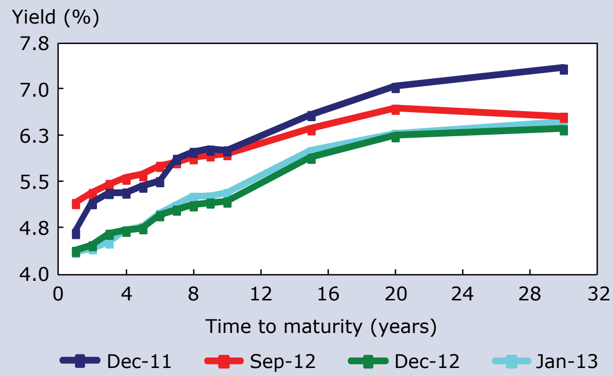
Indonesia

Yield Movements

Local currency (LCY) government bond yields in Indonesia fell for all tenors between end-September and end-December, resulting in the entire curve shifting downward **(Figure 1)**. By end-January, however, the yield curve rose slightly above its end-December level with a steepening bias, as the decline in yields at the short-end was outpaced by rising yields from the 4-year maturity through the long-end of the curve. Specifically, yields at the shortest-end (1-year maturity) of the curve fell only 1 basis point (bp) while yields from the belly through the end of the curve rose as much as 10 bps to 14 bps. The yield spread between the 2- and 10-year maturities widened to 90 bps at end-January from a spread of 71 bps at end-December 2012.

Figure 1: Indonesia's Benchmark Yield Curve—LCY Government Bonds



LCY = local currency.
Source: Bloomberg LP.

The downward shift in Indonesia's government bond yield curve may be attributed to foreign fund inflow as well as stable inflation. Foreign fund inflows into the Indonesian bond market remained strong in 4Q12 on the back of positive macro-fundamentals and attractive yields. The United States (US) Federal Reserve's announcement in December that it would expand its asset purchase program also helped boost demand for high-yield assets such as Indonesian debt instruments.

Consumer price inflation in Indonesia eased marginally in December, leveling off at 4.30% year-on-year (y-o-y), compared with 4.32% in November and 4.61% in October. Consumer price inflation for the full-year 2012 was at 4.3%, well within Bank Indonesia's (BI) 2012 inflation target range of between 3.5% and 5.5%, and below the Ministry of Finance's annual target of 5.3%. In January, consumer price inflation rose to 4.6% y-o-y due mainly to increases in power tariffs and food prices. On a month-on-month (m-o-m) basis, consumer prices rose to 1.0% in January, from 0.5% a month earlier.

In a meeting held on 12 February, BI's Board of Governors decided to keep its benchmark interest rate steady at 5.75%. The BI rate has remained at a record-low level since February of last year. At its current level, the BI rate remains consistent with the central bank's 2013 inflation target range (3.5%–5.5%). According to BI's assessment, Indonesia's economy continued its robust performance in 2012, yet pressure on the external balance remains strong due to the weak global environment.

Economic growth in Indonesia slowed to a still-robust rate of 6.1% y-o-y in 4Q12, following annual growth of 6.2% in 3Q12. On a quarter-on-quarter (q-o-q) basis, the economy contracted 1.5% in 4Q12, after posting 3.2% growth in 3Q12. Full-year GDP growth was recorded at 6.2% y-o-y, compared with 6.5% in 2011, amid weakened export performance. Domestic consumption (5.3%) and investment (9.8%) continued to drive growth in 2012. For 2013, BI is forecasting economic growth of between 6.3% and 6.7%, while the Ministry of Finance is targeting growth of 6.8% based on its budget forecast for the year.

Table 1: Size and Composition of the LCY Bond Market in Indonesia

	Outstanding Amount (billion)								**Growth Rate** (%)						
	Sep-12		**Oct-12**		**Nov-12**		**Dec-12**		**Sep-12**		**Oct-12**	**Nov-12**	**Dec-12**		
	IDR	**US$**	**IDR**	**US$**	**IDR**	**US$**	**IDR**	**US$**	**q-o-q**	**y-o-y**	**m-o-m**	**m-o-m**	**m-o-m**	**q-o-q**	**y-o-y**
Total	1,054,800	110	1,080,862	112	1,090,985	113	1,090,055	111	0.4	7.4	2.5	0.9	(0.1)	3.3	9.7
Government	883,479	92	905,942	94	913,119	95	902,594	92	(0.1)	4.2	2.5	0.8	(1.2)	2.2	6.6
Central Govt. Bonds	812,796	85	834,000	87	834,551	87	820,266	84	2.7	16.7	2.6	0.1	(1.7)	0.9	13.4
Central Bank Bills	70,683	7	71,942	7	78,568	8	82,328	8	(23.9)	(53.3)	1.8	9.2	4.8	16.5	(33.2)
Corporate	171,321	18	174,920	18	177,866	18	187,461	19	3.1	27.2	2.1	1.7	5.4	9.4	27.6

( ) = negative, LCY = local currency, m-o-m = month-on-month, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Calculated using data from national sources.
2. Bloomberg LP end-of-period LCY–US$ rates are used.
3. Growth rates are calculated from LCY base and do not include currency effects.
4. The total stock of non-tradable bonds as of end-December stood at IDR275.9 trillion.
Source: Bank Indonesia, Indonesia Debt Management Office, Indonesia Stock Exchange, and Bloomberg LP.

Size and Composition

The size of Indonesia's LCY bond market rose to IDR1,090 trillion (US$111 billion) at end-December, expanding a modest 3.3% q-o-q **(Table 1)**. On a y-o-y basis, the LCY bond market saw more rapid growth of 9.7%, with contributions to growth coming from both the government and corporate sectors of the bond market.

At end-December, outstanding LCY government bonds stood at IDR902.6 trillion for a 2.2% q-o-q increase. On a y-o-y basis, government bonds grew 6.6% in 4Q12. Growth in the government bond market was driven mainly by central government bonds, comprised of treasury bills and treasury bonds issued by the Ministry of Finance. The stock of central bank bills has declined significantly on a y-o-y basis since BI initiated measures to reduce issuance in 2010 to curb currency speculation, although central bank bills rose modestly on both q-o-q and m-o-m basis in 4Q12.

Central Government Bonds. The stock of central government bonds grew marginally in 4Q12, rising 0.9% q-o-q to IDR820.3 trillion. On a y-o-y basis, central government bonds rose 13.4%. **Table 2** provides a breakdown of central government bonds outstanding by type of bond.

In 4Q12, new issuance of treasury bills and bonds reached IDR27.1 trillion, falling 33.2% on a q-o-q basis. Issuance of treasury instruments, however, rose 6.1% in 4Q12 compared with a year earlier. Central government bond issuance normally slows down during the fourth quarter each year as the government has either fully realized its annual issuance target or has no additional need for financing. Issuance in 4Q12 consisted of treasury bills, fixed rate bonds, Islamic treasury bills, and project-based *sukuk*.

In 2013, the government plans to sell a total of IDR281.3 trillion (gross) of government bonds. Of which, about IDR57.5 trillion is being planned for issue in 1Q13. As part of its debt strategy for the year, the government will also issue US$-denominated bonds in the domestic market.

Table 2: Central Government Bonds Outstanding by Type of Bond

Government Bonds	Outstanding Amount (IDR billion)	% Share	Growth Rate (%)	
			q-o-q	y-o-y
Treasury Bills (SPN)	22,820	2.8	(19.1)	(23.7)
Fixed-Rate Bonds	576,241	70.3	0.8	21.4
Variable-Rate Bonds	122,755	15.0	(3.4)	(9.1)
Zero-Coupon Bonds	1,263	0.2	(49.7)	(49.7)
Retail Bonds	34,153	4.2	59.0	(19.9)
Islamic Treasury Bills	195	0.02	(78.5)	(85.2)
Sukuk	17,137	2.1	0.0	2.4
Retail *Sukuk*	28,989	3.5	0.0	38.5
Project-Based *Sukuk*	16,714	2.0	11.4	–
Total	**820,267**	**100.0**	**0.9**	**13.4**

– = not applicable, ( ) = negative.
Note: Data as of 31 December 2012.
Source: Indonesia Stock Exchange.

However, the government plans to prioritize LCY issuance by capping issuance in foreign currency (FCY) at a maximum of 14% of the total. The government will continue to issue in varying tenors, ranging from 3 months to 25 years, and conduct buyback and debt switches.

The government has identified FR0066, FR0063, FR0064, and FR0065 as the new benchmark series bonds this year for 5-, 10-, 15-, and 20-year maturities, respectively. Details for the new benchmark bonds series are provided in **Table 3**.

Central Bank Bills. The stock of central bank bills stood at IDR82.3 trillion at end-December, rising 16.5% q-o-q as issuance of *Sertifikat* Bank Indonesia (SBI) and *sharia'h*-compliant SBI rose 29.8% q-o-q. On a y-o-y basis, however, the stock of central bank bills dropped 33.2% in 4Q12. SBI are issued by the central bank as one of its tools for monetary operations to help contain inflation.

Corporate Bonds. The size of Indonesia's LCY corporate bond market reached IDR187.5 trillion in 4Q12, growing 9.4% q-o-q and 27.6% y-o-y. Corporate bonds, however, comprised a small share of Indonesia's LCY bond market, accounting for only 17.2% of the total.

Table 4 provides a breakdown of corporate bonds outstanding by type of bond as of end-December.

Table 3: Indonesian Government Benchmark Bonds for 2013

Bond Series	Outstanding Amount (IDR billion)	Coupon (%)	Maturity Date
1. FR0066	5,050	5.25	15-May-18
2. FR0063	10,550	5.63	15-May-23
3. FR0064	9,976	6.25	15-May-28
4. FR0065	13,850	6.63	15-May-33

Source: Indonesia Debt Management Office.

Conventional corporate bonds dominated the list, accounting for 81.9% of total corporate bonds outstanding. Subordinated bonds accounted for 14.2% of the total, while *sukuk* (Islamic bond) issues by corporate entities remained small, comprising only 3.5% of corporate bonds outstanding at end-December.

At end-December, the amount of LCY bonds outstanding of the top 33 corporate bond issuers in Indonesia reached IDR150.3 trillion, representing 80.2% of total corporate bonds outstanding **(Table 5)**. The composition of the top three LCY corporate bond issuers remained the same as in 3Q12, led by state-power firm PLN with outstanding bonds valued at IDR14.2 trillion. PLN was followed by leasing company Adira Dinamika Multifinance with a total LCY bond stock amounting to IDR9.4 trillion. Telecommunications firm Indosat was the third-largest LCY bond issuer with bonds outstanding of IDR9.2 trillion.

Table 4: Corporate Bonds Outstanding by Type of Bond

Corporate Bonds	Outstanding Amount (IDR billion)	% Share	Growth Rate (%)	
			q-o-q	y-o-y
Conventional Bonds	153,617	81.9	8.3	27.0
Subordinated Bonds	26,611	14.2	17.7	32.2
Convertible Bonds	150	0.1	0.0	–
Zero-Coupon Bonds	500	0.3	0.0	–
Sukuk Ijarah	4,694	2.5	6.9	(6.8)
Sukuk Mudharabah	775	0.4	0.0	(7.6)
Sukuk Mudharabah Subordinated	1,114	0.6	0.0	–
Total	**187,461**	**100.0**	**9.4**	**27.6**

– = not applicable, ( ) = negative.
Notes:
1. Data as of 31 December 2012.
2. *Sukuk Ijarah* refers to Islamic bonds backed by a lease agreement.
3. *Sukuk Mudharabah* refers to Islamic bonds backed by a profit-sharing scheme from a business venture or partnership.
Source: Indonesia Stock Exchange.

Table 5: Top 33 Issuers of LCY Corporate Bonds in Indonesia

Issuers	Outstanding Amount		State-Owned	Privately Owned	Listed Company	Type of Industry
	LCY Bonds (IDR billion)	LCY Bonds (US$ billion)				
1. PLN	14,208	1.45	Yes	No	No	Energy
2. Adira Dinamika Multifinance	9,421	0.96	No	Yes	Yes	Finance
3. Indosat	9,150	0.93	No	Yes	Yes	Telecommunications
4. Indonesia Eximbank	9,134	0.93	Yes	No	No	Banking
5. Astra Sedaya Finance	8,635	0.88	No	Yes	No	Finance
6. Bank Pan Indonesia	8,500	0.87	No	Yes	Yes	Banking
7. Federal International Finance	7,379	0.75	No	Yes	No	Finance
8. Bank Tabungan Negara	7,150	0.73	Yes	No	Yes	Banking
9. Bank Internasional Indonesia	7,000	0.71	No	Yes	Yes	Banking
10. Bank CIMB Niaga	6,480	0.66	No	Yes	Yes	Banking
11. Jasa Marga	5,000	0.51	Yes	No	Yes	Toll Roads, Airports, and Harbors
12. Perum Pegadaian	4,664	0.48	Yes	No	No	Finance
13. Bank Tabungan Pensiunan Nasional	4,550	0.46	No	Yes	Yes	Banking
14. Bank Permata	4,250	0.43	No	Yes	Yes	Banking
15. Indofood Sukses Makmur	3,610	0.37	No	Yes	Yes	Food and Beverages
16. Bank Mandiri	3,500	0.36	Yes	No	Yes	Banking
17. Antam	3,000	0.31	Yes	No	Yes	Petroleum and Natural Gas
18. Telekomunikasi Indonesia	3,000	0.31	Yes	No	Yes	Telecommunications
19. Medco-Energi Internasional	2,987	0.30	No	Yes	Yes	Petroleum and Natural Gas
20. Sarana Multigriya Finansial	2,902	0.30	Yes	No	No	Finance
21. Bank Danamon Indonesia	2,800	0.29	No	Yes	No	Banking
22. BCA Finance	2,530	0.26	No	Yes	No	Finance
23. Agung Podomoro Land	2,400	0.25	No	Yes	Yes	Property and Real Estate
24. Bank Jabar Banten	2,400	0.25	No	Yes	Yes	Banking
25. Indomobil Finance Indonesia	2,225	0.23	No	Yes	No	Finance
26. Bank Rakyat Indonesia	2,000	0.20	Yes	No	Yes	Banking
27. Surya Artha Nusantara Finance	1,995	0.20	No	Yes	No	Finance
28. Toyota Astra Financial Services	1,905	0.19	No	Yes	No	Finance
29. AKR Corporindo	1,500	0.15	No	Yes	Yes	Wholesale Distributor of Petroleum and Basic Chemicals
30. Bank Bukopin	1,500	0.15	No	Yes	Yes	Banking
31. Bank DKI	1,500	0.15	No	Yes	No	Banking
32. Japfa	1,500	0.15	No	Yes	Yes	Animal Feed
33. Surya Semesta Internusa	1,500	0.15	No	Yes	Yes	Property and Real Estate
Total Top 33 LCY Corporate Issuers	**150,273**	**15.34**				
Total LCY Corporate Bonds	**187,461**	**19.14**				
Top 33 as % of Total LCY Corporate Bonds	**80.2%**	**80.2%**				

LCY = local currency.
Notes:
1. Data as of 31 December 2012.
2. State-owned firms are defined as those in which the government has more than a 50% ownership stake.
Source: *AsianBondsOnline* calculations based on Indonesia Stock Exchange data.

Corporate issuers from the banking and financial sectors dominated the list of top LCY corporate bond issuers in Indonesia. Other bond issuers were from the following sectors: energy; telecommunications; toll roads, airports, and harbors; food and beverages; petroleum and natural gas; and property and real estate. About one-third of the companies on the list were state-owned firms while 23 firms were privately-owned. The top 33 list also includes 21 firms with shares listed on the Indonesia Stock Exchange.

In 4Q12, corporate bond issuance climbed to IDR21.8 trillion, a significant hike of 118.7% q-o-q and 36.4% y-o-y. Forty bond series were issued by 20 corporate firms during the quarter, with maturities ranging from 1 year to 7 years. The new corporate bond issues in 4Q12 were all conventional bonds except for two *sukuk* issues and four subordinated bond series. Corporate bonds issued in recent months carried coupons ranging from 6.25% to 9.4%. **Table 6** lists some of the notable corporate bonds issued in 4Q12.

Bank Internasional Indonesia (BII) raised a total of IDR3 trillion through a triple-tranche bond sale in November. The proceeds from the bonds will be used to strengthen BII's capital base and boost its lending business. The bond sale comprised the following issues:

- 3-year bonds worth IDR980 billion, coupon of 7.6%;
- 5-year bonds worth IDR1.02 trillion, coupon of 8.0%; and

Table 6: Notable LCY Corporate Issuance in 4Q12

Corporate Issuers	Issued Amount (IDR billion)
Bank Internasional Indonesia	3,000
Bank Pan Indonesia	3,000
Indonesia Eximbank	2,100
Bank CIMB Niaga	2,000
Bank Permata	1,800
Astra Sedaya Finance	1,530
AKR Corporindo	1,500
Surya Semesta Internusa	1,500
Others	5,350
Total	**21,780**

LCY = local currency.
Source: Indonesia Stock Exchange.

- 7-year subordinated bonds worth IDR1 trillion, coupon of 9.25%.

Bank Pan Indonesia sold a total of IDR3 trillion worth of bonds in a dual-tranche bond sale in December. The proceeds from the bond sale will be used to boost the bank's lending business. The bond issue consisted of the following series:

- 5-year bonds worth IDR1 trillion, coupon of 8.15%; and
- 7-year subordinated bonds worth IDR2 trillion, coupon of 9.40%.

State-owned export financing company Lembaga Pembiayaan Ekspor Indonesia (Indonesia Eximbank) raised a total of IDR2.1 trillion from a dual-tranche bond sale in November. The bonds consisted of the following series:

- 370-day bonds worth IDR1.43 trillion, coupon of 6.25%; and
- 3-year bonds worth IDR666 billion, coupon of 6.50%.

Bank CIMB Niaga sold a total of IDR2 trillion in a dual-tranche bond sale in October. Proceeds from the bond sale will be used by the bank for credit expansion. The bonds were rated IdAAA by Pefindo and AAA(idn) by Fitch Ratings Indonesia. The bond sale comprised the following issues:

- 3-year bonds worth IDR600 billion, coupon of 7.35%; and
- 5-year bonds worth IDR1.4 trillion, coupon of 7.75%.

Bank Permata sold IDR1.8 trillion of 7-year subordinated bonds in December. Proceeds from the bond sale will be used to further boost the bank's capital. The bonds carry a coupon of 9.4%. The subordinated bonds were rated idAA– by Pefindo.

Investor Profile

Central Government Bonds. At end-December, banking institutions were still the biggest holder of central government bonds in Indonesia **(Figure 2)**.

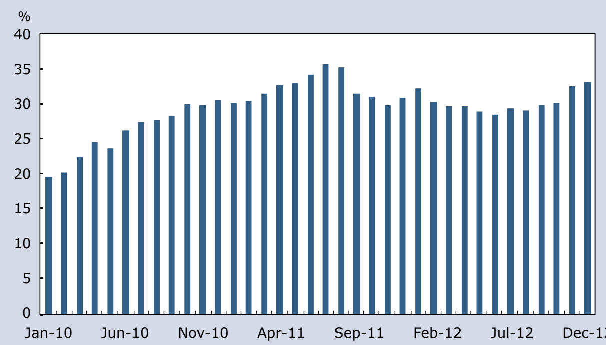
The share of central government bonds held by banking institutions in 4Q12 was almost unchanged at 36.5% from 36.6% in 4Q11. Banking institutions can be broken down into five categories: (i) state recap banks, (ii) private recap banks, (iii) non-recap banks, (iv) regional banks, and (v) *sharia'h* banks. Among these five types of banking institutions, state banks held the largest portion of central government bonds at end-December.

Foreign investors were the second-largest holder of Indonesian LCY central government bonds at end-December. The share of foreign investors in LCY central government bonds steadily increased from a share of 29.5% at end-March to 33.0% at end-December **(Figure 3)**. In absolute terms, outstanding bonds held by foreign investors climbed to IDR270.6 trillion as of end-December.

Foreign investors include among others, non-resident private banks, fund and asset management firms, insurance companies, and pension funds. Offshore financial institutions owned nearly 60% of bonds held by foreign investors at end-December **(Figure 4)**. They were followed by mutual funds with an ownership share of 25.9%. Meanwhile, pension funds accounted for 1.6% of the total and insurance companies held a share of 1.3%.

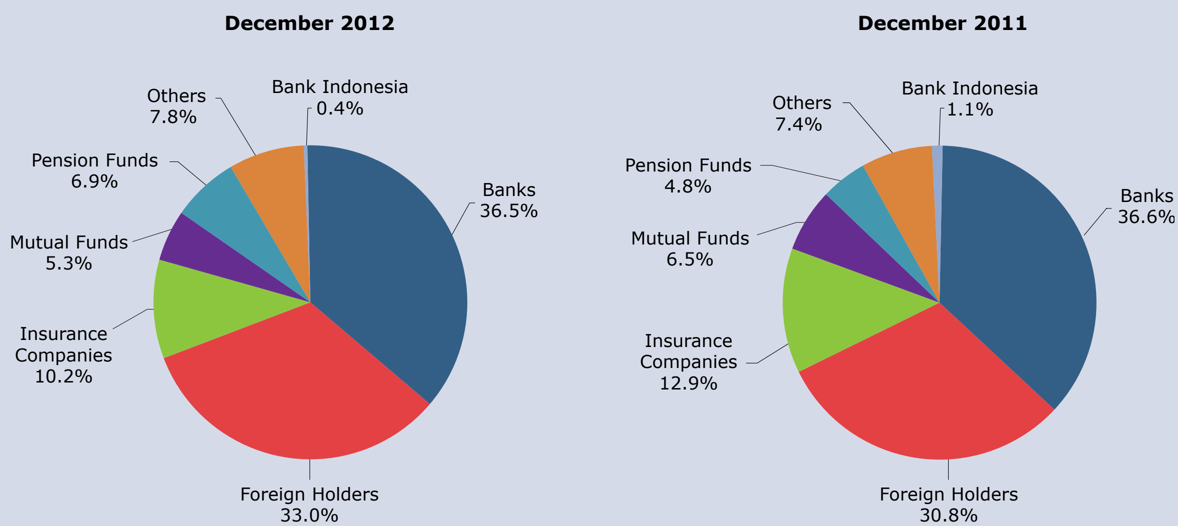
At end-December, the majority of foreign investors in Indonesia's LCY central government bonds were long-term investors. About 45% of bonds held by offshore investors were in maturities of more than 10 years **(Figure 5)** at end-December, compared with 38% at end-December 2011. In addition, foreign investors' holdings of bonds with maturities of more than 5 years and up to 10 years climbed to 28% of foreign investors' total holdings from 25%. Meanwhile, offshore holdings of short-dated tenors (bonds with maturities of less than 1 year) fell to 8% at end-December from 12% at end-December 2011.

Figure 3: Monthly Foreign Investor Share of LCY Central Government Bonds



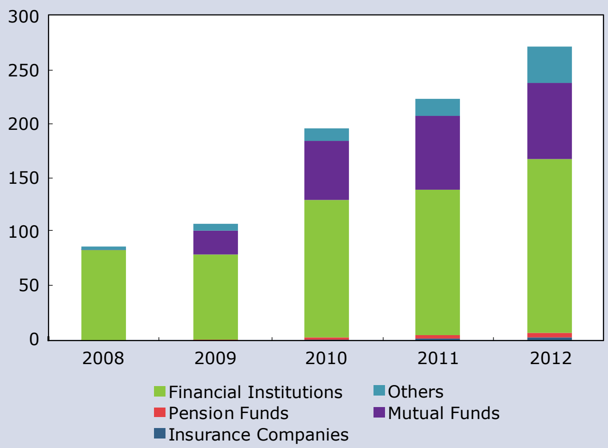
LCY = local currency.
Source: Indonesia Debt Management Office.

Figure 2: LCY Central Government Bonds Investor Profile



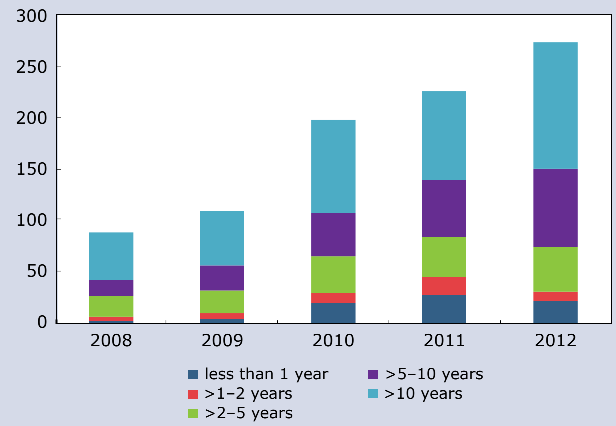
LCY = local currency.
Source: Indonesia Debt Management Office.

Figure 4: Foreign Holdings of LCY Central Government Bonds by Type of Investor



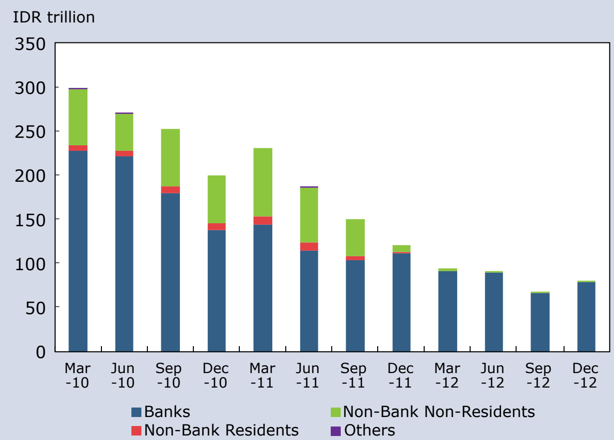
LCY = local currency.
Note: Others include corporations, individuals, security companies, foundations, and other investors not classified.
Source: Indonesia Debt Management Office.

Figure 5: Foreign Holdings of LCY Central Government Bonds by Maturity



LCY = local currency.
Source: Indonesia Debt Management Office.

Figure 6: LCY Central Bank Bills Investor Profile



LCY = local currency.
Source: Bank Indonesia.

Meanwhile, the share of insurance companies' holdings fell to 10.2% of the total in 4Q12 compared with 12.9% a year earlier. Mutual funds' holdings of government bonds remained relatively small compared with other investor classes, accounting for a share of only 5.3% at the end of 4Q12. Meanwhile, the share of bonds held by pension funds rose to 6.9% at end-December from 4.8% a year earlier.

Central Bank Bills. At end-December, central bank bills were held almost entirely by banking institutions with a share of 99.5%, compared with 92.2% at end-December 2011 **(Figure 6)**. In absolute terms, outstanding SBI held by banks stood at IDR78.5 trillion in 4Q12. Meanwhile, offshore investors held the remaining 0.5%, down from a 3.3% share at end-September. The share of SBI held by foreign investors has fallen precipitously since the central bank implemented a 6-month holding period for SBI in 2011.

Rating Changes

On 18 October, Ratings and Investment (R&I) raised Indonesia's sovereign credit rating to BBB– from BB+. The outlook on the rating was stable. R&I cited Indonesia's economic resilience amid the downturn in the global economy, conservative fiscal management, low debt burden, and stable financial system as reasons for the ratings action.

On 13 November, the Japan Credit Rating Agency (JCR) affirmed Indonesia's sovereign credit rating at BBB– with a stable outlook. JCR cited the following factors in its decision to affirm Indonesia's ratings: (i) the country's sustainable economic growth outlook, (ii) a low public debt burden, and (iii) a reinforced resilience to external shocks.

On 21 November, Fitch Ratings (Fitch) affirmed the long-term FCY and LCY issuer default ratings of Indonesia at BBB–. The outlook on the ratings was stable. Fitch also affirmed the country ceiling at BBB and the short-term FCY issuer default rating at F3. According to Fitch, the credit profile of Indonesia is supported by the country's strong and resilient economic growth, low and declining public debt ratios, high investment rate, and a broadly appropriate macroeconomic policy framework. The ratings agency opined that the pressures on Indonesia's external finances and its credit weakness are consistent with its BBB– rating.

Policy, Institutional, and Regulatory Developments

BI Announces New Capital Adequacy Ratios for Banks

In December, BI announced new capital requirements for banks as part of efforts to strengthen the banking system. Beginning in March, banks will be required to maintain a capital adequacy ratio (CAR) of between 8% and 14%, depending on their risk profile. Currently, the CAR for all banks is set at 8%. Based on the new regulation, banks with a low risk profile will continue to maintain a CAR of 8%, banks with a second-level risk profile will be required to maintain a CAR of 9%–10%, and those with a third-level risk profile will be required to maintain a ratio of 10%–11%. High-risk banks (fourth- and fifth-level risk profiles) will be required to maintain a CAR of 11%–14%. BI also set a special requirement, known as a capital equivalency maintained asset (CEMA), for foreign banks operating in Indonesia.

Bond Research Institute Established in Indonesia

In January, the Bond Research Institute (BondRI), a research institution for bonds and fixed income markets, was established in Indonesia. BondRI's mission is to produce research and analysis on bonds and fixed income to improve Indonesia's capital market competitiveness.

OJK Plans to Release Ratings on Corporate Governance

In January, Indonesia's supervisory bond agency, the Financial Services Authority (OJK), announced plans to publish ratings on the quality of corporate governance of Indonesian firms. OJK plans to provide ratings for the 50 largest listed companies this year. Among the criteria to be evaluated are how a company treats minority shareholders and the role played by its board of directors.

Indonesian Government to Hedge FCY Liabilities Against Fluctuations in Interest and Exchange Rates

In January, the Ministry of Finance issued a regulation that would allow the government to hedge its FCY-denominated liabilities, for both bonds and international loans, against fluctuations in interest and exchange rates. The decree, however, did not indicate which specific hedging instruments it will use. The mechanism for conducting hedging transactions is still being formulated by the government. The decree requires the government counterparty for hedging transactions to have at least an A credit rating from two international rating agencies.