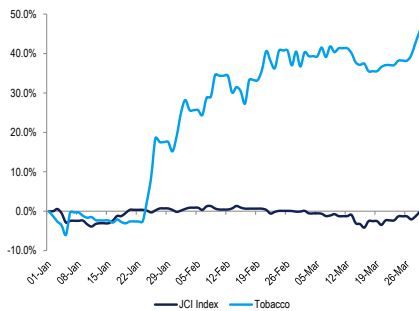


Sector Index Performance

	3M	6M	12M
Absolute	38.4%	31.7%	17.1%
Relative to JCI	39.6%	35.5%	19.6%



Summary Valuation Metrics

P/E (x)	2022F	2023F	2024F
GGRM IJ	15.8	9.5	8.6
HMSP IJ	20.4	16.3	14.7
EV/EBITDA (x)	2022F	2023F	2024F
GGRM IJ	8.1	5.4	4.7
HMSP IJ	13.2	10.4	9.3
Div. Yield	2022F	2023F	2024F
GGRM IJ	8.5%	3.8%	6.3%
HMSP IJ	5.2%	4.8%	6.1%

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Encouraging YTD price adjustment and outlook for cigarette sector

- HMSP/GGRM/Djarum have raised SKM prices (effective) by 6.0/8.4/9.1% YTD, affirming our thesis of margin expansion in FY23F.
- HMSP's new IQOS factory has the potential to be a significant growth driver for the company, leveraging on rising regional demand for HTU.
- Maintain our OW rating on sector; and BUY rating for HMSP & GGRM.

Encouraging price adjustments in 1Q23 YTD – supporting our margin expansion thesis

Throughout 1Q23, HMSP/GGRM/Djarum have increased its SKM effective ASP by 6.0/8.4/9.1% YTD (Fig. 2) and this was more aggressive than 1Q22's 4.7/2.8/3.0%. This implies that HMSP/GGRM only need to raise prices by 3.2/0.8% to fully pass on FY23 excise tax. In addition, this also suggests the current competition dynamics is much healthier as the top-3 players are prioritizing profitability rather than market share. With this, our margin expansion thesis remains firmly intact as we forecast HMSP/GGRM's GPM to improve from 15.3/8.8% in FY22F to 16.5/10.2% in FY23F.

HMSP's newly commissioned IQOS factory shall be the much needed growth driver

In-line with Philip Morris International's vision to be a majority (>50%) heated tobacco (HTU) business by FY25F from FY20/22's HTU contribution to total revenue of 25/32.1% and the strong growth of global HTU consumption (+c.16bn sticks incremental/year FY19-22), we believe HMSP's HTU production facility (15.5bn sticks capacity annually) would be able to ramp up quickly in terms of utilization. Based on PMI's disclosure that HTU's GPM is 10% point higher than conventional cigarettes (for PMI); and the export-oriented expectation of HTU sales of HMSP's factory, which would be exempt from the local excise – we expect HMSP's margins for HTU products to be significantly higher than HMSP's current margin profile. Additionally, we observed that governments tend to be more benign on HTU product' excise policy (Fig. 6-7, compared to conventional cigarette) possibly due to their claim on being less harmful to smokers' health. Our back of the envelope calculation indicates a potential +c.30% earnings booster by FY25F arising from this facility – which have yet to be included into our forecast as we seek further clarity from the company.

Maintain Overweight

We reiterate our Overweight rating on cigarette sector, amid attractive FY23F sector earnings growth of 38.5% yoy. In addition, we maintain our BUY calls for both HMSP/GGRM with TP of Rp1,275/30,750, pegged to 17.0/11.0x (at mean/-1.0sd below its 3Y mean). In addition, we see both HMSP/GGRM's FY23F ROE to improve by 550/350bps yoy to 29.6/9.0%. Risks to our call include competition from lower tier cigarette manufacturer and weaker than expected purchasing power leading to inability to fully pass on excise.

Fig. 1: Indonesia's tobacco summary

Ticker	Rating	Current price (Rp)	Target price (Rp)	P/E		ROE		Div. yield	
				2022F	2023F	2022F	2023F	2022F	2023F
HMSP	BUY	1,220	1,275	20.4	16.3	24.1%	29.6%	5.2%	4.8%
GGRM	BUY	26,450	30,750	15.8	9.5	5.5%	9.0%	8.5%	3.8%

Source: Company, Indo Premier

Fig. 2: Cigarette' retail price (in Rp) at MT

						% mom price chg				Total	YTD
Type	Sep-22	Dec-22	Jan-23	Feb-23	Mar-23	Dec-22	Jan-23	Feb-23	Mar-23	changes	
H.M. Sampoerna											
A Mild 16	28,500	29,750	32,150	32,000	32,000	4.4%	8.1%	-0.5%	0.0%	12.3%	7.6%
A Mild 12	22,250	23,750	24,300	24,600	24,600	6.7%	2.3%	1.2%	0.0%	10.6%	3.6%
DSS Magnum Mild 16	26,900	27,750	30,450	30,500	30,500	3.2%	9.7%	0.2%	0.0%	13.4%	9.9%
Magnum Filter 12*	19,600	21,950	22,600	22,600	23,624	12.0%	3.0%	0.0%	4.5%	20.5%	7.6%
Marlboro Filter Black 12*	19,950	21,100	21,550	21,550	22,590	5.8%	2.1%	0.0%	4.8%	13.2%	7.1%
Marlboro Filter Black 16*	26,750	27,400	27,850	27,850	28,887	2.4%	1.6%	0.0%	3.7%	8.0%	5.4%
SKM's simple average						5.7%	4.5%	0.2%	2.2%	13.0%	6.9%
Dji Sam Soe Kretek 12	19,550	19,600	19,550	19,550	19,550	0.3%	-0.3%	0.0%	0.0%	0.0%	-0.3%
Kretek Hijau 12	14,400	15,150	15,450	15,450	15,450	5.2%	2.0%	0.0%	0.0%	7.3%	2.0%
SKT's simple average						2.7%	0.9%	0.0%	0.0%	3.6%	0.9%
Marlboro Red 20	37,750	38,850	39,900	40,050	40,050	2.9%	2.7%	0.4%	0.0%	6.1%	3.1%
Marlboro Ice Burst 20	37,750	38,850	39,900	40,050	40,050	2.9%	2.7%	0.4%	0.0%	6.1%	3.1%
Marlboro Light 20	37,750	38,850	39,900	40,050	40,050	2.9%	2.7%	0.4%	0.0%	6.1%	3.1%
SPM's simple average						2.9%	2.7%	0.4%	0.0%	6.1%	3.1%
Gudang Garam											
Surya 16	28,400	30,600	31,950	31,950	33,850	7.7%	4.4%	0.0%	5.9%	19.2%	10.6%
Surya PRO 16	26,700	28,700	30,350	30,350	30,850	7.5%	5.7%	0.0%	1.6%	15.5%	7.5%
Surya PRO Mild 16	26,400	28,600	30,350	30,350	30,850	8.3%	6.1%	0.0%	1.6%	16.9%	7.9%
GG International Merah 12	22,500	23,600	24,400	24,400	25,100	4.9%	3.4%	0.0%	2.9%	11.6%	6.4%
GG Mild Shiver 16	27,500	29,050	31,200	31,200	32,800	5.6%	7.4%	0.0%	5.1%	19.3%	12.9%
GG Signature Mild (blue) 16	26,400	28,800	31,200	31,200	32,800	9.1%	8.3%	0.0%	5.1%	24.2%	13.9%
GG Kretek Move 12	19,200	21,600	22,750	22,750	23,700	12.5%	5.3%	0.0%	4.2%	23.4%	9.7%
Simple average						8.0%	5.8%	0.0%	3.8%	18.6%	9.8%
Djarum											
Djarum Super 16	28,600	30,900	32,100	32,500	34,250	8.0%	3.9%	1.2%	5.4%	19.8%	10.8%
Djarum Super Mld Black 16	28,500	30,000	31,600	31,600	32,850	5.3%	5.3%	0.0%	4.0%	15.3%	9.5%
Djarum Coklat Filter 12	21,250	21,700	22,000	22,600	25,250	2.1%	1.4%	2.7%	11.7%	18.8%	16.4%
LA Bold 16	27,500	27,500	28,500	30,000	30,000	0.0%	3.6%	5.3%	0.0%	9.1%	9.1%
SKM's Simple average						3.9%	3.6%	2.3%	5.3%	15.7%	11.4%
Djarum Kretek Coklat 12	14,900	15,200	15,300	15,300	15,300	2.0%	0.7%	0.0%	0.0%	2.7%	0.7%
SKT's Simple average						3.5%	3.1%	1.9%	4.4%	13.6%	9.6%
Other brands											
Lucky Strike Filters 20	29,850	29,900	29,850	29,850	29,850	0.2%	-0.2%	0.0%	0.0%	0.0%	-0.2%
Dunhill Fine Cut Filter 16	26,200	26,500	26,350	26,300	26,350	1.1%	-0.6%	-0.2%	0.2%	0.6%	-0.6%
Clas Mild 16	23,950	26,750	26,950	27,000	27,000	11.7%	0.7%	0.2%	0.0%	12.7%	0.9%
Clas Mild Silver 16	22,700	23,900	24,600	24,600	24,600	5.3%	2.9%	0.0%	0.0%	8.4%	2.9%
Simple average						4.6%	0.7%	0.0%	0.0%	5.4%	0.8%

Source: Alfagift, Klikindomaret, Indo Premier

*HMSP's price adjustment for end of Mar23 would be effective on 04 Apr 23 for certain SKUs

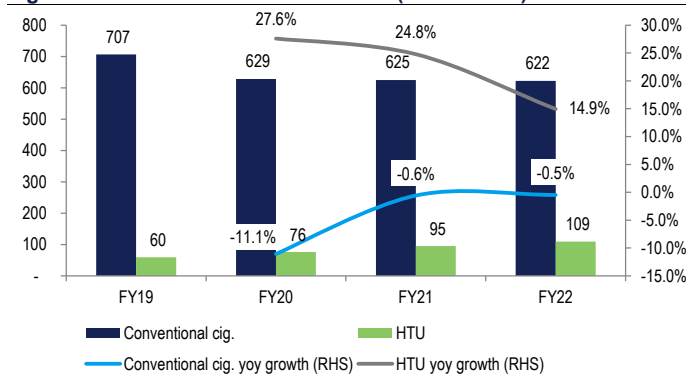
Fig. 3: Indonesia's SKM price adjustment in YTD basis

	IPS FY23F ASP changes	YTD effective SKM's ASP changes			
		Jan-23	Feb-23	Mar-23	YTD changes
HMSP*	9.9%	4.4%	0.1%	7.1%	11.9%
GGRM	11.9%	5.4%	0.0%	2.9%	8.4%
Djarum	N/A	3.4%	1.8%	3.6%	9.1%

Sources: Indo Premier

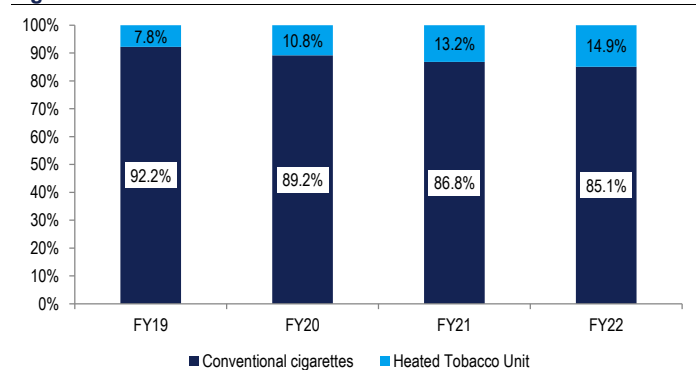
*HMSP's price adjustment for end of Mar23 would be effective on 04 Apr 23 for certain SKUs

Fig. 4: PMI's sales volume breakdown (in bn sticks)



Source: Philip Morris International, Indo Premier

Fig. 5: PMI's sales volume contribution



Source: Philip Morris International, Indo Premier

Fig. 6: Indonesia's tobacco excise tax structure

(In Rp/stick)	2022	2023	2024
Heets tobacco product*	705	750	799
yoy growth		6.5%	6.5%
Terea tobacco product**	854	909	968
yoy growth		6.5%	6.5%
SKM Tier-1	985	1,098	1,224
yoy growth		11.5%	11.5%

Source: Ministry of Finance Indonesia, Indo Premier

*0.26gram/stick

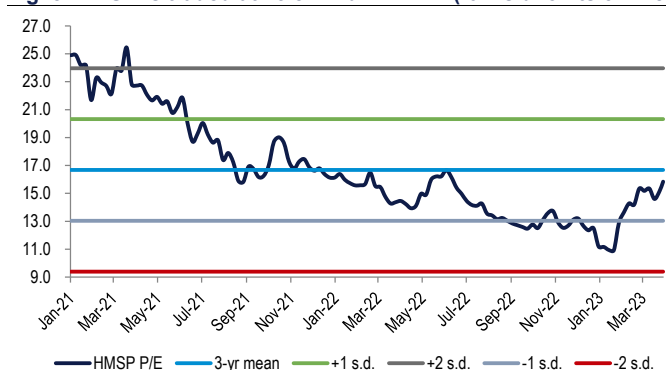
**0.32gram/stick

Fig. 7: Philippines' tobacco excise tax structure

(In Peso/stick)	2020	2021	2022	2023	2024
Heated tobacco product	25.0	27.5	30.0	32.5	34.1
yoy growth		10.0%	9.1%	8.3%	5.0%
Cigarettes packed by machine	45.0	50.0	55.0	60.0	63.0
yoy growth		11.1%	10.0%	9.1%	5.0%

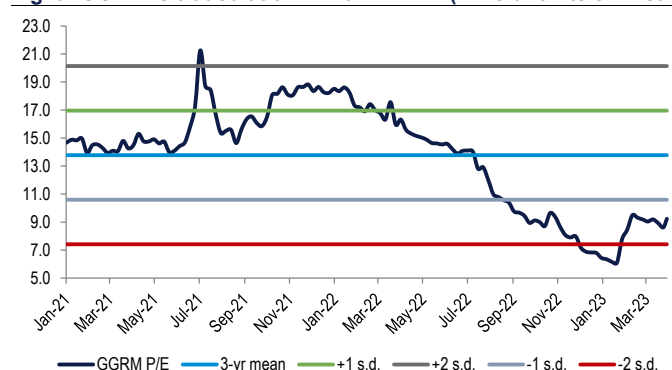
Source: Department of Finance Philippines, Indo Premier

Fig. 8: HMSP is traded at 15.8x fwd. 12M PE (-0.2 s.d. of its 3Y mean)



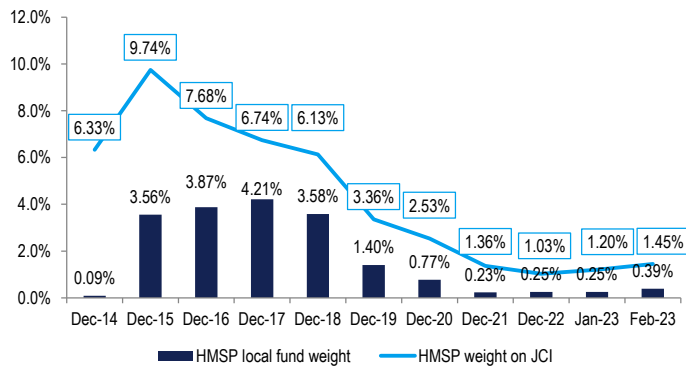
Source: Bloomberg, Indo Premier

Fig. 9: GGRM is traded at 9.2x fwd. 12M PE (-1.4s.d. of its 3Y mean)



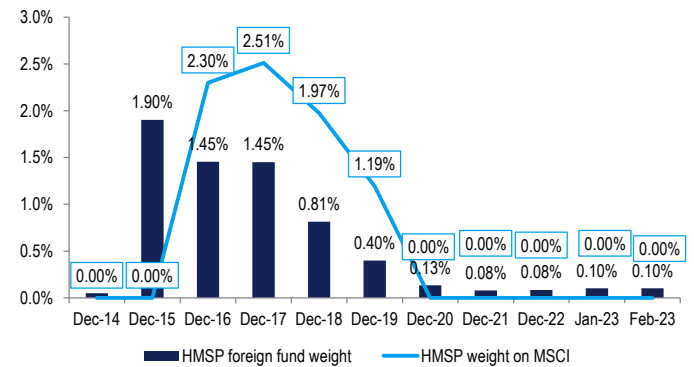
Source: Bloomberg, Indo Premier

Fig. 10: HMSP's local fund weight vs. JCI



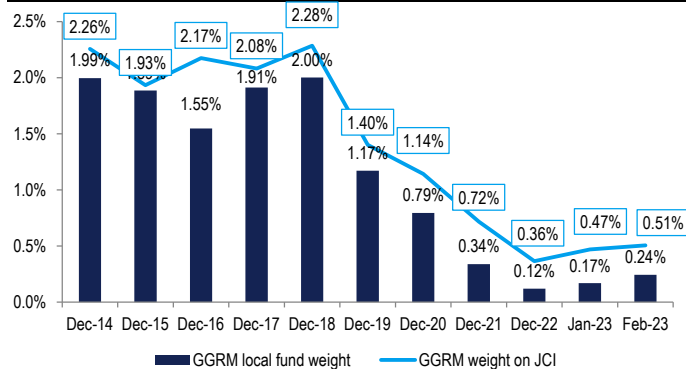
Source: KSEI, Indo Premier

Fig. 11: HMSP's foreign fund weight vs. MSCI



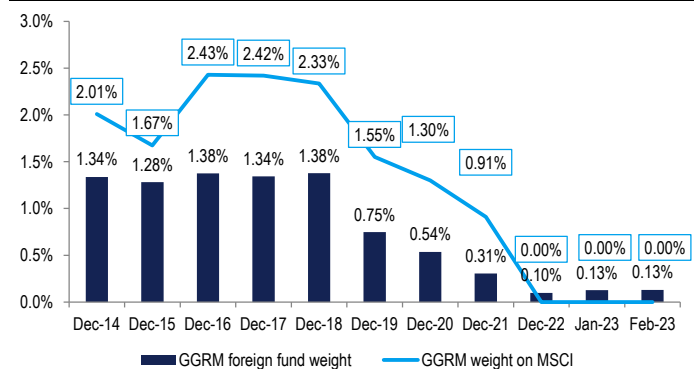
Source: KSEI, Indo Premier

Fig. 12: GGRM's local fund weight vs. JCI



Source: KSEI, Indo Premier

Fig. 13: GGRM's foreign fund weight vs. MSCI



Source: KSEI, Indo Premier

SECTOR RATINGS

- OVERWEIGHT : An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation
- NEUTRAL : A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation
- UNDERWEIGHT : An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation

COMPANY 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

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