



Research Paper

The Effect of Sustainable Alternative Cigarette to the Valuation of PT. Hanjaya Mandala Sampoerna, Tbk. (HMSP.JK)

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ABSTRACT: This research investigates the impact of sustainable alternative cigarettes on the valuation of PT Hanjaya Mandala Sampoerna Tbk (HMSP.JK), a leading tobacco company in Indonesia and a subsidiary of Philip Morris International (PMI), which is actively pursuing a smoke-free future. With growing global awareness of the health risks associated with traditional cigarettes, there has been a shift towards alternative tobacco products perceived as less harmful. This study evaluates how the introduction and adoption of these alternative products influence the company's market valuation. Using a comprehensive valuation model that integrates financial analysis, industry trends, and potential growth of the alternative cigarette market, the research applies discounted cash flow (DCF) analysis to the projected 10Y HMSP's FCF. The evaluation was conducted under three scenarios based on the rate of acceptance of Heated Tobacco Sales (HTU) in the market both domestic and international. In the scenario analysis, the projected stock price varies significantly depending on the rate of HTU sales. Under the most optimistic scenario (Scenario 3/10% HTU revenue mix), the stock price shows substantial upside potential up to 92% with intrinsic value of Rp. 1,297. The market price of HMSP's share is at Rp. 675 as of August 1, 2024, which indicated that current share price is undervalued. Therefore, it is recommended for investor to buy HMSP stock at current price. Based on these insights, the Author recommends that Sampoerna's management focus on accelerating the adoption of alternative products, navigating regulatory challenges proactively, and enhancing consumer education to solidify its market position in this evolving landscape.

KEYWORDS: Heated tobacco unit, tobacco, business diversification, valuation

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I. INTRODUCTION

The tobacco industry is undergoing a significant transformation, driven by innovation and sustainability (Philip Morris International Inc., 2017). As the demand for environmentally and socially responsible practices grows, the sector is shifting toward alternative smoking options. This study examines the impact of sustainable alternative cigarettes on the valuation of Sampoerna, a subsidiary of Philip Morris International (PMI) and a key player in the Indonesian market.

Recent data highlights the increasing popularity of products like IQOS, PMI's heat-not-burn device, reflecting a broader trend toward alternative smoking solutions. Southeast Asia's e-cigarette market, particularly in Indonesia, is projected to experience substantial growth, positioning IQOS as a strategic innovation for Sampoerna. This shift could significantly enhance Sampoerna's market standing and revenue potential.

Sampoerna, established in 1913, has long been a prominent figure in Indonesia's tobacco industry, known for its iconic Dji Sam Soe brand. As a subsidiary of PMI, Sampoerna has embraced smoke-free alternatives, aligning with PMI's vision of a smoke-free future. The company's recent investment in a smoke-free products factory in Karawang, West Java, underscores its commitment to sustainable economic value in Indonesia. IQOS, developed by PMI, reduces harmful chemical emissions by 90-95% (Farsalinos, 2018) compared to traditional cigarettes, making it a viable alternative for adult smokers. Sampoerna's introduction of the IQOS ILUMA, featuring advanced technology, further emphasizes its role in leading the market toward a smoke-free future.

II. PROBLEM STATEMENT

Figure II.1 HMSP Stock Price



HMSP's stock price has consistently declined over the past five years, largely due to the COVID-19 pandemic and continuous increases in excise tariffs by the Indonesian government. As a mature market leader in the tobacco industry, HMSP risks being viewed as a "sunset company" in the decline phase of its life cycle. Over this period, the stock value has dropped by 75%, posing significant challenges for investors.

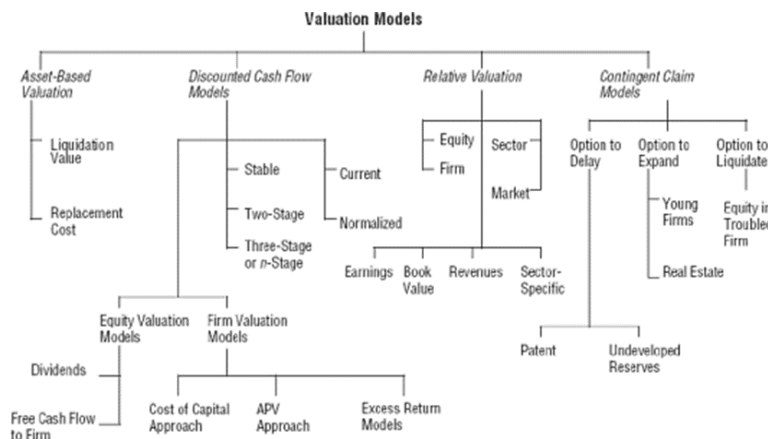
This study seeks to answer the question: "How does the introduction of sustainable alternative cigarettes impact the valuation and market position of Sampoerna in the Indonesian tobacco industry?". To address this, the research will:

- Analyze HMSP's financial health and value the company's stock price.
- Provide investors with a recommendation regarding HMSP's stock based on the company's valuation.
- Offer management strategies to enhance HMSP's valuation.

III. LITERATURE REVIEW

III.1 Stock Valuation

Figure III.1 Valuation Models (Damodaran, 2012)



Damodaran (2012) outlines four key valuation models: Asset-Based Valuation, Discounted Cash Flow (DCF), Relative Valuation, and Contingent Claim Valuation. Asset-Based Valuation calculates a company's value based on net asset value (NAV) minus liabilities, often used for firms with substantial tangible assets (Penman, 2013). DCF models, considered reliable for companies with stable cash flows, discount expected future cash flows to determine present value (Koller et al., 2020). Relative Valuation compares a firm's value to similar companies using multiples like Price-to-Earnings (P/E) or EV/EBITDA, commonly employed in equity analysis (Damodaran, 2012; Koller et al., 2020). Contingent Claim Valuation applies option pricing for assets with option-like characteristics but is not used in this study as it focuses on HMSP stock valuation.

The DCF model evaluates intrinsic value by discounting expected future benefits, including dividends (Pinto et al., 2010) or free cash flow (Berk and Demarzo, 2017). The Dividend Discount Model (DDM) suits companies with consistent dividends, while the Free Cash Flow to the Firm (FCFF) model is better for firms

without a clear dividend history (Fernández, 2007). Relative Valuation uses stock price or EV multiples based on fundamental variables like revenues or earnings, providing a comparative measure of intrinsic value (Koller et al., 2020).

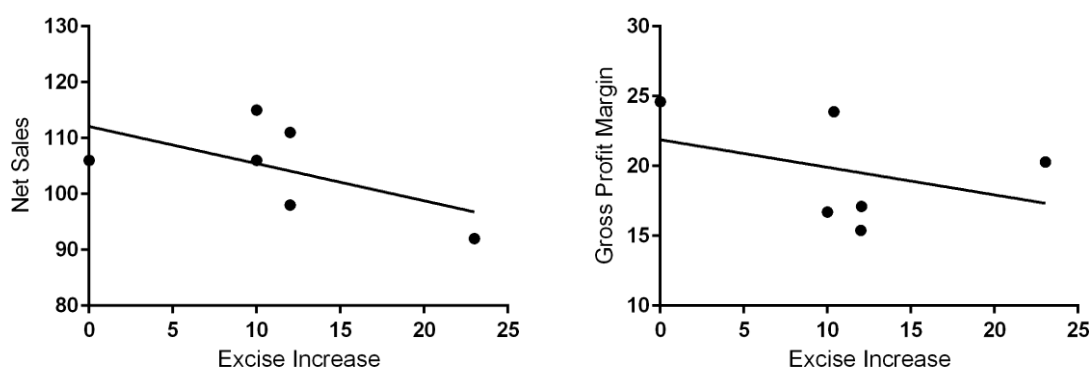
III.2 Cigarette Excise Tax

Figure III.2 Cigarette Excise Tariffs Increase YoY

Excise Tariff Increase	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
	9%	11%	11%	10%	0%	23%	12%	12%	10%	10%

Cigarette excise taxes, a form of indirect taxation, aim to generate revenue and mitigate smoking-related public health issues by addressing the negative externalities of tobacco consumption (Chaloupka et al., 2012; Jha and Peto, 2014). Higher taxes discourage smoking, especially among youth and low-income groups, and fund public health initiatives (Goodchild et al., 2016; World Health Organization (WHO), 2019). Indonesia's consistent increases in cigarette excise tariffs, like the 23.05% rise in 2020 and 12.05% in 2021, reflect a public health strategy to curb smoking (Van walbeek et al., 2013). These policies challenge companies like Sampoerna to maintain profitability and market share amid rising costs and shifting consumer behavior.

Figure III.3 Linear Regression of Cigarette Excise Tax Increase to Revenue & GPM



In examining the relationship between cigarette excise tax and its impact on sales, a regression analysis reveals a negative correlation between tax rates and net sales, with a slope of -0.6646 indicating that a 1% increase in tax leads to a 0.5 trillion IDR decrease in sales. Similarly, a 1% tax increase correlates with a 0.1974% decrease in Gross Profit Margin (GPM), showing the excise tax's significant impact on profitability.

III.3 ESG – Financial Performance Relationship

Sustainability in business, encompassing economic, environmental, and social dimensions, has shifted from a peripheral concern to a central strategic issue (Elkington, 1998; Porter and Kramer, 2006). Theoretical frameworks like Stakeholder Theory and the Resource-Based View (RBV) suggest that companies considering stakeholder interests and developing sustainable capabilities gain a competitive advantage (Edward Freeman and Phillips, 2002; Hart and Dowell, 2011).

Empirical research on the financial impact of sustainability shows mixed results. Some studies find a positive correlation between sustainability practices and financial performance, citing improved risk management, innovation, and customer loyalty (Margolis and Walsh, 2003; Eccles et al., 2014). However, others report neutral or negative impacts, highlighting the potential for significant upfront costs that may affect short-term profitability (Brammer et al., 2006; Schaltegger and Wagner, 2006).

Sustainability impacts financial performance through risk management, cost savings, revenue growth, and access to capital (Bhattacharya and Sen, 2004; Cheng et al., 2013; Clark L. et al., 2015). Companies with strong sustainability practices often enjoy lower risks, operational efficiencies, increased sales, and better access to capital, enhancing overall financial performance.

III.4 Internal Analysis

Sampoerna, a leading tobacco company in Indonesia, exhibits a strong position in the market due to several key strengths. Its established brand and extensive distribution network bolster its market presence, while its financial strength facilitates significant investments in research and development, marketing, and new product innovations such as Heated Tobacco Units (HTUs). As a subsidiary of Philip Morris International

(PMI), Sampoerna benefits from PMI's global expertise and strategic focus on harm reduction, enhancing its competitive edge through the early introduction of HTUs in the Indonesian market.

However, Sampoerna faces notable weaknesses. The high initial costs associated with developing and marketing HTUs could impact short-term profitability. The potential for cannibalization of traditional cigarette sales by HTUs poses a risk, as does the challenge of gaining consumer awareness and acceptance for these new products. Additionally, the reliance on imported components for HTUs can lead to higher production costs and expose the company to exchange rate fluctuations. Regulatory uncertainties regarding new tobacco products further complicate the product launch and long-term strategy.

The financial analysis of HMSP provides a detailed view of the company's financial health. The examination of current assets shows a significant fluctuation in cash and cash equivalents, with a rise in 2021 followed by a steep decline by 2023. This pattern suggests substantial expenditures or settlements of liabilities. Additionally, there was a dramatic reduction in time deposits over the years, indicating a strategic shift in the company's cash management approach. Trade receivables from third parties experienced variability, while inventories remained relatively stable, reflecting consistent management of inventory levels.

In terms of non-current assets, the analysis shows a peak in advance for fixed asset acquisitions in 2022, followed by a sharp drop in 2023. This could be due to the completion of significant acquisitions or a strategic change in focus. The company's fixed assets steadily increased, highlighting ongoing investments in property, plant, and equipment. However, there was an overall decline in total non-current assets, which may indicate divestments or a reduction in long-term investments.

The review of current liabilities reveals substantial increases, particularly in trade and other payables, which rose possibly due to expanded operational activities. The excise tax payable more than doubled over the analyzed period, reflecting higher production levels or changes in tax rates. The overall increase in current liabilities could impact on the company's liquidity, signaling a rise in short-term obligations.

Looking at the income statements, HMSP showed a recovery in net revenues following the challenges posed by the COVID-19 pandemic. Gross profit improved, and earnings per share (EPS) also increased by 2023, reflecting the company's rebound. The product mix is primarily dominated by machine-rolled cigarettes, with notable growth observed in segments like hand-rolled cigarettes and heated tobacco units. These segments, though smaller, showed significant potential within the company's overall product portfolio.

Analyzing key financial metrics, HMSP's profitability indicators like EPS and return on equity (ROE) have not yet returned to pre-pandemic levels, with EPS peaking at 118 in 2019 before dropping to 54 in 2022 and slightly recovering to 70 in 2023. Dividend per share (DPS) also declined from 119.8 in 2020 to 54.7 in 2023, though dividend yields rebounded to 7.4% in 2023, indicating some recovery in investor confidence. Valuation metrics show a decrease in the price-to-earnings (P/E) ratio from 17.4x in 2019 to 13.6x in 2023, suggesting reduced market optimism about the company's growth prospects. Revenue growth rebounded to 12.5% in 2022 but slowed to 4.3% in 2023, and while margins have shown signs of stabilization, they remain below pre-pandemic levels.

In comparison to its peers, HMSP, as a market leader in Indonesia's tobacco industry, shows signs of stagnation in growth when compared to smaller competitors like Wismilak (WIIM). Despite facing higher excise taxes due to its tier-1 status, HMSP maintains a greater gross profit margin (GPM) due to its product mix, which includes a higher percentage of hand-rolled cigarettes (SKT). Solvency-wise, HMSP's debt-to-equity ratio (DER) of 0.8x indicates manageable leverage with a strong interest coverage ratio of 275.1x. However, its shares are considered more expensive compared to its peers, reflected in higher price-to-earnings and price-to-book ratios.

III.5 External Analysis

Heated Tobacco Products (HTPs), also known as heat-not-burn (HnB) products, represent a significant innovation in the tobacco industry. Unlike traditional cigarettes, which burn tobacco to produce smoke, HTUs heat tobacco to release nicotine and flavors without combustion (World Health Organization, 2023). This heating process generates an aerosol with significantly fewer harmful chemicals compared to cigarette smoke (Simonavicius et al., 2019). Despite these benefits, HTUs still deliver nicotine and are not entirely risk-free, though they present a potential reduction in smoking-related disease risks (Glasser et al., 2017).

The technological mechanisms behind HTUs include resistive and induction heating. PMI's Tobacco Heating System (THS), marketed as IQOS, uses these methods to heat specially designed tobacco sticks. Resistive heating involves either internal or external elements to raise the temperature of the tobacco (Farsalinos, 2018). Induction heating uses a magnetic field to heat a metallic element in the stick, which in turn heats the tobacco (Farsalinos and Polosa, 2014). Scientific studies suggest that HTUs can reduce harmful chemicals by 90-95% compared to traditional cigarettes (Farsalinos, 2018), although ongoing research is necessary to fully understand their health impact (Breland et al., 2018). The aerosols from HTUs, unlike smoke,

result in lower concentrations of harmful compounds, improving indoor air quality (Goniewicz et al., 2018; McNeill et al., 2018).

Sampoerna's Heated Tobacco Units (HTUs) are navigating a multifaceted environment shaped by insights from PESTLE, Porter's Five Forces, and SWOT analyses. The PESTLE analysis highlights that Indonesia's regulatory framework is stringent, with strict controls on tobacco advertising, packaging, and sales that extend to HTUs. High excise taxes and government health initiatives targeting smoking reduction may affect HTU pricing and marketability. Economic factors such as inflation and currency fluctuations impact production costs and consumer purchasing power, crucial in a price-sensitive market.

From a Porter's Five Forces perspective, the threat of new entrants is moderate due to high barriers such as regulatory requirements and substantial capital needs. However, the relatively new HTU segment might present lower barriers for innovative entrants. Supplier bargaining power is generally low to moderate, with Sampoerna's diverse sourcing strategy mitigating risks, though crucial component suppliers may hold more sway. Buyer power remains moderate; while consumers face limited individual bargaining power, the presence of alternatives like e-cigarettes heightens competition. The threat of substitutes is high, given the availability of traditional cigarettes and other nicotine replacement therapies. Industry rivalry is intense, driven by numerous competitors and the need for differentiation.

The SWOT analysis reveals several opportunities, including the rising demand for healthier smoking alternatives and advancements in tobacco heating technology, which could enhance HTU performance and market appeal. Strategic partnerships and potential international expansion further support growth prospects. However, Sampoerna faces significant threats from intense competition and regulatory challenges. Public perception issues regarding HTUs, despite their reduced harm, and economic downturns pose additional risks. Technological risks related to HTU performance also need to be managed carefully.

Integrating PESTLE, Porter's Five Forces, and SWOT analyses provides a comprehensive view of the challenges and opportunities Sampoerna faces in the HTU market. Addressing regulatory pressures, economic conditions, competitive forces, and technological advancements will be crucial for leveraging HTUs' potential and achieving success in a competitive landscape.

IV. METHODOLOGY

This research employs both qualitative and quantitative methodologies to estimate HMSP's intrinsic value and refine the supporting assumptions. The quantitative aspect uses the Discounted Cash Flow (DCF) method, specifically focusing on Free Cash Flow to the Firm (FCFF), while qualitative methods include SWOT, PESTLE, and Porter's Five Forces analyses. These analyses help to evaluate the internal and external factors influencing HMSP's stock value.

The research begins by addressing the issue of HMSP's declining stock price, reviewing literature on external and internal factors through PESTLE, Porter's Five Forces, and SWOT analyses. For valuation, the research integrates both intrinsic and relative approaches. The intrinsic valuation employs the DCF method to project future cash flows and discount them to present value, providing a detailed assessment of HMSP's intrinsic stock value. Relative valuation compares HMSP's financial ratios historically and with industry peers to benchmark its market value.

Data collection involved sourcing information from Sampoerna's and PMI's official channels, such as corporate websites, annual reports, and financial statements. Additionally, professional analyses from sekuritas, online brokerages, and finance websites offered expert insights and market trends. Supplementary data from online articles and previous research on Sampoerna and the tobacco industry provided contextual information on industry trends and regulatory developments.

Data analysis utilized SWOT to assess internal capabilities and challenges, while PESTLE and Porter's Five Forces frameworks evaluated the external competitive environment. This integrated approach ensured a comprehensive and accurate valuation of Sampoerna's stock, grounded in both qualitative and quantitative assessments.

V. RESULT AND DISCUSSION

V.1 Analysts' Report & Consensus

HMSP is navigating a challenging environment characterized by declining sales volumes, intensified competition, and rising costs driven primarily by increased excise taxes. The shift in consumer preference towards more affordable alternatives has pressured HMSP's premium cigarette brands, resulting in a decrease in market share and overall profitability. The rise of the illicit cigarette trade further exacerbates competition, impacting the company's performance. To sustain its market position, HMSP will need to manage these challenges effectively by controlling costs. Investors should weigh the risks of continued margin pressure and competitive threats against the potential for modest revenue growth and stabilization in profitability.

Recent financial performance underscores these challenges. Sales volume declined by 5.7% YoY in 2Q2024, influenced by higher average selling prices and increased excise taxes, which led to a shift towards lower-priced cigarettes and reduced HMSP's market share. The gross profit margin fell to 13.7% in 2Q2024 due to rising raw material costs and higher taxes, resulting in a 33% YoY drop in net profit. Operating margins are anticipated to stabilize between 7.8% and 8.1% over the next two years, reflecting ongoing cost pressures. Revenue is projected to grow modestly, from IDR 115.9 trillion in 2023 to IDR 129.9 trillion by 2025. However, competitive pressures and rising costs are expected to continue limiting margin expansion and profit growth.

Table V.1 Analysts' Target Price

Securities	Target Price (TP)	Upside/ Downside %	Report Date
Binaartha Sekuritas	IDR 815	21%	August 2, 2024
BRI Danareksa Sekuritas	IDR 730	8%	July 17, 2024
BCA Sekuritas	IDR 950	41%	July 15, 2024
Sucor Sekuritas	IDR 1,565	132%	July 15, 2024
Average	IDR 1,015	50%	

In terms of valuation and investment outlook, HMSP's stock reflects cautious market sentiment. Target prices range from IDR 730 to IDR 1,565, with potential upsides driven by anticipated improvements in demand and margins later in 2024. Investment recommendations vary from BUY to HOLD, with some analysts adopting a NEUTRAL stance. BUY recommendations are based on expectations of demand recovery, while HOLD and NEUTRAL recommendations reflect concerns about the company's ability to maintain profitability amid rising excise taxes and increased competition.

V.2 Intrinsic Valuation

This research aims to assess the impact of HMSP's transition from conventional cigarettes to sustainable Heated Tobacco Units (HTUs) on the company's valuation by exploring three scenarios for 2033: Scenario 1 with 2% HTU sales, Scenario 2 with 5% HTU sales, and Scenario 3 with 10% HTU sales. The business-as-usual scenario assumes HMSP will largely maintain its focus on conventional cigarettes with minimal growth in HTUs. Conversely, the transition scenarios project a gradual phase-out of conventional cigarettes in favor of expanding the HTU segment to meet sustainability goals.

For valuation, both intrinsic and relative methods are employed. The intrinsic valuation method, which focuses on determining a company's true value based on its fundamental attributes and future cash flows (Damodaran, 2012; Koller et al., 2020), is used here. This method contrasts with relative valuation, which compares a company's metrics to market benchmarks (Penman, 2013). To enhance the valuation accuracy, a relative valuation approach is also included.

The primary intrinsic valuation technique utilized is the Discounted Cash Flow (DCF) analysis, which calculates the Net Present Value (NPV) of a company's future cash flows using a discount rate. The DCF formula requires accurate projections of future cash flows and an appropriate discount rate. The Weighted Average Cost of Capital (WACC) is used to determine this discount rate, taking into account the costs of equity and debt, and their proportions in the company's capital structure. This approach provides a comprehensive view of the company's risk and return dynamics, supporting a more precise valuation of HMSP's future cash flows.

a. Capital Value

The market value of the debt is calculated using the book value of HMSP's debt obtained from the 2023 audited financial statement.

Table V.2 Capital Value

Capital	Value	Source
Debt		
Related Party Loan (IDRm)	11,462,164	2023 Annual Report
Lease (IDRm)	445,289	2023 Annual Report
Total Debt	11,907,453	
Equity	29,869,853	2023 Annual Report
Total Capital (IDRm)	41,777,306	

b. Cost of Debt Calculation

As stated in the annual report, HMSP debt is financed by its subsidiaries of the controlling shareholder the Cost of Debt are as follows:

Table V.3 Cost of Debt

Related Parties	Interest Rate (Avg.)	Source
PT Philip Morris Finance SA	6.05%	2023 Annual Report
PT Philip Morris Indonesia	6.09%	2023 Annual Report

c. Cost of Equity Calculation

The risk-free rate of 6.99% is based on the yield of Indonesia's 10-year Government Bond as of July 2024. The company's beta was sourced from Pefindo as of April 18, 2024. Lastly, according to Damodaran's Country Default Spreads and Risk Premiums, Indonesia's Equity Risk Premium is 7.38%. With these inputs, the Cost of Debt calculation is as follows:

Table V.4 Cost of Equity

Cost of Equity	Value	Sources
Indonesia Risk Free Rate	6.99%	PHEI
Beta	0.234	Pefindo
Equity Risk Premium	7.38%	Damodaran
Cost of Equity	8.71%	

d. WACC Calculation

After Cost of Debt and Cost of Equity are obtained, WACC can be calculated, with detail as follows:

Table V.5 WACC

Calculation	Value
Weight of Debt	29%
Weight of Equity	71%
Total Weight	100%
Weighted of Debt Cost	1.73%
Weighted of Equity Cost	6.23%
WACC	7.96%

e. Income Statement Projection

By using the assumptions mentioned above, Author makes income statement projection for all product segments. The consolidation income statement projection under all scenarios is as follows:

Table V.6 Scenario 1 Income Statement Projection

(IDRb)	2023	P. 2024	P. 2025	P. 2026	P. 2027	P. 2028	P. 2029	P. 2030	P. 2031	P. 2032	P. 2033
Revenue	115,983	119,875	125,153	131,275	138,386	146,669	156,347	167,708	181,115	197,037	216,079
<i>Growth (%)</i>	20%	10%	10%	10%	10%	10%	10%	10%	10%	10%	10%
COGS	96,653	94,937	98,092	101,777	106,081	111,116	117,021	123,972	132,196	141,980	153,701
COGS/Revenue	83%	79%	78%	78%	77%	76%	75%	74%	73%	72%	71%
Gross Profit	19,330	24,938	27,061	29,498	32,305	35,553	39,326	43,736	48,920	55,056	62,378
SGA	8,977	10,717	11,189	11,736	12,372	13,112	13,977	14,993	16,192	17,615	19,317
EBIT	10,353	15,582	17,292	19,251	21,504	24,105	27,123	30,645	34,783	39,677	45,512
Interest	42	43	45	47	50	53	56	60	65	71	78
EBT	10,311	15,523	17,231	19,187	21,436	24,033	27,047	30,564	34,695	39,581	45,407
Tax	2,214	2,278	2,378	2,494	2,629	2,787	2,971	3,186	3,441	3,744	4,106
Net Income	8,097	12,462	14,035	15,834	17,902	20,287	23,054	26,281	30,069	34,549	39,888

Table V.7 Scenario 2 Income Statement Projection

(IDRb)	2023	P. 2024	P. 2025	P. 2026	P. 2027	P. 2028	P. 2029	P. 2030	P. 2031	P. 2032	P. 2033
Revenue	115,983	120,098	125,656	132,126	139,668	148,477	158,801	170,947	185,306	202,379	222,810
Growth (%)	20%	12%	12%	12%	12%	12%	12%	12%	12%	12%	12%
COGS	96,653	95,088	98,433	102,354	106,949	112,341	118,683	126,166	135,035	145,599	158,261
COGS/Revenue	83%	79%	78%	77%	77%	76%	75%	74%	73%	72%	71%
Gross Profit	19,330	25,010	27,223	29,772	32,718	36,136	40,118	44,781	50,271	56,780	64,549
SGA	10,369	10,737	11,234	11,812	12,486	13,274	14,197	15,283	16,566	18,093	19,919
EBIT	8,961	15,609	17,382	19,421	21,772	24,493	27,660	31,363	35,719	40,879	47,035
Interest	42	43	45	48	50	53	57	62	67	73	80
EBT	8,920	15,551	17,322	19,357	21,704	24,422	27,583	31,281	35,630	40,782	46,928
Tax	2,204	2,282	2,387	2,510	2,654	2,821	3,017	3,248	3,521	3,845	4,233
Net Income	6,716	12,499	14,131	16,005	18,163	20,661	23,564	26,958	30,948	35,673	41,308

Table V.8 Scenario 3 Income Statement Projection

(IDRb)	2023	P. 2024	P. 2025	P. 2026	P. 2027	P. 2028	P. 2029	P. 2030	P. 2031	P. 2032	P. 2033
Revenue	115,983	120,286	126,117	132,975	141,058	150,614	161,953	175,471	191,670	211,193	234,874
Growth (%)	20%	14%	14%	14%	14%	14%	14%	14%	14%	14%	14%
COGS	96,653	95,215	98,745	102,929	107,891	113,788	120,818	129,231	139,345	151,570	166,433
COGS/Revenue	83%	79%	78%	77%	76%	76%	75%	74%	73%	72%	71%
Gross Profit	19,330	25,071	27,372	30,046	33,167	36,825	41,135	46,240	52,324	59,623	68,441
SGA	10,369	10,754	11,275	11,888	12,611	13,465	14,479	15,687	17,135	18,881	20,998
EBIT	8,961	15,653	17,490	19,619	22,096	24,992	28,395	32,418	37,203	42,934	49,848
Interest	42	43	45	48	51	54	58	63	69	76	85
EBT	8,920	15,595	17,429	19,555	22,028	24,919	28,317	32,334	37,112	42,834	49,737
Tax	2,204	2,285	2,396	2,527	2,680	2,862	3,077	3,334	3,642	4,013	4,463
Net Income	6,716	12,539	14,230	16,186	18,461	21,117	24,238	27,925	32,309	37,558	43,888

Based on the income statement projections, the profitability under the HTU transition scenario is better than that of the BAU scenario. In the BAU scenario, conventional cigarettes remain the primary revenue stream, though their share decreases slightly over the years (SKM & SPM). In contrast, the HTU transition scenario shows a more significant reduction in the revenue contribution from conventional cigarettes, though they still dominate HMSP's overall revenue. However, this is still far from PMI's goal of achieving a 50% revenue contribution from smoke-free products by 2030. The Author's analysis suggests that this target may be challenging to reach, as the mass market in Indonesia continues to prefer conventional cigarettes.

f. Discounted FCFF Projection

Depreciation and CAPEX are calculated based on HMSP's 2023 Financial Statements, while WC Inv. percentages are sourced from Damodaran are calculated based on their ratios to company sales, the numbers are:

Table V.9 FCFF Assumption Calculation

Depreciation/ Sales	CAPEX/ Sales	WC/Sales	Terminal Growth
0.98%	1.47%	13%	2%

For terminal value calculation, Author assumes a conservative 2% figure of terminal growth rate which is a little lower than HMSP's 5Y average revenue growth at 2.72% nor Indonesia's 5Y GDP growth & inflation rate average at 3.4% and 2.89% respectively.

With all the necessary information in place, the FCFF and its Present Value, or discounted FCFF, for the next 10 years can now be calculated. The present value of FCFF calculations for all scenarios are as follows:

Table V.10 Scenario 1 FCFF Projection

(IDRb)	P. 2024	P. 2025	P. 2026	P. 2027	P. 2028	P. 2029	P. 2030	P. 2031	P. 2032	P. 2033
Revenue	119,875	125,153	131,275	138,386	146,669	156,347	167,708	181,115	197,037	216,079
EBIT	15,582	17,292	19,251	21,504	24,105	27,123	30,645	34,783	39,677	45,512
EBIT (1-Tax)	15,523	17,231	19,187	21,436	24,033	27,047	30,564	34,695	39,581	45,407
Depreciation	1,175	1,226	1,286	1,356	1,437	1,532	1,644	1,775	1,931	2,118
CAPEX	1,762	1,840	1,930	2,034	2,156	2,298	2,465	2,662	2,896	3,176
Delta WC Inv.	15,527	16,210	17,003	17,925	18,997	20,251	21,722	23,459	25,521	27,988
FCFF	(591)	407	1,541	2,834	4,318	6,030	8,020	10,348	13,095	16,361
Terminal Value										279,985
PV FCFF	(550)	353	1,240	2,122	3,008	3,908	4,835	5,804	6,832	143,844

Table V.11 Scenario 2 FCFF Projection

(IDRb)	P. 2024	P. 2025	P. 2026	P. 2027	P. 2028	P. 2029	P. 2030	P. 2031	P. 2032	P. 2033
Revenue	120,098	125,656	132,126	139,668	148,477	158,801	170,947	185,306	202,379	222,810
EBIT	15,609	17,382	19,421	21,772	24,493	27,660	31,363	35,719	40,879	47,035
EBIT (1-Tax)	15,551	17,322	19,357	21,704	24,422	27,583	31,281	35,630	40,782	46,928
Depreciation	1,177	1,231	1,295	1,369	1,455	1,556	1,675	1,816	1,983	2,184
CAPEX	1,765	1,847	1,942	2,053	2,183	2,334	2,513	2,724	2,975	3,275
Delta WC Inv.	15,556	16,276	17,114	18,090	19,232	20,569	22,142	24,002	26,213	28,859
FCFF	(593)	431	1,596	2,929	4,463	6,237	8,301	10,721	13,577	16,977
Terminal Value										290,527
PV FCFF	(552)	373	1,285	2,194	3,109	4,042	5,005	6,013	7,084	149,261

Table V.12 Scenario 3 FCFF Projection

(IDRb)	P. 2024	P. 2025	P. 2026	P. 2027	P. 2028	P. 2029	P. 2030	P. 2031	P. 2032	P. 2033
Revenue	120,286	126,117	132,975	141,058	150,614	161,953	175,471	191,670	211,193	234,874
EBIT	15,653	17,490	19,619	22,096	24,992	28,395	32,418	37,203	42,934	49,848
EBIT (1-Tax)	15,595	17,429	19,555	22,028	24,919	28,317	32,334	37,112	42,834	49,737
Depreciation	1,179	1,236	1,303	1,382	1,476	1,587	1,720	1,878	2,070	2,302
CAPEX	1,768	1,854	1,955	2,074	2,214	2,381	2,579	2,818	3,105	3,453
Delta WC Inv.	15,580	16,335	17,224	18,271	19,508	20,977	22,728	24,826	27,355	30,422
FCFF	(575)	476	1,680	3,066	4,673	6,547	8,746	11,347	14,445	18,164
Terminal Value										310,844
PV FCFF	(535)	412	1,352	2,296	3,256	4,243	5,273	6,364	7,537	159,699

g. Equity Value

To calculate the stock price valuation then, the Equity Value is divided by the number of shares. The equity value per share calculation for all scenarios as follow:

Table V.13 Equity Value

(IDRb)	Scenario 1	Scenario 2	Scenario 3
Total Discounted Enterprise Value	171,399	177,814	189,898
Less Debt	11,907	11,907	11,907
Less Non-Controlling Interest	29,870	29,870	29,870
Add Cash and Marketable Securities	2,695	2,695	2,695
Equity Value	132,316	138,732	150,815
Number of Shares	116	116	116
Equity Value per Share	IDR 1,138	IDR 1,193	IDR 1,297

Based on DCF method, the intrinsic value of HMSP is Rp. 1,138 per share for scenario 1 (BAU), and Rp. 1,193, and Rp. 1,297 for scenario 2 & 3 (HTU transition scenarios). Thus, it can be concluded that HMSP's diversification strategy in achieving a smoke-free future is able to increase the value of the company's shares.

If it refers to the current market price, HMSP's stock price is undervalued, as recalled that as of August 1, 2024, market price for HMSP's share is at Rp. 675, which if based on the intrinsic valuation, the upside potential for HMSP's stock at most could be at 92%. Based on the Author's observations, the movement of excise tariffs strongly influenced cigarette companies' value, which are currently declining.

V.3 Relative Valuation

Another method for stock valuation is relative valuation, also known as price multiple analysis. Key ratios used in this approach include EV/EBITDA, ROE, PBV, and PER. Additionally, market capitalization and debt-to-equity ratio (DER) are calculated to provide insights into the company's size and capital structure. This price multiple analysis involves examining three publicly traded tobacco companies.

Table V.14 Price Multiples

Companies	Market Cap (IDRt)	EV/EBITDA (x)	ROE (%)	PBV (x)	PER (x)	DER (x)
HMSP	85.40	7.71	27.1%	2.84	10.43	0.78
GGRM	32.58	6.10	8.7%	0.54	6.12	0.52
WIIM	2.62	4.06	27.4%	1.42	5.28	0.39
Avg.	40.20	5.96	21.1%	1.60	7.28	0.56
Median	32.58	6.10	27.1%	1.42	6.12	0.52

Another method for stock valuation is relative valuation, also known as price multiple analysis. Key ratios used in this approach include EV/EBITDA, ROE, PBV, and PER. Additionally, market capitalization and debt-to-equity ratio (DER) are calculated to provide insights into the company's size and capital structure. This price multiple analysis involves examining three publicly traded tobacco companies.

HMSP leads with the highest market cap (85.40 IDRt) and EV/EBITDA (7.71x), indicating strong investor confidence and growth prospects compared to GGRM and WIIM. Although WIIM has a slightly higher ROE (27.4%) than HMSP (27.1%), HMSP's higher PBV (2.84x) and PER (10.43x) suggest greater growth expectations and lower perceived risk. HMSP also has the highest DER (0.78x), implying more leverage and potential risk, but possibly indicating aggressive growth strategies. Using the multiple on the figure above, share price for HMSP based on relative valuation methods can be calculated as follows:

Table V.15 HMSP's Relative Valuation

Ratio	Value	Remarks
PER (x)	7.28	Peer average
Earning per Share	70	2023 Annual Report
Price per Share	509.3	
PBV (x)	1.60	Peer average
Book Value per Share	256.8	2023 Annual Report
Price per Share	410.3	

The relative valuation figures indicate that the company's current market price of IDR 675 is significantly higher than its relative value based on peer average ratios. Using a PER of 7.28 and an EPS of 70, the calculated share price is IDR 509.3. Similarly, using a PBV of 1.60 and a book value per share of 256.8, the derived price per share is IDR 410.3. These values suggest that the shares are trading at a substantial premium, with the PER-based valuation about -24% lower and the PBV-based valuation approximately -39%, lower than the current market price, making the shares appear overvalued based on peer averages.

V.4 Qualitative Considerations

When evaluating PT Hanjaya Mandala Sampoerna Tbk (HMSP), several key qualitative factors impact its valuation and future performance. The regulatory environment in Indonesia, characterized by stringent tobacco regulations and rising excise taxes, affects HMSP's profitability and market access. The potential for stricter regulations aimed at reducing smoking rates could pose additional challenges for the company.

Excise tax increases significantly impact HMSP's financial performance by raising production costs and pressuring the company to hike prices, which may decrease demand, particularly among cost-sensitive consumers. Balancing pricing strategies with cost management will be crucial for maintaining profitability.

As consumer preferences shift towards less harmful alternatives, HMSP's success will depend on its ability to expand its portfolio with products like Heated Tobacco Units (HTUs) and gain market acceptance in a traditionally cigarette-dominated market. The competitive landscape in Indonesia's tobacco industry is fierce, with many major players competing for market share. HMSP's ability to sustain its market position will hinge on innovation, brand strength, and product differentiation.

Technological advancements, particularly those from HMSP's parent company Philip Morris International, will be essential for future success. Investment in research and development (R&D) and new technologies will be crucial for growth. Economic factors, including inflation and currency fluctuations, also impact HMSP's performance. Economic downturns may reduce demand for premium products, and currency fluctuations can affect the cost of importing HTU components.

Social and cultural attitudes towards smoking and new tobacco products affect HMSP's marketing strategies and market penetration. Overcoming resistance and educating consumers on HTUs will be important. Lastly, addressing environmental and sustainability concerns is increasingly vital. HMSP must manage the environmental impacts of its products and operations to enhance its brand reputation and appeal to eco-conscious consumers.

V.5 Business Solution

To address challenges and leverage opportunities, PT Hanjaya Mandala Sampoerna Tbk. (HMSP) should focus on key areas for improvement and strategic shifts. Enhancing operational efficiency is crucial; HMSP needs to streamline production processes, optimize the supply chain, and reduce waste to lower costs and stabilize profit margins amidst rising excise taxes and other cost pressures.

A strategic shift towards Heated Tobacco Units (HTUs) is recommended. HMSP should prioritize increasing HTU sales while gradually reducing its reliance on conventional cigarettes. Emphasizing the health benefits of HTUs in marketing campaigns will appeal to health-conscious and younger consumers. By focusing on HTU expansion and reducing marketing expenditure on traditional cigarettes, HMSP can position itself as a leader in sustainable, reduced-risk products within the tobacco industry.

Adhering to Aswath Damodaran's principles for optimizing intrinsic value is also vital. According to Damodaran (2015), HMSP should focus on strategic investments, such as enhancing HTU technology and increasing marketing for HTUs, to drive growth. A balanced financing strategy, potentially utilizing sustainability-linked loans, will support these investments. Additionally, HMSP should reassess its dividend policy, maintaining a stable payout ratio of around 70% while retaining an extra 5-10% of earnings. This retained capital can be reinvested into HTU development and sustainability efforts, ensuring long-term value creation and growth.

VI. CONCLUSION

This research has examined the impact of sustainable alternatives, particularly Heated Tobacco Units (HTUs), on the valuation of PT Hanjaya Mandala Sampoerna Tbk. (HMSP). The intrinsic valuation, using the Discounted Cash Flow (DCF) method, forecasts HMSP's stock value under various HTU transition scenarios. In the Business-as-Usual scenario, where HTUs make up 2% of sales by 2033, the stock's intrinsic value is Rp. 1,138 per share. In the Moderate Transition scenario, with HTUs reaching 5% of sales, the value rises to Rp. 1,193 per share. The Aggressive Transition scenario, assuming HTUs comprise 10% of sales, projects a value of Rp. 1,297 per share. Compared to the market price of Rp. 675 per share as of August 2024, these scenarios suggest an upside potential ranging from 68% to 92%.

Qualitative analysis complements this valuation by addressing regulatory pressures, competitive dynamics, and evolving consumer preferences. The rise of HTUs represents a strategic response to challenges in the traditional cigarette market and aligns with global trends toward reduced-risk products. HMSP's focus on HTUs, and operational efficiency is expected to enhance its profitability and market valuation.

VI.1 Recommendations for Investors

- a. **Long-Term HTU Potential:** Investors should recognize the significant upside potential in HMSP's stock, particularly if HTUs achieve substantial market penetration. Holding or acquiring shares may be beneficial as the company shifts towards reduced-risk products.
- b. **Dividend Policy Monitoring:** Investors should be prepared for potential adjustments in HMSP's dividend policy to allow for reinvestment in strategic initiatives. Short-term dividend reductions may be offset by long-term capital gains.
- c. **Operational Efficiency:** Keep an eye on HMSP's progress in enhancing operational efficiency. Improvements in this area are crucial for margin stability and overall profitability.

VI.2 Recommendations for HMSP's Management

- a. **Accelerate HTU Shift:** Management should prioritize the aggressive expansion of HTUs, aiming for a 10% contribution to sales by 2033. This includes ramping up R&D and marketing efforts to capture market share and build brand loyalty.
- b. **Balanced Financing Strategy:** Explore sustainable financing options like sustainability-linked loans and maintain a balanced debt-to-equity ratio to support investments in HTUs and other strategic areas.
- c. **Dividend Policy Revision:** Consider adjusting the dividend payout ratio to retain more earnings for reinvestment in HTUs and other growth initiatives. Clear communication with shareholders about these changes will be crucial.
- d. **Enhance Operational Efficiency:** Focus on optimizing supply chain processes, advanced automation, and cost reduction to stabilize margins and improve profitability amidst rising costs and regulatory pressures.
- e. **Strengthen Sustainability and Education:** Invest in sustainability initiatives and consumer education about HTUs. Leading in these areas can strengthen HMSP's market position and appeal to a conscientious consumer base.

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