FLASH NOTES

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What do we see in 2019?

BATAVIA Institute

For Professional & Institution Investors Only

Our base case is the external headwinds (i.e. oil price, USD, UST yield, concern on Emerging Market, trade tension, etc) to ease/moderate going into 2019. Hence, this should bode well for Emerging Market, including Indonesia, amid slower global growth and less accommodative monetary policy. Meanwhile, domestic growth continues to be supported by government spending and populist policy toward to mass market segment toward election in April 2019.

What to expect in 2019?

Global growth: synchronized slowdown across major economies, driven by combination of 1) less accommodative monetary policy, 2) less supportive fiscal spending, 3) implication of trade policies. China's economy may slowdown further, but ready to ease their policies later on, which should put a floor to their economy. However, the stimulus is least likely to be positive for the rest of the world as previous intervention. On monetary policy, quantitative easing flow and rising interest rate are less supportive than before, but liquidity is still abundant. The peak of interest rate cycle may come earlier than expectation, so this may put a cap on US Treasury yield.
The implication of trade tension to real economy start to kick in, especially on China and US, which also contribute to the slower global growth. Despite future US-China's deal is still uncertain for now, the peak of US-China trade tension maybe behind us after the G20 meeting back in Nov 2018.

USD: the worst behind us? Strong USD happened in 2018, thanks to strong US growth and trade tension, put pressure on Emerging Market currency including Rupiah. But, this may wane through 2019, due to narrowing 1) growth differential (US's economy slow faster) and 2) unprecedented rate differentials between US against the rest-of-the-world.

Oil price: supply and demand remain tight, before getting better. Upside risk of supply from Saudi Arabia, US and Russia offset by downside risk from Iran, Venezuela and Libya. Additional supply from US shale oil may come to the market by the end of 2019 as infrastructure bottlenecking resolve later on. If this is true, this should be good news for net oil importer countries, including Indonesia. Every US$10/barrel decline in oil price, translate to 0.3% improvement in Indonesia's current account deficit.

Negative index return in 2018 amid positive earning growth bring **valuation at more reasonable level**. As of Nov 2018, JCI's 12 month rolling P/E is at 14.3X, slightly below its mean of 14.5X.

Meanwhile, earning expectation had come down since mid 2018 so earning risk is relatively manageable unless IDR weaken significantly.

How about us?

Easing external headwind (as we discuss above) should result to a less volatile Rupiah and domestic financial market (both equity and bond), which bring investors focus back to fundamental/earning. Meanwhile, foreign ownership in equity already at unprecedented low level. Other than external factor, Rupiah also need to see improvement in current account/trade balance. Import auto adjustment from Rupiah depreciation and lower oil price should help current account balance gradually. But, there could be a risk that export may contract faster than import in the short term.

On growth, we are optimistic that growth trajectory may continue into early 2019, on the back of government populist policy, fiscal pumping and reversal movement of IDR. After election, we expect government bring the reforms on track, which give certainty and confidence to the investment climate.

Macro and market forecast

	2016	2017	2018E	2019E
BI rate *	6.50%	N/A	N/A	N/A
7-day reverse repo	4.75%	4.25%	6.00%	6.00-6.50%
GDP	5.0%	5.1%	5.1-5.2%	5.1-5.2%
Oil price/brl	US$53.7	US$60.4	US$55 - 65	US$60 - 75
CPI	3.02%	3.61%	3.1-3.4%	4.0-4.5%
CAD	1.7%	1.7%	2.8-3.1%	2.7-3.0%
USD/IDR	13,473	13,555	14,000-15,000	14,500-15,500
JCI	5,297	6,356	6,100-6,300	6,800-7,000
EPS growth	4%	12%	5-8%	7-10%
10-y bond	7.97%	6.32%	7.6-7.9%	7.6-8.0%

* change to 7-day reverse repo, starting Aug'16