NH KORINDO SEKURITAS

Indonesia Market Insight | October 2020

Omnibus Law in the Midst of Recession

8 October 2020

Key Takeaways

- Indonesia has been experiencing deflation for three consecutive months with September deflation came in at 0.05%, which brought YoY Inflation to 1.42%.
- Manufacturing returns to contraction territory as September PMI Index recorded at 47.2, a setback after momentarily reached an expansion level in the previous month.
- The Ministry of Finance projected Indonesia GDP in Q3/2020 to contract between –2.9% to –1%, which will result in a second consecutive quarter with negative growth.
- The JCI fell sharply by -7.03%, ending a long market rally which started at the end of March. This was accompanied by a massive amount of foreign net sell which recorded at IDR 15.5 Trillion.
- The Financial Sector led the monthly decline with –12.26% as investors pulled out from big banks. Meanwhile, the property sector was an anomaly in September with a monthly gain of 14.53%.
- BBCA had the largest net sell by foreign investors with IDR 6,105 bn; followed by the State-owned bank BBRI with a net sell of IDR 2,077 bn. Meanwhile, the telco infrastructure firm, TOWR, led the net foreign buy list in September with IDR 165 bn.

Looking Ahead

- The Omnibus Law, on Job Creation was passed in early October. This law will attempt to streamline and simplify many regulations which have been viewed as non-productive to the ease of doing business in Indonesia. While this Act has raised a lot of controversies, mainly regarding the employment cluster, it will certainly benefit many business sectors if applied effectively.
- With the Indonesia economy set to enter into a Recession for the first time in over 2 decades, many will try to find some lessons from past crises. We revisit the 1998 monetary crisis in order to learn on what can be expected from the current recession and how should investors position themselves.

On our Watchlist

- Consumer staple picks

  ICBP, KLBF, UNVR
- Buying opportunities in big banks

  BBCA, BMRI
- Digital infrastructure sharing for telco stocks

  EXCL, TOWR
- Potential winners from Omnibus Law

  WIKA, PTPP, DMAS, ADRO

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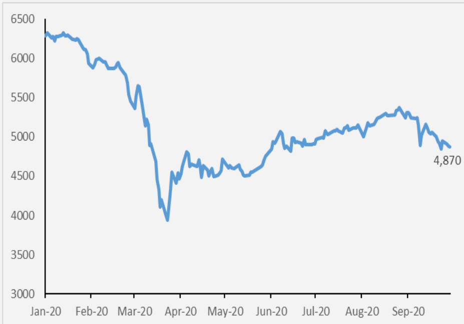
JCI as of 30 September 2020

Close	4,870
Monthly Change (%)	(7.03)
PER (x)	12.4
Market Cap (Tn)	5,664
Monthly Foreign Trx (Bn)	(15,591)

JCI Movement (YTD)



Indonesia Macroeconomic Data

Indicators	Last	Prev.
Real GDP YoY	-5.32%	2.97%
Current Acc (USD bn)	(2.90)	(8.08)
FDI (USD bn)	4.07	4.60
Cons. Confidence*	83.40	86.90
BI-7 Day Rev Repo Rate	4.00%	4.00%
FX Reserve (USD bn)	135.15	137.00
Trade Balance (USD bn)	2.33	3.26
Inflation YoY	1.42%	1.32%

Inflation remains low, further benchmark rate cut possible

For the third month in a row, Indonesia had a monthly deflation as September's Consumer Price Index (CPI) recorded at –0.05% MoM. This resulted in a YoY inflation currently at 1.42% or still below the Bank Indonesia target of 3% (+/-1%). Last month's deflation was partly contributed by Food & Beverage sector with –0.37% and Transportation segment with –0.33%. While the government has been introducing various direct stimulus programs, it has not been able to boost purchasing power. We view that this persistently low inflation will increase the chance of another benchmark rate cut before the end of the year.

Meanwhile from the production side, manufacturing also return back to contraction zone, as PMI index in September recorded at 47.2. The re-implementation of Large Scale Social Limitation (PSBB) in the Jakarta area has forced manufacturers to again reduce production capacities. This caused the purchase of raw materials and inventory to decline as part of cost reduction efforts. The index briefly reached an expansion mode in August, but with economic slowdown set to continue, we expect PMI to stay in contraction zone for the rest of the year.

Figure 1: Indonesia CPI (MoM)

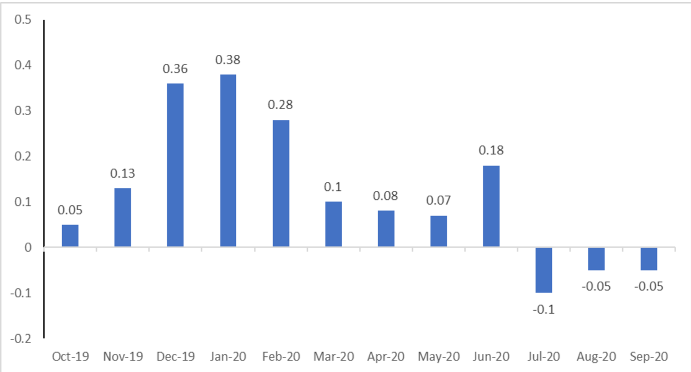
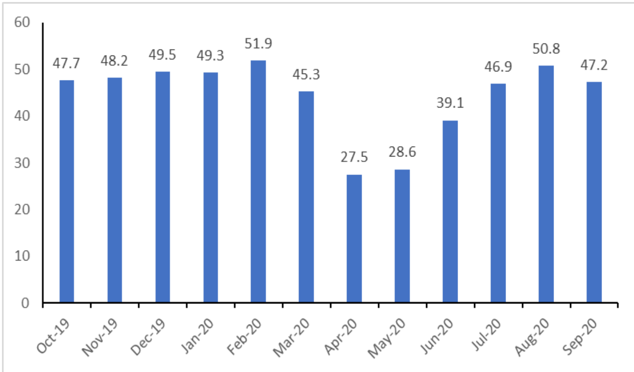


Figure 2: PMI Manufacturing Indonesia



Sources: Bloomberg, NHKSI Research

GDP growth projected to remain negative in 3Q20

The ministry of Finance predicts that economy growth in 3Q20 will be contracted between –1% to –2,9% ; and full year growth in a range of -0.6% to –1.7%. This would mark the second quarter in a row with negative growths, which satisfies the commonly accepted definition of a recession. One of the most severe consequences will be the unemployment level, which is predicted to increase by as many as 5 millions. Meanwhile, while projected to be negative, consensus number states that GDP growth will show an improvement from the –5.32% in 2Q20. The gradual re-opening of the economy, coupled with government stimulus disbursements, have resulted in better economic indicator numbers. We view that the government's plan to boost the economy must also be followed by increasing effort to combat the Covid-19 pandemic. Should the number of cases remain high, it will be difficult to expect a significant improvement for the overall economy.

Figure 3: Indonesia Economic Growth Projection 2020

Institution	Projected GDP Growth
Ministry of Finance	-0.6% to -1.7%
OECD	-3.3%
ADB	-1%
Bloomberg	-1%
IMF	-0.30%
World Bank	0%

Source: NHKSI Research

Significant drop for JCI in September, as massive foreign outflow hit big cap stocks

JCI's long rally which has started at the end of last March was halted in September as the benchmark index had a monthly correction of -7.03%. Concerns regarding the potential outcomes from a recession and the re-enforcement of large-scale social distancing (PSBB) as Covid-19 new cases remain high in the Jakarta Area, were amongst the key sentiments suppressing the JCI last month. Meanwhile, foreign investors booked the highest monthly net sell this year, with an outflow of IDR 15.5 Trillion. This brought the total net foreign sell since the start of the year to IDR 43.4 Trilion in all market.

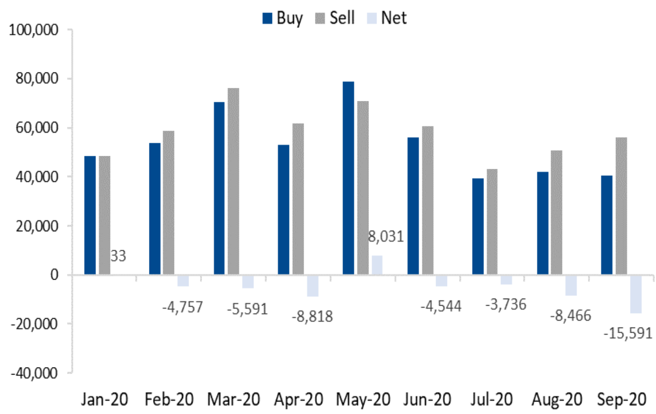
All four big banks in Indonesia were among the biggest net foreign sell, with BBCA (IDR 6.1 Tn) and BBRI (2.1 Tn) topping the list. Other big caps also hit by foreign outflow were the telco-giant TLKM (IDR 1.2 Tn); automotive giant ASII (IDR 759 Bn); and consumer goods companies UNVR & GGRM. On the other hand, the Djarum group-owned tower company, TOWR, led the Net Foreign Buy list, albeit with a mere IDR 165 Bn.

Figure 4: Sectoral Movement

Sector	31 Aug 2020	30 Sep 2020	Change
Consumer Goods	1933.18	1828.95	**-5.39%**
Mining	1398.81	1332.02	**-4.77%**
Agriculture	1185.13	1137.47	**-4.02%**
Finance	1185.07	1039.76	**-12.26%**
Miscellaneous Industry	912.72	820.30	**-10.13%**
Infra, Utilities, & Transportation	856.87	785.95	**-8.28%**
Basic Industry	760.26	709.51	**-6.67%**
Trade, Services, & Investment	628.75	631.21	**0.39%**
Const, Prop, & Real Estate	297.39	340.62	**14.53%**
JCI	5238.49	4870.04	**-7.03%**

Source: Bloomberg

Figure 5: Monthly Foreign Transactions



Sources: IDX Statistic, NHKSI Research

Figure 6: Top Foreign Transactions Sep 2020 (Regular Market)

Net Foreign Buy	
Stock	**Value (IDR Mn)**
TOWR	165,108
BULL	88,745
ANTM	43,427
LPPF	26,393
RALS	25,164
WOOD	21,686
POLL	21,348
BFIN	19,922
TINS	19,288
ISAT	17,236

Net Foreign Sell	
Stock	**Value (IDR Mn)**
BBCA	-6,105,631
BBRI	-2,077,114
TLKM	-1,266,251
BBNI	-1,024,432
ASII	-758,972
BMRI	-688,705
UNVR	-352,552
MDKA	-335,182
GGRM	-280,518
PGAS	-273,098

Source: NHKSI Research

Potential winners from the newly-passed omnibus law on Job Creation

The House of Representatives has passed the Job Creation bill into law in early October, amidst massive protests and objections. The bill was created as a solution to improve investment climate by streamlining many regulations and permits that are deemed counter-productive to the ease of doing business in Indonesia. By moving these red tapes, new investments are expected to be brought into the country, which in turn translate to job creation. The law will cover 11 clusters, which consist of 15 chapters and 186 articles. These main topics covered in this omnibus bill include: Land Permits, Investment Requirements, Employment Affairs, Empowerment of Micro & Small Medium Enterprises (MSME), Ease of Doing Business, Research & Innovation, National Strategic Projects, and Industrial Estates.

On the other hand, this bill has garnered many objections from the broader society, in particular the labor unions. Some of the most crucial aspects that have raised controversies are in regards to: Environmental Management, Education, Severance payments, and Outsourcing. Many parties also raised questions about the urgency about of this bill in the midst of a pandemic situation.

As this bill now has been passed in laws, we will try to identify potential sectors that might benefit from the implementation of the Job Creation Act.

1. Construction & Property Sector

At first glance of the Job Creation Bill, the construction sector is a clear winner. There are three main clusters that directly affect this sector, which are: Land Permits, National Strategic Projects, and Industrial Estates. This coupled with the government's decision to increase budget allocation for Infrastructure, will be a strong catalyst for construction sector, especially for state-owned construction firms.

From the property sector, the simplification of land permit process will act as a positive sentiment as this was often seen as the main obstacle to the advancement of this industry. As the Job Creation also put emphasize on Industrial Estates, we view this as a fresh breeze for companies such as: PT Puradelta Lestari Tbk (DMAS), PT Kawasan Industri Jababeka Tbk (KIJA), and PT Bekasi Fajar Industrial Estate Tbk (BEST). Furthermore, with the overall aim of the bill is to attract investments into Indonesia, it is expected that the demand for industrials land will also increase.

2. Coal Mining Sector

Coal Mining is another sector that potentially benefit from the Omnibus Law. This is due to an incentive in the form of 0% royalty for creating value-added to the raw materials. Companies which are willing to invest in downstream business and coal-fired power plants will be the ones to gain from this regulation. Some of the coal mining companies that have either operate or in the process of construction of power plants are ADRO, which co-owns several plants in South Kalimantan and Central Java; and PTBA, which is currently building a power plant project in South Sumatera.

3. Telecommunication Sector

The Omnibus Law on Job Creation also states several regulations that might be favorable to the telecommunication sector, specifically in regards to digital infrastructure. The law will amend the previous telecommunication law, which now enables operators to share infrastructure. Furthermore, the Omnibus Law also aim for synchronization of policies between Central and Regional Government to ensure that the construction of digital infrastructure such as; BTS and fiber optics, will be eased.

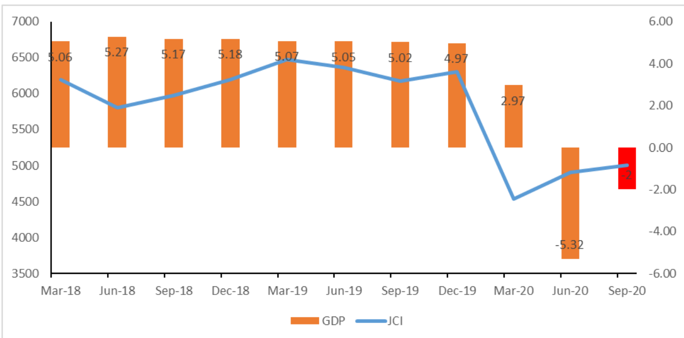
Revisiting the 1998 Monetary Crisis: Learnings from past recessions

With Indonesia set to enter its first recession in over 20 years, we revisit the 1998 monetary crisis to get a glimpse of what can be expected from a recession. It should be note that there are some key differences between the 1998 recession and the current economic slowdown (see table). We view that although this pandemic-caused recession is unprecedented, Indonesia has taken some lessons from past crises (1998 & 2008) which make the country better prepared in facing economic turbulence. Most notably, the banking sector, which is the key component of both the economy & JCI market cap, is currently far more stable in terms of liquidity and capital. Combine this with a well-targeted stimulus plan from the government, the stock market expects a faster recovery this time around, as shown by the JCI rally since its March downfall. Looking at the correlation between JCI and the GDP in 1998, it can be seen that the benchmark index can act as a reliable leading indicator to the broader economy. At this stage, we see that although the economic growth will still be contracted until the end of the year, it is an encouraging sign that the level of contraction is predicted to be trending in a positive direction. However, we remain cautious in our stock selection process by putting more emphasis on sectors that are more defensive, such as: Consumer Staples. Healthcare, and Banking.

Key Characteristics	1998 Monetary Crisis	2020 Covid-19 Crisis
Origin & Impact of crisis	♦ Started as monetary / currency crisis ♦ Began in east Asia with impact limited to South East Asia	♦ Started as a health-related issues / pandemic ♦ Began in Asia and spread globally
Social & Political Aspects	♦ Shortages of consumer staples ♦ Subsequent political crisis (Change in government regime) ♦ Social distancing measures not required ♦ Limited impact on MSMEs	♦ No Consumer Staples supply issue ♦ Stable political condition ♦ Enforcement of Large Scale Social Limitation ♦ Significant impact on MSMEs
Economic Indicators	♦ Great depreciation of the USD/IDR exchange rate ♦ High benchmark interest rate ♦ High inflation rate	♦ USD/IDR depreciation far more controllable ♦ Low benchmark interest rate ♦ Low inflation rate
Banking Industry	♦ Liquidity Crisis in Banking Industry ♦ Negative Capital Adequacy Ratio (CAR) ♦ High Non-performing loan (NPL) rate	♦ Excess Liquidity in Banking ♦ Average CAR above requirements ♦ Low NPL rate

Figure 7: JCI Movement vs GDP (1998-2000)

Figure 8: JCI Movement vs GDP (2018-2020)



Source: Bloomberg, NHKSI Research

On our Watchlist

The JCI's sharp decline in September has provided investors with buy opportunities for big cap consumer staple stocks. We take comfort in these stocks especially entering the recession era, since these are some of the safest companies which products are crisis-proofed. The F&B giant, **ICBP**, with its flagship instant noodle products will fare relatively well as people look for more affordable options. Pharmaceutical company, **KLBF**, has recently began distribution of a Covid-19 therapeutic drug, Remdesivir. Meanwhile, **UNVR** stock is currently trading at around –1 P/E Band of its 5-year average.

Recent massive foreign outflows have battered stock prices of big banks. We see this as accumulation opportunities with our top picks going to **BBCA** and **BMRI**. The Financial Services Authority (OJK) has agreed to extend the loan restructuring program until 2022.

Infrastructure sharing initiatives under Omnibus Law on Job Creation will benefit providers like **EXCL**. Moreover, the increase in demand for internet data which translate to higher demand for telco towers continue to support **TOWR** as our pick.

We also view that construction and property sector as the big winner from the Job Creation Act, as the law put heavy emphasis on land permits and investments. Coupled this with the increase in infrastructure budget in 2021, State-owned construction will surely benefit, with **WIKA** and **PTPP** considered as the strongest options. Furthermore, industrial estate firms are also set to capitalize on this new law, as it is expected to attract new investments in manufacture factories which will increase the demand for industrial land. Our top pick in this sector is **DMAS** which currently has excess cash position. This will enable the company for future expansions in order to meet the anticipated increase in demand.

Lastly, we include **ADRO** for our list as the 0% royalty on coal mining will be favorable for the firm. Moreover, the company has also been consistently paying out interim dividends in the past.

Figure 9: Stock Watchlist October 2020

Key Fundamental Statistics (as of 8 October 2020)

Stock	Market Cap (IDR Mn)	P/E (x)	P/B (x)	GPM (%)	OPM (%)	NPM (%)	ROE (%)	DER (%)	Net Gearing (%)
ICBP	116,910,628	20.01	4.07	37.57	19.53	12.64	22.68	9.38	Net Cash
KLBF	73,828,317	28.00	4.52	45.37	15.52	12.36	17.00	9.85	Net Cash
UNVR	304,246,250	41.53	34.54	50.25	22.15	16.55	105.38	10.79	Net Cash
BBCA	708,215,162	25.34	4.19	86.00	39.78	31.12	17.00	N/A	N/A
BMRI	255,500,000	10.54	1.42	58.60	19.33	12.58	13.28	N/A	N/A
EXCL	23,446,167	10.78	1.14	24.10	15.23	3.4	11.10	158.04	137.21
TOWR	52,545,064	19.57	5.61	69.73	58.40	41.94	31.13	207.95	193.20
WIKA	10,449,993	6.36	0.76	5.49	30.06	5.15	11.30	125.60	82.03
PTPP	5,424,910	9.32	0.50	11.30	3.95	0.08	4.92	130.95	92.13
DMAS	11,278,358	14.31	2.07	66.12	27.67	17.64	12.87	0.00	Net Cash
ADRO	36,304,067	9.40	0.67	20.33	15.84	9.29	7.02	42.69	15.47

Sources: Bloomberg, NHKSI Research

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