

### FLASH NOTE: ADHI Revised Down Financial Performance Target 2016

October 26<sup>th</sup>, 2016

State-owned construction company, PT Adhi Karya (Persero) Tbk (ADHI) has cut its financial performance target in 2016 as the development of light rail transit/LRT is not expected to meet the company's forecast. ADHI's Financial Director said that the new contract target in 2016 will be around IDR 18 Tn, lower than the initial estimate of IDR 25 Tn. The management put the initial estimate of IDR 25 Tn because they expect the LRT progress can reach up to IDR 5 Tn, however, after some delays related to funding and poor new contract achievements, the company finally has to revise down its target. From January to September 2016, the company has only won new contracts amounting to IDR 11 Tn. Therefore, with the new contract target of IDR 18 Tn, companies need to look for a contract of approximately IDR 7 Tn in the rest of the time in 2016. With this revision, ADHI is targeting sales of around IDR 12.3 Tn or lower than the initial target of IDR 20 Tn. The net profit is also expected to be lower than the initial target of IDR 750 Bn. LRT project is important because it is not only a matter of potential revenue of IDR 34 Tn to be booked over the next three years, but also generating works from the Transit Oriented Development (TOD) for 17 stations along the LRT route. ADHI will directly benefit from construction contracts for the TOD and indirectly through its subsidiary, PT Adhi Persada Properti, which is most likely become the concession owner of those TODs with total investment of around IDR 15 Tn. This will be the next long-term catalyst for ADHI.

**Our view: Previously, we assumed ADHI's valuation gap compare to its peers to narrow due to the better earnings visibility from the LRT project and the completion of the kitchen sinking initiative on EPC business. Nonetheless, recent development of LRT project may result in lower-than-expected contract value and earnings delivery, negating our expectation of a narrowing discount. ADHI is trading at 45% discount to its peers. We recommend to take wait and see position while waiting for the Q3 financial performance to be released and further clarity on LRT Project backed by Presidential Decree 65/2016. The valuation according to the changes on management guidance is still under review.**

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