Strategy

Time to Overweight

sekuritas sinarmas

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Evan Lie Hadiwidjaja
Head of Research
+62 21 392 5550 ext. 615
evan.hadiwidjaja@sinarmassekuritas.co.id

Wilbert
Deputy Head of Research
+62 21 392 5550 ext. 611
wilbert@sinarmassekuritas.co.id

Anthony Angkawijaya
Equity Analyst
+62 21 392 5550 ext. 611
anthony.angkawijaya@sinarmassekuritas.co.id

Richard Suherman
Equity Analyst
+62 21 392 5550 ext. 610
richard.suherman@sinarmassekuritas.co.id

Richardson Raymond
Equity Analyst
+62 21 392 5550 ext. 159
richardson.raymond@sinarmassekuritas.co.id

Paulina
Equity Analyst
+62 21 392 5550 ext. 610
paulina@sinarmassekuritas.co.id

FY19F JCI target: 6,770 (5.9% upside)

We raise our 2019F JCI target from 6,560 to 6,770 (16.7x FY19E PE) on the back of more favorable monetary policy framework and improving macro condition going forward. While uncertainty from US-China trade negotiation still persists, we see current development on FX, foreign flow, inflation, and monetary policy, to be in favor of JCI. On our macro assumption, we revise our USDIDR assumption to 14,000 - 14,500 from previously 14,300 - 14,800 and 7DRRR to 5.25% - 5.75% from previously 6.00% - 6.50%. Our index target upgrade is primarily driven by a higher PE multiple justified by the aforementioned key assumption changes and the incremental yield premium of high dividend stocks versus low global bonds yield environment.

What to buy?

In all, we are bullish on interest-sensitive names and selective stocks with strong fundamentals. With that being said, our top picks for the rest of the year are: **BMRI, BNGA, WIKA, WEGE, SMGR, EXCL, and BSDE.** On the flip side, we remain cautious on commodity sector as we see weakness in global manufacturing activity and stronger Rupiah to affect earnings quality.

Macro economic indicators

	2018	2019E
GDP Growth	5.17%	5.00% - 5.10%
Inflation	3.20%	3.00% - 4.00%
7 Day RR Rate	6.00%	5.25% - 5.75%
FX USDIDR	14.390	14,000 - 14,500
JCI Index	6,194	6,770
PE Ratio	16.6x	16.7x

The beginning of easing monetary policy cycle

On the monetary policy framework, BI has recently lowered 7DRRR by 25 bps on today's meeting to 5.75%, a decision that is seen to be more accommodative for economic growth. This move is in-line with global central banks' view of easing monetary policy as depicted by several countries' rate cuts (i.e. India, Australia, and many others) paired with the Fed's statement of openness to lower the benchmark rate as inflation remains below the 2% target. While we initially expected 7DRRR easing to trail behind FFR, conditions appear to be favorable for an earlier rate cut as foreign reserve stands at USD 123.8bn (up USD 3.1bn YTD), trade balance recorded a surplus in four out of six months YTD, and USDIDR appreciation provides room for BI to remain ahead-of-the-curve. Additionally, we think pressure on Rupiah has peaked last quarter post dividend paying season and foreign debt payment.

Strengthening USDIDR amidst favorable outlook

At current, USDIDR stands at 13,935 (up 3.1% YoY, up 2.9% YTD). The strengthening currency is attributable to a number of reasons: 1) oil price decline (dn 17 ppt YoY), 2) rising foreign purchase of bonds since Nov-18, 3) DXY depreciation stemmed by rate cuts expectation, 4) S&P sovereign rating upgrade to BBB with a stable outlook at the end of May-19, and 5) market expectation of better CAD at the end of 2019.

Compared to other EM countries, Rupiah is currently ranked number five out of 24 countries. While declining rate may offer pressure on Rupiah, we view current fundamentals should curb volatility and sustain Rupiah at a comfortable level of 14,000 - 14,500 throughout 2H19.

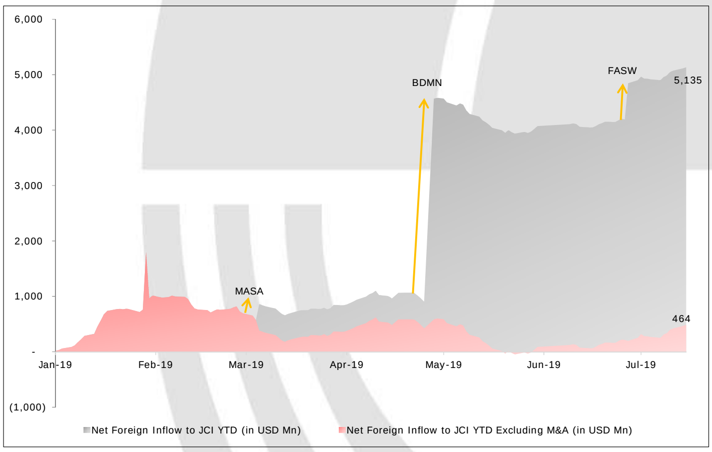
Figure 1. EM currencies YTD performance

Source: Bloomberg, Sinarmas Investment Research

Foreign buying in equity and bond market

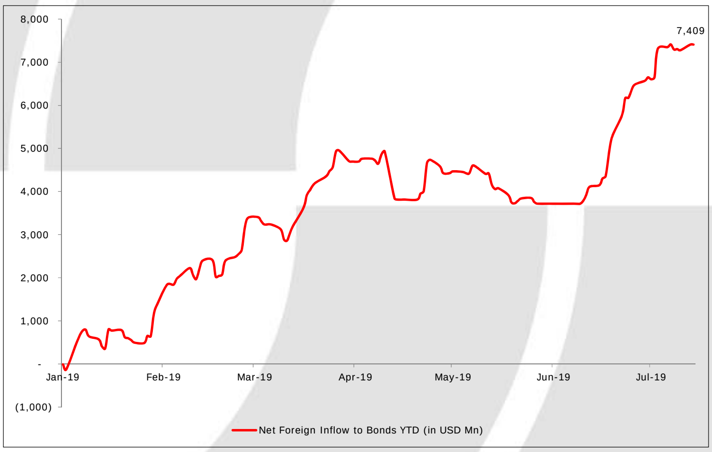
To date, Indo bond market recorded net foreign inflow of USD 7.4bn as foreign steadily increased their bond purchases in Indonesia. In addition to the attractive yield and real rates, Indonesia's sovereign rating upgrade by S&P to BBB with stable outlook at the end of May-19 also contributed to foreign inflow. We see rising foreign purchases in bonds to support USDIDR appreciation. On the equity market, JCI index recorded a net foreign inflow of USD 5.1bn YTD. However, M&A makes up majority of capital inflow through the acquisition of Bank Danamon (BDMN), Multistrada Arah Sarana (MASA) and Fajar Surya Wisesa (FASW), which accounted for 90% of total inflow this year. Excluding these transactions, we calculate a net inflow of USD 484Mn YTD, of which mostly were accumulated in the past one month. Throughout May to June, sectors bought by foreign pension funds (PF) and foreign mutual funds (MF) were consumer staples, media, plantation, and retail as depicted in figure 4 & 5.

Figure 2. Net foreign flow to equity



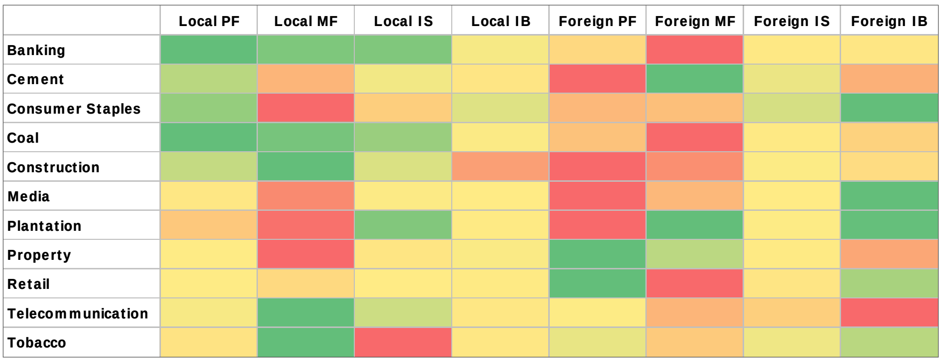
Source: Bloomberg, Sinarmas Investment Research

Figure 3. Net foreign flow to bond



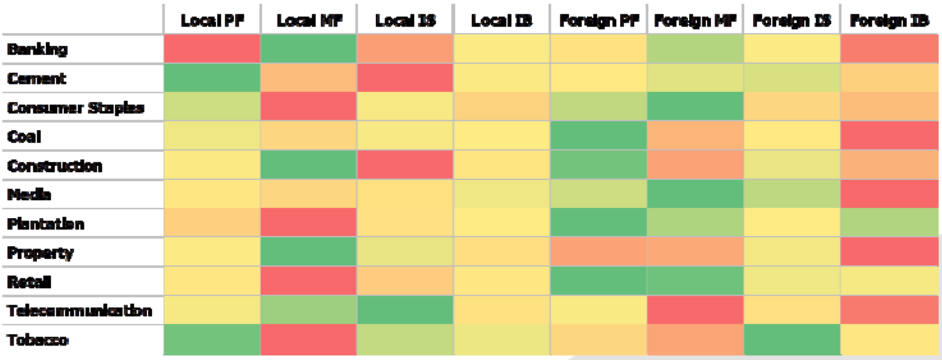
Source: Bloomberg, Sinarmas Investment Research

Figure 4. Changes in free-float ownership from Jan-19 to May-19



Source: KSEI, Sinarmas Investment Research

Figure 5. Changes in free-float ownership in Jun-19

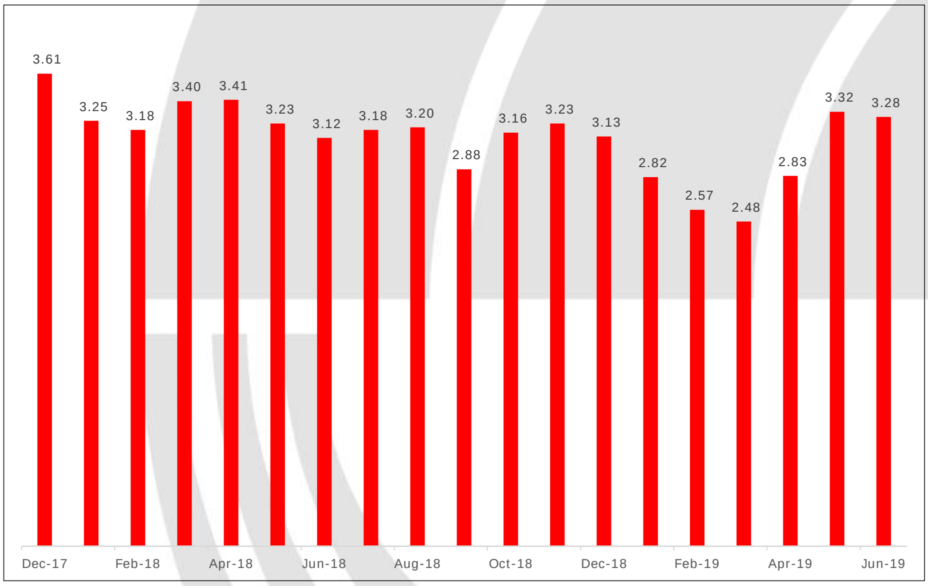


Source: KSEI, Sinarmas Investment Research

Benign inflation provides room for rate cuts

As of Jun-19, headline inflation remained benign as it expanded by only 3.28% YoY, still within BI's target of 3.5% ± 1% in FY19E. While inflation displayed an uptick on a YoY basis, Jun-19 figure was lower than May-19 due to the seasonality of food prices over Idul Fitri. In 2H19, we see less catalysts for rising inflation as Hari Raya holiday has ended and commodity prices remain subdued. In the meantime, we see no intentions from the government to increase utilities and fuel prices this year. Therefore, we are of the view that benign inflation in 2H19 will provide room for BI to ease.

Figure 6. Indonesia headline inflation



Source: Bloomberg, Sinarmas Investment Research

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ADD: Share price may range between 10% to 15% over the next 12 months.
NEUTRAL: Share price may range between –10% to +10% over the next 12 months.
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