

Indonesia Rating Raised To 'BBB' On Strong Growth Prospects; Outlook Stable

Overview

- Indonesia's economy has consistently outperformed its peers at a similar level of income, and we expect its strong growth prospects to remain over the coming years.
- Given Indonesia's stable policy and prudent fiscal settings, we believe its overall credit profile is enhanced.
- We are raising our sovereign credit rating on Indonesia to 'BBB' from 'BBB-'. The outlook is stable. We are also raising our short-term sovereign credit rating to 'A-2' from 'A-3'.
- The stable outlook reflects our expectations that Indonesia's economy will continue to perform strongly over the medium term, and that the country's external position will stabilize.

Rating Action

On May 31, 2019, S&P Global Ratings raised its long-term sovereign credit rating on Indonesia to 'BBB' from 'BBB-'. The outlook is stable. We also raised our short-term sovereign credit rating to 'A-2' from 'A-3'.

Outlook

The stable outlook reflects our view that the constructive policy environment in Indonesia will support its growth prospects over the coming years, enhancing the sovereign's broader credit profile.

We may raise the long-term rating if Indonesia's external settings improve materially from their current levels, or if its fiscal settings improve such that the general government deficit and associated change in net debt fall well below 1.0% of GDP over the next two years.

Conversely, we may lower the rating if economic growth slows substantially over the next two years, or if we observe notable weakening of Indonesia's external or fiscal positions. Indications of pressure on the rating are net general government debt and budget deficit surpassing 30% and 3% of GDP, respectively, in a sustained way, or interest costs exceeding 10% of government revenue. Indications of Indonesia's external settings weakening are liquidity (gross financing requirements as a percentage of current account receipts [CAR] and foreign exchange reserves) consistently exceeding 100%, and narrow net external debt above 100% of CAR. Such a deterioration could occur if Indonesia's terms of trade continue to worsen without a concurrent compression of import volumes, and real export growth materially underperforms our expectations.

Rationale

We raised the ratings to reflect Indonesia's strong economic growth prospects and supportive policy dynamics, which we expect to remain following the re-election of President Joko Widodo recently. The sovereign ratings on Indonesia continue to be supported by the government's relatively low debt and its moderate fiscal performance. These factors balance weaknesses associated with Indonesia's lower-middle-income economy and modest CAR.

Institutional and economic profile: Above-average growth, policy continuity support creditworthiness

- President Widodo's strong performance in the elections entails policy continuity over the next five years.
- Indonesia's economy is growing faster than that of peers at the same income level.

The Indonesian economy is growing faster than global peers at a similar level of income. This reflects the government's policymaking has been effective in promoting sustainable public finances and balanced economic growth. Real GDP per capita growth in Indonesia is an impressive 4.1%, on a 10-year weighted-average basis. This compares with an average of 2.2% across global sovereigns at a similar income level, and speaks to the constructive economic dynamics in Indonesia despite a challenging external environment over recent years.

Official results indicate that Indonesia's recent elections have provided incumbent President Widodo with a refreshed mandate, although challenger Prabowo Subianto continues to dispute the outcome. Mr. Prabowo's campaign has lodged a complaint with the Constitutional Court, which may entail an official review of the results over the coming months. Although this dispute and isolated pockets of unrest associated with it add some uncertainty to Indonesia's political settings over the near term, we do not expect it to have a material impact on the long-term policy environment or economic outlook.

Political and policy institutions in Indonesia are generally stable and free of challenges to their legitimacy. While the Widodo government implemented policy measures ahead of elections to support purchasing power and consumption, we believe these are temporary, and continue to expect reform momentum to pick up once the new government is in place.

Indonesian society is generally cohesive despite the expanse of the country over many islands. News and information flow freely in Indonesia, with key policy and other changes well publicized and debated. Indonesia publishes timely economic, fiscal, and financial statistics in detail. At the same time, it trails many similarly rated sovereigns in governance issues, such as control of corruption. Although Indonesia has shown gradual improvement in these areas over the past five years, further progress will likely be needed to attract more growth-enhancing, foreign direct investment.

Indonesia's economy is still considered lower-middle income. As a commodity exporter and capital importer, it is subject to shifts in external conditions. A key rating constraint is Indonesia's GDP per capita, which we estimate at US\$4,200 in 2019. Indonesia's strong per capita trend growth of approximately 4.1% will help to alleviate this weakness over time, assuming relative currency stability.

Growth of the Indonesian economy has been largely dependent on domestic demand in most recent years. From an expenditure perspective, consumption has been the leading contributor to real GDP growth, with investment also contributing a sizable share over the past five years. These trends should remain in place if President Widodo and his government continue to emphasize on investment in infrastructure and human capital. The contribution from net exports, on the other hand, has been modestly negative over the same period, and net trade flows subtracted 1.1% from real GDP growth in 2018.

Flexibility and performance profile: Fiscal deficit should remain about 2.0%, with potential subsidy reform on the horizon

- The fiscal deficit should remain about 2.0% with the return of the Widodo government.
- Monetary settings are relatively tighter following interest rate hikes in 2018, and easing is possible.
- Although Indonesia's external indebtedness and liquidity needs are moderate, a recent worsening in its terms of trade presents some downside risk.

In our view, the government's debt burden is relatively light. We forecast a stable general government debt ratio over the next few years, reflecting the fairly stable projected fiscal balance. The government's fiscal deficit fell to a multi-year low in 2018, and we expect it to stabilize just below 2.0% of GDP over the next four years. After the recent elections, we believe some remaining subsidies may either be rolled back or reduced, supporting the government's fiscal consolidation. This should increase budgetary allocation to the president's stated aims of human capital and infrastructure investment in his second term.

We project net general government debt to remain comfortably below 30% of GDP, given a contained fiscal deficit and consistent nominal GDP growth. On top of this relatively moderate debt burden, we expect contingent liabilities facing the government to remain limited. In particular, the government bears limited exposure to explicit guarantees, with reasonably strict controls in place.

The government's increasing orientation toward domestic borrowing, along with higher interest rates since 2018, have raised interest costs in recent years. However, interest payments should remain below 10% of general government revenue in the next three years, owing primarily to continued growth in the government's revenue base relative to GDP. Higher revenue associated with buoyant energy prices should also help government revenue. The government's debt-servicing remains subject to some foreign exchange risks because approximately 40% of debt is denominated in foreign currencies. The compositional shift in the government's borrowing may lower this ratio to below 40% within the next two years.

Bank Indonesia (BI), the central bank, is an important institution in Indonesia's ability to sustain economic growth and attenuate economic or financial shocks. The central bank has had significant operational independence to pursue its monetary policy target since July 2005, when it formally adopted the Inflation Targeting Framework. BI has since managed inflation roughly in line with that of its regional peers; in particular, price pressure has been well contained since the early 2010s.

BI relies increasingly on market-based instruments in implementing its monetary policy. The financial system has also grown steadily in recent years. Monetary flexibility has been augmented by the rising flexibility of the rupiah, a floating currency. In 2018, BI raised its policy rate by a total of 175 basis points to head off pressure from higher volatility in international financial markets. We believe this proactive approach helped to manage risks stemming from Indonesia's external vulnerabilities.

We expect Indonesia's current account deficit to shrink in the next few years, reflecting steady global demand and a recovery in its terms of trade. Although Indonesia's terms of trade and overall current account position worsened in 2018, we do not believe this trend is structural in nature. Instead a reversion to the mean will partially fuel a gradual improvement in the country's current account through 2022, especially as its terms of trade normalize. We expect total external debt--net of liquid assets held by the public and financial sectors--to fall to approximately 87% of CAR in

the next three to four years. That said, Indonesia's external debt burden has risen over the past five years. Gross external debt amounted to more than one-third of GDP at the end of 2018. CAR will need to grow faster in order to materially improve the ratio of external debt to GDP.

The degree of support for exports stemming from currency depreciation has its limits, given Indonesia is a significant exporter of commodities, which are generally priced in global markets. Nevertheless, the rupiah's flexibility should provide some benefit to Indonesia's external metrics over the next three to five years. At the same time, that flexibility has allowed the central bank to maintain ample foreign exchange reserves. Together with prudential policy measures to manage the risks of private sector short-term external borrowing, gross external financing needs (current account payments plus short-term external debt) should decline to approximately 96% of CARs plus useable reserves by 2022, versus just above 100% in 2019.

We do not believe Indonesia faces extraordinary risk of a marked deterioration in the cost of external financing, based on its sustained strong access to the markets and foreign direct investment over the recent years, even during periods of acute external volatility.

Key Statistics

Table 1 | [Download Table](#)

Indonesia--Selected Indicators										
Economic indicators (%)	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Nominal GDP (bil. LC)	9,546,134	10,569,705	11,526,333	12,401,729	13,587,213	14,837,358	16,160,490	17,672,642	19,337,057	21,091,123
Nominal GDP (bil. \$)	913	891	861	932	1,015	1,042	1,132	1,216	1,357	1,496
GDP per capita ('000s \$)	3.6	3.5	3.3	3.6	3.8	3.9	4.2	4.5	4.9	5.4
Real GDP growth	5.6	5.0	4.9	5.0	5.1	5.2	5.2	5.2	5.5	5.5
Real GDP per capita growth	4.2	3.7	3.6	3.8	3.9	4.1	4.1	4.2	4.5	4.5
Real investment growth	5.0	4.4	5.0	4.5	6.2	6.7	6.4	5.7	5.8	5.7
Investment/GDP	34.4	34.2	32.4	31.9	32.6	35.2	35.5	35.1	34.8	34.8
Savings/GDP	31.3	31.1	30.4	30.1	31.0	32.2	32.9	32.7	32.5	32.5
Exports/GDP	21.4	21.0	18.5	16.4	17.6	18.3	17.7	17.7	17.1	16.7

Real exports growth	3.8	0.8	(2.5)	(2.5)	9.3	6.5	5.0	5.0	5.0	5.3
Unemployment rate	6.2	5.9	6.2	5.6	5.5	5.3	5.1	5.2	5.0	4.6
External indicators (%)										
Current account balance/GDP	(3.2)	(3.1)	(2.0)	(1.8)	(1.6)	(3.0)	(2.5)	(2.3)	(2.3)	(2.3)
Current account balance/CARs	(13.5)	(13.1)	(9.5)	(9.3)	(7.7)	(13.5)	(12.0)	(11.1)	(11.3)	(11.5)
CARs/GDP	23.7	23.6	21.4	19.5	20.7	22.1	21.2	21.0	20.2	19.7
Trade balance/GDP	0.6	0.8	1.6	1.6	1.9	(0.0)	0.5	0.8	0.7	0.7
Net FDI/GDP	1.3	1.7	1.2	1.7	1.8	1.3	1.5	1.5	1.5	1.5
Net portfolio equity inflow/GDP	1.2	2.9	1.9	2.0	2.1	0.9	1.5	1.5	1.5	1.5
Gross external financing needs/CARs plus usable reserves	96.3	99.8	93.8	94.2	92.1	96.0	100.1	97.8	97.3	96.4
Narrow net external debt/CARs	72.6	81.6	104.3	100.0	94.0	99.3	96.3	93.2	89.5	86.6
Narrow net external debt/CAPs	64.0	72.2	95.3	91.5	87.2	87.5	86.0	83.9	80.4	77.7
Net external liabilities/CARs	187.2	201.2	226.1	206.9	175.7	169.9	174.1	173.7	172.5	172.0
Net external liabilities/CAPs	165.0	177.9	206.5	189.2	163.1	149.7	155.6	156.3	155.0	154.3

[illegible]

CPI growth	8.4	8.4	3.4	3.0	3.6	3.1	3.7	3.6	3.3	3.4
GDP deflator growth	5.0	5.4	4.0	2.4	4.3	3.8	3.5	3.9	3.7	3.4
Exchange rate, year-end (LC/\$)	12,189	12,440	13,795	13,436	13,548	14,481	14,400	14,437	14,166	14,053
Banks' claims on resident non-gov't sector growth	20.8	12.3	9.0	9.3	7.9	12.5	9.0	10.0	10.0	10.0
Banks' claims on resident non-gov't sector/GDP	36.8	37.3	37.3	37.9	37.4	38.5	38.5	38.7	38.9	39.3
Foreign currency share of claims by banks on residents	11.8	11.0	10.3	9.4	9.2	9.8	13.0	13.0	13.0	13.0
Foreign currency share of residents' bank deposits	18.4	17.1	17.3	15.7	14.7	15.0	16.4	16.4	16.4	16.4
Real effective exchange rate growth	(3.3)	(6.4)	2.1	4.1	1.6	(6.0)	N/A	N/A	N/A	N/A

Definitions: Savings is defined as investment plus the current account surplus (deficit). Investment is defined as expenditure on capital goods, including plant, equipment, and housing, plus the change in inventories. Banks are other depository corporations other than the central bank, whose liabilities are included in the national definition of broad money. Gross external financing needs are defined as current account payments plus short-term external debt at the end of the prior year plus nonresident deposits at the end of the prior year plus long-term external debt maturing within the year. Narrow net external debt is defined as the stock of foreign and local currency public- and private- sector borrowings from nonresidents minus official reserves minus public-sector liquid assets held by nonresidents minus financial-sector loans to, deposits with, or investments in nonresident entities. A negative number indicates net external lending. N/A--Not applicable. LC--Local currency. CARs--Current account receipts. FDI--Foreign direct investment. CAPs--Current account payments. e--Estimate. f--Forecast. The data and ratios above result from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. Sources: Bank Indonesia Official Web Site - Bank Sentral Republik Indonesia (Economic/Monetary/External /Debt Indicators), International Monetary Fund (Monetary/Fiscal Indicators), Directorate General of Budget Financing and Risk Management Ministry of Finance (Fiscal/Debt Indicators)

Ratings Score Snapshot

Table 2 | [Download Table](#)

Indonesia--Ratings Score Snapshot		
Key rating factors	Score	Explanation
Institutional assessment	3	Generally effective policymaking promoting balanced economic growth and sustained public finances. Moderate policy predictability, with possible policy shifts with changes in administration. Generally cohesive society. Significant jump in "Doing Business" ranking in recent years. However, corruption still remains high.
Economic assessment	4	Based on GDP per capita (US\$) and growth trends as per Selected Indicators in table 1.
		Weighted average real GDP per capita trend growth over a 10-year period is well above that of sovereigns in the same GDP category.
External assessment	3	Based on narrow net external debt and gross external financing needs as per the Selected Indicators table above.
Fiscal assessment: flexibility and performance	3	Based on the change in net general government debt (% of GDP) as per Selected Indicators table above.
		The sovereign faces shortfalls in basic services and infrastructure, as reflected, for instance, by its low ranking on the U.N. Development Program's human development index.
Fiscal assessment: debt burden	2	Based on net general government debt (% of GDP) and general government interest expenditure (% of general government revenue) as per Selected Indicators table.
		Over 40% of gross government debt is denominated in foreign currency.
Monetary assessment	3	The rupiah is a free-floating currency. However, the central bank intervenes intermittently in foreign exchange markets.
		The central bank has operational independence and uses market-based monetary instruments such as 7-Day Repo Rate; CPI as per Selected Indicators in table 1. The central bank has the ability to act as lender of last resort for the financial system. Depository corporation claims on residents in local currency and nonsovereign local currency bond market capitalization combined amount to about 45% of GDP.
Indicative rating	bbb	As per table 1 of "Sovereign Rating Methodology."
Notches of supplemental adjustments and flexibility	0	
Final rating		
Foreign currency	BBB	

Notches of uplift	0	Default risks do not apply differently to foreign- and local-currency debt.
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Local currency	BBB
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S&P Global Ratings' analysis of sovereign creditworthiness rests on its assessment and scoring of five key rating factors: (i) institutional assessment; (ii) economic assessment; (iii) external assessment; (iv) the average of fiscal flexibility and performance, and debt burden; and (v) monetary assessment. Each of the factors is assessed on a continuum spanning from 1 (strongest) to 6 (weakest). S&P Global Ratings' "Sovereign Rating Methodology," published on Dec. 18, 2017, details how we derive and combine the scores and then derive the sovereign foreign currency rating. In accordance with S&P Global Ratings' sovereign ratings methodology, a change in score does not in all cases lead to a change in the rating, nor is a change in the rating necessarily predicated on changes in one or more of the scores. In determining the final rating the committee can make use of the flexibility afforded by §§15 and §§126-128 of the rating methodology.

Related Criteria

- [Criteria | Governments | Sovereigns: Sovereign Rating Methodology](#), Dec. 18, 2017
- [General Criteria: Methodology For Linking Long-Term And Short-Term Ratings](#), April 7, 2017
- [General Criteria: Use Of CreditWatch And Outlooks](#), Sept. 14, 2009
- [General Criteria: Methodology: Criteria For Determining Transfer And Convertibility Assessments](#), May 18, 2009

Related Research

- [Sovereign Ratings List](#), May 6, 2019
- [Sovereign Ratings History](#), May 6, 2019
- [Sovereign Ratings Score Snapshot](#), May 3, 2019
- [Sovereign Risk Indicators](#), April 12, 2019; a free interactive version is available at <http://www.spratings.com/sri>
- [Default, Transition, And Recovery: 2018 Annual Sovereign Default And Rating Transition Study](#), March 16, 2019
- [Asia-Pacific Sovereign Rating Trends 2019](#), Jan. 15, 2019
- [Global Sovereign Rating Trends 2019](#), Jan. 14, 2019

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

[Download Table](#)

Upgraded

	To	From
Indonesia		
Sovereign Credit Rating	BBB/Stable/A-2	BBB-/Stable/A-3

Transfer & Convertibility Assessment

Local Currency	BBB+	BBB
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Indonesia

Senior Unsecured	BBB	BBB-
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Perusahaan Penerbit SBSN Indonesia III

Senior Unsecured	BBB	BBB-
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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

Media Contacts:

Chris Gle Davis, Hong Kong (852) 2533-3511
chris.g.davis@spglobal.com

Richard Noonan, Melbourne (613) 9631-2152
richard.noonan@spglobal.com

Analyst Contacts:

Andrew Wood, Singapore + 65 6239 6315
KimEng Tan, Singapore (65) 6239-6350