OUTLOOK INDONESIA

MONTHLY UPDATE- FEBRUARY 2020

FROM THE AMERICAN INDONESIAN CHAMBER OF COMMERCE

Highlights

❖ Issue To Watch: Salvage Job

Commentary by Wayne Forrest

Building Indonesia's new capital in East Kalimantan may turn out to be easier than preserving its current capital. However, the "capital" I mean is what has been invested in Indonesia's state-owned insurance and pension system, not Jakarta, a city sinking due to ground water loss and climate change. Once again a major scandal, involving at least $1 billion in losses at the state-owned life insurer PT Jiwasraya, has emerged with possible systemic risks to Indonesia's financial system as well as the potential for politicization reminiscent of the $700 million Bank Century scandal of 2008. Jiwasraya made high risk investments with its 17,000 customers' capital in mutual funds offered by a highly suspicious company promising 12% annual returns. In effect, it was a state-run "ponzy" scheme. A similar scandal is brewing at the Armed Forces Social Insurance fund, also a life insurance investment program. Losses are estimated between $700 million and $1.2 billion. Each of these bankruptcies alone are staggering numbers for an emerging economy.

The funds in many of these enterprises are often accrued by payroll deductions with a lack of transparency regarding benefits. In the 1990's AICC had a corporate member, ASI, skilled in actuarial sciences, that was invited to help President Soeharto create a modern social security system by restructuring the death benefit company PT Astek. In reviewing Astek's books, ASI was astounded to learn that less than 2% of its accrued funds were paid out in any year as survivors' death benefits. Plagued by years of mismanagement and corruption, Astek had a poor record paying claims and worse, had little to no outreach to educate policy holders and beneficiaries. ASI's project was ultimately scrapped by the 1998 Asian Financial Crisis.

The $700 million Bank Century bailout plagued the SBY administration. To this day accusations remain that President SBY, Vice President Boediono and Finance Minister Sri Mulyani made decisions that favored Bank Century's well-connected depositors and some go as far as to accuse them of personally benefiting, charges that were never substantiated. But in the face of the global unwinding of 2008, the bailout was justified and eventually investigations by the anti-corruption commission (KPK) led to arrests and convictions of the bank's owners as well as a central bank deputy governor.

Although arrests have been made in the Jiwasraya case and the new state-owned enterprises minister, Erik Thohir, has begun to discuss a bailout plan, details have yet to be released and rumors are already circulating that "higher ups" are being protected. The attorney general is leading the criminal investigation of Jiwasraya in coordination with the KPK, now operating under the new law. Both entities are pursuing leads, identifying and interrogating suspects. This a positive sign, however, Parliament's relegation of its own inquiry to a low-level committee rather than a full inquiry raises concerns that independent oversight to guard against a cover-up may never materialize. The scandal also sheds a negative light on the Financial Services Authority (OJK) and its anemic monitoring/compliance efforts. These must be revamped.

In a nation struggling to modernize its capital markets, lower risk premiums, and attract direct investment, revelations such as these are very disturbing and need to be addressed swiftly with transparency not just for the unfortunate customers whose retirement incomes are threatened but for investors (local and foreign) in general.

Chances are there may be more Jiwasrayas with the same ability to flood Indonesia's capital markets with uncertainty and higher risk. This capital, however, cannot be moved to Kalimantan.

(The opinions expressed here are solely the writer's and do not necessarily reflect those of the American Indonesian Chamber of Commerce or its members.)

UPCOMING/RECENT EVENTS

December 5th, 2019

New Directions in Indonesia's Investment and Tax Policies

Click Here For Notes

INDICATORS

US$= 13,662
JSX= 5940(last)
BI Rate: 5%
Inflation: 2.72%
Reserves: $129.18 billion

(source: Bank Indonesia)
JSX= Jakarta Stock Exchange

THIS WEEK IN INDONESIAN HISTORY

1950

US Ex-Im Bank loans $100 million to Indonesia

Economy and Business:

• Economic Risks of Coronavirus

The government believes the spreading coronavirus in China will add to downside risks and uncertainties in the domestic economy as Indonesia's largest trading partner braces for a blow to its economic growth. The Chinese New Year, which took place in January, should have given momentum to China's economy, Sri Mulyani has told lawmakers. "The outbreak has resulted in the country failing to realize its economic potential." Each percentage-point decline in China's growth rate results in a 0.3 percent drop in Indonesia's, the World Bank has said. "For now, the biggest battle is to keep investors' trust in the country's economy amid uncertainties and lower confidence," Sri Mulyani said. "We must first prepare policy instruments to mitigate the risks and maintain economic stability." Apart from the coronavirus, global manufacturing disruption and geopolitical tensions have also become sources of global economic uncertainty, said Coordinating Economic Minister Airlangga Hartarto. "The challenges to the global situation will continue in 2020 despite easing trade tensions," Airlangga added. *(Jakarta Post)*

• Chinese Digital Payment Companies Enter Indonesian Market

Bank Indonesia, the country's central bank, has told Chinese digital wallet company Alipay to rework their application for operating a payment service in Indonesia in collaboration with state-controlled lenders Bank Mandiri and Bank Rakyat Indonesia. Alipay and rival WeChat Pay have made public their plans to operate in Indonesia last year. Today, only the latter has managed to make the incursion into the key market, which is expected to make up a lion's share of Southeast Asia's $1 trillion digital payment market in the next five years according to a joint study from Google, Temasek and Bain & Company. BI Governor Perry Warjiyo said foreign digital wallet companies wanting to roll out operations in Indonesia must use the rupiah currency and the QR Indonesia Standard (QRIS), the local standard quick response code used in digital transactions. The code often appears as a small square filled with randomly-placed black and white rectangles. "Fintech companies must use QRIS. If you don't use QRIS, we will ban and shut down your system," Perry said. "We want the fintech and banking systems to be connected. We encourage an open banking and fintech infrastructure so we can connect all payment transactions. It's easy to do that now with the Open Application Programming Interface [API]," he said. So far, WeChat Pay is the only foreign digital wallet service that has been able to obtain permission from BI to operate in Indonesia through a partnership with Bank CIMB Niaga. *(Jakarta Globe)*

• Insurance Ownership Rules Changed

Indonesia now allows foreign investors to own more than 80 percent of shares in locally-listed insurance companies, loosening a rule that has for a long time stopped foreign insurance companies from expanding their business in Indonesia. Under previous regulations, the government capped foreign ownership at 80 percent, undermining the insurers' ability to expand. Foreign investors have long lobbied the government to change the rule, arguing they had not been able to inject new capital when the time came for expansion. Their local partners, more often than not, did not have enough money to keep their ownership from being diluted.

The rule also drops the requirement for a local partner, which, according to the old rule, had to be a locally-based entity wholly controlled by Indonesian citizens. Dody Dalimunthe, the executive director of the Indonesian General Insurance Association (AAUI), welcomed the new rule, saying foreign investors' local partners are often individuals with either shallow pockets or little expertise to commit more capital in the insurance industry. *(Editor's Note: Indonesia has been rocked by the insolvency of state-owned insurance company, Jawisraya, which may have contributed to the change.)*

• Indonesia Poised To Enter Golden Age: HSBC Report

Despite the forecast of slow global economic growth in 2020, Southeast Asia, including Indonesia, is expected to enter an economic golden age that will take the region well on the path to become the world's fourth-largest economic bloc in the next decade. HSBC Private Banking's chief market strategist for Southeast Asia, James Cheo, said he is convinced the region could ride out the current global slowdown and soon catch up with the world's economic powerhouses. "The most exciting story, if we look at the next decade, is Southeast Asia. The next ten years could very well be the region's golden age because if it continues to grow, say, at its current pace, it can become the fourth largest economic bloc, behind the US, Europe and China," Cheo said to the Jakarta Globe. Cheo pointed out there are at least three supporting factors behind Southeast Asia's economic rise.

- First is the demographic bonus that many countries in the region are already enjoying. "Sixty percent of Southeast Asians are under the age of 35. In the next ten years, they will come of age: they'll start working and get their first paycheck. They will increase their purchases. They'll buy cars. They'll get married and buy a house. They'll have kids and spend more money on education, and of course, they'll travel to see the world," Cheo said.
- Second, urbanization is getting more widespread in Southeast Asia, not only in big metropolitans but also in second-tier cities.
- The third is the fact that Southeast Asia is "more digital" than the rest of the world.

According to Chao there are several investment sectors with bright potentials in Indonesia this year. The first is consumption – the backbone of global economic growth. The next one is infrastructure, currently one of the Indonesian government's priority sectors. Cheo noted the increase in infrastructural spending is not only happening in Indonesia but also in other Southeast Asian countries, including Malaysia and Thailand. Sweeping regulatory reforms – especially in taxation and labor laws – promised by the Indonesian government, Cheo said now is the right time to push through significant changes. However, he warned foreign investors not to expect a complete overhaul of local bureaucracy, though they should still see the government's insistence on reform as a sign of good things to come.

• World Bank Predicts 5.1% GDP Growth

Indonesia's economy is expected to perform slightly better in 2020 on the back of improved commodity prices and easing external pressures, economists have said. In its latest Global Economic Prospect report, the World Bank forecast Indonesia would book 5.1 percent gross domestic product (GDP) growth in 2020 and 5.2 percent in 2021. The figures were 0.2 percent lower compared with its June 2019 projection. "Growth in Indonesia, which depends less on export growth than other regional economies, is projected to tick up to 5.1% [in 2020] reflecting continued support from private consumption, a pickup in investment, growth of the working-age population and improving labor markets," the Washington-based development bank wrote in a statement. Global growth, meanwhile, was set to pick up by 2.5 percent this year, higher than the 2.4 percent projected for 2019, driven by higher growth in emerging markets and developing economies, amid a recovery in global trade and investment. (*Editor's Note: Indonesia's former Minister of Trade. Mari Pangestu has been appointed the World Bank's Managing Director for Development Policy and Partnerships)*

❖ Politics, Law, and Security:

• Screening for Coronavirus

Health inspectors at Jakarta's Soekarno-Hatta International Airport started screening passengers for coronavirus after the Indonesian government issued a limited travel warning to China on Tuesday. All arriving passengers now have their body temperature checked twice before they leave the airport. *(Editor's Note: To date, Indonesia has issued a travel warning rather than an outright ban. It is monitoring closely what other countries are doing.)*

• Suspects Arrested in Jiwasraya Case

The Attorney General's Office says corruption has left state-owned life insurer Asuransi Jiwasraya on the brink of bankruptcy and names five suspects in the case, including former executives and a prominent local investor. The AGO on Tuesday detained Benny Tjokrosaputro, the commissioner of Hanson International, for his alleged involvement in the insurer's crooked investments, which have caused losses of Rp 13.7 trillion ($1 billion) to the state. Since Jiwasraya is a state-owned company, the losses automatically lead to a charge of corruption under the anti-corruption law. *(Jakarta Globe)*

• Armed Forces Social Insurance Graft

The National Police have opened an inquiry into allegations of corruption in the Indonesian Armed Forces Social Insurance, or Asabri, taking the lid off another potential scandal in a financial industry already ridden with billion-dollar graft cases. Earlier this week, the Coordinating Minister for Political, Legal and Security Affairs, Mahfud M.D., said Asabri, which manages life insurance funds belonging to close to a million Indonesian soldiers and police officers, had allegedly misappropriated the money under their care and lost between Rp 10 trillion and Rp 16 trillion ($730 million-$1.2 billion).

• Indonesia's Draft Bill on Data Privacy

The government has sent Parliament a draft bill on data which would be the first in the country. Included are regulation on data ownership, consumer rights and cross-border data transfer. Under the proposed regulations, a person must provide explicit consent to provide data, such as name, sex, nationality, religion, medical records, biometrics and sexual orientation, to another party. This info can only be used for reasons agreed by the data owner, and trading of private data will be prohibited.

❖ Foreign Affairs/US Indonesia Relations:

• Indonesia Reacts to US Middle East Peace Plan

Indonesia released a brief statement on 1/29 in reaction to the Palestinian/Middle East peace plan outlined earlier in the week by the US and Israel. Indonesia said it was concerned that the plan did not adhere to "internationally agreed parameters". "The issue of Palestine shall be resolved based on the principles of the 'two-state solution' that respects international law and internationally-agreed parameters," the ministry said in a statement to The Jakarta Post. "Indonesia once again encourages the resumption of dialogues among relevant parties to achieve stability and lasting peace," the ministry stressed. *(Jakarta Post)*

• Perceptions of China's Dominance: Survey

Indonesians perceive China as the dominant power in Asia, but they also view this development in an increasingly negative light, according to the latest study by the Indonesian Survey Institute (LSI). The survey reveals that China, the United States and Japan are the countries with the most influence in Asia, according to Indonesians. The survey, which was published on Sunday, polled 1,540 registered voters across Indonesia from July 10 to 15 last year in the aftermath of the general election. It showed that 39 percent of Indonesians believed that China was the most influential country in Asia, followed by the US and Japan with 18 and 14 percent, respectively. About 3 percent of respondents opted for other countries while the remaining 24 percent either said they did not know the answer, did not understand the question or declined to answer.

China's dominance increased sharply from the same survey in 2016, when the US and China were both considered equally influential in Asia — each by 24 percent of Indonesian respondents. In the LSI's 2011 survey, the US was the most dominant country in Asia with 29 percent of Indonesians opting for the US, while only 19 percent of respondents leaned toward China. "What is new is that the US' dominant influence has been replaced by China. A decade ago, it was the US that was seen as the most influential in Asia and in Indonesia. Now and 10 years from now, it is China," the LSI said. However, China's growing dominance also came with negative public sentiment, mostly related to political and economic factors, with China being perceived as an economic threat, according to the survey. *(Jakarta Post)*

• US Journalist Released

After the intervention of US Ambassador Joseph R. Donovan, Indonesia released journalist, Phillip Jacobson, after jailing him for attending a legislative meeting in Central Kalimantan. His crime was being on a business rather than a journalist visa. Indonesia's 2011 immigration law criminalizes such an offense. *(Editor's Note: Many journalists enter Indonesia on tourist visas, claiming requests for press credentials made through Indonesian embassies are never answered).*

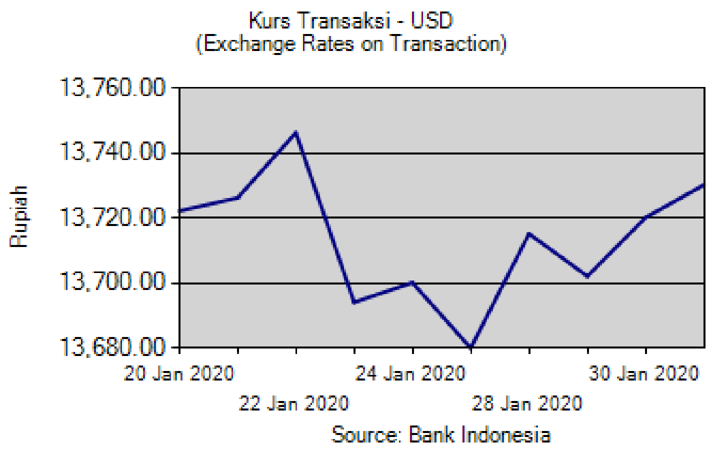
❖ Social/Culture/Education:

• Free The Croc Contest

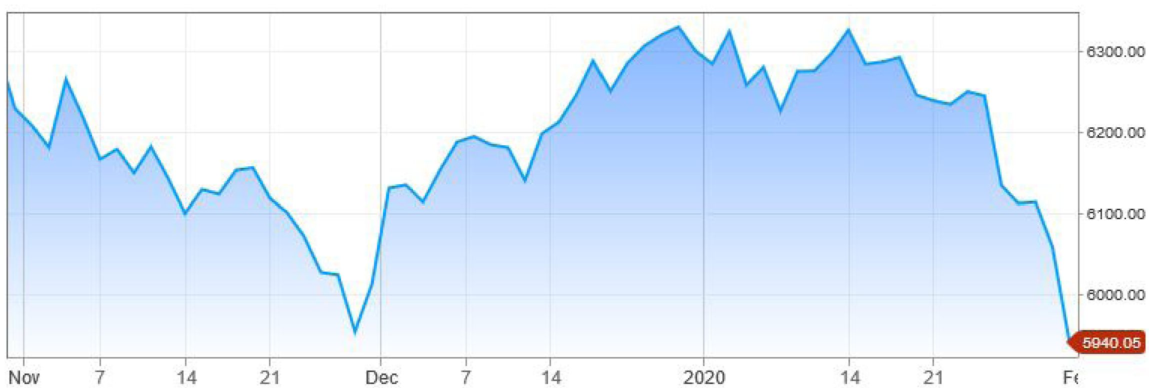
Central Sulawesi's Natural Resources Conservation Office (BKSDA) launched a contest to free a 13-foot wild crocodile from a motorcycle tire that got lodged around its neck for over three years, an official announced here, today. "A reward will be given to anyone, who can release the hapless reptile," Central Sulawesi BKSDA chief Hasmuni Hasmar stated in Palu City, Central Sulawesi Province, Tuesday, though he chose to not divulge details of the prize. The wild reptile, who many believe is a critically endangered Siamese crocodile, had to carry the tire around its neck since it was first spotted roaming in the Palu River to Palu Bay in 2016. *(Antara News)*

❖ CHARTS:

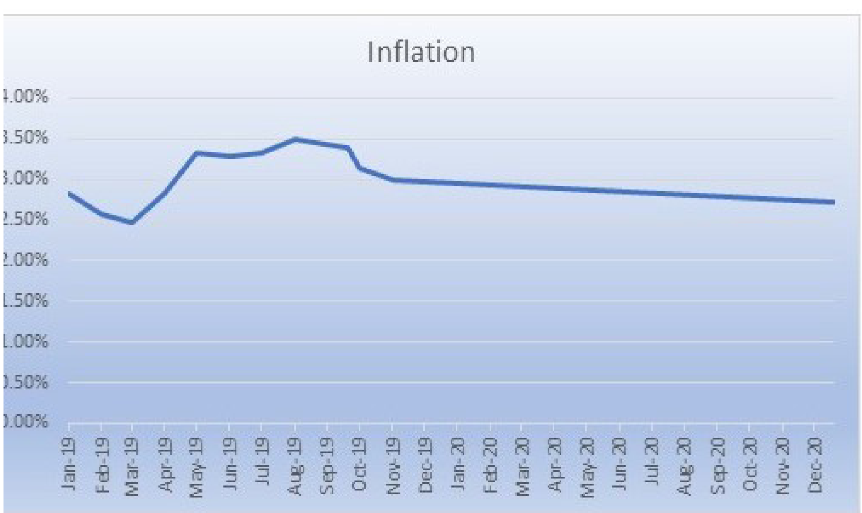
Dollar in Rupiah



Jakarta Stock Exchange Index



Inflation



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