SECTOR UPDATE REPORT

MNC Sekuritas Research Division

September 22, 2017

TOLL ROAD SECTOR UPDATE

Road to El Dorado

Traffic Volume is Key to Toll Road Business Continuity

As the largest toll road operator in Indonesia, PT Jasa Marga Tbk (JSMR) has managed to record an increase in traffic volume CAGR 4.50% p.a. (2012-2016). Throughout 1H17, JSMR successfully took in a 7.47% YoY increase in revenue, and net profit 9.79% YoY higher, supported by steeper toll revenues and a significant increase from its non-toll road businesses. With the opening of several new toll roads, it is expected that the increased traffic will be the main revenue stream support of toll road operator performance.

Still an Attractive Investment Destination

We assess that the toll road industry is an attractive industry, supported by several factors: 1) Acceleration of infrastructure construction by the government, driving the growth of the toll road business; 2) Potential to generate long-term recurring income and attractive returns; 3) Giving multiplier effect on allied businesses, thus spreading prosperity throughout society.

Land Acquisition and Funding Issues Still a Main Focus

Struggles over land acquisition and funding issues continue as the main challenges in the toll road business. Other than that, the feasibility of investing by taking into account IRR and payback period levels remains to be considered. Nevertheless, infrastructure development – especially toll roads – is sorely needed to increase the potential of the Indonesian economy. Therefore, cooperation between the government, SOE and private parties is needed to work out a scheme which ultimately is mutually beneficial.

OVERWEIGHT Outlook with JSMR as a Preferred Stock

We are being **OVERWEIGHT** for the toll road industry in Indonesia. We recommend **JSMR**, with a **Target Price Rp6,350** which implies **PE 24.68x FY17E** or equivalent with P / E multiple -0.25STD (average 3-years P/E) and **PBV 2.23x FY17E**. We see that JSMR will be able to offer long-term prospects, supported by 1) Acceleration of toll road infrastructure development by Government, 2) Operation of new toll roads in FY17E that will potentially increase future toll revenues, 3) Robust funding strategy.

Ticker	Market Cap (Rp bn)	PER (x)		EV/EBITDA (x)		Rec.	Target Price (Rp)
		FY17E	FY18F	FY17E	FY18F		
JSMR	43,18	23,12	17,87	12,37	11,16	BUY	6.350
CMNP	4,38	NA	NA	NA	NA	Not Rated	NA
META	2,46	NA	NA	NA	NA	Not Rated	NA

Sources: MNCS Estimate (as of 18 September 2017)

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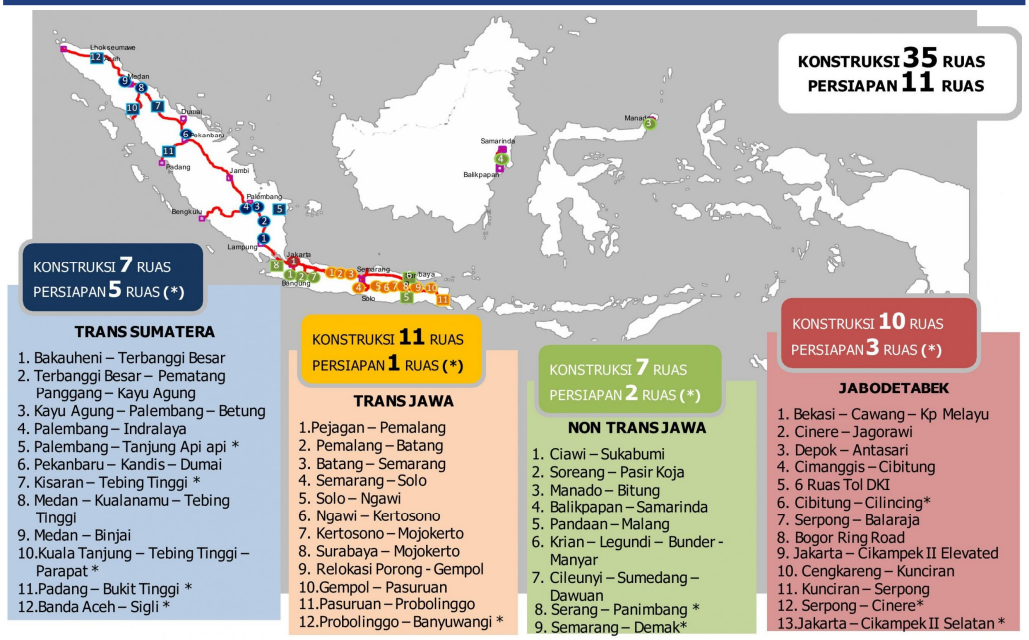
Acceleration of Infrastructure Construction into Main Catalyst

Currently the government is focusing on economic growth by boosting infrastructure development in Indonesia. The main sectors that receive positive impact from infrastructure development are the construction and operational sectors of toll roads. The Indonesia Toll Road Authority (BPJT) projects toll roads in Indonesia to extend 1,851 km by 2019. Until August 2017, the total length of operational toll roads in Indonesia is reported at 928.7 km, increasing by an average of 200 km per year – higher than five years ago, when they only expanded 100 km per year.

Exhibit 01. Progress of Total Road Development Indonesia, 2016



Source : The Indonesia Toll Road Authority (BPJT)

Positive Performance throughout 1H17

Most toll road operators have recorded positive performance in 1H17, as can be observed in PT Jasa Marga Tbk (JSMR) performance. JSMR, as the largest toll road operator in Indonesia, dominates with a market share of around 61%, with the highest concentration in Jabodetabek, Java and Sumatra. As of April 2017, JSMR operates 600 km of toll roads, with the longest concession period in Asia: until 2060. JSMR dominates with an average 80% of daily transaction volume.

JSMR revenue grew by 9.2% YoY CAGR throughout 2012-2016. Up to 1H17, JSMR managed to increase 7.47% YoY in revenue, moving from Rp4.21 trillion in 1H16 up to Rp4.53 trillion. Gross profit recorded an 8.03% YoY increase, with gross profit margin of 18.39%. Net income increased by 9.79%, from Rp 925.51 billion to Rp1.02 trillion, with a net profit margin of 7.76%. In our view, this proves that there is still growth potential for the toll road operator business in Indonesia.

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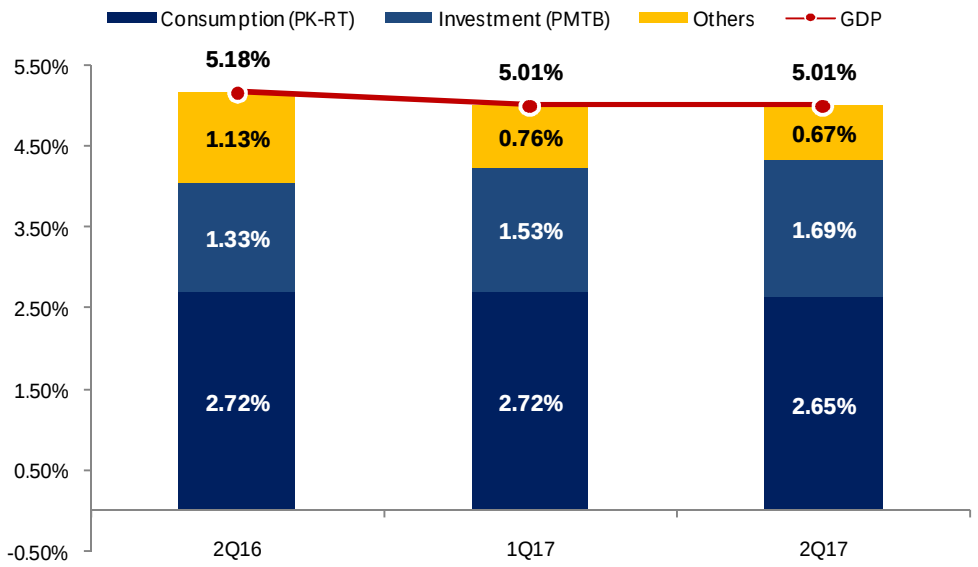
Increased investment became one of Indonesia's Economic Growth Supporters in 2Q17

The Indonesian government predicts that the economy of Indonesia in 2017 will grow by 5.2% YoY, while in 2018 is predicted to grow 5.2%-5.6% YoY. However, at present Indonesia's economic growth is stagnant, at 5.01% YoY level in 2Q17, or equal to economic growth in 1Q17 which was in fact largely by household consumption. Statistics Indonesia (BPS) recorded a 2.65% increase in the Indonesian economy, driven by a rise in household consumption which, despite slow growth, dominated Indonesia's economic base with 55.61% in 2Q17. The second-largest contribution is the value of Government Investments (PMTB) which grew by 1.69%, with a contribution of 31.36%. We assess an increase in the value of government investment, in both building and non-building sectors, proving that investment activity is increasing, in line with continuing private sector construction and government infrastructure projects. In our view, one of the more interesting sectors, as an ongoing government infrastructure project in line with the 2015-2019 infrastructure development plan, is the toll road sector.

Exhibit 02. Source of GDP Growth by Expenditure



Source : Statistics Indonesia

Toll Road Business Presents an Interesting Investment Opportunity ...

From the investment side, the toll road business is an attractive investment opportunity, one with potential for long-term recurring income. Further, the toll road business is able to provide attractive returns, with IRR above the yield of 10-year annual government bonds, at around 14%. It also complies with commercial financing requirements for infrastructure projects by banks: BNI corporate business materials lists four (4) main requirements: 1) minimum IRR of 14%, with self-funding of 30%; 2) a maximum payback period of 15 years – currently at an average level of 10 years; 3) minimum land acquisition already secured at 75%; 4) starting 2016, toll road development projects must be granted a funding guarantee by PT Penjaminan Infrastruktur Indonesia (PPI).

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... and a Potential Multiplier Effect on Other Businesses

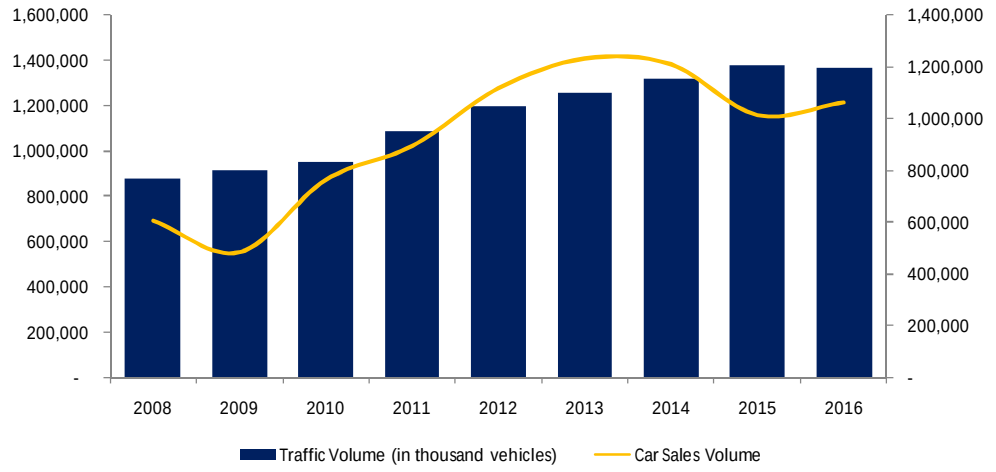
Currently the government is budgeting Rp 387.3 trillion from APBN 2017 for infrastructure development in 2017. The disbursement of APBN funds for infrastructure, which includes development fund of toll roads targeted to operate up to 1,851.4 km by 2019, has exerted a positive impact on Indonesia's economic growth. The development of the area around toll roads, both current and potential, has the potential to improve the welfare of the surrounding community, from the creation of jobs, property development and an increased level of public consumption.

In our opinion, the development of infrastructure construction is relatively on track, particularly for toll roads, which has the potential to exert a positive impact on several other sectors: 1) the automotive industry; 2) cement and precast industries; 3) the property industry; and 4) ceramics industry.

Opening of New Toll Road is Predicted to Increase Consumer Interest in Automotive Purchases

Infrastructure construction through toll roads has grown rapidly since 2015. This can be seen in the addition of toll road length, reaching 44 km in 2016 and rising to 392 km in 2017. Construction of toll roads has a multiplier effect, indirectly on the growth of the automotive sector. With the opening of several new toll roads, it is predicted that there will be an increase of public interest in automotive purchases. This can be seen as one of the reasons for increased car sales volume in Central Java and Yogya-karta D.I.Y., which rose 2.11% YoY in 2016, along with the opening of several new Trans Java toll roads in mid-2017. With the increased car sales volume, traffic of toll road operators is predicted to rise as well (Exhibit 03). The increased car sales volume was followed by an average growth of traffic volume in 2012-2016 of 4.66% YoY and 4.38% YoY, that will potentially pump the income of toll road operators an average of 10.43% YoY.

Exhibit 03. Development of Toll Trafic Volume and Car Sales Volume (2008-2016)



Source : PT Astra International Tbk and PT Jasa Marga Tbk

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Cement and Pre Cast Sectors Get Positive Catalysts from Toll Road Construction Projects

The greatest need for infrastructure development is cement and pre-cast concrete, for a total of 21.53 million tons by 2017. Based on estimated material resource requirements and construction equipment, the Ministry of Public Works and Public Housing (PUPR) predicted a 1.8 million ton need for cement and pre-cast concrete for road construction in 2016. Therefore, in our opinion the construction of toll roads is certainly able to be a positive factor for cement sector and pre cast cement.

Exhibit 04. Concrete Use in Solo-Kertosono Toll Road Construction

Source : PT Waskita Beton Pre Cast Tbk

Property Sector around Toll Road Construction has Potential for Growth

With high levels of congestion, people will choose their residence with easy and fast transportation access, thus boosting the economic sector in areas surrounding of toll road construction. Improved access will boost the public's willingness to secure a permanent residence and business place with easy access to transportation. Currently, construction companies are trying to develop areas around LRT and MRT development, known as 'Transit Oriented Developments' (TOD). This will result for high demand for property in areas surrounding TOD and toll road areas.

Exhibit 05. Property Development Project

Project	Locations	Completion Schedule	Developers with Exposure
JORR Seksi E3	Greater Jakarta	2017	MDLN
LRT Jakarta	Jakarta	2018	SMRA, Adhi Property
MRT Jakarta Line 1 (North-South)	Jakarta	2019	PWON
Trans Java Toll Road	Major Cities in Java	2019	CTRA, PWON, SMRA
JORR 2 Toll Road	Greater Jakarta	2019	BSDE, CTRA, LPKR, SMRA,
Trans Sumatra Road	Major Cities in Sumatra	2019/2020	CTRA
Jakarta- Bandung High Speed Rail	Jakarta, Bandung	2020	SMRA, Wika Property

Source : Company

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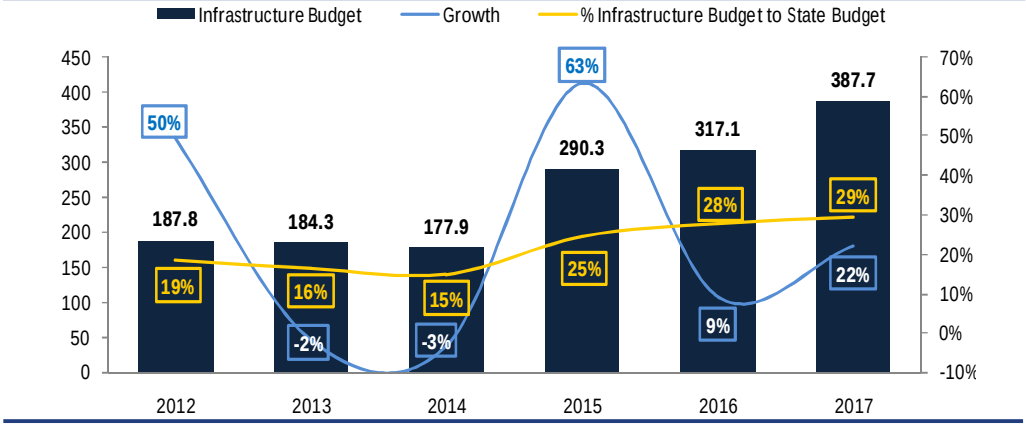
The lift of Property Business is Expected to Increase Performance of Ceramic Sector

The increase of economic activities due to the construction of toll roads has boosted the growth of the property sector, which ultimately raises the business potential of supporting sectors, such as the ceramics sector. Although the property business has been observed to be lagging since 2016 and has caused the demand for ceramic products to decline, we believe that the property business will again be lifted in 2018-2019, along with the completion of infrastructure development in Indonesia especially toll roads.

Infrastructure Sector Budget as a Motor Driving Toll Road Business Growth

The budget for infrastructure construction in the APBN steadily increases annually, with an average of 20% over the last 5 years. In the 2017 state budget, the government has budgeted Rp 387.7 trillion for infrastructure spending, or 29% of the total state budget - greater than the average infrastructure budget in recent years. We project the growth of state spending for infrastructure development will continue to rise until 2019.

Exhibit 06. Infrastructure Budget and National State Budget (Rp Trilion)



Source : Ministry of Finance

Exhibit 07. Government Projects 2015-2019

Sector	Amount (Rp Tn)	% of Total
Road Infrastructure	733	15
Railway Infrastructure	226	5
Sea Transportation	591	12
Air Transportation	144	3
Land Transportation	47	1
Urban Transportation	86	2
Electricity Infrastructure	1.000	21
Oil and Gas Infrastructure	507	11
Telecommunication and Information Infrastructure	280	6
Water Resource	451	9
Drinking and Waste Water	403	8
Housing	328	7
Total	4.796	100
Annual Spending	959	20

Sumber : Bappenas

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Toll Road Business Successfully Attracts Participation Not Only of SOE but Also Private Parties

Promising business properties are able to attract the participation of not only BUMN but also the private sector. The government invites private parties and BUMN to participate in capital participation, through Financial Investment of Non-Government (PINA). Beside PT Jasa Marga Tbk (JSMR), a state-owned company interested in this business is PT Waskita Karya Tbk (WSKT) through its subsidiary, Waskita Toll Road. One of the private sector organizations interested in this business is a subsidiary of PT Astra International Tbk (ASII) infrastructure, operating through PT Astratel Nusantara.

We see the interest of the private sector in the construction of toll roads as a positive catalyst for the growth of the business in the future. For example, PT Astra International Tbk (ASII), through its subsidiary PT Astratel Nusantara (Astra Infra) focuses on the expansion of toll road ownership by acquiring Cikopo-Palimanan toll road in May 2017 and PT Surya Semesta Internusa Tbk (SSIA). There are still some tender preparations conducted by the government, such as Semarang-Demak toll road section (25.25 km) and Suramadu Bridge (5.40 km) to confirm the massive development of toll road in Indonesia, especially on Java.

Exhibit 08. Cibubur Toll Gate, one of the Jasa Marga Toll Road Portfolio

Source : Infonitas

Exhibit 09. Palimanan Toll Gate, one of the Astratel Nusantara Toll Road Portfolio

Source : Kompas

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Exhibit 10. Toll Road owned by SOE and Private Companies

Indicator	Jasa Marga	Waskita Toll Road	Astratel Nusantara
Existing	Jagorawi (59 km)	Kanci-Penjagaan (35 km)	Tanggerang - Merak (72.4 km)
	Jakarta-Tanggerang (33 km)	Pejagan-Pemalang (57 km)	Kunciran - Serpong (11.2 km)
	Ulujami-Pondok Aren (5.55 km)	**Total 2 Operation Toll Road (92 km)**	Jombang - Mojokerto (40.5 km)
	Jakarta Inner Ring Road (23.55 km)		Semarang - Solo (72.6 km)
	Prof. Dr. Ir. Sedyatmo (14.3 km)		Serpong - Balaraja (39.8 km)
	Jakarta-Cikampek (83 km)		Cikopo - Palimanan (116 km)
	JORR (28.3 km)		**Total 6 Operation Toll Road (352.5 km)**
	Cikampek-Padalarang (58.5 km)		
	Padalarang-Cileunyi (64.4 km)		
	Palikanci (26.3 km)		
	JORR W2 North (7.7 km)		
	Semarang (24.75 km)		
	Surabaya-Gempol (49 km)		
	Nusa Dua-Ngurah Rai-Benoa (10 km)		
	Belmera (42.7 km)		
	Total 15 Operation Toll Road (530.05 km)		
Planning	Bogor Outer Ring Road (11 km)	Medan-Kualanamu-Tebing Tinggi (62 km)	
	Cengkareng-Kunciran (14.19 km)	Kuala Tanjung-Tebing Tinggi (143 km)	
	Kunciran-Serpong (11.19 km)	Kayu Agung-Palembang-Betung (112 km)	
	Cinere-Serpong (10.14 km)	Bogor-Ciawi-Sukabumi (54 km)	
	Jakarta-Cikapek II Elevated (36.4 km)	Cimanggis-Cibitung (26 km)	
	Semarang-Solo (72.64 km)	Bekasi-Cawang-Kp. Melayu (21 km)	
	Solo-Ngawi (90.1 km)	Cinere-Serpong (10 km)	
	Ngawi-Kertosono (87.02 km)	Cibitung-Cilincing (35 km)	
	Semarang-Batang (75 km)	Depok-Antasari (22 km)	
	Gempol-Pandaan (13.61 km)	Cileunyi-Sumedang-Dawulan (60 km)	
	Gempol-Pasuruan (34.15 km)	Pemalang-Batang (39 km)	
	Surabaya-Mojokerto (36.27 km)	Solo-Ngawi (90 km)	
	Pandaan-Malang (37.62 km)	Batang-Semarang (75 km)	
	Medan-Kualanamu-Tebing Tinggi (61.7 km)	Krian-Legundi-Bunder-Manyar (38 km)	
	Balikpapan-Samarinda (99.35 km)	Ngawi-Kertosono (87 km)	
	Manado-Bitung (39.9 km)	Pasuruan-Probolinggo (31 km)	
	Total 16 Toll Road in Progress (730.28 km)	**Total 16 Toll Road in progress (905 km)**	
Capex 2017	**Rp19,55 triliun**	**Rp32 triliun**	**Rp 4 triliun**

Source : Company

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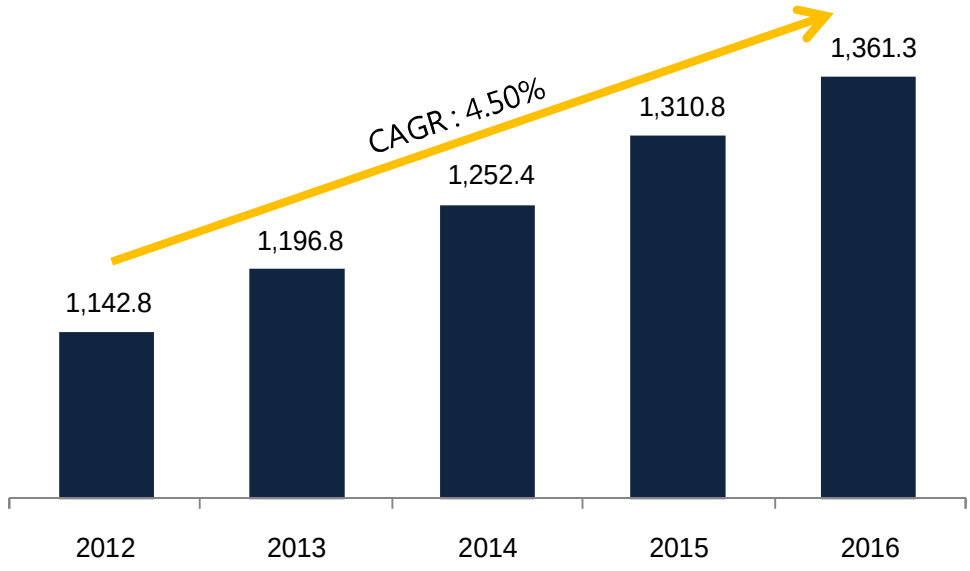
Investment Worthiness to Be Observed

We observe the growth of traffic volume in the last five years as stable. PT Jasa Marga Tbk (JSMR), as the largest toll road operator in Indonesia, has managed to record an increase in traffic volume (traffic) of CAGR 4.50% p.a. (2012-2016), supported by increased automotive sales and the opening of several new toll roads. The Company's traffic volume target is 1.36 billion vehicles by 2017. Opening of new sections, especially as it approaches the Idul Fitri holidays, is expected to increase traffic volume, with the homecoming (mudik) flow. This will have a positive impact on the increase of toll road operators' revenues. It cannot be denied that the growth of traffic volume is a key factor in the sustainability of toll road business.

Exhibit 11. JSMR Traffic Volume Trend, 2012-2016 (Million Vehicles)



Source : PT Jasa Marga Tbk

However in order to assure equitable distribution of infrastructure in all regions of Indonesia, several government projects are still considered not to meet the feasibility for investment. For example, currently the focus of Government development lies on the outer islands, such as Sumatra and Sulawesi. Trans Sumatra Toll Road construction, which is planned by the government, is a 2,818 km artery that will connect cities in Sumatra, from Bandar Lampung to Banda Aceh; it started in April 2015. According to data of the Toll Road Regulatory Agency (BPJT) of the Ministry of PUPR, estimated funding needs reach Rp 22.53 trillion. As of June 2017, three toll roads are already in operation and all construction is planned to be completed by 2019. However, we point out several obstacles in the development of this project: 1) geographical conditions, as the majority of the land is hilly, which will challenge construction work; 2) low-rated IRR; 3) land acquisition issues. We assess the development of the Trans Sumatra toll road project as having the potential to improve the regional economy, such as opening up employment and efficiency of distribution services. However, in our view the rate of profit offered is not very attractive from a business angle, with an IRR level below the industry average of 14%.

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Exhibit 12. Trans - Sumatra Main Toll Road Project

No	Segment	Length (km)	IRR (%)	Estimated Investment (Rp Triliun)
1	Lampung – Palembang	358	17%	44
2	Palembang – Pekanbaru	610	13%	95
3	Pekanbaru – Medan	548	16%	64
4	Medan – Banda Aceh	460	9%	95
5	Palembang – Bengkulu	303	9%	63
6	Pekanbaru – Padang	242	11%	35
7	Medan - Sibolga	172	7%	30

Source : Kementrian PUPR (Bisnis Indonesia)

Land Acquisition Is Still a Major Risk

Land acquisition plays an important role during pre-construction in the construction of toll roads. The consequences may include delays in project timelines, increased project costs, revenue delays, negative effect on cash flow and a negative response from adjacent communities. One of the land acquisition issues has come up in the construction of a PT Jasa Marga Tbk (JSMR) toll road project, with the Cengkareng-Batu toll road, Ceper-Kunciran or Kunciran-Bandara toll road, with a total length of 14.18 km targeted to be operational by 2019. As of April 2017, the procurement of land in the Kunciran-Cengkareng section IV section of Jurumudi-Benda only reached 59.14%, while the total progress of land acquisition of Kunciran-Soetta Airport is stuck at 27%. Even so, the Kunciran-Bandara toll project is included in the JORR 2 project, which is one of the government's priority national strategic projects.

In order to overcome the problem, the Government established a special institution which is responsible for resolving problems of land acquisition for infrastructure in Indonesia, namely Lembaga Manajemen aset negara (LMAN). LMAN Director Rahayu Puspasari said there are 22 toll road projects that will be financed by LMAN, in the amount Rp 13.286 trillion which includes Trans Sumatra toll road, Trans Java toll road, and a toll road in Jabodetabek. We believe that the agency responsible for arranging funding and land-bank land use planning, as well as compensation payments for land acquisition and national strategic projects, is able to address issues related to land acquisition.

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Concerns about Funding Issues?

In the effort of risk mitigation in the limitation of working capital, toll road operators need to apply various strategies in order to develop their business. Several financing strategies that can be pursued are: 1) Asset securitization of toll road assets through the issuance of a future revenue base securities (KIK) as alternative financing for new toll road development projects; 2) Issuance of project bonds; 3) an infrastructure financing scheme called 'Non-Government Investment Financing' (PINA) which derives from funds obtained from capital markets, insurance, financial institutions, and other legitimate financial institutions.

OVERWEIGHT Outlook with JSMR as a Preferred Stock

Our overall assessment is that the toll road industry is an attractive target, supported by several factors, such as the following: 1) Acceleration of infrastructure development by the government, with infrastructure budget as a driver of toll road business growth; 2) Potential to generate long-term recurring income and predicted to provide attractive returns with IRR above the 10-year government bond yield of about 14% p.a.; 3) Multiplier effect on assorted other businesses.

However, we point out that this industry requires large capital formation (capital intensive). In addition, investment feasibilities taking into account IRR and payback periods are the main focus of the problem. In addition, we consider that investment for toll segments outside of Java Island are not very attractive, considering their economic scale. However, infrastructure development, especially toll roads, is needed to increase the potential of the economy throughout Indonesia. Therefore, cooperation between the government, BUMN institutions and private parties is needed to view the scheme, which is ultimately mutually beneficial.

By considering some of the positive catalysts and risks that exist, we recommend **OVERWEIGHT** for the toll road industry in Indonesia. We recommend **JSMR**, with **Target Price of Rp6,350** which implies **PE 24.68x FY17E** or equivalent with P/E multiple -0.25STD (average 3-years P/E) and **PBV 2.23x FY17E**. We see that JSMR is able to offer long-term prospects supported by 1) Government backing for toll road infrastructure construction in Indonesia; 2) Operation of new toll roads in FY17E that potentially increase future toll revenues; 3) Strong funding strategy.

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