Research Update:

Indonesia Outlook Revised To Stable From Negative; 'BBB/A-2' Ratings Affirmed

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Overview

- Indonesia's external settings are benefiting from improved terms of trade on higher commodity prices.
- The economy continues to recover from the pandemic-driven slowdown, supporting the government's fiscal consolidation efforts.
- We revised our rating outlook on Indonesia to stable from negative. At the same time, we affirmed our 'BBB/A-2' sovereign credit ratings on Indonesia.
- The stable outlook reflects our expectation that Indonesia's economic recovery will continue over the next two years.

Rating Action

On April 27, 2022, S&P Global Ratings revised the outlook on its long-term sovereign credit rating on Indonesia to stable from negative. At the same time, we affirmed our 'BBB' long-term and 'A-2' short-term sovereign credit ratings.

Outlook

The stable outlook reflects our expectation that Indonesia's economic recovery will continue over the next two years, supporting the government's continued fiscal consolidation efforts.

Downside scenario

We may lower the rating if Indonesia's economic recovery stalls such that trend growth in real GDP per capita is no longer faster than that of peers.

Indications that the government's change in net general government debt will remain above 3% of GDP annually, and that the general government's interest payments would surpass 15% of revenues on a sustained basis would exert downward pressure on the ratings.

A significant reversal in Indonesia's current account receipts leading to a weakening in Indonesia's external balance sheet would indicate further downward pressure on the rating.

Upside scenario

We may raise the rating if Indonesia's net external indebtedness falls below 50% of current account receipts, or if gross external financing needs fall below 50% of current account receipts plus usable reserves.

Change in net general government debt of less than 3% of GDP per year, in addition to a net debt stock of less than 30% of GDP or interest payments below 10% of general government revenues, would also indicate upward pressure on the ratings.

Rationale

We revised the outlook to stable in recognition of Indonesia's improved external position and gradual progress toward fiscal consolidation.

Our ratings on Indonesia reflect the economy's solid growth prospects and historically prudent policy dynamics. These strengths are balanced by Indonesia's low GDP per capita, moderate stock of public debt, and costs associated with servicing the debt relative to the government's limited revenue base.

The Indonesian government's debt has stabilized following a notable increase in 2020. However, the interest burden is likely to remain somewhat elevated as interest rates rise over the next one to two years. In contrast, Indonesia's narrow net external debt metrics have improved considerably, underpinned by constructive terms-of-trade dynamics.

Institutional and economic profile: Growth set to accelerate in 2022 as economy reopens

- We forecast real GDP growth will accelerate to 5.1% in 2022, versus 3.7% in 2021, as pandemic-related restrictions continue to ease.
- The conflict in Ukraine poses fresh risks, particularly to consumer demand. However, these are likely to be manageable, barring a more severe global economic downturn.
- The landmark Job Creation law first passed in November 2020 will help employment and foreign direct investment trends, in our opinion. This is assuming the government is able to resolve associated legal challenges.

The Indonesian economy returned to growth in 2021, expanding 3.7% in real terms following a 2.1% decline in 2020. We expect the pace of the recovery to accelerate further this year. Broad vaccination coverage, significant natural immunity, and milder outcomes from the omicron variant of the coronavirus are likely to result in a continued loosening of pandemic-related restrictions, supporting more normalization of economic activity and employment outcomes. The resources sector is also poised to further benefit from continued elevated commodity prices.

Political and policy institutions in Indonesia are generally stable and free of challenges to their legitimacy. The strength of Indonesia's institutions was tested by the immense scale and breadth of the COVID-19 pandemic.

In response to the medical, economic, and social challenges posed by COVID-19, President Joko

Widodo signed an unprecedented government regulation in lieu of law (Perppu) in April 2020. This allowed the government's budget deficit to overshoot the 3% of GDP legal limit during the ensuing three calendar years. The regulation also permits Bank Indonesia (the central bank) to purchase bonds in the primary bond market on a last resort basis. The Perppu allows the government to spend more and ease revenue collection to support the economy and address the evolving public health crisis through the end of 2022.

Indonesia's economic outlook faces fresh risks, largely stemming from the ongoing conflict in Ukraine. Although higher prices of key export commodities including coal, nickel, copper, and natural gas help corporate earnings and fiscal revenues, the conflict also poses downside risks to external demand and global economic growth. Further, domestic consumption growth could be challenged by higher consumer prices of basic goods such as food and cooking oil. While pandemic-related risks have dramatically receded over the past year, the advent of new variants of concern would pose an additional downside risk to our growth projections.

Indonesia's GDP per capita, which we estimate is nearly US$4,700 this year, is low relative to that of most investment-grade peers. Nonetheless, Indonesia's strong per capita trend growth of approximately 3.2% should help to alleviate this condition. We expect the country's long-term growth rate to remain well above the median achieved by its peers.

Indonesia's constructive structural dynamics will underpin the economy's outperformance. We believe the Job Creation law passed in 2020 will improve the business environment and reduce red tape, boosting investment and increasing the economy's potential growth rate. Key provisions in the law are a lower corporate tax rate and more flexible labor market policies that should help to generate jobs, especially in manufacturing. The law is facing a legal challenge that may require further legislative efforts to ensure it remains in force beyond 2023. Our base case assumes that this process will be resolved, maintaining the key reform initiatives as initially passed.

Flexibility and performance profile: Indonesia's external balance sheet is quickly improving on better terms of trade, with fiscal consolidation proceeding gradually

- Indonesia's external position has stabilized following a pandemic-driven deterioration in 2020. Continued improvement in terms of trade will lead to strong growth in current account receipts this year.
- Stronger revenue performance is helping the government to consolidate its fiscal position, and we expect deficits to fall further over the next two to three years.
- However, Indonesia faces an increasing interest burden on its debt stock owing to a faster rise in global inflation and interest rates than we previously expected.

Indonesia is making headway toward restoring its historically moderate fiscal deficits. The general government achieved a fiscal deficit of about 4.7% of GDP in 2021, considerably lower than the 6.1% shortfall in 2020. We expect the deficit to decline further this year, to 4% of GDP, as revenue growth continues to outperform owing to much higher commodity prices and an accelerated normalization of economic activity.

The Perppu adopted in 2020 allows the government to run fiscal deficits exceeding 3% of GDP through the end of 2022, after which Indonesia's long-standing fiscal rule will limit shortfalls to 3% or less. We forecast the government will be able to reduce its deficit to 3% of GDP. However, lower global economic growth related to the Ukraine conflict and the potential for further pandemic-related developments are prescient risks to this outcome.

Indonesia's net general government debt stock will remain higher than pre-pandemic levels, even after the government has further consolidated its deficits. We expect net general government debt to increase by an average of 3.1% per year over 2022-2025.

Indonesia's narrow revenue base is an additional constraint on the ratings. A higher debt stock and rising interest rates have exerted additional upward pressure on the sovereign's interest burden. We expect Indonesia's interest to revenue ratio, a key metric of operational efficiency, to average just below 15% over the next three to four years. In our view, a healthy recovery in government revenues will be necessary to keep this ratio from rising above 15% on a more sustained basis. Similarly, the trajectory of local and global interest rates will also be an important driver of Indonesia's interest burden.

Bank Indonesia has partially helped to offset the interest burden from the government's higher debt stock. However, Indonesia bears risks should global interest rates continue to rise and remain elevated for a more extended period.

The Indonesian government's external debt-servicing remains subject to some foreign exchange risk. However, foreign-currency-denominated debt has fallen to well below 40% of total debt over the past year owing to a much higher issuance of local currency debt. Foreign ownership of rupiah-denominated government bonds as a proportion of the total outstanding stock has also fallen sharply, primarily reflecting much higher marginal purchasing by domestic entities including Bank Indonesia and commercial and state banks.

Nevertheless, Indonesia has retained strong access to markets and foreign direct investment in recent years, even during periods of acute external volatility.

We expect Indonesia's total external debt--net of liquid assets held by the public and financial sectors—as a share of current account receipts (CARs) to fall well below 100% on an annual basis through 2025. This position has materially improved following a deterioration in 2020. Higher market prices for key Indonesian commodity exports such as coal, copper, natural gas, and nickel, along with solid demand dynamics, are driving rapid growth in current account receipts. Policies incentivizing higher value-added processing of mineral ores are also helping to solidify higher export receipts.

Indonesia's foreign exchange reserves are hovering near US$140 billion, supported by current account dynamics. We forecast gross external financing needs will continue to average slightly less than 90% of CARs plus useable reserves through 2025.

Bank Indonesia has been an important institution supporting the country's ability to sustain economic growth and attenuate economic or financial shocks. The central bank has purchased government bonds on the primary market and through private placements since the onset of the pandemic to help the government to manage its borrowing costs as the debt stock rose.

In August 2021, an extension of the scheme for sharing the debt burden between the Ministry of Finance and Bank Indonesia was rolled out. The central bank could participate in the financing of healthcare and humanitarian efforts to cope with the pandemic. Under the scheme, Bank Indonesia will purchase government securities at a value up to Indonesian rupiah (IDR) 439 trillion (US$30.5 billion) through end 2022, and will bear all interest costs for securities totaling IDR98 trillion.

Moreover, all debt issuance under this program will be via private placement based on the central bank's three-month reverse repo rate.

The scale of Bank Indonesia's activity in the primary market, and the central bank's perceived degree of independence, will be important determinants of its impact on financial stability. Thus far, there are few indications that either Bank Indonesia's primary market purchases or the debt burden sharing agreement have led to materially higher inflation expectations or upward pressure on bond yields. This suggests that the market has generally digested these developments without any significant concern. We expect purchases to be wound down at the end of the year, though the related securities may remain on Bank Indonesia's balance sheet for longer.

Bank Indonesia has had significant operational independence to pursue its monetary policy target since July 2005, when it formally adopted the Inflation Targeting Framework. The central bank 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.

Bank Indonesia has also relied increasingly on market-based instruments in implementing its monetary policy, and 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 subject to intermittent intervention.

Key Statistics

Indonesia - Selected Indicators

Economic indicators (%)	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**
Nominal GDP (bil. LC)	12,401,728.5	13,589,825.7	14,838,756.0	15,832,657.2	15,438,017.5	16,970,789.2	18,873,433.2	20,616,794.1	22,480,166.1	24,382,239.6
Nominal GDP (bil. $)	931.9	1,015.6	1,042.3	1,119.1	1,058.7	1,186.1	1,306.1	1,410.2	1,526.1	1,647.7
GDP per capita (000s $)	3.6	3.8	3.9	4.1	3.9	4.3	4.7	5.0	5.4	5.7
Real GDP growth	5.0	5.1	5.2	5.0	(2.1)	3.7	5.1	4.8	4.9	5.0
Real GDP per capita growth	3.8	3.8	4.0	3.9	(3.1)	2.6	4.1	3.8	3.9	4.0
Real investment growth	4.5	6.2	6.7	4.5	(5.0)	3.8	5.0	5.6	5.2	5.3
Investment/GDP	31.9	32.6	35.1	33.7	29.9	32.5	31.1	31.4	31.5	31.5
Savings/GDP	30.1	31.0	32.1	31.0	29.5	32.8	31.5	30.4	30.2	30.1
Exports/GDP	19.1	20.2	21.0	18.6	17.3	21.6	23.1	22.0	21.4	20.9
Real exports growth	(1.7)	8.9	6.5	(0.5)	(8.1)	24.0	7.7	2.0	4.3	4.7
Unemployment rate	5.6	5.5	5.3	5.2	7.1	6.5	5.7	5.4	5.2	5.1
External indicators (%)										
Current account balance/GDP	(1.8)	(1.6)	(2.9)	(2.7)	(0.4)	0.3	0.4	(0.9)	(1.2)	(1.4)
Current account balance/CARs	(9.3)	(7.7)	(13.1)	(13.8)	(2.3)	1.3	1.5	(4.1)	(5.5)	(6.3)
CARs/GDP	19.5	20.7	22.4	19.7	18.3	22.3	23.7	22.8	22.4	22.1
Trade balance/GDP	1.6	1.9	(0.0)	0.3	2.7	3.7	3.9	2.5	2.1	1.9
Net FDI/GDP	1.7	1.8	1.2	1.8	1.3	1.4	1.3	1.3	1.3	1.3

Indonesia - Selected Indicators (cont.)

Economic indicators (%)	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Net portfolio equity inflow/GDP	0.1	(0.4)	(0.5)	(0.1)	(0.5)	0.2	(0.3)	(0.3)	(0.3)	(0.3)
Gross external financing needs/CARs plus usable reserves	94.2	92.1	95.9	98.2	88.6	87.3	87.3	88.6	89.2	89.2
Narrow net external debt/CARs	102.2	96.0	100.9	115.6	132.6	90.1	74.4	70.6	66.4	64.3
Narrow net external debt/CAPs	93.4	89.1	89.2	101.6	129.6	91.2	75.5	67.8	62.9	60.5
Net external liabilities/CARs	205.4	174.5	153.3	171.5	164.2	117.2	98.5	96.4	94.1	92.0
Net external liabilities/CAPs	187.9	162.0	135.5	150.8	160.6	118.7	100.0	92.6	89.2	86.6
Short-term external debt by remaining maturity/CARs	39.7	35.5	36.3	38.3	45.2	33.4	29.7	27.5	26.3	25.3
Usable reserves/CAPs (months)	6.4	6.2	5.9	5.8	7.8	6.2	5.7	5.6	5.4	5.4
Usable reserves (mil. $)	116,373.6	130,231.6	120,663.1	129,172.0	135,934.3	144,930.8	156,529.8	163,298.7	173,523.9	181,268.2
Fiscal indicators (general government; %)										
Balance/GDP	(2.5)	(2.5)	(1.7)	(2.2)	(6.1)	(4.7)	(4.0)	(3.0)	(2.7)	(2.5)
Change in net debt/GDP	2.7	2.3	3.2	2.2	7.4	5.1	4.1	3.1	2.7	2.5
Primary balance/GDP	(1.0)	(0.9)	0.0	(0.5)	(4.1)	(2.7)	(1.9)	(0.8)	(0.5)	(0.2)
Revenue/GDP	14.3	14.1	14.9	14.2	12.1	14.0	14.5	14.9	15.0	15.2
Expenditures/GDP	16.8	16.6	16.6	16.4	18.2	18.7	18.5	17.9	17.7	17.7
Interest/revenues	10.3	11.3	11.7	12.3	16.8	14.2	14.3	14.9	15.0	14.9
Debt/GDP	28.4	29.0	30.1	30.6	39.8	41.2	41.2	40.9	40.3	39.7
Debt/revenues	198.3	205.8	202.2	215.2	328.6	294.0	284.2	274.2	268.6	261.5
Net debt/GDP	26.1	26.2	27.2	27.6	35.7	37.6	37.9	37.8	37.4	37.0
Liquid assets/GDP	2.2	2.9	3.0	2.9	4.0	3.6	3.3	3.1	2.9	2.7
Monetary indicators (%)										
CPI growth	3.0	3.6	3.1	2.8	2.0	1.6	3.2	3.1	3.0	2.9
GDP deflator growth	2.4	4.3	3.8	1.6	(0.4)	6.0	5.8	4.3	3.9	3.3

Indonesia - Selected Indicators (cont.)

Economic indicators (%)	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Exchange rate, year-end (LC/$)	13,436.0	13,548.0	14,481.0	13,901.0	14,105.0	14,269.0	14,550.0	14,660.0	14,770.0	14,820.0
Banks' claims on resident non-gov't sector growth	9.3	7.9	12.5	5.6	(1.7)	5.3	10.0	10.0	10.0	10.0
Banks' claims on resident non-gov't sector/GDP	37.9	37.3	38.5	38.1	38.4	36.8	36.4	36.6	37.0	37.5
Foreign currency share of claims by banks on residents	9.4	9.2	9.8	8.8	7.6	7.2	12.0	12.0	12.0	12.0
Foreign currency share of residents' bank deposits	15.7	14.7	15.0	14.5	13.9	14.0	15.0	15.0	15.0	15.0
Real effective exchange rate growth	4.5	1.6	(6.3)	4.5	(1.6)	(1.4)	N/A	N/A	N/A	N/A

Sources: Bank Sentral Republik Indonesia (Economic/External Indicators), International Monetary Fund and Bank Sentral Republik Indonesia (Monetary Indicators), Directorate General of Budget Financing and Risk Management, Ministry of Finance and Bank Sentral Republik Indonesia (Fiscal/Debt Indicators).

Adjustments: None.

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 claims on 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. 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.

Ratings Score Snapshot

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, with a concomitant, gradual improvement in human development indicators. However, corruption still remains elevated.
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 (% of current account receipts) and gross external financing needs (% of current account receipts and usable reserves) as per the Selected Indicators in table 1.

Indonesia - Ratings Score Snapshot (cont.)

Key rating factors	Score	Explanation
Fiscal assessment: flexibility and performance	3	Based on the change in net general government debt (% of GDP) as per Selected Indicators in table 1.
Fiscal assessment: debt burden	4	Based on net general government debt (% of GDP) and general government interest expenditure (% of general government revenue) as per Selected Indicators in table 1.
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 seven-day repo rate, however there is some reliance on reserve requirements. 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.
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.
Local currency	BBB	

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

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- 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: Methodology For Rating Sukuk, Jan. 19, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Methodology: Criteria For Determining Transfer And Convertibility Assessments, May 18, 2009

Related Research

- Sovereign Risk Indicators, April 11, 2022. An interactive version is also available at http://www.spratings.com/sri
- Global Sovereign Rating Trends: First-Quarter 2022, April 13, 2022

- Sovereign Ratings Score Snapshot, April 7, 2022
- Sovereign Debt 2022: Asia-Pacific Central Governments To Borrow US$3.8 Trillion, April 6, 2022
- Sovereign Ratings History, April 5, 2022
- Credit FAQ: COVID And Conflict Strain Asia-Pacific Sovereigns, March 24, 2022
- Asia-Pacific Sovereign Rating Trends 2022, Jan. 28, 2022
- Default, Transition, and Recovery: 2020 Annual Sovereign Default And Rating Transition Study, April 13, 2021

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

Ratings Affirmed; Outlook Action

	To	From
Indonesia		
Sovereign Credit Rating	**BBB/Stable/A-2**	**BBB/Negative/A-2**
Ratings Affirmed		
Indonesia		
Transfer & Convertibility Assessment		
Local Currency	BBB+	
Indonesia		
Senior Unsecured	BBB	
Perusahaan Penerbit SBSN Indonesia III		
Senior Unsecured	BBB	

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors,