Domestic focus : lesson learnt from recent macro trends

Key Takeaways

- We identify 7 domestic macro trends throughout 2022, they are : 1) recovery momentum continued in 3Q22; 2) volatile food prices drop help to lower inflation in Oct-22; 3) IDR experiences a persistent pressure from Fed aggressive rate hikes; 4) risk of FX liquidity dry-up that needs to be anticipated; 5) policy makers aims to have a soft landing strategy through pro-growth, pro-stability policy; 6) equity & government bond market continued to diverge; 7) a more resilient corporate bond market.

- Our guidance : IDR may still continue to depreciate further as commo prices slowing and stability depends on how BI manage narrowed nominal interest rate differential. Key focus on government bond will be fiscal consolidation & how BI engineer yield curve., while for corporate bond mainly on refinancing needs and higher cost of fund. In addition, in the equity market expect for slower revenue growth & lower margin, as well as more conservative stance on capex next year. Deleveraging story could favor resilience, we recommend to stay defensive amidst highly volatile market by focusing on companies that have ample liquidity. Recent trend may revert next year with banking taking a more conservative guidance on LDR and lower coal price possibly trigger revenue contraction for FY23F.

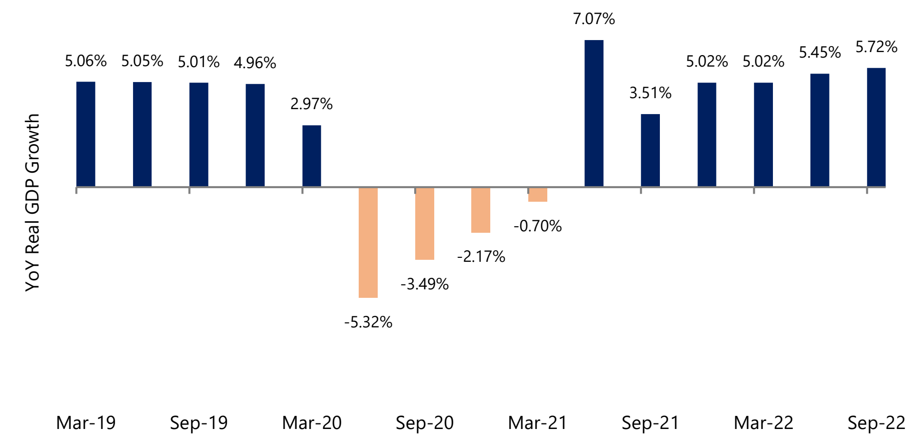
Victoria Venny N.S
Head of Research
victoria.nawang@mncgroup.com

Tirta Widi Gilang Citradi
Economist & Fixed Income Analyst
tirta.citradi@mncgroup.com

Macro trend 1 : recovery momentum continued

Indonesia's GDP expanded +5.72% YoY, higher than our & consensus estimate of +5.66% YoY/+5.60% YoY in 3Q22. Economic output grew at the fastest pace for over a year, marking recovery momentum continued. Firm consumption & investment (+5.39% YoY & +4.96% YoY) could offset lower government expenditure (-2.88% YoY). On the other hand, robust exports performance continued despite lower trade surplus (USD14.92bn in 3Q22 vs USD15.61bn in 2Q22), largely driven by rising imports. Cumulatively domestic output rose +5.40% throughout 9M22. We expect a more normalized growth in 4Q22 on the back of seasonality factor & weakening momentum due to the uptick of inflation. However, given the adequate fiscal space (+0.33% GDP as of Oct-22 vs -3.92% GDP FY22E), government may boost spending to promote growth in the last quarter. Hence, we maintain our forecast for GDP growth at 5.00-5.20% FY22E.

Exhibit 1. Indonesia's output back to its growth trajectory of 5% YoY

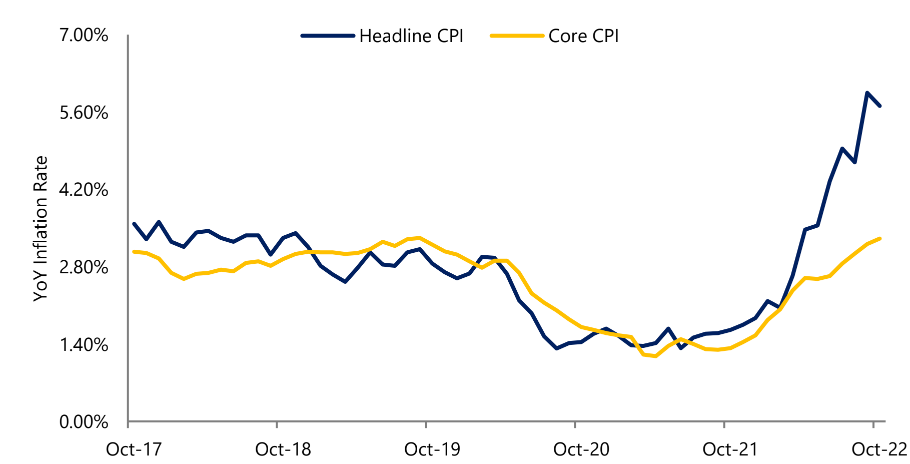


Source : Statistic Indonesia, MNCS Research

Macro trend 2 : volatile food prices drop help to lower inflation

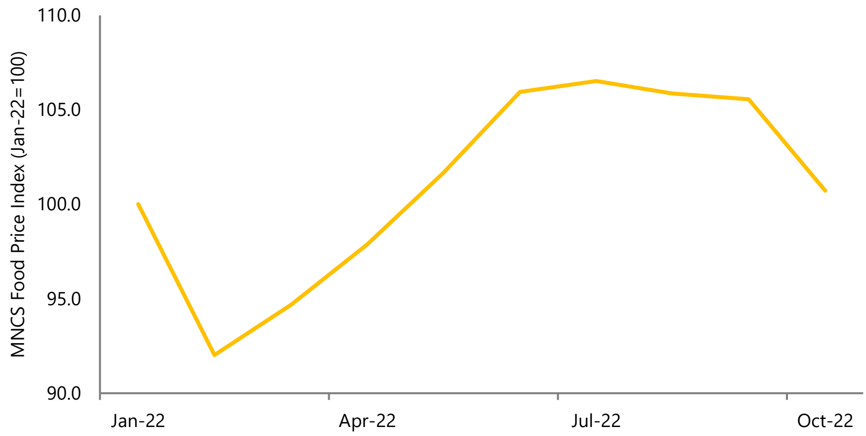
Indonesia recorded a deflation in Oct-22 (-0.11% MoM). Headline CPI increased +5.71% YoY (vs +5.95% YoY in the previous month). Administered prices remained elevated 2 months post subsidized fuel prices adjustment (+30%), largely driven by gasoline, household fuel and transport prices. Meanwhile, on the other hand, volatile food prices declined, yet core CPI increased +3.31% YoY in Oct-22 (vs +3.21% YoY in Sep-22). As we are heading to the year-end festive momentum, seasonality factor is expected to play a role in jacking up inflation, thus we maintain our FY22F end-year headline CPI at +6.12% YoY.

Exhibit 2. Slowing inflation in Oct-22



Source : Statistic Indonesia, MNCS Research

Exhibit 3. MNCS Food Price Index declined

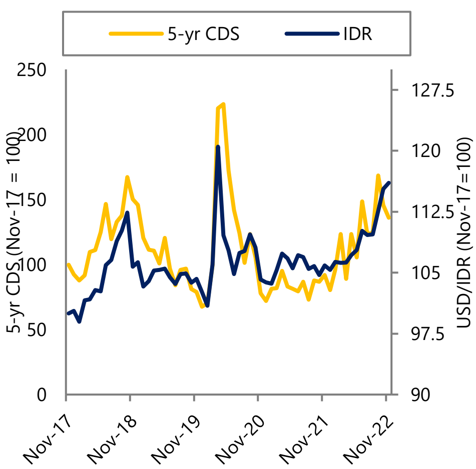


Notes : MNCS Food Price Index was constructed using high frequency data of 10 food staples weighted based on monthly consumption/capita. Sources : PIHPS Nasional, MNCS Research

Macro trend 3 : persistent pressures on IDR

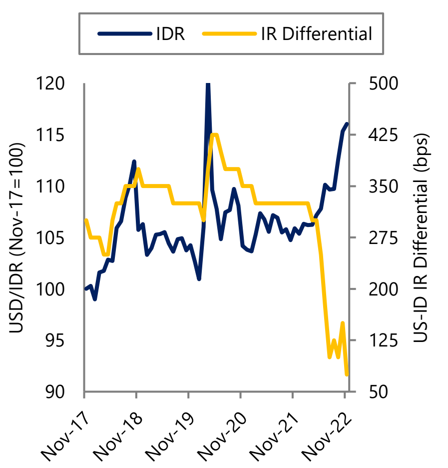
Fed's aggressive rate hikes throughout this year has catapulted DXY index to soar +14.21% YTD causing a steep IDR depreciation (-10.14% YTD). This has forced BI to undertake intervention resulting in FX reserves depletion. As of Oct-22, domestic FX reserves position stood at USD130.2bn, declining -USD600mn from previous month position equivalent to 5.8 months of imports on the back of external debt payment & IDR stabilization. FX reserves position has been consistently on a downward pressure as pressures on IDR lingers. Despite having +144 bps real rate (benchmark policy rate-core CPI) and +125 bps cumulative hikes since Aug-22, IDR still depreciating against USD and now hitting above 15,700/USD due to deteriorating risk perception as well as lower interest rate differential. Prior to pandemic, US-ID interest rate differential was maintained at >300 bps on average (vs now stood at 75 bps only). Therefore, we expect BI to raise another 50-75 bps this year as Fed's Chair Powell has signaled further rate hikes, leaning against pivot narrative.

Exhibit 4. Risk perception deteriorated



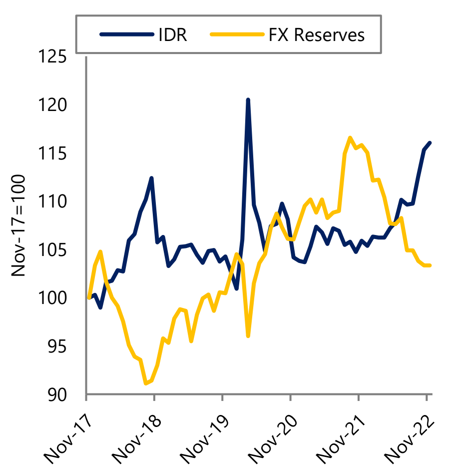
Source : Bloomberg, MNCS Research

Exhibit 5. IR differential decreased



Source : Bloomberg, MNCS Research

Exhibit 6. IDR intervention & lower FX reserves

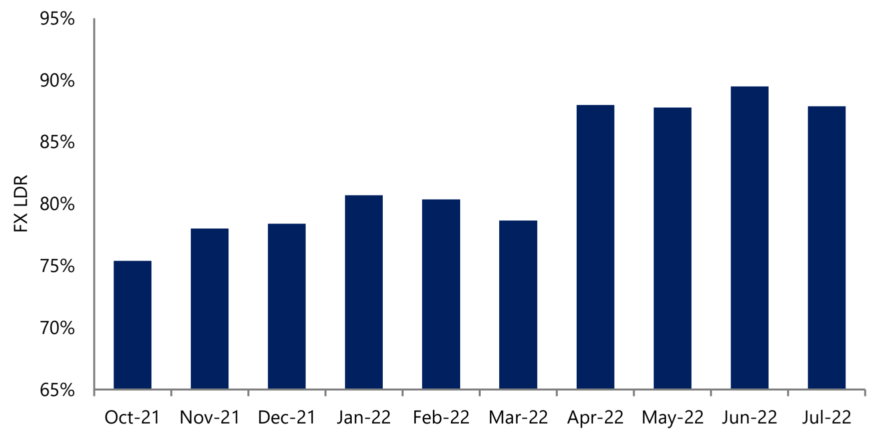


Source : Bloomberg, MNCS Research

Macro trend 4 : dried-up domestic FX liquidity (?)

Recent trend shows FX LDR is approaching its pre-pandemic historic level (88-92%) as FX loan growth has outpaced the deposit growth (FX loan +18.4% YoY; FX deposit +8.4% YoY as of Sep-22). Spook around FX liquidity dried up has attracted attention from analysts & policy makers. We think, several action could be taken to avert such condition by : 1) government issuing global bond; 2) banks seeks external funding and 3) BI enforcing FX receipts from exports. By doing so, further pressures on IDR could be mitigated.

Exhibit 7. FX liquidity in the banking system hitting average historic level



Sources : OJK, MNCS Research

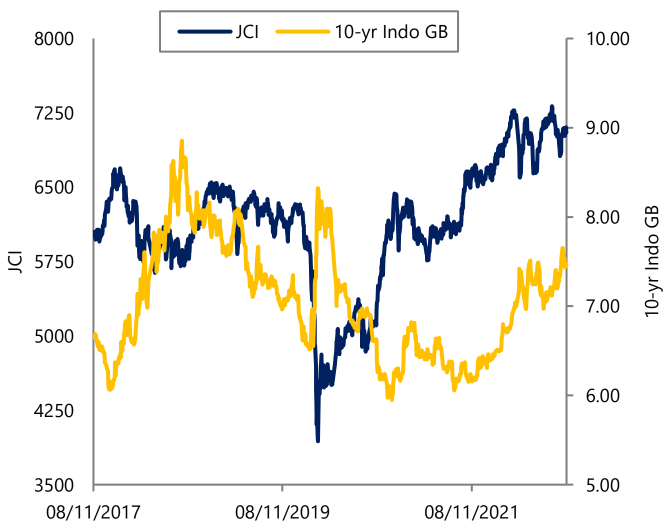
Macro trend 5 : aiming a soft landing through pro-growth & pro-stability policy

Fiscal-monetary policy coordination is crucial to promote growth while maintaining stability at the same time. Indeed, this is not an easy task for policy makers and sounds so ambitious. As government sticks to fiscal consolidation agenda next year, domestic central bank has started policy normalization through rate hikes and raising statutory reserves to anchor inflation. On the other hand, BI has reaffirmed that macro-prudential policy to remain accommodative to promote growth.

Macro trend 6 : equity & government bond market divergence

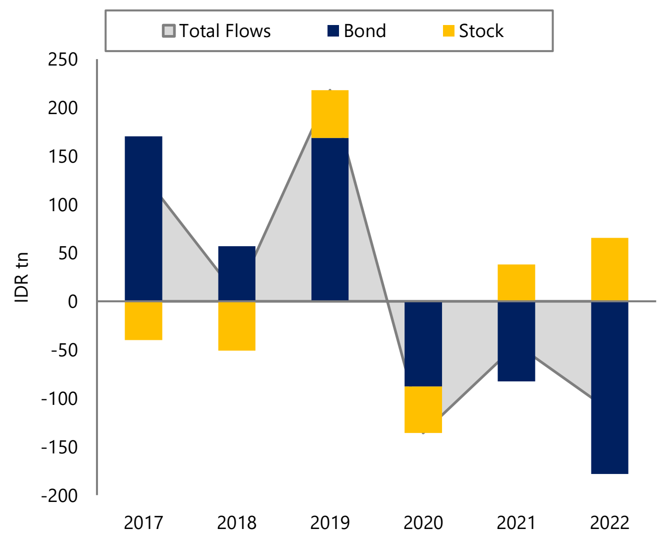
Interesting to note, despite current unfavorable global macro backdrop that trigger nearly all asset class sell off, domestic risky asset proxied by JCI outperformed government bond. JCI has returned +7.12% YTD (vs INDOBeX Clean Price -6.17% YTD). Yield on benchmark 10-year SUN has increased +103bps YTD, while at the same time JCI remained traded near its LT historical average of 15-16x P/E. Valuation wise, equity asset should be less attractive given JCI dividend yield 2.7-3.2% compared 1-year IDR-denominated government bond offering >5% yield. However, unlike in the government bond that experienced massive outflows (>IDR170tn), JCI performance was lifted of by a massive net foreign inflows (>IDR60tn YTD). In addition, companies' financials recorded a solid performance, 41 out of 54 companies under our coverage (~76% MNCS universe) have reported double digit growth, both in top line & bottom line throughout 9M22. Aggregate revenue grew +25% YoY, whilst net income increased +47% YoY. Banks & commodity related sector drive the aggregate earnings this year favored by lower provisioning expense & high commodity prices.

Exhibit 8. JCI & 10-year Indo GB yield movement diverged



Source : Bloomberg, MNCS Research

Exhibit 9. Stock market posted a net inflows, govt bond recorded outflows



Source : Bloomberg, MNCS Research

Exhibit 10. Revenue & net profit of our universe grew double digits

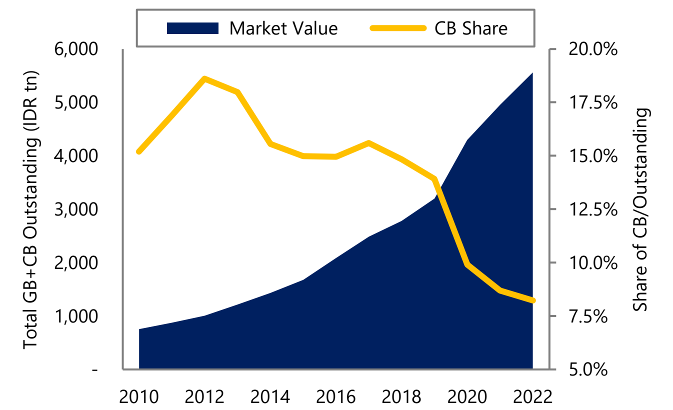
Sectors	Revenue (IDR bn)			Net Profit (IDR bn)		
	9M21	9M22	YoY	9M21	9M22	YoY
Automotive	**178,443**	**234,850**	**32%**	**16,831**	**26,411**	**57%**
ASII	167,402	221,354	32%	16,385	25,579	56%
AUTO	11,041	13,496	22%	446	832	86%
Banking	**170,978**	**211,553**	**24%**	**53,292**	**77,183**	**45%**
ARTO	345	1,036	200%	- 33	41	224%
BBCA	41,934	63,228	51%	23,199	28,955	25%
BBNI	41,504	45,192	9%	7,746	13,692	77%
BMRI	75,381	89,810	19%	19,229	30,653	59%
BNGA	11,813	12,288	4%	3,150	3,843	22%
Telco	**125,843**	**130,469**	**4%**	**19,888**	**17,562**	**-12%**
TLKM	106,043	108,874	3%	18,872	16,581	-12%
EXCL	19,800	21,595	9%	1,016	981	-3%
Toll Road & Utilities	**44,953**	**51,939**	**16%**	**5,107**	**5,735**	**12%**
JSMR	10,632	11,721	10%	749	1,007	34%
PGAS	34,321	40,218	17%	4,358	4,728	8%
Consumers	**32,806**	**34,153**	**4%**	**5,244**	**5,332**	**2%**
UNVR	30,030	31,539	5%	4,379	4,611	5%
SIDO	2,776	2,614	-6%	865	720	-17%
Healthcare	**15,178**	**13,596**	**-10%**	**2,188**	**1,439**	**-34%**
SILO	7,144	6,931	-3%	532	449	-16%
HEAL	4,627	3,591	-22%	773	246	-68%
MIKA	3,407	3,073	-10%	883	744	-16%
Retail	**18,660**	**26,007**	**39%**	**342**	**2,147**	**527%**
ACES	4,601	4,783	4%	323	352	9%
MAPI	12,080	18,821	56%	- 83	1,497	1893%
RALS	1,978	2,403	21%	103	298	190%
Construction	**25,688**	**32,899**	**28%**	**321**	**587**	**83%**
ADHI	7,351	9,133	24%	17	21	24%
PTPP	11,212	13,462	20%	129	141	9%
WSKT	7,125	10,304	45%	174	425	144%
Property	**20,701**	**24,336**	**18%**	**3,473**	**4,712**	**36%**
BSDE	5,167	7,146	38%	931	918	-1%
PWON	3,788	4,495	19%	722	1,191	65%
SMRA	3,790	4,212	11%	170	310	82%
CTRA	6,649	7,227	9%	1,015	1,525	50%
DMAS	1,307	1,256	-4%	635	768	21%
Agriculture	**23,067**	**23,103**	**0%**	**1,885**	**2,109**	**12%**
AALI	18,014	16,517	-8%	1,469	1,216	-17%
DSNG	5,053	6,586	30%	416	893	115%
Coal Mining	**58,495**	**121,096**	**107%**	**11,176**	**38,981**	**249%**
ADRO	39,113	90,025	130%	6,408	28,979	352%
PTBA	19,382	31,071	60%	4,768	10,001	110%
Metal Mining	**10,451**	**13,303**	**27%**	**1,872**	**2,564**	**37%**
INCO	10,451	13,303	27%	1,872	2,564	37%
Poultry	**70,397**	**80,232**	**14%**	**4,183**	**4,614**	**10%**
CPIN	37,593	43,439	16%	2,676	3,186	19%
JPFA	32,803	36,793	12%	1,507	1,428	-5%
Cigarette	**164,590**	**177,318**	**8%**	**9,689**	**6,400**	**-34%**
GGRM	92,071	93,919	2%	4,135	1,498	-64%
HMSP	72,519	83,398	15%	5,554	4,902	-12%
Cement	**35,939**	**36,942**	**3%**	**2,596**	**2,597**	**0%**
INTP	10,609	11,661	10%	1,208	947	-22%
SMGR	25,330	25,281	0%	1,388	1,650	19%
Basic & Chemicals	**1,885**	**2,003**	**6%**	**347**	**458**	**32%**
ARNA	1,885	2,003	6%	347	458	32%
Heavy Equipment	**75,072**	**126,115**	**68%**	**8,614**	**17,431**	**102%**
UNTR	57,822	91,533	58%	7,817	15,867	103%
AKRA	17,250	34,582	100%	797	1,564	96%
Total	**1,073,146**	**1,339,914**	**25%**	**147,050**	**216,260**	**47%**

Source : Bloomberg, MNCS Research

Macro trend 7 : corporate bond offer low risk investment

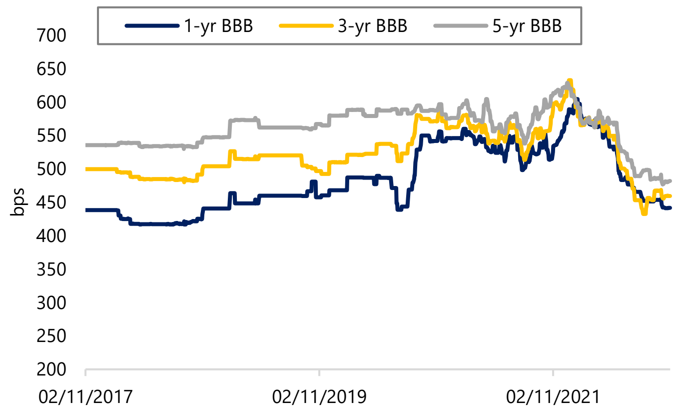
Corporate bond issuance has risen throughout 2022. We estimate corporate bond issuance to hit above IDR140tn this year, yet the market share still below 10%. Albeit posing higher liquidity risk in the secondary market, corporate bond still outperformed government bond on a clean price basis (INDOBeX Corporate Clean Price -2.99% YTD vs INDOBeX Government Clean Price -6.17% YTD). In addition, credit spread matrix remains narrow, even for BBB-rated bonds. We believe the outperformance was partly due to a more attractive investment thesis (higher coupon rates, YTM and offer shorter duration amidst rising interest rate risk).

Exhibit 11. Market share of corporate bond declined



Source : IDX, MNCS Research

Exhibit 12. Credit spread remains narrow even for BBB-rated companies



Source : Bloomberg, IBPA, MNCS Research

Exhibit 13. Corporate bonds offer higher coupon & YTM while at the same time having shorter duration than government bond

	No of Bonds	Mkt Value (IDR tn)	Index Weight	Avg Coupon	Avg YTM	Avg Duration
Composite	574	4,351	100%	7.36%	7.31%	5.58
Government	80	4,041	93%	7.29%	7.29%	5.79
>Conventional	50	3,292	76%	7.41%	7.38%	5.75
>Sukuk	30	749	17%	6.73%	6.89%	5.95
Corporate	494	310	7%	8.36%	7.65%	2.87
>Conventional	433	294	7%	8.33%	7.63%	2.84
>Sukuk	61	16	0%	8.97%	8.08%	3.46
Corporate by Rating						
>AAA	216	156	4%	7.94%	7.15%	3.13
>AA	128	75	2%	8.24%	7.56%	2.77
>A	128	72	2%	9.19%	8.50%	2.47
>BBB	22	7	0%	10.45%	11.17%	2.09

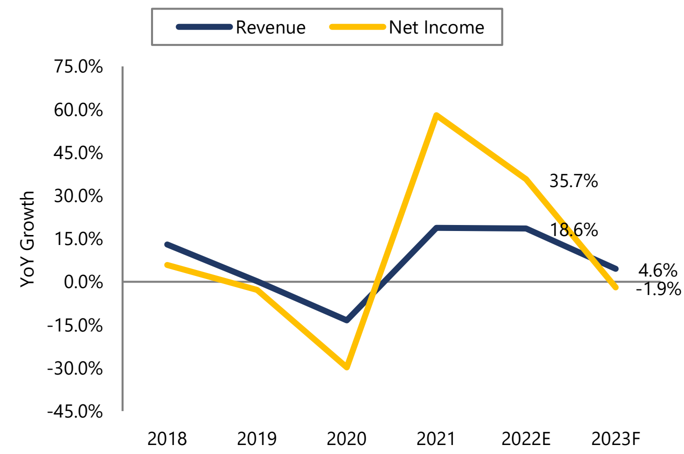
Source : IBPA, MNCS Research

Guidance

- **IDR** : currency stability will still matters. Note that IDR depreciation against USD was relatively manageable than peers. Yet we still believe, IDR stability will depend on how BI manage such a narrow nominal interest rate differential to US and lower domestic FX liquidity condition. On the other hand, declining commodity prices may also put some pressure on IDR as current CA surplus possibly reverts next year (+0.3% GDP FY22E vs -1.5% GDP FY23E). Any pivot narrative from Fed should provide pressure relieve for IDR, though room for further depreciation still widely open in our view (our base target for FY22E at IDR15,425/USD & FY23F at IDR15,550/USD).
- **Bonds** : ensuring smooth fiscal consolidation will play a key role in managing supply side risk as well as sovereign rating affirmation. Besides that, government bond asset will also depend on how BI engineer the yield curve providing attractive short end as well as belly to buy . Besides that, for corporate bonds refinancing needs may increase amidst monetary policy normalization. For issuers this may increase cost of financing, while for investors may take this opportunity to diversify. Our guidance still favor investment grade corporate bond, with fair forward yield for AAA-rated companies should be at 7.8% for 3-year maturity & 8.5% for 5-year maturity.

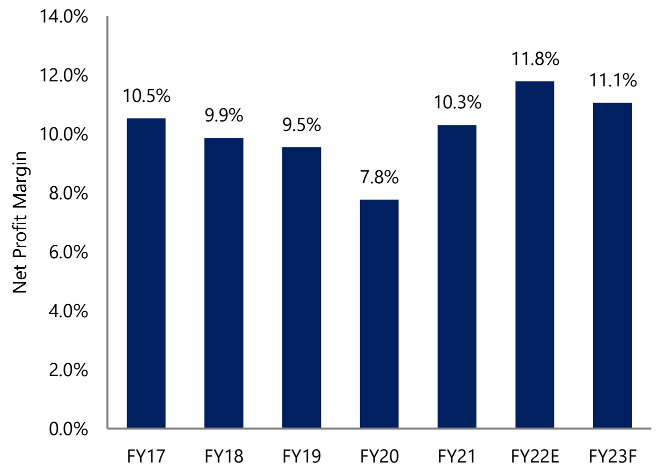
- **Equity** : key downside risks for JCI valuation : a more normalized top line growth but contracted bottom line as margin decrease. As economic uncertainty linger, consensus expect companies to build up a free cash flow which means they are more conservative on capex. Wee see that companies in our universe (~61% JCI weight) have been deleveraging, thus we expect risk during tightening could be contained. We recommend to stay defensive in equity. Our FY22E target at 7,006 implying 14.12x P/E, whilst for FY23E we forecast JCI target for bear case at 6,860 (13.90x P/E) and bull case at 7,554 (14.37x P/E), indicating a minimum decline to moderate growth aggregate EPS -2% to 6% on a YoY basis. Expect companies with ample FCF & lower leverage ratio to be more resilient. We expect banking asset growth to be more limited as they take a more conservative LDR while for commodity related sector possibly experience revenue contraction.

Exhibit 14. Consensus expect moderate rev & NP contraction MNC universe



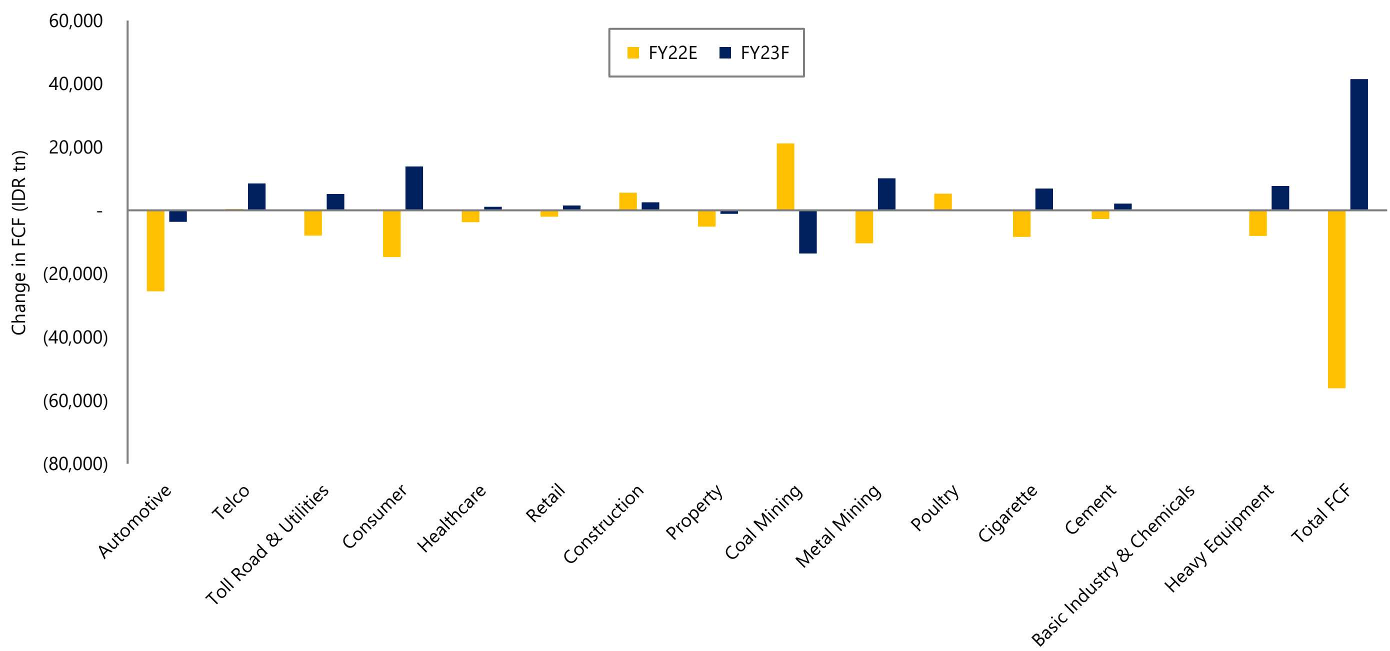
Note : non-bank MNCS Universe. Source : Bloomberg, MNCS Research

Exhibit 15. Consensus expects for lower margin



Note : non-bank MNCS Universe. Source : Bloomberg, MNCS Research

Exhibit 16. Consensus expects companies to be more conservative on capex and accumulating cash flow during tightening



Source : Bloomberg, MNCS Research

Exhibit 17. Deleveraging continues, expect to be more resilient during rate hikes

Source : Bloomberg, MNCS Research

MNC Research Industry Ratings Guidance

OVERWEIGHT: Stock's total return is estimated to be above the average total return of our industry coverage universe over next 6-12 months

NEUTRAL: Stock's total return is estimated to be in line with the average total return of our industry coverage universe over next 6-12 months

UNDERWEIGHT: Stock's total return is estimated to be below the average total return of our industry coverage universe over next 6-12 months

MNC Research Investment Ratings Guidance

BUY : Share price may exceed 10% over the next 12 months

HOLD : Share price may fall within the range of +/- 10% of the next 12 months

SELL : Share price may fall by more than 10% over the next 12 months

Not Rated : Stock is not within regular research coverage

PT MNC SEKURITAS
MNC Financial Center Lt. 14 – 16
Jl. Kebon Sirih No. 21 - 27, Jakarta Pusat 10340
Telp : (021) 2980 3111
Fax : (021) 3983 6899
Call Center : 1500 899