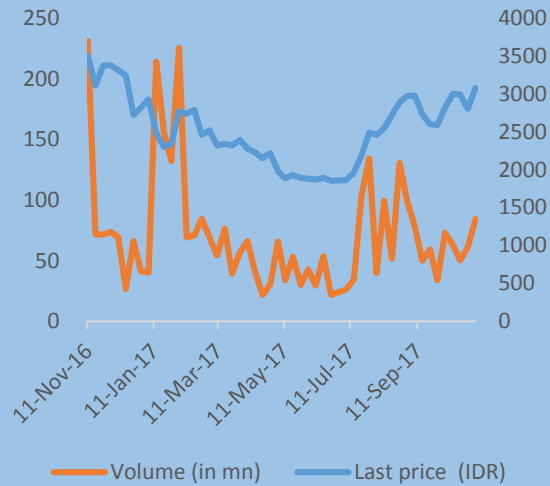


10 November 2017  
Nickle Mining, Equity

Price **IDR 3120**  
Target Price **IDR 3550**  
JKSE Index **6026.47**



**Stock Code**  
**Bloomberg code** **INCO IJ**  
**Market cap (IDR.bn)** **31895**  
**52-Week High (IDR)** **3630**  
**52-Week Low (IDR)** **1835**  
**6-m Avg Daily. Val (IDR)** **2729**  
**Free Float (%)** **20.49**

**Major Shareholders (%)**  
**Vale Canada ltd** **58.73%**  
**Sumitomo Metal Mining Co Ltd** **20.09%**  
**Vale japan Ltd** **0.55%**  
**Sumitomo Corp** **0.14%**  
**Public** **20.49%**

**USD/IDR-YE**  
**2016A** **13,436**  
**2017F (Avg)** **13,368**

**Key Indicators** **2018F**  
**ROE (%)** **1.86**  
**Total Debt/ Equity (x)** **0.22**  
**Current ratio (x)** **3.41**

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### Investment Consideration

#### Production volume on track

We have lowered our nickel production target to 78,000 MT, in line with INCO's forecast, which is close to their 2016FY production of 77,581 MT. Despite a volume decline, the average price is increasing in line with rising global nickel prices. This can be seen in 9M17, where 9M17 volume of nickel in matte production declined -0.87% to 57494 MT but was 74% of the annual target while nickel in matte deliveries increased 0.76% to 57,724 MT. Average realized price jumped 9.82% to 7,773 US\$/MT. As a result, we have adjusted our revenue forecast in 2017 – 2018F to USD. 667,1 mn and USD. 735.99 mn respectively.

#### Executing on cost competitiveness

INCO is on track to continue improving efficiency and reduce costs as can be seen in 3Q17. As of 3Q17, cost of revenue per metric ton nickel matte sold declined 13% to 7,255 USD/MT compared to 2Q17. This was driven primarily by a recovery in provisions for a decline in inventory value. EBITDA in 3Q17 was US\$34.1mn higher than US\$. 10.9 mn in 2Q17 due to higher sales volume. We adjust our bottom line target in line with the 9M17 result which showed an improving trend. in 2Q17 the company's net loss was US\$. (15,32mn) higher than in 1Q17 of US\$ (6,16mn), INCO managed to book a net profit in 3Q17 of US\$. 1,85mn.

#### Valuation: 14% upside

Because of the improvement in cost per metric ton in 3Q17 despite lower production volume and the stable nickel price, we are adjusting our target based on the 9M17 result. With WACC of 11.45%, we have a one year TP of 3550 / share higher than our previous target of 3345/shares. With only 14% upside compared to the last closing price, our recommendation is HOLD.

Profit and Loss (USD.mn)	2013 A	2014 A	2015 A	2016 A	2017 F	2018 F
<b>Revenues</b>	<b>922</b>	<b>1,038</b>	<b>790</b>	<b>584</b>	<b>667</b>	<b>736</b>
<b>COGS</b>	<b>(782)</b>	<b>(731)</b>	<b>(671)</b>	<b>(550)</b>	<b>(642)</b>	<b>(647)</b>
<b>Gross Profit</b>	<b>140</b>	<b>307</b>	<b>118</b>	<b>34</b>	<b>25</b>	<b>89</b>
Operating expense	(70)	(57)	(39)	(20)	(23)	(25)
<b>Operating Profit</b>	<b>70</b>	<b>249</b>	<b>80</b>	<b>14</b>	<b>3</b>	<b>64</b>
Other income	(15)	(13)	(10)	(9)	(13)	(15)
<b>Pretax income(PBT)</b>	<b>55</b>	<b>237</b>	<b>70</b>	<b>5</b>	<b>(11)</b>	<b>49</b>
taxes	(17)	(65)	(19)	(3)	3	(15)
<b>Net Profit</b>	<b>39</b>	<b>172</b>	<b>51</b>	<b>2</b>	<b>(7)</b>	<b>35</b>
EPS	0.004	0.0173	0.0051	0.0002	(0.0007)	0.0035
<b>EBITDA</b>	<b>181</b>	<b>372</b>	<b>201</b>	<b>138</b>	<b>119</b>	<b>173</b>

**Company Profile**

PT Vale Indonesia Tbk (INCO), a nickel mining company, was established in July 1968. Since its establishment, INCO has been operating under the Contract of Work (CoW) agreement with the Government of Indonesia to explore, develop, mine, process, store, transport, and sell all nickel and nickel-containing minerals in the CoW areas. INCO’s CoW area is nearly 118,435 hectares (Ha) in total. The original area of 6.6 million Ha, covering the eastern and southeastern part of Sulawesi, was granted on July 27, 1968. The Concession area has been reduced to 2.9% of the original size under a series of relinquishments, the last of which occurred when the CoW renegotiation was signed on October 17, 2014. The original CoW was valid until March 31, 2008. It was modified and extended under the Agreement on Modification and Extension signed in 1996 and will be valid until Dec 28, 2025.

**Contract of Work status**

The Indonesian government and INCO signed amendments to the Contract of Work (CoW) as of 17 October 2014 as mandated by the Law for Minerals and Coal 2009. The amendments include:

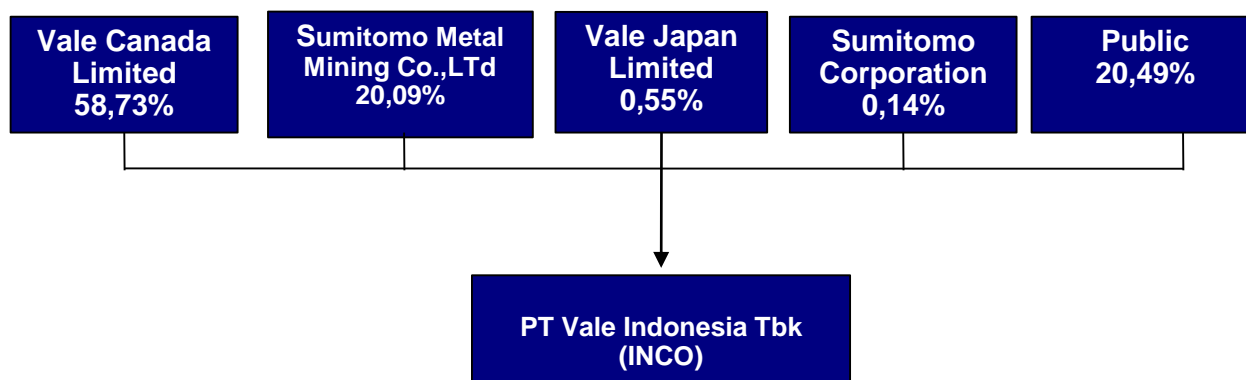
- (I) To increase the royalty rate to 2% of sales (& up to 3% if the previous month average LME nickel price is \$21,000/T or above).
- (II) An obligation to divest a further 20% of the Company’s shares to Indonesian investors. The divestment process to be carried out within a period of 5 years.
- (III). To reduce the CoW area from 190,510 ha to 118,435 ha. At the expiry of the CoW on December 28, 2025, the company will maintain a 25,000 ha ore zone that has been proposed.

In return PT Vale Indonesia (PTVI) will get:

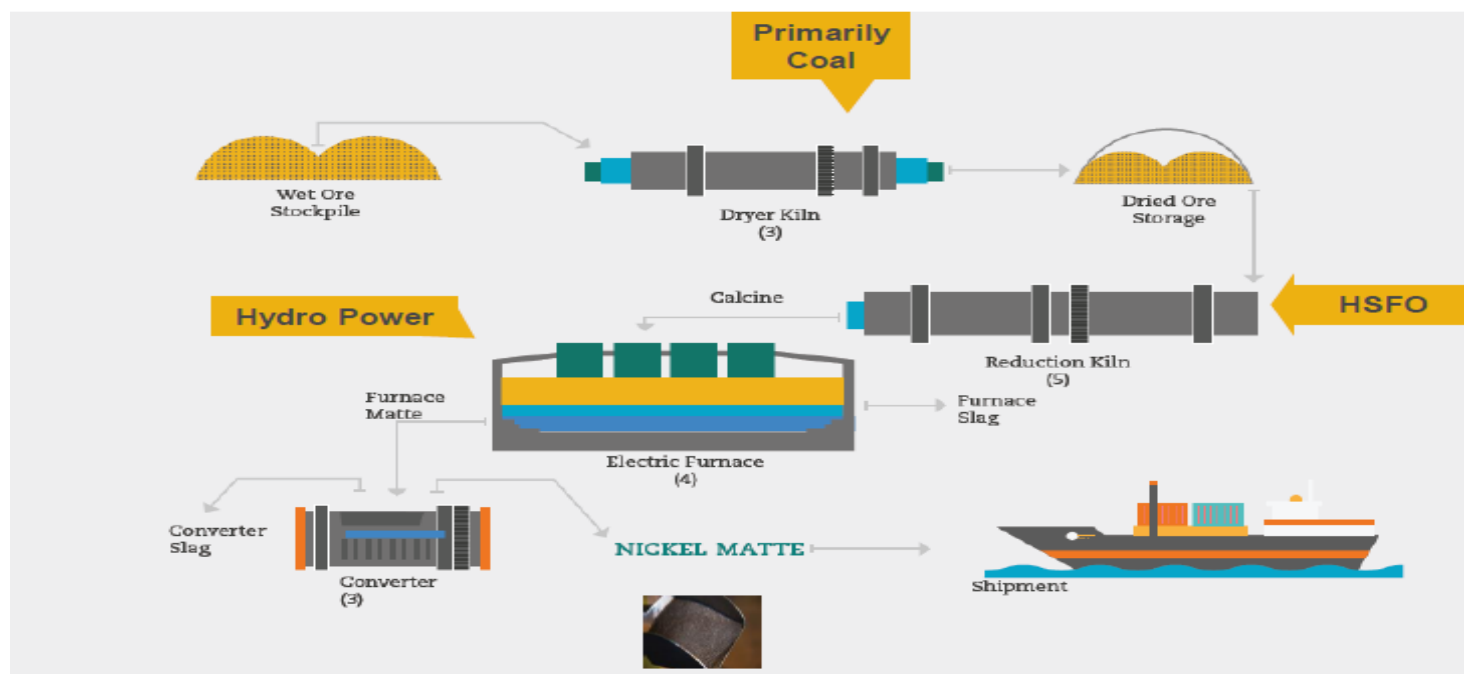
- (1). The ability to apply for extensions through Business Licenses up to 2045,
- (2). Sufficient conditions to secure PTVI’s investment and growth targets.

The company produces nickel in matte, an intermediate product, from lateritic ores at its integrated mining and processing facilities near Sorowako on the island of Sulawesi. INCO’s entire production is sold in US dollars under long-term contracts for refining in Japan (mainly for stainless steel consumption).

**Company Structure**

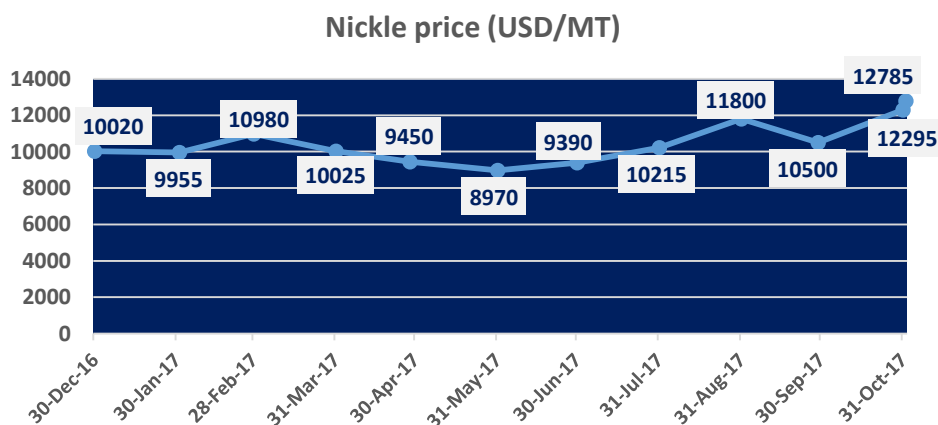


Nickle in Matte production scheme



Nickle outlook 2017

The nickel price was expected to improve driven by several factors such as an improvement in Chinese demand & several mine closures in the Philippines accounting for 10% of world supply. These two factors should have already boosted global prices of the metal. But, on 2 March 2017, the Indonesian government mining regulations were amended so that 100% of existing and planned smelter capacity could be exported as ore. This is higher than previously. As a result, nickel prices retreated, briefly falling below US\$10,000/MT in 1H17. In 2H17, starting October nickle prices rose to 12000 US\$/MT, due to sentiment from a recent report which said that demand from china and the electric car battery market could spur prices. But, the latest news from the Philippnes, the Mining Industry Coordinating Council (MICC) has voted in favour of lifting a ban on open-pit mining, by the end of 2017. If this is approved then we assume nickle prices movement will be stable. In addition, although the market has been gaining attention from the role of nickel in electric vehicle batteries, we believe that demand from electric car batteries will be over the long term and will not happen in the short term. We forecast nickle price in 2017 – 2018 to average 10800 – 11750 US\$/MT.



Source: summary from World bank, bloomberg

Chart: Nickle in matte production (MT) yoy

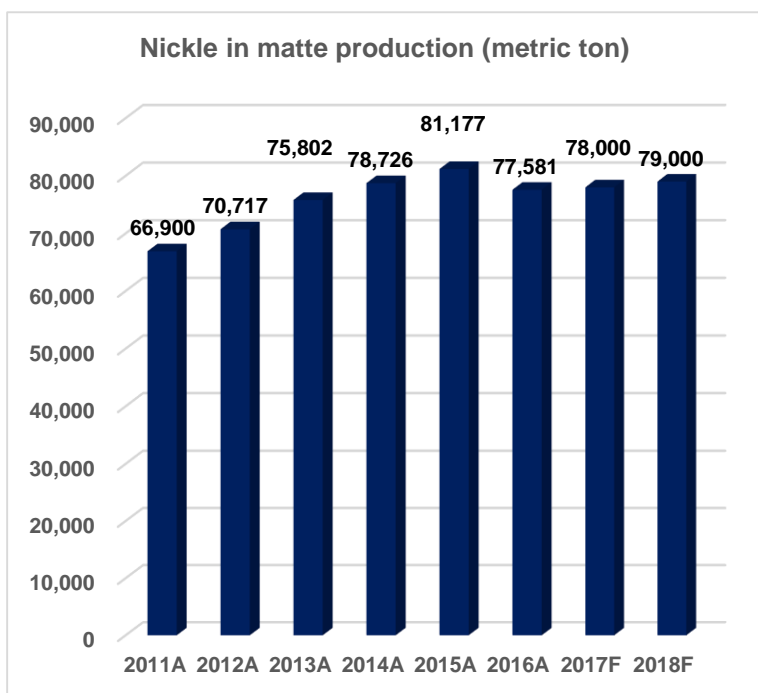


Chart: Nickle in matte sales volume deliveries (MT) yoy

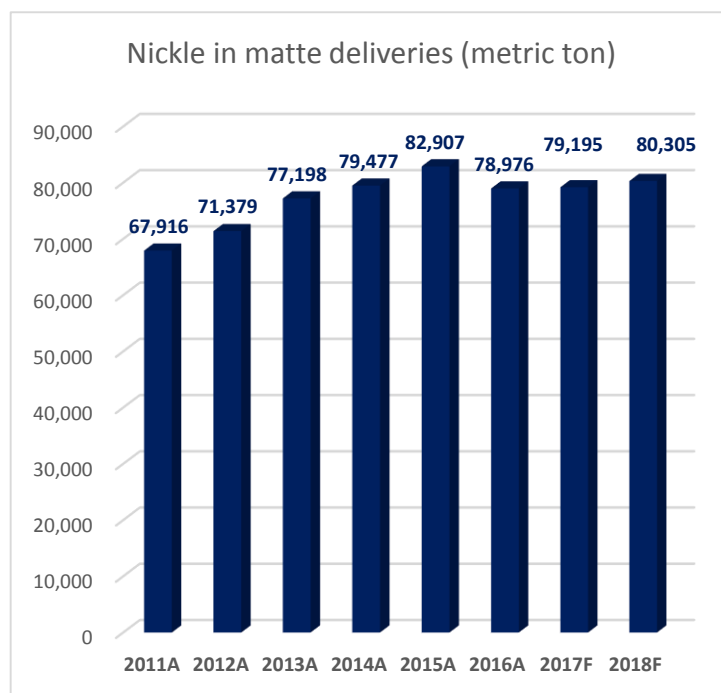


Chart: HSFO vs HSD volume yoy

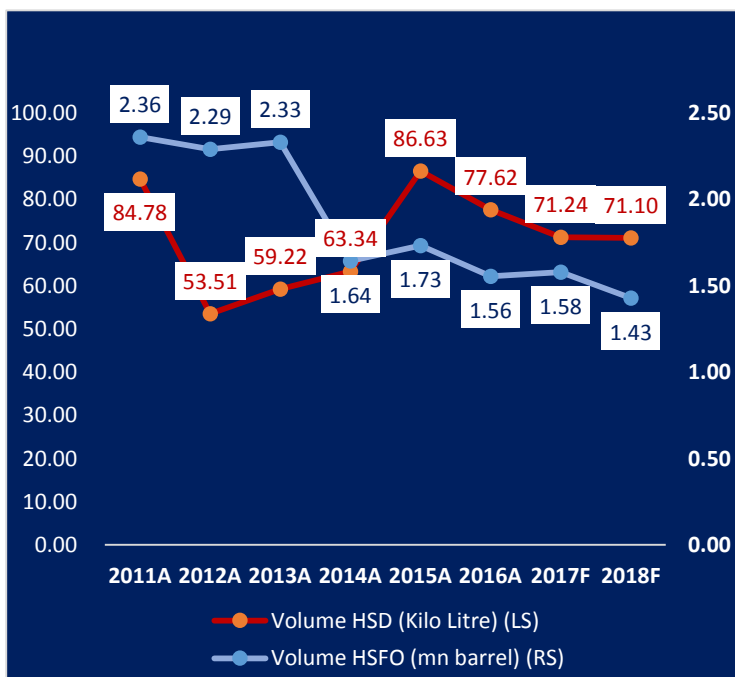
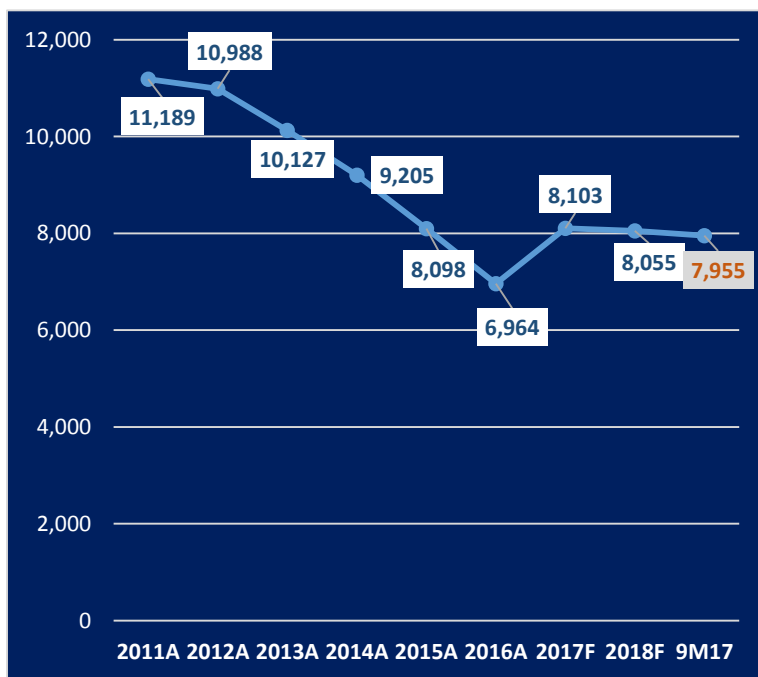


Chart: cost of revenue/MT nickle in matte deliveries



Profit and Loss (US\$ in mn)

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Balance Sheet (US\$ in mn)

Balance sheet (US\$ in mn)	2010A	2011A	2012A	2013A	2014A	2015A	2016A	2017F	2018F
Cash and cash equivalent	404	399	172	200	302	195	186	244	143
restricted cash	1	17	17	17	16	28	30	0	0
short term investment	0	0	0	0	0	90	0	0	0
Trade Account Receivable	124	66	113	66	93	78	147	167	184
inventory	102	163	153	151	139	104	130	129	143
Other current asset	82	135	110	124	71	100	107	84	107
<b>Current Asset</b>	<b>713</b>	<b>781</b>	<b>565</b>	<b>557</b>	<b>621</b>	<b>595</b>	<b>599</b>	<b>624</b>	<b>578</b>
Net Fixed Asset	1,465	1,579	1,625	1,652	1,609	1,603	1,533	1,513	1,602
other long term asset	13	16	144	72	104	91	94	84	98
<b>Total non current Asset</b>	<b>1,477</b>	<b>1,641</b>	<b>1,768</b>	<b>1,724</b>	<b>1,713</b>	<b>1,694</b>	<b>1,626</b>	<b>1,597</b>	<b>1,700</b>
<b>Total Asset</b>	<b>2,190</b>	<b>2,421</b>	<b>2,333</b>	<b>2,281</b>	<b>2,334</b>	<b>2,289</b>	<b>2,225</b>	<b>2,221</b>	<b>2,278</b>
Trade Account Payable	41	84	79	76	74	86	64	73	81
Other Short term liabilities	117	95	87	93	134	63	68	77	88
<b>Total current liabilities</b>	<b>158</b>	<b>179</b>	<b>166</b>	<b>169</b>	<b>208</b>	<b>148</b>	<b>132</b>	<b>151</b>	<b>169</b>
Long term borrowings	141	255	220	183	147	110	73	36	18
Other Long term liabilities	212	219	226	215	194	197	186	207	228
<b>Total long term/ non current liabilities</b>	<b>352</b>	<b>473</b>	<b>446</b>	<b>398</b>	<b>340</b>	<b>307</b>	<b>259</b>	<b>243</b>	<b>246</b>
<b>Total Liabilities</b>	<b>510</b>	<b>652</b>	<b>612</b>	<b>567</b>	<b>549</b>	<b>455</b>	<b>391</b>	<b>394</b>	<b>416</b>
<b>Total Equities</b>	<b>1,680</b>	<b>1,769</b>	<b>1,721</b>	<b>1,714</b>	<b>1,785</b>	<b>1,834</b>	<b>1,835</b>	<b>1,827</b>	<b>1,862</b>
<b>Total Liabilities and equity</b>	<b>2,190</b>	<b>2,421</b>	<b>2,333</b>	<b>2,281</b>	<b>2,334</b>	<b>2,289</b>	<b>2,225</b>	<b>2,221</b>	<b>2,278</b>

Cash Flow (US\$.mn)

Cash Flow (US\$ in mn)	2013A	2014A	2015A	2016A	2017F	2018F
+ Net Income	39	172	51	2	(7)	35
Depresiasi+amortization+depletion	111	122	121	123	125	121
- Change in WC	38	78	(141)	(30)	52	(36)
<b>Cash From Operating Activities</b>	<b>188</b>	<b>372</b>	<b>31</b>	<b>95</b>	<b>170</b>	<b>120</b>
capex	(138)	(79)	(116)	(53)	(106)	(209)
other non current asset	72	(32)	13	(3)	10	(15)
	<b>(66)</b>	<b>(111)</b>	<b>(103)</b>	<b>(56)</b>	<b>(96)</b>	<b>(224)</b>
other long term liabilities	(48)	(58)	(34)	(48)	(16)	3
Equity	(46)	(101)	(2)	(1)	0	0
<b>cash from financing activities</b>	<b>(94)</b>	<b>(159)</b>	<b>(36)</b>	<b>(49)</b>	<b>(16)</b>	<b>3</b>
Net Changes in Cash	28	102	(108)	(9)	58	(101)
<b>Beginning Balance</b>	<b>172</b>	<b>200</b>	<b>302</b>	<b>195</b>	<b>186</b>	<b>244</b>
<b>Ending balance</b>	<b>200</b>	<b>302</b>	<b>195</b>	<b>186</b>	<b>244</b>	<b>143</b>

Ratio Highlight

	2013A	2014A	2015A	2016A	2017F	2018F
<b>Growth (% YoY)</b>						
Sales	-5%	13%	-24%	-26%	14%	10%
OP	-34%	256%	-68%	-82%	-81%	2224%
EBITDA	-14%	105%	-46%	-31%	-14%	45%
NP	-43%	346%	-71%	-96%	-477%	-581%
EPS	-43%	346%	-71%	-96%	-477%	-581%
<b>Profitability (%)</b>						
Operating Margin	8%	24%	10%	2%	0.41%	8.72%
EBITDA margin	20%	36%	25%	24%	17.83%	23.46%
NET Profit margin	4%	17%	6%	0.33%	-1.08%	4.70%
ROA	2%	7%	2%	0.09%	-0.32%	1.52%
ROE	2%	10%	3%	0.10%	-0.39%	1.86%
<b>Solvability</b>						
Tot. debt/ Tot. Equity (x)	0.33	0.31	0.25	0.21	0.22	0.22
int coverage (x)	4.78	19.93	8.04	1.57	0.64	29.59
<b>Liquidity</b>						
Current Ratio (X)	3.30	2.98	4.01	4.54	4.14	3.41
<b>Per Share data (USD)</b>						
EPS	0.004	0.017	0.005	0.000	(0.001)	0.003
BVS	0.173	0.180	0.185	0.185	0.184	0.187

**Stock Ratings:**

Buy: a recommendation to purchase the security with upside potential of 20% or greater

Hold: a recommendation to neither buy nor sell a security with upside potential of 0-20%.

Sell: a recommendation to close out a long position in a security with upside potential below 0% or negative.

**RESEARCH TEAM  
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