



Ace Hardware Indonesia

Recommendation: BUY

Target Price (12-month horizon): IDR2,075 (+22%)

Current price: IDR1,700

Number of Shares outstanding: 17.15bn

Market Capitalization: IDR29.2tr

Earnings Result

ACES - 3Q19

November 18, 2019

9M19 Results

Ace Hardware Indonesia (ACES) published its financials for the period of nine (9) months ending September this year (9M19) with net profit of IDR727.2bn (+4.3% YoY) on the back of net sales of IDR5.9tr (+15.7%, YoY). Meanwhile, gross margin during 9M19 recorded at 47.5% vs. 48.0% in 9M18, operating margin declined to 15.5% in 9M19 vs. 17.2% in 9M18, and net profit margin was registered at 12.2% during 9M19 vs. 13.5% in 9M18.

We view sales growth of 15.7% YoY during 9M19 showed resilience which were backed by higher tickets sales rather than transactions volume. At the other end, depreciating US\$IDR last year impacted 9M19 gross margin by 50bp. Up to September this year, ACES expanded by 14 (fourteen) new ACE stores across the main cities in Indonesia, totally added 26,720sqm and c.1,500 new workers which weighed on the 9M19 profit & loss that which showed a decreased in operating margin to 15.5% vs. 17.1% during 9M18. With stable tax rates net profit margin of the company declined to 12.2% in 9M19 vs. 13.5% in 9M18.

Earnings Estimates

We expect ACES to book revenue of IDR8.6tr this year (+18.2% YoY), back by higher 4Q19 sales, while operating margins is estimated to decline to 16.3% (2018: 17.0%) for investments spending, and net margin this year to 12.7% (2018: 13.3%) to net profit of IDR1.09tr (+12.6% YoY). For next year, we are at present comfortable that sales growth to grow by 19.1% YoY to IDR10.2, and with stable profitability net profit in the year 2020 is expected to be IDR1.4tr. Our projections were based on the argument that better economic climate in the year 2020 is expected to increase buying power of middle income class in Indonesia, the company's backbone of growth.

Valuations

At our 12 months – target price (12M-TP) of IDR2,070, ACES is trading at 26.8x our FY19 earnings estimate and falling to 21.9x our FY20 earnings estimates. Those multiples are below the company's historical average of 28.5 x.

As mentioned in the last review of the company (dated November 2, 2018), AMRT is considered the most proximate of similar type of ACES, while of higher ticket items but nevertheless comprised of almost basic necessity of the aspiring middle class of Indonesia. At its target price, ACES is trading at significant discount to AMRT, also within the range of earnings multiple for retail sector in the United States at the range of 11.7x -38.9 x.

Earnings Forecasts

Year To 31 Dec	2016A	2017A	2018A	2019F	2020F
Revenue (IDRbn)	4,936	5,939	7,240	8,560	10,199
Operating profit (IDRbn)	881	968	1,229	1,394	1,686
Net Profit (IDRbn)	711	778	976	1,147	1,383
EPS (IDR)	41	45	56	63	77
EPS Growth (%)	20.4	9.4	24.0	12.6	22.1
PER (x)	41.0	37.5	30.2	26.8	22.0

Source: ACES, Analisa Saham Indonesia, share price close 18-Nov-2019

Recommendation

We maintain our BUY rating for the company, mainly for the reason of prospect of higher purchasing power of Indonesia middle-income class due to the estimated better economic growth next year. Higher income of the consumers not only will maintain the need of quality products that a more comfortable and convenient life style require, but also enable the company to pass on higher cost to consumers in terms of higher selling prices. More important, the company has a proven track record of managing cost, of applying growth strategies, and of maintaining strong balance sheets (see Graphs in the next pages)

Indonesia aspiring middle class

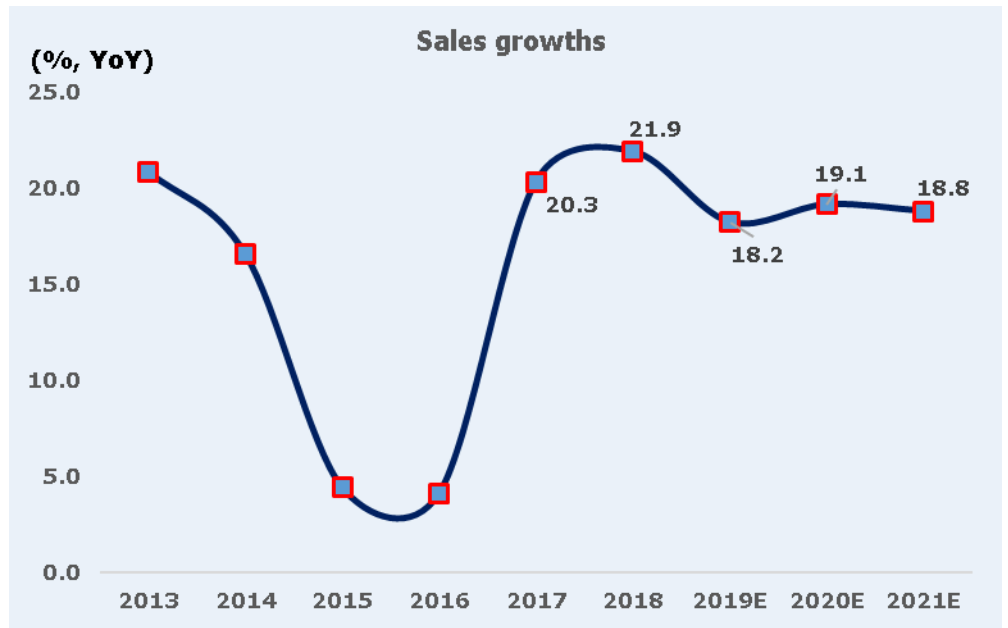
For general view, based on the World Bank publication for the coverage of East Asia and Pacific regions, October 2018, recent economic growth, public services, and social assistance is expected to reduce poverty rate in the regions from 9.4% in 2017 to 6.4% in 2020. Meanwhile, more than 140 million people in the regions are expected to rise above the UMIC (Upper Middle-Income Class) poverty line of USD5.5/day by purchasing power parity.

Further, by the World Bank study, between 2002 and 2016, the Indonesian middle class rose from 7 percent of the population to 20 percent, while its share in total national consumption increased from 21 % to 43%. Combined with the country's very small upper class, the middle class now accounts for about half of all consumption.

For the case of Indonesia, characteristics of the work force is a closer proxy of middle – income class, in our view. The higher trained and educated the work force and the more are included in the productive age bracket, the better the quality of the work force. Better quality of the work force and combined with robust investment spending will naturally create an aspiring middle class, we expect. Indonesia work force and investment spending are indeed forming positive trends (see Graphs in the next pages).

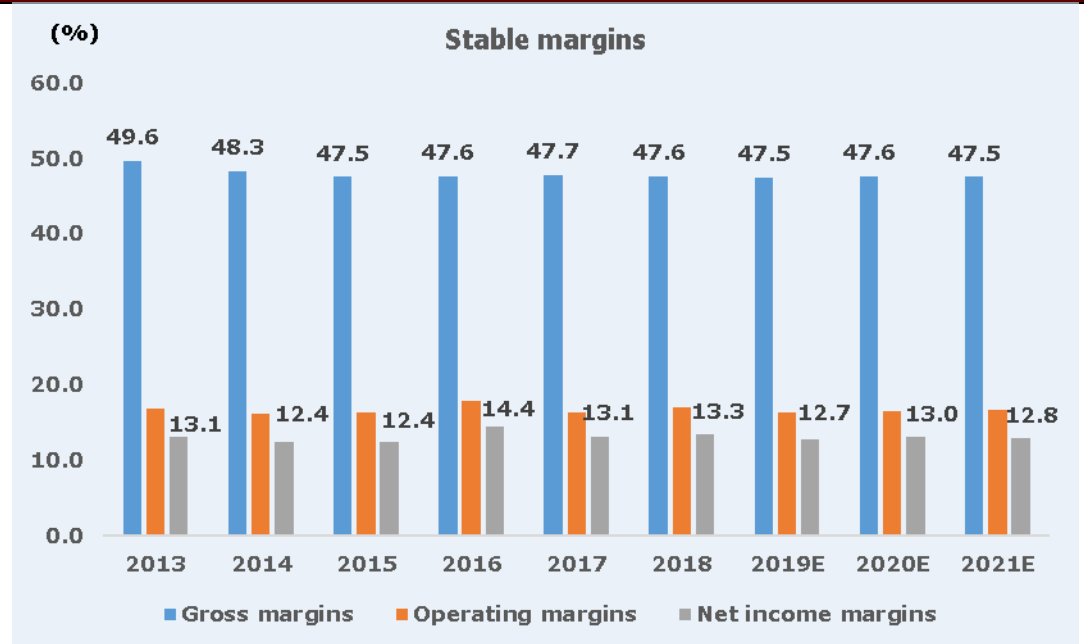
Contact analyst: Dang Maulida

Graph (1): Sales growths by transactions and price



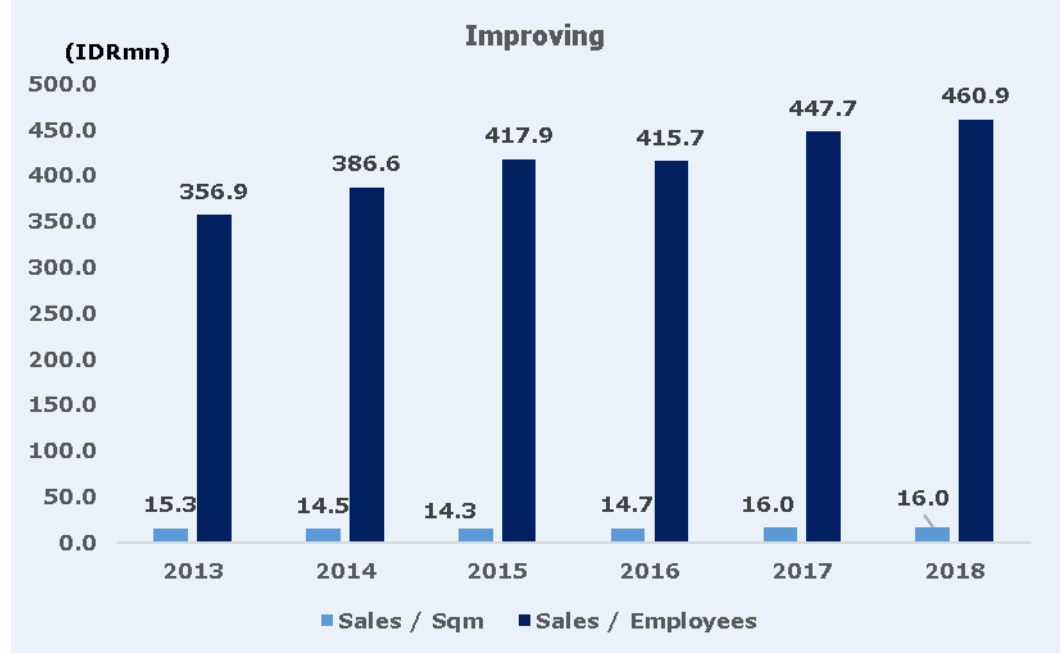
Source: Annual Report ACES, Analisa Saham Indonesia

Graph (2): Stable profitability



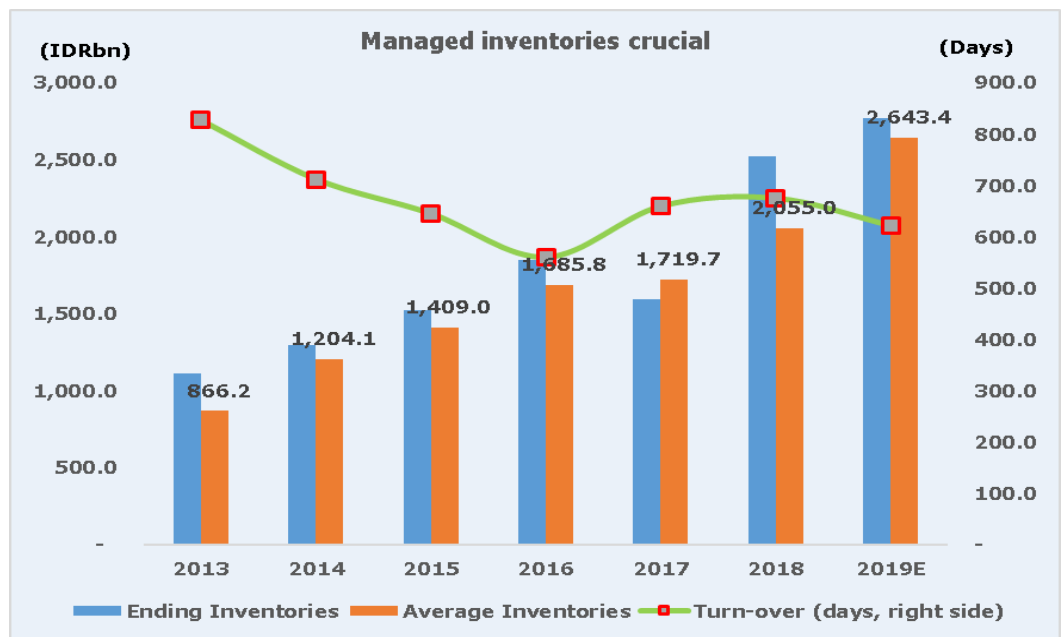
Source: Annual Report ACES, Analisa Saham Indonesia

Graph (3): Cost – effective expansions



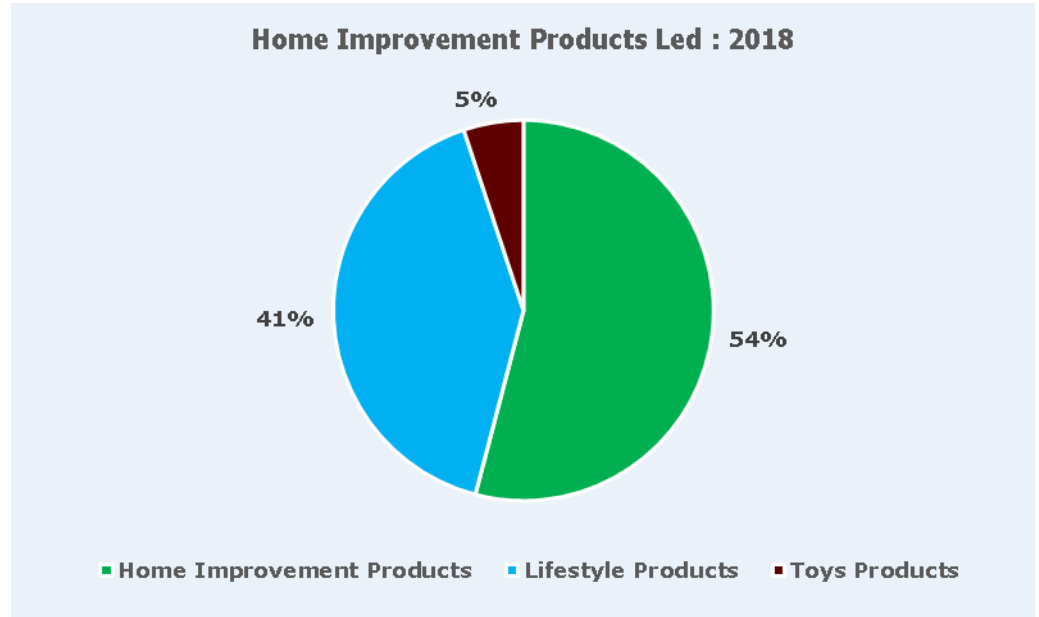
Source: Annual Report ACES, Analisa Saham Indonesia

Graph (4): Inventories prone to USDIDR value



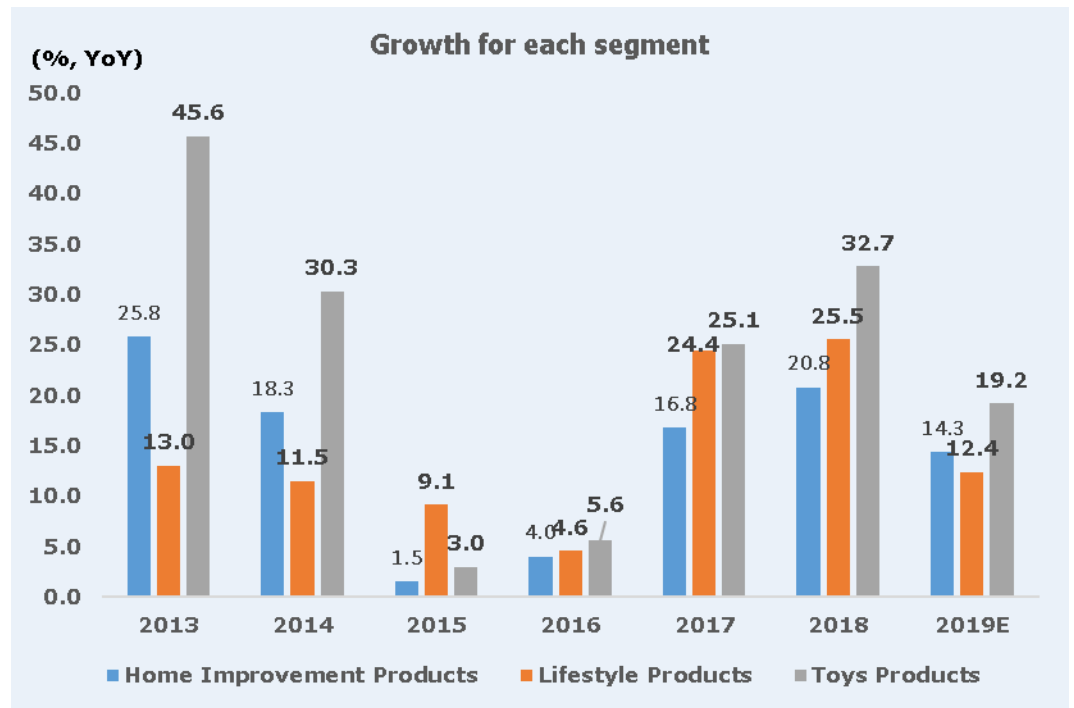
Source: Annual Report ACES, Analisa Saham Indonesia

Graph (5): Sales composition with Home Improvement Products Led since '13



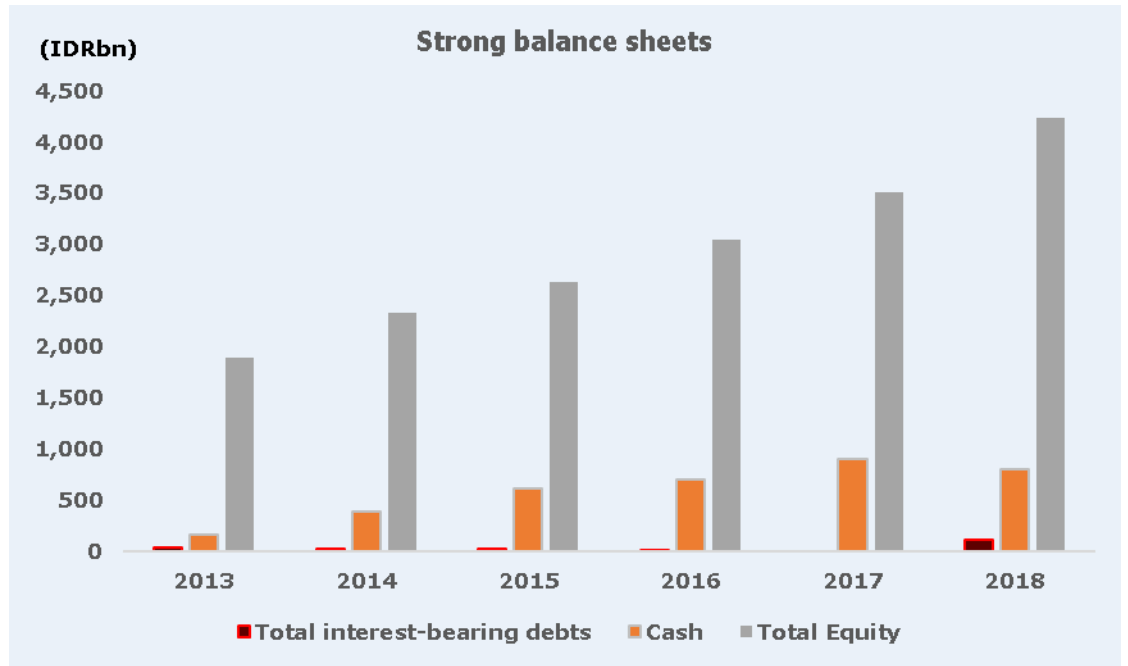
Source: Annual Report ACES, Analisa Saham Indonesia

Graph (6): Sales composition growths



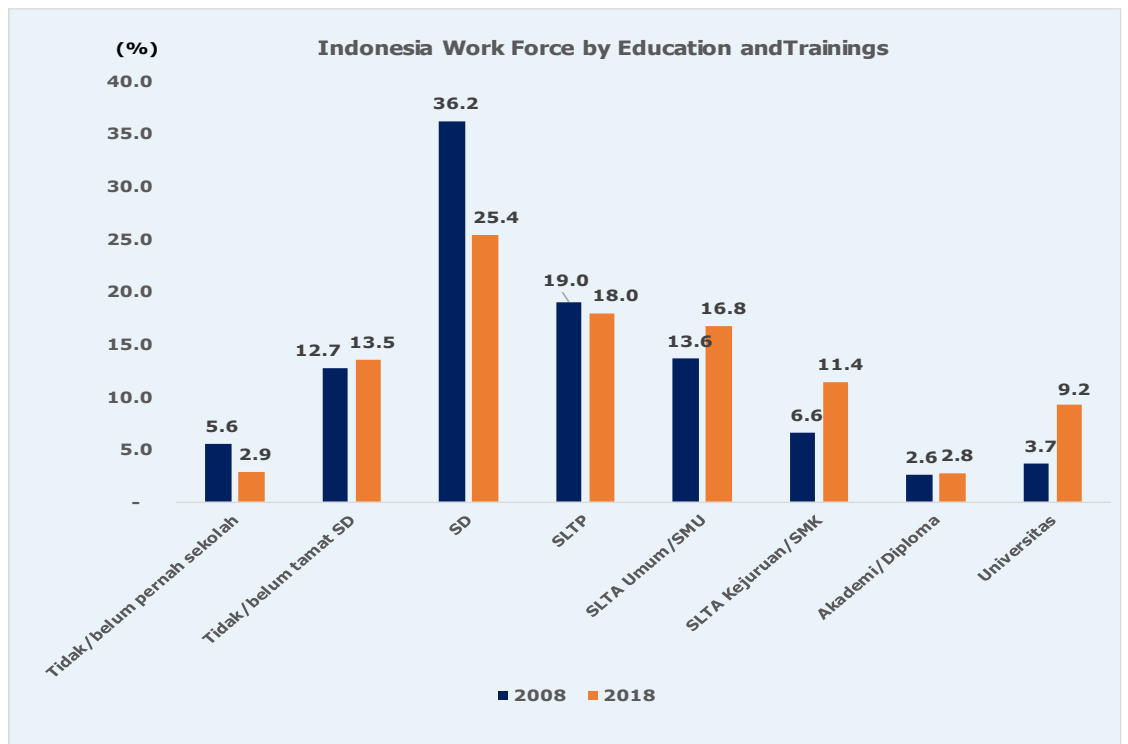
Source: Annual Report ACES, Analisa Saham Indonesia

Graph (7): Net – cash positions



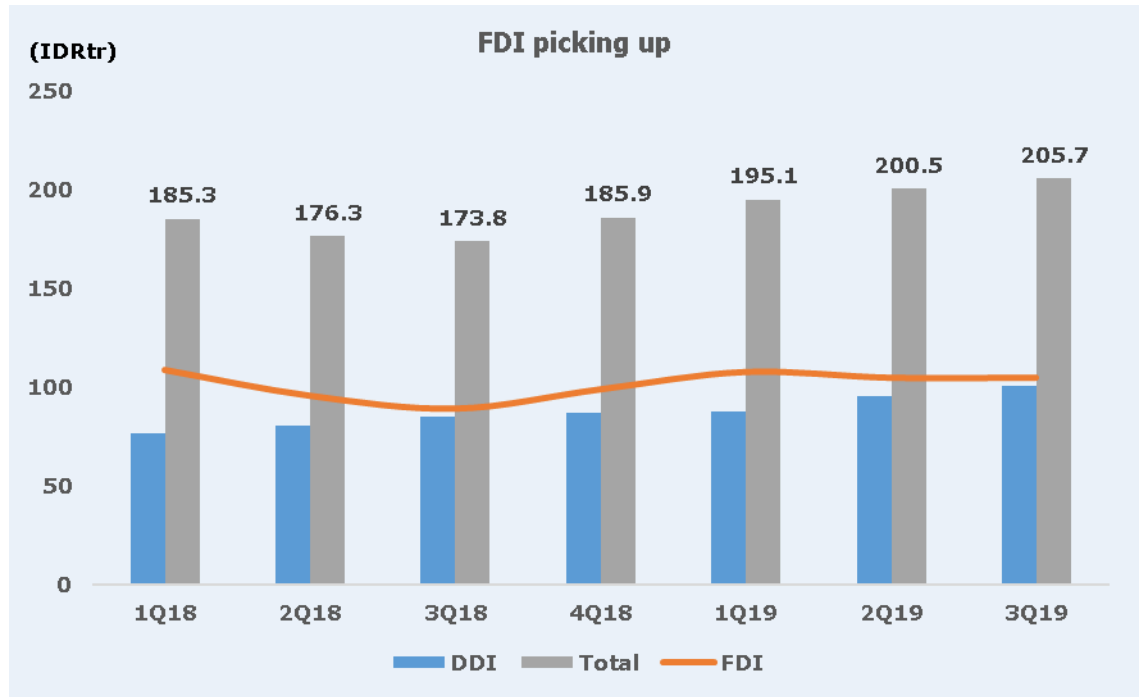
Source: Annual Report ACES, Analisa Saham Indonesia

Graph (8): Indonesia Work – Force: 127.1mn people in 2018



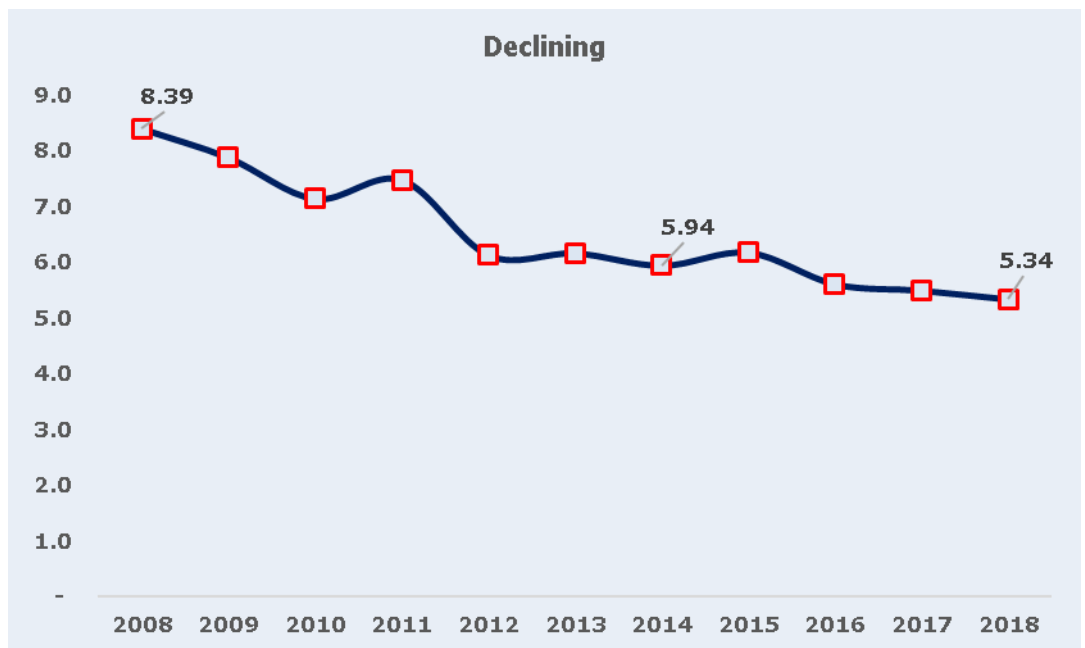
Source: Central Statistics, Analisa Saham Indonesia

Graph (9): Domestic and foreign investment spendings



Source: Investments Coordinating Board, Analisa Saham Indonesia

Graph (10): Indonesia Unemployment Rates



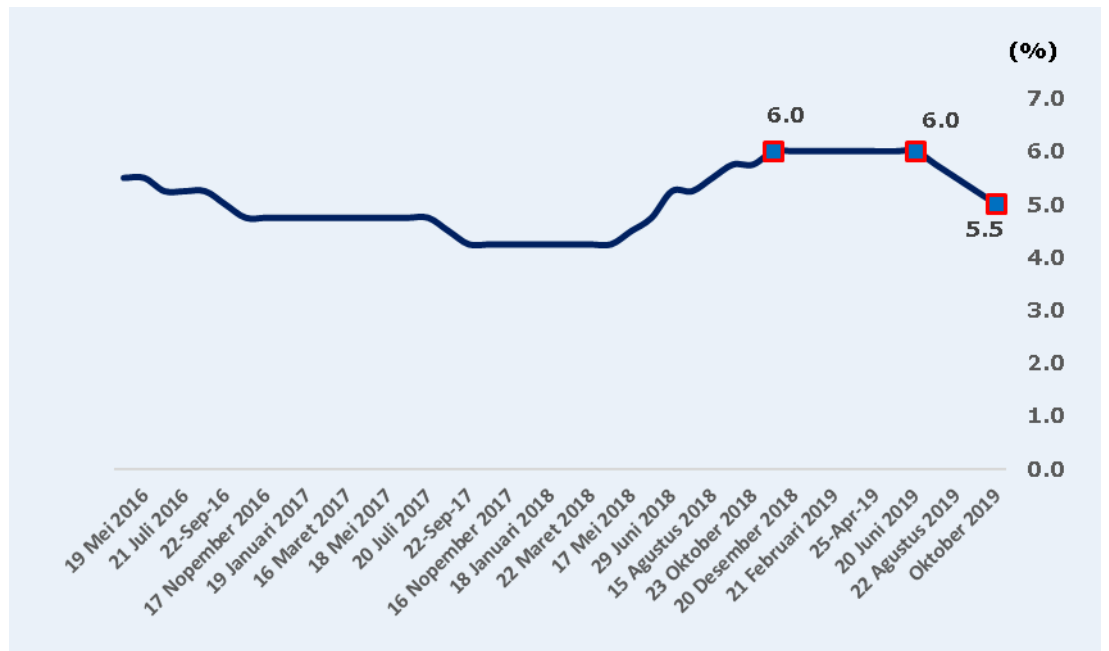
Source: Central Statistics, Analisa Saham Indonesia

Graph (11): Encouraging start of 4Q19: surplus



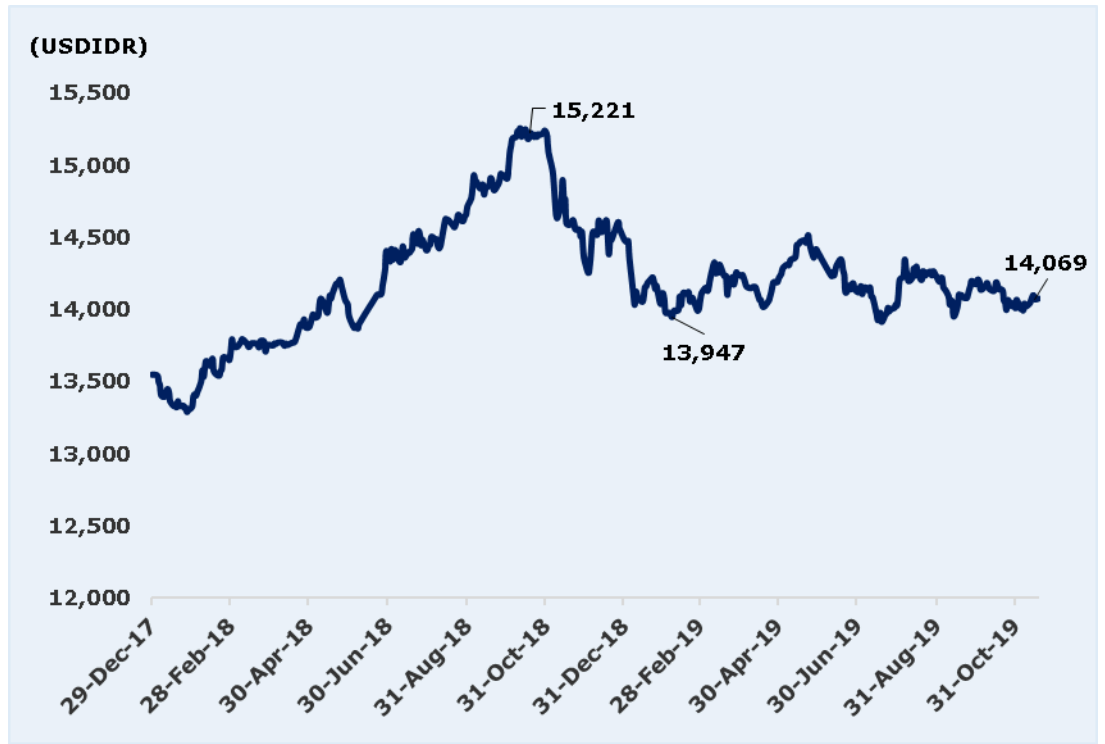
Source: Central Statistics, Analisa Saham Indonesia

Graph (12): BI7D-RRR accommodates growths



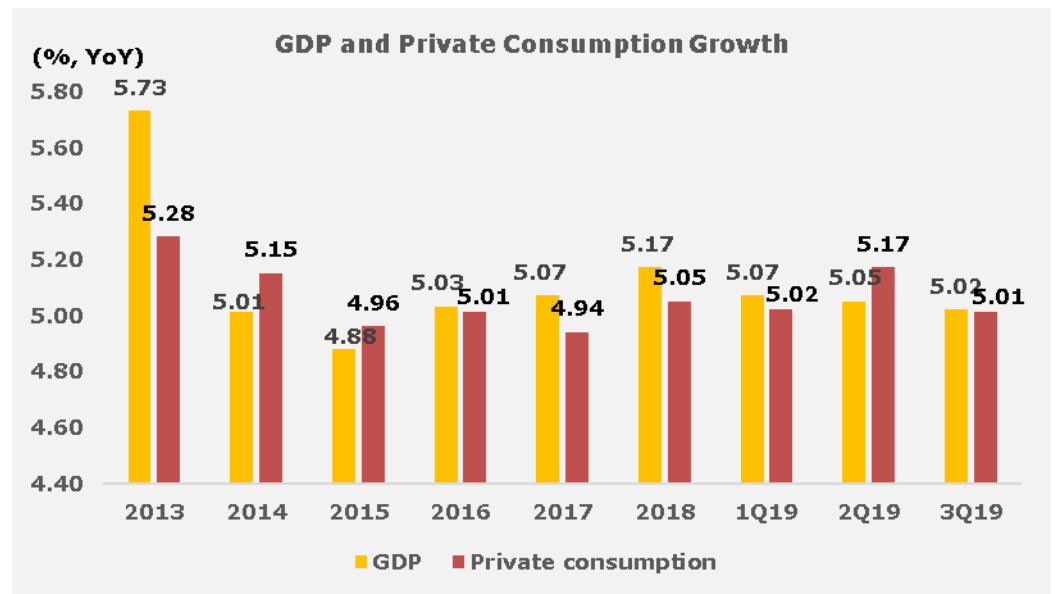
Source: Bank Indonesia, Analisa Saham Indonesia

Graph (13): Strengthening and stable IDR is much expected



Source: Bank Indonesia, Analisa Saham Indonesia

Graph (14): Private Consumption is made up c.50% of middle class consumers



Source: Central Statistics, Analisa Saham Indonesia