

Investment:

Remain cheerful but beware of the rainy season

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Executive Summary

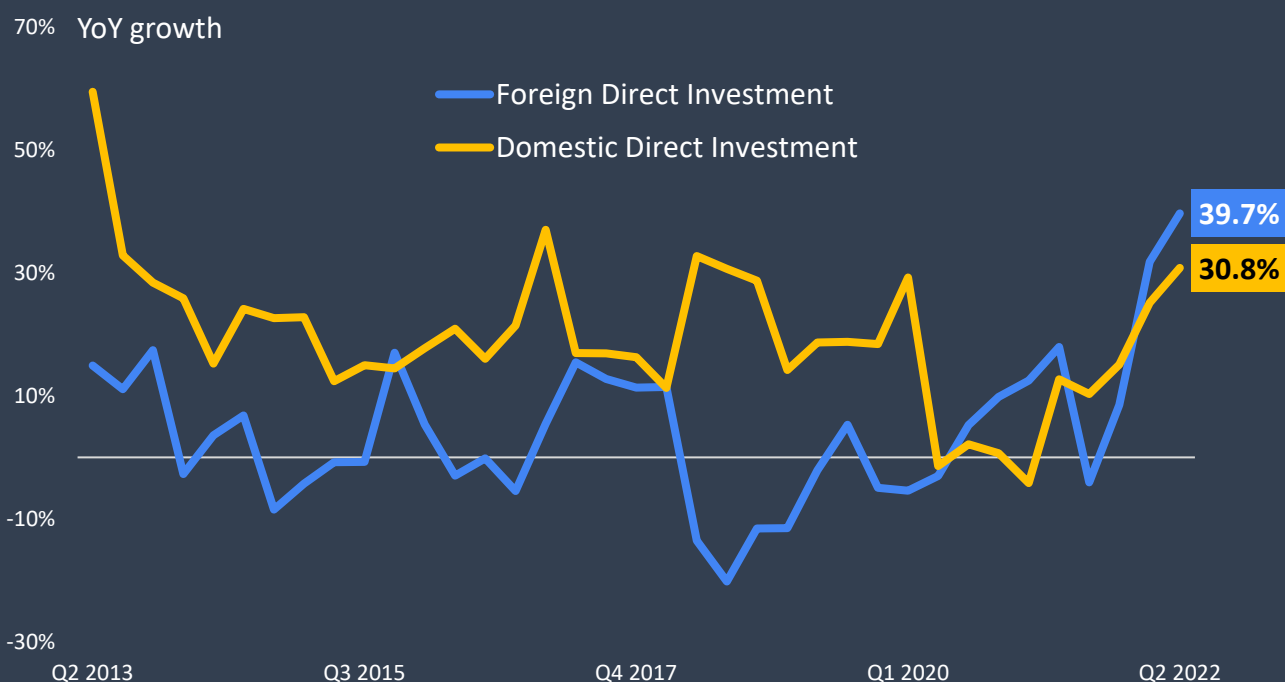
- Foreign direct investment grew by 39.7% YoY in Q2 2022, outpacing domestic direct investment (DDI), which grew by 30.8% YoY.
 - Apart from government regulation, FDI's growth trajectory appears to be influenced by the increasingly competitive global commodity market as the presently restricted market renews global interests in securing dependable supply of commodities.
 - Recovering business confidence led to private sectors taking a more active role in accelerating DDI growth while the government stepped back a little. Alas, prospects of FDI and DDI realisation may not be as stellar in the next couple of quarters due to darkening global prospects and the government's limited fiscal room.
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- The darkening global economic outlook has erased the optimism which had previously characterised the start of the year. Disrupted supply chains and market imbalances are fuelling inflationary pressures to levels unseen in the last four decades. Production costs rose higher, consumer demand began to recede, and business confidence withered along with it. However, one won't arrive at such a dismal conclusion by glancing at Indonesia's investment data in Q2 2022. Investment continues to pick up steam in Q2 2022 (**Chart 1**), strutting along the upward momentum despite the increasingly murky global economic condition.
 - Domestic direct investments (DDI), continuing its solid post-COVID growth, expanded by 30.8% YoY in Q2 2022. Last quarter's DDI is more consistent with the growing confidence in the domestic business sector as manageable inflation strengthens demand, boosting activities in the manufacturing sector that incentivize businesses to expand their operations. Adding to the positive news is that last quarter's DDI may bear less scent of government activities, as evident from lower investments in sectors with a heavy government footprint, such as utilities and transportation & communication. Indeed, the secondary (manufacturing) sector is the only one that recorded a positive DDI growth on a quarterly basis (+54.7% QoQ). In comparison, investments made to the primary and tertiary sectors dwindled by -14.2% and -7.3% respectively (**Chart 2**).
 - Accelerating DDI growth due to robust business confidence and the government's renewed support for infrastructure spending is, by any definition, good news. But what is hidden beneath this seemingly exuberant DDI number may not be all positive. We have to consider that investment data are accounted for in nominal terms. The sharp increase in the nominal DDI growth does not necessarily reflect similar growth in real terms as there is probably less 'bang for the buck' for the investment figure. Hence, the rampaging global inflation and the much stronger US Dollar's value, the dominant theme throughout

2022, would increase investment costs and may hinder further CAPEX initiatives by companies whose earnings are not in US Dollars or otherwise unable to access financing thereof.

“Structural (green) changes to the global economy are behind the optimistic outlook for foreign investments, especially in the commodity sector”.

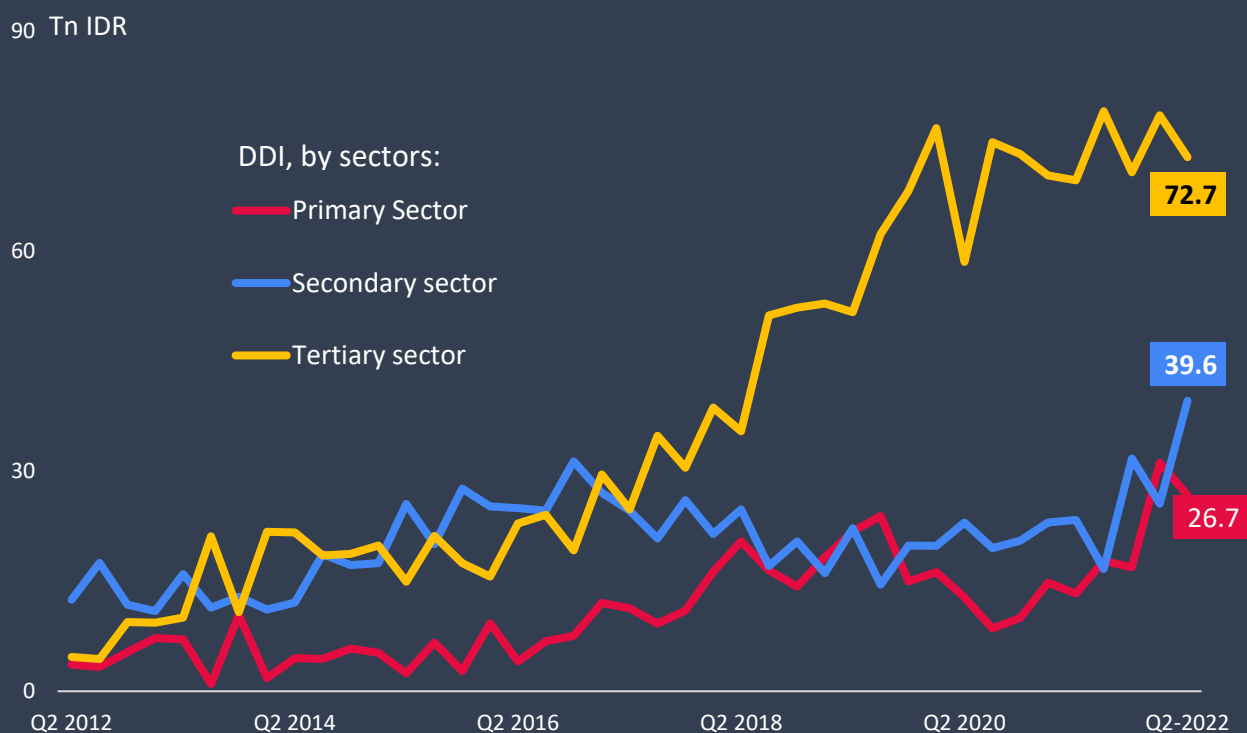
- Accelerating DDI numbers may also entail some risks. For one, expanding the manufacturing sector would require more imported machinery and intermediate materials, fuelling demand for hard currencies that could burden the IDR's value in the face of a stronger USD. The prospect of higher imports and dwindling export due to normalising commodity prices might threaten Indonesia's trade balance, the most robust defensive mechanism against the proliferation of external risks.
- The numbers are even more encouraging on the other side of the spectrum, as the watershed of global economic challenges did little to deter foreign investors from fixating their eyes on the Indonesian economy. A record-high IDR 163.2 Tn worth of foreign direct investments (FDI) flowed into the domestic economy as growth accelerated to 39.7% YoY in Q2 2022 compared to 31.8% in the previous quarter.
- It is also not surprising that FDI remains concentrated in two sectors, mining and base metals. The economic and geopolitical fallout from the Russia-Ukraine war appears to renew global interests in securing a long-term and dependable supply of commodities, especially against the prospects of a global energy crunch and energy transition. This is further supported, as we have always mentioned before, by the government's strict export ban on nickel, which forces foreign producers to invest in smelting capacities in Indonesia.
- These structural drivers are why we are still relatively sanguine about the prospects of foreign investments in the commodity sector going forward. The government's plan to extend the list of raw materials banned for exports to include copper, tin, and bauxite may also be helpful, considering the success of the nickel ban. Still, with the global economy entering a period of (potentially extended) uncertainty, we expect FDI and especially DDI growth to moderate in the coming periods, with the attendant slowdown of investment growth in the national accounts as well. This is something that the BKPM itself has acknowledged as the investment promoter agency slashed its annual target in 2022 by 19.3% to IDR 968.4 Tn.
- The upcoming announcement of the 2023 state budget draft may also foretell DDI's potential for the coming year, with odds in favour of a less stellar outcome considering that the darkening global outlook would necessitate heightened subsidy and social protection spending. The government is also obliged to comply with the 3% budget deficit redline, further limiting the government's fiscal room to participate in projects that would boost next year's DDI number. The economy is indeed gearing up for a more challenging season, and moderating investments would certainly be on the to-do list of one or two investors.

Chart 1. Foreign and domestic fixed-asset investments remained hot despite the increasingly challenging global economic condition



Source: BKPM

Chart 2. DDI in the secondary sector remain in full swing while investment in the (partly government-driven) tertiary sector plateaued



Source: BKPM

Selected Macroeconomic Indicators

Table 1. FDI realization by sector (USD Million, current price)

	2019	2020	2021	Q3-2021	Q4-2021	Q1-2022	Q2-2022
PRIMARY SECTORS	3,293.8	3,280.0	4,826.2	1,177.2	1,676.8	1,636.5	1,695.1
Food crops, plantations, & livestock	946.9	1,184.2	950.6	274.9	190.7	456.2	401.1
Forestry	36.3	42.6	41.4	8.4	9.0	8.0	23.8
Fishery	54.1	48.1	17.2	2.8	4.0	1.2	12.0
Mining	2,256.5	2,005.1	3,816.9	891.1	1,473.0	1,171.1	1,258.2
SECONDARY SECTORS	9,550.8	13,202.2	15,802.8	3,628.0	3,898.6	5,429.2	6,114.3
Food industry	1,272.2	1,592.2	2,337.4	516.0	319.2	685.9	552.7
Textile industry	238.9	279.8	312.1	81.1	67.9	126.1	109.5
Leather goods & footwear industry	188.2	214.0	484.9	97.8	200.2	96.8	163.1
Wood industry	94.9	84.7	68.1	19.2	20.8	22.6	112.0
Paper & printing industry	446.1	942.8	952.5	346.0	359.6	156.4	504.8
Chemical & pharmaceutical ind.	1,486.1	1,742.6	1,656.5	483.0	355.3	854.0	896.5
Rubber & plastic industry	291.6	291.4	262.2	65.5	38.0	67.2	72.4
Non metallic mineral ind.	475.0	248.3	327.0	34.1	72.7	101.5	94.1
Metal, machinery, electronics, & other instruments	4,058.6	6,570.5	7,653.8	1,657.7	2,146.4	2,716.7	3,283.1
Transport equipment & other transport	754.1	941.9	1,501.9	268.9	271.8	542.0	236.0
Other industries	245.3	294.0	246.3	58.7	46.6	60.0	90.1
TERTIARY SECTORS	15,364.3	12,183.8	10,464.2	2,266.2	2,795.9	3,193.3	3,560.9
Electricity, gas and water supply	5,921.2	4,613.9	2,938.6	497.0	995.8	982.5	836.3
Construction	161.6	189.5	93.3	53.7	22.7	24.5	31.0
Trade & reparation	421.3	434.1	463.8	70.3	114.4	184.5	242.8
Hotel & restaurant	625.9	441.1	432.2	107.4	136.9	155.3	95.6
Transport, warehouse & telco	4,727.8	3,580.5	3,159.1	617.2	782.1	872.1	881.4
Real estate, industrial estate & business activities	2,888.6	2,191.4	2,186.4	511.3	401.0	516.1	997.4
Other services	617.9	733.3	1,190.7	409.3	342.9	458.3	476.4
TOTAL	28,208.9	28,666.0	31,093.2	7,071.4	8,371.3	10,259.0	11,370.3

***Gold = Top 5 sectors for the year**

Source: BKPM

Table 2. DDI realization by sector (IDR Billion, *current price*)

	2019	2020	2021	Q3-2021	Q4-2021	Q1-2022	Q2-2022
PRIMARY SECTORS	78,884.9	47,580.1	62,766.7	17,764.2	16,905.2	31,125.0	26,713.3
Food crops, plantations, & livestock	43,598.9	32,096.6	29,374.7	7,494.6	5,793.4	10,073.3	9,814.8
Forestry	9,366.5	1,163.6	6,862.7	2,166.0	4,392.4	2,526.0	1,672.1
Fishery	247.5	564.9	1,012.1	153.1	251.7	140.1	242.5
Mining	25,672.0	13,755.0	25,517.1	7,950.5	6,467.6	18,385.6	14,983.9
SECONDARY SECTORS	72,673.8	82,817.9	94,698.7	16,672.4	31,724.1	25,575.7	39,575.1
Food industry	36,602.6	27,872.7	26,517.5	5,736.6	6,089.8	9,715.9	14,485.7
Textile industry	1,312.6	2,103.3	1,972.4	376.8	436.9	587.9	2,008.4
Leather goods & footwear industry	77.3	394.7	700.4	318.0	238.9	61.1	127.8
Wood industry	1,585.5	1,263.4	1,143.7	321.7	418.1	733.3	855.1
Paper & printing industry	2,950.2	3,745.9	7,833.6	288.8	2,144.9	1,584.1	3,009.7
Chemical & pharmaceutical ind.	9,484.2	22,526.1	23,363.6	3,864.4	11,123.6	4,657.1	8,226.0
Rubber & plastic industry	3,069.1	4,428.7	7,803.1	624.8	3,953.4	1,062.2	1,941.3
Non metallic mineral ind.	3,572.9	5,861.9	6,522.2	707.3	1,082.1	1,231.3	1,783.0
Metal, machinery, electronics, & other instruments	9,334.8	10,013.6	16,190.9	3,732.5	5,511.2	3,652.9	4,419.9
Transport equipment & other transport	2,608.2	2,556.6	1,459.3	504.9	276.4	385.7	677.0
Other industries	2,076.5	2,051.0	1,192.0	196.6	448.8	1,904.2	2,041.2
TERTIARY SECTORS	234,933.2	283,137.7	289,598.5	79,019.7	70,708.0	78,481.1	72,728.8
Electricity, gas and water supply	37,164.2	35,518.8	38,727.7	7,864.5	7,715.5	8,970.7	6,297.9
Construction	55,090.7	68,289.2	39,569.4	10,339.8	9,742.5	6,229.7	11,127.2
Trade & reparation	13,662.9	16,748.4	22,432.3	5,402.8	6,051.0	6,840.7	10,646.0
Hotel & restaurant	16,163.6	10,203.1	17,819.3	3,851.1	5,064.6	5,000.4	7,233.3
Transport, warehouse & telco	68,082.5	93,282.8	61,241.6	17,548.6	15,915.3	26,966.7	12,932.0
Real estate, industrial estate & business activities	27,796.5	44,852.8	85,497.8	20,625.9	22,724.4	17,467.4	12,428.4
Other services	16,972.7	14,242.6	24,310.4	13,387.0	3,494.7	7,005.5	12,064.0
TOTAL	386,491.9	413,535.7	447,064.0	113,456.30	119,337.35	135,181.80	139,017.20

***Gold = Top 5 sectors for the year**

Source: BKPM

Indonesia – Economic Indicators Projection

	2017	2018	2019	2020	2021	2022E
Gross Domestic Product (% YoY)	5.1	5.2	5.0	-2.1	3.7	4.8
GDP per Capita (US\$)	3877	3927	4175	3912	4350	4615
Consumer Price Index Inflation (% YoY)	3.6	3.1	2.7	1.7	1.9	4.7
BI 7 day Repo Rate (%)	4.25	6.00	5.00	3.75	3.50	4.50
USD/IDR Exchange Rate (end of year)**	13,433	14,390	13,866	14,050	14,262	15,070
Trade Balance (US\$ billion)	11.8	-8.5	-3.2	21.7	35.3	39.2
Current Account Balance (% GDP)	-1.6	-3.0	-2.7	-0.4	0.3	0.9

** Estimation of Rupiah's fundamental exchange rate

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