

13th October 2011

PT Indofood CBP Sukses Makmur Tbk

Strong Franchise With Proven Track Record

HOLD

Domestic market to remain strong & resilient

Growth in F&B industry has been driven by huge domestic market, growing economy with growing income which drives consumption. As a result, household consumption, in which 51% is spent on food, has been growing at 16.5% CAGR since 2005. With the economy is set to continue its strong growth outlook, and a higher disposable income and thus purchasing power, the domestic food & beverage industry is set to continue its double digit growth. Such development will be beneficial for PT Indofood CBP (ICBP), as a dominant player in the Indonesian F&B industry.

Superb brand that needs no introduction

ICBP is a major player in the F&B industry especially in the packaged food segment. One of the core reason is that its products are well known across the board due to its innovative, quality and taste of its products. For example, products such as Indomie—where most people refer to instant noodle as Indomie, Pop mie and Indomilk have such a strong brand equity which bring along tremendous brand loyalty. Therefore giving ICBP the edge over its competitors in terms of pricing power and margin. The company also has large variety of household food packaged products which cater noodle, diary, food seasonings and nutritional food segment.

Wide distribution network

ICBP has been able to leverage off ISM wide distribution network, which gives them access to 275.000 grocers and 1.100 stock point. In addition, it has access to thousands of modern retail channel such as Indomaret to distribute its products. Such network gives consumer easy access to ICBP products. In addition it also has 35 production facilities across Indonesia. Large production capacities which are spread across Indonesia combined with its extensive distribution network gives ICBP economies of scale. In future, ICBP is looking to boost its products penetration into the villages area, where penetration of fast moving consumer products is still low at 27.9%

Initiating coverage with HOLD recommendation

Based on our valuation using DCF model with WACC set at 13.2% and long term growth rate at 6%, we have derived an intrinsic value of IDR 5,400 for ICBP. At this valuation, ICBP will be trading at P/E 2011E 16x and P/E 2012F 14X. In comparison with its local peers which has an average P/E 2011E of 20.8x, ICBP is trading on par. ICBP is looking well from the fundamental perspective. It has superb brands which is supported by extensive distribution channels & proven management. However at current stock price, it is trading at a premium to our valuation.

Jansen Kustianto

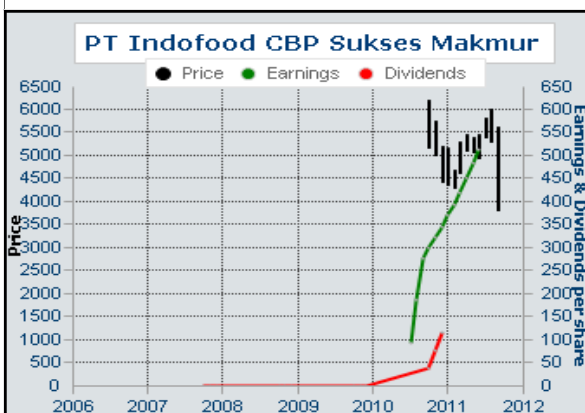
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Ticker: ICBP

Stock Data

Sector	Consumer
Price (October 13th 2011)	5,350
Target Price 2011	5,400
EPS 2010A	292
EPS 2011E	346
EPS 2012F	375
Market Cap (IDR)	31.1T
Issued Shares (bn)	5.83
P/E 2010	18
P/E 2011—Estimate	15.5
P/E 2012—Forecast	14.3
Three Years Average (annualized historical)	
Sales Growth (%)	24
Net Profit Growth (%)	212
ROE (%)	28
Dividend Payout Ratio (%)	N/A
Major Shareholders	
PT Indofood Sukses Makmur Tbk	80%
Public	20%



Source: www.corporateinformation.com

REVENUE FORECAST	2011E	2012F	2013F
Revenue (IDR in bn)	19,666	21,830	23,969
Gross Margin (%)	26.5	26.7	26.9
Revenue Growth (%)	9.5	11	9.8

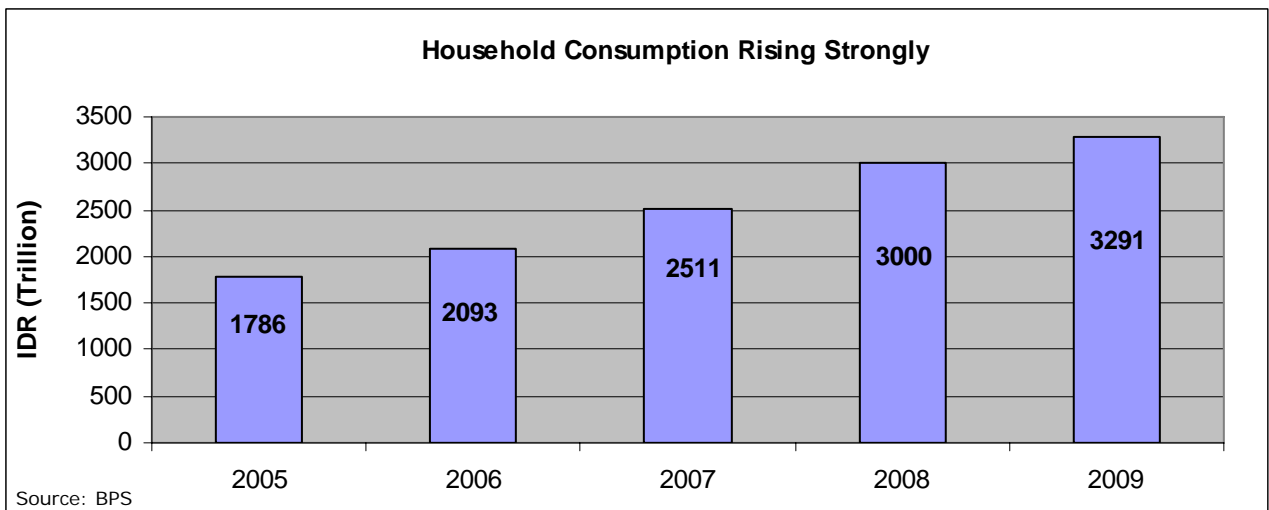
The domestic purchasing power will remain strong, thus creating positive environment for ICBP.

We see that the Indonesian economy is to remain strong due to the structural and the strong foundation it has. Indonesia economic growth should remain solid as domestic consumption made up almost 75% of Indonesia total GDP. Therefore it is less affected by the negative issues related to the global economy. Indonesia relatively young demographic and rising middle class are the driver behind its strong domestic consumption.

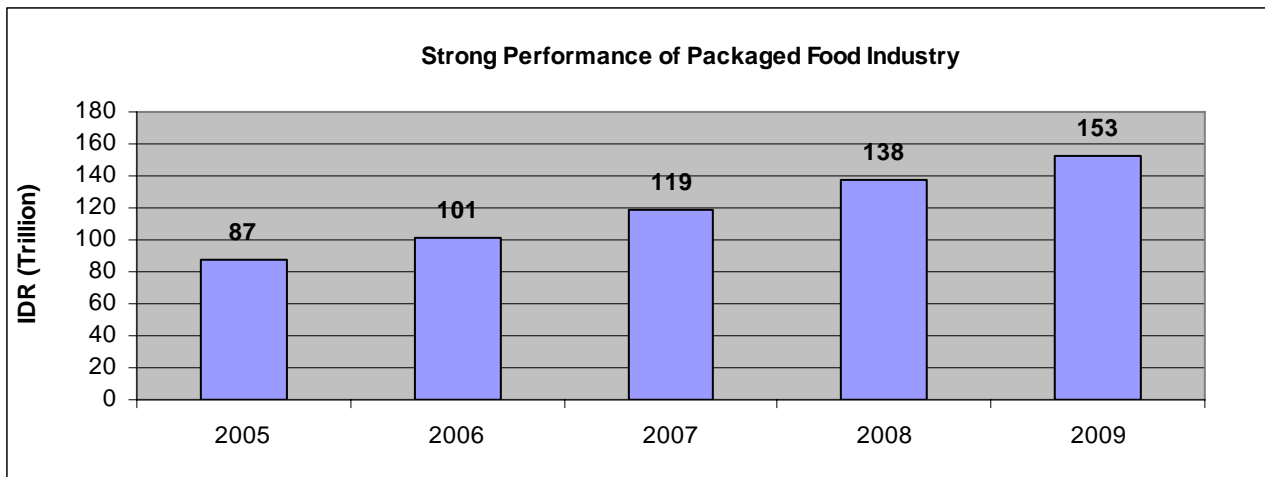
As the economic growth is to remain strong, per capita income has risen 19.3% CAGR since 2005 and should rise alongside strong economic growth.



As national income rises, so does household expenditure. Household expenditure grew at 16.5% CAGR since 2005. According to BPS, more than 50% of household expenditure is on food. As a result, packaged food industry has experienced solid growth of 15.5% CAGR since 2005. Demand for packaged food products is seen as a necessity and is resilient to economic downturn. These indicators create positive environment for ICBP.



Packaged food industry which includes segments such as noodles, dairy products, ice cream, sauces, dressings, sweet & savory snacks, and baby food; where ICBP have products catering to all those segments, remained resilient even during the global financial crisis in 2008-2009. Therefore, we are expecting that revenue of the industry will continue to show growth in the future, due to Indonesia's robust economic growth, higher purchasing power and it's resilient to any economic downturn.



Source: Euromonitor International & ICBP prospectus

Benign inflation translated to stable consumer purchasing power

Inflation problem is one of the main risk which could dampen purchasing power and thus reducing demand for consumer based products. Inflation currently stands at 4.61% YoY as of September 2011. Food & food materials are the highest contributor to inflation. However as commodities price tend to be declining since the beginning of the year, we see inflation to remain stable and be within the area of 5% to 5.5% for 2011. Therefore we think there should be no negative effect to the consumer' purchasing power.

ICBP snapshot

ICBP is the biggest players in the Indonesia food and beverage industry. It has a long presence in the Indonesian food industry and its brands are household names and well known among the population. It focuses on the packaged food segment covering noodle, dairy, food seasoning, snack and nutrition products. ICBP household brands are easily accessible by Indonesian population thanks to its extensive distribution network and its production facilities which are spread across Java, Kalimantan, Sumatera and Sulawesi island.

Division	Products	Competitors
Noodle	Indomie, Supermi, Sarimi, Pop mie	Wings Group, ABC food
Dairy	Indomilk, Cap enak, Tiga sapi, Indoeskrim, Kremer	PT Frisian Flag, Ultrajaya, PT Nestle
Food seasoning	Indofood, Piring Lombok	PT Heinz ABC, Unilever Indonesia
Snack	Chitato, Chiki, Lays, Cheetos, Qtela, Trenz, Wonderland	TPS Food, Garudafood
Nutrition	Promina, SUN	PT Nestle Indonesia, PT Nutricia Indonesia, Kalbe Farma

High varieties of brand portfolio—source from ICBP 2010 annual report:

Noodles



Dairy



Food Seasonings



Snack Food



Nutrition & Special Food



Revenue breakdown per division—as a % of total revenue

	2009	2010
Noodles	71.5	69.9
Dairy	19.3	18.8
Food Seasonings	3.5	4.3
Snack Food	4.7	5.5
Nutrition & Special Food	2.6	2.7

Source: Company's data

Revenue growth YoY 2009-2010

	YoY growth (%)
Noodles	7.5
Dairy	7.4
Food Seasonings	35
Snack Food	26.8
Nutrition & Special Food	12

Source: Company's data

Strong branding power

One of the core reason for ICBP becoming a major player in the packaged food industry is due to its innovative, quality, taste and consistency of its products. Combined with management ability to promote its brand and strengthening its brand positioning, creates such a strong brand equity associated to ICBP products. A testament to ICBP brand power is the fact that most consumer referring to instant noodle as "Indomie", which is ICBP main brand in the noodles division. This translate into ICBP dominant market share in the instant noodle market, where it controls around 75% of the total market. ICBP other flagship brand such as "Indomilk" and most of its brands do also have tremendous brand loyalty in the eyes of its consumer. Having such a strong brand power enable ICBP to become the market leader and price mover, especially within the instant noodle market. Furthermore, strong brand power has given ICBP advantages over its competitors in terms of pricing and maintaining margin in the case of rising cost of materials and also in terms of generating revenue.

Leveraging off PT Indofood Sukses Makmur (ISM) distribution channel to create extensive network and economies of scale

ICBP has been able to leverage off ISM extensive distribution network to market its strong varieties of brand. Its distribution network gives ICBP access to 275.000 grocers and around 1.100 stock point across Indonesia, where most of these stock points are located in close proximities of grocers & traditional markets. By having such distribution system, ICBP can have faster movement in terms of goods and inventory therefore ensuring products availability and less distribution and transportation cost. In addition, ICBP also has 35 production facilities—16 instant noodles, 3 seasonings, 4 dairy, 2 food seasonings, 3 snacks, 1 nutrition, 6 packaging facilities, which are spread across Indonesia. By having large number of production facilities which are spread across Indonesia, and the ability to utilize access to PT Indofood Sukses Makmur' excellent network in sourcing ICBP raw materials, gives the company economies of scale over its competitors.

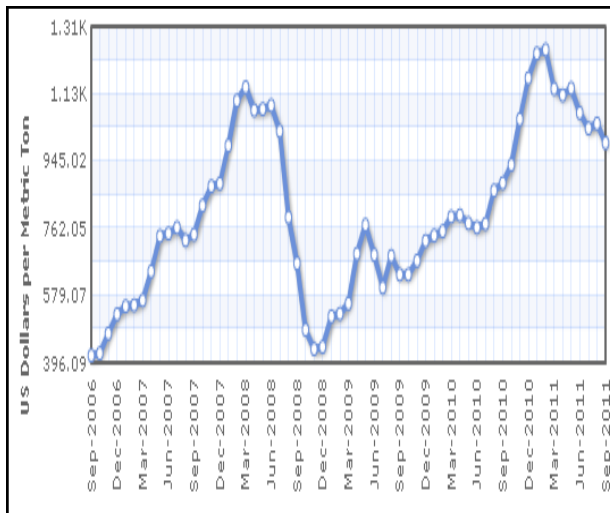
In the next few years, ICBP is looking to boost revenue by improving its distribution network further, in order to boost its product penetration into the villages area, where penetration of fast moving consumer goods is still relatively low at 27.9% in 2009, according to Nielsen report. ICBP is also planning to build new facilities and improve capacities at current facilities to keep up with rising demand. It has plan to build two new instant noodle facilities in Palembang and Semarang, whilst currently consolidating its Jakarta facilities. It is also in the process of building new dairy facilities in East Java, sauce facilities in Semarang and undergoes several capacity upgrades in its existing facilities.

We expect margin & profitability to remain solid

Cost of raw material is the main cost component, accounted to around 85% of total cost of goods sold. Therefore any sudden increase in commodities price, especially wheat, palm oil and sugar which are the main components of raw material for ICBP, could impact upon its profitability. We see commodities price such as wheat, palm oil and sugar to remain subdued until the end of year, after a period of high price during the end of 2010 and early 2011, which also contributes to a high inflation environment. Since then, prices tend to be declining, hence inflation is also under control at 4.61% YoY as of September 2011. ICBP source its main raw materials such as flour—where wheat is the main ingredients and cooking oil from its parent company, ISM. Therefore availability should not be a concern.

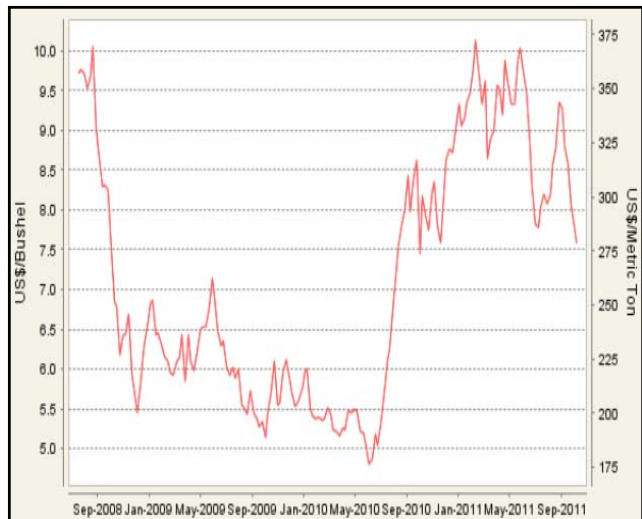
Through several price increase on its selling price almost across all division, ICBP managed to maintain and slightly improved its profit margin from 9% in 1H2010 to 10.5% during 1H2011 amidst rising cost of material. As the outlook for the commodities price remains stable for the time being, we don't think there will be another cost pressure and as a result, it seems less likely that there will be another price increase on ICBP products for 2011. We forecast that net profit margin should remain on average above 10%, and should there be another extraordinary rise on the cost of raw materials, which is remain unlikely for the time being due to the slowing down of global economy meaning that commodities price will remain under pressure, ICBP has the ability to increase its selling price without losing too much of its market share and revenue wise. This is due to its strong brand equity which makes it a dominant player in its industry.

CPO—Malaysia Future Price



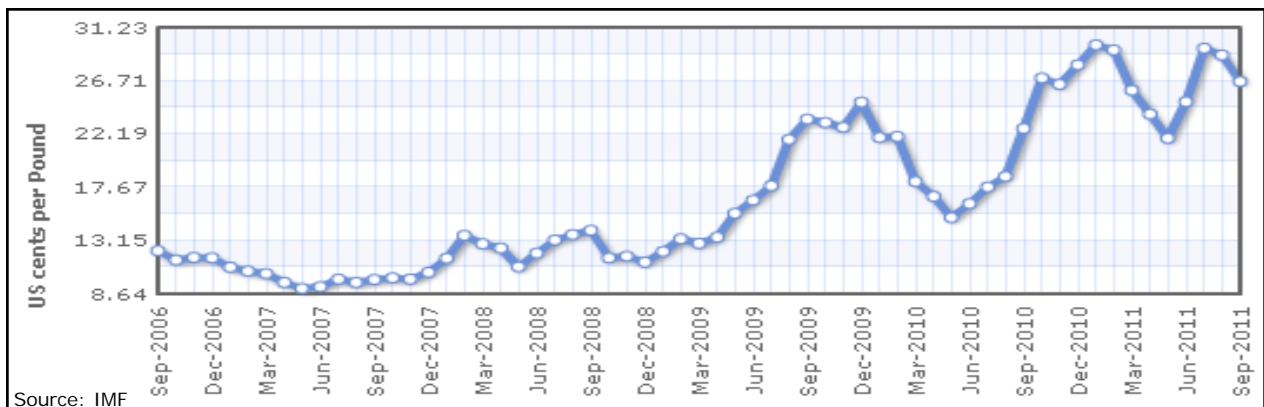
Source: IMF

Wheat price—US Hard wheat



Source: US Wheat Associate

Sugar price –CSCE Index



Source: IMF

1H 2011 result is encouraging

ICBP performed well during 1H2011. Net profit grew 23.7% to IDR 990 billion supported by growth in revenue of 5.7% to IDR 9.4 trillion driven by higher demand for its products and improvement in the company's margin, where net income margin improved to 10.5% during 1H2011, compared to 9% during 1H2010, as a result of several increase in the average selling price of ICBP products across all segments. Overall it's a good performance by ICBP considering the environment of high commodities price, and high inflation early in the year. The company's balance sheet has improved in 1H2011, with cash balance of IDR 3.9 trillion, and the company has been able to reduce its debt by 28.7% from IDR 526.3 billion to IDR 375.4 billion in 1H2011. This is partly attributable to ICBP good cash flow management which shows positive operating cash flow consistently. Therefore the company has a nice looking capital structure and healthy balance sheet to support its expansion plan.

Indicators are there for a positive FY 2011 result

We expect conditions to be better for ICBP in the second half of 2011, as it usually the busiest period for food producers due to festivities and holiday season such as Ramadhan and Christmas. In addition, the company is also less likely to increase its selling price of its products during 2H2011 as commodities price has tended to weaken since its high level early in the year. Therefore we should see an improvement in ICBP sales volume, especially in the noodles division.

Income statement (IDR billion)

	1H2010	1H2011	% (YoY)
Revenue	8,918	9,423	5.7
Gross Profit	2,400	2,425	1.1
Operating Profit	1,220	1,315	7.8
Net Profit	800	990	23.7

Company's margin (%)

	1H2010	1H2011	% (YoY)
Gross Margin	26.9	25.7	(4.5)
Operating Margin	13.7	14	2.2
Net Profit Margin	9	10.5	16.7

Balance Sheet (IDR billion)

	1H2010	1H2011	% (YoY)
Cash & Equivalent	3,408	3,939	15.6
Total Assets	13,361	14,540	8.8
Total Funded Debt	526	375	28.7
Total Equity	9,362	9,735	4

Cash Flow (IDR billion)

	1H2010	1H2011	% (YoY)
Operating Cash Flow	1,093	877	19.8
Cash Flow from Investing activities	(522)	(227)	(56.6)

Source: Company's data

Potential challenges in the future

Potential challenges are the increasing competition in the market as the packaged food industry is a very competitive industry. Therefore, more competition will have an impact on pricing structure which could translate upon pressure on ICBP profit margin & decline in market share. Inflation could also potentially derail consumer purchasing power, as expected increase in electricity tariff, petrol and basic food price might hamper affordability and purchasing power. Thus could impact on lower demand for ICBP products. Another potential challenge is the fluctuation and volatility of commodities price which has strong impact on the company's cost of raw materials. The fact that ICBP does not do hedging on its contracts added an extra risk in a period of rising commodities price and in an environment where ICBP could not increase its selling price

How we derived our valuation

We derived our valuation using DCF method. The valuation is based on projected sales growth of 10.1% CAGR by 2013, and a long term terminal growth rate of 6%, with 13.2% as the firm's WACC. Based on our valuation, we have derived an intrinsic value of IDR 5,400 for ICBP. At this target price, ICBP is trading on P/E multiple of 16x based on 2011 estimated net profit, and P/E multiple of 14x based on 2012 forecasted net profit. The company has strong fundamental highlighted by its strong brand power which is supported by a solid distribution network and structure as well as healthy balance sheet to support its expansion plan. ICBP has consistently growing and has a track record of strong performance in the past. We see the growth pattern will continue due to its fundamental and Indonesia strong and resilient domestic market. ICBP is in a good position to leverage off such favorable environment, and therefore is a good investment play with strong exposure to domestic market. Although, at current share price of IDR 5,350 valuation is not that attractive compared to our intrinsic valuation of IDR 5,400. Thus we recommend to hold.

ICBP has positive earning multiples comparison towards its local listed competitors

	EPS 2010A	EPS2011F	P/E 2011F
PT Unilever Indonesia	444	516	30.7
PT Mayora Indah	631	759	18.4
PT Nippon Indosari	99	122	25.8
PT Kalbe Farma	126	157	22
PT Ultrajaya Milk	37	50	20.2
PT Tiga Pilar Food	45	52	13.1
PT Indofood CBP	292	346	15.5
Average			20.8

Source: Bloomberg, SinarMas Sekuritas. P/E 2011F calculation is based on closing price of October 13th 2011

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<i>Fiscal Year End</i>	2009	2010	2011E	2012F	2013F
Income Statement (IDR bn)					
Sales Revenue	16,333	17,960	19,666	21,830	23,969
Cost of Goods Sold	(12,420)	(12,993)	(14,455)	(16,001)	(17,521)
Gross Profit	3,913	4,967	5,212	5,829	6,448
Operating Expenses	(2,335)	(2,535)	(2,458)	(2,772)	(2,900)
Operating Income	1,578	2,432	2,753	3,056	3,547
EPS		292	346	375	433
Net Interest Income (Expenses)	(77)	(84)	(67)	(61)	(55)
Other Income (Expenses)	103	171	215	195	178
Income Before Tax	1,603	2,519	2,901	3,190	3,670
Income Tax Expense	430	691	783	893	1,028
Minority Interest	94	124	98	109	120
Net Income	1,078	1,704	2,020	2,188	2,523
Balance Sheet (IDR bn)					
Cash & Cash Equivalents	705	3,427	3,135	3,908	4,184
Account Receivables	1,448	1,954	2,203	2,358	2,756
Inventories	1,311	1,422	1,573	1,725	2,277
Other Current Assets	337	214	295	284	407
Net Fixed Assets	2,180	2,305	3,316	4,017	4,693
Total Non-Current Assets	6,423	6,343	8,429	9,693	10,925
Total Assets	10,224	13,361	15,635	17,967	20,550
Current Liabilities	7,378	2,701	3,153	3,581	3,680
Long-Term Liabilities	1,221	1,298	1,428	1,560	1,970
Total Liabilities	8,599	3,999	4,581	5,141	5,650
Shareholder's Equity	1,279	8,920	11,054	12,826	14,900
Minority Interest	346	442	541	650	770
Total Equity & Liabilities	10,224	13,361	15,635	17,967	20,550
Cash Flow (bn)					
Operating Cash flow	1,670	2,248	2,415	2,853	2,193
Net Capex	(330)	(353)	(1,320)	(1,075)	(1,153)
Other Investing Items	22	(292)	(1,074)	(562)	(556)
Free Cash Flow	1,362	1,603	21	1,216	484
Dividends paid	(28)	(144)	(426)	(525)	(569)
Other financing items	(1,143)	1,253	113	82	361
Net Cash Flow	191	2,712	(292)	773	276
KEY RATIO					
Sales Growth (%)	36	10	9.5	11	9.8
Net Profit Growth (%)	318	58	19	8	15
Operating Margin (%)	9.7	13.5	14	14	14.8
Payout Ratio (%)	-	-	25	25	25
Acid-Test Ratio	0.3	2	1.7	1.7	1.9
ROE (%)	52	31	20	18	18
P/E	-	18	15	14	12
P/BV	-	3.3	2.8	2.4	2.1
ROA (%)	10.6	14.5	13.9	13	13.1