

Monday, 23 March 2020

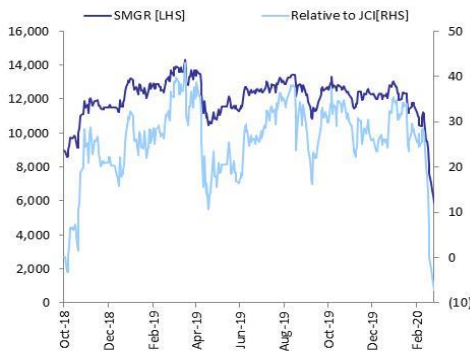
**OVERWEIGHT**

**Maintain**

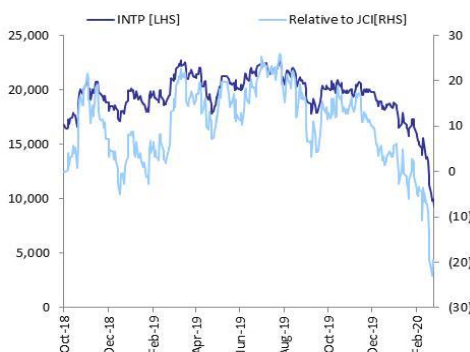
# Cement

**Flattish growth might be offset by higher ASP**

SMGR relative to JCI Index



INTP relative to JCI Index



Source : Bloomberg

We expect a similar pattern for cement demand this year as in 2019 (the political year) with demand reined in by the COVID-19 outbreak in 1Q20 followed by Ramadhan and the subsequent holidays. The correlation between cement demand and GDP growth over the past five years is 60.7% compared to 82.5% over the past 12 years, as reflected in only 0.3%yoy growth in cement consumption in FY19 despite 5.05% GDP growth. We believe the sector has medium-to-high risk from the ongoing crisis.

**Similar demand pattern expected in 2020.** We believe the COVID-19 outbreak will have a medium-to-high impact on the sector as cement demand will be affected directly and indirectly by the government's move to curtail the people's activities. Demand for bagged cement might be soft as most people will postpone their plans for house hunting and renovation. By comparison, demand for bulk cement will be affected by delays in infrastructure development for both private and government projects. Delays might also result from cuts in the infrastructure budget as the government is focusing on overcoming the COVID-19 outbreak. As such, we believe that cement demand might show a similar pattern as in FY19 (the political year), with demand also dampened by the heavy rainfall in the first three months of the year. The correlation between cement demand and GDP growth over the past five years is 60.7% compared to 82.5% over the past 12 years, as reflected in only 0.3%yoy growth in cement consumption in FY19 despite 5.05% GDP growth. The two biggest players in the industry, SMGR and INTP, target flattish sales volume growth this year at 0%-2%yoy. As they control almost 80% of the cement demand, the sector's growth will show a similar rate of growth. However, weak sales growth might be offset by higher ASP. The two players raised ASP by 3%-6%yoy in FY19 and expect to have similar pattern this year.

**Lower oil and coal prices to be offset by IDR weakness.** The fuel cost is 40% of the COGS and the packing cost is ~8% of the COGS. Hence, the USD exposure is 45-50% of the cost. However, the lower oil and coal prices have been offset by IDR weakness against the USD. This is also reflected in the stable retail price of fuel sold by Pertamina and other fuel sellers.

**Strong balance sheets.** INTP is a zero-debt company with a huge amount of cash. INTP's cash stood at IDR7.7tn as of Dec19, higher than IDR7.2tn as of Dec18. By comparison, SMGR had IDR28.0tn of debt as of Dec19, resulting in a 0.83x debt-to-equity ratio and 1.90x interest coverage. The company has sizable debt as it acquired a 98.3% stake in SMCB, known as Solusi Bangun Indonesia (SBI), in early FY19. Back then, the debt cost reached 11.7% including the hedging cost as the debts were not denominated in IDR. However, during the year, SMGR undertook refinancing. Also helped by falling interest rates, the debt cost fell to around 8.5%pa. The refinancing includes the issuance of bonds amounting to IDR4.0tn with a coupon rate of 9%pa and bank loans amounting to IDR9.0tn with a cost based on JIBOR 3 month + 1.85%. Using Bloomberg data, the JIBOR 3-month rate fell significantly to 4.88% pa as of 20 Mar20 compared to 7.11%pa as of 20 Mar19. The downtrend in interest rates will benefit companies which issued debt with floating interest rates such as SMGR.

**Medium-to-high risks assessment.** We remain overweight on the sector given: 1) its attractive valuation, 2) less risk of a price war with room for ASP to increase further, 3) healthy balance sheets, 4) benefiting from interest rate cuts and 4) generous dividend payments. INTP's dividend payout reached 176.7% last year, while SMGR's reached 40%.



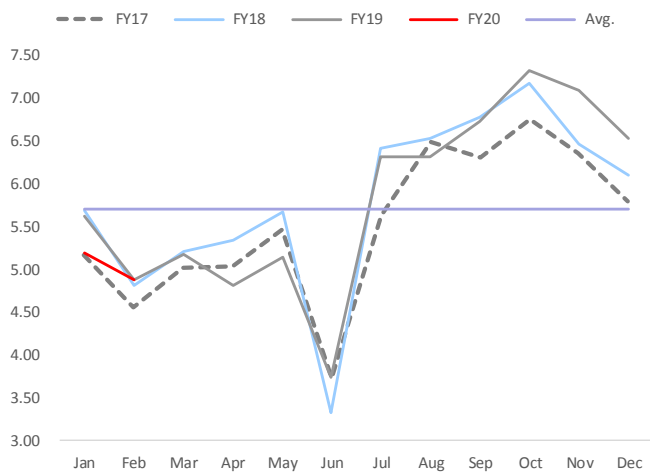
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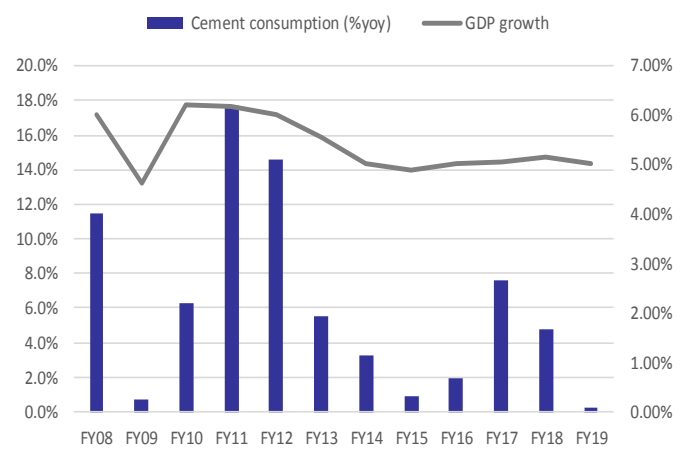
Company	Ticker	Rec	Target	Market	P/E (x)		P/BV (x)		ROE (%)
			Price (Rp)	Cap. (RpBn)	2019F	2020F	2019F	2020F	2020F
Semen Indonesia	SMGR IJ	BUY	13,100	41,817.2	23.6	17.7	1.3	1.3	7.2
Indocement	INTP IJ	BUY	17,600	40,953.7	25.2	22.5	1.7	1.7	7.7

**Exhibit 1. Monthly Domestic Cement Consumption**



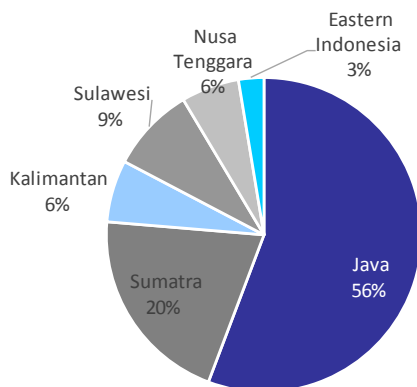
Source: Cement Association

**Exhibit 2. Correlation between Cement Demand and GDP Growth**



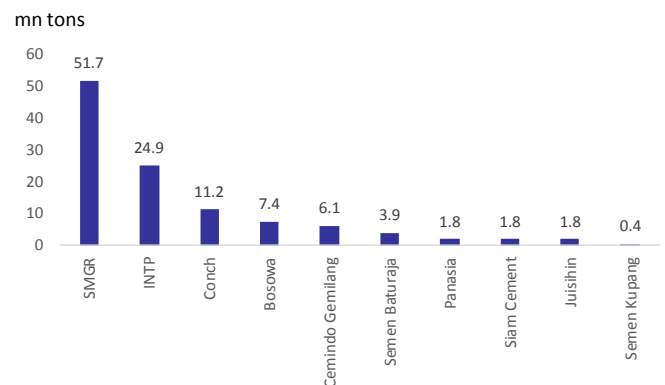
Source: Indonesia Statistic

**Exhibit 3. Cement Demand by Region in FY19**



Source: Cement Association

**Exhibit 4. Indonesia Cement Player Breakdown**



Source: Cement Association

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