

REPUBLIC OF INDONESIA

AUGUST 2010

CREDIT GUARANTEE COUNTRY PROFILE:

IES/02: ATTACHMENT N

Country	<u>S/T Business Cycle</u>	<u>S/T Political</u>	<u>Debt Recovery</u>
Rating	<u>Indicator</u>	<u>Indicator</u>	The use of a collection agent is recommended.
3C	↑	→	

Credit Guarantee Experience

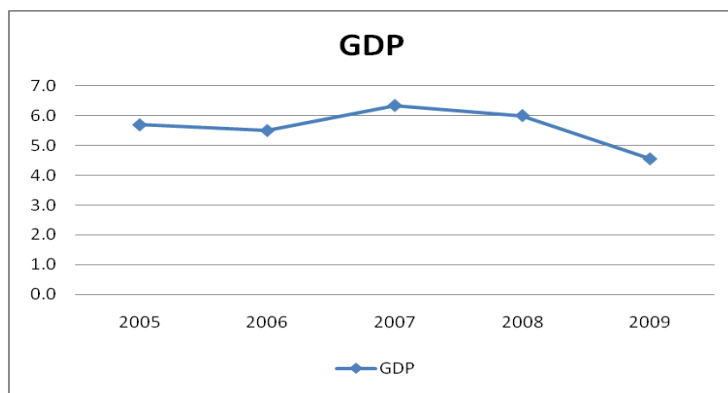
Cover is offered on a case-by-case basis only.

Political Highlights:

- President Susilo Bambang Yudhoyono was re-elected for a second term as head of government on 8 July 2010.
- The next election will be held in 2014.
- On July 22, the US lifted a ban on an Indonesian military unit called Kopassus, after 10 years as the unit was implicated in past killings of civilians and other abuses. The unit will undergo training within the limits of the US law.

Economic Developments:

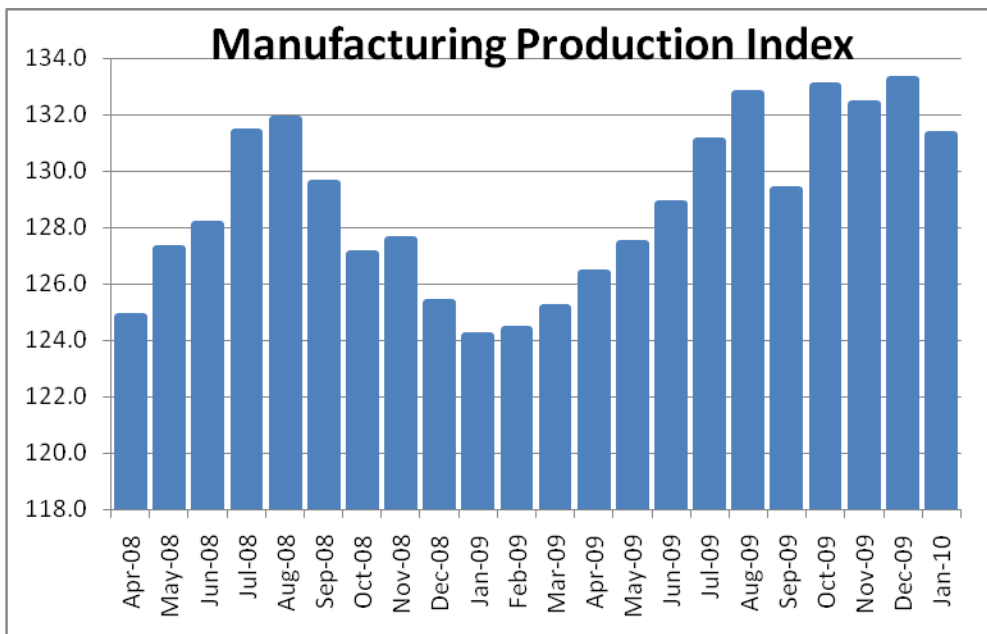
- Indonesia is a member of the G20 countries and is characterized by a developed economy with a strong government presence. The government administers the prices of basic products including rice, electricity and fuel. Over 164 state-owned enterprises are run by the government.
- As one of the largest economies in the world with a population of about 230 million, Indonesia remains attractive for investment due to its strong customer base.
- The economy weathered the global economic crisis as it is largely driven by domestic demand.
- Indonesia outperformed many of its neighbouring peers and joined China and India as the only G20 members posting growth during the crisis. The government implemented fiscal and monetary stimulus measures to offset the effects of the crisis. This combined with presidential election-related spending boosted the economy.
- The debt-to-GDP ratio declined steadily in recent years due to strong GDP growth and sound fiscal policies.
- The country faces the following economic challenges: high poverty and unemployment levels, inadequate infrastructure, corruption and a complex regulatory environment. Indonesia's poor condition of their infrastructure is reflected in the many factories that are still using old and outdated machinery.
- Although growth slowed from 6.1% in 2008 to 4.5% in 2009, it remained in positive territory reflecting the economy's low dependence on exports (representing 30% of the nominal GDP in 2008) and the large domestic market.



Source: Graph compiled by CGIC. Data obtained from ADB.

- GDP composition by sector: Industrial sector: 47.6%, services sector: 37.1% and the agricultural sector: 15.3%.
- A good harvest in 2009 resulted in an increase in rural income. This combined with low inflation; government cash transfers to poor households early in 2009, election-related spending and tax cuts led to an increase in private consumption, the biggest contribution to GDP.

- Construction expanded by 7.1% as a result of government spending on infrastructure and investment in buildings.
- Net foreign direct investment inflows decreased by 43% to \$5.3bn in 2009, but portfolio investment increased strongly, indicating increased investor confidence.
- The government implemented a fiscal stimulus package in 2009 to offset the effect of the global economic crisis on the economy. This amounted to \$7.7 trillion ($\pm 1.4\%$ of GDP in 2008). It consisted of:
 - Tax cuts for companies, workers and individuals (\$4.5bn) and tax subsidies and import duty exemptions (\$1.4bn).
 - Infrastructure projects and empowerment programmes for people living in rural areas including the improvement of highways, ports, bridges and irrigation systems (\$1.3bn).
 - Diesel and electricity subsidies and loans for rural empowerment (\$0.5bn).
- The stimulus programme helped to create more than 1m additional jobs, of which around 94% were in the public works programmes. The unemployment rate declined slightly from 8.4% in 2008 to 7.7% in 2009.
- Inflation decreased from 9.9% in 2008 to 4.8% in 2009, its lowest level in 10 years, as a result of the good harvests, an appreciating currency and lower global food and fuel prices.
- Growth in manufacturing production decreased in late 2008 and early 2009, but started to show improvements thereafter.



Source: Graph compiled by CGIC. Data obtained from ADB.

- The Asian Development Bank expects a V-shaped recovery as the leading indicators that include the purchasing manager's indices indicate strong activity in the coming months.
- The bank expects foreign direct investments to rebound due to improved global trade, the country's positive growth record and the upgrades in its credit rating. Domestic investment is also expected to increase as a result of the increase in economic activity, tax breaks and improved credit availability. Real GDP growth of 5.5% and 6% is expected in 2010 and 2011 respectively.
- The World Bank stated that strong domestic demand and world economic recovery would be the main drivers of Indonesia's growth in 2010 but the government will need to boost investment and improve infrastructure.
- Commodity prices are expected to increase placing upward pressure on inflation, which is expected to reach 5% in 2010.
- In recent years, Indonesia's government managed to reduce the public debt to less than 30% of GDP. This led to ratings upgrades and contributed to an influx of portfolio capital from the second half of 2009 as international capital flows resumed.
- S&P raised Indonesia's credit rating to BB- from BB- in March 2010, with a positive outlook. S&P and Moody's both rank Indonesia two levels below investment grade, while in January 2010 Fitch Ratings raised its rating to one step below investment grade. This reflects Indonesia's resilience to the global economic crisis.
- The government revised their budget deficit target for 2010 from 1.6% of GDP to 2.1% of GDP as a result of higher oil prices and a forecast 15% rise in electricity charges.
- The IMF recommends that the government improve the budget execution, increase the tax base and reduce costly subsidies. This is expected to create room for infrastructure spending and better social services to support sustained growth.

- Foreign tourist arrivals increased by 14% in the first half of 2010 from the same period in 2009 with more than 3.38m foreign tourists visiting Indonesia.
- BMI indicated in their June report that Indonesia's economic growth will exceed 7% in 10 years time, in line with China and India's growth rates with investment opportunities in the infrastructure and consumer markets. They rated Indonesia's economy as attractive due to their sound banking system, low private sector debt, strong demographics with growing middle class consumer potential, a strong resource base and a healthy fiscal position.

Trade Developments:

- Exports declined from \$139bn in 2008 to \$119bn in 2009.
- Export commodities include oil, gas, electrical appliances, plywood, textiles and rubber.
- A recovery in commodity prices are expected to support growth in Indonesia's exports as the world economy continues to recover together with increasing demand for raw materials from China and India.
- The World Bank expects imports to recover faster than exports as Indonesia's domestic economy is expected to grow at a faster pace than the economies of their major trading partners.
- Imports declined from \$116bn in 2008 to \$84bn in 2009.
- Import commodities include: machinery and equipment, chemicals, fuels and foodstuffs.
- Main trading partners include: China, Singapore, Japan, Malaysia, South Korea and India.
- International reserves increased from \$50.6bn in 2008 to \$66.1bn by the end of 2009. This represents 6.5 months of imports and government foreign debt payments.
- SA's exports to Indonesia totaled ±R2.4bn in 2008, ±R3.2bn in 2009 and ±R1.3bn up to May 2010.
- SA's imports from Indonesia totaled ±R5.4bn in 2008, ±R5.8bn in 2009 and ±R1.8bn up to May 2010.

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