral	1,250	1,150
2014-08-29	Neutral	1,320	1,315
2014-05-02	Neutral	1,250	1,140

Source: RHB, Bloomberg

12 March 2018

Basic Materials | Mining

Bukit Asam

Buy (Maintained)

Factoring The Ceiling Coal Price Impact

MEMR has issued a ministry decree that regulates the selling price of coal with CV of 6,322kcal/kg GAR to domestic coal power plants. This is set at a ceiling of USD70.00/tonne. To factor in the impact of this decree, we cut Bukit Asam's FY18F-19F earnings by 7.4% and 5.4% respectively. We also reiterate our Buy call with a revised IDR3,900 TP (from IDR4,100, 35% upside). Our DCF-derived TP implies FY18F P/E of 9x on our FY18F EPS.

Ceiling coal prices of USD70.00/tonne for domestic power plants. MEMR has issued Ministry Decree No. 1395 K/30/MEM/2018. This regulates the selling price of coal with a CV of 6,322kcal/kg GAR to domestic coal power plants at USD70.00/tonne, or based on the domestic HBA – whichever is lower. The selling prices of lower CV and quality of coal are adjusted proportionally, according to the calorific value of the coal.

This USD70.00/tonne ceiling coal price for domestic power plants is valid for 2018 and 2019, with maximum coal sales volumes of 100m tonnes pa. At the end of 2019, this ceiling coal selling price and maximum quota is to be reviewed.

Allowing the increase of coal production by ~10% from the original coal production plan. The MEMR's decree also states that coal companies that have fulfilled the:

- i. Minimal domestic market obligation of 25%;
- ii. Ceiling coal selling prices for domestic coal-fired power plants...

...are able to get a 10% higher coal production level from their original approved production plans.

Cutting FY18F-19F earnings by 7.4% and 5.4% respectively. We fine-tune our FY18-19 assumptions – to factor in the impact of the USD70.00/tonne ceiling coal price to domestic power plants (for 2018-2019) – for 25% of Bukit Asam's coal production. This is lower than its total coal sales to PLN – ~50% of the company's coal production – and results in a cut in FY18F-19F earnings of 7.4% and 5.4% respectively.

Reiterate BUY with a revised IDR3,900 TP (from IDR4,100, 35% upside). Our DCF-derived TP of IDR3,900 implies 9x FY18F P/E. We like Bukit Asam, as we think consensus has still not factored in its sizable FY18 earnings growth. Post earnings adjustments for the ceiling coal price, the counter is trading at 6.7x FY18F P/E on our FY18F EPS. This is undemanding, considering Bukit Asam's superb FY18F ROE of 30.5%.

Key risks to our call include lower-than-expected coal prices, significant increases in oil prices, unfavourable government policies domestically, and unfavourable policies towards coal in China.

Target Price:	IDR3,900
Price:	IDR2,890
Market Cap:	USD2,413m
Bloomberg Ticker:	PTBA IJ

Share Data

Avg Daily Turnover (IDR/USD)	92,587m/6.85m
52-wk Price low/high (IDR)	1,845 - 3,430
Free Float (%)	33
Shares outstanding (m)	10,818
Estimated Return	35%

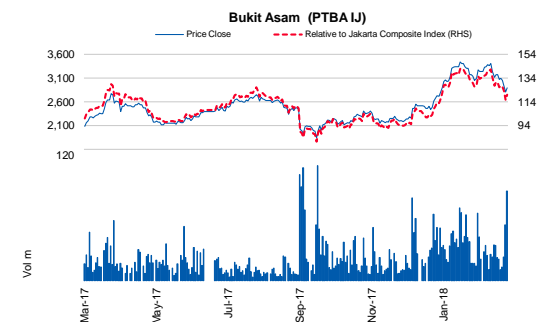
Shareholders (%)

Government of Indonesia	65.0
Vanguard Group	1.1
Dimensional Fund Advisors	0.8

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	17.5	(5.3)	30.8	16.8	33.2
Relative	16.3	(4.2)	24.1	7.0	14.1

Source: Bloomberg



Source: Bloomberg

Forecasts and Valuations	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Total turnover (IDRb)	13,734	14,485	19,684	22,973	26,850
Reported net profit (IDRb)	2,036	1,802	4,015	4,668	4,557
Recurring net profit (IDRb)	2,036	1,802	4,015	4,668	4,557
Recurring net profit growth (%)	9.4	(11.5)	122.8	16.3	(2.4)
Recurring EPS (IDR)	188	167	371	431	421
DPS (IDR)	60	66	58	130	151
Recurring P/E (x)	15.4	17.3	7.8	6.7	6.9
P/B (x)	3.41	3.05	2.29	1.85	1.58
P/CF (x)	13.1	16.4	7.5	6.3	6.1
Dividend Yield (%)	2.1	2.3	2.0	4.5	5.2
EV/EBITDA (x)	10.6	11.3	5.3	4.3	4.1
Return on average equity (%)	23.2	18.5	33.6	30.5	24.8
Net debt to equity	net cash	net cash	net cash	net cash	net cash
Our vs consensus EPS (adjusted) (%)			14.5	22.2	19.7

Source: Company data, RHB

Analyst

Hariyanto Wijaya, CFA, CPA, CFTe, CMT
+6221 2970 7061

hariyanto.wijaya@rhbgroup.com



Financial Exhibits

Financial model updated on: 2018-03-12.

Asia	Financial summary	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Indonesia	Recurring EPS (IDR)	188	167	371	431	421
Basic Materials	EPS (IDR)	188	167	371	431	421
Bukit Asam	DPS (IDR)	60	66	58	130	151
Bloomberg PTBA IJ	BVPS (IDR)	848	949	1,262	1,563	1,833
Buy	Weighted avg adjusted shares (m)	10,818	10,818	10,818	10,818	10,818
Valuation basis	Valuation metrics	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
We use DCF as the main valuation method because we want to factor in the impact of long-term sustainable coal prices. We also use P/E as a corroborative valuation.	Recurring P/E (x)	15.4	17.3	7.8	6.7	6.9
	P/E (x)	15.4	17.3	7.8	6.7	6.9
	P/B (x)	3.41	3.05	2.29	1.85	1.58
	FCF Yield (%)	1.7	4.1	0.6	9.6	9.9
	Dividend Yield (%)	2.1	2.3	2.0	4.5	5.2
	EV/EBITDA (x)	10.6	11.3	5.3	4.3	4.1
	EV/EBIT (x)	11.8	12.3	5.5	4.5	4.4
Key drivers	Income statement (IDRb)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Our TP is mostly sensitive to a change in:	Total turnover	13,734	14,485	19,684	22,973	26,850
i. Coal sales volumes;	Gross profit	4,140	4,158	7,203	8,253	8,268
ii. Coal prices;	EBITDA	2,693	2,457	5,354	6,274	6,130
iii. Forex fluctuations;	Depreciation and amortisation	(279)	(200)	(226)	(274)	(338)
iv. Cost of mining contracting.	Operating profit	2,414	2,257	5,128	6,000	5,791
	Net interest	115	(33)	(10)	(28)	36
	Income from associates & JVs	134	134	134	134	134
	Pre-tax profit	2,664	2,358	5,252	6,106	5,961
	Taxation	(627)	(555)	(1,236)	(1,437)	(1,402)
	Minority interests	(1)	(1)	(2)	(2)	(2)
	Recurring net profit	2,036	1,802	4,015	4,668	4,557
Key risks	Cash flow (IDRb)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
i. Delay in expanding railway capacity;	Change in working capital	232	(101)	(49)	52	192
ii. A significant drop in coal prices;	Cash flow from operations	2,393	1,901	4,192	4,994	5,086
iii. Weaker-than-expected coal demand;	Capex	(1,871)	(627)	(4,000)	(2,000)	(2,000)
iv. Strengthening IDR.	Cash flow from investing activities	(1,976)	(627)	(4,000)	(2,000)	(2,000)
	Proceeds from issue of shares	(618)	0	0	0	0
	Dividends paid	(651)	(713)	(631)	(1,405)	(1,634)
	Cash flow from financing activities	(1,341)	(711)	(629)	(1,403)	(1,631)
	Cash at beginning of period	4,039	3,115	3,678	3,240	4,831
	Net change in cash	(924)	563	(437)	1,591	1,455
	Ending balance cash	3,115	3,678	3,240	4,831	6,286
Company Profile	Balance sheet (IDRb)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
PT Bukit Asam (Persero) Tbk is the only state-owned coal miner in Indonesia. Its business activities include conducting thermal coal mining operations, managing and operating thermal power plants (internal/external use), and providing coal mining and production related consultation and engineering services. The company has coal mining concessions in Sumatra and Kalimantan. Its core mining operations are in Tanjung Enim in South Sumatra. Its coal from Tanjung Enim is delivered via rail from Tanjung Enim to Tarahan Port in Lampung and to Kertapati Port in Palembang.	Total cash and equivalents	3,115	3,678	3,240	4,831	6,286
	Tangible fixed assets	5,579	6,007	9,781	11,507	13,169
	Total investments	1,240	1,240	1,240	1,240	1,240
	Total other assets	2,476	2,476	2,476	2,476	2,476
	Total assets	16,894	18,052	22,230	26,176	30,169
	Short-term debt	739	739	739	739	739
	Total long-term debt	670	670	670	670	670
	Total liabilities	7,606	7,674	8,466	9,147	10,215
	Shareholders' equity	9,175	10,264	13,648	16,911	19,834
	Minority interests	113	114	116	118	120
	Total equity	9,288	10,378	13,764	17,029	19,954
	Net debt	(1,706)	(2,269)	(1,831)	(3,422)	(4,877)
	Total liabilities & equity	16,894	18,052	22,230	26,176	30,169
	Key metrics	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
	Revenue growth (%)	5.0	5.5	35.9	16.7	16.9
	Recurrent EPS growth (%)	9.4	(11.5)	122.8	16.3	(2.4)
	Gross margin (%)	30.1	28.7	36.6	35.9	30.8
	Operating EBITDA margin (%)	19.6	17.0	27.2	27.3	22.8
	Net profit margin (%)	14.8	12.4	20.4	20.3	17.0
	Dividend payout ratio (%)	32.0	39.5	15.7	30.1	35.9
	Capex/sales (%)	13.6	4.3	20.3	8.7	7.4
	Interest cover (x)	15.3	14.3	32.6	38.1	36.8

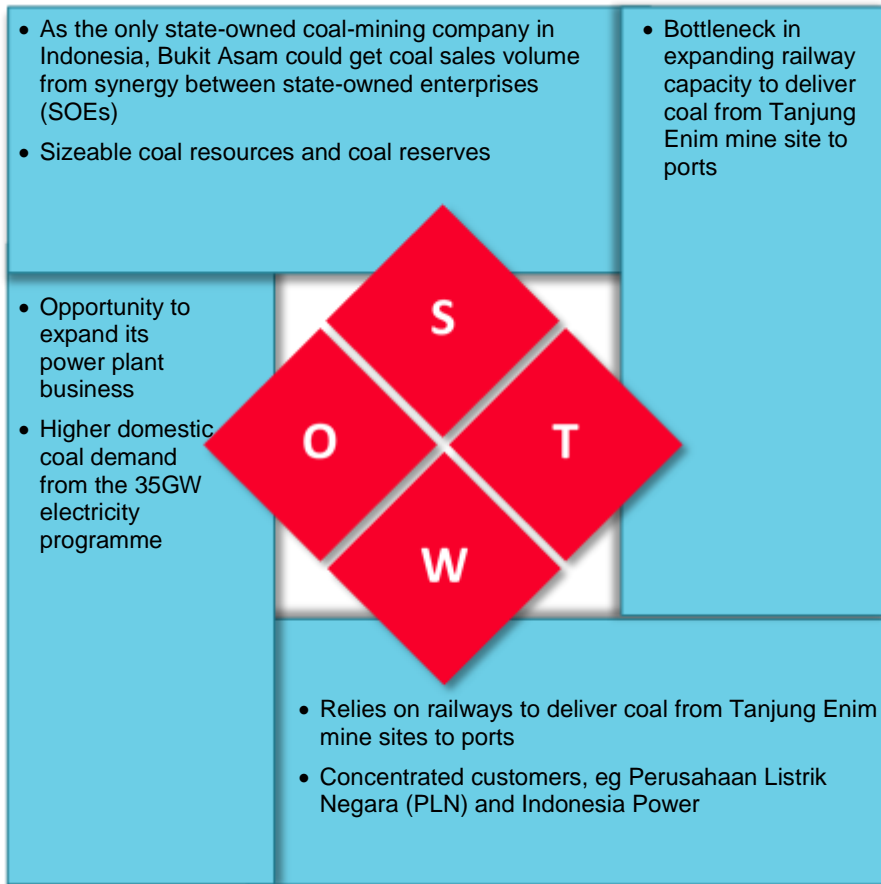
Source: Company data, RHB

Figure 1: Changes in forecasts

IDR bn	Previous forecasts		Current forecasts		Change (%)	
	FY18F	FY19F	FY18F	FY19F	FY18F	FY19F
Average coal price (USD per tonne) (Newcastle. CV of 6,000kcal/kg)	90	85	90	85	0.0%	0.0%
Average oil price (USD per barrel)	64	60	64	60	0.0%	0.0%
Coal production volume (m tonnes)	26	33	26	33	0.0%	0.0%
Purchased coal volume (m tonnes)	0	0	0	0	0.0%	0.0%
Sales coal volume (m tonnes)	26	34	26	34	0.0%	0.0%
Revenue	23,565	27,247	22,973	26,850	-2.5%	-1.5%
Gross profit	8,756	8,605	8,253	8,268	-5.7%	-3.9%
Operating profit	6,488	6,118	6,000	5,791	-7.5%	-5.3%
Net profit (net of minority interests)	5,041	4,817	4,668	4,557	-7.4%	-5.4%

Source: RHB

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2018-01-26	Buy	4,100	3,330
2017-07-31	Buy	17,400	2,620
2017-02-26	Buy	17,600	2,230
2015-11-04	Not Rated	na	1,555
2015-03-04	Buy	14,400	2,160
2014-10-31	Buy	14,400	2,590
2014-07-22	Buy	12,400	2,130
2014-05-02	Buy	11,200	1,960
2013-11-05	Buy	13,600	2,310
2013-10-21	Buy	15,050	2,740

Source: RHB, Bloomberg

12 March 2018

Basic Materials | Mining

Harum Energy

Buy (Maintained)

Factoring In The Impact Of The Coal Price Ceiling

MEMR issued a ministry decree to regulate the selling prices of coal with CV of 6,322kcal/kg GAR to domestic coal power plants, by setting a ceiling of USD70/tonne. To factor in the impact of the MEMR regulation, we cut our FY18F-19F earnings for Harum Energy by 14% and 11.8% respectively. We reiterate our BUY call with revised TP of IDR3,300 (from IDR3,500, 20% upside). Our DCF-derived TP of IDR3,300 implies FY18F P/E of 11x. We maintain our BUY call on the back of undemanding valuations and potential accretive acquisitions.

Ceiling for coal price of USD70.00/tonne for domestic power plants. On 7 Mar, MEMR issued Ministry Decree No.1395 K/30/MEM/2018 to regulate the selling prices of coal with CV of 6,322kcal/kg GAR to domestic coal power plants. The ceiling was set at USD70/tonne or based on the domestic HBA, whichever is lower.

The selling price for coal with lower CV and quality was adjusted proportionally according to the CV of the coal. The ceiling coal price for domestic power plants is valid during 2018-2019, with maximum coal sales volume of 100m tonnes pa. At the end of 2019, the ceiling for coal selling price and maximum sales pa would be reviewed.

Allowance for an increase in coal production of 10% from original coal production plan. MEMR also stated that coal companies that fulfil the minimum domestic market obligation of 25% and the ceiling for coal selling price for domestic coal-fired power plants would be able to receive a 10% increase in coal production from their original approved production plan.

FY18F-19F earnings cut by 14% and 11.8% respectively. We fine-tune our FY18F-19F assumptions to factor in the impact of the ceiling coal price to domestic power plants for 2018-2019 for 25% of Harum Energy's coal production. This is higher than its current coal sales to PLN of 0% of its total coal production. This has resulted in a cut in our FY18F-19F earnings of 14% and 11.8% respectively.

Reiterate BUY call with revised TP of IDR3,300. Our DCF-derived TP of IDR3,300 implies FY18F P/E of 11x. We maintain our BUY call on the back of undemanding valuations and potential accretive acquisitions. With its strong cash flows and net cash position, we believe Harum Energy may look for accretive acquisitions ahead.

Key risks to our BUY call include lower-than-expected coal prices, significant increases in oil prices, unfavourable government policies domestically, and unfavourable policies on coal in China.

Target Price:	IDR3,300
Price:	IDR2,740
Market Cap:	USD537m
Bloomberg Ticker:	HRUM IJ

Share Data

Avg Daily Turnover (IDR/USD)	19,377m/1.44m
52-wk Price low/high (IDR)	1,980 - 3,490
Free Float (%)	26
Shares outstanding (m)	2,612
Estimated Return	20%

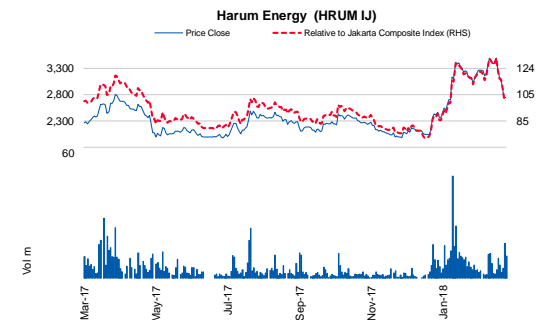
Shareholders (%)

Karunia Bara Perkasa	73.6
Dimensional Fund Advisors	1.4
Hartford Financial Services	0.6

Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	33.7	(9.0)	37.3	21.2	16.6
Relative	32.5	(7.9)	30.6	11.4	(2.5)

Source: Bloomberg



Source: Bloomberg

Forecasts and Valuations	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Total turnover (USDm)	249	217	340	407	506
Reported net profit (USDm)	(19.2)	13.3	43.8	57.1	76.8
Recurring net profit (USDm)	(6.0)	19.1	43.8	57.1	76.8
Recurring net profit growth (%)	(143.0)	0.0	129.8	30.3	34.6
Recurring EPS (USD)	(0.00)	0.01	0.02	0.02	0.03
DPS (USD)	na	na	na	na	na
Recurring P/E (x)	na	27.8	12.1	9.3	6.9
P/B (x)	1.95	1.88	1.63	1.38	1.15
P/CF (x)	na	13.5	10.8	8.1	6.3
Dividend Yield	na	na	na	na	na
EV/EBITDA (x)	37.4	8.6	4.1	2.8	1.6
Return on average equity (%)	(6.9)	4.8	14.4	16.1	18.2
Net debt to equity	net cash	net cash	net cash	net cash	net cash
Our vs consensus EPS (adjusted) (%)			(3.5)	1.8	30.8

Source: Company data, RHB

Analyst

Hariyanto Wijaya, CFA, CPA, CFTe, CMT
+6221 2970 7061

hariyanto.wijaya@rhbgroup.com



Financial Exhibits

Financial model updated on: 2018-03-11.

Asia	Financial summary	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Indonesia	Recurring EPS (USD)	(0.00)	0.01	0.02	0.02	0.03
Basic Materials	EPS (USD)	(0.01)	0.00	0.02	0.02	0.03
Harum Energy	BVPS (USD)	0.10	0.11	0.12	0.14	0.17
Bloomberg HRUM IJ	Weighted avg adjusted shares (m)	2,687	2,671	2,671	2,671	2,671
Buy						
	Valuation metrics	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Valuation basis	Recurring P/E (x)	na	27.8	12.1	9.3	6.9
We use DCF as the main valuation method because we want to factor in the impact of long-term sustainable coal prices. We also use P/E as a corroborative valuation.	P/E (x)	na	39.7	12.1	9.3	6.9
	P/B (x)	1.95	1.88	1.63	1.38	1.15
	FCF Yield (%)	(1.2)	7.2	8.3	11.0	14.5
	EV/EBITDA (x)	37.4	8.6	4.1	2.8	1.6
	EV/EBIT (x)	697	11	5	3	2
Key drivers	Income statement (USDm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Our TP is mostly sensitive to changes in:	Total turnover	249	217	340	407	506
i. Coal sales volume;	Gross profit	46	68	112	135	170
ii. Coal price;	EBITDA	11	43	80	98	127
iii. Oil prices.	Depreciation and amortisation	(10)	(11)	(10)	(11)	(11)
	Operating profit	1	32	70	88	116
	Net interest	1	1	4	4	5
	Income from associates & JVs	(4)	(3)	(2)	1	3
	Pre-tax profit	(18)	29	72	92	124
	Taxation	(1)	(11)	(18)	(22)	(30)
	Minority interests	(0)	(5)	(10)	(13)	(17)
	Recurring net profit	(6)	19	44	57	77
Key risks	Cash flow (USDm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
i. A significant drop in coal prices;	Change in working capital	4	13	(5)	(3)	(4)
ii. Weaker-than-expected coal demand;	Cash flow from operations	(5)	39	49	65	84
iii. A significant increase in oil prices.	Capex	(2)	(1)	(5)	(7)	(7)
	Cash flow from investing activities	(2)	(5)	(9)	(14)	(16)
	Dividends paid	(0)	0	0	0	0
	Cash flow from financing activities	1	1	(41)	13	17
	Cash at beginning of period	201	196	231	231	296
	Net change in cash	(6)	35	(0)	65	86
	Ending balance cash	196	231	231	296	381
Company Profile	Balance sheet (USDm)	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
Harum Energy, established in 1995, is a holding company that has successfully expanded its portfolio of businesses in coal mining and logistics activities in East Kalimantan. One of Harum Energy's key strengths is its vertically integrated supply chain linking its mine-sites through to the offshore vessel loading. The company produces bituminous coal with a low sulphur and low ash content that ensures a wide acceptance amongst buyers. It exports to buyers in the established coal importing markets of China, India, Japan, South Korea, Taiwan and Malaysia, where multiple-year long-term contracts are held with many blue-chip buyers.	Total cash and equivalents	196	231	231	296	381
	Tangible fixed assets	99	89	84	80	76
	Total investments	8	6	5	7	11
	Total other assets	49	50	55	59	64
	Total assets	381	413	419	494	595
	Other liabilities	5	5	5	5	5
	Total liabilities	37	58	61	65	72
	Shareholders' equity	272	282	326	383	460
	Minority interests	71	73	33	46	63
	Total equity	343	355	359	429	523
	Net debt	(196)	(231)	(231)	(296)	(381)
	Total liabilities & equity	381	413	419	494	595
	Key metrics	Dec-15	Dec-16	Dec-17F	Dec-18F	Dec-19F
	Revenue growth (%)	(47.8)	(12.9)	56.6	19.6	24.4
	Recurrent EPS growth (%)	(143.3)	0.0	129.8	30.3	34.6
	Gross margin (%)	18.4	31.3	33.0	33.1	33.7
	Operating EBITDA margin (%)	4.3	19.7	23.5	24.2	25.0
	Net profit margin (%)	(7.7)	6.1	12.9	14.0	15.2
	Capex/sales (%)	0.7	0.6	1.5	1.7	1.4
	Interest cover (x)	0.25	20.49	44.20	55.63	73.40

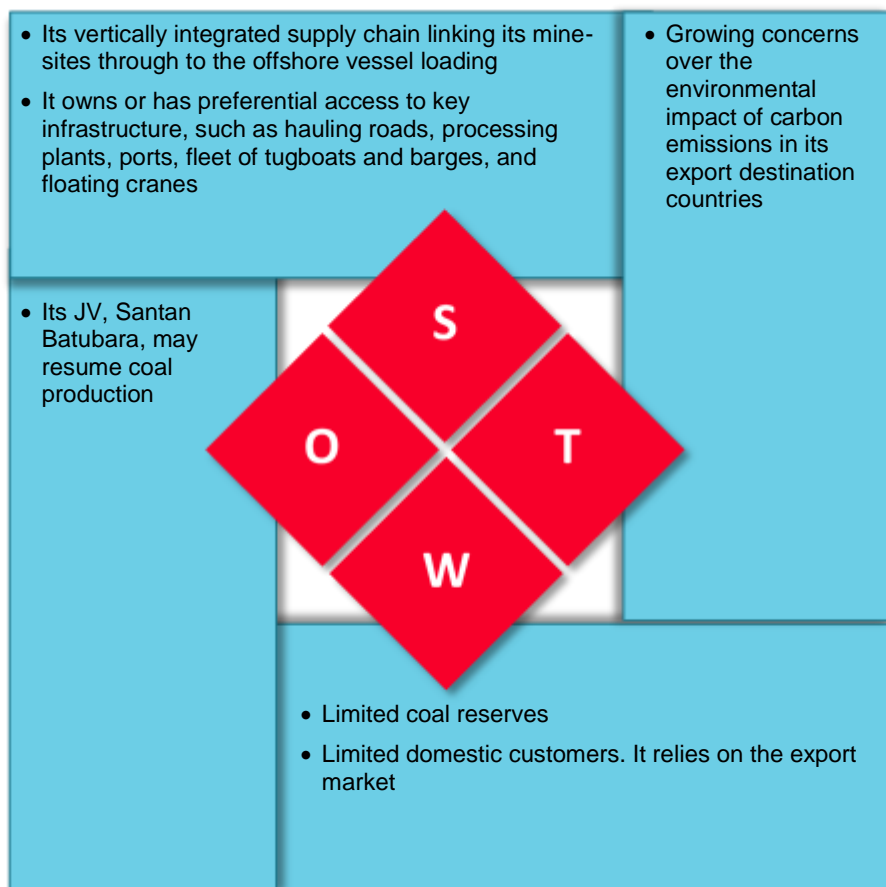
Source: Company data, RHB

Figure 1: Changes in our forecasts

USD m	Previous forecasts		Current forecasts		Change (%)	
	FY18F	FY19F	FY18F	FY19F	FY18F	FY19F
Average coal price (USD per tonne) (Newcastle. CV of 6,000kcal/kg)	95	89	95	89	0.0%	0.0%
Average oil price (USD per barrel)	67	63	67	63	0.0%	0.0%
Coal production volume (m tonnes)	5.8	8.2	5.8	8.2	0.0%	0.0%
Purchased coal volume (m tonnes)	0.8	0.8	0.8	0.8	0.0%	0.0%
Sales coal volume (m tonnes)	6.1	7.8	6.1	7.8	0.0%	0.0%
Revenue	426	523	407	506	-4.5%	-3.2%
Gross profit	150	187	135	170	-10.3%	-9.0%
Operating profit	103	132	88	116	-14.7%	-12.5%
Net profit (net of minority interests)	66	87	57	77	-14.0%	-11.8%

Source: RHB

SWOT Analysis



Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2018-01-26	Buy	3,500	3,380
2017-08-01	Buy	2,800	2,320
2017-05-02	Buy	3,000	2,500
2017-04-03	Buy	2,800	2,470
2017-03-02	Buy	2,800	2,200
2015-11-04	Not Rated	na	860
2014-11-03	Sell	1,370	1,530
2014-07-31	Neutral	2,250	2,110
2014-05-02	Neutral	2,290	2,275
2013-11-05	Neutral	2,720	3,325

Source: RHB, Bloomberg

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Trading Buy: Share price may exceed 15% over the next 3 months, however longer-term outlook remains uncertain

Neutral: Share price may fall within the range of +/- 10% over the next 12 months

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Kuala Lumpur	Hong Kong	Singapore
RHB Research Institute Sdn Bhd Level 3A, Tower One, RHB Centre Jalan Tun Razak Kuala Lumpur 50400 Malaysia Tel : +(60) 3 9280 8888 Fax : +(60) 3 9200 2216	RHB Securities Hong Kong Ltd. 12 th Floor World-Wide House 19 Des Voeux Road Central, Hong Kong Tel : +(852) 2525 1118 Fax : +(852) 2810 0908	RHB Research Institute Singapore Pte Ltd. 10 Collyer Quay #09-08 Ocean Financial Centre Singapore 049315 Tel : +(65) 6533 1818 Fax : +(65) 6532 6211
Jakarta	Shanghai	Bangkok
PT RHB Sekuritas Indonesia Wisma Mulia, 20th Floor Jl. Jenderal Gatot Subroto No. 42 Jakarta 12710, Indonesia Tel : +(6221) 2783 0888 Fax : +(6221) 2783 0777	RHB (China) Investment Advisory Co. Ltd. Suite 4005, CITIC Square 1168 Nanjing West Road Shanghai 20041 China Tel : +(8621) 6288 9611 Fax : +(8621) 6288 9633	RHB Securities (Thailand) PCL 10th Floor, Sathorn Square Office Tower 98, North Sathorn Road, Silom Bangrak, Bangkok 10500 Thailand Tel: +(66) 2 088 9999 Fax : +(66) 2 088 9799