

Indonesia Bond

Bond note

Oct 1, 2019

Bond price in the conservative fiscal risk tracking

Bond yield recovering. The volatility in the bond market has moved to the lower level compared to the last month as the combination of the dovish monetary policy both adopted by Bank Indonesia, regional monetary authority and also from US that considered to lose the policy amid the slower economic pace growth that has supported the better liquidity to the emerging market. However, the deterioration of the volatility would come from the combination of several factors such as the oil price shock, unpredicted intensifying of the trade war statement. The recovery in the bond market was seen in the short, medium and long maturity. The 2Yr yield declined to 6.37% or down 91bps mom, while 10yr yield decreased 1bps mom to 7.32%. The short maturity leads the gain in the bond market. **Going forward we expect that the bond would still at the mildly bullish on the back of the global monetary policy outlook and benign domestic inflation from the domestic side. The political uncertainty in US regarding President Trump and the parliament would be another additional risk that could trigger the higher demand for US bond due to the flight to quality or risk aversion.** We pencil this risk to the potential factor that could deteriorate our mildly bullish outlook on the domestic bond market.

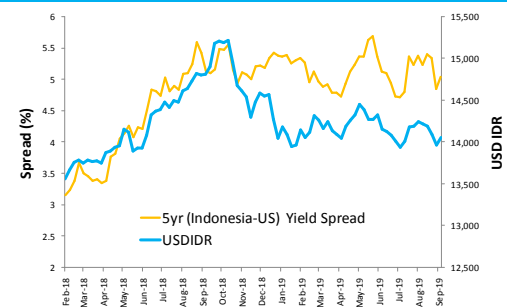
Dovish global and regional monetary policy tone as the supporting factors. The Federal Reserve lowered the target range for the federal funds rate to 1.75% - 2% during its September meeting or the second rate cut due to the ongoing concern trade tension. The several reasons or the supporting data for this expectation is slower job creation, lower and the slower capital investment against the backdrop of trade policy uncertainty and tepid global demand. The dovish tone would halt the capital outflow from the emerging market such as Indonesia and could be the supporting factor for the rupiah to move at the narrow range. This is important as we see the correlation between the 10yr Indonesia government bond yield and the rupiah which describe the dependency of the rupiah toward the global risk appetite and the foreign capital movement as the main factor behind the bond price. Another dovish tone in the Euro and China were another reason that provides the space for the Indonesia monetary authority to continue its dovish monetary policy without worrying about the negative impact on the rupiah weakening.

Indonesia monetary policy remains dovish. The Bank of Indonesia has slashed down the 7D Repo rate or the second times this year by 25bps on September to 5.5%. The slower domestic aggregate demand (5.05%yoy in 1H19) amid the external challenges was part of the reason for the BI to cut the rate. On the other hand, the slower domestic demand and the GDP growth that would only grow below 5.2% this year or somewhat at 5.1% paved the way for the BI to relax the policy. We expect the one more rate cut is possible before first quarter 2020 amid the stable domestic inflation. This would support the bond yield to move lower until the end of this year despite the limited room.

	10/1/2019	9/30/2019
USD/IDR	14190	14195
EUR/USD	1.089	1.0899
USD/JPY	108.23	108.08
USD/SGD	1.3832	1.3819

Government Bond Ownership (in trillion)		
Investor	9/27/2019	9/26/2019
BI	168.52	177.46
Bank	637.96	629.06
Foreign	1,028.02	1,028.32
Others	829.83	829.49
Total	2,664.33	2,664.33

Yield Spread (Indonesia-US) & USDIDR – Easing Pressure



Source: Bloomberg, Shinhan Sekuritas Indonesia

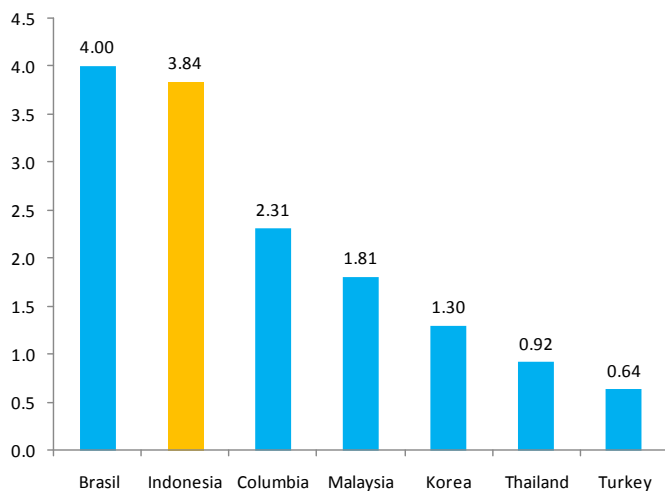
Helmi Therik, FRM
+6221 80869900
helmi.therik@shinhansekuritas.co.id

Benign inflation and attractive real yield. The inflation was at 3.3%yoy while we estimate the inflation would fluctuate at around 3% to 4% this year or remain manageable. The stable rupiah, limited inflation in administrated price and government intervention by opening the imported product has helped to stabilize the domestic inflation. This would maintain the Indonesia real yield remain attractive compares the peers which provide another reason for the capital inflow amid the external volatility. **The Indonesia real yield was at 3.8% or higher than Malaysia, Korea and Thailand at 2.17%, 1.3%, 0.92% respectively.**

Bond prices and healthy fiscal risk. The conservative fiscal deficit that set at 1.9% of GDP for 2019 and 1.76% GDP for 2020 or lower than this year point to the lesser bond supply and sending the prudence fiscal risk message to the bondholder which would increase the credibility. From the last government bond auction year to date, the total proceeds was about IDR701tn or 83% of the target. The appetite in the government bond remains sound as reflected in the bid to cover ratio at 2.86x compared to 1.97x last month. The foreign ownership in the bond market has been resiliently accelerated to IDR 1,026tn on September from IDR 1,008tnn August or implying 38.8% of the total bond market. This was as the result of the improvement of the global risk appetite due to the dovish tone. Overall, we expect the improvement of the bond price ahead on the back of the recovery of the liquidity to emerging market with a slower pace as the yield has fluctuated at our targeted estimation range.

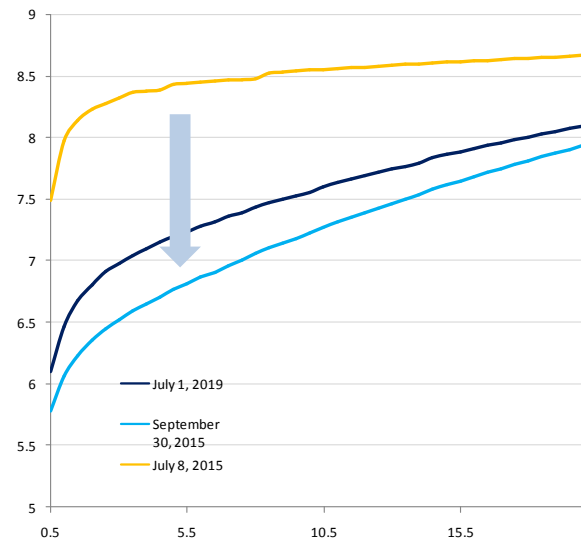
Improvement in credit risk premia with the limited room for further bond price appreciation. The credit risk premium for the Indonesia bond has reduced gradually to the level of 77bps compared to the last month at around 90bps. The appetite for the emerging market as a result of the low-interest rate outlook amid the modest economic growth has provided the room for the better credit risk premium. **However, we remain to assume the CDS fluctuate at 82bps to 90bps, the FFR at 2.25% and inflation steady at 3.5% for our model and find that the select series such FR71 would be at 7% to 7.5% as the fair yield, while FR68 at 7.3% to 7.9%. This suggests that the bond price has reached its fair price.**

Gov. Bond 10Yr real yield comparison -Indonesia real yield remains attractive



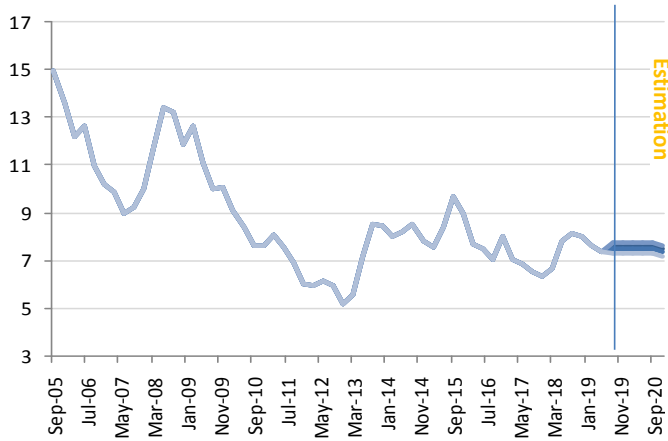
Source: MOF, Shinhan Sekuritas Indonesia

Indonesia Yield Curve



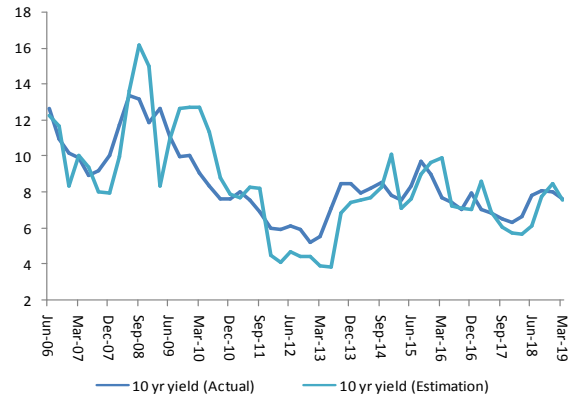
Source: Shinhan Sekuritas Indonesia Yield curve

10 Yr Yield Estimation



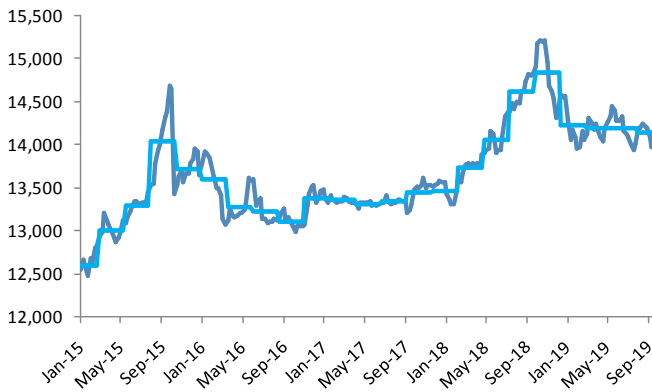
Source: Shinhan Sekuritas Indonesia Estimates

10 Yr yield actual VS estimation – Cointegrated model



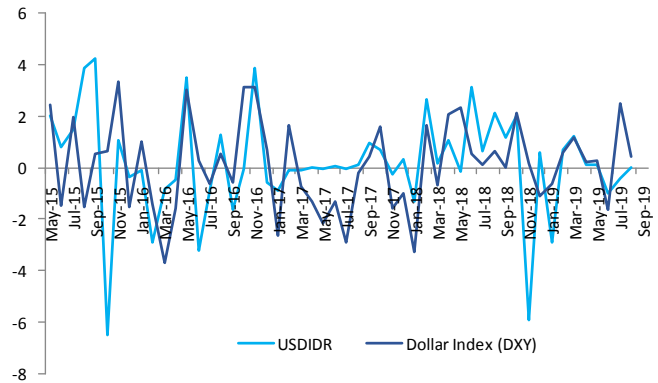
Source: Bloomberg, Shinhan Sekuritas Indonesia

USD IDR fluctuate at IDR14,000/USD



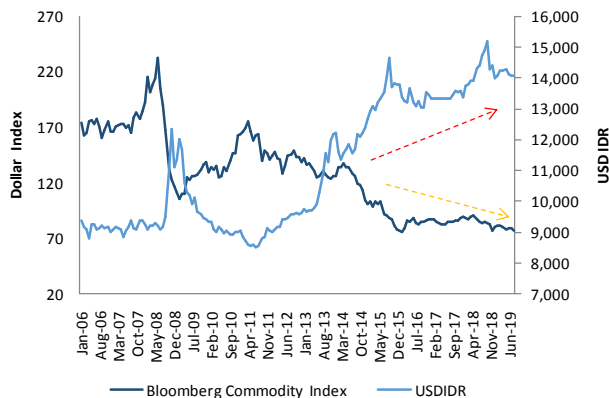
Source: Bloomberg, Shinhan Sekuritas Indonesia

USD IDR and Dollar Index (mom%), Weakening of US Dollar help to easy rupiah



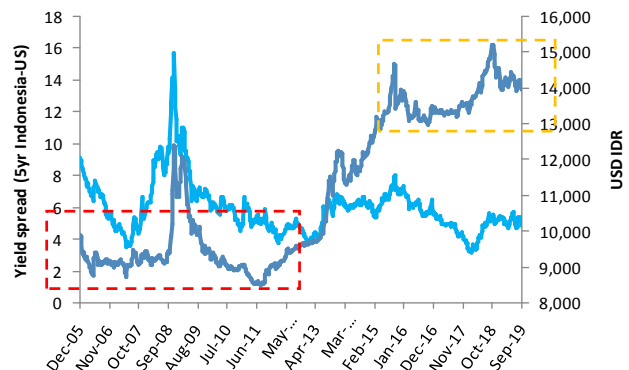
Source: Bloomberg, Shinhan Sekuritas Indonesia

The commodity price contributes to the rupiah movement- Stable outlook for rupiah ahead



Source: Bloomberg, Shinhan Sekuritas Indonesia

Rupiah and Yield Spread (5yr Indonesia-US)



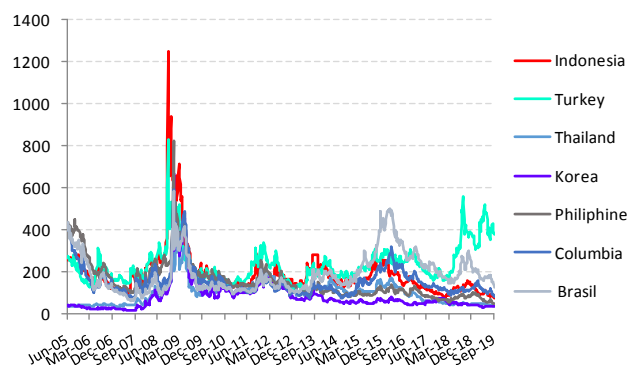
Source: Bloomberg, Shinhan Sekuritas Indonesia

Resilience foreign ownership in Indonesia Gov. Bond



Source: Bloomberg, Shinhan Sekuritas Indonesia

5Yr CDS remains below the 2008 and 2013



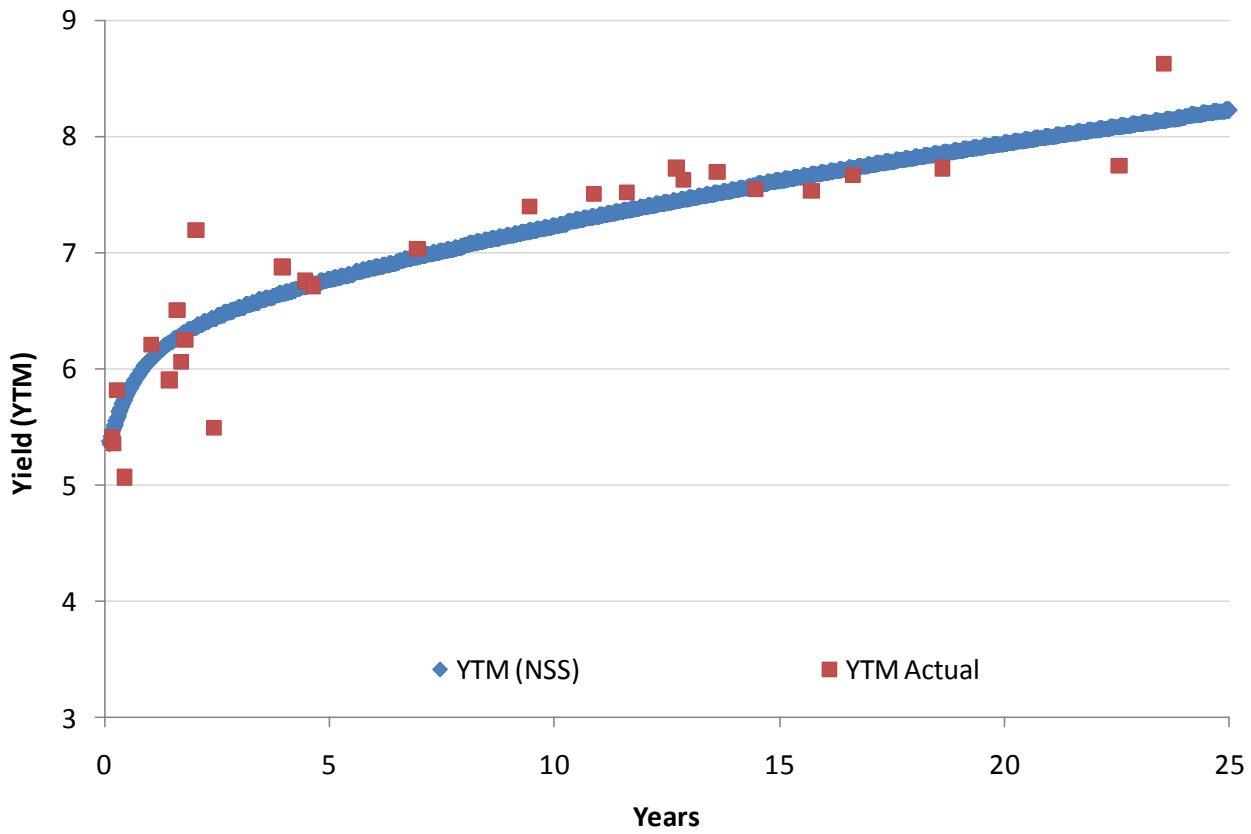
Source: Bloomberg, Shinhan Sekuritas Indonesia

Bond Valuation (Nelson Siegel Svensson Model)

Series	Tenor	Coupon	Last Price	Fair Price	Bps (+/-)	YTM	Yield Curve (NS)	Spread to YC (bps)	Trading Idea
SR009	0.44	10.3%	99.5	101.63	-2.13	5.06%	6.15%	-1.1	Over value
ORI014	1.04	12.0%	99.65	105.76	-6.11	6.20%	6.08%	0.1	Neutral
SR010	1.44	10.3%	98.4	105.44	-7.04	5.90%	6.17%	-0.3	Neutral
PBS014	1.62	10.3%	99.94	105.88	-5.94	6.50%	6.31%	0.2	Neutral
ORI015	2.04	12.0%	102	110.45	-8.45	7.19%	6.36%	0.8	Under value
SR011	2.44	10.3%	105.8	108.49	-2.69	5.49%	6.39%	-0.9	Over value
PBS019	3.96	10.3%	104.35	112.23	-7.88	6.87%	6.67%	0.2	Neutral
FR0070	4.46	12.0%	106.14	119.81	-13.67	6.75%	6.68%	0.1	Neutral
FR0077	4.63	12.0%	105.55	120.47	-14.92	6.71%	6.68%	0.0	Neutral
FR0071	9.46	12.0%	110.8	132.41	-21.61	7.39%	7.15%	0.2	Neutral
FR0073	11.63	12.0%	109.5	135.21	-25.71	7.51%	7.37%	0.1	Neutral
FR0074	12.88	12.0%	99	136.58	-37.58	7.62%	7.47%	0.2	Neutral
FR0065	13.63	11.5%	90.9	133.60	-42.70	7.69%	7.47%	0.2	Neutral
FR0068	14.47	12.0%	107.25	137.89	-30.64	7.54%	7.58%	0.0	Neutral
FR0080	15.72	12.0%	99.75	138.41	-38.66	7.53%	7.69%	-0.2	Neutral
FR0072	16.64	12.0%	105.5	139.55	-34.05	7.66%	7.69%	0.0	Neutral
FR0075	18.64	12.0%	98.4	139.17	-40.77	7.72%	7.90%	-0.2	Neutral
FR0062	22.56	6.4%	85.55	82.59	2.96	7.74%	8.10%	-0.4	Neutral
PBS005	23.56	10.3%	81.3	122.71	-41.41	8.62%	8.10%	0.5	Neutral
FR0076	28.64	12.0%	96	138.04	-42.04	7.72%	8.43%	-0.7	Over value

Source: Shinhan Sekuritas Indonesia

SSI's Fair Yield Curve Vs Actual



Source: Shinhan Sekuritas Indonesia model.



Research Team		
Helmi Therik, FRM	Head of Research	helmi@shinhansekuritas.co.id
Teuku Hendry Andrean	Research Manager	hendry@shinhansekuritas.co.id
Billy Ibrahim Djaya	Research Analyst	billy@shinhansekuritas.co.id

Office
<p>PT. Shinhan Sekuritas Indonesia Member of Indonesia Stock Exchange</p>
<p>Head Office : International Finance Center 2 Floor. 30 Jl. Jendral Sudirman Kav. 22-23 Karet Jakarta 12920 Indonesia Telp.: (+62-21) 80869900 Fax : (+62-21) 22057925</p>

Disclaimer : All opinions and estimates included in this report constitute our judgments as of the date of this report and are subject to changes without notice. This information has been compiled from sources we believe to be reliable, but we do not hold ourselves responsible for its completeness or accuracy. It is not an offer to sell or solicitation of an offer to buy any securities. Clients should consider whether it is suitable for their particular circumstances before acting on any opinions and recommendations in this report. This report is distributed to our clients only, and any unauthorized use, duplication, or redistribution of this report is prohibited.