

CHINA
DEVELOPMENT
FINANCIAL

INDON 3.75% 04/25/22 (INDON)

Short-Term Carry (USD)

Marc Tan / 65 6202 1195 / marc.tan@kgi.com

Macro Trend: Indonesia is the 4th most populous country in the World and the largest economy in Southeast Asia with a population of more than 260 million people. The country is the 16th largest economy in the world with a GDP of ~US\$1 trillion. For the past 5 years, GDP growth has averaged 5% every year but downside risks to the country's growth outlook remain substantial as the escalation of trade tensions between China and the United States pose significant risks to Indonesia through a weaker external sector and dampened commodity prices.

Investment Considerations:

Economic growth momentum continues on the back of domestic demand. Economic growth in Indonesia reached 5.18% in fourth quarter of 2018 as compared to 5.17% (yoy) in the previous period, driven by continued expansion on resilient domestic demand, in line with increasing household consumption and consumption by nonprofit institutions serving households (NPISH). While net exports were negative due to falling commodity prices and global economic softness, economic growth has accelerated in Java and Kalimantan in line with vibrant agricultural, services and mining activities. As a result, economic growth in Indonesia accelerated to 5.17% in 2018 from 5.07% in 2017, the fastest rate in 5 years.

Figure 1: Economic Growth by Sector and Future Projections

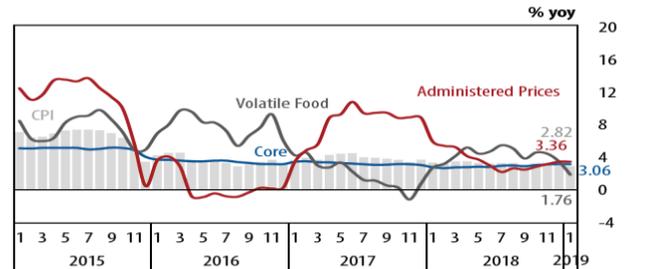
| Components | 2016 | 2017 | 2018 | | | | 2018 | 2019 [^] | 2020 [^] |
|---|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------------|-------------------|
| | | | I | II | III | IV | | | |
| Agriculture, Livestock, Forestry and Fisheries | 3.37 | 3.87 | 3.34 | 4.72 | 3.66 | 3.87 | 3.91 | 3.8-4.2 | 3.6-4.0 |
| Mining and Quarrying | 0.95 | 0.66 | 1.06 | 2.65 | 2.67 | 2.25 | 2.16 | 1.4-1.8 | 1.7-2.1 |
| Manufacturing Industry; | 4.26 | 4.29 | 4.60 | 3.88 | 4.35 | 4.25 | 4.27 | 4.3-4.7 | 4.4-4.8 |
| Utilities (Electricity, Gas and Water Supply)* | 5.26 | 1.76 | 3.33 | 7.29 | 5.62 | 5.64 | 5.47 | 5.1-5.5 | 5.2-5.6 |
| Construction | 5.22 | 6.80 | 7.35 | 5.73 | 5.79 | 5.58 | 6.09 | 6.1-6.5 | 6.2-6.6 |
| Trade, Hotel, and Restaurant** | 4.23 | 4.63 | 5.02 | 5.29 | 5.39 | 4.68 | 5.10 | 5.0-5.4 | 5.1-5.5 |
| Transportation, Warehousing, Information and Communication*** | 8.23 | 9.12 | 8.12 | 6.70 | 7.01 | 6.35 | 7.03 | 7.1-7.5 | 7.2-7.6 |
| Financial Services, Real Estate and Corporate Services**** | 7.14 | 5.43 | 4.63 | 4.22 | 4.47 | 6.13 | 4.87 | 4.9-5.3 | 5.0-5.4 |
| Other Services***** | 4.48 | 4.37 | 6.01 | 6.85 | 7.68 | 6.82 | 6.85 | 5.6-6.0 | 5.6-6.0 |
| GDP | 5.03 | 5.07 | 5.06 | 5.27 | 5.17 | 5.18 | 5.17 | 5.0-5.4 | 5.1-5.5 |

Source: Bank Sentral Republik Indonesia, KGI Research

Moving forward, the central bank expects solid economic growth for 2019 in the 5.0-5.4% range, bolstered by household and NPISH consumption as well as strong investment.

Inflation kept under control within targets. Inflation in 2018 came in at 3.13% compared to 3.61% in 2017, remaining within the central bank's targeted range for the fourth consecutive year. Low and stable inflation has also been maintained at the beginning of 2019, supported by lower inflation stemmed from milder price pressures on volatile foods (VF) and deflation of administered prices (AP).

Figure 2: Inflation

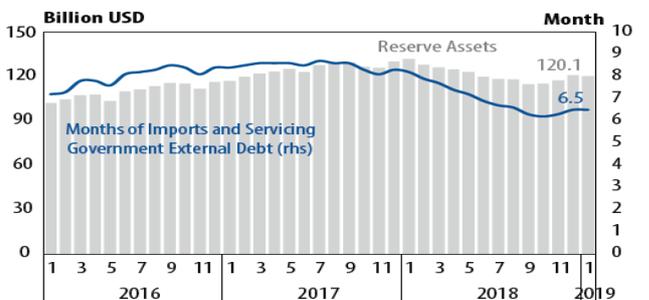


Source: Bank Sentral Republik Indonesia, KGI Research

Despite higher house rental prices and higher wages, core inflation was kept under control and the central bank expects inflation to remain low and stable within the target of 3.5% ± 1% in 2019.

Position of reserve assets remained solid. International reserves were recorded at USD120.7 billion in December 2018, equivalent to 6.7 months of imports or 6.5 months of imports and servicing government external debt, above the international adequacy standard of three months.

Figure 3: Reserve Assets



Source: Bank Sentral Republik Indonesia, KGI Research

Investment Recommendations: Currently, the bond is rated Baa2/BBB-/BBB by Moody's/S&P/Fitch and trading at 101.46 with a YTW of 3.2% and duration of 2.8.

Pending any spikes in USDIDR or capital outflows due to external factors such as a hawkish Fed or trade war, we expect INDON's short-term dollar debt to trade in a tight range and delivery positive carry, complementing our defensive portfolio.

Financials

| Economic Activity | 2016A | 2017A | 2018A |
|---------------------------------|--------------|--------------|--------------|
| Real GDP (YoY %) | 5.0 | 5.1 | 5.2 |
| CPI (YoY %) | 3.5 | 3.8 | 3.2 |
| Unemployment (%) | 5.6 | 5.4 | - |
| External/Fiscal Balances | 2016A | 2017A | 2018A |
| Current Account (% of GDP) | (1.8) | (1.6) | (3.0) |
| Budget (% of GDP) | (2.5) | (2.9) | - |
| Interest Rates | 2016A | 2017A | 2018A |
| Central Bank Rate (%) | 4.75 | 4.25 | 6.00 |
| USDIDR | 13,473.0 | 13,555.0 | 14,390.0 |

Source: Company Data, KGI Research

KGI's Ratings

| Rating | Definition |
|---------------|--|
| | KGI Securities Research's recommendations are based on an Absolute Return rating system. |
| BUY | >10% total return over the next 12 months |
| HOLD | -10% to +10% total return over the next 12 months |
| SELL | <-10% total return over the next 12 months |

Disclaimer

This report is provided for information only and is not an offer or a solicitation to deal in securities or to enter into any legal relations, nor an advice or a recommendation with respect to such securities. This report is prepared for general circulation. It does not have regard to the specific investment objectives, financial situation and the particular needs of any recipient hereof. You should independently evaluate particular investments and consult an independent financial adviser before dealing in any securities mentioned in this report.

This report is confidential. This report may not be published, circulated, reproduced or distributed and/or redistributed in whole or in part by any recipient of this report to any other person without the prior written consent of KGI Securities. This report is not intended for distribution and/or redistribution, publication to or use by any person in any jurisdiction outside Singapore or any other jurisdiction as KGI Securities may determine in its absolute discretion, where the distribution, publication or use of this report would be contrary to applicable law or would subject KGI Securities and its connected persons (as defined in the Financial Advisers Act, Chapter 110 of Singapore) to any registration, licensing or other requirements within such jurisdiction.

The information or views in the report ("Information") has been obtained or derived from sources believed by KGI Securities to be reliable. However, KGI Securities makes no representation as to the accuracy or completeness of such sources or the Information and KGI Securities accepts no liability whatsoever for any loss or damage arising from the use of or reliance on the Information. KGI Securities and its connected persons may have issued other reports expressing views different from the Information and all views expressed in all reports of KGI Securities and its connected persons are subject to change without notice. KGI Securities reserves the right to act upon or use the Information at any time, including before its publication herein.

Except as otherwise indicated below, (1) KGI Securities, its connected persons and its officers, employees and representatives may, to the extent permitted by law, transact with, perform or provide broking, underwriting, corporate finance-related or other services for or solicit business from, the subject corporation(s) referred to in this report; (2) KGI Securities, its connected persons and its officers, employees and representatives may also, to the extent permitted by law, transact with, perform or provide broking or other services for or solicit business from, other persons in respect of dealings in the securities referred to in this report or other investments related thereto; and (3) the officers, employees and representatives of KGI Securities may also serve on the board of directors or in trustee positions with the subject corporation(s) referred to in this report. (All of the foregoing is hereafter referred to as the "Subject Business".)

However, as of the date of this report, neither KGI Securities nor its representative(s) who produced this report (each a "research analyst"), has any proprietary position or material interest in, and KGI Securities does not make any market in, the securities which are recommended in this report.

Each research analyst of KGI Securities who produced this report hereby certifies that (1) the views expressed in this report accurately reflect his/her personal views about all of the subject corporation(s) and securities in this report; (2) the report was produced independently by him/her; (3) he/she does not carry out, whether for himself/herself or on behalf of KGI Securities or any other person, any of the Subject Business involving any of the subject corporation(s) or securities referred to in this report; and (4) he/she has not received and will not receive any compensation that is directly or indirectly related or linked to the recommendations or views expressed in this report or to any sales, trading, dealing or corporate finance advisory services or transaction in respect of the securities in this report. However, the compensation received by each such research analyst is based upon various factors, including KGI Securities' total revenues, a portion of which are generated from KGI Securities' business of dealing in securities.

Copyright 2019. KGI Securities (Singapore) Pte. Ltd. All rights reserved.