

## Indonesia

### Yield Movements

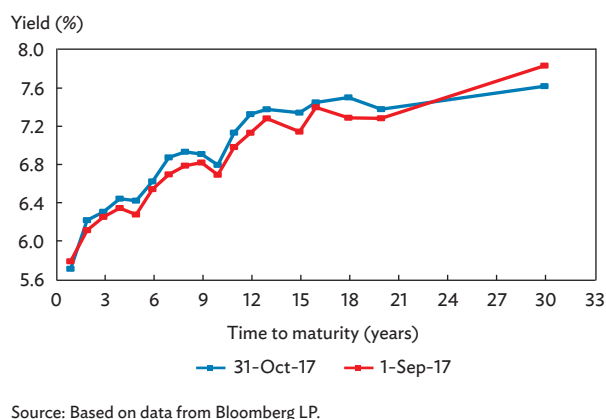
Between 1 September and 31 October, all local currency (LCY) government bond yields climbed in Indonesia except for the 1-year and 30-year maturities (**Figure 1**). Bond yields rose an average of 12 basis points (bps) from the 2-year through the 20-year tenors, while shedding 8 bps and 21 bps, respectively, at the short-end and long-end of the curve. The spread between the 2-year and 10-year tenors slipped from 58 bps on 1 September to 57 bps on 31 October.

The overall rise in yields was due largely to a sell-off as investor sentiment turned negative. In September, the United States (US) Federal Reserve signaled further tightening and the beginning of its balance sheet normalization in October. In addition, the European Central Bank also announced that it will taper its asset purchases beginning in January 2018.

Compared to its regional peers, a relatively large share of Indonesia's bonds are held by foreign investors, making its bond market sensitive to capital flight risks. At the end of September, the share of foreign investors hit 40.0%, up from the end-June level of 39.5%. This share had reached a high of 40.5% earlier in September after Bank Indonesia's policy rate cut. However, as monetary policy direction in most advanced economies became hawkish, investors turned cautious and took profits. At the end of October, nonresident holdings of Indonesian government bonds had fallen to 38.4% of the total. The Ministry of Finance, however, stated that this decline was just a temporary market reaction. Meanwhile, onshore demand continues to support the market.

Bank Indonesia lowered its policy rate by 25 bps each in August and again in September. Low inflation provided the central bank room for easing monetary policy to boost growth. In its meeting on 18–19 October, the central bank took a pause and maintained the 7-day reverse repurchase rate at 4.25%. The deposit facility rate and the lending facility rate were also maintained at 3.50% and 5.00%, respectively. The central bank deems that current rates are consistent with holding inflation within its target range and keeping the current account deficit at a manageable level. Consumer price inflation trended lower in July–October and has remained within

**Figure 1: Indonesia's Benchmark Yield Curve—  
Local Currency Government Bonds**



Bank Indonesia's full-year 2017 target range of between 3.0% and 5.0%.

Real gross domestic product (GDP) growth inched up to 5.06% year-on-year (y-o-y) in the third quarter (Q3) of 2017 compared with 5.01% from the prior quarter, falling below Bank Indonesia and analysts' expectations. Growth in household consumption continued to weaken, rising 4.93% y-o-y in Q3 2017 versus 4.95% in the previous quarter. Government spending rebounded, posting growth of 3.5% after contracting in the previous 2 quarters. Also, contributing to the overall y-o-y growth in Q3 2017 were investments (7.1%) and exports (17.3%). Based on the revised state budget for 2017, full-year economic growth is estimated at 5.2%.

### Size and Composition

The LCY bond market in Indonesia continued to expand to reach a size of IDR2,426.1 trillion (USD180 billion) at the end of September. Growth was up 4.1% quarter-on-quarter (q-o-q) in Q3 2017 from 1.8% in the second quarter (Q2) of 2017 (**Table 1**). On a y-o-y basis, growth moderated to 12.7% from 16.4% in the same review period. Both the government and corporate bond segments contributed to overall growth during the quarter.

At the end of September, government bonds accounted for 85.2% of Indonesia's total LCY bond stock. The

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q3 2016		Q2 2017		Q3 2017		Q3 2016		Q3 2017	
	IDR	USD	IDR	USD	IDR	USD	q-o-q	y-o-y	q-o-q	y-o-y
<b>Total</b>	2,153,035	165	2,331,240	175	2,426,060	180	7.5	27.2	4.1	12.7
<b>Government</b>	1,866,325	143	1,998,689	150	2,066,296	153	7.7	29.4	3.4	10.7
Central Govt. Bonds	1,749,384	134	1,952,234	146	2,046,933	152	6.2	25.6	4.9	17.0
of which: <i>Sukuk</i>	239,868	18	297,424	22	329,039	24	9.6	59.5	10.6	37.2
Central Bank Bills	116,941	9	46,455	3	19,363	1	35.8	132.3	(58.3)	(83.4)
of which: <i>Sukuk</i>	9,442	0.7	9,421	0.7	12,626	0.9	26.4	22.3	34.0	33.7
<b>Corporate</b>	286,710	22	332,550	25	359,763	27	6.2	14.9	8.2	25.5
of which: <i>Sukuk</i>	10,744	0.8	13,385	1	13,958	1	12.4	29.7	4.3	29.9

( ) = negative, IDR = Indonesian rupiah, LCY = local currency, q-o-q = quarter-on-quarter, Q2 = second quarter, Q3 = third quarter, USD = United States dollar, y-o-y = year-on-year.

Notes:

1. Calculated using data from national sources.

2. Bloomberg LP end-of-period LCY-USD rates are used.

3. Growth rates are calculated from an LCY base and do not include currency effects.

4. The total stock of nontradable bonds as of end-September stood at IDR233.4 trillion.

Sources: Bank Indonesia; Directorate General of Budget Financing and Risk Management, Ministry of Finance; Indonesia Stock Exchange; and Bloomberg LP.

remaining share of 14.8% was accounted for by corporate bonds. In the same period, conventional bonds dominated the LCY bond market with a share of 85.3% of the total. Nonetheless, the share of *sukuk* (Islamic bonds) has been slowly but steadily rising. *Sukuk* accounted for 14.7% of the aggregate bond stock at the end of September, up from 13.7% at the end of June and 12.1% at the end of September 2016.

**Government bonds.** The outstanding amount of LCY government bonds rose 3.4% q-o-q in Q3 2017 and 10.7% y-o-y at the end of September. Growth was solely driven by central government bonds, which comprise Treasury bills and bonds issued by the Ministry of Finance. The outstanding size of central bank bills, or Sertifikat Bank Indonesia (SBI), which are issued by Bank Indonesia, continued to fall during the review period.

**Central government bonds.** At the end of September, central government bonds outstanding reached IDR2,046.9 trillion on growth of 4.9% q-o-q and 17.0% y-o-y. Increased demand for bonds allowed the government to accept more than its targeted amount in 11 out of 13 auctions during the quarter. Only one auction was partially awarded in Q3 2017. New issuance of Treasury instruments in Q3 2017 reached IDR153.2 trillion on growth of 32.3% q-o-q and 28.9% y-o-y.

**Central bank bills.** The outstanding amount of central bank bills contracted to IDR19.4 trillion at the end of September on declines of 58.3% q-o-q and 83.4% y-o-y.

The decline in the stock of central bank bills was due to Bank Indonesia's cessation of issuance of conventional SBI at the beginning of 2017. Bank Indonesia, however, continues to issue shariah-compliant SBI, the issuance volume of which is relatively small compared with previous issuance of conventional SBI.

New issuance of shariah-compliant SBI climbed from a low base of IDR1.1 trillion in Q2 2017 to IDR6.8 trillion in Q3 2017. While issuance was higher during the quarter, the size of central bank certificates declined, as maturities exceeded new issuance.

**Corporate bonds.** At the end of September, LCY corporate bonds outstanding rose to IDR359.8 trillion on higher growth of 8.2% q-o-q and 25.5% y-o-y in Q3 2017 compared with 3.6% q-o-q and 23.1% y-o-y in the previous quarter. The q-o-q expansion in corporate bonds was due to more active issuance during the quarter.

Corporate bonds in Indonesia lagged in terms of growth vis-à-vis the government segment, which is consistent with the findings of our annual bond market liquidity survey as bond market participants cited some of the factors deterring growth. Among these are the lengthy issuance process for issuing bonds, absence of market makers, and need for greater diversity in the investor base.

At the end of September, 111 corporate firms were tapping the bond market for their funding requirements. Of which, the top 30 largest issuers had outstanding bonds

Table 2: Top 30 Issuers of Local Currency Corporate Bonds in Indonesia

	Issuers	Outstanding Amount		State-Owned	Listed Company	Type of Industry
		LCY Bonds (IDR billion)	LCY Bonds (USD billion)			
1.	Indonesia Eximbank	33,538	2.49	Yes	No	Banking
2.	Bank Rakyat Indonesia	24,175	1.79	Yes	Yes	Banking
3.	Bank Tabungan Negara	17,950	1.33	Yes	Yes	Banking
4.	Indosat	14,113	1.05	No	Yes	Telecommunications
5.	Bank Pan Indonesia	12,085	0.90	No	Yes	Banking
6.	Bank Mandiri	11,000	0.82	Yes	Yes	Banking
7.	PLN	10,883	0.81	Yes	No	Energy
8.	Federal International Finance	10,780	0.80	No	No	Finance
9.	Adira Dinamika Multifinance	9,833	0.73	No	Yes	Finance
10.	Telekomunikasi Indonesia	8,995	0.67	Yes	Yes	Telecommunications
11.	Astra Sedaya Finance	8,215	0.61	No	No	Finance
12.	Bank Maybank Indonesia	8,121	0.60	No	Yes	Banking
13.	Hutama Karya	7,115	0.53	Yes	No	Non-Building Construction
14.	Medco-Energi International	7,000	0.52	No	Yes	Petroleum and Natural Gas
15.	Bank CIMB Niaga	6,850	0.51	No	Yes	Banking
16.	Sarana Multigriya Finansial	6,714	0.50	Yes	No	Finance
17.	Waskita Karya	6,557	0.49	Yes	Yes	Building Construction
18.	Sarana Multi Infrastruktur	5,900	0.44	Yes	No	Finance
19.	Bank Permata	5,810	0.43	No	Yes	Banking
20.	Perum Pegadaian	5,140	0.38	Yes	No	Finance
21.	Permodalan Nasional Madani	4,933	0.37	Yes	No	Finance
22.	Toyota Astra Financial Services	4,864	0.36	No	No	Finance
23.	Pupuk Indonesia	4,701	0.35	Yes	No	Chemical Manufacturing
24.	Bank OCBC NISP	4,400	0.33	No	Yes	Banking
25.	Indofood Sukses Makmur	4,000	0.30	No	Yes	Food and Beverages
26.	Adhi Karya	3,997	0.30	Yes	Yes	Building Construction
27.	Surya Artha Nusantara Finance	3,862	0.29	No	No	Finance
28.	Mandiri Tunas Finance	3,675	0.27	No	No	Finance
29.	BFI Finance Indonesia	3,350	0.25	No	Yes	Finance
30.	Bank Bukopin	3,305	0.25	No	Yes	Banking
<b>Total Top 30 LCY Corporate Issuers</b>		<b>261,861</b>	<b>19.44</b>			
<b>Total LCY Corporate Bonds</b>		<b>359,763</b>	<b>26.70</b>			
<b>Top 30 as % of Total LCY Corporate Bonds</b>		<b>72.8%</b>	<b>72.8%</b>			

IDR = Indonesian rupiah, LCY = local currency, USD = United States dollar.

Notes:

1. Data as of end-September 2017.

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.

of IDR261.9 trillion, representing 72.8% of the aggregate corporate bond stock (**Table 2**). The top 30 list is dominated by banking and financial institutions. The list also includes 14 state-owned corporations, though state-owned firms Pupuk Indonesia and Adhi Karya were not among the top 30 corporate issuers at the end of June.

The top three firms on the list were state-owned banks. Maintaining its top spot was state-owned lender Indonesia Eximbank with outstanding bonds amounting to IDR33.5 trillion at the end of September. Next was another state-owned lender, Bank Rakyat Indonesia, whose total bonds increased to IDR24.2 trillion after it issued an aggregate of IDR5.2 trillion in new bonds in August. Climbing to the third spot at the end of September (from the fourth spot at the end of June) was Bank Tabungan Negara, which issued IDR5.0 trillion of new bonds in July.

In Q3 2017, corporate bond issuance reached IDR46.9 trillion, up 36.4% q-o-q and 71.7% y-o-y. A total of 27 firms tapped the bond market in Q3 2017 versus 18 issuers in Q2 2017. There were 71 new corporate bond series issued during the quarter, with issuance coming mostly from bank and financial institutions.

**Table 3** presents the largest corporate bond issuances in Q3 2017. Leading the list were two state-owned banks, Bank Rakyat Indonesia and Bank Tabungan Negara, with aggregate bond issuance amounting to IDR5.2 trillion and IDR5.0 trillion, respectively. Third on the list was state-owned chemical manufacturing company, Pupuk Indonesia, whose dual-tranche issuance amounting to IDR3.6 trillion placed it among the top 30 corporate issuers at the end of September.

## Investor Profiles

Offshore investors continued to comprise the largest investor group in Indonesia's LCY government bond market. The foreign holdings share climbed to 40.0% at the end of September from 39.5% at the end of June and from 39.2% in the same period a year earlier (**Figure 2**). In nominal terms, foreign investor holdings of LCY government bonds climbed to IDR819.4 trillion from IDR770.6 trillion at the end of June and from IDR685 trillion at the end of September 2016. While bond yields have declined since the start of the year, nonresident investors are still attracted to Indonesia's

**Table 3: Notable Local Currency Corporate Bond Issuance in the Third Quarter of 2017**

Corporate Issuers	Coupon Rate (%)	Issued Amount (IDR billion)
Bank Rakyat Indonesia		
3-year bond	7.50	981
5-year bond	8.00	1,653
7-year bond	8.25	2,517
Bank Tabungan Negara		
3-year bond	8.30	1,466
5-year bond	8.50	1,295
7-year bond	8.70	853
10-year bond	8.90	1,386
Pupuk Indonesia		
3-year bond	7.90	1,485
7-year bond	8.60	2,085
Hutama Karya		
5-year bond	7.80	1,165
10-year bond	8.40	2,367
Indonesia Eximbank		
3-year bond	7.80	1,000
5-year bond	7.90	436
7-year bond	8.25	1,786
Bank Negara Indonesia		
5-year bond	8.00	3,000
Adhi Karya		
5-year bond	9.25	2,997

IDR = Indonesian rupiah.  
Source: Indonesia Stock Exchange.

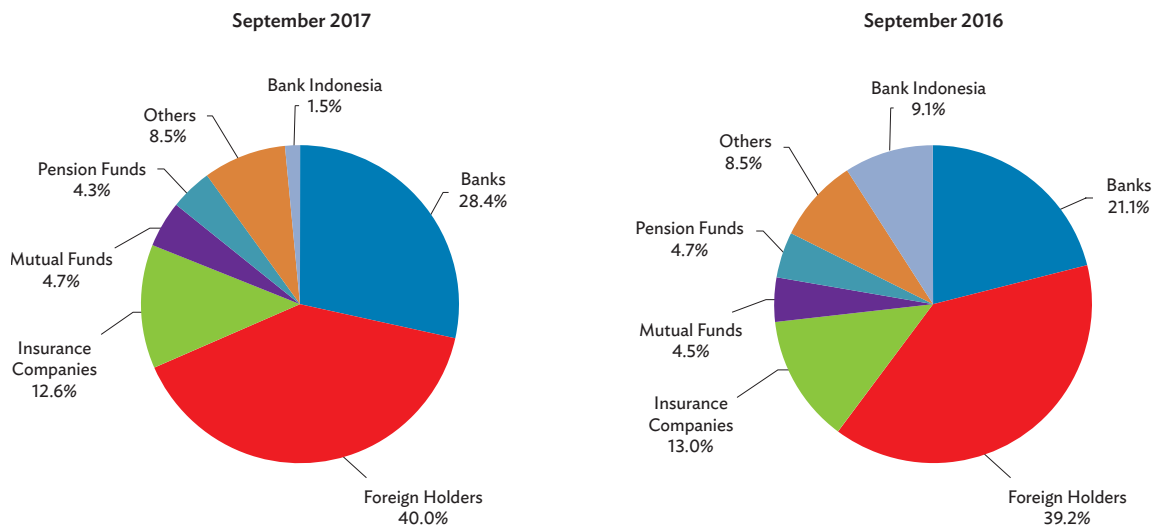
LCY government bonds as they offer the highest yields in the region.

In terms of maturity, foreign investors are mostly invested in longer-dated bonds (maturities of 10 years or more), which represent 36.0% of aggregate bond holdings, while 35.3% of offshore holdings are in bonds with maturities of 5 years to 10 years (**Figure 3**). At the end of September, bonds with maturities of 1 year or less comprised 6.1% of the total holdings of foreign investors.

Among domestic investors, banking institutions were the largest holder of government bonds. At the end of September, their holdings had risen significantly to a 28.4% share from 21.1% a year earlier. Banks have been increasing their holdings of government bonds as they seek alternative higher-yielding investments in which to park their excess funds.

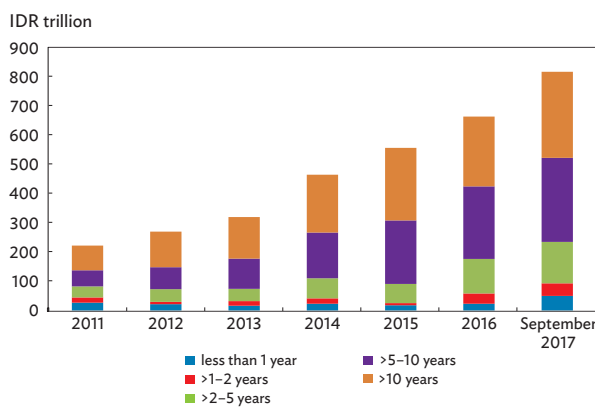
The only other domestic investor group that saw an increase in its holdings was mutual funds, whose share of

**Figure 2: Local Currency Central Government Bonds Investor Profile**



Source: Directorate General of Budget Financing and Risk Management, Ministry of Finance.

**Figure 3: Foreign Holdings of Local Currency Central Government Bonds by Maturity**



IDR = Indonesian rupiah.

Source: Directorate General of Budget Financing and Risk Management, Ministry of Finance.

the total inched up to 4.7% at the end of September from 4.5% in the same period a year earlier. All other investor groups recorded marginal declines in their respective holdings of government bonds except for Bank Indonesia, whose holdings slipped to a share of 1.5% at the end of September from 9.1% in September 2016.

## Policy, Institutional, and Regulatory Developments

### Bank Indonesia Allows Euro Swaps

In October, Bank Indonesia allowed hedging transactions involving the euro. The minimum transaction size for euro swaps is EUR1 million with terms of 3 months and 6 months. Earlier in July, the central bank allowed hedging transactions for Japanese yen swaps. These measures are expected to reduce dependence on the US dollar for trade and investment activities.

### Indonesia's 2018 State Budget Bill Approved

In October, the House of Representatives approved the government's proposed 2018 state budget, which estimates revenue amounting to IDR1,894.7 trillion and expenditure of IDR2,220 trillion. The budget deficit is projected to reach an equivalent of 2.2% of GDP. The underlying macroeconomic assumptions for the 2018 state budget include (i) annual GDP growth of 5.4%, (ii) annual inflation of 3.5%, (iii) an exchange rate of IDR13,400 per USD1, (iv) a 3-month Treasury bill annual rate of 5.3%, and (v) an Indonesian crude oil price of USD48 per barrel.