

Research Report December 2018

INDONESIA INVESTMENTS

“Looking Back and Looking Forward”



Indonesia Investments Research Report

Looking Back and Looking Forward

December 2018



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Preface

Indonesia Investments' monthly research report is written and published by Van Der Schaar Investments B.V. - located in Delft, the Netherlands. The report aims to inform the reader of the latest, most relevant political, economic and social developments in Indonesia as well as those key global developments that are impacting on the Indonesian economy or politics.

Our research reports are intended for a wide audience, including both individual and corporate investors, financial market participants, policy makers, journalists, academics, and analysts.

The website Indonesia Investments is the reference and access point for gaining knowledge about Indonesian markets, the economy and cultures. The website is owned by Van Der Schaar Investments B.V., a privately-held investment company (Ltd.) which was established in 2009 but stands in a tradition that stretches back to urban development in the Dutch capital city of Amsterdam in the early 20th century. For information about Indonesia Investments, please visit: www.indonesia-investments.com.



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Lastly, we would like to emphasize that - although we strive to present accurate, up-to-date, and objective information to the reader - Indonesia Investments cannot guarantee the accuracy of all data that is included in this report.



Introduction

Another year has flown by, and what a volatile year it was indeed! US President Donald Trump's unpredictable style of leadership (which, among other things, triggered a tariff war between the United States and China; a war that is felt across the globe), four interest rate hikes in the USA (as the US economy expands at a fast pace, with tax cuts and spending growth stimulating demand), US dollar strength putting pressure on other currencies, the end of unprecedented monetary stimulus in the European Union, while global economic growth experienced a loss of momentum (with the US economy having peaked, while China's economic growth continues to slow).

These abovementioned issues injected a high degree of volatility in global markets throughout 2018. And being among the countries that are more vulnerable to capital outflows in times of global turmoil, Indonesia was heavily affected. For example, the Indonesian rupiah touched a 20-year low against the US dollar in October 2018. It brought back haunting memories of the traumatic Asian Financial Crisis in the late 1990s (which in Indonesia evolved from a financial crisis to a social and political one). Moreover, the fragile rupiah rate came at the wrong time for those who are in charge of the country as Indonesia's legislative and presidential elections are around the corner (scheduled for 17 April 2019). Serious rupiah weakness provided some new ammunition to political opponents of incumbent President Joko Widodo as they were able to increasingly question Widodo's economic and financial credentials (after all economic growth in Indonesia has also remained stubbornly around the 5 percent mark in recent years; for most Indonesians that is a disappointing pace).

This challenging external context is expected to be extended into 2019. Although, one crucially influential issue seems to have changed. At the beginning of January 2019, Federal Reserve Chairman Jerome Powell said the Fed will be "flexible on policy and it is in no hurry to raise interest rates", a message that sparked a huge stock market rally. Two weeks earlier, after the Fed's policy meeting in December 2018, several US central bank officials had already lowered their 2019 forecast to two interest rate increases, down from three rate hikes that were projected previously. Some analysts now even suggest that the Fed may not raise its benchmark rate at all in 2019. Others believe it will hike the rate only once.

Considering monetary policy tightening in the world's top economy has been the key factor in triggering capital outflows from emerging markets, including Indonesia, a 'dovish' Fed opens up opportunities for Indonesia to see capital inflows in 2019. Still, there remain plenty of other external challenges lurking about, and undermining investors' risk appetite.

With regard to the Indonesian economy and politics, the month of December 2018 was a solid one. As the Federal Reserve turned dovish, while Washington and Beijing are back on speaking terms and pausing a new round of (retaliatory) import tariffs, Indonesia was able to see plenty

of capital inflows in December 2018. Meanwhile, despite the fact that we are approaching the 2019 elections, the political atmosphere has remained conducive in Indonesia so far.

Indonesia is a young democracy - with a massive population that is characterized by diversity - and where consequently various sides (such as the traditional political elite, nationalists, and religious fractions) are engaged in a (sometimes bitter) battle for top political power. Elections in Indonesia can therefore give rise to tensions. With the 2017 Jakarta gubernatorial election still fresh in mind (an occasion where religious and ethnic tensions peaked alarmingly, not only in Jakarta but also in other parts of Indonesia), and with one presidential hopeful - Prabowo Subianto - seemingly eager to incite fear and anxiety among the population in a bid to boost his chances in the presidential election, there was serious concern that the events of Jakarta's 2017 election would be repeated.

However, Widodo's decision to select renowned Islamic clerk Ma'ruf Amin as his running mate in the 2019 election has probably been key in taming outbreaks of religious tensions ahead of the election. Hence, the situation remained conducive in December 2018. In fact, we have not seen much campaigning yet from both sides. But this could also be related to another national tragedy that unfolded. On 22 December another tsunami - this time completely unexpected - struck in the Sunda Strait, doing serious damage to the coastal areas (and taking at least 437 lives). It is the last natural disaster in a remarkably long series of disasters in Indonesia in 2018. Amid continued national grief it may not be the correct timing for presidential hopefuls to fully focus on the election (particularly in the case of Widodo who has a job to do). Also local media's spotlights have needed to be focused on these disasters. But with the first presidential debate scheduled for 17 January 2019, we should soon see the focus turn on the election and on both sides' campaigning.

Lastly - something that impacts on both the economy and politics - is the news that Indonesia officially became the majority owner of Freeport Indonesia after increasing its share ownership from 9.36% to 51.23% through a USD \$3.85 billion deal involving state-owned mining company Indonesia Asahan Aluminium (Inalum). Although it will take until 2022 before Indonesia can see significant additional revenue from Freeport Indonesia (related to an arrangement with Anglo-Australian mining giant Rio Tinto that was made in 1996), it is news that was well received in Indonesia (although Widodo's political opponents obviously criticized the deal).

Thank you for purchasing the December 2018 edition of our monthly research report - entitled "**Looking Back & Looking Forward**" - and we hope that this report contains valuable information for you!

Research Department
Indonesia Investments
Delft & Jakarta, 5 January 2019

10th
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PRESENTS

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