Inside Indonesia

Momentum Play

Indonesia's strong GDP data adds oomph to positive sentiment

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- **At 5.18%, Indonesia's Q2 GDP data comes better than the 5.0% we pencilled in, and marks an acceleration from Q1's 4.92%. For good measure, it is also the strongest quarter achieved by the economy since President Jokowi took power in late 2014.**
- **Encouragingly, private consumption regained some vitality, helped by Bank Indonesia's frontloaded rate cuts this year, while government spending helped to boost overall growth too.**
- **Overall, a print that should help to boost the success rate of the Tax Amnesty program, by reminding savvy Indonesians that more rewarding investment opportunities might be had at home than abroad.**

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From good to great?

Indonesia is on a roll. Having pushed through a potentially game-changing Tax Amnesty Law, President Jokowi offered market another pleasant surprise just last week. Instead of a humdrum sort of reshuffle, he managed to coax the well-respected Sri Mulyani away from the cushy, high-paying job at the World Bank to return home and re-helm the Finance portfolio.

And just this morning, the Q2 GDP data shows that the Indonesian economy has a lot more momentum going for it, than market had expected. At 5.18% yoy, the GDP data shows Indonesia's growth at its best since President Jokowi took over in Oct 2014. It has also more than made up for the disappointment in Q1 GDP data a few months ago.

Source: Bloomberg, OCBC.

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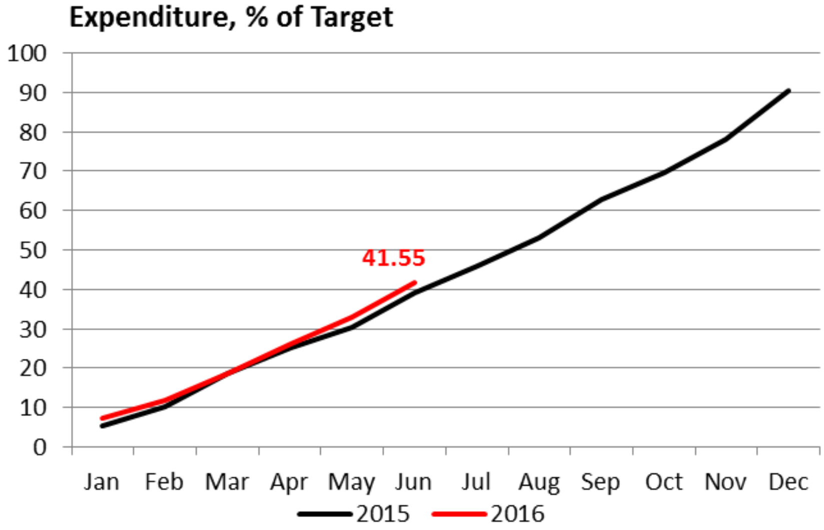
Looking more closely beyond the headline print, we also see some largely encouraging signs. First and foremost, the crucial private consumption regained some vitality, notching up a gain of 5.04%yoy in Q2, compared to 4.94% of the previous quarter. While some seasonal factor may be at play – with more days of the Ramadan fasting month falling into Q2 this year compared to the last – there is likely to be some boost starting to be seen from the frontloaded monetary policy easing early this year by the central bank, as well.

Meanwhile, support from government spending has also come forth more readily in Q2. Public consumption portion of GDP grew by 6.28%yoy in Q2, markedly higher than the 2.93% yoy posted in Q1. With the government focusing on disbursement of planned expenditure, this should not come as a surprise. It's also reflected by a faster pace of spending of full-year budget in the first half of this year – at 41.55% as of end-June – compared to the same period last year.



Source: CEIC, OCBC.

Elsewhere, things look less rosy even if there is no cause for concern at this stage. Specifically, investment activities have yet to pick up all that encouragingly. Going by the GDP breakdown, gross fixed capital formation grew at 5.06%yoy. This is not too bad in and of its own, given the global uncertainties, but is still lower than the 5.57% printed in the previous quarter.

All in all, the GDP numbers can be characterized as a set of prints reflecting that things are going good for Indonesia, but not quite great yet.

To get Indonesia going from "Good to Great", to shamelessly borrow a phrase from the management guru Jim Collins, the government still has work to do. And, an upside surprise it may have been, today's GDP data should act as a spur for more momentum from the government, simply because it reflects what Indonesia can yet achieve.

Here, the near-term focus has to be still the success of the Tax Amnesty program. In and of its own, the GDP data itself is helpful for this cause. If nothing else, it showcases the tremendous growth potential and investment opportunities that the country presents. For savvy (and loaded) Indonesians, the fact that their very own country can still print a better-than-expected encouraging growth rate in such a testy global environment serves as reminder that they should take another look at their risk-reward calculations, which is more likely than not to tip in favour of putting more investment money to work in the motherland than elsewhere.

Still, as we mention in last week's "*Pincer Movement*" note, the new Finance Minister has her work cut out in terms of better utilizing such fortuitous backdrop. Apart from the necessary groundwork of preparing her staff to offer more compelling service and offering more helpful answers the queries of potential amnesty applicants, she has also started to prepare as well for the unfortunate case of less enthusiastic take-up rate of the program.

To begin with, she has moved to adjust the targets for this year's budget, estimating a revenue shortfall of IDR219tn that would bring fiscal deficit from 2.35% of GDP to 2.5%. Her boss, the president, has also talked about instructing various ministries and agencies "to be disciplined in reducing expenditure". In a tone that might sound familiar to those facing belt-tightening in the corporate world too, Jokowi reportedly said that he has demanded again and again, for them to "study each [expenditure] point, one by one, and in detail."

Hence, as much as government spending did help to lift up growth in Q2, its help cannot be counted upon as readily in the coming quarters. With private consumption already playing its part and any forceful exports recovery being a pipe dream in this global environment, the onus thus falls on investment spending. That, in turn, is going to be a function of whether Jokowi and his team can continue to show enough reform momentum to convince investors – be it foreign or domestic – to pile in real money into the country.

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