



## INDONESIA: ECONOMIC AND FINANCIAL HIGHLIGHTS SEPTEMBER-OCTOBER 2007

### Summary:

- Inflation was higher for September and October due to seasonal factors including the Islamic fasting month of Ramadhan and Eid holiday.
- Bank Indonesia (BI) kept its policy rate steady in view of volatile markets and inflationary pressure.
- On July 31, Government of Indonesia (GOI) announced the biggest privatization since 1995 of the second largest state-owned Bank Negara Indonesia (BNI) which raised Rp 8.1 trillion (\$890 million).
- GOI bond auctions on September and October raised a total of Rp 16.45 trillion (\$1.8 billion) in funds.
- GOI received Rp 799 billion (\$88 million) from debt swap for its 16-year bonds yielding at 9.79%.
- On September 12, the Parliament approved the GOI's plans to recapitalize two state firms tasked with helping small-and-medium enterprises (SMEs) in obtaining loan financing.
- On October 9, the Parliament approved the GOI's 2008 state budget, with a deficit of 1.7% of GDP and economic growth of 6.8%.
- Moody's Investors Service upgraded Indonesia's credit ratings and foreign currency long-term debt and foreign currency long-term deposit ratings of 11 Indonesian banks.
- Standard and Poor's Ratings Services affirmed its ratings on Indonesia with a stable outlook.
- This cable uses an exchange rate of 9,103 per dollar.

### Rising Inflation from Holiday Season

On November 1, the Central Bureau of Statistics (BPS) announced it recorded 0.79% inflation in October, bringing the year-on-year (YoY) inflation rate to 6.88%. It eased slightly compared to 6.95% logged in September. Within analysts' expectations, inflation was relatively high for these two months as demand for food products and transportation picked up. The Eid holiday celebrations marking the end of fasting month Ramadhan fell in mid-October this year. Core inflation went up by 0.8% month-on-month (MoM), and 6.13% YoY in October, compared to September's 0.7% and 6.03% respectively.

## CPI Components

Components	September		October	
	MoM	YoY	MoM	YoY
Food stuff	1.81	12.99	1.87	12.64
Food, beverages, tobacco, cigarettes	0.45	6.82	0.51	6.67
Housing, water, electricity, oil/gas	0.18	5.22	0.21	5.18
Clothing	1.22	5.39	2.05	6.49
Health	0.44	3.16	0.45	5.14
Education, recreation, and sport	1.70	8.57	0.21	8.69
Transportation, communication, financial services	0.07	1.18	0.47	1.19
<b>TOTAL</b>	<b>0.80</b>	<b>6.95</b>	<b>0.79</b>	<b>6.88</b>
<b>Core Inflation *</b>	<b>0.70</b>	<b>6.03</b>	<b>0.80</b>	<b>6.13</b>

Source: Central Bureau of Statistics (BPS)

\* Core inflation is a measure of inflation which excludes certain items that face volatile price movements i.e. energy, food products.

### Interest Rate Cut to 8.25%

Amid volatile markets and inflationary pressure connected with the religious holidays, BI maintained its policy rate at 8.25% at October 8's monetary policy meeting, the fourth month in a row of steady rates. "It is not the right time to cut the interest rate. It would be better to hold it at the current level," Senior Deputy Governor Miranda Goeltom said. "We expect to keep it steady for now while assessing the situation and will make the decision at the right time on when interest rates should fall," she added as quoted by Reuters. BI is maintaining its 2007 year-end inflation forecast of about 6%. Analysts expect one more rate cut in the remainder of the year to bring the key BI rate to 8%, as inflation is likely to moderate following the fasting month of Ramadhan and the Islamic holiday season.

### BNI Bank Shares Sold – 26%

In the first major privatization for years, the State Minister for State Enterprises announced on July 31 that the sale of a 26% stake in second largest state-owned Bank Negara Indonesia (BNI) raised Rp 8.1 trillion (\$890 million). The share sale, via a secondary public share offering, was the biggest privatization since the government sold a minority stake in telecommunications giant Telkom in 1995. "The transaction has been successfully accomplished although the market has not been really conducive. It reflects investor confidence in the Indonesian economy, the banking sector and BNI's prospects in the future," the office said in a statement, according to Reuters. The government plans to use around half the funds to help plug the state budget deficit and the rest to strengthen the bank's capital base. The bank, which has a strong presence in corporate and retail banking, had total assets of about Rp 175 trillion (\$19 billion) in the first quarter of 2007.

### **August, September Long-Term Bond Auctions**

The GOI raised a total of Rp 9.5 trillion (\$1 billion) from bond auctions on August 28. It sold Rp 3.5 trillion (\$385 million) of 21-year bonds at a 10.29% yield and Rp 6 trillion (\$659 million) worth of 15-month zero-coupon papers at an average yield of 8.24%. The Ministry of Finance's Director General of Debt Management Rahmat Waluyanto said that the auction drew a good response from the market. He suggested that the impact of the US sub-prime credit crisis on Indonesia's financial markets is gradually waning. On September 29, the GOI raised another Rp 6.95 trillion (\$764 million), Rp 3.45 trillion (\$379 million) from auctioning 21-year bonds at an average yield of 9.9%, and Rp 3.5 trillion (\$385 million) from 11-year bonds yielding 9.4%.

### **GOI Swaps Debt**

The Ministry of Finance received Rp 799 billion (\$88 million) in bids from investors who wanted to swap shorter-maturity bonds for GOI's 16-year bonds yielding at 9.79%. Investors submitted a total of Rp 1.46 trillion (\$160 million) in bids at the auction. The government has been trying to lengthen its debt maturity profile by offering investors the opportunity to exchange shorter-term bonds for longer-dated paper to reduce the burden of maturing paper in the next five years. So far this year, the department has exchanged a total of Rp 15.2 trillion (\$2 billion) of short-dated government bonds in longer-dated paper.

### **Parliament Approves 2008 State Budget**

On October 9, the Parliament approved the GOI's 2008 state budget, which proposes a larger deficit of 1.7% of GDP compared with 1.5% this year and economic growth of 6.8% against 6.3% this year. Total budget revenue for 2008 is set at Rp 781.4 trillion (\$86 billion) or 18.1% of GDP while total expenditure is set at Rp 854.7 trillion (\$94 billion), resulting in a budget deficit of Rp 73.3 trillion (\$8 billion) or 1.7% of GDP. During the plenary session, Finance Minister Sri Mulyani said that, "The government is optimistic it can achieve the 2008 economic growth, supported by an expected improvement in consumer spending and higher investment in line with the improving investment climate."

The 2008 state budget assumes inflation at 6%, lower than the government's forecast of 6.5% for this year, while the rupiah exchange rate is set at 9,100 to the US dollar compared to 9,050 in this year's budget. The three-month Bank Indonesia Certificate (SBI) rate is projected to fall to 7.5% from 8% this year, while the oil price assumption is \$60 per barrel, unchanged from this year. The parliament and the GOI also agreed on a dividend payment of Rp 26 trillion (\$3 billion) by state-owned companies.

### **Parliament Approves SOE Recapitalization**

The Parliament, on September 12, approved plans to recapitalize two state firms tasked with providing loan insurance to small and medium sized enterprises (SMEs). According

to the plan, the GOI will inject Rp 850 billion (\$93 million) into Askrindo and the remaining Rp 600 billion (\$66 million) into Perum Sarana Pengembangan Usaha to allow them to offer more loan insurance for banks in case their SME loans turn sour. The scheme is part of GOI's efforts to aid the financing for SMEs, which employ the majority of the country's 100 million labor force. Sahala Lumban-Gaol, deputy minister in the economic coordinating ministry told Reuters, "The aim is to increase the capability of the firms in providing guarantees on bank loans extended to SMEs." Finance Minister Sri Mulyani Indrawati, in a parliamentary hearing on September 11, stated that SMEs (defined as those with annual sales of a maximum \$15 million) play an important role in the economy.

### **Moody's Upgrades Indonesia's Credit Ratings**

On October 18, Moody's Investors Service upgraded Indonesia's credit ratings, lifting the Indonesian government's foreign- and local-currency bond ratings to Ba3 from B1 and its foreign-currency bond ceiling to Ba2 from Ba3. It said the outlook on all ratings is stable, citing progress in cutting its debt and ample foreign exchange reserves and trade surplus, which offer buffers against external shocks. The move brings Moody's rating belatedly into line with rankings by both Standard and Poor's Ratings Services and Fitch Ratings. Fitch, which has a positive outlook on its Indonesia grade, is still the most upbeat on the country. "Along with prolonged fiscal restraint and recurrent under-execution of regional and local level spending targets, exchange-rate appreciation has also assisted in reducing the government debt ratio from a high of 100% of gross domestic product (GDP) in 2000 to an expected 34% in 2008," Moody's lead analyst for Indonesia Aninda Mitra was quoted as saying.

Moody's also raised the foreign currency long-term debt and foreign currency long-term deposit ratings of 11 Indonesian banks -- Bank Central Asia, Bank Danamon, Bank Internasional Indonesia, Bank Lippo, Bank Mandiri, Bank Negara Indonesia, Bank Niaga, Bank Permata, Bank Rakyat Indonesia, Bank Tabungan Negara and Pan Indonesia Bank.

### **Standard and Poor's Affirms Ratings for Indonesia**

On September 25 Standard and Poor's Ratings Services affirmed its ratings on Indonesia with a stable outlook, stating that the ratings are underpinned by continued improvements in the nation's debt and external liquidity positions. "Despite a modest rise in the central government deficit, we expect the government to adhere to fiscal discipline," said analyst Sani Hamid. The current account surplus continued to grow and there were steady FDI inflows and portfolio investments, he added. S&P has 'BB-/B' foreign currency and 'BB+/B' local currency ratings on Indonesia.

## Selected Economic, Monetary & Financial Statistics

	Jul 07	Aug 07	Sep 07	Oct 07
CPI Inflation (YoY)	6.06	6.51	6.95	6.88
CPI Inflation (MoM)	0.72	0.75	0.80	0.79
Rp/USD Exchange rate <sup>1</sup>	9,186	9,410	9,137	9,103
30-day SBI Interest Rate <sup>2</sup>	8.25	8.25	8.25	8.25
Foreign reserves <sup>3</sup>	51.9	51.4	52.9	51.4
JSX Composite Index	2,349	2,194	2,359	2,643
Exports (USD billion)	9.8	9.6	9.5	
% Change (YoY)	10.5	7.8	7.6	
Import (USD billion)	6.3	6.9	6.8	
% Change (YoY)	16.1	16.9	17.4	
Trade Balance <sup>5</sup>	3.5	2.7	2.7	

Source: Bank Indonesia, BPS

(1) Rp/USD, end of period

(2) End of period

(3) USD billions, end of period

(4) Jakarta Stock Exchange average daily transaction volume, in billions of shares

(5) USD billions

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