

Indonesia

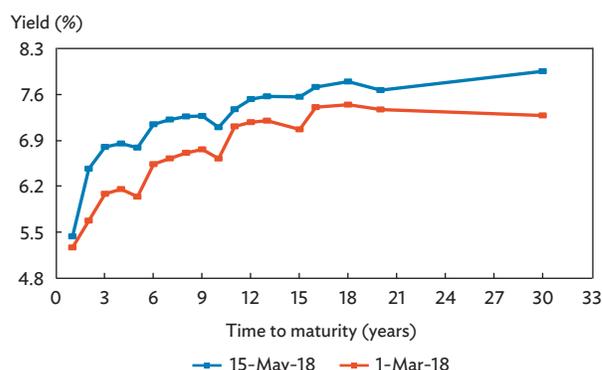
Yield Movements

Local currency (LCY) government bond yields in Indonesia rose for all tenors between 1 March and 15 May, leading the entire yield curve to shift upward (**Figure 1**). Bond yields gained the most at the short-end through the 9-year maturity, rising by an average of 65 basis points (bps), except for the 1-year tenor, which rose 17 bps. Yields for bonds with maturities from 10 years to 20 years climbed at a much slower average of 36 bps. This resulted in the narrowing of the spread between the 2-year and 10-year maturities to 63 bps on 15 May from 95 bps on 1 March.

The uptick in yields was largely driven by a market sell-off as investor appetite for Indonesian bonds waned amid rising yields for United States (US) Treasuries and the broad strengthening of the US dollar against other currencies. Foreign investors dumped Indonesian bonds as they rebalanced their portfolios, shifting their holdings away from emerging market assets. As a result, the foreign holdings' share in Indonesia's bond market declined from 41.3% at the end of January to 38.0% on 15 May. Capital outflows from the LCY government bond market were recorded in February and April. Net flows in January–April, however, remained positive at USD0.7 billion. Nonetheless, Indonesia remains vulnerable to the risk of capital outflows, given that foreign investors account for the largest investor group in its bond market.

Global market uncertainties weighed down the Indonesian rupiah as it weakened 2.1% against the US dollar between 1 March and 15 May, making it the worst-performing currency in emerging East Asia during the review period. Rising risks in global financial markets, as liquidity conditions tighten amid expectations of accelerated rate hikes by the US Federal Reserve and the normalization of monetary policies in other advanced economies, rising oil prices, trade rifts, and other geopolitical factors contributed to the overall weakness of the Indonesian rupiah. Bank Indonesia has intervened heavily to stabilize the currency and avert further sell-offs in its financial markets. Aside from external debt repayments, interventions by Bank Indonesia to stabilize the Indonesian rupiah led to the decline of foreign exchange reserves from USD132.0 billion at the end of January to USD124.9 billion at the end of April. Bank

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



Source: Based on data from Bloomberg LP.

Indonesia, however, noted that while reserves declined in April, the reserve asset position is still deemed adequate.

The Board of Governors of Bank Indonesia raised policy rates twice in a period of 2 weeks in May to ensure economic and financial stability amid continued weakness in the Indonesian rupiah. Initially, the central bank raised the 7-day reverse repurchase rate 25 bps in its meeting on 16–17 May. Another 25 bps rate hike was subsequently announced on 30 May when an off-schedule monetary policy meeting was held. Corresponding adjustments were announced for the deposit facility rate to 4.0% and the lending facility rate to 5.5%. The most recent rate hike was a preemptive move by the central bank to stabilize the Indonesian rupiah amid expectations the Federal Reserve will raise its policy rate in its June meeting. Bank Indonesia noted in its statement that “it will make use of available room to raise policy rates in a measured way.” Meanwhile, the central bank noted that inflation remains low and is expected to stay within its full-year 2018 target range of 2.5%–4.5%. Consumer price inflation rose 3.4% year-o-y in April, broadly unchanged from March.

For full-year 2018, Bank Indonesia maintained its economic growth projection of between 5.1% and 5.5%. In the first quarter (Q1) of 2018, real gross domestic product growth dipped slightly to 5.1% y-o-y from a 5.2% y-o-y expansion in the fourth quarter (Q4) of 2017. Domestic consumption remained subdued, expanding less than

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

	Outstanding Amount (billion)						Growth Rate (%)			
	Q1 2017		Q4 2017		Q1 2018		Q1 2017		Q1 2018	
	IDR	USD	IDR	USD	IDR	USD	q-o-q	y-o-y	q-o-q	y-o-y
Total	2,290,966	172	2,497,112	184	2,598,075	189	4.6	20.3	4.0	13.4
Government	1,970,089	148	2,109,783	156	2,197,585	160	4.9	19.4	4.2	11.5
Central Govt. Bonds	1,891,043	142	2,099,766	155	2,184,588	159	6.6	20.1	4.0	15.5
of which: <i>Sukuk</i>	274,492	21	342,989	25	329,204	24	11.7	34.4	(4.0)	19.9
Central Bank Bills	79,047	6	10,017	0.7	12,997	0.9	(25.0)	6.0	29.7	(83.6)
of which: <i>Sukuk</i>	12,273	0.9	10,017	0.7	12,997	0.9	13.8	74.4	29.7	5.9
Corporate	320,877	24	387,330	29	400,490	29	3.0	26.4	3.4	24.8
of which: <i>Sukuk</i>	11,834	0.9	15,387	1	16,449	1	2.2	28.4	6.9	39.0

() = negative, IDR = Indonesian rupiah, LCY = local currency, q-o-q = quarter-on-quarter, Q1 = first quarter, Q4 = fourth 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-March stood at IDR228.7 trillion.

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

5.0% y-o-y in Q1 2018. Contributing to the slower gross domestic product growth in Q1 2018 was a smaller increase in government expenditures and a worsening trade performance.

Size and Composition

Indonesia's LCY bond market reached a size of IDR2,598.1 trillion at the end of March, expanding at a faster pace of 4.0% quarter-on-quarter (q-o-q) in Q1 2018 versus 2.9% q-o-q in Q4 2017 (Table 1). Compared with the same period a year earlier, LCY bond market growth eased to 13.4% y-o-y from 14.0% y-o-y. The overall growth of the market was largely driven by the government bond segment.

The LCY bond market of Indonesia remains dominated by government bonds, which comprised 84.6% of the total LCY bond stock at the end of March. Corporate bonds accounted for the remaining 15.4% share. A larger share of Indonesia's bond market comprises conventional bonds, representing a share of 86.2%. The remaining 13.8% share is accounted for by bonds structured as *sukuk* (Islamic bonds).

Government bonds. The total government bond stock climbed to IDR2,197.6 trillion at the end of March, up 4.2% q-o-q and 11.5% y-o-y. Much of the growth came from increases in the stock of Treasury bills and bonds issued by the Ministry of Finance for budget financing. The outstanding size of central bank bills, or

Sertifikat Bank Indonesia (SBI), also contributed to the growth, albeit to a lesser extent.

Central government bonds. The stock of central government bonds climbed to IDR2,184.6 trillion at the end of March, on hikes of 4.0% q-o-q and 15.5% y-o-y in Q1 2018. As in past years, the government adopted a strategy of frontloading its issuance in a bid to secure the bulk of its funding requirements within the first half of the year. The government also plans to pursue most of its issuance in domestic currency as part of efforts to lower the foreign currency-to-gross domestic product ratio.

In Q1 2018, gross issuance of Treasury bills and bonds reached IDR219.4 trillion, up 86.5% q-o-q and 24.2% y-o-y. The government conducted 13 auctions of conventional bonds and *sukuk*, with demand remaining strong for most auctions despite escalating global uncertainties. The government accepted bids exceeding its targeted amount in all auctions, except for one *sukuk* auction, in line with its frontloading strategy. Aside from the scheduled auctions, the government also raised IDR8.4 trillion from the sale of retail *sukuk* in March. According to the Ministry of Finance, bond issuance during the quarter (including foreign currency bond issuance) was equivalent to 27.8% of the net target in the 2018 state budget.

Central bank bills. The outstanding stock of SBI reached IDR13.0 trillion at the end of March, up 29.7% q-o-q in Q1 2018. On a y-o-y basis, however, central bank bills

outstanding fell 83.6% from a high base as a number of conventional SBI remained outstanding in Q1 2017. Beginning in 2017, Bank Indonesia ceased issuance of conventional SBI and limited its issuance to sharia'h-compliant SBI. New issuance of sharia'h-compliant SBI climbed more than twofold to IDR4.3 trillion in Q1 2018 from IDR1.9 trillion in Q4 2017.

Corporate bonds. The outstanding size of corporate bonds stood at IDR400.5 trillion, gaining 3.4% q-o-q and 24.8% y-o-y. New issuance of corporate debt contracted 53.7% q-o-q but gained 5.5% y-o-y. Issuance of corporate bonds only resumed in February.

The corporate bond market in Indonesia comprises 115 corporate entities. The aggregate bonds outstanding of the 30 largest bond issuers amounted to IDR295.0 trillion at the end of March, accounting for 73.7% of the aggregate corporate bond stock during the review period (**Table 2**). Banking and financial institutions continued to dominate the top 30, accounting for more than two-thirds of the list. There were 14 state-owned corporations on the list, with six of them landing in the top 10.

The composition of the three largest corporate issuers in Q1 2018 was the same as in Q4 2017. At the top of the list was state-owned Indonesia Eximbank, whose outstanding bonds were IDR30.9 trillion at the end of March, which was lower than its end-December stock of IDR31.4 trillion as the volume of maturing bonds exceeded new issuance in Q1 2018. State-owned lender Bank Rakyat Indonesia was in the second spot with its outstanding bonds rising to IDR26.0 trillion at the end of March on issuance of IDR2.4 trillion during the quarter. In the third spot was Bank Tabungan Negara with bonds valued at IDR18.0 trillion.

A total of 11 corporate institutions issued bonds during the quarter. Most bond issuers had a quarterly aggregate issuance volume of more than IDR1.0 trillion, except for Bank BII (IDR646 billion) and Chandra Asri Petrochemicals (IDR500 billion). A total of 39 new corporate bond series were issued during the quarter, led by banking and financial institutions. Of this total, seven new corporate bond series were structured as *sukuk*.

The five largest corporate bond issuances in Q1 2018 are presented in **Table 3**, all of which were from state-owned firms. Perum Pegadaian, a state-owned

pawnshop operator, had the largest aggregate issuance at IDR3.5 trillion. It was followed by building construction firm Waskita Karya with new issuance of IDR3.5 trillion and energy firm PLN with aggregate issuance of IDR3.2 trillion. Rounding out the list were state-owned lenders Indonesia Eximbank and Bank Rakyat Indonesia with issuance of about IDR2.5 trillion each.

Foreign currency bonds. In February, the Government of Indonesia raised USD1.25 billion from the sale of global green bonds, marking the first Asian issuance of this type of bond. The bond sale was structured as a *sukuk* with a 5-year maturity and a coupon of 3.75%. In addition, the government sold USD1.75 billion of 10-year global *sukuk*. The bonds carried a coupon of 4.4%.

Investor Profiles

At the end of March, foreign investors remained the largest investor group in Indonesia's LCY government bond market, with their share of holdings rising to 39.3% of the total market from 38.2% a year earlier (**Figure 2**). In nominal terms, foreign investors held IDR858.8 trillion in March versus IDR723.2 trillion in the same period a year earlier. Foreign holdings, however, have steadily declined in 2018 on a monthly basis through mid-May. The decline has been due mainly to the sell-off in most emerging markets amid rising US Treasury rates and a strengthening US dollar.

A substantial portion of nonresident holdings are in longer-dated maturities (more than 10 years), representing 37.0% of their total bond holdings (**Figure 3**). Also, 35.6% of their holdings are invested in bonds with maturities of more than 5 years to 10 years. Only 5.9% of their holdings are in short-dated maturities (less than 1 year).

Banking institutions were the second-largest investor group in the LCY government bond market at the end of March. Bank holdings, however, slipped to a share of 25.9% at the end of March from 26.2% a year earlier. The bond holdings of insurance institutions also declined to 7.6% of the total from 13.2% during the review period.

All other domestic investors saw increases in their holdings of LCY government bonds, led by pension funds, whose holdings share gained significantly to 9.6% at the end of March from 4.6% a year earlier. Bank Indonesia's holdings of government bonds inched up to 4.3% of the

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	30,888	2.25	Yes	No	Banking
2.	Bank Rakyat Indonesia	26,001	1.89	Yes	Yes	Banking
3.	Bank Tabungan Negara	17,950	1.31	Yes	Yes	Banking
4.	PLN	17,357	1.26	Yes	No	Energy
5.	Indosat	16,519	1.20	No	Yes	Telecommunications
6.	Sarana Multi Infrastruktur	12,900	0.94	Yes	No	Finance
7.	Federal International Finance	12,562	0.92	No	No	Finance
8.	Bank Pan Indonesia	12,525	0.91	No	Yes	Banking
9.	Waskita Karya	12,509	0.91	Yes	Yes	Building Construction
10.	Adira Dinamika Multifinance	11,749	0.86	No	Yes	Finance
11.	Perum Pegadaian	11,140	0.81	Yes	No	Finance
12.	Bank Mandiri	11,000	0.80	Yes	Yes	Banking
13.	Pupuk Indonesia	9,076	0.66	Yes	No	Chemical Manufacturing
14.	Telekomunikasi Indonesia	8,995	0.66	Yes	Yes	Telecommunications
15.	Bank Maybank Indonesia	7,747	0.56	No	Yes	Banking
16.	Sarana Multigriya Finansial	7,293	0.53	Yes	No	Finance
17.	Hutama Karya	7,115	0.52	Yes	No	Non-Building Construction
18.	Bank CIMB Niaga	7,018	0.51	No	Yes	Banking
19.	Astra Sedaya Finance	6,280	0.46	No	No	Finance
20.	Bank Permata	5,810	0.42	No	Yes	Banking
21.	Medco-Energi International	5,000	0.36	No	Yes	Petroleum and Natural Gas
22.	Bank OCBC NISP	4,924	0.36	No	Yes	Banking
23.	BFI Finance Indonesia	4,801	0.35	No	Yes	Finance
24.	Maybank Indonesia Finance	4,425	0.32	No	No	Finance
25.	Permodalan Nasional Madani	4,246	0.31	Yes	No	Finance
26.	Toyota Astra Financial Services	4,064	0.30	No	No	Finance
27.	Indofood Sukses Makmur	4,000	0.29	No	Yes	Food and Beverages
28.	Adhi Karya	3,747	0.27	Yes	Yes	Building Construction
29.	Mandiri Tunas Finance	3,675	0.27	No	No	Finance
30.	Indomobil Finance	3,650	0.27	No	No	Finance
Total Top 30 LCY Corporate Issuers		294,964	21.49			
Total LCY Corporate Bonds		400,490	29.17			
Top 30 as % of Total LCY Corporate Bonds		73.7%	73.7%			

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

Notes:

1. Data as of 31 March 2018.

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.

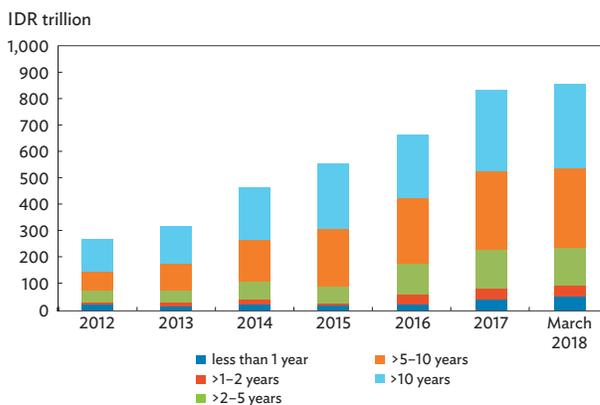
Table 3: Notable Local Currency Corporate Bond Issuance in the First Quarter of 2018

Corporate Issuers	Coupon Rate (%)	Issued Amount (IDR billion)
Perum Pegadaian		
370-day bond	6.00	450
3-year bond	6.90	1,050
5-year bond	7.10	2,000
Waskita Karya		
3-year bond	7.75	1,175
5-year bond	8.25	2,277
PLN		
5-year bond	6.50	457
5-year <i>sukuk ijarah</i>	6.50	104
7-year bond	6.80	10
10-year bond	7.25	341
10-year <i>sukuk ijarah</i>	7.25	88
15-year bond	8.20	362
15-year <i>sukuk ijarah</i>	8.20	58
20-year bond	8.75	1,365
20-year <i>sukuk ijarah</i>	8.75	449
Indonesia Eximbank		
3-year bond	6.35	610
5-year bond	6.70	1,650
7-year bond	6.90	206
Bank Rakyat Indonesia		
5-year bond	6.65	1,837
7-year bond	6.90	605

IDR = Indonesian rupiah.

Note: *Sukuk ijarah* are Islamic bonds backed by a lease agreement.

Source: Indonesia Stock Exchange.

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

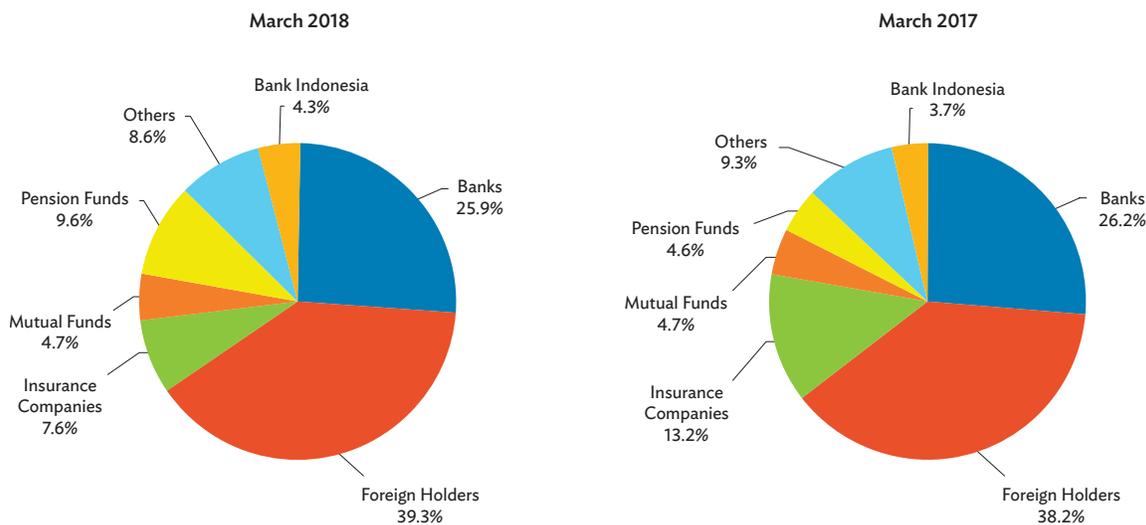
IDR = Indonesian rupiah.

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

total at the end of March as it engaged in bond purchases from the secondary market to help stabilize the foreign exchange market. By mid-May, bond holdings of the central bank had further climbed to a share of 6.8%.

Ratings Update

On 8 February, Japan Credit Rating Agency (JCR) upgraded Indonesia's foreign currency long-term issuer

Figure 2: Local Currency Central Government Bonds Investor Profile

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

rating to BBB and LCY long-term issuer rating to BBB+. Both ratings were assigned a stable outlook by JCR. In its decision to raise the credit ratings one notch higher, JCR noted (i) the improving investment climate as a result of the slew of economic policy packages since September 2015, (ii) accelerating infrastructure development, and (iii) declining private sector debt due to new prudential regulations on external borrowings.

On 7 March, Rating and Investment Information upgraded Indonesia's sovereign credit rating to BBB with a stable outlook from BBB- and a positive outlook. In its decision to upgrade the rating, Rating and Investment Information took note of Indonesia's strengthening economic performance, improvements in the management of the fiscal deficit, and low government debt.

Policy, Institutional, and Regulatory Developments

Bank Indonesia to Increase Liquidity in the Banking System

In January, Bank Indonesia announced improvements to the average reserve requirement ratios. The central

bank eased the daily minimum reserve requirement of conventional domestic banks to 4.5% of Indonesian rupiah deposits from 5.0%. The 2-week average reserve requirement was, however, raised to 2.0% from 1.5%. This new reserve requirement for domestic conventional banks will take effect on 16 July.

New reserve requirement regulations will also come into effect on 1 October for foreign exchange for conventional domestic banks and Islamic banks. For foreign exchange, the daily minimum reserve requirement for conventional bank was lowered to 6.0% from 8.0%. For Islamic banks, the daily minimum reserve requirement was reduced to 3.0% from 5.0%. In addition, a 2-week average reserve requirement of 2.0% will be implemented for foreign exchange for both conventional banks and Islamic banks.

IDR-Denominated Bonds to Become Part of Bloomberg Barclay's Global Aggregate Index

In February, Bloomberg announced that it will include IDR-denominated bonds as part of Bloomberg Barclay's Global Aggregate Index, with effect in May. Some 50 series of IDR-denominated bonds will be added to the index, contributing to its returns by 1 June. This move is expected to boost interest in Indonesian bonds.