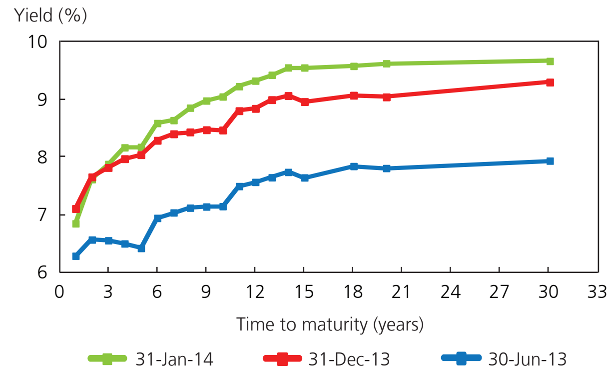
Indonesia

Yield Movements

Between end-June and end-December, local currency (LCY) government bond yields in Indonesia rose dramatically, with the entire curve shifting upward **(Figure 1)**. The steep rise in yields reflected negative sentiments generated by external and domestic factors. Bond yields have been on the rise since May over uncertainty about United States (US) monetary policy. In December, the US Federal Reserve announced that it would begin tapering its asset purchase program by US$10 billion per month—from US$85 billion to US$75 billion—beginning in January 2014. On the domestic front, a slew of negative news weighed on the market, including a rising inflation rate, a widening current account deficit, and a weakening rupiah.

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



LCY = local currency.
Source: Bloomberg LP.

Government bond yields continued to rise between end-December and end-January from the 3-year maturity through the long-end of the curve, while yields at the short-end of the curve (1- and 2-year maturities) fell, resulting in a steepened yield curve. The spread between 2- and 10-year maturities widened to 143 basis points (bps) at end-January from 81 bps at end-December and 58 bps at end-June.

In January, the Federal Reserve announced another US$10 billion cut in its monthly asset purchase program to US$65 billion starting in February. As a result, increasing risk aversion in emerging market assets has pushed yields upward in Indonesia and elsewhere. In addition, inflation expectations remained high as the flooding that affected various areas in Indonesia in January disrupted food supplies and resulted in higher food prices. Consumer price inflation slowed in September but remained elevated in January at 8.2% year-on-year (y-o-y). Indonesia's inflation rate has been the highest in emerging East Asia since July of last year after the government reduced fuel subsidies.

Bank Indonesia initiated macroprudential measures and tightened its monetary policy in the second half of 2013 on the back of a widening current account deficit. Bank Indonesia raised its benchmark rate by a cumulative 175 bps to 7.50% between June and November. In its Board of Governors meeting held on 9 January, Bank Indonesia held steady its benchmark interest rate, and kept the lending facility rate at 7.50% and the deposit facility rate at 5.75%. The central bank noted that at current levels these rates were in line with ongoing efforts to bring down the inflation rate toward its full-year 2014 target range of 3.5%–5.5%, and reduce the current account deficit to a more sustainable level.

Gross domestic product (GDP) growth in Indonesia was below 6.0% y-o-y for the third consecutive quarter in 4Q13, coming in at 5.7%, which was up from 5.6% in 3Q13 but down from a growth rate of 6.2% recorded a year earlier. According to the Ministry of Finance, the government geared its policies toward addressing the current account deficit and sacrificed economic growth in the process. Exports recovered strongly, rising 7.4% y-o-y in 4Q13 due to higher demand from developed economies. Growth in domestic consumption, which slowed to 5.4% in 4Q13, also helped boost economic growth. Investment growth moderated to 4.4% in 4Q13 after rising 4.5% in the previous quarter. On a quarter-on-quarter (q-o-q) basis, the economy contracted 1.4% in 4Q13.

Size and Composition

The outstanding stock of LCY bonds in Indonesia reached IDR1,309.6 trillion (US$108 billion) at end-December, expanding 6.8% q-o-q and 20.1% y-o-y **(Table 1)**.

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

	Outstanding Amount (billion)						Growth Rate (%)			
	4Q12		3Q13		4Q13		4Q12		4Q13	
	IDR	US$	IDR	US$	IDR	US$	q-o-q	y-o-y	q-o-q	y-o-y
Total	**1,090,055**	**111**	**1,226,334**	**108**	**1,309,576**	**108**	**3.3**	**9.7**	**6.8**	**20.1**
Government	902,594	92	1,011,443	89	1,091,356	90	2.2	6.6	7.9	20.9
Central Govt. Bonds	820,266	84	942,859	83	995,252	81.8	0.9	13.4	5.6	21.3
of which: *Sukuk*	63,035	6	87,690	8	87,174	7	1.6	61.7	(0.6)	38.3
Central Bank Bills	82,328	8	68,584	6	96,104	8	16.5	(33.2)	40.1	16.7
of which: *Sukuk*	3,455	0.4	3,610	0.3	4,712	0.4	38.5	(0.6)	30.5	36.4
Corporate	187,461	19	214,891	19	218,220	18	9.4	27.6	1.5	16.4
of which: *Sukuk*	6,883	0.7	6,974	0.6	7,553	0.6	4.6	17.1	8.3	9.7

( ) = negative, LCY = local currency, 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 IDR266.4 trillion.
Sources: Bank Indonesia, Indonesia Debt Management Office, Indonesia Stock Exchange, Otoritas Jasa Keaungan, and Bloomberg LP.

At end-December, outstanding LCY government bonds stood at IDR1,091.4 trillion, up 7.9% q-o-q and 20.9% y-o-y. In recent quarters, growth in the government bond sector was mainly driven by central government bonds, comprising treasury bills and treasury bonds issued by the Ministry of Finance. In 4Q13, central bank bills, which are known as *Sertifikat* Bank Indonesia (SBI), also contributed to growth.

Central Government Bonds. The stock of central government bonds climbed 5.6% q-o-q and 21.3% y-o-y to reach IDR995.3 trillion at end-December. Conventional fixed-rate bonds, which account for the bulk of the central government bond stock, continued to drive growth **(Table 2)**. Retail bonds also grew significantly with the issuance in October of the government's 10th series of retail bonds known as ORI010. Project-based *sukuk*, which are backed by government infrastructure projects, also helped boost growth in the government sector during the quarter. On the other hand, short-term instruments—treasury bills and Islamic treasury bills—registered negative growth in 4Q13.

Total treasury bills and bond issuance in 4Q13 reached IDR69.8 trillion, down slightly from 3Q13. The government conducted five auctions of conventional bonds, three auctions of Islamic bonds, and a retail bond offering. As in the past, auctions of conventional bonds were fully awarded while auctions for Islamic bonds did not meet their targets.

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	34,050	3.4	(1.6)	49.2
Fixed-Rate Bonds	707,391	71.1	4.9	22.8
Variable-Rate Bonds	122,755	12.3	0.0	0.0
Retail Bonds	43,882	4.4	85.3	28.5
Islamic Treasury Bills	8,633	0.9	(9.9)	4,327.2
Sukuk	16,587	1.7	(3.2)	(3.2)
Retail *Sukuk*	35,924	3.6	0.0	23.9
Project-Based *Sukuk*	26,030	2.6	3.9	55.7
Total	**995,252**	**100.0**	**5.6**	**21.3**

( ) = negative, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Note: Data as of end-December 2013.
Source: Indonesia Stock Exchange.

Central Bank Bills. The stock of central bank bills (SBI) reached IDR96.1 trillion, posting double-digit growth on both a q-o-q and y-o-y basis. In 3Q13, new issuance of SBI and *shari'ah*-compliant SBI rose 4.1% q-o-q, but contracted 46.2% y-o-y. Bank Indonesia issues SBI as one of its monetary tools to contain inflation.

Corporate Bonds. The size of Indonesia's LCY corporate bond market reached IDR218.2 trillion, posting 1.5% q-o-q and 16.4% y-o-y expansions. Growth came mainly from an increase in outstanding conventional corporate bonds, subordinated bonds, and *Sukuk Ijarah*. **Table 3** presents the

Table 3: Corporate Bonds Outstanding by Type of Bond

Corporate Bonds	Outstanding Amount (IDR billion)	% Share	Growth Rate (%)	
			q-o-q	y-o-y
Bonds	184,771	84.7	1.1	20.3
Subordinated Bonds	25,746	11.8	3.5	(3.3)
Convertible Bonds	150	0.1	0.0	0.0
Sukuk Ijarah	4,974	2.3	21.5	6.0
Sukuk Mudharabah	1,079	0.5	0.0	39.2
Sukuk Mudharabah Subordinate	1,500	0.7	0.0	34.6
Total	**218,220**	**100.0**	**1.5**	**16.4**

– = not applicable, q-o-q = quarter-on-quarter, y-o-y = year-on-year.
Notes:
1. Data as of end-December 2013.
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.

breakdown of outstanding corporate bonds by type at end-December. The stock of corporate bonds is dominated by conventional corporate bonds, which account for 84.7% of total corporate bonds. *Sukuk* (Islamic bonds) accounted for less than 4.0% of the total.

In 4Q13, the aggregate amount of bonds issued by the top 30 LCY corporate bond issuers in Indonesia reached IDR168.4 trillion **(Table 4)**. This represented 77.2% of total corporate bonds outstanding at end-December. The top 30 issuers were largely dominated by financial and banking institutions, which accounted for two-thirds of the firms. The top 30 list was led by state-power firm PLN with outstanding LCY corporate bonds of IDR16.9 trillion, followed by financing firms Astra Sedaya Finance (IDR11.9 trillion) and Adira Dinamika Multi Finance (IDR11.4 trillion).

New issuance of corporate bonds reached IDR11.2 trillion in 4Q13. A total of 10 firms issued 26 series of corporate bonds during the quarter, led mostly by firms from the banking and non-bank financial sectors. All bonds were conventional except for three issues of *Sukuk Ijarah* and one subordinated bond issue. The maturity structure of these new issues was mostly concentrated between 3 and 5 years. In addition, there was one issue carrying a 7-year maturity and two issues of a 10-year tenor. **Table 5** shows some notable corporate bonds issued in 4Q13.

Foreign Currency Bonds. In November, the government conducted its first sale of US$-denominated bonds targeted for the domestic market. The government raised US$190 million from the sale of 3.5-year bonds that carry a coupon of 3.5% and were priced to yield 3.51671%. The bond sale fell short of the government's target of US$450 million as investors sought higher yields. A total of US$293.6 million in bids was received.

In January, the Indonesian government tapped the international market and raised US$4 billion from a two-tranche bond sale. The government sold US$2 billion of 10-year bonds to yield 5.95% with a coupon of 5.875%, and US$2 billion of 30-year bonds to yield 6.85% with a coupon of 6.75%. The bonds were oversubscribed with the order book reaching US$17.5 billion. The bulk of the 10-year tranche was sold to investors from the US (66%), while the remainder was sold to investors from Europe (17%), Indonesia (11%), and Asia (6%). The 30-year bonds were also mostly sold to investors from the US (70%), with the remainder was distributed among investors from Europe (16%), Asia (11%), and Indonesia (3%). The bonds were rated BBB– by Fitch Ratings and BB+ by Standard & Poor's.

Investor Profile

Central Government Bonds. Banking institutions were the largest holder of LCY government bonds in Indonesia at end-December 2013, accounting for a 33.7% share of the total **(Figure 2)**. However, this was down from a 36.5% share a year ago. Banking institutions comprise state recap banks, private recap banks, non-recap banks, regional banks, and *shari'ah* banks.

The second largest investor group was foreign investors, whose share slightly dropped to 32.5% in 4Q13 from 33.0% a year earlier. Their share, however, has gradually recovered after hitting a low of 30.6% at end-August, but is still lower compared with levels prior to May **(Figure 3)**. In nominal terms, outstanding bonds held by foreign investors stood at IDR323.8 trillion at end-December.

At-end December, foreign investor holdings of government bonds were largely concentrated in longer-dated tenors. About 44% of government bonds

Table 4: Top 30 Issuers of LCY Corporate Bonds in Indonesia

Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
	LCY Bonds (IDR billion)	LCY Bonds (US$ billion)			
1. PLN	16,881	1.39	Yes	No	Energy
2. Astra Sedaya Finance	11,852	0.97	No	No	Finance
3. Adira Dinamika Multi Finance	11,384	0.94	No	Yes	Finance
4. Indonesia Eximbank	11,135	0.91	Yes	No	Banking
5. Bank Tabungan Negara	8,850	0.73	Yes	Yes	Banking
6. Bank CIMB Niaga	7,930	0.65	No	Yes	Banking
7. Federal International Finance	7,901	0.65	No	No	Finance
8. Indosat	7,820	0.64	No	Yes	Telecommunications
9. Bank Internasional Indonesia	7,000	0.58	No	Yes	Banking
10. Bank Pan Indonesia	7,000	0.58	No	Yes	Banking
11. Bank Permata	6,478	0.53	No	Yes	Banking
12. Perum Pegadaian	5,739	0.47	Yes	No	Finance
13. Jasa Marga	5,600	0.46	Yes	Yes	Toll Roads, Airports, and Harbors
14. Bank Tabungan Pensiunan Nasional	4,985	0.41	No	Yes	Banking
15. Medco-Energi International	4,487	0.39	No	Yes	Petroleum and Natural Gas
16. Bank OCBC NISP	3,880	0.32	No	Yes	Banking
17. Sarana Multigriya Finansial	3,629	0.30	Yes	No	Finance
18. Indofood Sukses Makmur	3,610	0.30	No	Yes	Food and Beverages
19. Agung Podomoro Land	3,600	0.32	No	Yes	Property, Real Estate, and Building Construction
20. Bank Mandiri	3,500	0.29	Yes	Yes	Banking
21. Antam	3,000	0.25	Yes	Yes	Petroleum and Natural Gas
22. Telekomunikasi Indonesia	3,000	0.25	Yes	Yes	Telecommunications
23. BCA Finance	2,850	0.23	No	No	Finance
24. Bumi Serpong Damai	2,750	0.23	No	Yes	Petroleum and Natural Gas
25. Indomobil Finance Indonesia	2,728	0.22	No	No	Finance
26. Toyota Astra Financial Services	2,595	0.21	No	No	Finance
27. Bank Jabar Banten	2,400	0.20	No	Yes	Banking
28. Bank Rakyat Indonesia	2,000	0.16	Yes	Yes	Banking
29. Garuda Indonesia	2,000	0.16	Yes	Yes	Infrastructure, Utilities, and Transportation
30. Surya Artha Nusantara Finance	1,841	0.20	No	No	Finance
Total Top 30 LCY Corporate Issuers	**168,423**	**13.94**			
Total LCY Corporate Bonds	**218,220**	**17.93**			
Top 30 as % of Total LCY Corporate Bonds	**77.2%**	**77.7%**			

LCY = local currency.
Notes:
1. Data as of end-December 2013.
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.

held by non-residents carried maturities of more than 10 years **(Figure 4)**. Their share of holdings in medium-dated tenors or those with maturities of more than 5–10 years also climbed to 32% at end-2013 from 28% at end-2012. Meanwhile, foreign holdings of short-term securities (less than 1 year) declined to 5.0% at end-2013 from 8.0% a year earlier.

The share of other domestic investors in central government bond holdings, except for mutual funds and pension funds, increased in 2013. Insurance companies' holdings of government bonds rose to a share of 13.0% from 10.2% in the previous year. Bank Indonesia also registered a significant increase in its holdings of central government bonds to a share of 4.5% at end-December

Table 5: Notable LCY Corporate Bond Issuance in 4Q13

Corporate Issuers	Coupon Rate (%)	Issued Amount (IDR billion)
Bank Permata		
370-day bond	10.00	696
3-year bond	10.50	672
7-year bond	12.00	860
Adira Dinamika Multi Finance		
370-day bond	9.15	722
3-year bond	10.50	880
5-year bond	11.00	490
Astra Sedaya Finance		
370-day bond	8.75	545
3-year bond	9.50	870
4-year bond	9.75	385
PLN		
5-year bond	9.00	593
5-year *Sukuk Ijarah*	9.00	321
10-year bond	9.60	651
10-year *Sukuk Ijarah*	9.60	108
Bank CIMB Niaga		
2-year bond	8.75	285
3-year bond	9.15	315
5-year bond	9.75	850

LCY = local currency.
Note: *Sukuk Ijarah* refers to Islamic bonds backed by a lease agreement.
Source: Indonesia Stock Exchange.

from 0.4% a year earlier. Mutual fund and pension fund holdings of central government bonds both declined on a y-o-y basis.

Central Bank Bills. At end-December, banking institutions were the largest holders of central bank bills (SBI) with holdings equivalent to a share of 95.9% of the total **(Figure 5)**. The nominal amount of SBI held by banks totaled IDR87.7 trillion at end-December, up sharply from IDR60.9 trillion in the previous quarter. Foreign non-bank investors held the remaining 4.1% of outstanding SBI. Foreign investor interest in SBI remained low despite Bank Indonesia's decision in August to reduce the minimum holding period from 6 months to 1 month.

Rating Changes

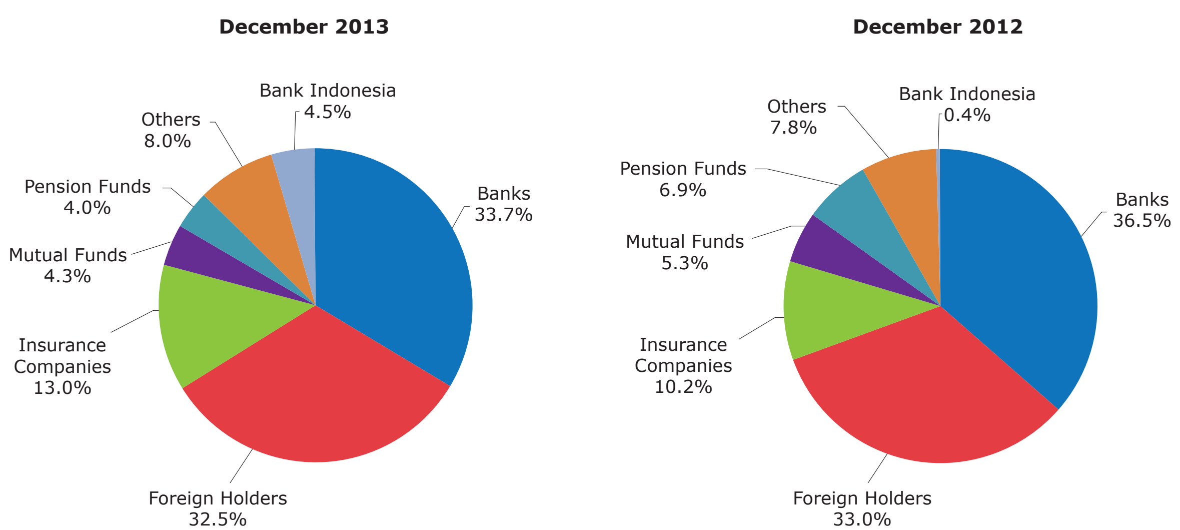
On 15 November, Fitch Ratings (Fitch) affirmed Indonesia's sovereign credit rating at BBB– with a stable outlook. In making its decision, Fitch took note of Indonesia's policy measures in response to market pressures, its relatively high long-term growth prospects, its low public debt and prudent fiscal management, and its well-capitalized banking system.

Policy, Institutional, and Regulatory Developments

Bank Indonesia and Bank of Japan Sign Third BSA Establish Cross-Border Liquidity Arrangement

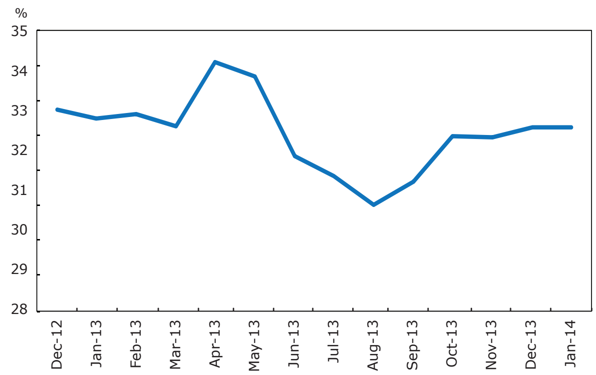
On 12 December, Bank of Japan, acting as the agent for the Ministry of Finance, and Bank Indonesia signed a third Bilateral Swap Arrangement (BSA). Under

Figure 2: LCY Central Government Bonds Investor Profile



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

Figure 3: Foreign Investor Share of LCY Central Government Bonds



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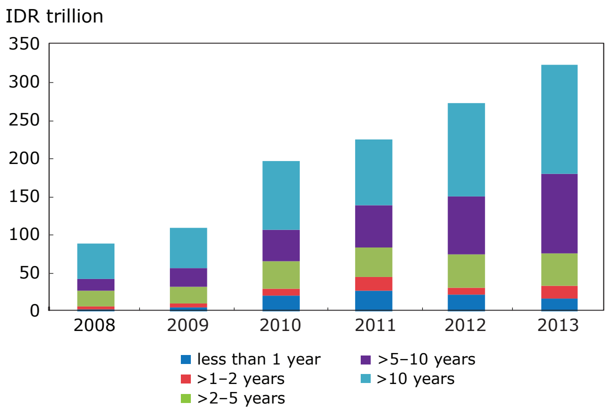
Source: Indonesia Debt Management Office.

Figure 4: Foreign Holdings of LCY Central Government Bonds by Maturity

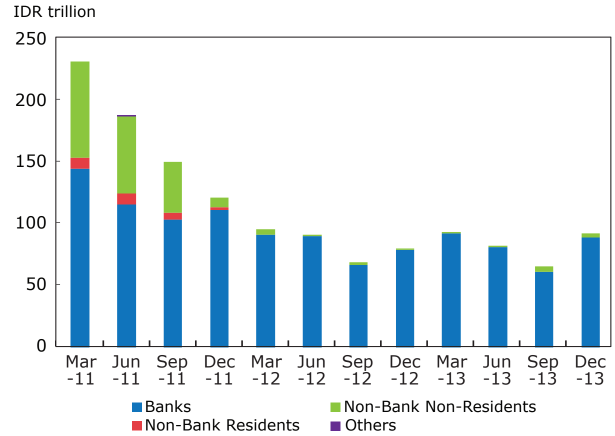


LCY = local currency.
Source: Indonesia Debt Management Office.

this new arrangement, the size of the facility was increased to US$22.76 billion from US$12.0 billion. The BSA introduced a new feature in the form of a crisis prevention scheme to support potential and actual liquidity requirements.

Also in December, a cross-border liquidity arrangement was established between Bank of Japan and Bank Indonesia to ensure stability in the Indonesian financial market. With the arrangement, eligible banks with operations in Indonesia may obtain IDR liquidity from Bank Indonesia by providing Japanese government securities.

Figure 5: LCY Central Bank Bills Investor Profile



LCY = local currency.
Source: Bank Indonesia.

Bank Indonesia Signs MRA with Domestic Banks

On 18 December, a mini Master Repo Agreement (MRA) was signed between Bank Indonesia and eight Indonesian banks. The mini MRA will serve as a standard contract for interbank repo transactions. The eight banks include Bank Mandiri, Bank Rakyat Indonesia, Bank Negara Indonesia, Bank Central Asia, Bank Panin, Bank Bukopin, Bank DKI, and Bank Jabar Banten. This move is expected to promote and deepen the repo market as most transactions were previously undertaken through bilateral agreements due to the absence of a standardized global MRA in Indonesia.

Bank Indonesia Issues New Regulations for Hedge Swap Transactions

As part of efforts to deepen Indonesia's domestic foreign exchange market, Bank Indonesia announced new regulations to expand currency swap facilities for hedging transactions. The new regulations, which took effect on 3 February, aim to minimize exchange rate risks and increase investment activities in Indonesia. Under the new regulations, a hedging contract may be entered into by a bank within a period of up to 3 years through hedge swap transactions with Bank Indonesia at maturities of 3, 6, and 12 months. Other regulatory improvements were also announced, including the expansion of underlying transaction coverage, the extension of transaction tenors, and settlement by netting.