Indonesian Economic Outlook 2017

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Creco Research
Unchartered waters
The world is desperate to learn what Donald Trump is thinking...

Nobody seems to have a clue...

Can you help?

Sure... but first...

I have to finish with another client...

I was elected president of the United States...

What was I thinking?
GDP growth: Indonesia is one of the least unattractive countries in Asia

**TABLE 2.1.2 East Asia and Pacific country forecasts**
(Real GDP growth at market prices in percent, unless indicated otherwise)

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<td>Solomon Islands</td>
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<td>Timor-Leste(^b)</td>
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Source: World Bank, 2017

World Bank forecasts are frequently updated based on new information and changing (global) circumstances. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of countries’ prospects do not significantly differ at any given moment in time.

a. GDP at market prices and expenditure components are measured in constant 2010 U.S. dollars. Excludes American Samoa and Democratic People’s Republic of Korea.

b. Non-oil GDP. Timor-Leste’s total GDP, including the oil economy, is roughly four times the non-oil economy, and highly volatile, sensitive to changes in global oil prices and local production levels.

For additional information, please see www.worldbank.org/egp.
GDP growth: Indonesia, one of the least unattractive countries
New normal growth?

- Success story of East Asia: Industrialization and trade
- A world with creeping protectionism
- Services is not a perfect substitute to manufacturing
Why services are not like manufact

Taken from Dani Rodrik (2014)

High-productivity (tradable) services sector cannot absorb as much labor

- Premium skill-intensive
- Requires good institution

Low productivity (non-tradable) services cannot act as growth poles

- since they cannot expand without turning their terms of trade against themselves
- continued expansion in one segment relies on expansion on others
- limited gains from sectoral “winners”
Trump Effect

- Too early to conclude
- Short term, volatility in financial market
- Protectionist policy, world trade will shrink
- Boost domestic demand through tax cut and govt spending
- Medium term: every President will become a normal President after a while
Commodity prices stabilized in 2016 and are expected to grow gradually in 2017.

A. Commodity prices

Index, nominal term, 2010=100
- Energy
- Agriculture
- Metals

B. Changes in commodity prices

Percent
- 50
- 30
- 10
- -10
- -30
- -50
- -70

Energy
Metals
Agriculture

C. U.S. oil rig count and oil price

US$/bbl
- Oil price, WTI (LHS)
- US oil rig count (RHS)

D. Stock-to-use ratios

Ratio
- 0.4
- 0.3
- 0.2
- 0.1

Maize
Wheat
Rice

A. Latest observation is November 2016.
B. Commodity prices represent actual data up to 2016 and forecasts from 2017 to 2019.
C. Last observation is December 16, 2016.
D. Stock-to-use ratios denote the ratio of ending stocks to domestic consumption and represent a measure of how well supplied the market is. The last observation (2016-17 crop year) reflects the December 2016 U.S. Department of Agriculture update.
The macroeconomic impact of the global volatility

Negative interest rate → capital inflow → Exchange rate (?) → Trade balance/current account deficit

The Fed: raising interest rate → Risks of assets re pricing → Trump Effect → commodity price (?) → Slow down of China

Bank Indonesia: no much room for lowering interest rate or maybe will raise interest rate → Fiscal expansion (?) → Economic growth → Solution: FDI (export oriented) ↑ + reform → Oil price (?) → Short fall of Government Revenue
Domestic economy
Source: CEIC (2016)
Industrial production indicators
(PMI diffusion index; industrial production growth yoy, percent)

Motor vehicle sales
(seasonally-adjusted sales growth yoy, percent)

Consumer indicators
(retail sales index 2010=100)

Balance of Payment
(USD billion)

Source: CEIC (2016)
Indonesia: GDP growth and ICOR

- **ICOR=6.2-64 (ratio Investment/GDP)**

- 1% GDP growth will require Investment/GDP 6.2-6.4%

- **S=I**

- The Indonesia Gross Domestic Savings/GDP 33.8% (World Bank)

- Thus GDP Growth more or less 5-5.5%

- If Indonesia wants to achieve 6% GDP growth:

  - I/GDP should be 6%*6.2-6.4%=37.2-38.4%

  - S/GDP=34% → S-I= - 3% (current account deficit)

- To get higher growth: we should increase S or lower ICOR (improve productivity and efficiency)
Recent development
Improvement in export: thanks to commodity prices
Financial sector
Source: CEIC (2016),
*from Aug 2016 Bank Indonesia adopt 7-days repo rate as new benchmark of monetary tool
**Reserve and Capital Inflow (USD billion)**

- **Central Bank**
- **Gov**
- **Private Sector**

**International Reserves (RHS)**

- **Dec-13**
- **Dec-14**
- **Dec-15**
- **Dec-16**

**Inflation Contribution (yoy growth, percent)**

- **Volatile**
- **Administrated**
- **Core**
- **Headline**

**Inflation comparison across countries (as of Oct 2016; change yoy)**

- **India** 4.9
- **Indonesia** 3.5
- **Philippines** 1.8
- **China** 2.0
- **Malaysia** 1.9
- **US** 1.3
- **Britain** 0.6
- **Thailand** 0.2
- **Japan**
- **Singapore**

**Regional equity indices (daily index in local currency, Oct 1 2013=100)**

- **Shanghai-China**
- **BSE-India**
- **JSI-Indonesia**
- **SET-Thailand**
- **SGX-Singapore**

Source: CEIC, Economist Intelligence Unit (2016)
Exchange Rates
(IDR/USD)

Nominal and Real Effective Exchange Rate Index
(Dec 2010 = 100)

Currency Movement
(Exchange rates appreciation, %, ytd)

Selected currencies against USD
(monthly index May 2013=100)

Source: CEIC (2016)
Currency and Reserve
(Monthly, Currency: IDR/USD, Reserve: USD mn)

Reserve (LHS)

IDR/USD (RHS)

10-year local currency gov. bond yields
(percent)

Yield Curve of Indonesia Government Bond
(percent)

Yield Curve of Treasury Bond
(percent)

Source: CEIC (2016)
Indonesia and USA Government Bond
(10y, percent)

Government Debt
(percent of GDP; USD billion)

External Debt
(percent of GDP; USD billion)

Indonesia Government Bond Ownership:
Foreign
(percentage of total government bond)

Source: CEIC (2016)
Credit growth, consumption and interest rate (Zahro, 2016)

- Consumption positively affect credit growth
- Investment does not significantly affect credit growth.
- BI rate does not significantly affect credit growth.
- Fed fund rate significantly affects credit growth. When the fed fund rate goes up, credit growth falls. This also explains the role of liquidity inflow.
- The short term problem is on the demand side
Banking sector indicators
(Monthly, percent)

- Loan to deposit ratio
- Return on assets (RHS)
- Non performing loans (RHS)
- Capital adequacy ratio

Deposit Growth
(yoy growth, percent)

- Demand Deposit
- Saving Deposit
- Time Deposit

Credit Growth
(yoy growth, percent)

- Investment
- Consumption
- Working Capital

Real Interest Rate
(Monthly, Gov.Bond 10y, %)

- Indonesia
- China
- United States
- Germany
- India
- Japan

Source: CEIC (2016)
Indonesian Government Debt: maturity schedule

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<tr>
<td>Pinjaman</td>
<td>63%</td>
<td>30%</td>
<td>26%</td>
<td>25%</td>
<td>35%</td>
<td>24%</td>
<td>29%</td>
<td>24%</td>
<td>15%</td>
<td>22%</td>
<td>14%</td>
<td>29%</td>
<td>23%</td>
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<tr>
<td>SBN</td>
<td>37%</td>
<td>70%</td>
<td>74%</td>
<td>75%</td>
<td>65%</td>
<td>76%</td>
<td>71%</td>
<td>76%</td>
<td>85%</td>
<td>78%</td>
<td>86%</td>
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<td>Pinjaman</td>
<td>16%</td>
<td>39%</td>
<td>12%</td>
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<td>10%</td>
<td>21%</td>
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<td>3%</td>
<td>17%</td>
<td>8%</td>
<td>3%</td>
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<tr>
<td>SBN</td>
<td>84%</td>
<td>61%</td>
<td>88%</td>
<td>75%</td>
<td>78%</td>
<td>90%</td>
<td>79%</td>
<td>94%</td>
<td>93%</td>
<td>97%</td>
<td>83%</td>
<td>92%</td>
<td>97%</td>
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Some risks

- Fiscal risk due to the short fall of tax revenue
- NPL is rising
- Liquidity tightening
## Government Budget

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<th>2015</th>
<th>2016</th>
<th>Growth</th>
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<td></td>
<td>Rp trillion</td>
<td>Rp trillion</td>
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<td>Government Revenue</td>
<td>1508</td>
<td>1551.8</td>
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<td>Domestric Revenue</td>
<td>1496</td>
<td>1546</td>
<td>3.34</td>
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<td>1. Tax Revenue</td>
<td>1240.4</td>
<td>1283.6</td>
<td>3.48</td>
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<td>1060.8</td>
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<td>2. Import duty and excise</td>
<td>179.6</td>
<td>178.7</td>
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<td>Non Tax Revenue</td>
<td>255.6</td>
<td>262.4</td>
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<td>Grant</td>
<td>12</td>
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<td>Government Spending</td>
<td>1806.4</td>
<td>1859.5</td>
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<td>Central Govt.</td>
<td>1183.3</td>
<td>1148.6</td>
<td>-2.93</td>
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<td>Transfer to region and villag fund</td>
<td>623.1</td>
<td>710.9</td>
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<td>Primary Balance</td>
<td>-142.5</td>
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<td>Surplus/Deficit</td>
<td>-298.4</td>
<td>-307.7</td>
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2.46% of GDP
Tax revenue and tax amnesty

- Non oil Tax revenue 2016 : Rp 1069 T (incl. TA)
- TA as of Dec 31, 2016: 107 T
- Tax Revenue 2016 (without TA): Rp 962 T
- Tax revenue, 2015: Rp1011.2 T
- The economy still posts a positive growth, however growth of tax revenue (without TA) was -4.5% in 2016
What about the next year?

- Total assets declared Rp 4296 T
- Domestic Rp 3143 T
- Overseas Rp 1013 T
- Assuming all assets are income generating
- ROA 5%
- Average tax 25%
Outlook 2016 and 2017

- Private consumption: bottoming out, may slightly improve, thanks to some rebound in commodity prices
- Exports: Exports: may improve thanks to higher commodity prices, but global environment remain fragile
- Investments: remain sluggish
- Government spending: no much room for fiscal stimulus due to short fall in the revenue
- Interest rate: not much room for BI to cut the rate
- Capital inflows: remain
- Exchange rate: tend to weaken
- Fiscal risk: revenue tends to decline unless there is a significant reform on tax and re focusing on spending quality
Thank you