INDOPREMIER

MacroInsight

23 April 2020

Macroeconomics Indicator

	2019	2020F
GDP growth (%YoY)	5.04	2.45
Inflation (%YoY)	2.72	2.50
BI rate (% Year-end)	5.00	4.00
IDR/USD (Year-end)	14,155	15.500
CA balance (% of GDP)	2.82	2.51
Fiscal balance (% of GDP)	2.21	5.07

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Low oil price may widen the deficit; spending cut may be inevitable

- State revenue grew by 7.7% yoy in Mar20 due to one-off higher non-tax revenue (it grew by 37% yoy). Tax revenue contracted by 2.5% yoy.
- State spending in total is unchanged compared to last year, but regional transfer and village fund spending contracted by 8.8% yoy.
- Wider budget deficit of 5.07% of GDP will not proportionally translate to higher spending as revenue may come short from lower oil price.

Sluggish state revenue realization especially from oil related

State revenue grew by 7.7% yoy in Mar20, quite high considering it only grew by 4.6% yoy in Mar last year. This was due to higher non-tax revenue at 36.8% yoy. The high non-tax revenue was coming from an earlier dividend payment from SOE that usually happens in May-Jun. In the meantime, tax revenue contracted by 2.5% yoy, due to contraction in oil & gas tax receipt at 28.6% yoy. With the current movement in the oil price, the trajectory of the tax shortfall from the latest revision in the FY2020 state budget may reach around Rp250tn (assumption around US$20 in average oil price/barrel), translating to an additional of roughly 1.4% of GDP to the proposed 5.07% of GDP fiscal deficit to make the total of fiscal deficit to 6.5% of GDP.

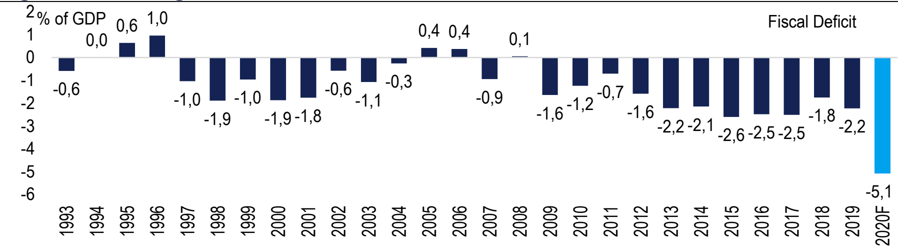
Spending rationalization will be inevitable

We are on the view that recent crash in oil price will be prolonged to make the average oil price throughout the year to be below expectation at around US$20 per barrel. This is only half from the revised government budget at c.US$40 per barrel. As such, spending rationalization will likely be taken by government to keep the fiscal deficit as planned at 5.07%. According to recent presentation by the Head of the Fiscal Policy Office, the first priority of government expenditure is health and social aid related. Thus, we are on the view that most of the cut will be directed to infrastructure or capital spending.

Trade-off between economic activity and rising debt

The government may still be able to propose a higher fiscal deficit to meet the expected spending. However, at above 5.1% fiscal deficit, the sustainability of debt servicing will be in jeopardy as it will increase the debt servicing ratio to 20% (against total spending) from 12%. This may drag down other development programs in subsequent years and adversely impact the growth prospect. In addition, we must underline that the wider fiscal deficit is only a temporary solution. In the near future, there should be a tighter measure for the fiscal deficit or else a solvency problem may arise, as tax revenue will mathematically be lower under the new omnibus law.

Fig. 1: All-time high fiscal deficit in 2020



Source: IMF GFS, MoF, Indo Premier

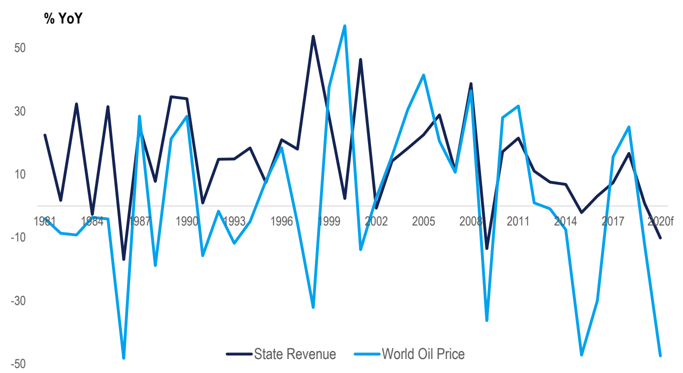
Challenging state revenue

Current weak global oil price trajectory will have a negative impact to the state revenue. Taking into account recent global growth forecast at -3.0% by the IMF, we see the potential of oil price to be at around US$20 in average in 2020 (vs. average of around 60/barrel in 2019). This is about half of the revised government assumption in the revised FY2020 state budget. Thus, we see a tax shortfall from the revised state revenue at about Rp250tn.

Already, total tax revenue (excluding excise and duties) was contracting by 2.5% in Mar. The contraction comes from both oil & gas and non-oil &gas tax collection at -28.6% and -0.8% yoy in Mar. In addition, the duties receipt also contracted by 5.0% yoy, due to contracting export and import.

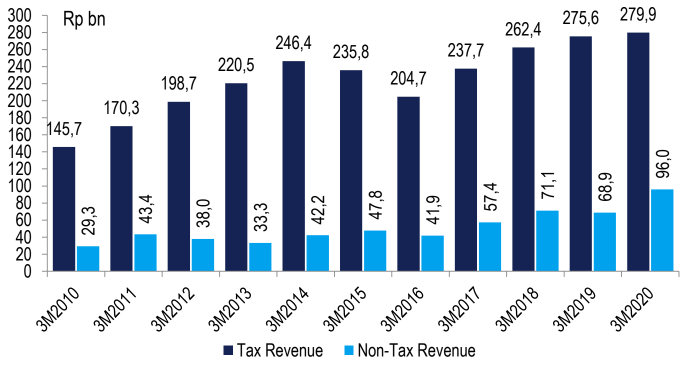
On the contrary, excise collection expanded by 36.5% yoy partially due to sustained cigarette sales volume which contracted by only 0.1% yoy even with the high increase in the excise tariff. Interestingly, value-added tax (VAT) was pretty resilient as it still grew by 2.5% yoy. The VAT is frequently used as a proxy to formal economic activity.

Fig. 2: State revenue correlates with oil price



Source: IMF GFS, MoF, Indo Premier

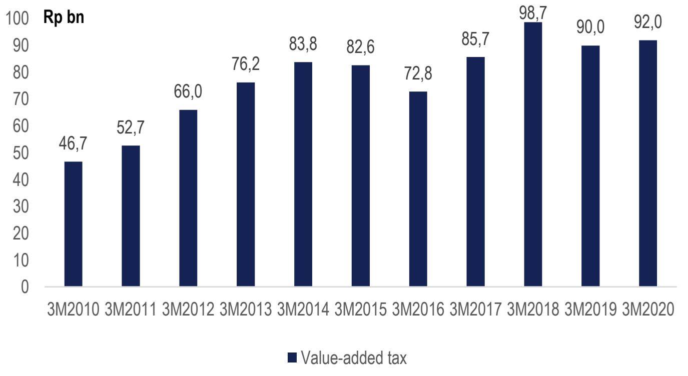
Fig. 3: Both tax and non-tax revenue will be contracting



Source: MoF, CEIC, Indo Premier

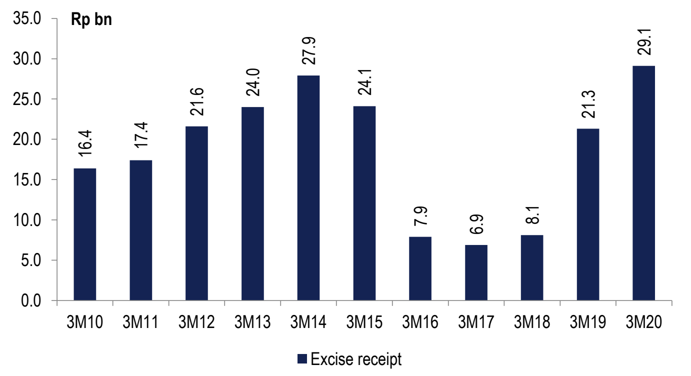
On the non-tax revenue, the increase was due to a one off dividend payment from SOEs that grew to Rp24tn in Mar, from Rp2.6tn the same period last year. This was due to earlier payment schedule, which usually happen in May – June. In addition, non-tax revenue from BLU (public services agencies such as government plantation, government hospital, etc) increased to Rp12.9tn from Rp9.4tn last year. On the contrary, non-tax revenue from natural resources sharing was contracted by 22.4% yoy. Steepest decline came from mineral and coal mining that contracted by 24.1% yoy.

Fig. 4: VAT will be less due to lower economic growth



Source: MoF, CEIC, Indo Premier

Fig. 5: but excise receipt will likely be strong



Source: MoF, CEIC, Indo Premier

On the revised FY2020 budget figure, total tax revenue target was lowered by Rp403.1tn to Rp1,462.6tn from Rp1,865.7tn. Most of the adjusted target will be coming from income tax, partially due to lowered company income tax rate by 3% to 22%. Moreover, the VAT target was also being lowered by Rp156.2tn to Rp529.7tn from Rp685.9tn due to the perceived decline in economic growth to around 2.3% from 5.3% initially. On the non-tax revenue, the receipt from natural resources sharing was lowered by Rp78tn, mostly due to revised oil price assumption to around US$40/barrel, from US$60/barrel initially.

Lastly, it was interesting to see that the SOE dividend payment, or the profit transfer, is increased by Rp16tn. Anecdotal evidence suggest the increase will be coming from health related SOEs and the financial sector SOEs.

Fig. 6: Tax revenue revision for FY2020

Tax revenue breakdown (Rp tn)	Initial Figure	Revision	Changes
Tax Revenue	**1.865,7**	**1.462,6**	**-403,1**
Domestic Tax Revenue	**1.823,1**	**1.427,0**	**-396,1**
Income Tax (PPh)	929,9	703,3	-226,6
O&G Income Tax	57,4	43,7	-13,7
Non-O&G Income Tax	872,5	659,6	-212,9
PPh 21	163,4	139,0	-24,3
PPh 22	22,9	19,8	-3,2
PPh 22 Import	69,7	48,9	-20,7
PPh 23	52,7	39,1	-13,6
PPh 25/29 person	12,0	10,6	-1,4
PPh 25/29 Institution	323,4	232,0	-91,5
PPh 26	74,9	51,4	-23,5
PPh Final	153,3	118,7	-34,6
Other Non-O&G Income Tax	0,2	0,1	-0,1
Value Added Tax (VAT) and Luxury Tax	685,9	529,7	-156,2
Excise	180,5	172,9	-7,6
Tobacco Product Excise	173,1	165,6	-7,5
Other Tax	7,9	7,7	-0,3
International Trade Tax	**42,6**	**35,6**	**-7,0**
Import Duties	40,0	33,9	-6,1
Export Duties	2,6	1,8	-0,9

Source: MoF, Indo Premier

Fig. 7: Non-tax revenue revision for FY2020

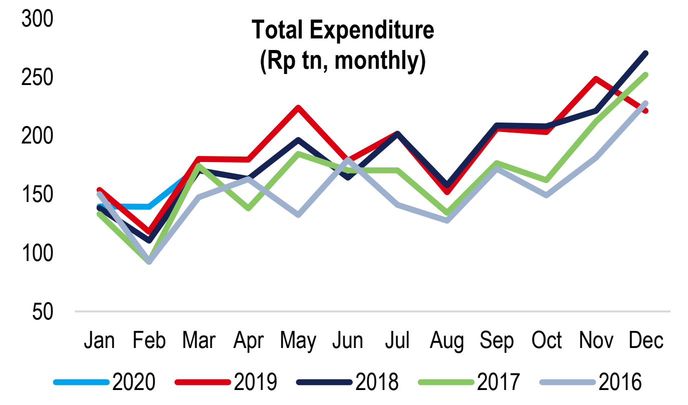
Non-tax revenue breakdown (Rp Tr)	Initial Figure	Revision	Changes
Non-Tax Revenue	**367,0**	**297,8**	**-69,2**
Natural Resources	**160,4**	**82,2**	**-78,1**
Oil and Gas	127,3	53,3	-74,0
- Oil	96,8	40,4	-56,4
- Gas	30,5	12,9	-17,6
Non Oil and Gas	33,0	28,9	-4,1
- Mineral and Coal Mining	26,2	22,1	-4,1
- Forestry	4,7	4,4	-0,3
- Fishery	0,9	0,9	0,0
- Geothermal Mining	1,2	1,5	0,3
Profit Transfer From SOEs	**49,0**	**65,0**	**16,0**
Other	**100,9**	**94,7**	**-6,2**
BLU Revenue	**56,7**	**55,8**	**-0,9**

Source: MoF, Indo Premier

Spending rationalization is unavoidable

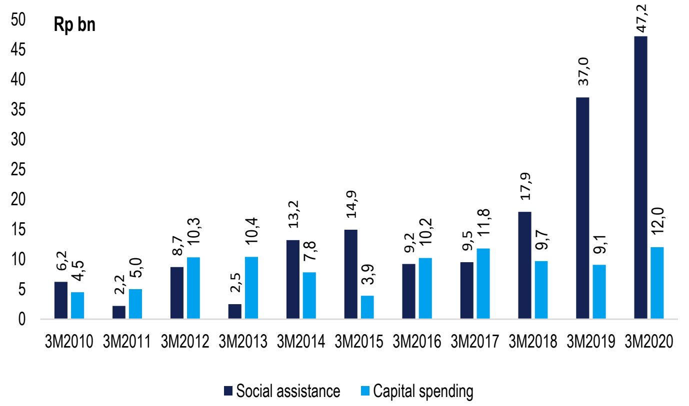
With the weakening oil price, we see the policy of spending rationalization is unavoidable. Without proper spending management, we estimate the fiscal deficit to be widened to 6.5% of GDP. We believe the rationalization will be targeted to infrastructure and capital related spending. Already, the government's material expenditure was down by -6.6% yoy, from the same period last year. Nevertheless, we believe the government's focus will be on health and social aid. The social aid reached an all-time high level at Rp47.2tn in Mar. This is ultimately to safeguard the biggest portion of the population from the negative impact of the virus and from poverty circle.

Fig. 8: Total expenditure will likely adjusted along with revenue



Source: MoF, CEIC, Indo Premier

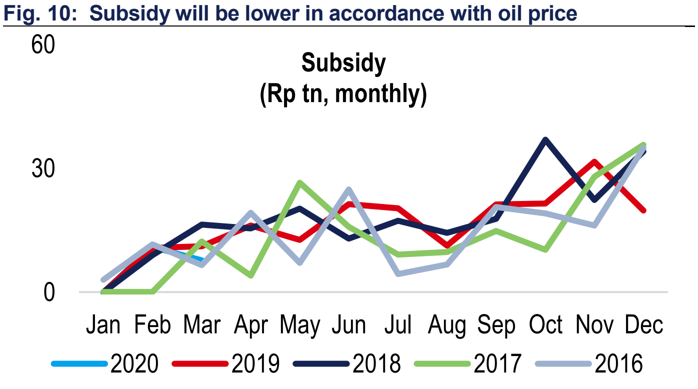
Fig. 9: More emphasis on social aid instead of capital spending



Source: MoF, CEIC, Indo Premier

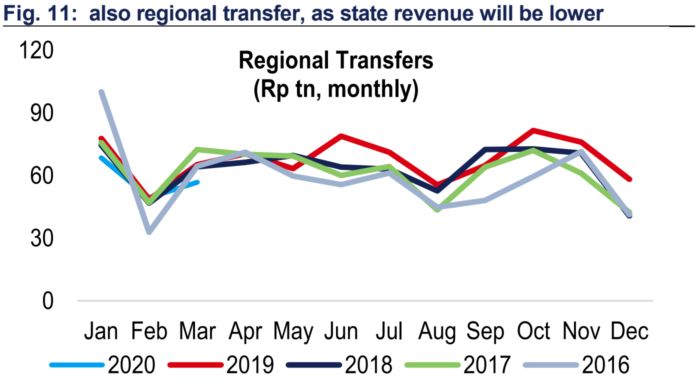
The subsidy spending naturally will be lower as the average oil price declines by around 50% yoy from the same period last year. We are on the view that weak global demand will make oil price to remain low until year-end. This shall translate to lower regulated fuel price, as the current price level has not being adjusted since last year in spite of the drop in oil price. The adjustment shall directly impact inflation figure to remain relatively benign. On paper, the downward adjustment in the regulated fuel price could be around 20% in average. This will translate to lower yearly inflation figure from 2.5% yoy initially to around 2.0% yoy.

Fig. 10: Subsidy will be lower in accordance with oil price



Source: MoF, CEIC, Indo Premier

Fig. 11: also regional transfer, as state revenue will be lower



Source: MoF, CEIC, Indo Premier

On the revised figure, the government slashed spending allocation to Ministry of Public Works and almost all other Ministerial and Agencies except Ministry of Health and Ministry of Education. In addition, it is interesting to see that budget for state treasures (BUN) is increased significantly. This is due to most of the government stimulus and social safety net will be managed under the Ministry of Finance.

Fig. 12: Summary of changes in ministerial budget

State Expenditure (Rp tn)	Initial Figure	Revision	Changes
Ministry of Defense	131,2	122,4	-8,7
Ministry of Education and Culture	36,3	70,7	34,4
Ministry of Health	57,4	76,5	19,2
Ministry of Public Works and Housing	120,2	95,7	-24,5
Ministry of Research and Technology	42,2	2,5	-39,7
State Treasurer BA 999	773,9	1.014,6	240,7
Central Government Expenditure	**1.683,5**	**1.851,1**	**167,6**

Source: MoF, Indo Premier

Fig. 13: Summary of revised FY2020 budget, financing will be key

Category	Initial Figure	Revision	Changes
Total Revenue	**2.233,2**	**1.760,9**	**-472,3**
I. Domestic Revenue	2.232,7	1.760,4	-472,3
1. Tax Revenue	1.865,7	1.462,6	-403,1
2. Non-Tax Revenue	367,0	297,8	-69,2
II. Grant	0,5	0,5	0,0
Total Spending	**2.540,4**	**2.613,8**	**73,4**
I. Central Government Expenditure	1.683,5	1.851,1	167,6
II. Transfer to Region and Village Fund	856,9	762,7	-94,2
Primary Balance	**-12,0**	**-517,8**	**-505,8**
Fiscal Deficit	**-307,2**	**-852,9**	**-545,7**
Fiscal deficit (% GDP)	-1,76	-5,07	-3,31
Financing	**307,2**	**852,9**	**545,7**
I. Debt Financing	351,9	1.006,4	654,6
II. Investment Financing	-74,2	-229,3	-155,1
III. Lending	5,2	5,8	0,6
IV. Loan Provision	-0,6	-0,6	0,0
V. Other Financing	25,0	70,6	45,6

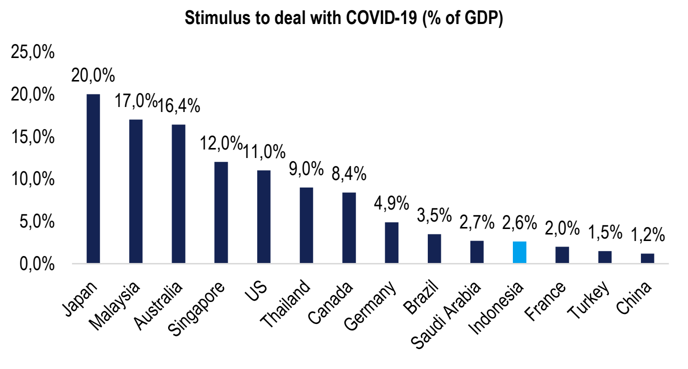
Source: MoF, Indo Premier

Financing will follow spending policy

Financing will be playing an important role as it is at the centre stage of the whole stimulus and social safety net package. With almost all countries in a race to raise additional funding to mitigate the economic downfall, the competition for global liquidity will be steep.

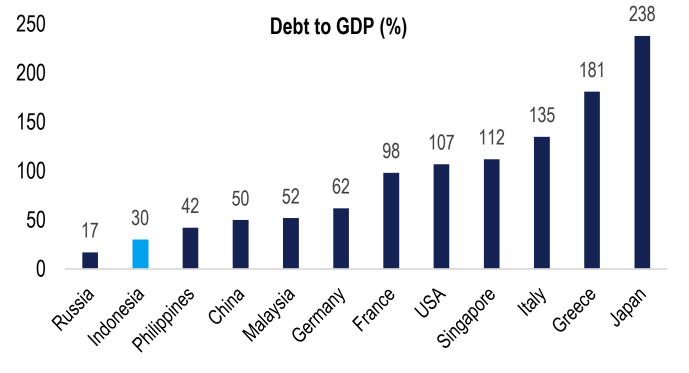
Fortunately, our debt profile still relatively low at around 30% of GDP and the size of the stimulus is at around 2.6% of GDP. Please note that total fiscal deficit is at 5.07% of GDP, which consist of various government spending other than the stimulus to deal with virus outbreak.

Fig. 14: Indonesia's stimulus is among the lowest



Source: Bloomberg, CEIC, Indo Premier

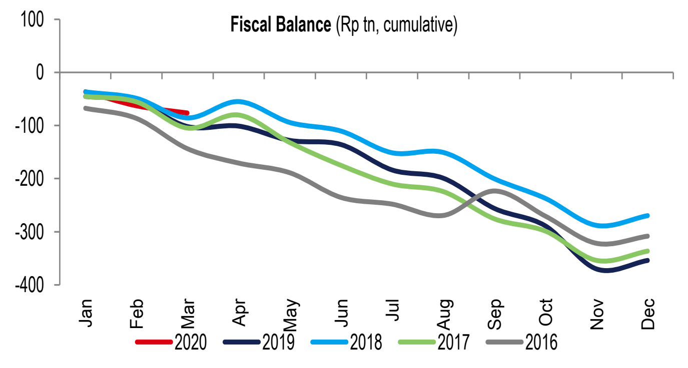
Fig. 15: Indonesia debt to GDP also relatively very low



Source: Bloomberg, CEIC, Indo Premier

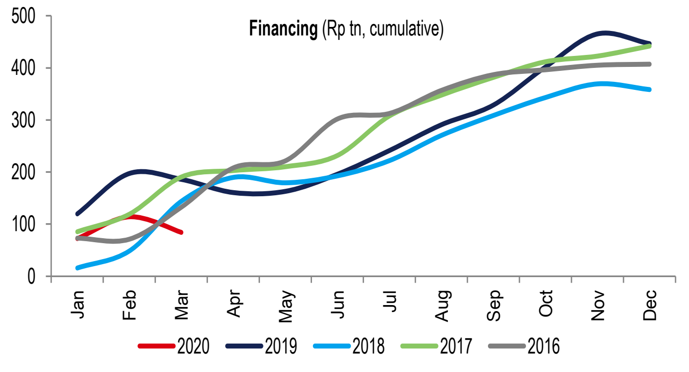
Fortunately this year the government have not conducted the usual front loading strategy on financing. The realization of government bond issuance is still 21.6% of total targeted amount. About a half compared to the same period last year issuance at 47.8% of total targeted amount. Generally speaking, the remaining of the government bond issuance should be at cheaper cost as the risk free rate and the inflation figure should be lower compared to the beginning of the year.

Fig. 16: Fiscal deficit will be wider as spending increases



Source: Bloomberg, CEIC, Indo Premier

Fig. 17: Financing front loading not yet started



Source: Bloomberg, CEIC, Indo Premier

The government's national economic recovery program will be key to the recovery speed of domestic economic activity. As this report being written, the government have not decided on the program detail. Anecdotal evidence suggest that the size of the stimulus at Rp150tn is not sufficient to cushion the fall in economic activity. However, higher allocation of the economic recovery program means more government debt. It is somewhat transferring the debt burden from SOEs to the central government. In the future, the higher government debt servicing could cripple the central government's ability to conduct development agendas, in our view.

Fig. 18: Detailed financing breakdown, economic recovery program crucial

Category	Initial Figure	Revision	Changes
Financing	**307,2**	**852,9**	**545,7**
Debt Financing	**351,9**	**1.006,4**	**654,6**
Govt Securities (netto)	389,3	549,6	160,2
Borrowings (netto)	-37,5	7,0	44,4
Domestic Borrowings (netto)	1,3	1,3	0,0
Foreign Borrowings (netto)	-38,8	5,7	44,4
Pandemic Bond	-	449,9	449,9
Investment Financing	**-74,2**	**-229,3**	**-155,1**
Investment to SOEs	-17,7	-16,0	1,8
State Capital Investment to PT. PLN	-5,0	-5,0	0,0
State Capital Investment to PT. Hutama Karya	-3,5	-3,5	0,0
State Capital Investment to PT. Sarana Multigriya Finansial	-2,5	-1,8	0,8
State Capital Investment to PT. Bahana Pembinaan Usaha Indonesia	-0,3	-0,3	0,0
State Capital Investment to PT. Geo Dipa Energi	-0,7	-0,7	0,0
State Capital Investment to PT. Permodalan Nasional Madani	-1,0	-1,0	0,0
State Capital Investment to PT. Pengembangan Armada Niaga Nasional	-3,8	-3,8	0,0
State Capital Investment to Strengthen Current Account Balance	-1,0	-	-1,0
Investment to Other Institutions	-5,0	-5,0	0,0
State Capital Investment to LPEI	-5,0	-5,0	0,0
Investment to Public Service Agency	-52,5	-41,0	11,5
Revolving Fund	-10,0	-10,0	0,0
PPDPP	-9,0	-9,0	0,0
PIP	-1,0	-1,0	0,0
DPPN	-18,0	-18,0	0,0
LMAN	-10,5	-	-10,5
LDKPI	-1,0	-	-1,0
Research Endowment Fund	-5,0	-5,0	0,0
Cultural Endowment Fund	-1,0	-1,0	0,0
Collage Endowment Fund	-5,0	-5,0	0,0
BPDLH	-2,0	-2,0	0,0
Investment to International Agency	-1,0	-0,8	-0,2
Other Investment Financing	-	-168,6	-168,6
Financing to Support the National Economic Recovery Program	-	-150,0	-150,0
Financing for Education	-	-18,6	-18,6
Other Financing	**25,0**	**25,0**	**25,0**
SiLPA	**25,0**	**70,6**	**70,6**

Source: MoF, CEIC, Indo Premier

In sum, the size of the government's financing will be contingent to the government spending realization. Thus, the allocated financing figure in the budget could still be lower than expected. At the end of the day, it is a matter of trade-offs. We could have a softer impact of virus outbreak to the economy, but at the expense of future debt.

ANALYSTS CERTIFICATION

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