

Corona Crisis Hits Hardest Indonesia's Economy

Counting on Government's Stimulus

The unprecedented corona shock to spread since the early of March 2020 throws all-across economic sectors into disarray and exaggerates jitters of the severe damages it brings into the global and domestic financial sector. JCI's bearish trend at 13.5% from March to April 2020, a jump of almost 100 bps in yields of 10-year government bonds, a 4.3% rupiah depreciation showed impairment in the financial sector. JCI ended Tuesday's trading session of March 24, 2020 at 3,937 or snapping to an 8-year low at 3,955 in June 2012. Worried investors pulled out their money circa IDR125.2 trillion from JCI's stocks since early 2020, not to mention surging infected cases to burden JCI with significant foreign selling.

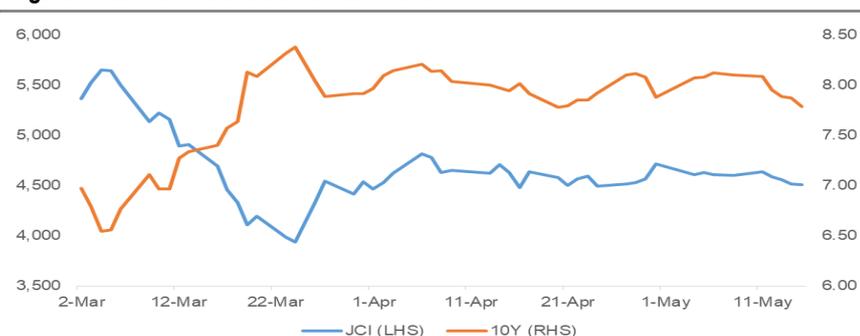
The Financial Service Authority (Otoritas Jasa Keuangan, "OJK") took "whatever-it-takes" backstop to deal with the impaired equity market and shield it against a far more severe disruption. OJK unleashed a relaxed measure of trading halt or a 30-minute trading suspension whenever JCI falls below 5% effective, and JCI as of Thursday of March 12, 2020 had recorded 5 times trading halt.

OJK to act in unison with Indonesia Stock Exchange (IDX), Indonesian Stock Market Clearing House (KPEI), and Indonesian Central Securities Depository (KSEI) agreed on shorter trading sessions. OJK unleashed the regulation of IDX's trading sessions of five days (Monday to Friday) in a week with a first trading session from 09:00 to 11:30 Western Indonesian Time (WIB) following the second trading session from 13:30 to 15:00 WIB.

The virus also weakens the rupiah exchange rate against foreign currencies. Bloomberg's data narrated hit-hardest USD/IDR at 16,575, while Jakarta Interbank Spot Dollar Rate (JISDOR) recorded USD/IDR to settle down at 16,741 or the lowest level since the crisis in July 1998.

As well as, the virus sparks risks of mounting premium, significant lay-off, soaring production costs, tumbling demands, ballooning state budget—serious disruption to Indonesia's economy. The Government through 2020's state budget initially target GDP growth of 5.3%, and lockdowns to stop the virus vicious spread daunt as Indonesia has to grapple with agonizing lay-off: idle and unproductive workers infected by the virus as well as caregivers prone to infection.

Figure 1: JCI Vs. Indonesia 10-Year Yield



Source: Bloomberg, NHKSI Research

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Fourteen-day economic lockdowns to contain the virus surpass annual leave days workers have, while COVID-19 infection and death toll necessarily mean soaring production costs driven by disruptions in Chinese-imported capital goods and raw materials. So those disruptions result in inevitable skyward prices of goods.

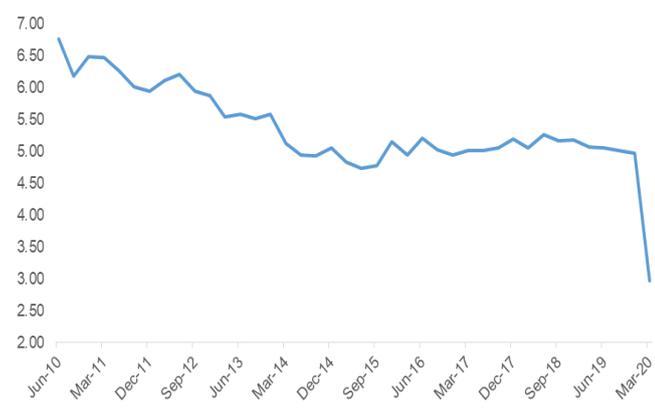
Corona Diminishes Consumption

Soaring prices and declining income diminish consumption so that the Government unleashes stimulus to whet consumers' appetite for spending—the crucial footing for Indonesia's GDP growth and re-locates budget by changes of the central and regional state budget. The Government's extraordinary backstop to deal with corona wreaking havoc on Indonesia's economy light up optimism.

Wuhan's Origin

The virus has its origin in Wuhan Market, China spreads into global pandemic and throws the global economy into disarray. With respect to the virus severity and unprecedented duration, the Indonesian government revised the 2020 State Budget (APBN) pursuant to the 2020 out of targeted macro APBN. First, the Minister of Finance projects that economic growth will only be at 2.5%-3% or much lower than 5.3%: APBN assumption by the end of this year. Limited public activities have impacts on all business sectors, excluding staple foodstuffs, health, and telecommunications sectors.

Figure 2: Indonesia GDP Constant 2010



Source: Bloomberg, NHKSI Research

Figure 3: Indonesia's Consumer Confidence Index



Source: Bloomberg, NHKSI Research

Second, USD/IDR exchange rate assumption also changed from 14,400 to 15,083. Based on Bloomberg data, JISDOR's USD/IDR had touched the low level of 16,741 on April 2, 2020. During this period, USD/IDR depreciation reached 20.4% YtD. Third, the realization of Indonesia's crude oil price (ICP) is projected to be valued at USD63 per barrel or higher than USD56.61 per barrel: the realization in February 2020.

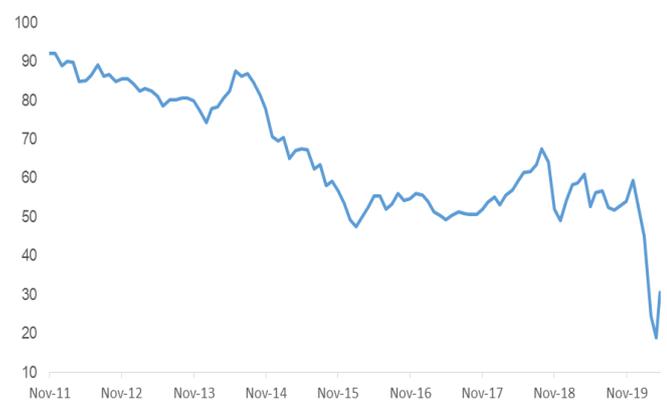
Downbeat ICP is in line with respective declining prices of Brent oil futures at USD27.8 per barrel and WTI at USD 24.19 per barrel. Meanwhile, the realization of oil and gas Income Tax (PPH) in February 2020 amounted to IDR 6.6 trillion or lower than IDR10.5 trillion in February 2019. That backdrop concurrently suppressed state revenues, particularly tax revenues.

Oil Price War

Economic lockdowns to stop Coronavirus' vicious spread lock commercial activities, press demand, and trigger oil oversupplied. The lockdowns cause dramatic drops in global oil prices reaching USD18 per barrel or steady at USD 38 per barrel: lower than the 2020 APBN assumption. A number of countries (i.e., Malaysia and Vietnam) have responded to the lockdowns by reducing selling price of fuel oil (BBM).

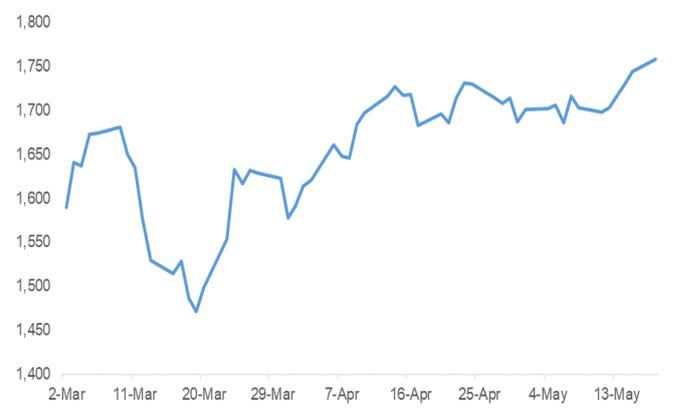
In contrast to the Government of Malaysia and Vietnam, the Indonesian government holds its domestic fuel prices unchanged as affirmed in the Decree of Minister of Energy and Mineral Resources (ESDM) Number 83 K /12/MEM/2020 on Retail Selling Prices for Specific Types of Fuel Oil. The Indonesian Government is looking at a number of influencing factors (i.e., the rupiah depreciation, reduction in domestic fuel consumption, and OPEC+'s curbed outputs starting in June 2020. As a matter of fact, OPEC+ agreed to cut output by 9.7 million barrels per day in May and June.

Figure 4: WTI's Contract Prices



Source: Bloomberg, NHKSI Research

Figure 5: Gold United States Dollar Spot



Source: Bloomberg, NHKSI Research

Meanwhile, Indonesia as the oil importer does not automatically stand benefits from falling global oil prices because one of Indonesia's state revenues is derived from oil and gas. The Special Unit for Oil and Gas (SKK Migas) projects that the state oil and gas revenues are only at USD19 billion or lower than the 2020 State Budget target of USD 32 billion. In addition, volatile global oil prices, the rupiah exchange rate are factors contributing to state budget's revenues deriving from oil and gas. On the other hand, declines in oil and gas revenues widen budget deficits. The Fiscal Policy Agency projects prices of Indonesian Crude Price (ICP) fall to USD 30.9 per barrel in a year, and it causes widening deficits by IDR12.2 trillion.

Gold as Safe Haven

High volatility in gold prices occurred in 1Q20 as reflected in prices of global gold and Antam. Of note, prices of gold in the spot market fall short at the range of USD1,470 per ounce troy to USD1,700 per ounce troy. It means that there is an exchange rate gab amounting to USD260 per troy ounce throughout 1Q20. In addition, Antam's gold falls in the range of IDR762,000 per gram to IDR926,000 per gram. In addition to the volatile rupiah exchange rate, the current gold price differences are wide as investors are more interested in safe haven assets rather than risk assets (i.e.,) stocks. On the other hand, no sentiments can weaken prices of gold. Indeed, massive stimulus unveiled by the Government and the central banks will spur prices of gold.

Government's Stimulus

The government unveils funds of IDR438.3 trillion which will be used as phase I, II, and III stimulus. The stimulus will be used to deal with the corona virus outbreak and social assistance. The allocation makes state expenditure increase to IDR2,613.8 trillion from IDR2,540.4 trillion or an increase of 2.9%. This value exceeds the 2020 state budget revenue target of IDR1,760.9 trillion. The increase in APBN spurred the budget deficits up to 5.07% of Gross Domestic Product (GDP). Previously, the budget deficit was at IDR307.2 trillion or 1.76% of GDP, rising to IDR852.9 trillion or equal to 5.07% of GDP.

The government also plans to issue special debt securities (a pandemic bond of IDR449.89 trillion) for funds allocated to manage the coronavirus. The plan to issue a pandemic bond is regulated in Perpu 1/2020 which can be purchased by Bank Indonesia (BI) as stipulated in article 16 paragraph 1. Meanwhile, the purpose of pandemic bond issuance is not to cover the budget deficit instead of a recovery bond to stimulate the world business affected by Corona.

The Right Investment Instrument

Uncertainty still looms Indonesia's domestic stocks and bond market. However, there are options for investors in choosing investments amid JCI's current volatility and the U.S. Wall Street stock exchange. Amid the high volatility and uncertainties, investors can selectively choose prospective stocks making a quite deep drop. JCI has recorded a decrease of 26.2% during 2020 and started to look at the health, infrastructure and banking sectors. Given normal conditions, stocks in those sectors are relatively expensive.

Stocks of banking sector as one of the sectors hit hardest by Coronavirus outbreak are potentially suffering from long-term impacts. The economic lockdowns—large-scale social restrictions (PSBB)—potentially increase the banking's hiking credit rate. On the other hand, the banking sector faces challenges of low interest rate, suppressing banking profits. However, potential dividends provided by the banking sector compared to other sectors can be an option for investors. Previously, the banking sector had been able to bounce back in a relatively quick time after the economic crisis.

Figure 6: IDX's Finance Index



Source: Bloomberg, NHKSI Research

Figure 7: IDX's Consumer Goods Index



Source: Bloomberg, NHKSI Research

Consumer sector. The spread of coronavirus cause panic buying and leads to the growth in the consumer sector. Investors can collect stocks of large-cap. consumer sector falling into LQ45 category.

Pharmacy—one of the consumer subsectors—benefits from increasing demands for a number of drug types as the Government decides to procure avigans and chloroquine for coronavirus treatments. Although there is yet proven medical studies, the Government is trying to imitate what China and Japan have done. Avigan is a drug brand developed by Fujifilm Toyama, while chloroquine can be produced domestically. Chloroquine is ready to be produced in Indonesia.

Telecommunications sector is one sector to benefit from the mandatory physical distancing, work from home, and independent isolation. Cellular data traffic increases significantly as the access to video content applications absorb more quota. Cellular data users more actively use information access, video applications, and purchasing goods via the internet.

Figure 8: Indonesia CDS 10Y



Source: Bloomberg, NHKSI Research

Figure 9: IBPA INDOBeX Government Total Return



Source: Bloomberg, NHKSI Research

In addition to the stock market, investors can look at gaps in choosing investments in the bond market. Foreign investors currently avoid potential capital losses and risks of the rupiah exchange rate. Based on Bloomberg data, IBPA INDOBeX Government Total Return was at minus of 4.24% YtD on Tuesday (3/25/2020). On the other hand, the Government and BI issued a number of policies in order to maintain economic growth momentum. In addition to lower interest rates, BI also routinely intervenes in the rupiah spot market, Domestic Non Deliverable Forward (DNDF) & the Government Securities (SBN) markets. Meanwhile, the selling action of foreign investors was influenced by the the rupiah depreciation and increasing risks of investment risk or Indonesia's credit default swap (CDS).

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