

An aerial night view of a city, likely Jakarta, Indonesia, featuring a large, illuminated glass sphere in the foreground. The sphere reflects the city lights and traffic. The background shows a dense urban landscape with numerous skyscrapers and buildings, some with glowing windows. The overall scene is illuminated by city lights, creating a vibrant and modern atmosphere.

**Schroders**

**Mapping The Opportunities Amid The Trade Frictions & Upcoming Election**

PT Schroder Investment Management Indonesia

Michael T. Tjoajadi - CEO

07 November 2018

# Indonesia Market Update

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## 2018



Global  
Factors



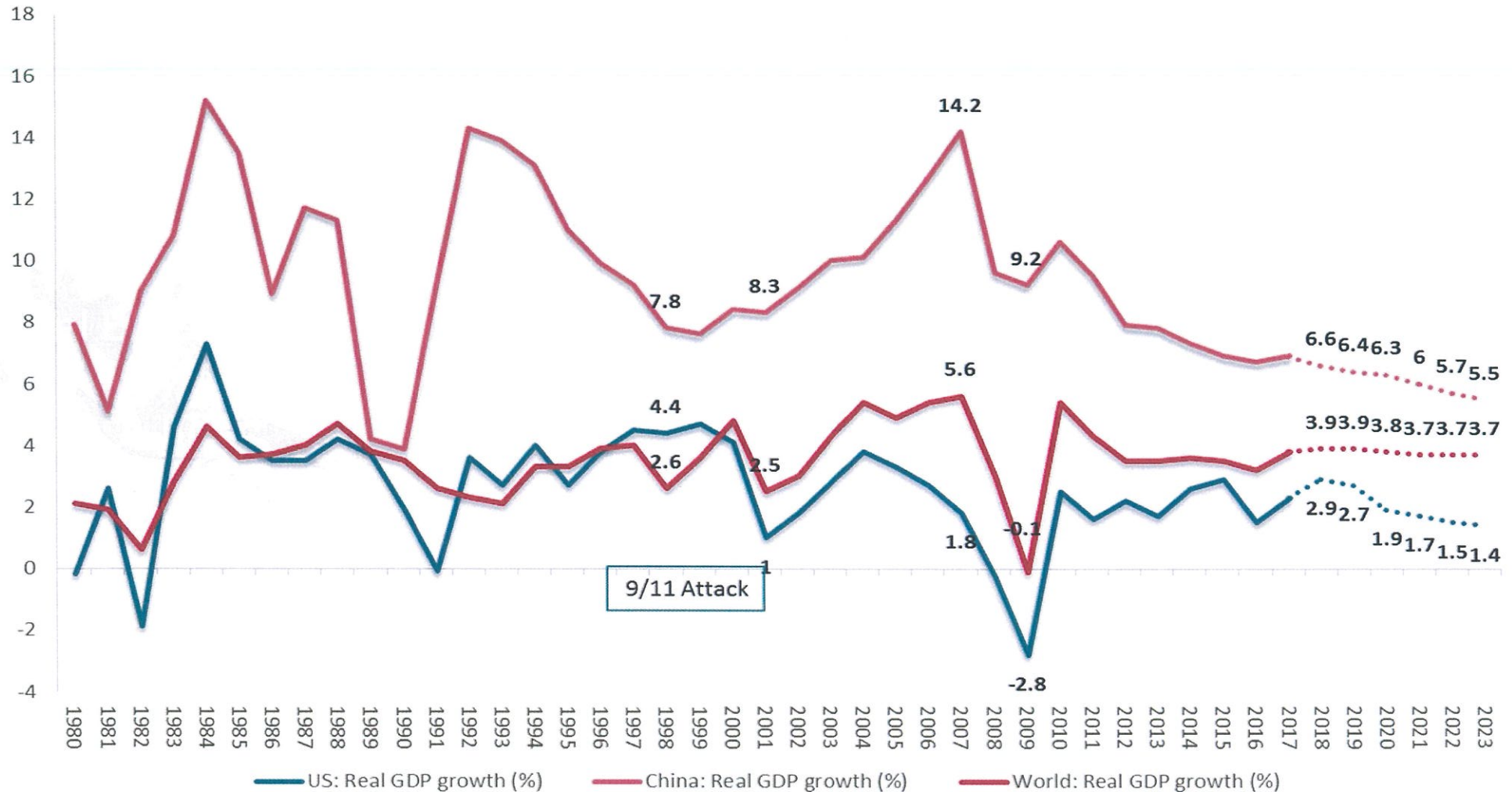
Domestic  
Macroeconomics



Local  
Markets

# Global Economic Growth is expected to be flat

## With China's growth expected to ease in the upcoming years

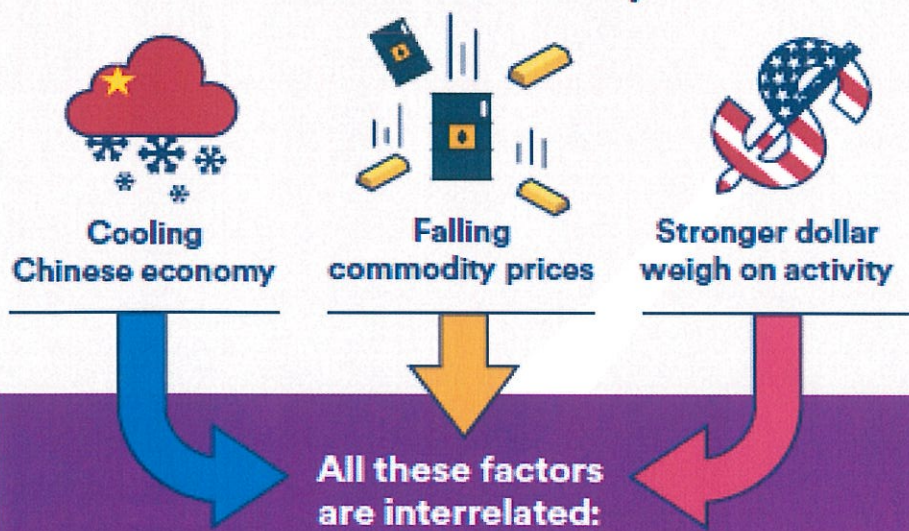


Source: Mandiri Securities Research

# The global economy

## Global

### Concerns over slower growth for world economy



China is a major consumer of commodities whose prices tend to be depressed by periods of dollar strength



Trade wars could have created a boom and bust as importers front loaded spending to avoid higher tariffs and are now cutting back, hitting commodities

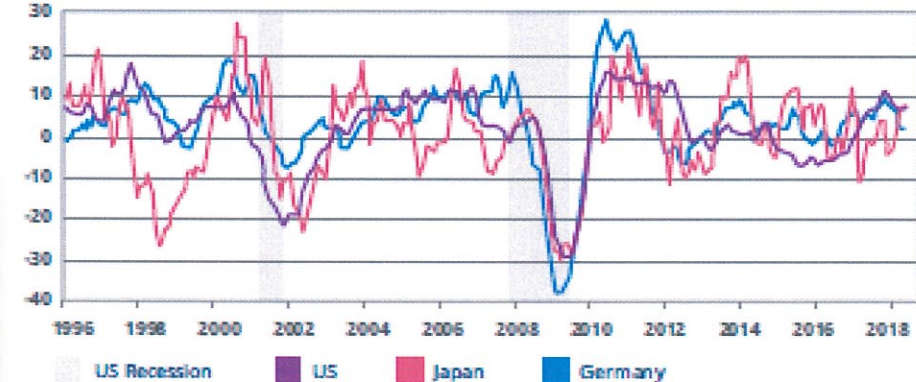
### How much of a slowdown?



We expect this slowdown to be temporary unless trade wars undermine business confidence

### Capital expenditure orders remain healthy

% y/y (3m, monthly average)



Source: Thomson Reuters Datastream, Schroders Economics Group, 27 July 2018.

### Impact on US consumers?

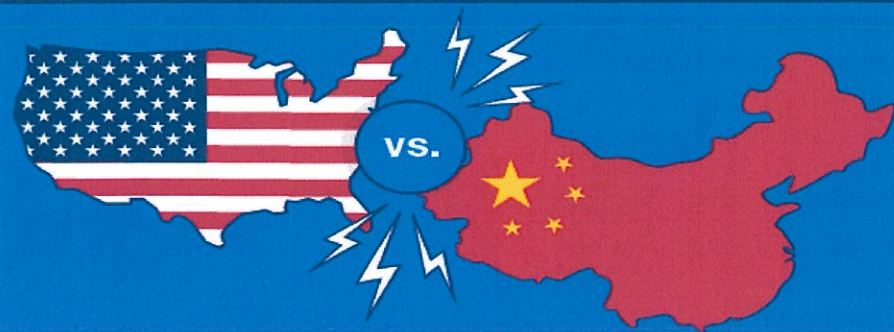


The combination of trade tariffs and tax cuts likely to bring higher inflation to the US

# The Global Economy

## Global : Trade war tension intensify

### Global: Perang dagang semakin menegangkan



**AS:** Trump mengancam mengenakan tarif terhadap impor dari Tiongkok senilai \$200 miliar



Kami memperkirakan Trump akan melibatkan UE lebih jauh lagi dengan mengancam akan mengenakan tarif pada impor mobil UE



Tiongkok kemungkinan akan merespons dengan menggunakan regulasi terhadap perusahaan AS di Tiongkok



**Jika perang dagang semakin meningkat:** Tarif yang lebih tinggi dapat menyebabkan inflasi yang lebih tinggi karena beban tambahan akan memiliki efek langsung terhadap barang konsumen. Menurut kami hal ini akan memperlambat pertumbuhan, menyebabkan kondisi yang lebih stagnan.

### Perang dagang menjadi perang mata uang?



Ada insentif untuk mempertahankan kebijakan tetap longgar di negara-negara yang akan terkena pengaruh dari perang dagang Trump → mata uang melemah terhadap dolar AS



Bank Sentral Eropa (ECB) akan mengakhiri QE di Desember tetapi menahan nilai suku bunganya hingga H2 2019



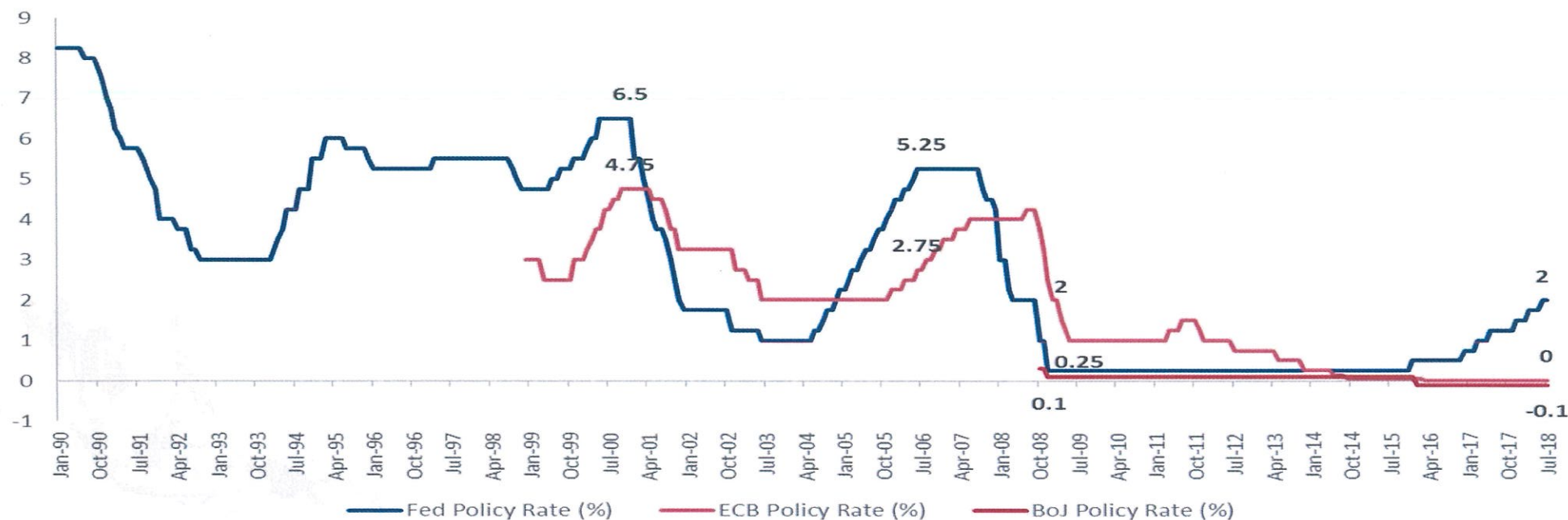
Tiongkok memotong rasio persyaratan cadangan (RRR) (jumlah minimum uang tunai yang diperlukan untuk disimpan oleh bank)



Sumber: Thomson Datastream, Schroders Economics Group, 27 Juni 2018.

# Meanwhile, the policy rates are expected to rise...

## Key advanced countries

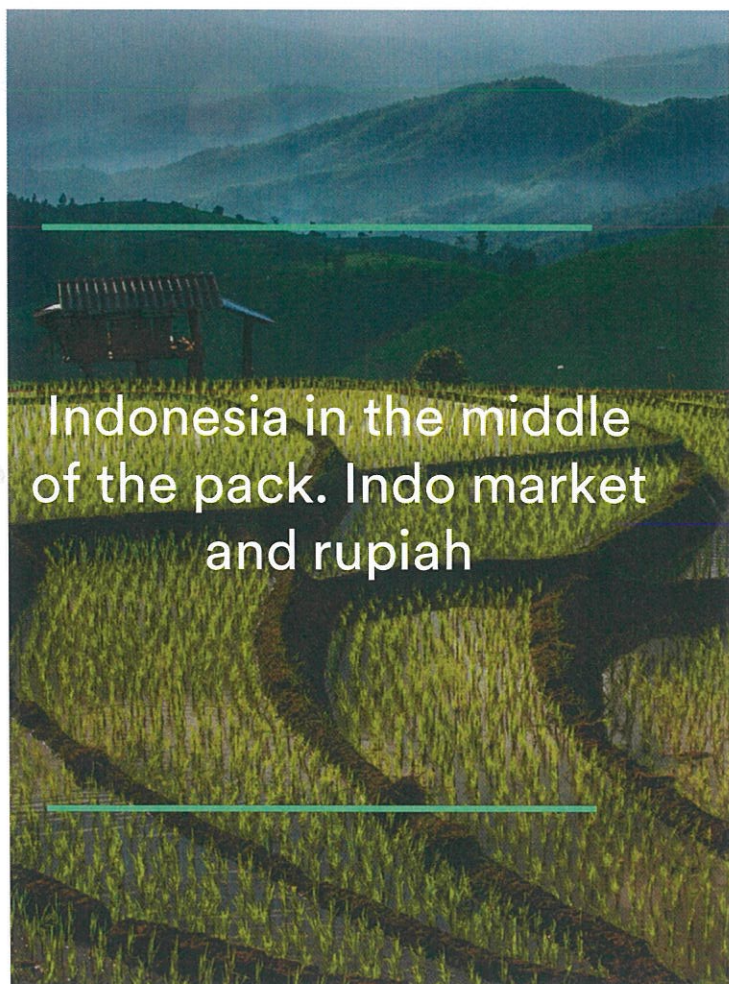


### Forecast of benchmark rates in G3 countries

| Forecast             | 2018  | 2019  | 2020  |
|----------------------|-------|-------|-------|
| FFR                  | 2.5%  | 3.25% | 3.5%  |
| ECB MRO*             | 0%    | 0.15% | 0.75% |
| BoJ short-term rate* | -0.1% | 0%    | 0%    |

Note: \*) Bloomberg Forecast

# Indonesia Macro issues

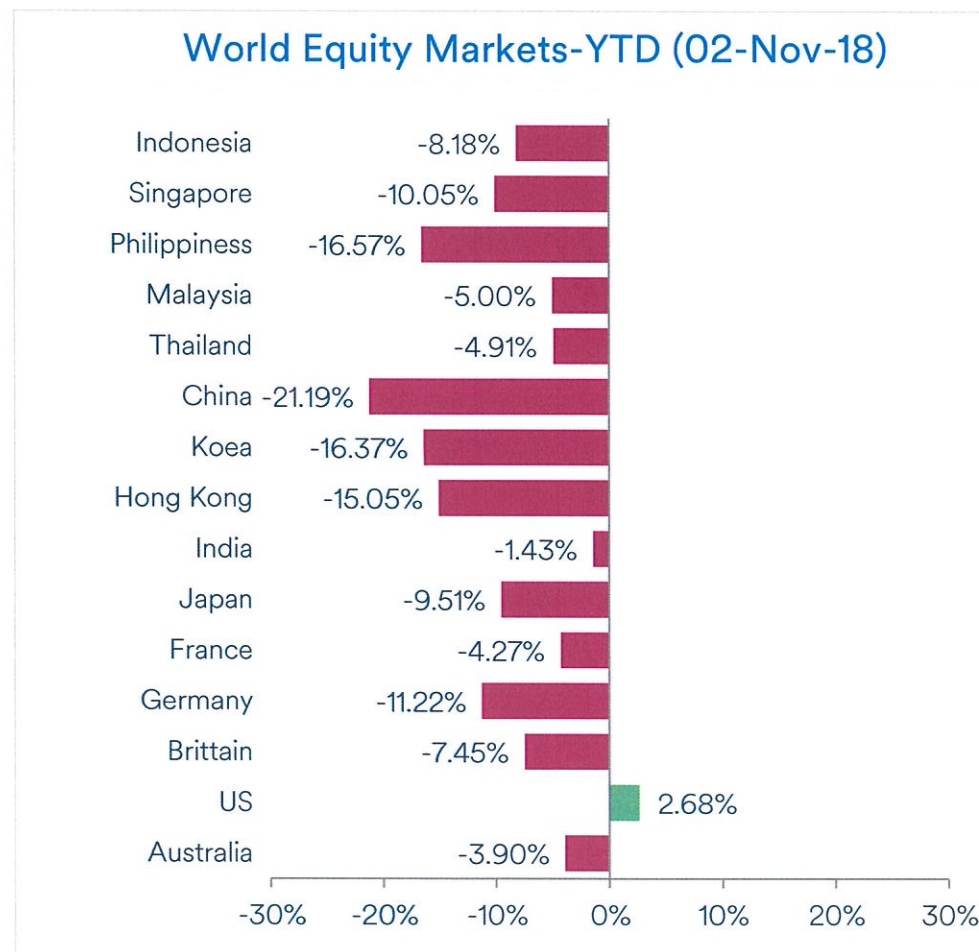
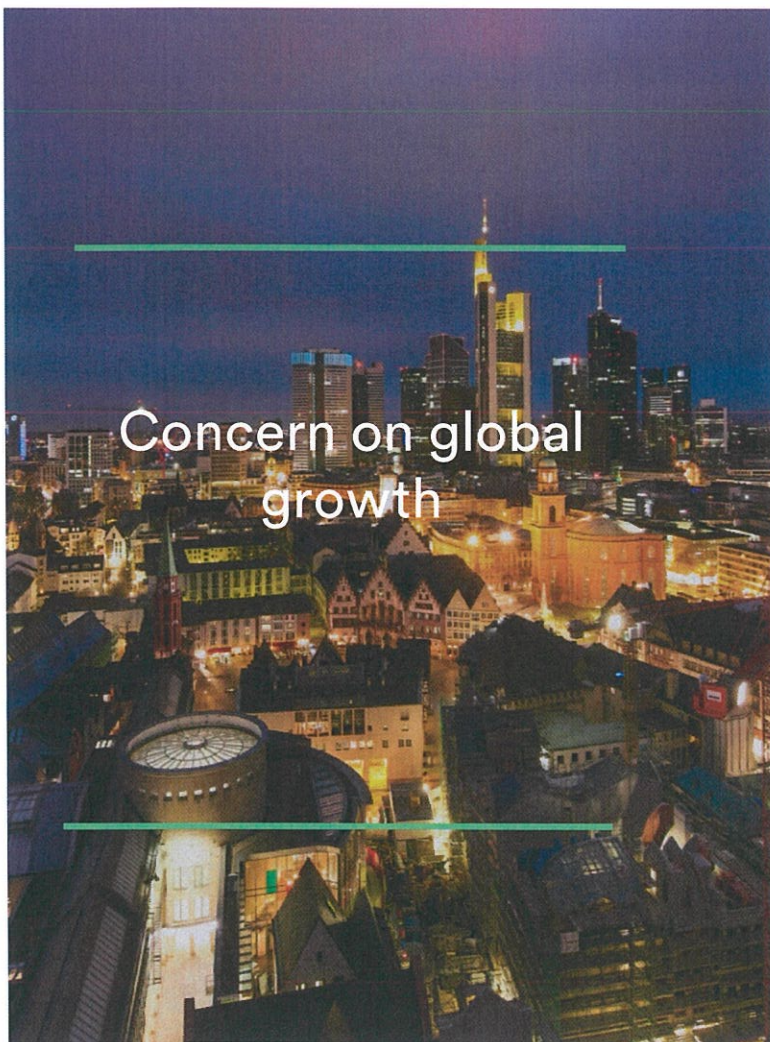


Indonesia in the middle of the pack. Indo market and rupiah

- **Global Market** : Slower Growth, Stronger USD and Trade and Currency War
- **Indonesia Market** :
  - Pressure on Rupiah due to EM sell off
  - Widening CAD and Trade Balance
  - Leads to monetary tightening
  - Liquidity is drying up
  - Eventually will curb GDP growth
  - Slowing down overall top line growth
  - Weak purchasing power
  - USD cost pressure and Increasing competition
  - Heightened political noises from presidential election

# Global market correction

## Most markets did not perform this year

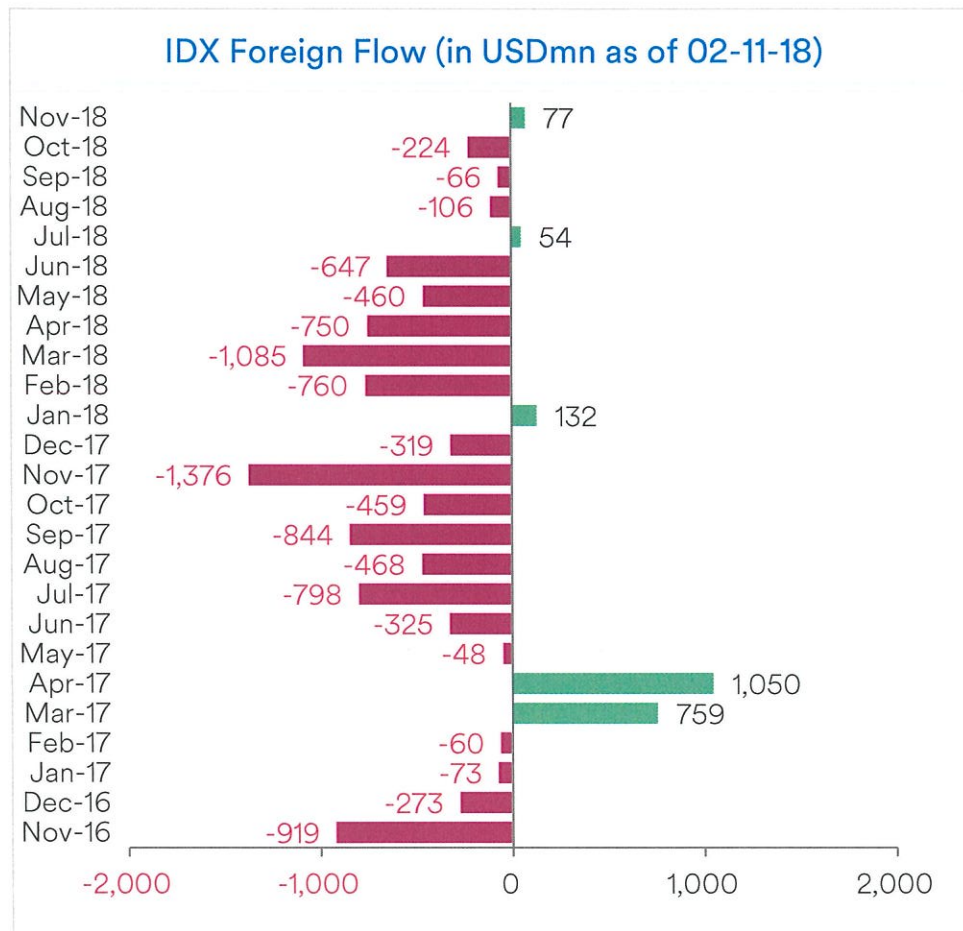


Source: Bloomberg, as of November 2018



# Foreign Flows to Indonesia

## Historical Data



Source: Bloomberg, Schroders, as of Nov 2018.

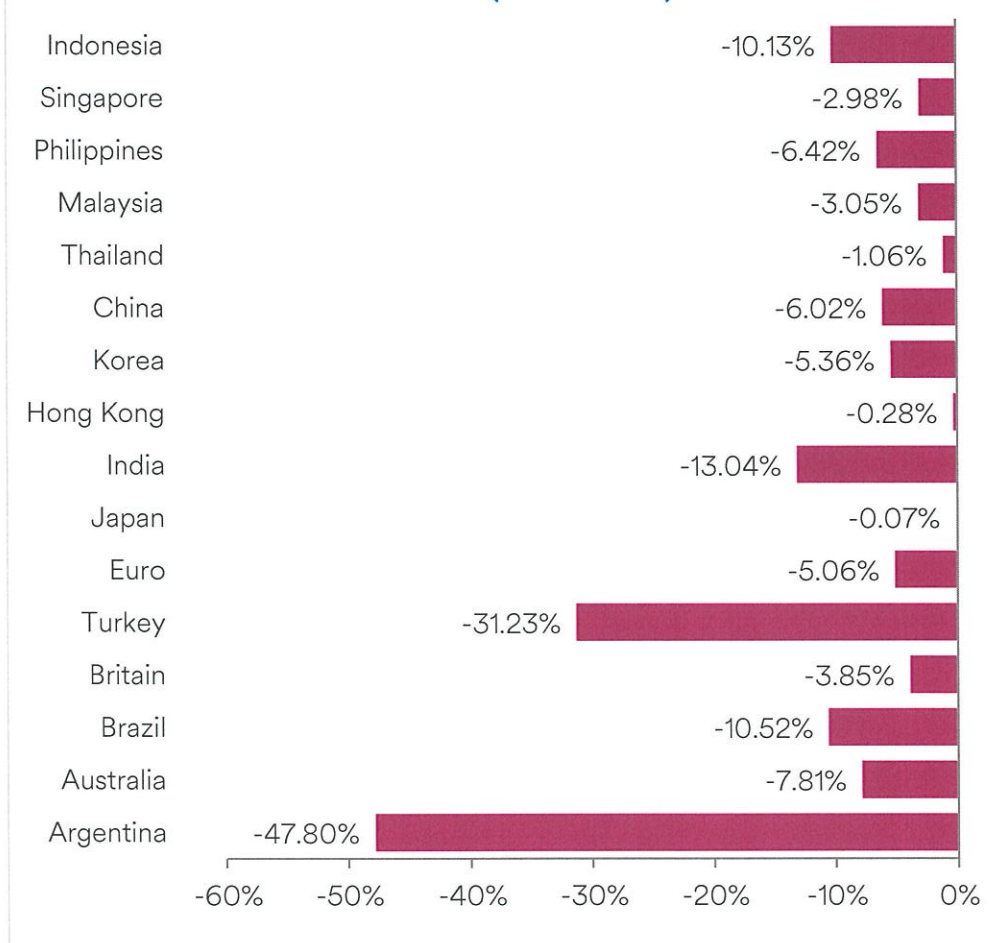
# Rupiah under selling pressure

## Both global and domestic front



### Exchange rate movement (%ytd)

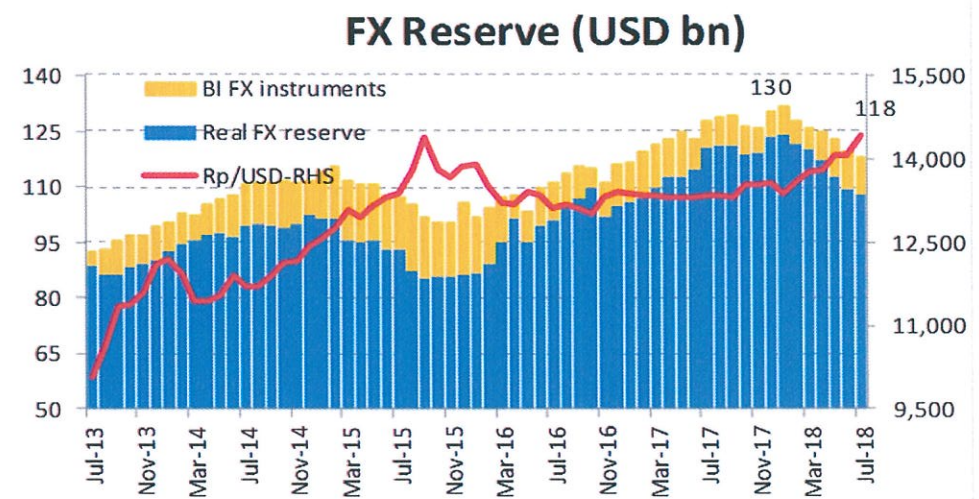
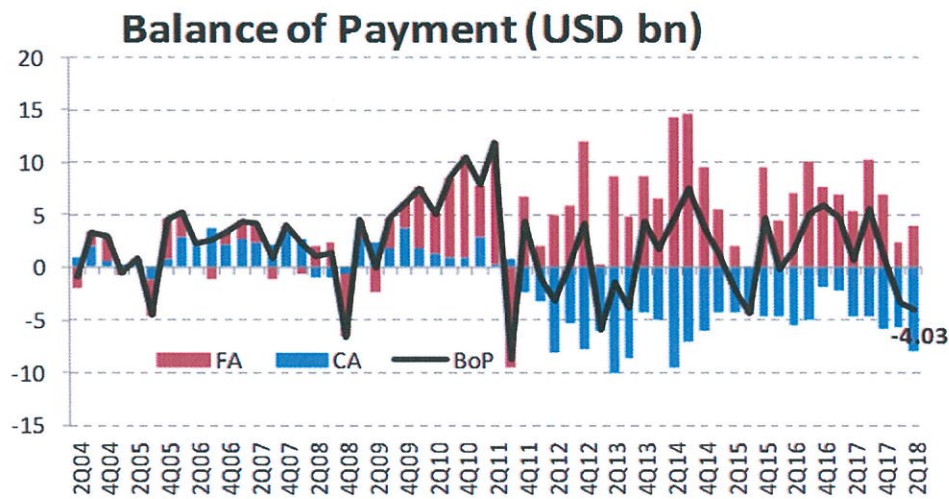
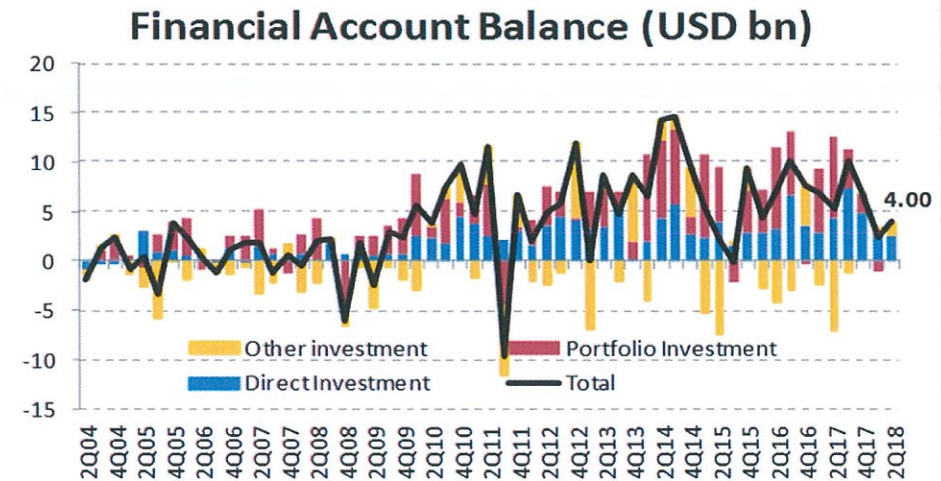
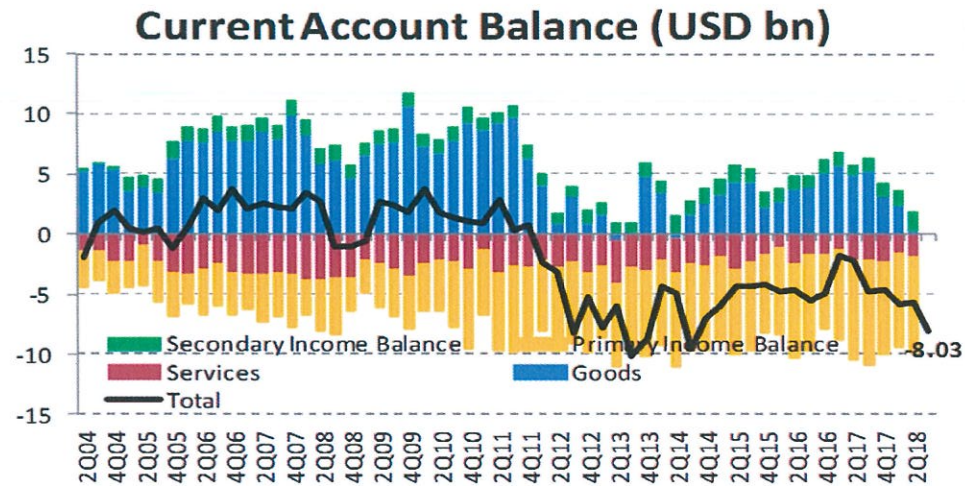
#### World Currencies vs USD-YTD (02-Nov-18)



Source: Bloomberg

# Where is the pressure on Rupiah come from?

## Insufficiency of the financial account surplus to finance CAD



Source: Mandiri Securities Research

# Indonesia's macro condition

Better position compared to the previous downward pressures



| Year | FY (%) | CAD to GDP (%) | External debt to GDP (%) | Debt Service Ratio (%) | Inflation (%) | Economic growth (%) |
|------|--------|----------------|--------------------------|------------------------|---------------|---------------------|
| 1998 | 48.1   | 3.5            | 128.4                    | 32.3                   | 58.4          | -13.1               |
| 2001 | 7.5    | 3.9            | 75.8                     | 21.3                   | 11.5          | 3.6                 |
| 2005 | 6.0    | 0.1            | 43.0                     | 18.7                   | 10.5          | 5.7                 |
| 2008 | 20.5   | 0.0            | 27.8                     | 13.7                   | 9.9           | 6                   |
| 2013 | 26.3   | -3.2           | 29.2                     | 20.4                   | 6.4           | 5.6                 |
| 2018 | 9.0    | -2.7           | 34.3                     | 32.3                   | 3.6           | 5.2                 |

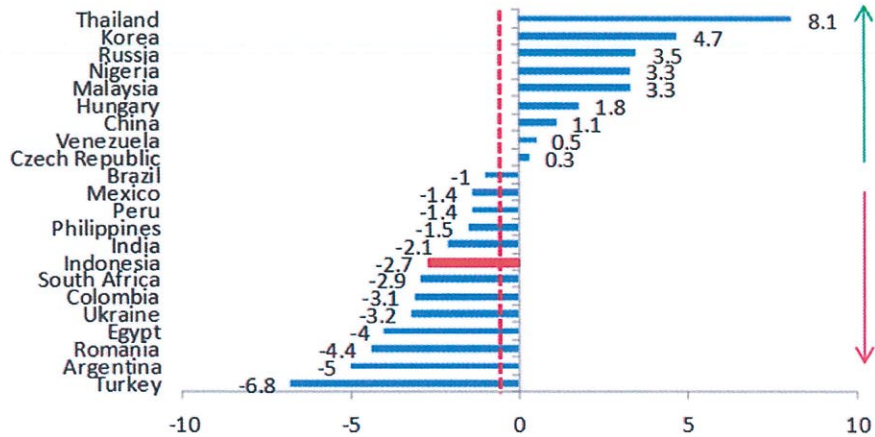
Source: Mandiri Securities Research

# Macro Indicators Affecting Exchange Rate

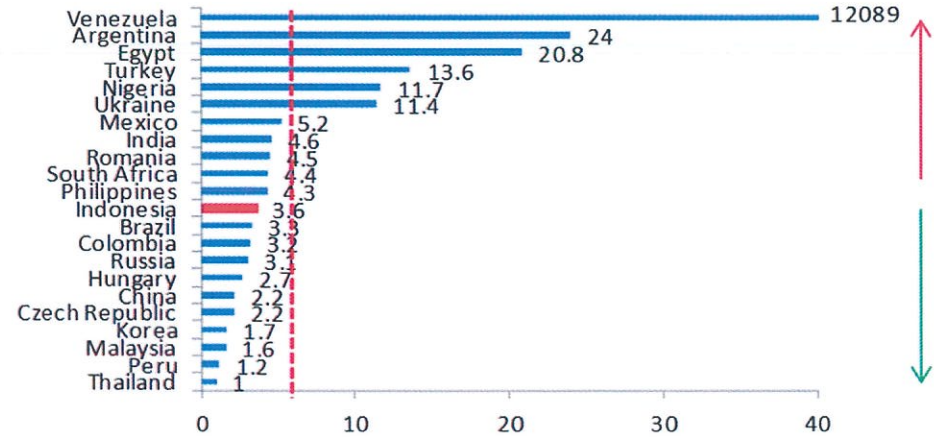
Are we vulnerable?



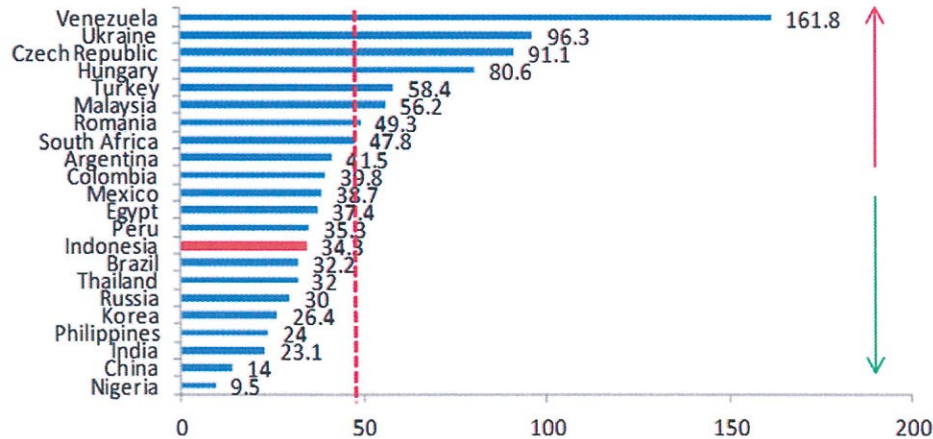
### CA to GDP (%)



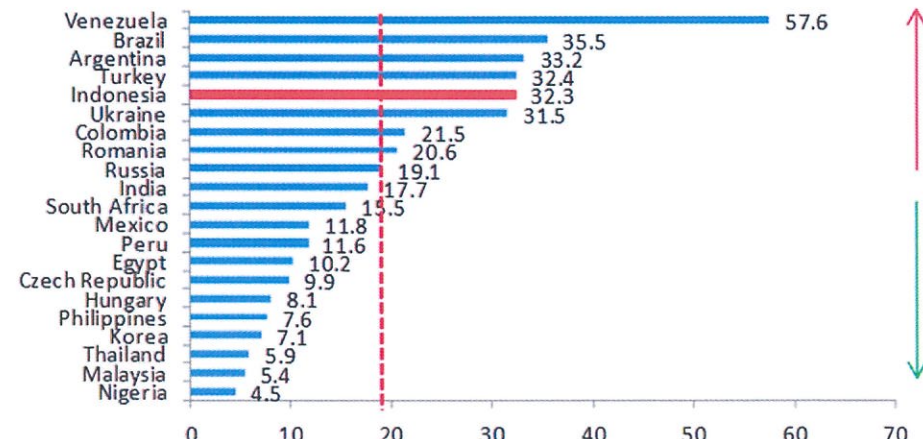
### Inflation (%)



### External Debt to GDP (%)



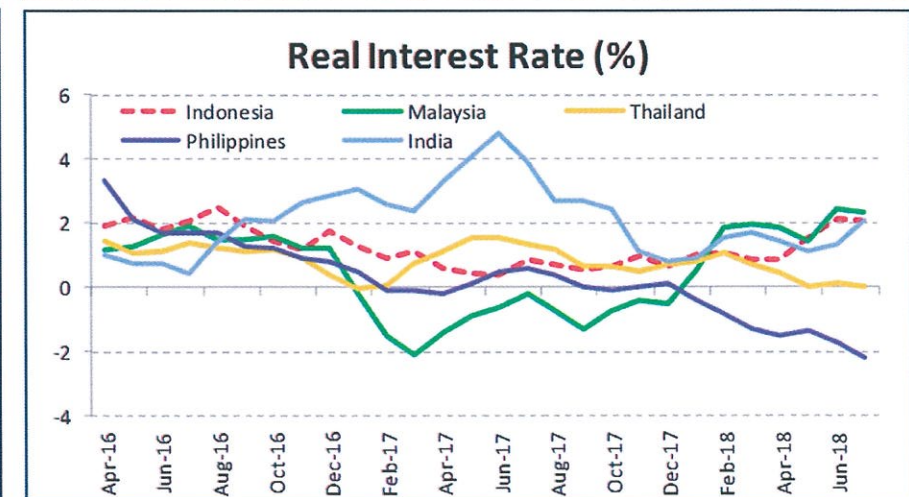
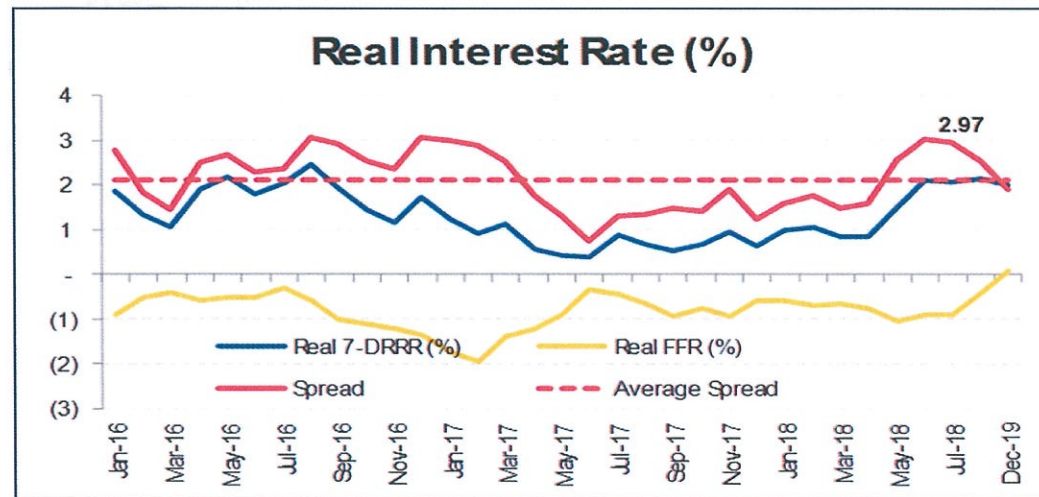
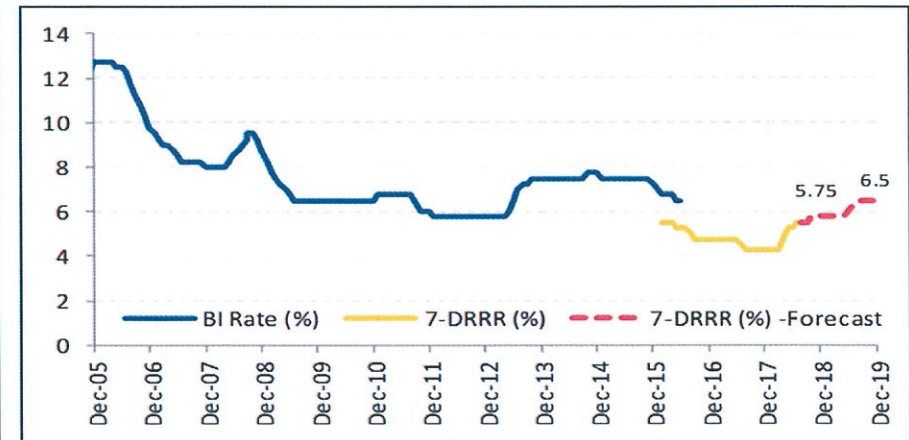
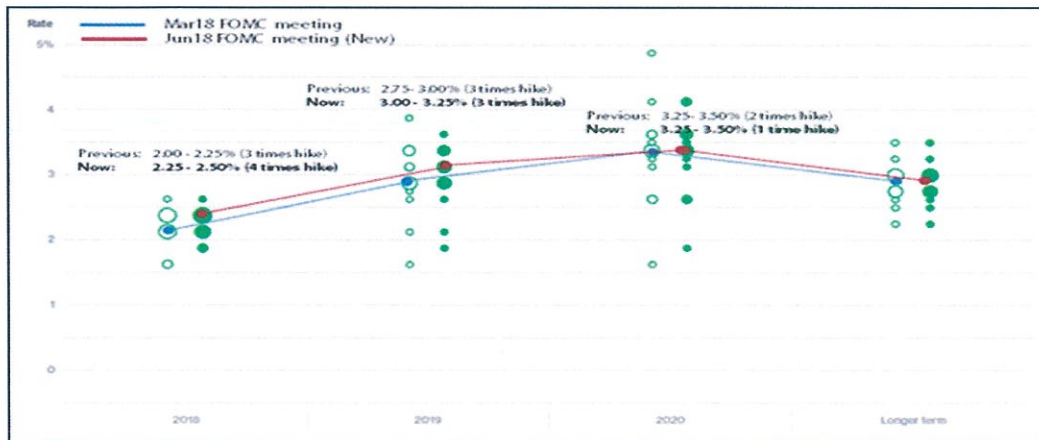
### Debt Service Ratio (%)



Source: Mandiri Securities Research

# Maintaining attractive real interest rate differential

## Expect policy rate to increase by another 25 (75) bps this year (2019)



| Year | 7DRRR (%) | Inflation (%) | Indo Real Interest Rate (%) | FFR (%) | Inflation (%) | U.S. Real Interest Rate (%) | Spread |
|------|-----------|---------------|-----------------------------|---------|---------------|-----------------------------|--------|
| 2018 | 5.75      | 3.60          | 2.15                        | 2.50    | 2.90          | -0.40                       | 2.55   |
| 2019 | 6.50      | 4.50          | 2.00                        | 3.00    | 2.90          | 0.10                        | 1.90   |

Source: Mandiri Securities Research

# Fiscal Policy Response

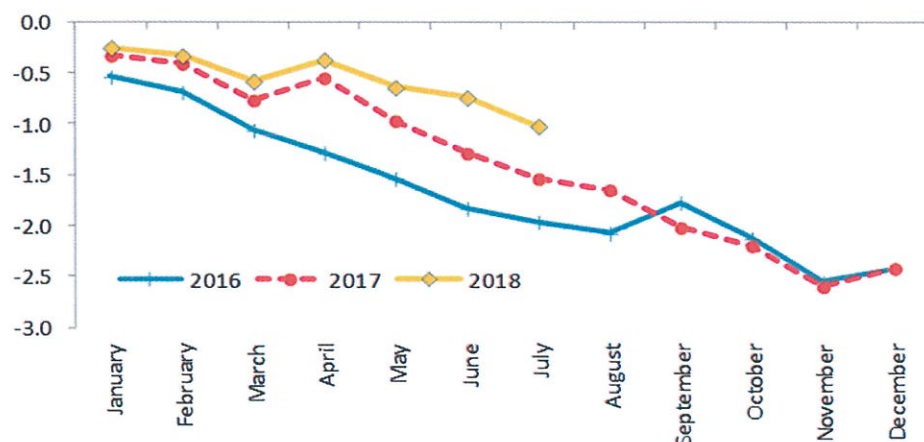
## Tightening Budget



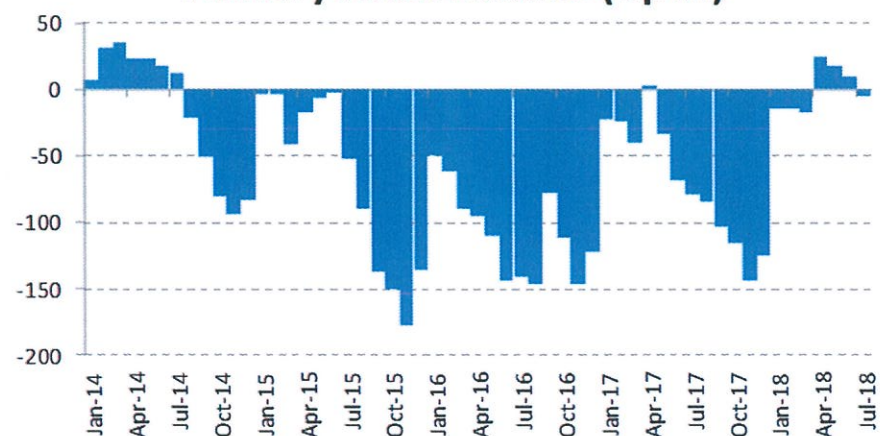
Budget deficit trend has been the lowest since the last several years

...as MoF's target is to improve primary fiscal balance going forward

### Budget Deficit (% of GDP)



### Primary Fiscal Balance (Rp tn)



The Government aims to have positive primary balance in 2020

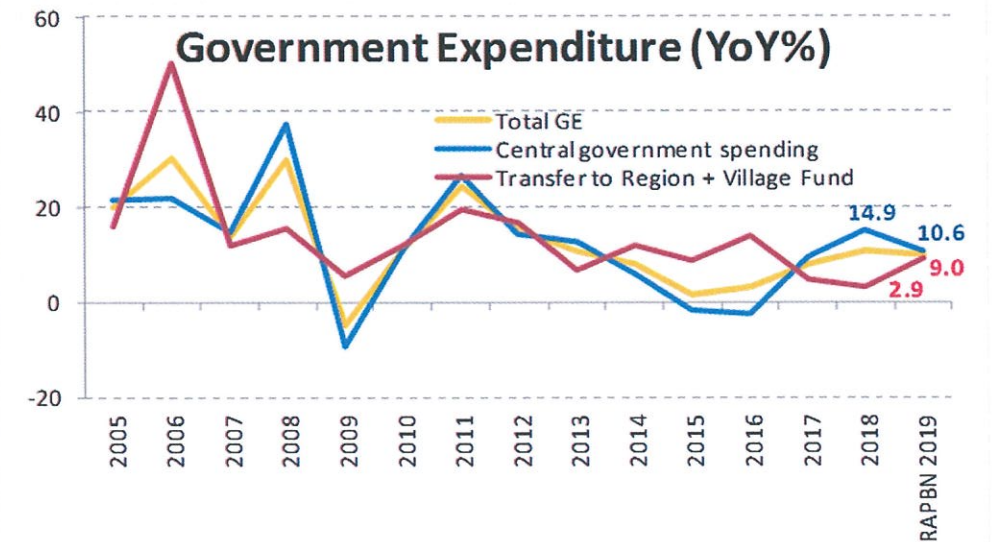
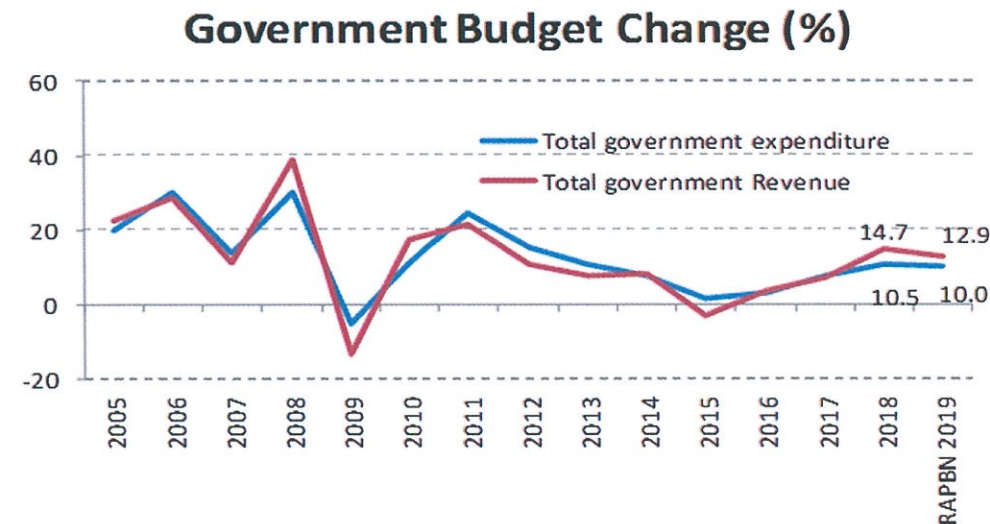
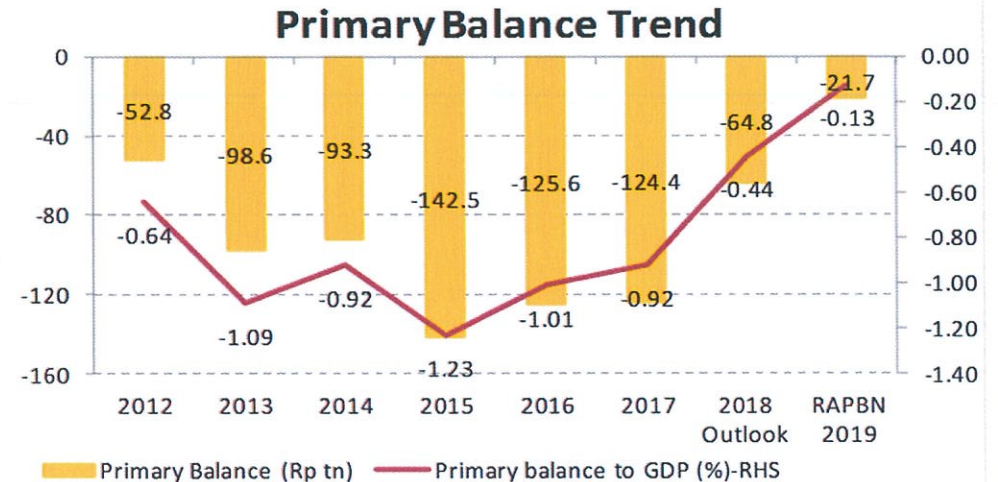
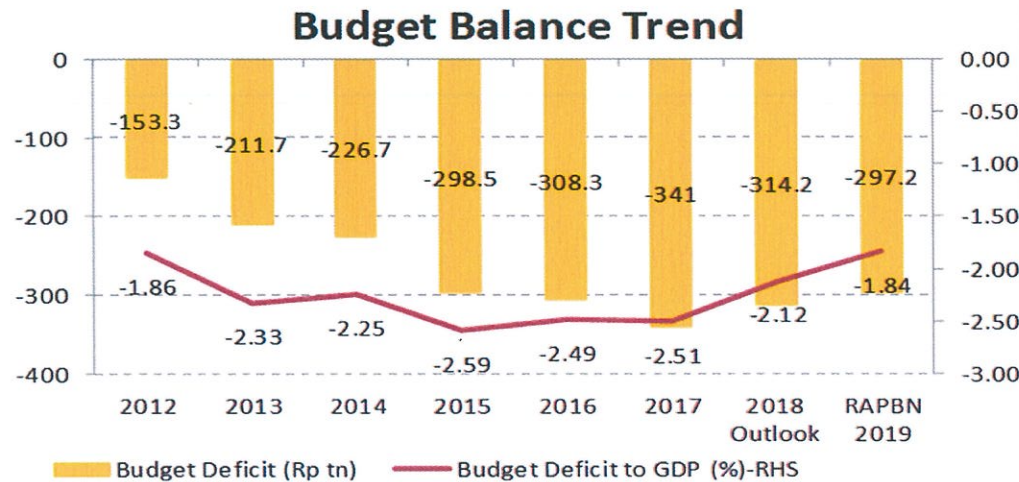
| Description (% GDP) | Budget 2018 | 2019**        | 2020          | 2021          | 2022          |
|---------------------|-------------|---------------|---------------|---------------|---------------|
| Revenue & Grants    | 12.76       | 12.7 – 13.5   | 12.7 – 13.9   | 13.5 – 14.0   | 13.6 – 14.4   |
| Tax Ratio*          | 11.6        | 11.4 – 11.9   | 11.4 – 12.5   | 11.6 – 13.0   | 11.8 – 13.6   |
| Total Spending      | 14.95       | 14.2 – 15.4   | 14.3 – 15.6   | 15.0 – 15.7   | 15.1 – 16.0   |
| Capital Expenditure | 1.4         | 1.5 – 1.7     | 1.8 – 2.3     | 2.2 – 2.7     | 2.3 – 3.0     |
| Primary Balance     | (0.59)      | 0.05 – (0.30) | 0.05 – 0.01   | 0.10 – 0.01   | 0.1 – 0.05    |
| Budget Deficit      | (2.19)      | (1.6) – (1.9) | (1.6) – (1.7) | (1.5) – (1.7) | (1.5) – (1.6) |
| Debt Ratio          | 29.07       | 28.8 – 29.2   | 28.50 – 28.61 | 27.81 – 28.30 | 26.25 – 27.87 |

\*Including revenue from oil&gas and general mining  
 \*\* submitted to parliament for discussion

Source: Mandiri Securities Research

# 2019 Fiscal Policy Target

Focus on stability, lower budget and primary fiscal deficits



Source: Mandiri Securities Research



# Pertamina has taken the burden from the “Off-balance-sheet subsidy”- consequence of maintaining the fuel



We estimated roughly a Rp60tn loss per year due to the unchanged Premium and Solar price (assuming ICP at USD70/bbl)

| No. | ICP (USD/bbl) | Brent Price (USD/bbl) | Rupiah/liter  |       |                  |       |         |       |                    |       | Rp trn                     |       |        | Rp trn (if solar subsidy is increased to Rp1000) |       |        | Rp trn (if solar subsidy is increased to Rp1500) |       |        | Rp trn (if solar subsidy is increased to Rp2000) |       |        |
|-----|---------------|-----------------------|---------------|-------|------------------|-------|---------|-------|--------------------|-------|----------------------------|-------|--------|--|-------|--------|--|-------|--------|--|-------|--------|
|     |               |                       | Selling Price |       | Economical Price |       | Subsidy |       | Price Differential |       | Gain (loss) of certain SOE |       |        | Gain (loss) of certain SOE                       |       |        | Gain (loss) of certain SOE                       |       |        | Gain (loss) of certain SOE                       |       |        |
|     |               |                       | Premium       | Solar | Premium          | Solar | Premium | Solar | Premium            | Solar | Premium                    | Solar | Total  | Premium  | Solar | Total  | Premium  | Solar | Total  | Premium  | Solar | Total  |
| 1   | 60            | 63                    | 6450          | 5150  | 8394             | 8362  | 0       | 500   | -1944              | -2712 | -33.0                      | -40.7 | -73.7  | -33.0  | -33.2 | -66.2  | -33.0  | -25.7 | -58.7  | -33.0  | -18.2 | -51.2  |
| 2   | 65            | 68                    | 6450          | 5150  | 8916             | 8884  | 0       | 500   | -2466              | -3234 | -41.9                      | -48.5 | -90.4  | -41.9  | -41.0 | -82.9  | -41.9  | -33.5 | -75.4  | -41.9  | -26.0 | -67.9  |
| 3   | 70            | 73                    | 6450          | 5150  | 9438             | 9406  | 0       | 500   | -2988              | -3756 | -50.8                      | -56.3 | -107.1 | -50.8  | -48.8 | -99.6  | -50.8  | -41.3 | -92.1  | -50.8  | -33.8 | -84.6  |
| 4   | 75            | 78                    | 6450          | 5150  | 9960             | 9928  | 0       | 500   | -3510              | -4278 | -59.7                      | -64.2 | -123.8 | -59.7  | -56.7 | -116.3 | -59.7  | -49.2 | -108.8 | -59.7  | -41.7 | -101.3 |
| 5   | 80            | 83                    | 6450          | 5150  | 10482            | 10450 | 0       | 500   | -4032              | -4800 | -68.5                      | -72.0 | -140.5 | -68.5  | -64.5 | -133.0 | -68.5  | -57.0 | -125.5 | -68.5  | -49.5 | -118.0 |

Assumption used:

- 1.) Solar Consumption Per year = 15 mn kiloliter      15
- 2.) Premium Consumption Per year = 20 mn kiloli      17
- 3.) Rupiah/USD = 14,400

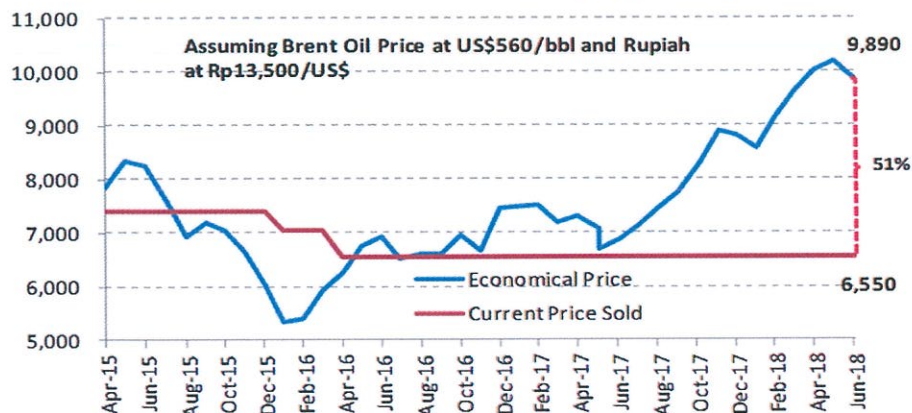
Source: Mandiri Securities Research

# Yet we believe fuel price will likely increase in 2H19

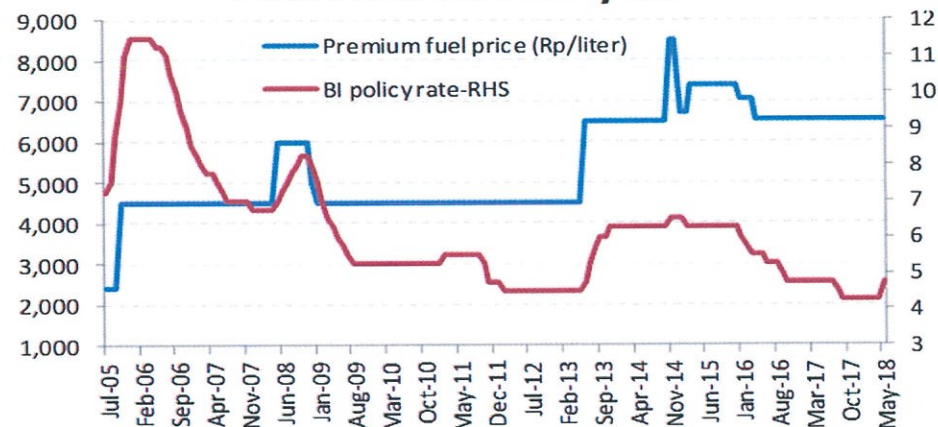
Impact : YE18/19 inflation is expected to reach 3.7/4.5%



### Indonesia's Retail Fuel Price (Rp/liter)



### Fuel Price vs. Policy Rate



### Simulation of Fuel Price Adjustment towards Headline Inflation

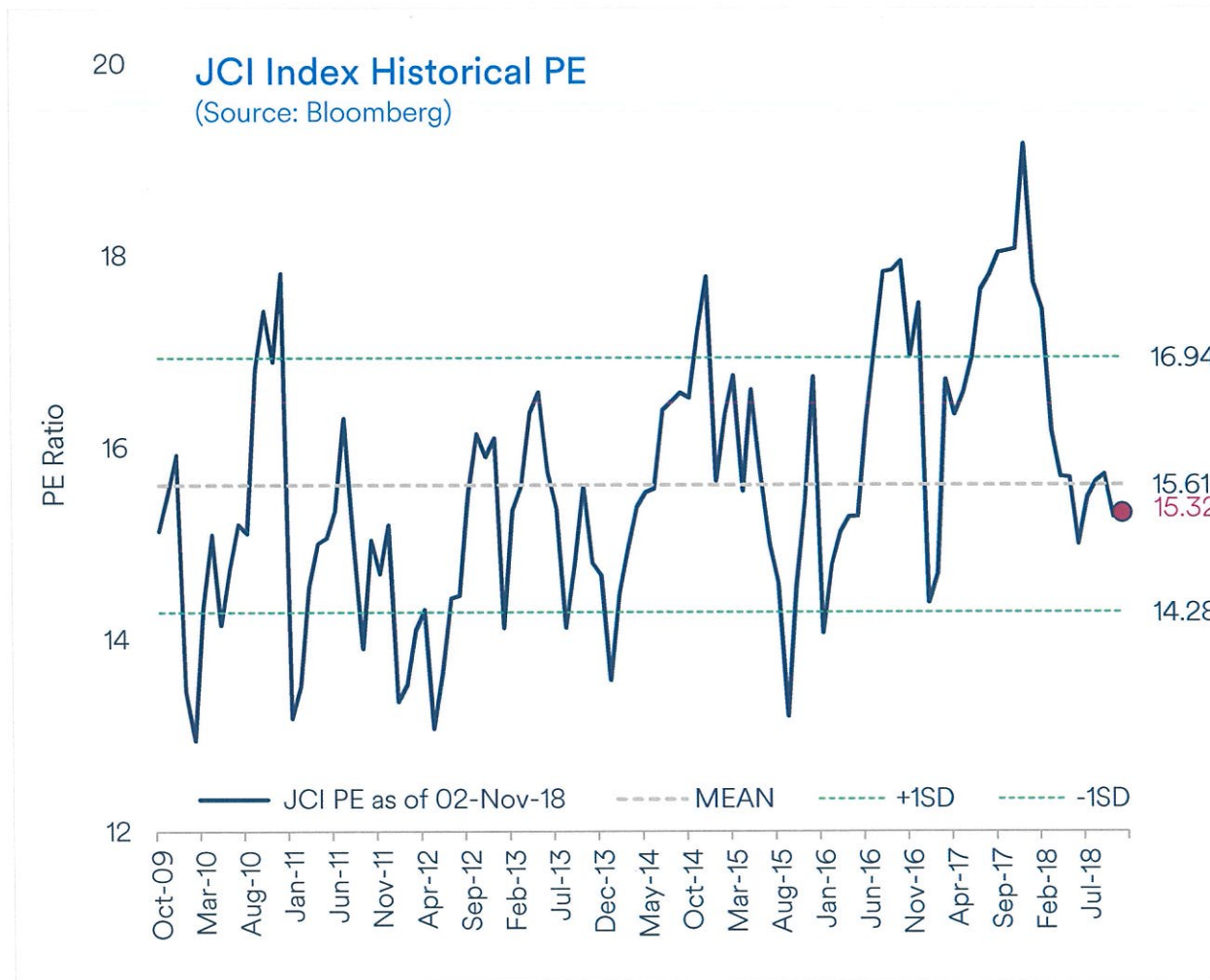
| Fuel Products  | Selling Price (Rp/liter) | Economical Price Calculation (Rp/liter) | Price difference Rp/liter (Econ - Selling) | Price Gap % (Econ - Selling) | BPS weight for fuel in CPI basket | Potential weight for fuel consumption in the new CPI basket | Potential inflation using BPS basket | Potential inflation using latest basket |      |
|--|--------------------------|---|--|------------------------------|-----------------------------------|---|--------------------------------------|---|------|
| Premium  | 6,550                    | 9,454                                   | 2,904                                      | 44.3                         | 2.01                              | 1.46  | 0.89                                 | 0.65                                    |      |
| Pertalite  | 7,800                    | 9,879                                   | 2,079                                      | 26.7                         | 1.32                              | 1.79  | 0.35                                 | 0.48                                    |      |
| Pertamax   | 8,900                    | 10,521                                  | 1,621                                      | 18.2                         | 0.64                              | 0.72  | 0.12                                 | 0.13                                    |      |
| Pertamax +   | 10,000                   | 11,504                                  | 1,504                                      | 15.0                         | 0.02                              | 0.03  | 0.00                                 | 0.00                                    |      |
| Calculation Impact towards Inflation assuming a one off increase |                          |   |  |                              |                                   |   | First round                          | 1.37                                    | 1.26 |
|  |                          |   |  |                              |                                   |   | Second                               | 0.68                                    | 0.63 |
|  |                          |   |  |                              |                                   |   | Total additional inflation           | 2.05                                    | 1.89 |

Assumptions used on the calculation:

- Economical Price calculation is based on exchange rate at Rp14,400/USD and oil price at USD71/bbl
- BPS fuel weight is based on BPS fuel consumption to total data
  - Premium : 50.4
  - Pertalite : 33.1
  - Pertamax : 16.0
  - Pertamax + : 0.6
- Current fuel weight is based on Pertamina fuel consumption to total data as of 2H17
  - Premium : 36.4
  - Pertalite : 44.8
  - Pertamax : 18
  - Pertamax + : 0.8

Source: Mandiri Securities Research

# The good thing is Valuation is not expensive



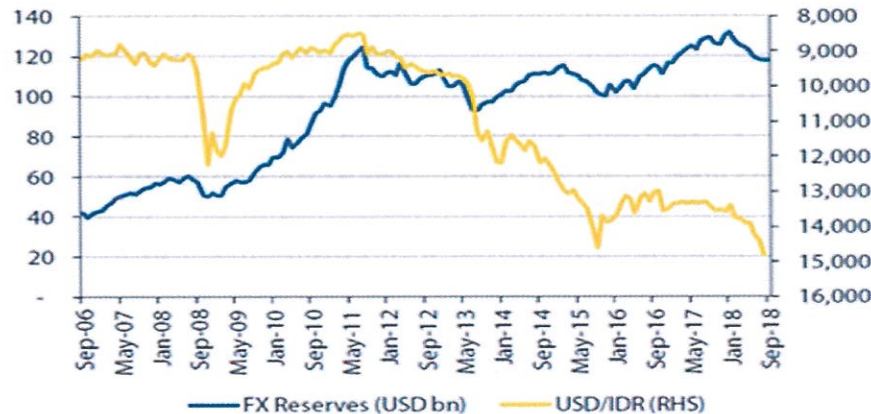
Source: Bloomberg, Schroders, as of Nov. 2018.

# The good thing is...

The sell off have made JCI more attractive, however need FX stability

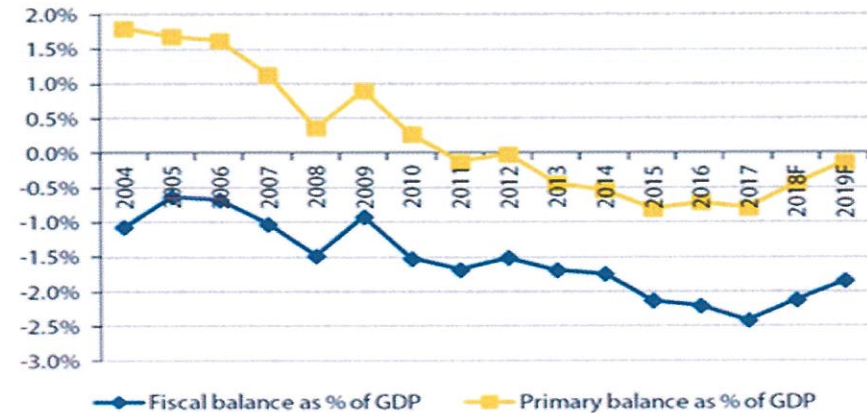


FX reserve trend vs Rupiah



Source: Bloomberg

Fiscal and primary balance trend



Source: Ministry of Finance

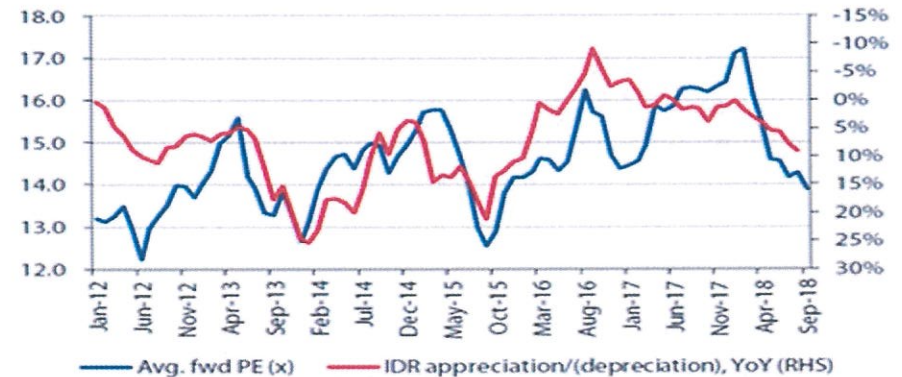
JCI valuation vs Foreign ownership- the sell offs have made JCI more attractive



Note: We adjusted the foreign stakes to exclude tax amnesty changes

Source: Bloomberg, Mandiri Sekuritas calculations

But conviction is needed in the currency as it will affect earnings growth and valuation



Source: Bloomberg, Company, Mandiri Sekuritas calculations

# Government Action

## Short term

### Strategi Perbaikan Defisit Neraca Transaksi Berjalan: Jangka Pendek

|  |   |
|--|---|
| <b>Pengendalian kebutuhan impor proyek-proyek infrastruktur</b>                | <ul style="list-style-type: none"><li>• Penundaan selektif proyek infrastruktur yang tingkat urgensi dan dampak ekonominya rendah → mengurangi tekanan kebutuhan impor barang modal dan bahan baku</li><li>• Mendorong kepatuhan pelaksanaan aturan TKDN proyek infrastruktur energi → impor produk sejenis dapat dipenuhi oleh industri domestik</li></ul>   |
| <b>Implementasi Biodiesel B20</b>  | <ul style="list-style-type: none"><li>• Berbagai kendala implementasi bahan bakar biodiesel B20 perlu segera diatasi, hal ini berpotensi untuk mengurangi impor migas yang relatif besar</li></ul>  |
| <b>Perluasan cakupan produk yang dikenakan PPh impor</b>                       | <ul style="list-style-type: none"><li>• Saat ini terdapat sekitar 500 produk yang telah dikenakan PPh Impor sebesar 7,5%</li><li>• Berdasar kajian, masih terdapat sekitar 500 produk yang dapat dikenakan PPh Impor atau dinaikkan tarifnya dan produk tersebut memiliki substitusinya dari dalam negeri</li></ul>   |
| <b>Percepatan penerapan tarif MFN &amp; reviu batas nilai transaksi barang</b> | <ul style="list-style-type: none"><li>• Perubahan tarif bea masuk <i>most favoured nations</i> (MFN), s.d. Maret 2017 baru sekitar 300 produk dari usulan Kemenperin 1089 produk; diatur PMK No. 06/PMK.010/2017</li><li>• Reviu batas nilai transaksi yang dikenakan bea masuk dan/atau Pajak Dalam Rangka Impor (PPh dan PPN), sebesar USD100 - dapat disesuaikan hingga USD50 per pengiriman</li></ul> |

Selain itu, pemerintah terus berkomitmen untuk melakukan kebijakan peningkatan daya saing dan promosi ekspor untuk memperbaiki masalah struktural defisit neraca transaksi berjalan

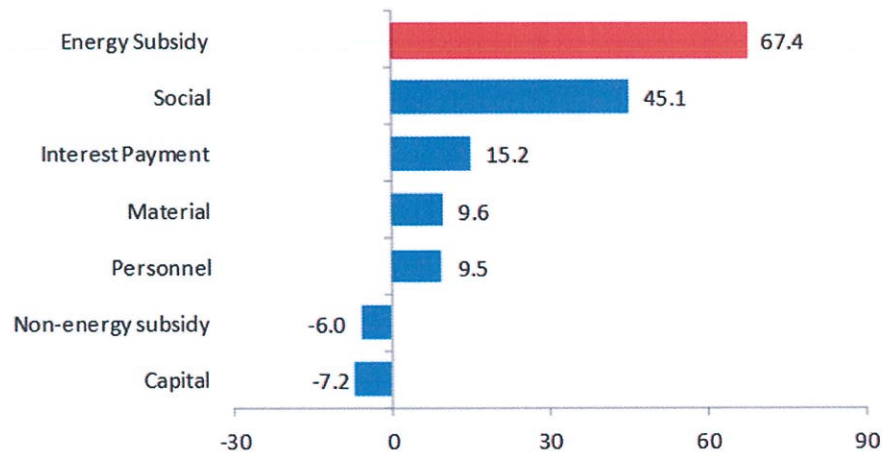
Source : Ministry of Finance

# 2019 Government Spending Focus (1)

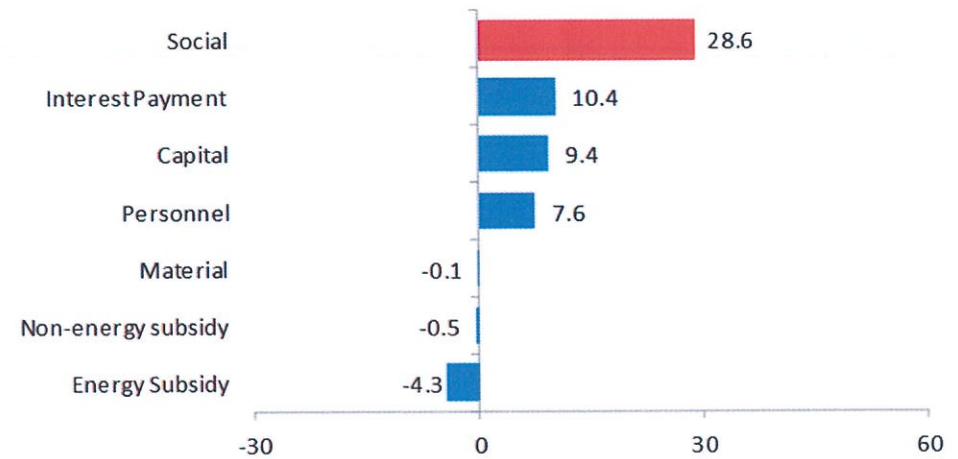
## Supporting the bottom 40% of the income group



2018 Central Government Expenditure (YoY%)



2019 Central Government Expenditure (YoY%)



| No.   | Programs to support the bottom 40% of the population | APBN 2018      |                                 | RAPBN 2019     |                                 |
|-------|--|----------------|---------------------------------|----------------|---------------------------------|
|       |  | Amount (Rp tn) | Target                          | Amount (Rp tn) | Target                          |
| 1     | Village Fund   | 60             | 74,957 villages                 | 73.0           | 74,957 villages                 |
| 2     | PKH (Family Hope Program)                            | 17.3           | 10 mn families                  | 34.4           | 10 mn families                  |
| 3     | JKN (National Health Insurance)                      | 25.5           | 92.5 million persons            | 26.7           | 98 mn persons                   |
| 4     | BPNT (Non-cash food program)                         | 20.8           | 15.6 mn families                | 20.8           | 15.6 mn families                |
| 5     | PIP (Indonesia Smart Program)                        | 10.5           | 19.7 mn students                | 10.8           | 20.1 mn students                |
| 6     | College program fund (Bidik Misi)                    | 4.1            | 401.5 thousand college students | 4.4            | 471.8 thousand college students |
| 7     | Ultra micro financing                                | -              | 0.8 mn                          | 3.0            | 1.4 mn debitur                  |
| Total |  | 138.2          |                                 | 173.1          |                                 |

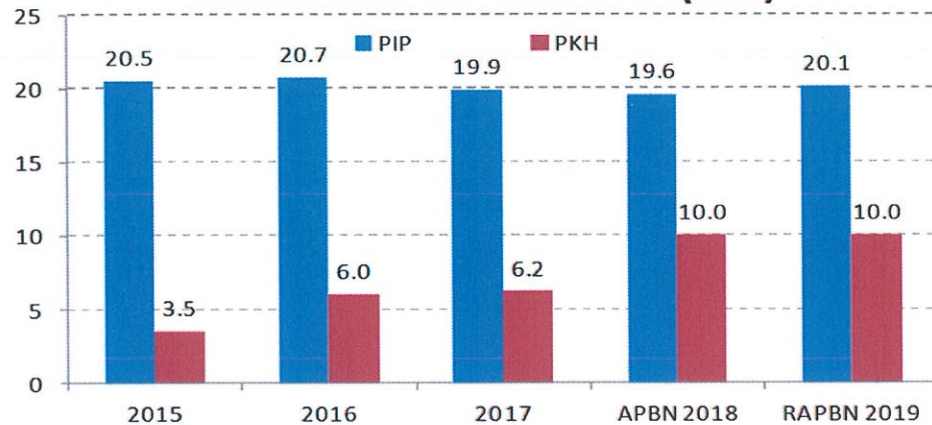
Source: Mandiri Securities Research

# 2019 Government Spending Focus (2)

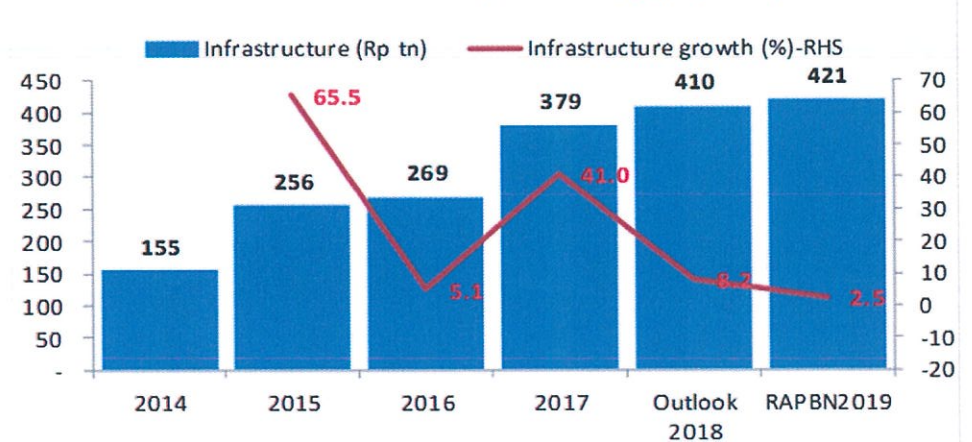
Supporting the bottom 40% of the income group



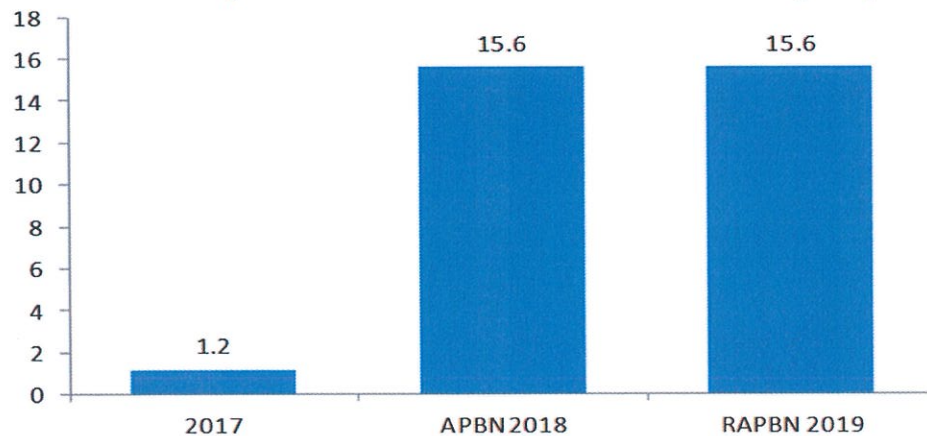
### Amount of PIP and PKH (mn)



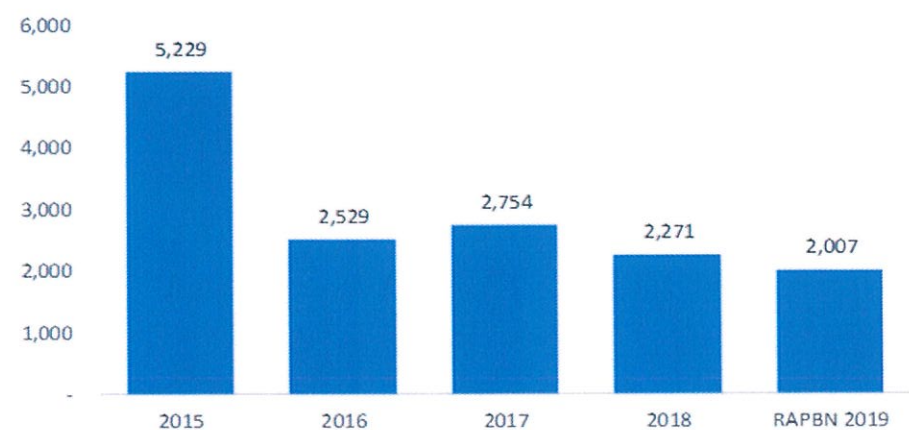
### Infrastructure Spending (Rp tn)



### Family that receive non-cash food aid (mn)



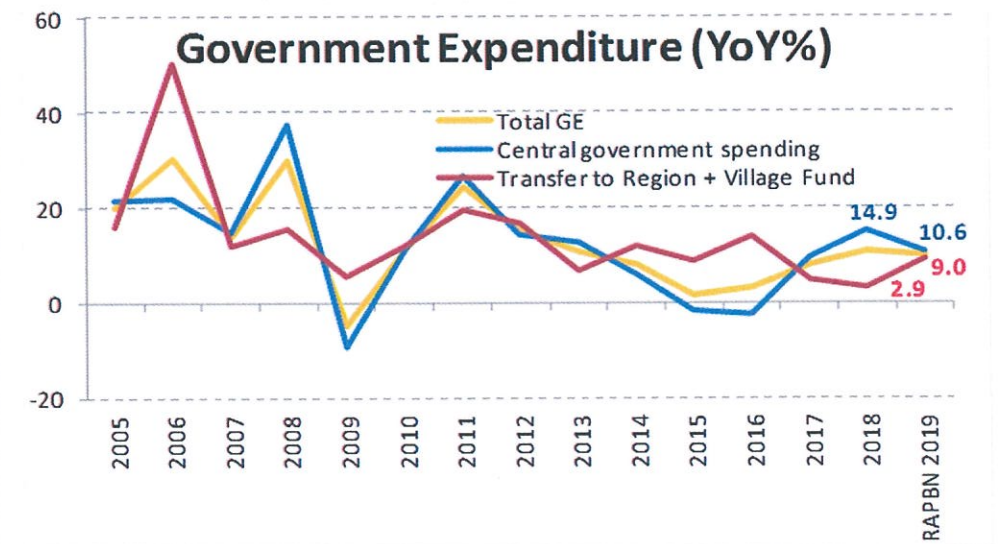
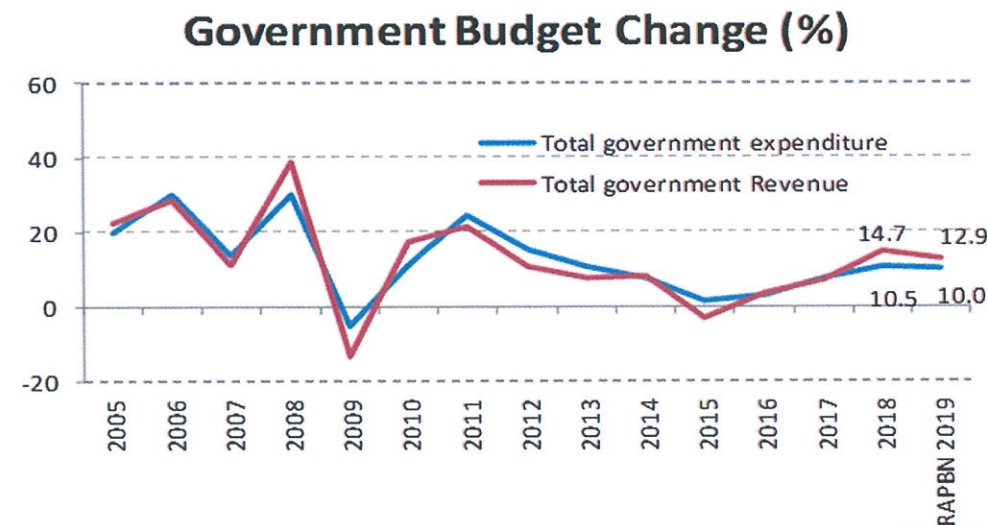
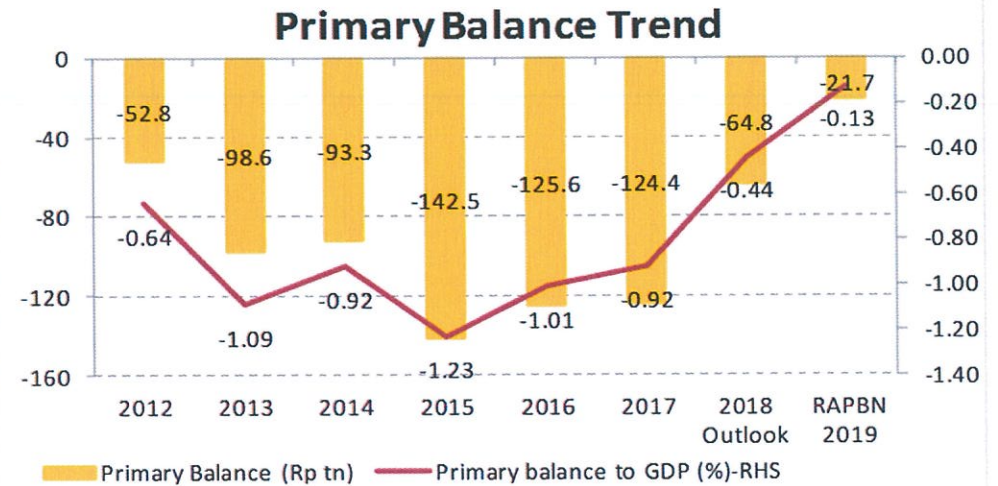
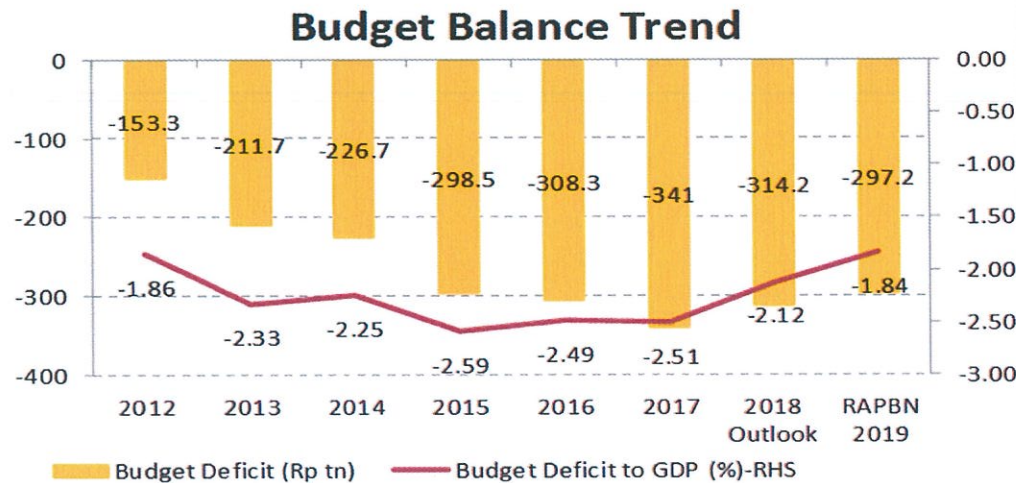
### 2019 Road Target Realization (km)



Source: Mandiri Securities Research

# 2019 Fiscal Policy Target

Focus on stability, lower budget and primary fiscal deficits

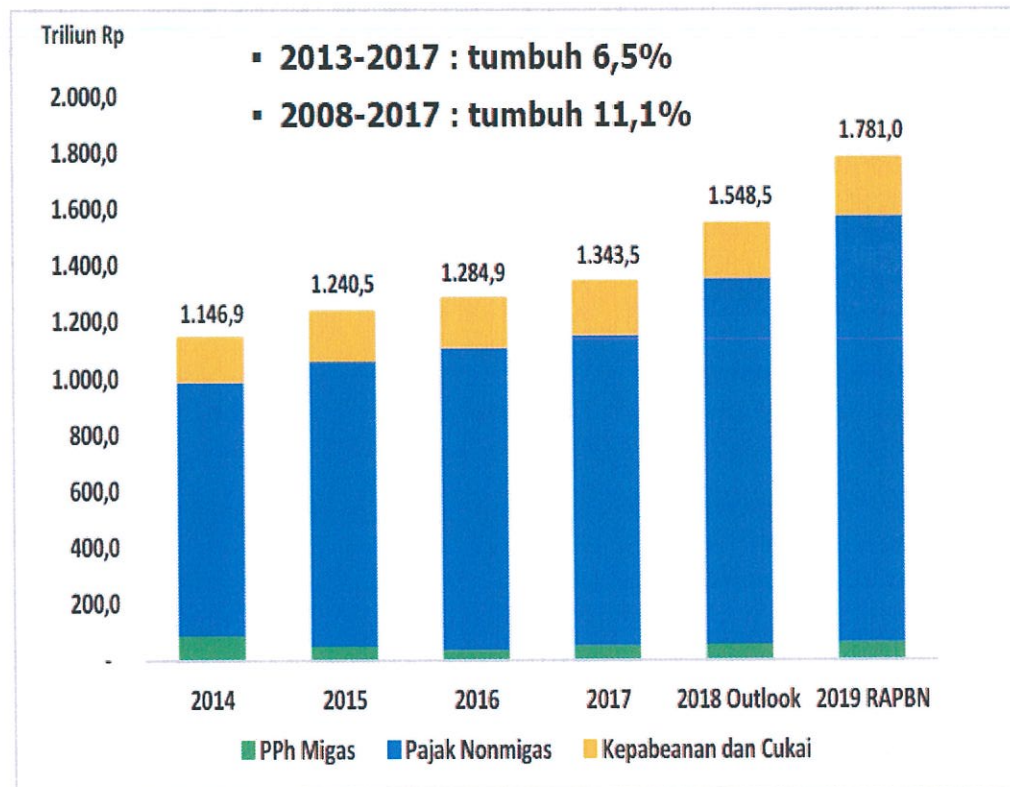


Source: Mandiri Securities Research



# Tax Reform

## On the track



### Dalam RAPBN 2019:

- Target Pajak nonmigas (*excl.* PPh migas) tumbuh 16,6% dari *Outlook* 2018
- Kepabeanan dan Cukai tumbuh 5,6% dari *outlook* 2018

**Kontribusi Penerimaan Perpajakan semakin meningkat → menuju kemandirian**

dari 74% di tahun 2014 menjadi 83,1% di tahun 2019

**Pajak Menjaga keberlangsungan iklim investasi dan peningkatan daya saing**

### Penguatan Pelayanan Perpajakan

- simplifikasi registrasi, perluasan tempat pemberian pelayanan
- perluasan cakupan *e-filing*, dan
- kemudahan restitusi

### Penegakan Hukum

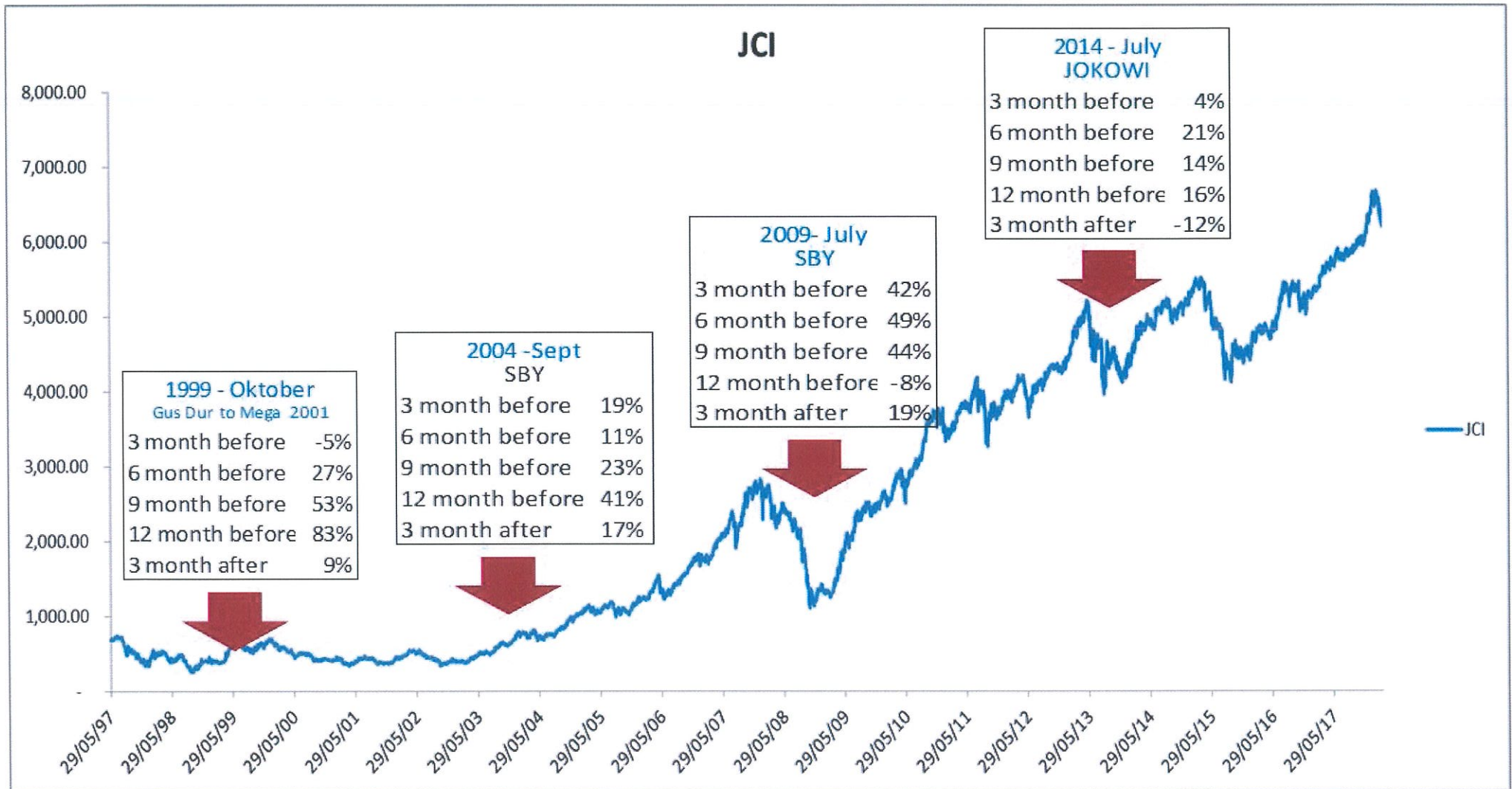
- Pelaksanaan penegakan hukum (*law enforcement*) secara berkeadilan
- Peningkatan mutu pemeriksaan melalui perbaikan tata kelola pemeriksaan

### Pengawasan Kepatuhan Perpajakan

- Implementasi AEOI dan akses informasi keuangan
- Ekstensifikasi dan peningkatan pengawasan sebagai tindak lanjut pasca *tax amnesty*
- Penanganan UMKM secara *end-to-end* melalui pendekatan *Business Development Services* (BDS)
- Joint Program* DJP-DJBC
- Pembenahan basis data perpajakan
- Penerapan pengawasan Wajib Pajak berbasis risiko (*Compliance Risk Management /CRM*)

# Indonesia election

How historically the market reacts?



Source: Schroders Research, Bloomberg



Thank you

# Disclaimer

## Important information

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