

Indonesia Market Focus

Balikpapan & Samarinda

Refer to important disclosures at the end of this report

DBS Group Research . Equity

8 Jun 2015

Basking in past glory

- East Kalimantan depends on its natural resources (coal, oil and natural gas) to drive the economy
- But the region is currently suffering from low commodity prices, 1Q15 GDP was (-)1.32% y-o-y
- Slow infrastructure development is also capping the growth of supporting sectors
- Stay defensive and stick with staples (and healthcare service); INDF and SILO

Large area + rich natural resources = investor's heaven? East Kalimantan is the third largest province in Indonesia by area, and has the second highest per capita GDP in Indonesia after Jakarta. This commodity-rich province (with a relatively small population) is also the sixth largest contributor to national GDP.

Hurt by weak commodity prices. East Kalimantan produces more than 55% of Indonesia's thermal coal output. Mining and minerals account for c.50% of East Kalimantan's GDP, and hence, the weak coal and oil prices is having a significant impact on its economy; 1Q15 GDP contracted by 1.32% y-o-y.

Room for infrastructure improvements. The province needs to develop its infrastructure to support economic activity. However, like much of Indonesia, progress can be slow (or even stalled in some areas).

Supporting sectors also hurt by weak commodity prices. Consumer spending in the province has tumbled along with commodity prices, and this has affected the consumer discretionary and property sectors.

Stay defensive – stick to staples in challenging times. East Kalimantan is a vast and rich province but we think the coal boom is over based on observations from our trip. The best bet is infrastructure and our top pick is PTPP but this is not without execution risk on new projects. We prefer to stick to consumer staples and healthcare. Our picks are Indofood (INDF) for exposure to Indofood CBP (ICBP), a good proxy to Indonesia's rising consumption trend (particularly during the coming Lebaran holiday season) and healthcare service provider SILO.

JCI : 5,100.57

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STOCKS

	Price	Mkt Cap	Target	Performance (%)		Rating
	Rp	US\$m	Price Rp	3 mth	12 mth	
Adaro Energy	895	2,141	1,030	(9.1)	(30.1)	HOLD
Agung Podomoro	366	561	380	(17.8)	36.1	FULLY VALUED
Bumi Serpong	1,920	2,764	2,150	(8.1)	21.9	HOLD
Ciputra	1,450	1,645	1,340	4.3	34.9	HOLD
Garuda Indonesia	463	896	640	(11.8)	6.8	BUY
Harum Energy	1,200	243	1,200	(24.8)	(51.0)	HOLD
Indo Tambangraya	12,975	1,097	18,500	(24.1)	(56.2)	HOLD
Indocement	21,650	5,962	20,000	(10.9)	(6.6)	FULLY VALUED
Indofood CBP	13,450	5,867	14,300	(7.4)	31.9	HOLD
Indofood Sukses	7,050	4,631	9,050	(5.7)	2.2	BUY
Matahari	17,500	3,820	22,200	(3.7)	22.4	BUY
Mitra Adiperkasa	5,700	708	5,620	6.5	11.8	HOLD
PT PP (Persero)	3,950	1,431	4,650	(0.3)	114.7	BUY
Semen Indonesia	13,225	5,868	12,000	(11.5)	(12.4)	FULLY VALUED
Siloam International	14,025	1,213	12,750	7.1	(5.1)	HOLD
United Tractors	22,200	6,195	22,400	2.1	(1.1)	HOLD
Waskita Karya	1,685	1,250	1,320	(5.3)	147.8	FULLY VALUED
Wijaya Karya	3,045	1,401	3,000	(13.1)	30.7	HOLD

Source: DBS Vickers

Balikpapan & Samarinda

East Kalimantan – waiting to re-live its glory days

We paid a short visit to the two main cities in East Kalimantan - Balikpapan and Samarinda. During the coal boom, these two cities were bustling. Fast forward to 2015, the coal boom is over and the impact of low commodity prices in these two cities is quite significant although on the surface, business activity has not come to a halt.

Our first check-point had to be the new Sultan Aji Muhammad Sulaiman International Airport (formely known as Sepinggan airport) in Balikpapan. This airport is the busiest in Kalimantan and the 6th busiest in Indonesia with 7.2m passenger traffic in 2014. With the addition of 110k sqm of terminal space (officially inaugurated by Indonesia's former President Susilo Bambang Yudhoyono on 15 Sep 2014), this airport can now process 10m passengers annually and is the biggest airport in East Indonesia. It was a major upgrade as the existing terminal only had capacity for 1.7m passengers previously.

Old Balikpapan International Airport



Source: DBS Vickers, <http://www.jotravelguide.com/>

New and revitalized Balikpapan International Airport



Source: DBS Vickers

New and revitalized Balikpapan International Airport



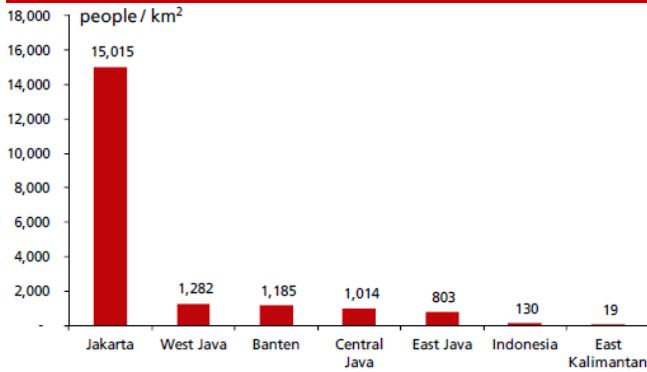
Source: DBS Vickers

Kalimantan (also known as Borneo) is the largest island in Indonesia, and the 3rd largest in the world, with a total land area of 743,330 sqkm. The trademark of the island is extensive rainforest cover, although deforestation and exploitation is rapidly shrinking the "green" area.

East Kalimantan province is the 3rd largest province in Indonesia by area, with 127,265.52 sqkm of land and 25,656 sqkm of marine area. Demographically, East Kalimantan is not densely populated, with only 19 people per sqkm (ranked 30 out of 33 provinces in Indonesia). This is mainly because of the lack of basic infrastructure and other essentials. As a comparison, the capital city Jakarta has the highest density with 15k people per sqkm.

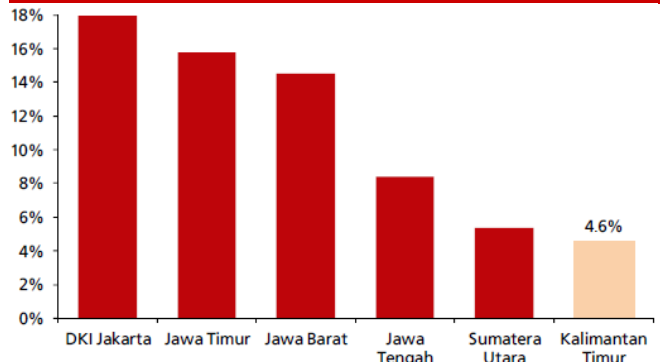
Given the bleak outlook for commodities this year, it was mildly surprising to find economic activities in Balikpapan and Samarinda were not too bad on the surface. The morning flight that we took to Balikpapan from Jakarta was full, and Garuda (GIAA) used a bigger plane, the Airbus A330 with c.300 seats instead of a Boeing 737-800 with less than 200 seats.

East Kalimantan is the 4th least-dense province



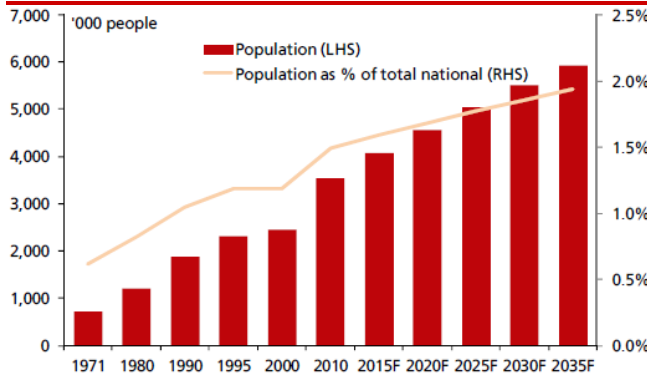
Source: DBS Vickers, National Statistic Bureau (BPS)

East Kalimantan – 6th largest contributor to national GDP



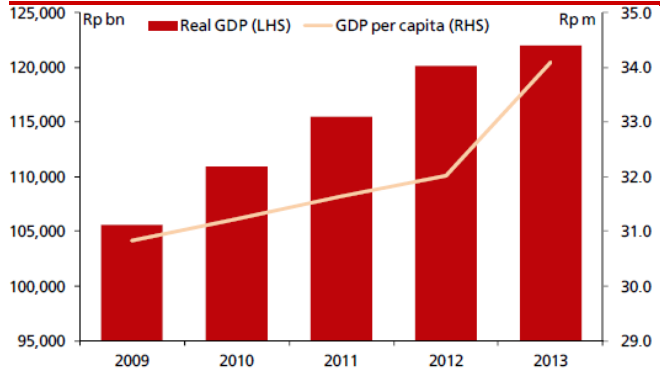
Source: DBS Vickers, National Statistic Bureau (BPS)

East Kalimantan population



Source: DBS Vickers, National Statistic Bureau (BPS)

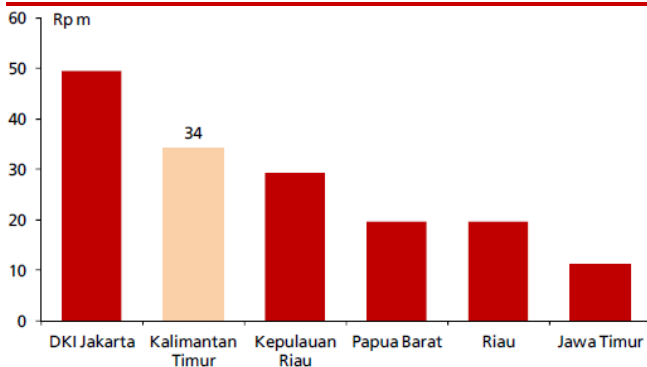
East Kalimantan – Real GDP and GDP per capita trend



Source: DBS Vickers, National Statistic Bureau (BPS)

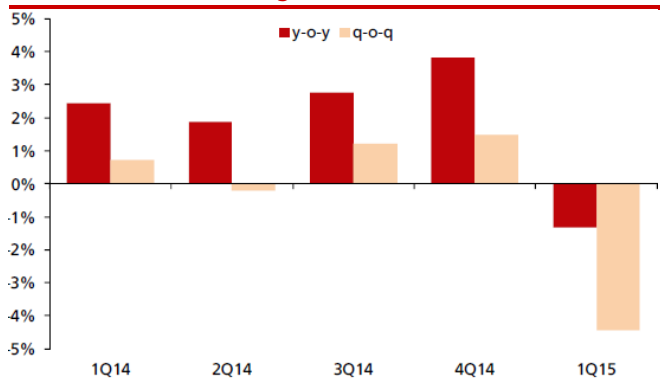
East Kalimantan's economy is highly dependent on its natural resources, particularly coal, oil and natural gas. Besides being the 6th largest contributor to national GDP, this commodity rich province (and relatively small population) has the 2nd highest GDP per capita in Indonesia after Jakarta.

East Kalimantan – 2nd highest GDP per capita



Source: DBS Vickers, National Statistic Bureau (BPS)

East Kalimantan – GDP growth data



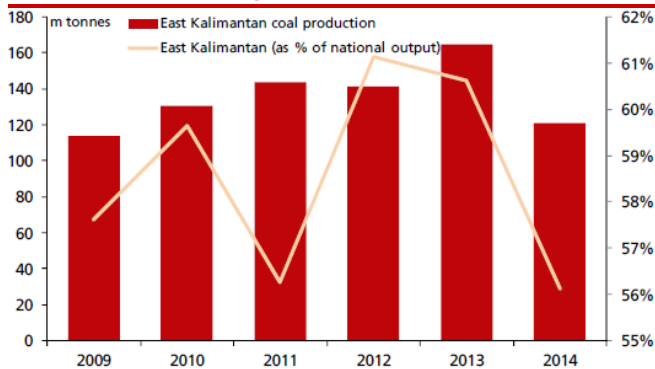
Source: DBS Vickers

Balikpapan & Samarinda

Coal industry – neither here nor there

East Kalimantan region, with its hundreds of mining sites, accounts for more than 55% of Indonesia’s thermal coal output. Abundant coal reserves and close proximity to ports (resulting in lower transportation cost and faster turnaround time) are the main advantages for mining concession owners in East Kalimantan.

East Kalimantan coal production



Source: Directorate General Minerals and Coal (part of Energy & Resources Ministry), DBS Vickers

Major coal producers in East Kalimantan

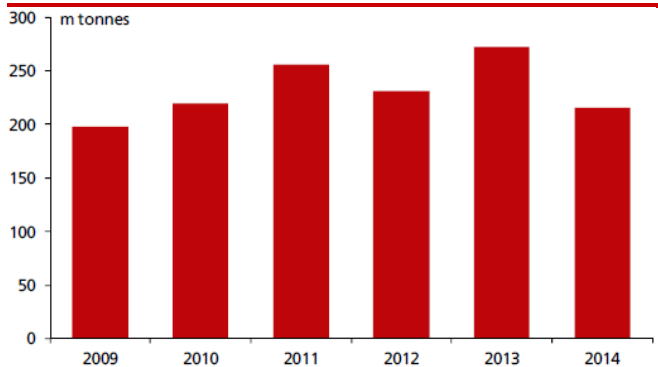
Concession	Company	Location	Concession area (ha)	2014 production (m tonnes)
Berau Coal	Berau Coal Energy (BRAU)	Berau	118,400	24
Kaltim Prima Coal	Bumi Resources (BUMI)	Sangata	90,960	22.3
Kideco	Indika Energy (INDY)	Pasir	50,921	40.3
Multi Harapan Utama	n/a	Busang	47,232	1.4
Tanito	Harum Energy (HRUM)	Samarinda	35,757	1.6
Indominco	Indo Tambangraya (ITMG)	Bontang	25,000	14.8
Gunung Bayan	Bayan Resources (BYAN)	Gunung Bayan	24,546	1.5
Insani Bara	Resource Alam Indonesia (KKGI)	Kutai Kertanegara	24,478	3.4

Source: Companies, DBS Vickers

Our checks with several local subcontractors confirmed our coal analyst’s view that most of the large miners are not cutting output in 2015. In particular, miners with a PKP2B (CCoW – Coal Contract of Work) license tend to have economies of scale, lower production cost, and a healthy balance sheet to deal with the current low coal prices. Their cash cost is low enough to allow them to remain profitable

although the coal price has dropped by 20% y-o-y to hover at US\$58 per ton (a level last seen in 2009).

Indonesia coal production



Source: Directorate General Minerals and Coal (part of Energy & Resources Ministry), DBS Vickers

According to the Energy and Resources Ministry, coal production in East Kalimantan dropped to 120m tonnes in 2014 from a peak of 165m tonnes in 2013. The biggest drops were seen at the small and illegal miners, as demand and prices dropped last year. The small miners, especially IUP holders, do not have the scale and or long term customers like the big miners do. Meanwhile, the illegal miners were also affected by the clean and clear regulation implemented last year. Approximately one third or all IUPs in East Kalimantan did not get the clean and clear clearance, which means they are not allowed to export their coal.

Coal barges on the Mahakam River



Source: DBS Vickers

How slow is the mining contracting business? Without giving specific figures, the subcontractors we met suggested they used to operate 24 hours a day before, but only 12 hours now. On top of that, miners are expecting better efficiency and lower costs to cope with lower coal prices. For the subcontractors, they are at the mercy of mine owners during

both good times and bad. Big mining contractors such as PAMA, Leighton and Theiss have either laid off or put a number of their employees on paid leave in the past several months.

Based on our conversation, utilisation rates for heavy equipment is currently below 50%, and there are many used equipment for sale at attractive prices. For example, a 2012 Scania 10-wheeler truck used for hauling coal can be purchased at c.Rp200m (compared to the original purchase price of Rp1.1bn). Given no growth in output and a large supply of heavy equipment in the market, demand for equipment is pretty much non-existent. Is it any wonder that United Tractors (UNTR)'s equipment segment is weak?

Overall, there is no doubt the coal mining industry is suffering from low coal prices. East Kalimantan experienced the biggest impact of the slide in the coal mining industry, because the region contributes more than 55% of national production. It will remain challenging in the foreseeable future and earnings of coal miners are expected to be down YoY this year on lower ASP and flat output volumes. Among the coal companies we cover, we like Adaro Energy (ADRO), but despite the cheap valuation, there is no catalyst for the sector currently. For more details on the outlook for thermal coal, refer to our report, *Lingering Pain*, dated 10 April 2015.

Balikpapan & Samarinda

Infrastructure sector – the classic example of slow progress

Under former President SBY's Masterplan for the Acceleration and Expansion of Indonesian Economic Development (MP3EI), one of the major regions on Kalimantan island to receive significant attention was East Kalimantan. It was designated the hub for mining, minerals and energy sectors in Indonesia. According to the plan, there were 157 projects planned for East Kalimantan, including 43 infrastructure projects worth over Rp40tn.

The vast size of the province (as big as Java island) needs infrastructure to support economic activity. Nevertheless, as we have witnessed, the progress of infrastructure development is slow; some have stalled or are well behind schedule.

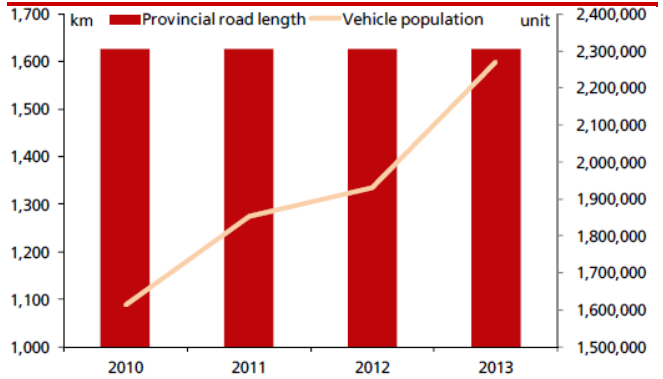
One big project that has not even taken off is the much needed 180km railway project (supposedly with UAE and Russian investors) to connect the northern and southern parts of East Kalimantan. The recent news indicated that work on this project will commence in 2016. Furthermore, under Jokowi's 2015-2019 plan, the central government will build a passenger train line in East Kalimantan using government budget (APBN) but we are not aware of any details on the project timetable.

East Kalimantan planned coal railway projects



Source: East Kalimantan provincial government

East Kalimantan provincial roads and traffic



Source: DBS Vickers, National Statistic Bureau (BPS)

Below is an update on those infrastructure projects we had the privilege to check out:

• **Balikpapan - Samarinda toll road**

It took us almost three hours to get from Balikpapan to Samarinda using the normal road, c.90km distance under good traffic conditions. The planned 99km toll road project is expected to cut the travel time by more than a half. Based on news, construction is just over 80% but the project has stalled for some time due to land clearing and budget issues.

Balikpapan – Samarinda toll road project details

Distance (km)	99.02
Value (Rp tr)	6.2
Planned since	2011
Project groundbreaking	2012
Expected date of completion	2013
Current status (% of completion)	±80%

Source: MP3EI plan, DBS Vickers

Balikpapan – Samarinda toll road (U/C)



Source: Antara news

- **Mahakam river bridge – the twin bridge**

The Mahakam bridge is the artery that connects the two sides of Samarinda city. Traffic is busy as the existing bridge only has one lane for each direction, and moreover, the bridge was built in 1987. A barge accident in 2010 caused this bridge connection to be closed temporarily and created major transportation havoc in the city.

This led to the calls for a new bridge, next to the existing one, creating a twin Mahakam river bridge. The bridge was supposed to be completed in 2014. But, here we are in mid-2015 and the foundation has not even been completed.

Proposed Mahakam twin bridge: project details

Distance (km)	0.4
Value (Rp tr)	0.383
Planned since	2011
Project groundbreaking	2012
Expected date of completion	2013 (1st phase), 2016 (final)
Current status	Foundation works only

Source: MP3EI plan, DBS Vickers

The plan - Proposed Mahakam twin bridge



Source: Antara news

The reality - bridge foundation still under construction



Source: DBS Vickers

- **New Samarinda airport**

- The length of the runway at the old airport, Temindung, is only 1.5km, which means it can only cater for smaller planes (e.g. propeller planes). Wider and bigger body planes or jets have to land at neighbouring city Balikpapan's Sultan Aji Muhammad Sulaiman International Airport. This can be challenging for some passengers – it is a seven-hour drive for those who want to visit/reach major coal production areas such as Berau, Sangatta, and tourist attractions such as Derawan Island.

New Samarinda Airport: project details

Annual passenger capacity (m people)	2.5
Runway (km)	2.5
Investment (Rp tr)	1.2
Planned since	2008
Project groundbreaking	2012
Expected date of completion	2016
Current status	Stalled

Source: MP3EI plan, DBS Vickers

The proposed new airport is supposed to be able to cater to Boeing 737 jets and process 2.5 million passengers annually. Apparently, the supporting facilities have been built, but budget limitations has stalled further works on both runways and apron. The locals are skeptical this airport would be operational by 2016.

Sadly, in Indonesia's history, infrastructure projects can be delayed and or face funding issues when managed by local governments, like the classic examples above. Recently, the central government decided to give funding aid from the central budget (APBN) for Samarinda's new airport and the Mahakam twin bridge. Therefore, these two projects are expected to be revived in 2H15. Overall, the situation in East Kalimantan is not different (if not worse) than infrastructure developments in other parts of Indonesia.

On the flipside, there are a lot infrastructure projects for this region which present huge opportunities for construction companies that we cover such as PTPP, Wijaya Karya, Waskita Karya and Wika Beton.

For the cement sector, we also did our channel checks on Chinese cement producer Anhui Conch (Conch) which commenced production at its manufacturing plant in Tanjung Tabalong, South Kalimantan late last year. The full capacity is c.1.5m tons annually. It started selling its products earlier this

year and the products are already available in Balikpapan and Samarinda as well. What we found is that prices are c.10% cheaper than products from Semen Indonesia and Indocement in East Kalimantan. The feedback is also good in general with customers saying that the quality is on par with the incumbents (i.e. Indocement (INTP) and Semen Indonesia (SMGR)) and better than Makassar-based cement producer Bosowa.

Cement Conch available in East Kalimantan



Source: DBS Vickers

However, Conch's distribution network is limited for now and a few stores that we visited did not have "Conch" in stock. These stores only obtain Conch's products from the local distributor on request basis. Our analyst Tjen-San in his report on Indonesia Infrastructure titled *Time to Deliver* on 26May2015 believes that supply is also a concern with new players such as Conch coming in with bigger capacities next year. We recommend to sell the cement players.

Property – the complementary segment

A few big developers, such as Agung Podomoro Land (APLN), Bumi Serpong Damai (BSDE) and Ciputra Development (CTRA) have presence in both Balikpapan and Samarinda, mostly through joint operation (JO) projects with local developers.

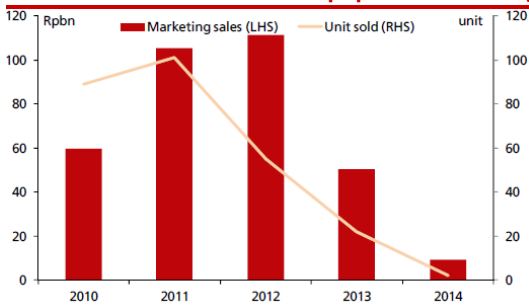
New property developments in Balikpapan are now more concentrated either along the main streets (Sudirman and M.T Haryono) or coastline facing Makassar Strait (an important sea lane in the Indonesia archipelago that connects two main islands in east Indonesia - Kalimantan and Sulawesi).

In Samarinda, the property developments are also concentrated along the banks of Mahakam River, the longest in East Kalimantan at 920km. The river opens out to the Makassar Strait.

Property development has stalled, and even shrank, in the last two years in these two cities as commodity prices tumbled. CTRA is a good proxy to current trends; marketing sales have been falling at Citra BukitIndah Balikpapan (launched in May 2008) and CitraLand City Samarinda (launched in Nov 2009).

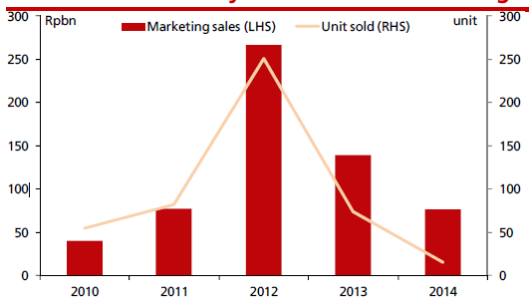
We will remain cautious towards the property sector given potential changes to tax regulations and slower unit demand growth going forward (discussed in our property sector reports *Tread carefully* dated 27 Apr 2015, and *When the going gets tough* dated 2 Dec 2014).

CTRA: Citra BukitIndah Balikpapan – marketing sales



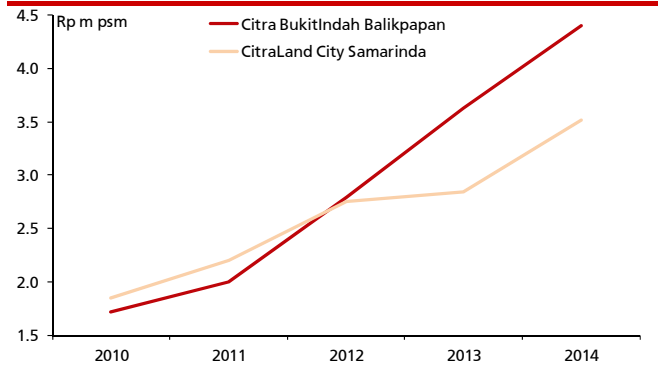
Source: DBS Vickers, Company

CTRA: CitraLand City Samarinda – marketing sales



Source: DBS Vickers, Company

CTRA: Land price psm trend



Source: DBS Vickers, Company

CTRA: Citra BukitIndah Balikpapan – township gate



Source: DBS Vickers

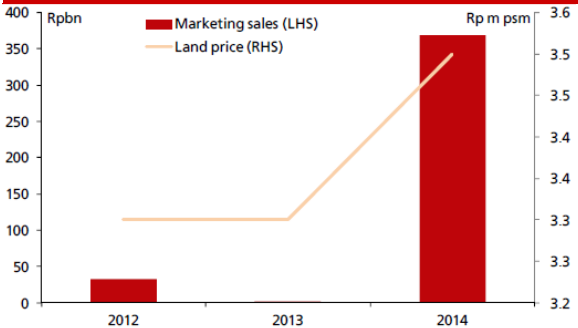
CTRA: Citra BukitIndah Balikpapan – typical unit



Source: DBS Vickers, Company

Balikpapan & Samarinda

BSDE: Grand City Balikpapan – marketing sales



Source: DBS Vickers, Company. Note: A jump in 2014 marketing sales was due to new project re-launch

APLN – Borneo Bay existing mall



Source: DBS Vickers

BSDE: Grand City Balikpapan – Amsterdam cluster gate



Source: DBS Vickers

APLN – Borneo Bay mall extension & apartments (U/C)



Source: DBS Vickers

BSDE: Grand City Balikpapan – typical luxury house



Source: DBS Vickers

BSDE: Bumi Samarinda project (to be launched soon) – gate and current raw land



Source: DBS Vickers

APLN – Borneo Bay Balikpapan (miniature model)



Source: DBS Vickers

Consumer – slower growth and generally more expensive

As highlighted in our ASEAN Consumer Food for thought titled *Moderate your appetite* released on 25 May 2015, 1Q15 results of consumer companies were mostly disappointing with slower-than-expected sales volume growth (reflecting generally slower domestic consumption this year).

The margins of consumer staples companies were somewhat saved by low raw material prices and the ability to adjust ASP to pass-on rising costs (such as logistics cost). We compared prices of basic food staples (such as instant noodles, coffee, flour, etc) in Hypermart (MPPA) and found that they are c.10% more expensive than prices in Jakarta. Better infrastructure in this region will help to bring down logistics cost, and the new government seems to realise this, and is trying to address the pressing issue.

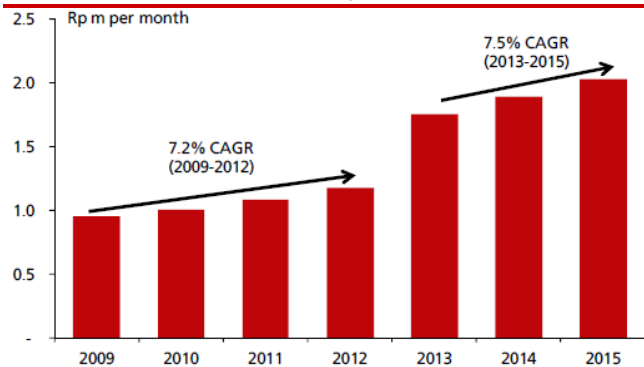
There is no buffer for consumer spending as the minimum wage has not risen significantly in the past few years (except the big jump from 2012 to 2013) and the gap with Jakarta’s has been widening over the past few years.

Hypermart grocery store in Plaza Balikpapan Mall



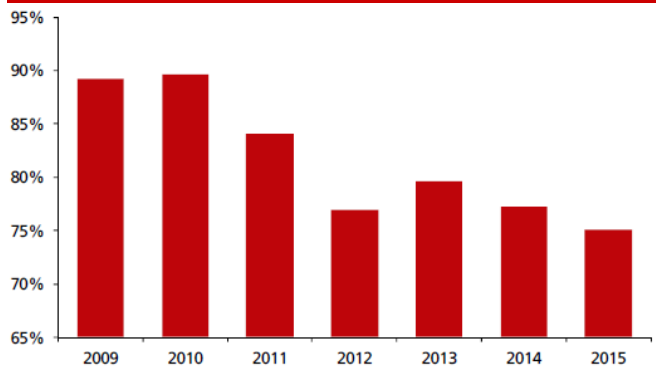
Source: DBS Vickers

East Kalimantan minimum wage trend



Source: DBS Vickers

East Kalimantan minimum wage as % of Jakarta’s



Source: DBS Vickers. Note: In 2015, Jakarta’s minimum wage is Rp2.7m per month, while East Kalimantan’s is Rp2.03m per month

Consumer discretionary players are unable to charge higher prices for the same items in more efficient market like Jakarta. Because of this, they are hit by both slower (or even negative) same store sales growth (SSSG) and higher overall cost.

We looked at Indonesia’s largest retailers by market capitalisation, Matahari Department Store (MDS), as a proxy to consumer discretionary spending. SSSG at MDS hit a 4-year low recently, partly dragged by stores in Kalimantan (estimate negative 7.5% SSSG in 1Q15). MDS has a big presence with three stores each in Balikpapan and Samarinda’s main retail malls. In addition, we did not see much traffic during weekday lunch time and after-work during our visits to several other retail chains such as home improvement store Ace Hardware (ACES), and Mitra Adiperkasa (MAPI) brand stores (e.g. Sports station, Payless, etc).

Denim section at MDS in Plaza Balikpapan Mall



Source: DBS Vickers

Balikpapan & Samarinda

MDS is the largest anchor in Mal Balikpapan Baru -



Source: DBS Vickers

MDS in E-Walk (retail mall in Balikpapan Superblock) -



Source: DBS Vickers

ACE stand-alone store in Balikpapan city center



Source: DBS Vickers

SportsStation stand-alone store in Balikpapan city center



Source: DBS Vickers

Payless shoe store in E-walk



Source: DBS Vickers

New retail mall (under-construction) along the Mahakam River with SOGO as main anchor tenant

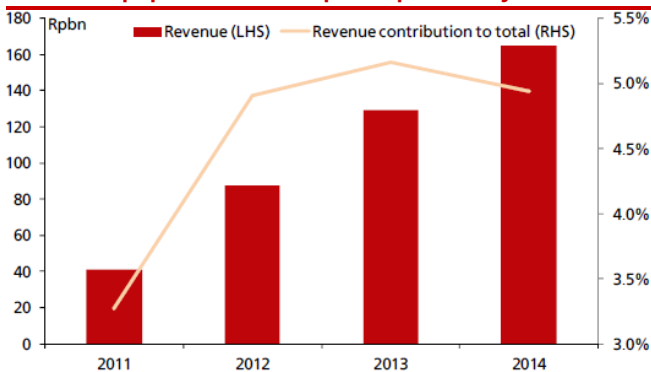


Source: DBS Vickers

Healthcare service – a real necessity

We visited Lippo Group’s Siloam Hospitals Balikpapan, which was acquired back in 30 Jan 2011. This hospital was formerly known as RS International Balikpapan in 2002 and RS Balikpapan Husada in 2007. The 8-floor hospital with 165 operational beds (out of 232 bed capacity) is one of the “matured” hospitals in Siloam Hospitals International (SILO)’s portfolio, generating 5% and 11% of consolidated revenue and net profit, respectively, in 2014.

SILO Balikpapan’s revenue quadrupled in 4 years

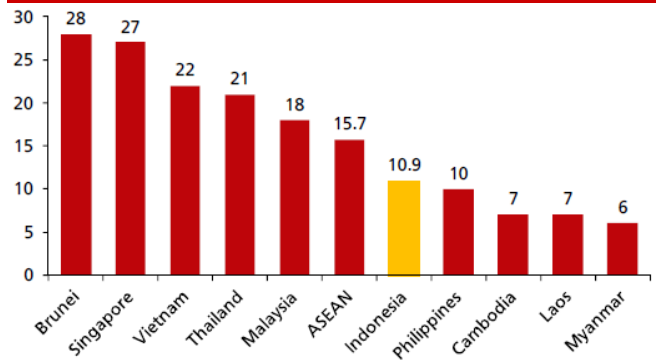


Source: DBS Vickers, Company

Siloam Hospital Balikpapan is a tertiary referral hospital with a large number of specialists to provide health care following referrals from primary and secondary care, and serve a lot of companies in the natural resources sector in he region (i.e. oil & gas and coal). Its overall bed occupancy rate (BOR) is c.65% (close to optimal level), and it is setting aside the required 48 beds (on 6th floor) for the much talked about universal health coverage program (JKN). About 30% of patients pay out of their own pockets for treatment, while the rest are paid by companies and insurers.

According to Indonesia’s Health Ministry data, there are 26 hospitals in both Balikpapan and Samarinda. With an estimated 3,000 beds, the bed to population ratio is respectable at 22 beds per 10,000 population (better than ASEAN average of 15.7 and above the national average of 10.9). The healthcare sector is still a growing sector in Indonesia.

Bed to 10,000 population (country comparison)



Source: CIA Factbook, Indonesia Ministry of Health, DBS Vickers

SILO Balikpapan



Source: DBS Vickers

SILO Balikpapan lobby – heavy crowd



Source: DBS Vickers

SILO Balikpapan emergency section



Source: DBS Vickers

SILO Balikpapan – BPJS section



Source: DBS Vickers

The helipad in the parking lot – for emergency cases



Source: DBS Vickers

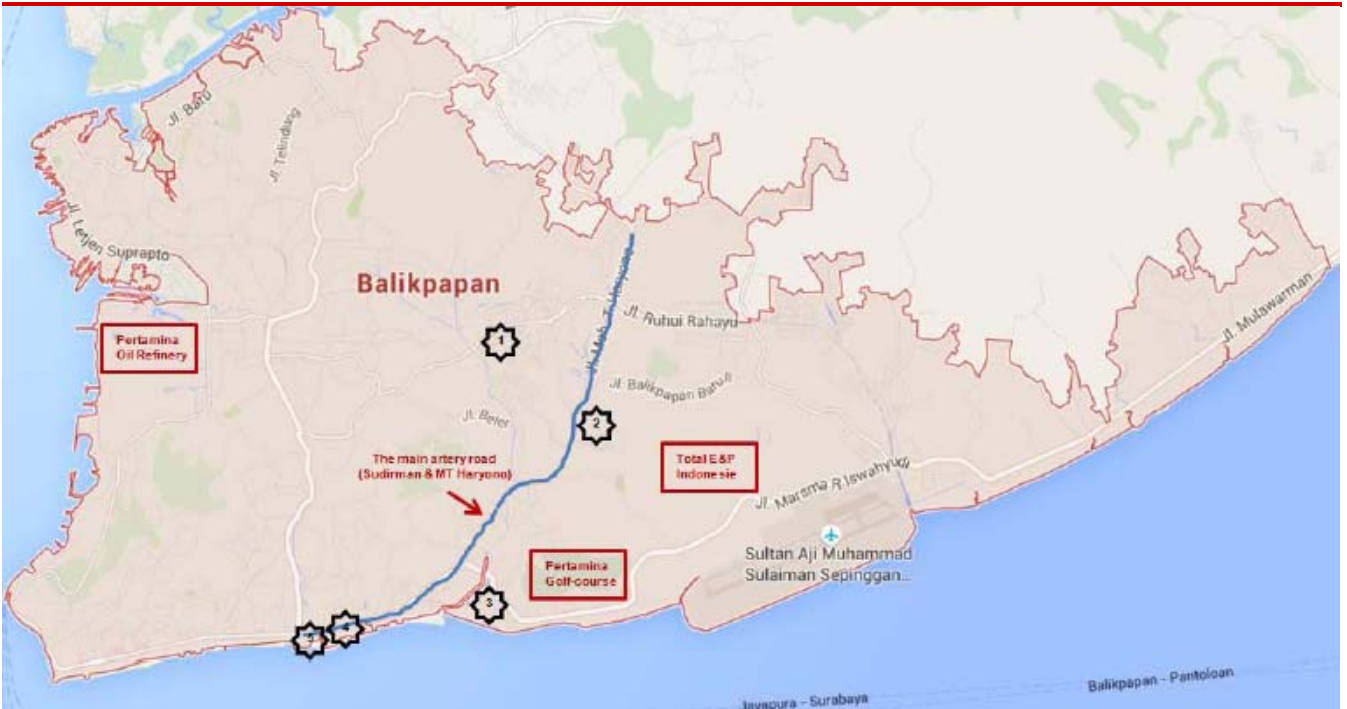
APPENDIX

Indonesia map



Source: DBS Vickers, Wikimedia.org

Balikpapan map: major property developments



Source: DBS Vickers, Google maps.

Legend: 1. Balikpapan Baru township (developed by Bumi Serpong Damai - BSDE); 2. Citra Bukit Indah Balikpapan township (developed by Ciputra Development - CTRA); 3. Balikpapan Superblock (developed by BSB); 4. Balcony City (potential acquisition by PTPP Properti - PPRO); 5. Borneo Bay Residence Superblock (developed by Agung Podomoro Land - APLN)

Samarinda map: major property developments



Source: DBS Vickers, Google maps

Legend: 1. CitraLand Samarinda township (developed by Ciputra Development - CTRA); 2. Bumi Samarinda township (developed by Bumi Serpong Damai – BSDE)

DBSV recommendations are based on an Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return i.e. > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

* Share price appreciation + dividends

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