S&P Global Ratings

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Research Update:

Indonesia Ratings Affirmed At 'BBB/A-2'; Outlook Stable

July 4, 2023

Overview

- Indonesia has achieved rapid fiscal consolidation, backed by solid revenue growth and well-calibrated policies.
- Economic growth and external settings will stabilize further following the country's recovery from the pandemic. An improved external balance sheet will help the country weather normalizing commodity prices.
- We affirmed our 'BBB/A-2' sovereign credit ratings on Indonesia.
- The stable outlook on the long-term rating reflects our expectation that the government will maintain its prudent fiscal stance, with support from economic growth of about 5% per year.

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Rating Action

On July 4, 2023, S&P Global Ratings affirmed its 'BBB' long-term and 'A-2' short-term sovereign credit ratings on Indonesia. The outlook on the long-term rating is stable.

Outlook

The stable rating outlook reflects our expectation that Indonesia will achieve solid economic growth over the next two years. This will support prudent fiscal outcomes and stabilize debt.

Downside scenario

We may lower the ratings if Indonesia's economy slows materially, such that trend growth in real GDP per capita no longer outpaces that of peers.

Indications that changes in the net general government debt will rise consistently, and average more than 3% of GDP annually, or general government interest payments will surpass 15% of revenues on a sustained basis, will exert downward pressure on the ratings.

A significant reversal of Indonesia's current account receipts, leading to a weakening in the external balance sheet or liquidity profile, would also indicate downward pressure on the ratings.

Upside scenario

We may raise the ratings 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.

A decline in Indonesia's net debt stock to less than 30% of GDP, or interest payments below 10% of general government revenues, and a sustained decline in change in net general government debt of less than 3% of GDP per year, would indicate upward pressure on the ratings.

Rationale

Our ratings on Indonesia reflect the economy's sound growth prospects and judicious policy dynamics. Balancing these strengths are low GDP per capita, a moderate stock of public debt, and high cost of servicing debt relative to the government's limited revenue base.

Indonesia has quickly consolidated its fiscal deficit, with support from a surge in commodity prices, better domestic economic conditions, and a strong institutional commitment to sustainable fiscal policy settings. This rapid progress has helped to stabilize the government's debt stock relative to GDP, following an increase during the pandemic in 2020-2021.

Institutional and economic profile: Growth to stabilize at about 5% over the next three years, following an above-trend recovery in 2022

- We forecast real GDP growth will dip to 4.8% in 2023 from 5.3% in 2022, as external demand softens and domestic conditions normalize.
- Indonesia's real GDP growth rate will settle at about 5% through 2026, with support from gradual improvements in mineral ore processing and manufacturing.
- Elections in February 2024 will lead to a new government, although policy conditions are unlikely to change dramatically.

Real GDP growth accelerated to a multi-year high of 5.3% in 2022, powered by strong external demand for key commodities and a further reopening of the domestic economy.

We anticipate some normalization in 2023, which will moderate economic growth to 4.8%. A slower global economy will dent Indonesia's resource exports, weighing on both prices and volumes following two strong years for most commodities.

Political and policy institutions in Indonesia are generally stable and free of challenges to their legitimacy. Indonesia will hold general elections in February 2024 to elect a new president and legislative assembly.

This will mark the first change in Indonesia's president since 2014, following the conclusion of Joko Widodo's two consecutive five-year terms. The country has established a track record of democratic transitions of power over the past 20 years. We do not anticipate major policy changes, regardless of the election's outcome.

In order to address the medical, economic, and social challenged posed by the COVID-19 pandemic, President Joko Widodo signed a regulation in lieu of law (Perppu) in April 2020 to allow the government's budget deficit to overshoot the legal limit of 3% of GDP for a period of three years. The government was able to reduce its deficit to less than 3% of GDP one year ahead of schedule, burnishing its track record of sustainable fiscal policy and long-term adherence to core fiscal rule.

Indonesia's economy is likely to downshift this year as global demand cools, and domestic monetary conditions tighten. In particular, positive flow-on effects of higher commodity prices, including employment gains and surging fiscal revenues, are likely to abate.

Nevertheless, easing domestic inflation and more supportive public-sector spending ahead of elections could put a floor under private consumption growth in the second half of 2023.

Indonesia's GDP per capita, which we estimate will rise to nearly US$5,000 this year, is lower than that of most investment-grade peers. That said, the country's strong trend growth in per capita income of about 3.7% could help to narrow the gap. We expect the country's long-term growth rate to remain well above the median of its peers.

Policy improvements and healthy demographics will underpin Indonesia's economic performance. In our view, the country's Job Creation law will improve the business environment and reduce red tape, boosting investment and Indonesia's potential growth rate. Key provisions in the law will foster more flexible labor-market policies, which will help to generate jobs, especially in manufacturing. The government published the latest version of this law earlier this year.

Flexibility and performance profile: Indonesia's fiscal performance has rapidly improved and deficits below 3% of GDP should further reduce the debt stock through 2026

- Indonesia is quickly repairing its fiscal position, with the help of surging revenues and prudent expenditure management.
- Deficits below 3% of GDP will gradually reduce the government's debt stock, and relieve pressure on its interest burden, assuming revenue growth is intact.
- Following two years of rapid improvement, the country's external position will likely stabilize over the next one to two years, even as commodity prices cool.

Rapid fiscal consolidation has reduced Indonesia's deficit to less than 3% of GDP a year ahead of schedule. The fiscal deficit for the general government was about 2.3% of GDP in 2022, much lower than the 4.5% shortfall in 2021.

We expect the deficit to remain at about 2.3% of GDP in 2023, on higher revenue and continued expenditure management. The change in net general government debt, a closely related metric, will likely average 2.4% through 2026.

Despite rapid revenue growth during the past two years, Indonesia's narrow revenue base remains a constraint on the ratings. The narrow base contributes to an elevated interest burden on the government's debt stock. The extent of fiscal deficit, cost of capital, and revenue growth over the next few years will determine the country's ability to cap interest cost at below 15% of revenues, following a peak of 16.3% in 2020.

Bank Indonesia has helped to offset part of the interest burden from the government's higher debt stock. Local-currency interest rates are also well off their cycle high as domestic inflation continues to fall. Still, Indonesia bears risks should global interest rates rise further and for longer than we expect.

External debt-servicing remains subject to foreign-exchange risk. However, foreign currency-denominated debt has fallen to well below 40% of total debt, following much higher issuance of local-currency debt since 2020.

Foreign ownership of rupiah-denominated government bonds is now well below 20% of the total outstanding stock. This reflects 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 amid acute volatility in external markets.

We expect total external debt (net of liquid assets held by the public and financial sectors) as a share of current account receipts to average about 64% through 2026. This position has materially improved, following a sharp deterioration to 132.6% in 2020. Policies incentivizing higher value-added processing of nickel have helped to solidify higher export receipts. Similar policies for other mineral ores may broaden this trend once the mining industry sets up the requisite processing capacity.

Indonesia's foreign-exchange reserves have quickly recovered this year, following a decline in the second half of 2022. A current account surplus and renewed financial account inflows support this. We forecast gross external financing needs will continue to average about 90% of current account receipts plus usable reserves through 2026.

Bank Indonesia has been an important institution in supporting sustained economic growth and attenuating economic or financial shocks. The central bank purchased government bonds in the primary market and through private placements during the pandemic to help the government manage borrowing costs as its debt stock rose.

Bank Indonesia's ownership of government debt (from purchases in primary and secondary markets and private placements) has leapt to about Indonesian rupiah (IDR) 1,400 trillion, from less than IDR300 trillion in 2019. We do not anticipate rapid unwinding of this ownership position over the next few years. Extensive additional accumulation is also unlikely.

We do not believe that Bank Indonesia's sizable government debt purchases have led to materially higher inflation expectations or upward pressure on bond yields.

Bank Indonesia has been independently pursuing its monetary policy target since July 2005, when it adopted the Inflation Targeting Framework. The central bank has since managed inflation at levels in line with those of regional peers. It has contained price pressure since early the 2010s.

Consumer price index inflation fell to 3.5% year on year in June 2023, from a cycle peak of about 6.0% in September 2022, as energy and food prices abated. Bank Indonesia will likely keep its key policy rate on hold at 5.75% for the remainder of 2023, before gradually cutting rates from the beginning of 2024.

Bank Indonesia has also increasingly relied on market-based instruments to implement its monetary policy. Financial system assets have also grown steadily in recent years. Rising flexibility of the rupiah (a floating currency subject to intermittent intervention) has improved monetary flexibility. While the Omnibus Law on the Financial Sector introduced earlier this year will provide the central bank with the authority to purchase government debt securities, it can only do so during economic emergencies.

Key Statistics

Indonesia - Selected Indicators

Economic indicators (%)	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**
Nominal GDP (bil. LC)	13,589,826	14,838,756	15,832,657	15,443,353	16,976,691	19,588,446	20,952,221	22,658,033	24,586,738	26,692,069
Nominal GDP (bil. $)	1,016	1,042	1,119	1,059	1,187	1,319	1,394	1,504	1,622	1,756
GDP per capita (000s $)	3.8	3.9	4.1	3.9	4.3	4.8	5.0	5.3	5.7	6.1
Real GDP growth	5.1	5.2	5.0	(2.1)	3.7	5.3	4.8	5.0	5.1	5.1
Real GDP per capita growth	3.8	4.0	3.9	(3.1)	3.0	4.6	4.0	4.1	4.3	4.3
Real investment growth	6.2	6.7	4.5	(5.0)	3.8	3.9	3.5	5.9	5.2	5.2
Investment/GDP	32.6	35.1	33.7	29.7	32.5	35.7	35.3	35.6	35.5	35.4
Savings/GDP	31.0	32.1	31.0	29.3	32.8	36.7	35.4	35.0	34.6	34.3
Exports/GDP	20.2	21.0	18.6	17.3	21.4	24.5	22.5	22.1	22.0	21.9
Real exports growth	8.9	6.5	(0.5)	(8.4)	18.0	16.3	4.8	3.7	4.9	4.9
Unemployment rate	5.5	5.3	5.2	7.1	6.5	5.9	5.4	5.3	5.3	5.2
External indicators (%)										
Current account balance/GDP	(1.6)	(2.9)	(2.7)	(0.4)	0.3	1.0	0.1	(0.6)	(0.9)	(1.1)
Current account balance/CARs	(7.7)	(13.1)	(13.8)	(2.3)	1.3	3.9	0.3	(2.5)	(4.0)	(4.8)
CARs/GDP	20.7	22.4	19.7	18.3	22.3	25.3	23.3	22.9	22.8	22.6
Trade balance/GDP	1.9	(0.0)	0.3	2.7	3.7	4.8	3.2	2.3	1.7	1.4
Net FDI/GDP	1.8	1.2	1.8	1.3	1.5	1.1	1.3	1.3	1.3	1.3
Net portfolio equity inflow/GDP	(0.4)	(0.5)	(0.1)	(0.5)	0.2	0.1	(0.3)	(0.3)	(0.3)	(0.3)
Gross external financing needs/CARs plus usable reserves	92.1	95.9	98.2	88.5	87.0	86.2	89.8	90.0	90.9	91.0
Narrow net external debt/CARs	96.0	100.9	115.6	132.6	90.4	67.7	70.7	66.7	61.9	58.4
Narrow net external debt/CAPs	89.1	89.2	101.6	129.6	91.6	70.4	70.9	65.0	59.5	55.7
Net external liabilities/CARs	174.5	153.3	171.5	164.3	117.3	85.5	85.5	81.3	77.5	74.7

Indonesia - Selected Indicators (cont.)

Net external liabilities/CAPs	162.0	135.5	150.8	160.7	118.8	89.0	85.8	79.3	74.5	71.3
Short-term external debt by remaining maturity/CARs	35.5	36.3	38.3	45.2	33.0	27.4	28.1	25.4	24.0	22.7
Usable reserves/CAPs (months)	6.2	5.9	5.8	7.8	6.3	5.4	5.1	4.9	4.7	4.6
Usable reserves (mil. $)	130,203	120,654	129,183	135,897	144,905	137,233	144,898	150,914	159,022	164,290
Fiscal indicators (general government; %)										
Balance/GDP	(2.5)	(1.8)	(2.2)	(6.1)	(4.5)	(2.3)	(2.3)	(2.4)	(2.4)	(2.4)
Change in net debt/GDP	2.3	3.2	2.2	7.4	5.1	3.7	2.3	2.4	2.4	2.4
Primary balance/GDP	(0.9)	(0.1)	(0.4)	(4.1)	(2.5)	(0.4)	(0.2)	(0.3)	(0.3)	(0.4)
Revenue/GDP	14.1	14.9	14.2	12.5	13.6	15.2	15.0	15.0	15.0	15.0
Expenditures/GDP	16.6	16.7	16.3	18.6	18.2	17.5	17.3	17.4	17.4	17.4
Interest/revenues	11.3	11.7	12.3	16.3	14.8	13.0	14.3	14.3	13.8	13.6
Debt/GDP	29.0	30.1	30.6	39.7	41.1	40.1	39.9	39.4	38.7	38.1
Debt/revenues	206.5	202.4	215.6	319.0	301.6	264.1	266.0	262.4	258.3	254.3
Net debt/GDP	26.2	27.2	27.6	35.7	37.6	36.2	36.2	35.8	35.4	35.0
Liquid assets/GDP	2.9	3.0	2.9	4.0	3.6	3.9	3.7	3.5	3.3	3.1
Monetary indicators (%)										
CPI growth	3.6	3.1	2.8	2.0	1.6	4.2	3.9	3.5	3.4	3.2
GDP deflator growth	4.3	3.8	1.6	(0.4)	6.0	9.6	2.1	3.0	3.2	3.3
Exchange rate, year-end (LC/$)	13,548.00	14,481.00	13,901.01	14,105.01	14,269.01	15,731.00	15,000.00	15,100.00	15,200.00	15,200.00
Banks' claims on resident non-gov't sector growth	7.7	12.4	5.8	(1.2)	4.6	10.1	10.0	10.0	10.0	10.0
Banks' claims on resident non-gov't sector/GDP	35.0	36.0	35.7	36.2	34.4	32.8	33.8	34.3	34.8	35.3
Foreign currency share of claims by banks on residents	13.2	13.6	12.3	11.8	11.8	12.4	12.0	12.0	12.0	12.0
Foreign currency share of residents' bank deposits	14.7	15.0	14.5	13.9	14.0	15.6	15.0	15.0	15.0	15.0

Indonesia - Selected Indicators (cont.)

Real effective exchange rate growth	1.7	(6.3)	4.5	(1.8)	(1.5)	2.9	2.9	2.9	2.9	2.9

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 sustainable public finances. Moderate policy predictability, with possible policy shifts with changes in administration. Generally cohesive civil society.
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.
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	

Indonesia - Ratings Score Snapshot (cont.)

Key rating factors	Score	Explanation
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

- Economic Outlook Asia-Pacific Q3 2023: Domestic Demand, Inflation Relief Support Asia's Outlook, June 26, 2023
- Sovereign Ratings Score Snapshot, June 7, 2023
- Global Sovereign Rating Trends: First-Quarter 2023, April 18, 2023
- Sovereign Risk Indicators, April 10, 2023 (An interactive version of the Sovereign Risk Indicators can be found at www.spratings.com/SRI)
- Sovereign Debt 2023: Asia-Pacific Central Government Borrowing To Fall Below US$4 Trillion, March 9, 2023
- Asia-Pacific Sovereign Rating Trends 2023: A Break In The Weather, Jan. 27, 2023
- Indonesia, Nov. 22, 2022

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	
Indonesia	
Sovereign Credit Rating	BBB/Stable/A-2
Transfer & Convertibility Assessment	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, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.