

4 July 2024

Consumer Non-cyclical | Tobacco

Gudang Garam (GGRM IJ)

Sell (from Neutral)

Missing The Rule Of Thumb; Downgrade To SELL

Target Price (Return): IDR13,700 (-21.0%)
 Price (Market Cap): IDR17,350 (USD2,036m)
 ESG score: 2.9 (out of 4)
 Avg Daily Turnover (IDR/USD) 16,390m/1.02m

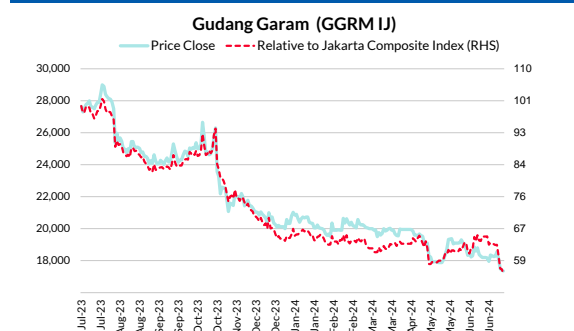
- **D/G SELL from Neutral, new IDR13,700 TP from IDR17,325, 21% downside, c.7% FY25F yield.** Increased downtrading due to slim pocket size can hamper Gudang Garam's sales volume growth as a Tier-1 player. The need to offset excise tax and maintain margins further propels sales volume contractions. We cut FY24F-25F earnings by 5.3% and 16.4% given the potential drop in sales volume and likely milder price hikes ahead to cushion GPMs. Our TP is based on 6x P/E, ie at a 26% discount to the peer average of 8.1x. GGRM is trading at 7.7x 2025F P/E or -1SD from its 5-year mean.
- **Deserves higher discount in the absence of dividends.** Despite strong FY23 earnings of IDR5.3trn (+91.6% YoY), GGRM did not distribute dividends vis-a-vis Hanjaya Mandala Sampoerna (HMSP IJ, BUY, TP: IDR970), which consistently distributes dividends with pay-out ratios of almost 100%. Considering an expansion of the cigarette unit is not favourable while that of the toll road business needs time to monetise (commercial operations to start in 3Q25), while growth is not expected for the tobacco core business, we believe GGRM should trade at a discount when compared with its peer.
- **Missing the rule of thumb.** 1H is the most crucial period for tobacco firms to raise prices to offset excise tax expenses by 70-80% or, at least, 1Q GPM should exceed the previous year's full-year GPMs. However, GGRM's 1H24 price hike only offset 30-50% of the excise tax hike. Given the national minimum wage grew <5% while 2024's excise tax hike is averaging 10%, we expect 2H24's price hikes (to maintain GPMs) to contract volume growth.
- **Flat earnings growth would be nice, but see a decline.** While 2025's excise tax has not been unveiled (expected in 4Q24), we are pessimistic that the Government will lower the excise tax hike for this period. As in 1Q24, Tier-1 players HMSP and GGRM's price increments have been soft, yet the former's volume growth was relatively flat (+1.5% YoY) vs the industry's +6.4% YoY, which implies strong downtrading behaviour. Therefore, with another series of excise tax increments slated for 2025, we see Tier-1 tobacco players posting flat growth at best and highly anticipate a volumes decline.
- **Declining market share.** GGRM's overall market share has been declining for the past three years (Figure 4) vis-à-vis HMSP, whose market share has been maintained. GGRM is more known for its machine-rolled *kretek* or SKM full flavour cigarettes and less popular in the hand-rolled *kretek* (SKT) segment. Additionally, its SKT unit only contributes c.8% of total revenue vs c.30% for HMSP. Hence, market share in this segment may also be decreasing.
- **GGRM has an ESG score of 2.9** (below the 3.0 country median). Accordingly, we apply a 2% ESG discount to its intrinsic value to derive our IDR13,700 TP.

Analyst

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Share Performance (%)

	YTD	1m	3m	6m	12m
Absolute	(14.6)	(5.3)	(11.3)	(17.5)	(37.2)
Relative	(13.5)	(7.6)	(11.7)	(16.4)	(44.7)
52-wk Price low/high (IDR)	17,350 – 29,000				



Source: Bloomberg

Forecasts and Valuation	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
Total turnover (IDRb)	124,683	118,953	105,226	103,576	102,006
Recurring net profit (IDRb)	2,783	5,190	4,468	4,354	4,054
Recurring net profit growth (%)	(50.4)	86.5	(13.9)	(2.5)	(6.9)
Recurring P/E (x)	12.00	6.43	7.47	7.67	8.24
P/B (x)	0.6	0.5	0.5	0.5	0.5
P/CF (x)	3.22	5.07	3.66	4.70	5.00
Dividend Yield (%)	13.0	6.9	na	6.9	6.7
EV/EBITDA (x)	1.23	1.11	0.92	0.87	0.83
Return on average equity (%)	4.7	9.0	7.3	6.7	6.1
Net debt to equity (%)	9.9	15.0	3.0	2.0	1.4

Source: Company data, RHB

Overall ESG Score: 2.9 (out of 4)

E: GOOD

GGRM has started its environmental measures and manages Scope 1 emissions from its manufacturing operations, which includes energy, greenhouse gas (GHG), water, and waste.

S: GOOD

GGRM values equality, inclusiveness, and sound labour relations, which includes the provision of minimum wages, and investments in human capital and communities.

G: GOOD

Under the supervision of the board of commissioners, the board of directors is responsible for maintaining corporate governance standards. The work of the independent audit committee has continued throughout 2022 – overseen by the board of commissioners.

Financial Exhibits

Asia Indonesia Consumer Non-cyclical Gudang Garam GGRM IJ Sell	Financial summary (IDR)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Recurring EPS	1,446.40	2,697.56	2,321.90	2,263.04	2,106.81
	DPS	2,250.00	1,200.00	-	1,195.82	1,166.39
	BVPS	30,069.26	31,632.01	34,019.11	35,151.53	36,157.14
	Return on average equity (%)	4.7	9.0	7.3	6.7	6.1
Valuation basis	Valuation metrics	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Recurring P/E (x)	12.00	6.43	7.47	7.67	8.24
	P/B (x)	0.6	0.5	0.5	0.5	0.5
	FCF Yield (%)	15.0	(4.6)	23.1	8.8	7.8
	Dividend Yield (%)	13.0	6.9	-	6.9	6.7
Key drivers	EV/EBITDA (x)	1.23	1.11	0.92	0.87	0.83
	EV/EBIT (x)	10.37	5.86	5.85	6.01	6.33
	i. Rising interest income;					
	ii. New products launched;					
	iii. Stronger-than-expected consumer purchasing power.					
Key risks	Income statement (IDRb)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Total turnover	124,683	118,953	105,226	103,576	102,006
	Gross profit	11,096	14,596	13,231	12,848	12,396
	EBITDA	31,708	38,200	38,408	40,056	41,599
	Depreciation and amortisation	(27,938)	(30,939)	(32,363)	(34,280)	(36,169)
Company Profile	Operating profit	3,771	7,261	6,045	5,775	5,430
	Net interest	(111)	(579)	(294)	(170)	(212)
	Pre-tax profit	3,647	6,861	5,929	5,784	5,396
	Taxation	(867)	(1,536)	(1,328)	(1,295)	(1,208)
	Reported net profit	2,780	5,325	4,602	4,488	4,188
	Recurring net profit	2,783	5,190	4,468	4,354	4,054
	Cash flow (IDRb)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Change in working capital	4,728	(1,593)	2,681	741	678
	Cash flow from operations	10,358	6,583	9,132	7,097	6,673
	Capex	(5,338)	(8,134)	(1,428)	(4,143)	(4,080)
	Cash flow from investing activities	(5,157)	(8,219)	(1,305)	(4,125)	(4,068)
	Dividends paid	(4,329)	(2,309)	0	(2,301)	(2,244)
	Cash flow from financing activities	(4,964)	1,486	(5,006)	(2,462)	(2,386)
	Cash at beginning of period	4,170	4,407	4,256	7,071	7,589
	Net change in cash	237	(151)	2,821	510	218
	Ending balance cash	4,407	4,256	7,077	7,581	7,808
	Balance sheet (IDRb)	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Total cash and equivalents	4,407	4,256	7,071	7,589	7,824
	Tangible fixed assets	32,426	24,551	37,563	39,788	41,980
	Total assets	88,563	92,451	91,002	93,092	94,943
	Short-term debt	10,071	13,396	9,036	8,911	8,800
	Total long-term debt	65	0	0	0	0
	Total liabilities	30,707	31,588	25,547	25,458	25,373
	Total equity	57,856	60,863	65,456	67,635	69,570
	Total liabilities & equity	88,563	92,451	91,002	93,092	94,943
	Key metrics	Dec-22	Dec-23	Dec-24F	Dec-25F	Dec-26F
	Revenue growth (%)	(0.2)	(4.6)	(11.5)	(1.6)	(1.5)
	Recurrent EPS growth (%)	(50.4)	86.5	(13.9)	(2.5)	(6.9)
	Gross margin (%)	8.9	12.3	12.6	12.4	12.2
	Operating EBITDA margin (%)	25.4	32.1	36.5	38.7	40.8
	Net profit margin (%)	2.2	4.5	4.4	4.3	4.1
	Dividend payout ratio (%)	155.7	43.4	0.0	51.3	53.6
	Capex/sales (%)	4.3	6.8	1.4	4.0	4.0
	Interest cover (x)	14.4	12.5	10.9	13.0	12.4

Source: Company data, RHB

Figure 1: Changes to our estimates

	New			Old			New/old (%)		
	2024F	2025F	2026F	2024F	2025F	2026F	2024F	2025F	2026F
Income statement (IDRbn)									
Total turnover	105,226	103,576	102,006	105,658	104,841	104,489	(0.4)	(1.2)	(2.4)
Gross profit	13,231	12,848	12,396	13,659	14,100	14,844	(3.1)	(8.9)	(16.5)
EBIT	6,045	5,775	5,430	6,444	6,940	7,709	(6.2)	(16.8)	(29.6)
Net profit	4,602	4,488	4,188	4,858	5,371	5,981	(5.3)	(16.4)	(30.0)
Key metrics									
EPS (IDR)	2,392	2,333	2,177	2,525	2,791	3,108			
Revenue growth (%)	(11.5)	(1.6)	(1.5)	(11.2)	(0.8)	(0.3)			
Gross margin (%)	12.6	12.4	12.2	12.9	13.4	14.2			
EBIT margin (%)	5.7	5.6	5.3	6.1	6.6	7.4			
Net profit margin (%)	4.4	4.3	4.1	4.6	5.1	5.7			

Source: Company data, RHB

Figure 2: RHB vs Street estimates

	RHB			Street			RHB/Street (%)		
	2024F	2025F	2026F	2024F	2025F	2026F	2024F	2025F	2026F
Income statement (IDRbn)									
Total turnover	105,226	103,576	102,006	111,320	118,729	125,226	94.5	87.2	81.5
Gross profit	13,231	12,848	12,396	13,169	13,541	13,769	100.5	94.9	90.0
EBIT	6,045	5,775	5,430	6,392	6,683	5,936	94.6	86.4	91.5
Net profit	4,602	4,488	4,188	4,567	4,890	4,360	100.8	91.8	96.1

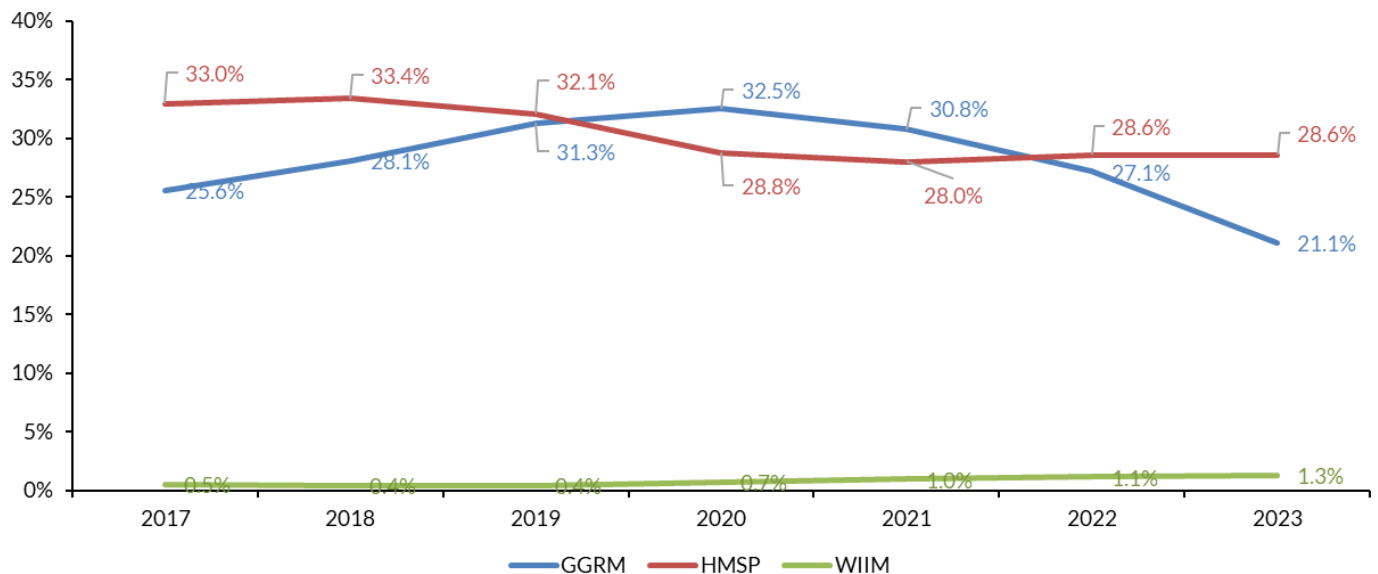
Source: Company data, Bloomberg, RHB

Figure 3: Peer comparison

Company	Ticker	Market cap (USDm)	P/E (x)	
			2024F	2025F
Hanjaya Mandala Sampoerna	HMSP IJ	5,001	9.9	8.3
Gudang Garam	GGRM IJ	2,036	7.5	7.7
Global weighted average		7,037	9.2	8.1

Source: Bloomberg, RHB

Figure 4: Market share trend of the tobacco players (2017-2023)



Source: Company data, RHB

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Figure 5: Tobacco retail prices in Apr-Jun 2024 (IDR)

Type	Brand	Cigarette	Apr 2024	MoM	May 2024	MoM	Jun 2024	MoM	Price/ stick	Mar-Jun 2024	YTD
Machine-rolled kretek cigarettes (SKM)											
Full flavour	GGRM	GG Signature (12 pcs)	25,000	0.0%	26,300	5.2%	26,300	0.0%	2,192	5.2%	3.1%
		GG International	26,300	0.0%	27,200	3.4%	27,200	0.0%	2,267	3.4%	7.1%
		Surya Pro (16 pcs)	33,100	0.0%	32,500	-1.8%	32,500	0.0%	2,031	-1.8%	0.3%
	Djarum	Surya Pro Exclusive	46,400	0.0%	46,400	0.0%	46,400	0.0%	2,900	0.0%	4.3%
		LA Bold (12 pcs)	23,700	0.9%	24,200	2.1%	24,900	2.9%	2,075	6.0%	11.7%
		Djarum Super	25,900	-0.4%	25,700	-0.8%	25,000	-2.7%	2,083	-3.8%	-2.0%
		LA Bold (20)	36,600	4.6%	38,600	5.5%	38,600	0.0%	1,930	10.3%	12.9%
Low tar low nicotine (LTLN)	GGRM	GG Signature Mild (16)	33,700	0.0%	33,700	0.0%	33,700	0.0%	2,106	0.0%	2.1%
		Surya Pro Mild	33,100	0.0%	33,100	0.0%	33,100	0.0%	2,069	0.0%	2.2%
		GG Move	24,500	0.0%	24,500	0.0%	24,500	0.0%	2,042	0.0%	0.0%
		GG Shiver	33,000	0.0%	33,000	0.0%	32,000	-3.0%	2,000	-3.0%	-3.0%
	HMSP	A Mild	34,000	0.0%	34,500	1.5%	34,700	0.6%	2,169	2.1%	6.8%
		Magnum Filter Mild	30,400	0.0%	30,400	0.0%	30,400	0.0%	1,900	0.0%	0.0%
		A Ultra Mild	31,900	0.6%	31,900	0.0%	31,900	0.0%	1,994	0.6%	4.6%
	WIIM	Diplomat Evo	25,500	0.0%	25,800	1.2%	25,000	-3.1%	1,563	-2.0%	1.2%
	Djarum	Djarum Super MILD	38,900	1.6%	38,900	0.0%	40,000	2.8%	2,000	4.4%	9.6%
Hand-rolled kretek cigarettes (SKT)	GGRM	Gudang Garam Merah	16,500	0.0%	16,500	0.0%	16,500	0.0%	1,375	0.0%	5.8%
	HMSP	Djisamsoe	21,000	0.0%	21,000	0.0%	21,000	0.0%	1,750	0.0%	0.0%
		Sampoerna Kretek	15,900	0.0%	15,500	-2.5%	15,000	-3.2%	1,250	-5.7%	-4.5%
Machine- rolled white cigarettes (SPM)	HMSP	Marlboro Red	45,200	1.6%	46,200	2.2%	47,300	2.4%	2,365	6.3%	12.1%
		Marlboro Filter Black	40,000	0.0%	40,500	1.3%	40,500	0.0%	2,025	1.3%	9.5%
	Bentoel Group	Dunhill	39,300	0.0%	38,900	-1.0%	38,900	0.0%	1,945	-1.0%	2.4%
		Lucky Strike	31,900	0.0%	31,500	-1.3%	30,000	-4.8%	1,500	-6.0%	-0.7%

Source: Company data, RHB

Emissions And ESG

Trend analysis

In FY23, Scope 1 emissions decreased to 108,917 tCO₂e from 145,060tCO₂e in 2020.

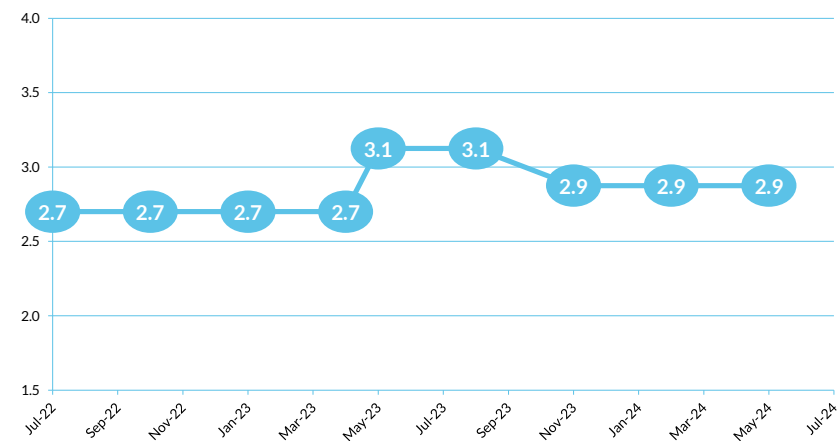
Emissions (tCO ₂ e)	Dec-21	Dec-22	Dec-23
Scope 1	148,006	132,042	108,917
Scope 2	na	na	na
Scope 3	na	na	na
Total emissions	148,006	132,042	108,917

Source: Company data, RHB

Latest ESG-Related Developments

- In 2023, GGRM spent IDR29.4bn on CSR programs, actively participated in Kediri's anniversary events like the Kediri Night Carnival, and donated tent facilities during *Idul Fitri*, Christmas, and New Year to support officers managing homecoming traffic in East and Central Java, enhancing road safety and community security.
- In 2023, GGRM's Occupational Health and Safety Management System (SMK3) was regularly audited by external auditor Sucofindo and achieved a rating of 93.97 percent (satisfactory) in the advanced assessment category, demonstrating compliance with government regulations. GGRM's environmental management practices include compliance with wastewater quality standards as per East Java's Regulation No. 72, 2013, monthly testing in collaboration with the National Accreditation Committee (KAN), biannual air quality tests by an external KAN laboratory in line with Government Regulation No. 22, 2021, and proper management of hazardous and toxic (B3) waste through licensed third parties and temporary storage under local government licenses.
- GGRM continued its greening program in Kediri utilizes diverse vegetation to enhance air quality through natural CO₂ absorption and aesthetically improve the operating area. Kediri and Gempol facilities were rated "Blue" under the Company Performance Rating Program in Environmental Management (PROPER). In 2023, GGRM utilised biomass, such as used tobacco packaging and wood packaging, as a source of fuel contributes to responsible energy management through the use of renewable resources.

ESG Rating History



Source: RHB

Recommendation Chart



Source: RHB, Bloomberg

Date	Recommendation	Target Price	Price
2024-05-05	Neutral	17,325	17,925
2023-11-22	Neutral	19,640	21,425
2023-10-31	Buy	31,700	23,275
2023-05-26	Buy	31,700	27,575
2021-04-01	Neutral	36,000	36,325
2020-12-11	Neutral	40,000	41,350
2020-04-29	Buy	60,000	45,000
2020-03-31	Buy	60,000	41,100
2019-11-05	Buy	66,000	53,925
2019-10-31	Buy	66,000	56,100
2019-09-20	Neutral	57,700	54,600
2019-09-16	Sell	57,700	54,600
2019-08-28	Buy	100,000	74,525
2019-08-01	Buy	100,000	74,625
2019-05-02	Buy	100,000	81,650

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
Take Profit:	Target price has been attained. Look to accumulate at lower levels
Sell:	Share price may fall by more than 10% over the next 12 months
Not Rated:	Stock is not within regular research coverage

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