

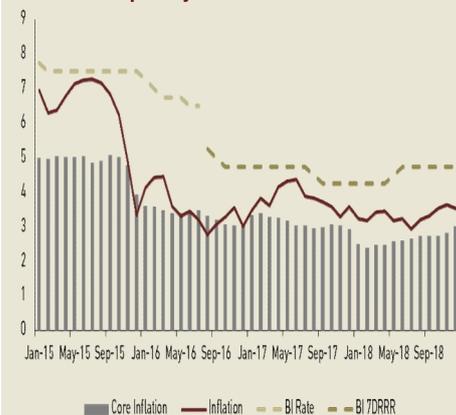
Monetary and Bonds Review

Hawkish move initiated

Policy rates' outcome

	Apr 2018	May 2018	Est.	Cons.
BI 7DRRR (%)	4.25	4.50	4.50	4.50
Deposit facility rate (%)	3.50	3.75	3.75	
Lending facility (rate) (%)	5.00	5.25	5.25	

Inflation & policy rate



Source : BPS & Bank Indonesia

Rupiah and Foreign Reserve



Source : Bloomberg

Imanuel Reinaldo

+62 21 2557 4800 ext. 820

reinaldoimanuel@ciptadana.com

<http://www.ciptadana.com>

Central bank raise 7 days reverse repo rate by 25 bps

Bank Indonesia (BI) decided to raise policy rate by 25bps to 4.50% in the May board of governor meeting. It also increased deposit facility rate to 3.75% and lending facility rate to 5.25%. Central bank pointed out that this move is necessary to maintain macroeconomic stability amidst high global financial volatility. It is even ready to take stronger measure to maintain the stability.

BI macro guidance: dilemma of stability and growth

In its statement, we see that central bank had a dilemma between macroeconomic stability and growth. It said that rate hike is necessary to prevent Rupiah depreciation effect on inflation. As of April 2018, inflation reached 3.41% YoY and we still predict that year end inflation will be around 3.5% YoY. A rate hike prevents us to increase our inflation forecast this year. However, BI also said that the rate hike may change growth estimate in this year. GDP growth is estimated to be slightly lower than target, especially government target at 5.4%. However, BI still maintained its target for economic growth at range 5.1% - 5.5%. We have a view that 25 bps rate hike effect on GDP growth will not significant but another rate hike of 25bps to 4.75% may affect our view on GDP. We see BI is ready to sacrifice growth a little in order to maintain Rupiah stability.

Downside from FFR hike expectation almost near the end

In 1H18 we face peaked global volatility due to FFR hike shifting expectation. In the beginning of 2018, most of economist surveyed by Bloomberg still predicted 2x FFR hike in 2018. However, the prediction shifted to 3x hike in February and shifted again to 4x in April. We see that Rupiah, as of May 17, has depreciated 3.4% YTD and 5.8% from its strongest position in January 29 (Rp 13,289). We see that FFR hike projection from FOMC in June 2018 will denote 4x FFR hike in 2018 and 2x hike in 2019. The latest Bloomberg survey showed that 41.4% economists predicted 4 times FFR hike in 2018, implying that market had priced in to 4x FFR hike. We believe the increase in market volatility due to FFR hike expectation will last until late 2Q18 (next FOMC meeting in June) and market will look calm after that. However, global risk may still come from trade war and geopolitical conflict as the uncertainty of US-China and US-North Korea meeting remained high.

Our call: 4x FFR hike, 2x BI 7DRRR hike and Rupiah to Rp13,975/USD in 2018 average

Judging from BI hawkish tone of it is willing to sacrifice the growth to maintain stability, we decide to revise our call for rate hike. We retain our view that The Fed will raise FFR by 4x in this year and 2x in 2019. Current BI's forecast may imply that Fed will only increase FFR by 3x in this year. However, we see that June's FOMC meeting projection will change BI's view as the new projection should be similar with our forecast and force Bank Indonesia to have another rate hike in the same month (next BoG meeting on June 27-28) for currency stabilization sake. Rupiah volatility should gradually ease as we see global volatility will decline due to in line FFR hike expectation. We see Rupiah will average around Rp13,975/USD in 2018 and Rp14,050 at year end 2018. Although we expect that the market volatility will decline in 2H18 and started to trigger capital inflow, we believe Rupiah has limited room to strengthen due to current account deficit pressure. We expect CAD will be at 2.1% of GDP in 2018, widen from 2017 position at 1.7% of GDP. However, please beware of our forecast risk as mentioned in the last paragraph.

Bearish trend dominate bonds market in 1H18

After experiencing bullish period in 2017, Indonesia bonds market finally turned to bearish period in 1H18. Yield of 10-yr Indonesia's government bonds rose from its lowest position at 6.13% in Jan 8 to current position at 7.2% in May. Shifting of FFR hike expectation played the main role in the bearish bonds market as it pushed US bonds market and global bonds market to bearish trend. Furthermore, higher FFR hike expectation triggered capital outflow from emerging market, especially from countries which had twin deficit like Indonesia, India and Philippines, and brought down these countries currency to a deep depreciation (see exhibit 6). Higher global volatility also brought Indonesia's 5 yr credit default swap (CDS) back to above 100 levels after it experienced the lowest level at 76.9 in January. It made the positive catalysts like Moodys rating upgrade, Indonesia's bonds inclusion in global bonds index and low inflation almost had no effect to the market.

Expect 10-yr yield to reach 7.25% in YE 2018

We believe that bearish trend in bond market may continue until June, when FOMC will give new projection which reveals its preference of 4x FFR hike in 2018. Limited downside from FFR expectation means limited downside from US treasury yield and Rupiah. We see that US treasury 10-yr yield may end 2018 at 3.12% level. Current level of UST 10-yr yield is approaching 3.1% level but we believe it is due to the impact of higher geopolitical tension in Korea Peninsula and US-China trade war. We expect both conflicts will ease in near term and bring UST 10-yr yield to 3.0% level. We also expect Indonesia's CDS 5 yr will ease from current level at around 120 to 100 in year end as global volatility decline and Indonesia's GDP growth will pick up to around 5.3%. Inflation is expected to be around 3.5% in this year. Assuming that central bank will increase the policy rate once more to 4.75%, we expect that 10-yr yield will reach 7.31% at end of 1H18 and 7.25% in 2H18.

Risk to our policy rate, Rupiah and bond yield forecast

Our call for policy rate, Rupiah and bond yield also comes with some risks. Globally, we see the risk will still come from higher geopolitical tension in Korea Peninsula and US-China trade war. In previous paragraph, we expect that the conflict may end in near term. However, it may not close any risks of further higher tension of conflict that cause higher UST yield and in the end affect our Rupiah and bond yield estimate. Global risk also comes from ECB plan of monetary tightening. We expect ECB to end monetary stimulus by 2H18 and started to tighten the policy in 2019. Although ECB's move should give less impact to our forecast than Fed but the risk from ECB's move is still worth to watch. Domestically, we see the risk will come from higher than expected inflation, especially due to higher global oil price. If government cannot hold the subsidized oil price at current price, it may affect administered price and inflation in overall. Higher inflation may force central bank to raise another rate. Second risk comes from current account deficit (CAD). We expect 2.1% of GDP CAD in 2018 but we still do not close any opportunity of higher CAD, especially after huge trade deficit in April (USD-1.68 bn). Third risk comes from political instability. 2H18 will be the kick off for 2019 presidential election. Although we expect stable political condition in for presidential election 2019, the risk of political instability is still worth to watch.

Exhibit 1: Macroeconomic Indicator

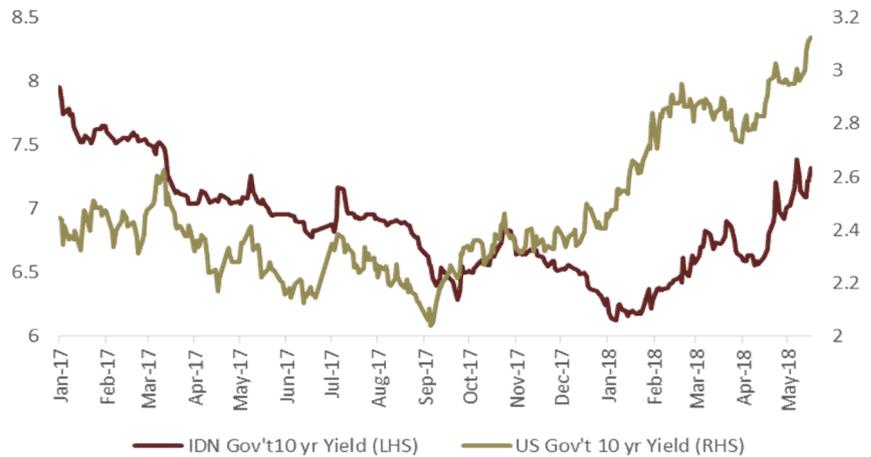
Year-end 31-Dec	14A	15A	16A	17A	18F
Nominal GDP (Rp tn)	10,543	11,541	12,407	13,588	14,878
Nominal GDP (USD bn)	888	861	974	1,015	1,102
GDP/capita (USD) - Nominal	3,530	3,377	3,605	3,877	4,158
Real GDP (%YoY)	5.0	4.8	5.0	5.1	5.3
Private Consumption (%YoY)	5.1	5.0	5.0	4.9	5.0
Government consumption (%YoY)	2.0	5.4	-0.1	2.1	3.5
Gross Fixed Capital Formation (%YoY)	4.1	5.1	4.5	6.1	7.5
Exports (%YoY)	1.0	-2.0	-1.7	9.1	7.3
Imports (%YoY)	2.2	-5.8	-2.3	8.1	10.5
Inflation rate (%YoY) - year end	8.4	3.4	3.0	3.6	3.5
Core inflation rate (%YoY) - year end	5.5	4.0	3.1	3.0	3.3
BI Rate	7.75	7.50			
BI 7 Days Reverse Repo Rate - year end			4.75	4.25	4.75
Rupiah / US Dollar - average	11,878	13,398	13,473	13,380	13,975
Rupiah / US Dollar - year end	12,440	13,788	13,346	13,555	14,050
Current account as % of GDP	-2.9	-2.1	-1.8	-1.7	-2.1
Fiscal balance as % of GDP	-2.4	-2.8	-2.5	-2.5	-2.4

Source: BI, BPS, MoF and Ciptadana Estimates

We revise our Rupiah expectation to 13,975/USD for 2018 average and Rp 14,050/USD for YE 2018

FFR hike expectation made US bonds market and global bonds market experienced bearish period

Exhibit 2: Indonesia and US 10-yr Govt Bonds Yield



Source: Bloomberg

Exhibit 3: Forecasted Bond Yield

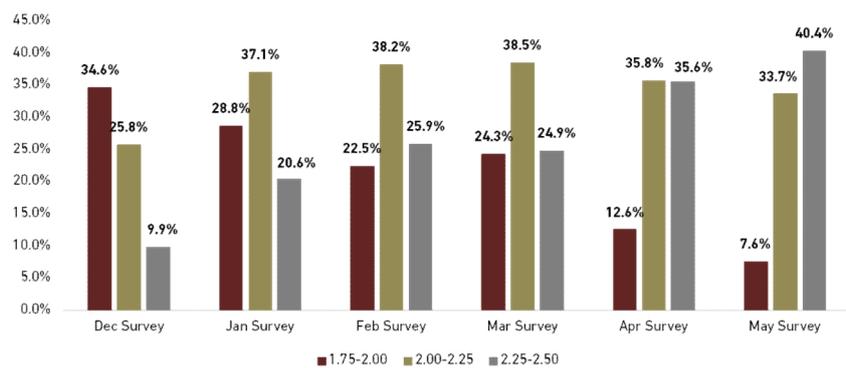
	1H18		2H18	
BI 7DRRR:	4.50%	4.75%	4.50%	4.75%
5 yr	6.75%	6.81%	6.67%	6.73%
10-yr	7.18%	7.31%	7.12%	7.25%
20 yr	7.89%	7.96%	7.86%	7.93%

We expect 10yr yield at 7.31% in 1H18 and 7.25% at YE 2018

Source: Ciptadana Estimates

Economists has priced in 4x FFR hike in 2018

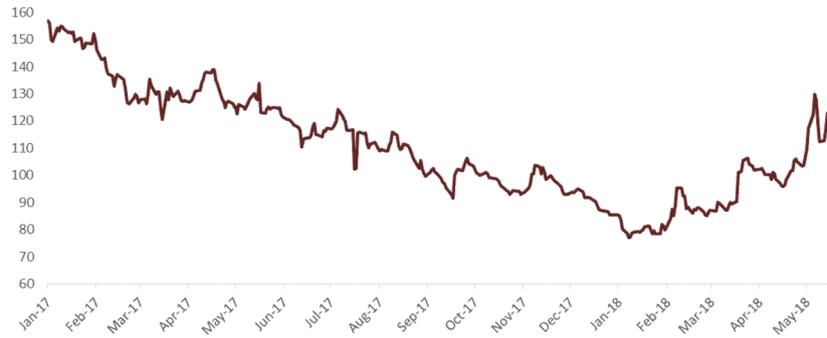
Exhibit 4: Bloomberg Survey of FFR Projection



Source: Bloomberg

High global volatility and depreciating Rupiah made Indonesia CDS is on uptrend

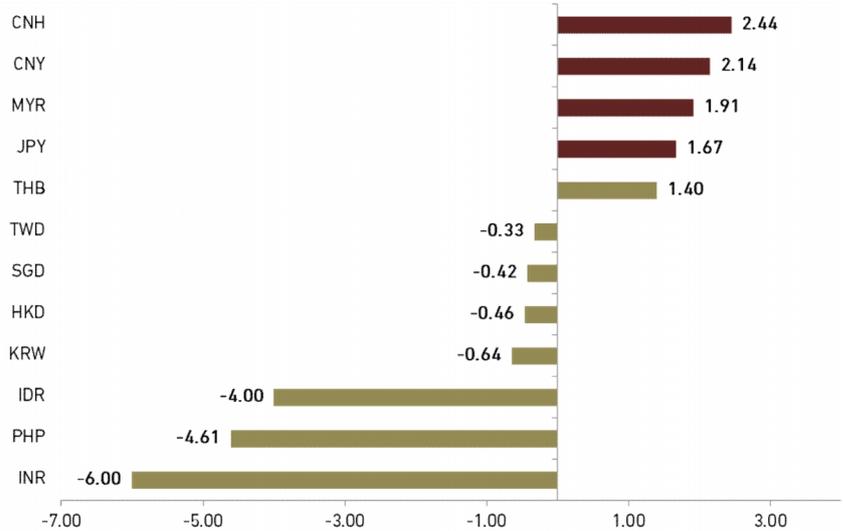
Exhibit 5: Indonesia Credit Default Swap 5 yr



Source: Bloomberg

Indonesian Rupiah became one of worst performer in Asia but still had better performance from PHP and IDR which had twin deficit and similar rating

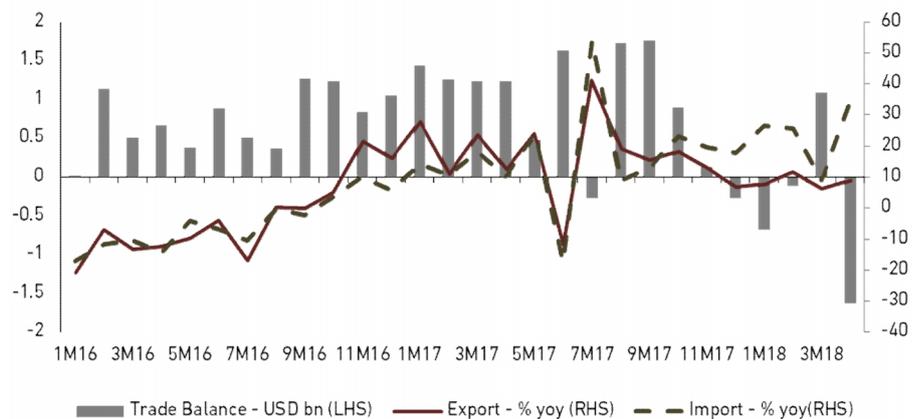
Exhibit 6: Asian Currency Performance YTD as of May 18, 2018



Source: Bloomberg

April huge trade deficit may give some risks to current account deficit in 2018.

Exhibit 7: Indonesia Trade Balance



Source: Bloomberg

EQUITY RESEARCH

HEAD OF RESEARCH

Arief Budiman

Strategy, Automotive, Heavy Equipment,
Construction, Oil & Gas
T +62 21 2557 4800 ext 819
E budimanarief@ciptadana.com

ECONOMIST

Imanuel Reinaldo

T +62 21 2557 4800 ext 820
E reinaldoimanuel@ciptadana.com

ANALYST

Stella Amelinda

Consumer
T +62 21 2557 4800 ext 740
E amelindastella@ciptadana.com

TECHNICAL ANALYST

Trevor Gasman

T +62 21 2557 4800 ext 934
E gasmantrevor@ciptadana.com

ANALYST

Erni Marsella Siahaan, CFA

Banking
T +62 21 2557 4800 ext 919
E siahaanerni@ciptadana.com

ANALYST

Niko Margaronis

Telecommunication, Tower, Healthcare
T +62 21 2557 4800 ext 734
E margaronisniko@ciptadana.com

ANALYST

Fransisca Maharani Putri

Media, Retail
T +62 21 2557 4800 ext 760
E putrifransisca@ciptadana.com

RESEARCH ASSISTANT

Sumarni

T +62 21 2557 4800 ext 920
E sumarni@ciptadana.com

ANALYST

Yasmin Soulisha

Property, Plantations
T +62 21 2557 4800 ext 799
E soulisyasmin@ciptadana.com

ANALYST

Fahressi Fahalmesta

Cement, Toll Road, Poultry
T +62 21 2557 4800 ext 735
E fahalmestafahressi@ciptadana.com

ANALYST

Christian Saortua

Coal, Metal mining
T +62 21 2557 4800 ext 739
E saortuachristian@ciptadana.com

EQUITY SALES

Co HEAD OF INSTITUTIONAL SALES

Dadang Mulyana

Plaza ASIA Office Park unit 2
Jl. Jend. Sudirman Kav. 59
Jakarta - 12190
T +62 21 2557 4800 ext 838
F +62 21 2557 4900
E mulyanadadang@ciptadana.com

Co HEAD OF INSTITUTIONAL SALES

The Fei Ming

Plaza ASIA Office Park unit 2
Jl. Jend. Sudirman Kav. 59
Jakarta - 12190
T +62 21 2557 4800 ext 807
F +62 21 2557 4900
E thefeiming@ciptadana.com

BRANCH OFFICES

JAKARTA - MANGGA DUA

Komplek Harco Mangga Dua
Rukan Blok C No.10
Jl. Mangga Dua Raya
Jakarta - 10730
T +62 21 600 2850
F +62 21 612 1049

JAKARTA - PURI KENCANA

Perkantoran Puri Niaga III
Jl. Puri Kencana Blok M8 No.2E
Kembangan
Jakarta - 11610
T +62 21 5830 3450
F +62 21 5830 3449

SURABAYA

Intiland Tower Surabaya
Ground Floor Suite 5 & 6
Jl. Panglima Sudirman 101-103
Surabaya - 60271
T +62 31 534 3938
F +62 31 534 3886

SEMARANG

Gedung Menara Suara Merdeka
6th Floor Unit 02
Jl. Pandanaran No.30
Semarang - 50134

Analyst Certification

Each contributor to this report hereby certifies that all the views expressed accurately reflect his or her personal views about the companies, securities and all pertinent variables. It is also certified that the views and recommendations contained in this report are not and will not be influenced by any part or all of his or her compensation.

Disclaimer

This report does not constitute an offer to buy or sell any security/instrument, invitation to offer or recommendation to enter into any transaction. Nor are we acting in any other capacity as a fiduciary to you. When making and investment decision, you should determine, without reliance upon us or our affiliates, the economic risks and merits (and independently determine that you are able to assume these risks) as well as the legal, tax and accounting characterizations and consequences of any such transaction. In this regard, by accepting this report, you acknowledge that (a) we are not in the business of providing (and you are not relying on us for) legal, tax or accounting advice, (b) there may be legal, tax or accounting risks associated with any transaction, (c) you should receive (and rely on) separate and qualified legal, tax and accounting advice and (d) you should apprise senior management in your organization as to such legal, tax and accounting advice (and any risks associated with any transaction and our disclaimer as to these matters).

The information contained in this report is based on material we believe to be reliable; however, we do not represent that it is accurate, current, complete, or error free. Assumptions, estimates and opinions contained in this report constitute our judgment as of the date of the document and are subject to change without notice. Any projections are based on a number of assumptions as to market conditions and there can be no guarantee that any projected results will be achieved. Past performance is not a guarantee of future results. PT CIPTADANA SECURITIES AND ITS AFFILIATES SPECIFICALLY DISCLAIMS ALL LIABILITY FOR ANY DIRECT, INDIRECT, CONSEQUENTIAL OR OTHER LOSSES OR DAMAGES INCLUDING LOSS OF PROFITS INCURRED BY YOU OR ANY THIRD PARTY THAT MAY ARISE FROM ANY RELIANCE ON THIS REPORT OR FOR THE RELIABILITY, ACCURACY, COMPLETENESS OR TIMELINESS THEREOF.

Disclaimer: This document is not intended to be an offer, or a solicitation of an offer, to buy or sell relevant securities (i.e. securities mentioned herein or of the same issuer and options, warrants or rights to or interest in any such securities). The information and opinions contained in this document have been compiled from or arrived at in good faith from sources believed to be reliable. No representation or warranty, expressed or implied, is made by PT CIPTADANA SECURITIES or any other member of the Ciptadana Capital, including any other member of the Ciptadana Group of Companies from whom this document may be received, as to the accuracy or completeness of the information contained herein. All opinions and estimates in this report constitute our judgment as of this date and there can be no assurance that future results or events will be consistent with any such opinions, forecasts or estimates. The information in this document is subject to change without notice; its accuracy is not guaranteed; and it may be incomplete or condensed.