Key Figures

- GDP Growth* (Q3 '18)
  5.1%
- GDP Growth* (FY 2018)
  5.1-5.2%
- GDP Growth* (FY 2019)
  5.2-5.3%
- Inflation (y.o.y. Sept '18)
  2.88%
- Credit Growth (y.o.y. Sept '18)
  12.69%
- Trade Balance (Q2 '18)
  USD -1.02 billion
- Current Account (Q2 '18)
  -3.04 %

*) *Forecast*

Current Account Deficit: The Unresolved Homework

Highlights

- GDP to grow 5.1% in Q3, 5.1-5.2% in FY2018, and slightly accelerated to 5.2-5.3% in FY2019
- Slower-than-expected manufacturing growth in 1H2018 and slower investment realization are likely caused by combination of increased global volatility, relatively rapid depreciation, and upcoming national election
- Consumption growth will exceed 5% for the whole 2018 and accelerate in 2019 if inflation remains under control; this will face a challenge if government is forced to hike retail fuel price
- Current account deficit will be remained challenged as full-scale trade war between US and China looms
- Although better than 2018, FDI will still perform below its potential due to barriers to trade and invest in Indonesia

Current account deficit and political climate will be two of the key themes that will affect Indonesia's economy in 2019. Relatively weak export performance due to overreliance on raw materials export, particularly on crude palm oil, and higher imports due to infrastructure drives have driven Indonesia to run trade deficit again in Q2 and Q3 2018, and we do not see room for trade position to improve significantly in 2019. The downside risk to Indonesia's trade performance will also be considerable as full-scale trade war threatens to reduce GDP growth in China and United States, which directly accounts for 24.2% of Indonesia's export value in 2017. These trade risks, along with rising interest rate and drop in FDI to Indonesia, will put pressure additional on export and Rupiah exchange rate in the medium term.

Table 1: LPEM FEB UI GDP Growth Forecast

Q3 2018	FY 2018	FY 2019
5.1%	5.1-5.2%	5.2-5.3%

Political dynamics may have mixed effects on growth and other macroeconomic indicators in 2019. On one side, campaign spending, politically driven measures by the incumbent administration to hold retail fuel price, and introduction of new spending packages such as Dana Kelurahan (sub-district fund) will further boost domestic consumptions in the first half of 2019. However, decision to hold retail fuel price may not be sustainable for long, given the rising crude oil prices and its impact on trade balance, and whoever wins the election may have to cut fuel price once in office. Should incoming administration decide to raise retail fuel price, we see some risk of rising inflation in Q3 and Q4 of 2019 and may reduce real consumption growth. Steps by Bank Indonesia to stem depreciation, particularly benchmark interest rate by 150 basis points this year may also counteract the stimuli provided by government through slews of proposed new government spending.

All in all, we see GDP to grow by 5.2-5.3% in 2019, or slightly higher than our revised forecast for 2018 (5.1-5.2%). As the risks for growth comes, given weaknesses in Indonesia's trade performance relative to its comparable neighbors, structural reforms are critically needed. Aside

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from regulatory reforms, opening Indonesia's economy and removing barriers to trade will be needed as the nature of trade shifts towards global value chain. Policies that restricts import in materials and capital goods, in particular, may backfire if it leads to shortage of necessary input for exports.

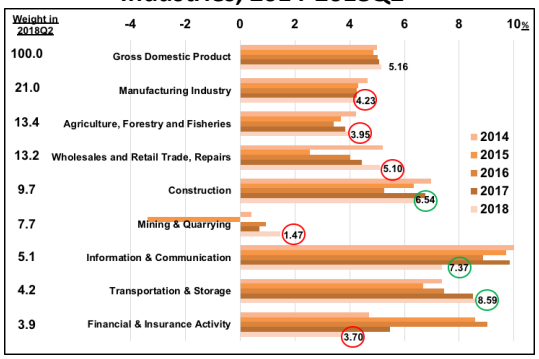
Manufacturing Growth Slows Down as Indonesia Becomes Less Competitive than Peers

After manufacturing industry as a whole accelerated again in Q1 2018 to 4.50%, growth in manufacturing slows down again considerably in Q2 to 4.23%. Food and beverage industry is still the biggest and fastest growth driver of manufacturing industry; also significantly slowing down from 12.7% (y.o.y) in Q1 to 10.68% in Q2. While we do not see the growth to pick up again in Q3 or Q4, we still see growth in food and beverage industry to still be above 10% in Q3 and Q4. Similar trend also happens in transport equipment and textile manufacturing; growth in these two sectors decelerate from 6.3% and 7.5% (y.o.y) in Q1 to 4,72% and 6.96% in Q2.

"Slower manufacturing growth after several quarters of marked increase should be a source of concern for Indonesian economy"

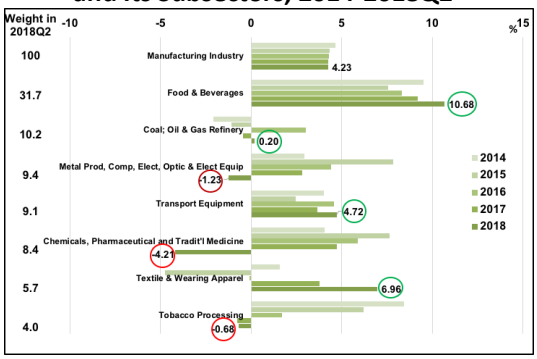
While improving from last quarter, growth in chemicals and pharmaceutical manufacturing and electronics manufacturing continue to record negative growth; growth in these two subsectors are -4.21% and -1.23% (y.o.y) respectively. These two sectors rely on imports; hence they are directly hit by the IDR volatility and depreciation.

Figure 1: Growth of GDP and the Main Industries, 2014-2018Q2



Source: CEIC

Figure 2: Growth of Manufacturing Sector and Its Subsectors, 2014-2018Q2



Source: CEIC

Slower manufacturing growth after several quarters of marked increase should be a source of concern for Indonesian economy. We see the confluence of short-term and long-term factors that drive the weaknesses in manufacturing sector growth in Q2 and the second half of 2018. Short-term manufacturing growth was likely and is still likely to be dampened by increased volatility in exchange rate. Indonesia's exporters rely heavily on imported materials and capital goods to process their goods, and as such, significantly stronger US dollar is likely to increase the manufacturing costs for export-oriented manufacturers and local-oriented manufacturers who use imported materials and machineries. Some contraction in manufacturing activities are therefore inevitable in order to manage costs for manufacturers until exchange rate stabilize.

However, manufacturing sector also have long-term problems that have not been fully addressed by government, chief of which is protectionism. Protectionist measures designed with thinking that increase in tariff and non-tariff barriers will increase the relative competitiveness of locally-manufactured products compared to imported products. This is evident in recent decision to

increase tariffs on various products that can be manufactured domestically. However, such thinking ignores the complex reality of modern trade, where countries trade in intermediate components (the so-called global value chain) and that components cannot be easily substituted with locally-made components. Thus, imposing tariffs may actually backfire as manufacturers, faced with higher manufacturing costs due to increased tariff and non-tariff barriers, will decide to partially or permanently shift their manufacturing processes to other manufacturing base with less barriers, such as Thailand or Vietnam.

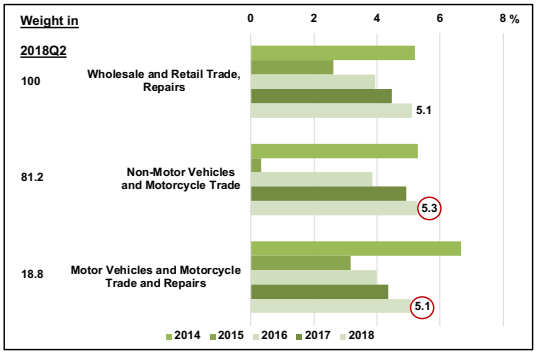
Another long-term structural problem that belies Indonesia is relatively hostile policies and practices toward foreign investment and workers. Although current administration has vowed to open more industries to foreign investments by removing negative lists, progresses have been rather slow so far. Bureaucratic red tapes for foreign investors and contradictory policies on regional level, such as minimum hiring quota to residents who hold locally-issued ID card in Bekasi regency, may reduce attractiveness of investment in manufacturing sector in Indonesia relative to other regional manufacturing base, such as Thailand and Vietnam.

"…manufacturers, faced with higher manufacturing costs due to increased tariff and non-tariff barriers, will decide to partially or permanently shift their manufacturing processes to other manufacturing base with less barriers, such as Thailand or Vietnam"

Construction sector also experiences slower growth of 6.54% in Q2 2018, significantly less than 7.35% in Q1 2018. In addition to government's decision to postpone non-critical infrastructure projects to contain current account deficit, reduced investment in factories and business structures and increase in benchmark policy rate dampen the demand for new buildings and thus construction growth. This trend could change in 2019. The government will continue its push with above IDR400 trillion government budget for infrastructure. Nevertheless, with state-owned enterprises already bearing most of the burden, 2019 performance will depend on government performance in involving private sector in financing the infrastructure projects.

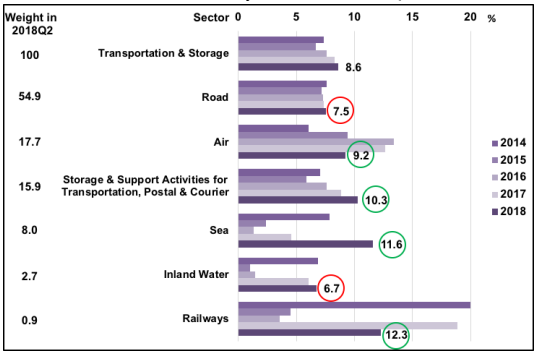
Higher Consumer Confidence in 2018, Strong Headwinds in 2019

Figure 3: Growth of Wholesale and Retail Trade and Its Subsectors, 2014-2018Q2



Source: CEIC

Figure 4: Growth of Transport and Its Major Subsectors, 2014-2018Q2



Source: CEIC

Despite interest rate that has started to rise since first half of 2018 and more than 12% year-to-date USD/IDR depreciation, consumer confidence seems to have returned, thanks to more robust wage growth and lending rate that is still near historic low despite the 150-bps policy rate hike. Wholesale and retail trade sector grew by 5.1% in Q2 2018, driven primarily by higher increases in motor vehicle sales, which grew by 5.3% in Q1 2018, or significantly higher than in Q1 at 4.7% (y.o.y). Overall, non-motor-vehicle trades are less affected by changes in interest rate consumers seem to be less affected by changes in interest rate, as compared to motor vehicle and motorcycle trade. The impact of rise in interest rate and stagnating price of key export

commodities, such as palm oil, reduce the demand for motor vehicles. Motor vehicle trade subsector growth slowed to 4.4% in Q2 from 6.1% in Q1, thus bringing 1H-2018 growth to 5.1%.

The growth for retailers, however, are not equally shared between traditional brick-and-mortar retailers and online-based retailers. While the exact data for online retailers are unavailable, we see robust growth in storage and courier activities as proxy sign for rapid growth in online retail trades; growth in storage, postal, and courier subsector grew by 10.3% (y.o.y) in first half of 2018 as overall transport and storage sector only by 8.6% over the same period. This growth level represents four consecutive acceleration of growth in storage and courier subsector and can only be explained by deeper penetration of online trade, particularly in major urban areas. We see robust growth in 2019 for online trade and complementing activities, such as storage and courier activities, even as brick-and-mortar retailers see slower-than-average growth.

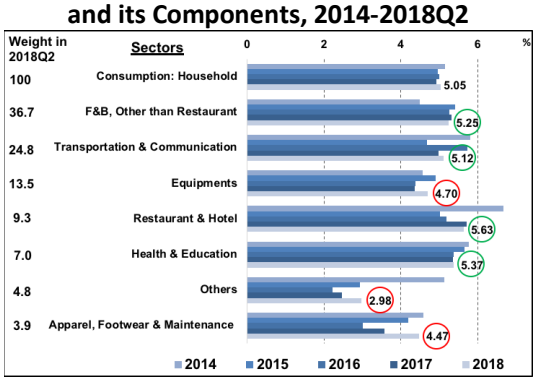
"…despite higher growth that is expected to continue until end-of-2018, external factors and rising interest rates create major headwinds for trade and transportation sectors"

However, despite higher growth that is expected to continue until end-of-2018, external factors and rising interest rates create major headwinds for trade and transportation sectors. Rising international fuel price and Rupiah depreciation, for example, will hurt transportation sector (particularly air transport and sea transport) and motor vehicles trade in 2019. Rising interest rate, the effect of which has been felt by motor vehicles trade in 2018, will continue to slow down growth for motor vehicles trade and transportation sectors in general. We expect considerably lower growth in 2019 for both motor vehicles trade, which may grow below 5% (y.o.y), and transportation sector, which will hover around 8% (y.o.y) in 2019.

Significant slowdown is also felt by communication and information sector, which grew by just 6.06% (y.o.y) in Q2 2018 after growing by 8.52% in Q1 2018. This steep drop may be explained by either error in Q2 2018 data or inevitable reversion to the mean given that this sector grew by 11.06% in Q2 2017. Nevertheless, such slowdown may be inevitable, particularly in 2019, given Indonesia's cellphone penetration already reach point of saturation. Growth area for communication and information sector may be limited to niche areas, such as digitalization of day-to-day activities through adoption of internet-of-things and more adoption of artificial intelligence solutions for business services, which still have very limited market in Indonesia.

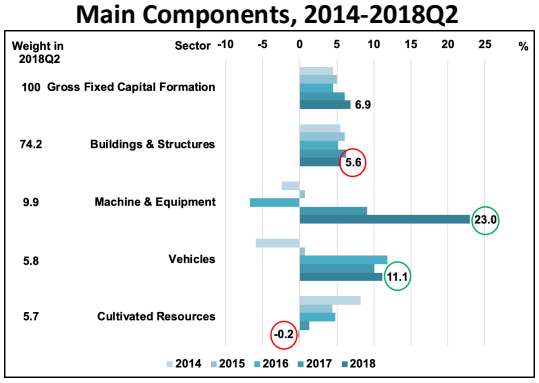
Consumption to grow above 5% in 2018, could get even better in 2019

Figure 5: Growth of Household Consumption and its Components, 2014-2018Q2



Source: CEIC

Figure 6: Growth rate of Investment and its Main Components, 2014-2018Q2



Source: CEIC

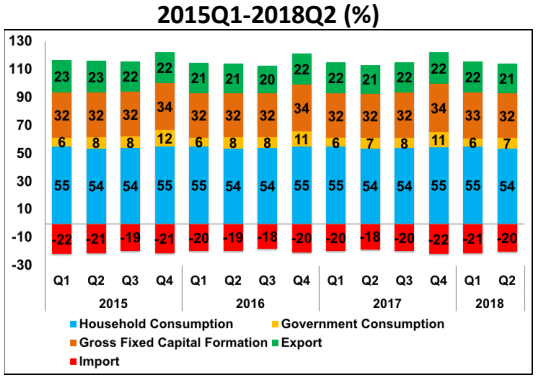
After several years of sub-5% growth, household consumption growth eventually accelerated in Q2 2018 to 5.14%, bringing 1H-2018 growth to 5.05% (y.o.y), compared to 4.95% in Q1 2018. Acceleration in consumption growth is also accompanied by rapid acceleration of consumption

credit growth in September, which stands at 11.4% y.o.y. and better consumer confidence through the Q3 2018. It is noteworthy that consumption credit grew rapidly despite increase of benchmark policy rate by 150 basis points.

Most of the components that constitute household consumptions growth grew considerably in Q2, with notable exception of apparel, footwear, and maintenance (decelerating 3.86% in Q2 2018 from 5.09% in Q1 2018). Consumption on restaurant and hotel accelerated to 5.38% in Q2 2018 from 5.12% in Q1 2018. Consumption on transportation and communication also accelerated to 5.32% in Q2 2018 from 4.92% in Q1 2018. This growth rate is remarkable given the stable headline and core inflation remain at 2.88% and 2.82% (y.o.y) in September, which in itself suggests that GDP growth remains below its full employment level.

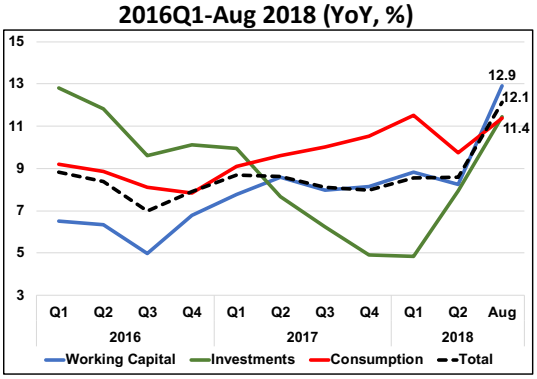
"…upward risk to inflation for 2019 comes mostly from remote possibility of increase in fuel price, particularly if government cannot sustain current level of retail fuel price, and exchange rate"

Figure 7: Shares of GDP Components, 2015Q1-2018Q2 (%)



Source: CEIC

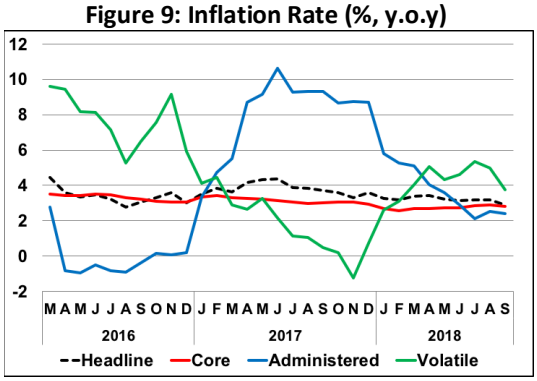
Figure 8: Credit Growth by Purposes, 2016Q1-Aug 2018 (YoY, %)



Source: Bank Indonesia

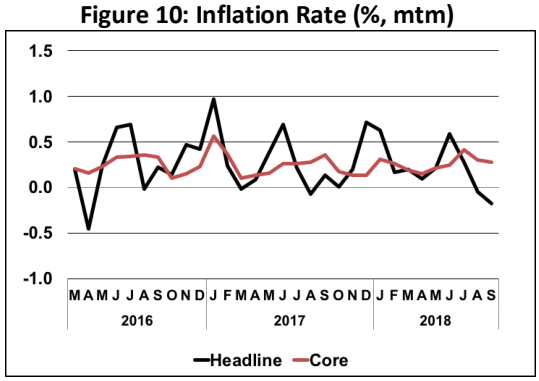
We still see slight upward trend for consumption in 2019, accompanied by slightly higher inflation at around 3.2-3.5% level in 2019. We see consumption growth to accelerate given (1) government's explicit indication that they pledge to hold retail fuel price ahead of 2019 General Election, (2) higher spending for items that are related to 2019 General Election and (3) introduction of Dana Kelurahan in 2019. The upward risk to inflation for 2019 comes mostly from remote possibility of increase in fuel price, particularly if government cannot sustain current level of retail fuel price, and exchange rate, although there is no indication of upward trend in inflation so far despite year-to-date depreciation of USD/IDR of around 12%.

Figure 9: Inflation Rate (%, y.o.y)



Source: CEIC

Figure 10: Inflation Rate (%, mtm)



Source: CEIC

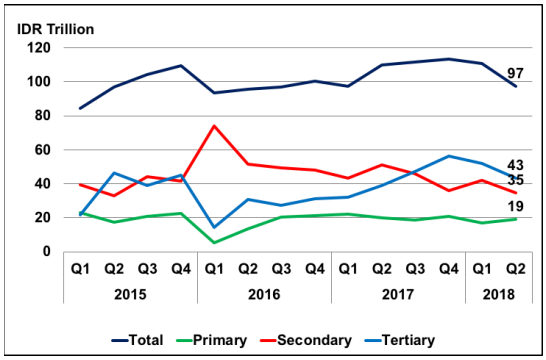
Better Investment Growth in 2019

While there are indications of faster investment activities in early 2018, inward flow of direct investments seems to slow down for the rest of 2018. Gross fixed capital formation, the measure of investment in GDP, grew at 5.87% (y.o.y) in Q2, bringing 1H 2018 real investment growth to 6.9%. Government's decision to postpone key infrastructure projects to lower current account deficit in 2018 will be one of the main factors. 74% of gross fixed capital formation are for buildings and structures and growth for this type of investment dropped from 6.13% in Q1 to 5.02% in Q2. On the other hand, machine and equipment investments grew at stellar rate of 22.48% in Q2 2018, just slightly lower than the rate of 23.49% in Q1 2018, due to front-loading behavior by the machine importers ahead of the IDR depreciation in 2018.

"The combination of very high growth of investment in machineries and equipment and slower manufacturing growth is puzzling; double-digit growth in machineries and equipment investment has been going for four consecutive quarters yet manufacturing growth is still below 5% level"

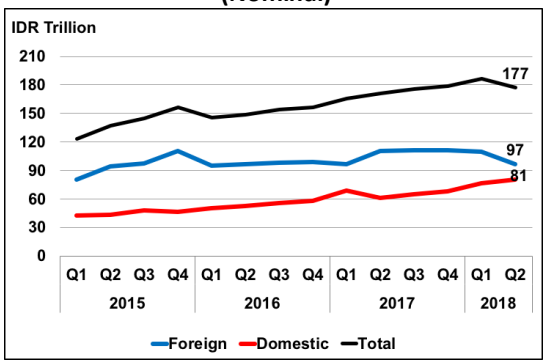
The combination of very high growth of investment in machineries and equipment and slower manufacturing growth is puzzling; double-digit growth in machineries and equipment investment has been going for four consecutive quarters yet manufacturing growth is still below 5% level. In addition to the front-loading hypothesis, there are several hypotheses that may account for this paradox. First, it is possible that rapid growth in machineries and equipment investment for the last four quarters just offset the trend of negative growth in this type of investment that has been recorded in the preceding three years; after accounting for depreciation, there might not be much net increase in manufacturing capacity despite high growth in the last four quarters. Second, it is also probable that investment in these items may not be instantly translated into higher manufacturing output due to the fact that investment in machineries and equipment are not necessarily absorbed by manufacturers, but more by businesses in other sectors, especially construction.

Figure 11: FDI Realization (Nominal)



Source: CEIC

Figure 12: Foreign and Domestic Investment (Nominal)



Source: CEIC

Rather steep drop in foreign direct investment realization in Q2 2018 also affected total investment realization, despite being slightly offset by increase in domestic investment. Direct investment data by the Indonesian Investment Coordinating Board (BKPM) show that FDI realization in Q2 dropped below Rp100 trillion mark. This drop in FDI can be explained by combination of tighter monetary policy worldwide, which increases long-term borrowing cost for firms globally, and Rupiah volatility, which might negatively affect value of investments by foreign firms. Higher domestic investments are supported by robust loan growth for investment purposes and working capital purposes, which grew by 11.4% and 12.9% in August 2018.

Despite gloomy picture for FDI in 2018, we see opportunities for FDI to start coming back in 2019 especially after the election in April 2019. Trade war between the US and China has caused businesses to relocate their operation from China to other emerging economies, especially Southeast Asia. Clearly, Indonesia will need to step up its game to compete with ever-competitive rivals in terms of attracting FDI to Southeast Asia, namely Malaysia, Thailand, and Vietnam. The latest publication on the Ease of Doing Business Index shows that comparatively Indonesia is stagnant while these rival countries are still improving. Among others, contract enforcement issue is still one of the biggest drags for Indonesia. Even with minimal improvement, we see that FDI will be better than 2018.

Another factor that will help investment in general in 2019 is the fact that US economy will risk overheating despite at least two foreseen Fed funds rate hikes. Ballooning US budget deficit will have to be managed in 2019. This will slow down its GDP growth rate and slow down, if not starting to reverse, the capital outflow from emerging economies.

"Similar trend is recorded across all revenue items, signaling that increased tax realization does not only reflect higher commodity prices, but also that tax collection effort has materially improved apparently has materialized in 2018"

Fuel Subsidy Remains as Biggest Threat to 2019 Budget

The 2019 Indonesian Government Budget has been approved by the parliament. One of the reasons to be cautiously optimistic about 2019 Budget is the considerable improvement in tax collection results in 2018. In the first 9 months of 2018, non-oil-and-gas income tax revenue has grown by 16.72% in nominal value and has reached 59.73% of its budgetary target, higher than the realization throughout the same period in 2017 (56.3%). Similar trend is recorded across all revenue items, signaling that increased tax realization does not only reflect higher commodity prices, but also that tax collection effort has materially improved apparently has materialized in 2018. Given the realistic growth in revenue target of 13.1% over the 2018 Budget, we see that government may be able to further improve its tax revenue realization in 2019.

However, despite the revenue side being a cause for optimism for 2019 Budget, we continue to be gravely concerned over the way Government of Indonesia treats the fuel subsidy problem in its 2019 budget. In particular, government's insistence to keep retail fuel price at current level, particularly for Premium (RON 88) and Solar (Diesel) types, without adjusting its fuel subsidy budget accordingly, are unsustainable as it requires Pertamina to shoulder the difference between stated budget subsidy and the "actual subsidy".

Table 2: 2019 Energy Subsidy (Billion IDR)

	APBN 2019	LPEM Projection	Unfunded
Premium (RON 92)	-	43,208	(43,208)
Solar (Diesel)	31,737	94,863	(63,126)
Total	**31,737**	**138,071**	**(106,334)**

We estimated the actual subsidy required if GoI wants to keep fuel price at its current level throughout 2019 by assuming exchange rate (USD/IDR) at 15,200, quota for Premium to remain at 2018 level, and using monthly futures price for the respective reference oil type (Platts RON92 Gasoline for Premium, Platts Gasoil 500ppm for Solar). We find that actual subsidy for just Premium and Solar to reach Rp138.07 trillion throughout 2019, of which only Rp31.74 trillion is already earmarked in 2019 Budget for fuel subsidy. This leaves Pertamina with Rp106.33 trillion in projected unfunded subsidy, which has to be shouldered by internal cash. It should be noted

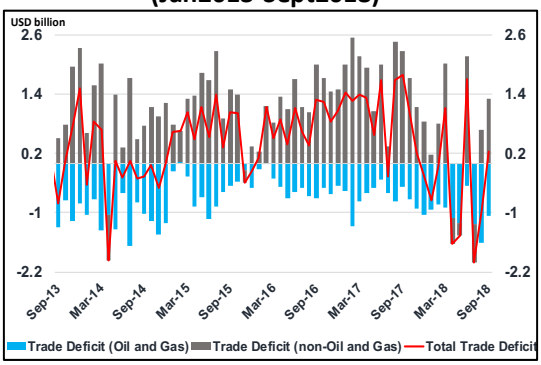
that this figure may underestimate the total unfunded subsidy that Pertamina has to shoulder as Pertalite and Dexlite may also be currently sold at loss.

As we have reiterated several times over, forcing Pertamina to shoulder the losses from selling retail fuel price below its fair price may seriously damage Pertamina's ability of doing business in the long run; it will drain Pertamina of much-needed operating cash flow. In the short term, this will reduce whatever remains of Pertamina's dividend or retained earnings, which will show up in reduced non-tax revenues. In the long term, production capacity and competitiveness of Pertamina will deteriorate due to shortage of much-needed capital for investment. As 2019 General Election nears, existing retail fuel price policy will also invite unwanted accusations that current administration tries to manipulate budget by hiding the true cost of subsidies from government's balance sheet and pass it to Pertamina's balance sheet.

"Rupiah depreciation throughout 2018 cannot be separated from the persistent weakening of balance of payments, given that widening of current account deficit and episode of capital outflow happened almost simultaneously throughout 2018"

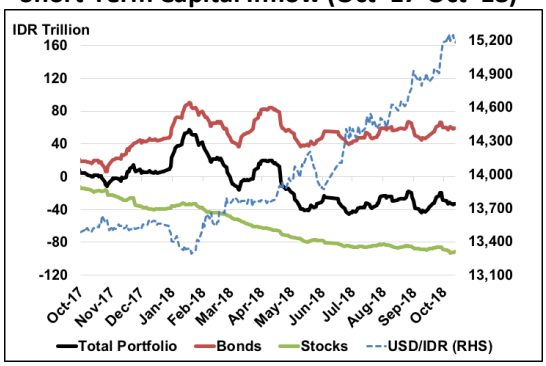
Furthermore, government's decision to increase energy subsidy may also indirectly lead to increase in current account deficit. Keeping retail fuel price at artificially low level will increase oil demand more than what it should be if fuel price is set at market rate, given that Indonesia is a net importer of oil.

Figure 13: Monthly Trade Balance (Nominal) (Jan2013-Sept2018)



Source: CEIC

Figure 14: Exchange Rate and Accumulated Short-Term Capital Inflow (Oct '17-Oct '18)



Source: CEIC

Rising External Risks, Deteriorating Current Account Position as Major Growth Risk

Rupiah depreciation throughout 2018 cannot be separated from the persistent weakening of balance of payments, given that widening of current account deficit and episode of capital outflow happened almost simultaneously throughout 2018. At US$8.0 billion, current account deficit in Q2 2018 has reached its highest nominal level and is equivalent to 3% GDP. The current account deficit increased quite sharply compared to Q1 2018, which only recorded deficit of USD5.7 billion (2.2% GDP). Narrowed non-oil and gas trade surplus amid persistent oil and gas trade deficit was the main driver of higher current account deficit.

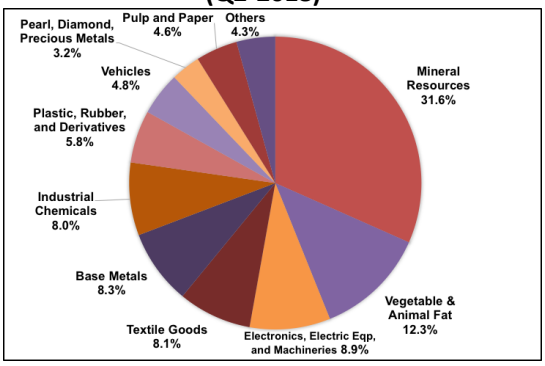
Extended higher crude oil price, along with limited national production capacity in line with increasing domestic demand, has led to persistent oil and gas trade deficit since 2013. we predict it to continue through 2019. Taking into account changes in global fuel prices will greatly influence the trade balance, thus, maintaining domestic demand is necessary. Following current trend, we expect withholding fuel price at the same level until the election year on 2019 can still be compensated as long as crude oil price do not rise any higher.

As oil and gas trade balance has remained in deficit for the last 5 years and has only fluctuated along with crude oil price dynamics, imported oil is not the main culprit for the widening of current account deficit in 2018. Rather, higher growth in household consumption and investment through Q2 2018, and disappointing export performance in 2018 means that non-oil current account deficit plays a significant dynamic in deterioration of current account balance. The first ever surge in non-oil and gas imports on April 2018, along with falling non-oil and gas exports, has contributed to trade deficit of USD1.6 billion, thus worsening the current account deficit. This trend continued through July 2018, which recorded the highest trade deficit of USD2.03 billion. It should be noted, however, that the rise in import activities was unusual and mainly influenced by sudden purchase of machinery and equipment; these purchases are related to construction and completion of major infrastructure and development projects as 2019 General Election nears.

"…the imbalance between rise in demand for imported goods and stagnating trend export makes Indonesia's traditionally healthy trade surplus turned into deficit in recent quarters"

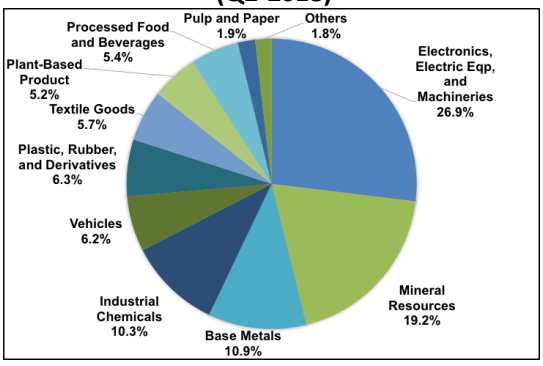
In details, the dynamics of what Indonesia exports and imports help explain the deterioration of trade balance and current account position in the last few years. As exports are still dominated by raw goods such as mineral resources, vegetable and animal fat as well as base metals (which represents 52.2 percent of total export values), stagnating price of key commodities, CPO in particular, has not helped and will not help to increase export values in the medium term. On the other hand, input goods and capital goods tend to have higher price stability and continue to rise in demand, tracking the GDP growth of overall sector. Thus, the imbalance between rise in demand for imported goods and stagnating trend export makes Indonesia's traditionally healthy trade surplus turned into deficit in recent quarters.

Figure 15: Indonesia Export Profile (Q2-2018)



Source: CEIC

Figure 16: Indonesia Import Profile (Q2-2018)



Source: CEIC

While higher crude oil price and relatively stagnant CPO price may pose risk for Indonesia's current account position in 2019, we still see significant possibility of improvement in current account deficit in 2019 following some steps that have been undertaken by the government. First, by postponing several non-critical infrastructure projects, chiefly for projects that have not been commenced, Indonesia can postpone imports to later dates and help reducing current account deficit in 2018 and possibly 2019. Second, the decision to enact B20 requirement, which mandates all diesel fuel to have 20% palm-oil blend, can help to shore up demand for palm oil, which will increase price of CPO in the medium-run and will improve our current account deficit considerably, given that palm oil is one of the most important export commodities in Indonesia.

However, the problem with current account deficit does not stop there, as export values, particularly for manufactured goods, have grown slower in recent years. Several of the long-term structural problems that plagued Indonesia's current account balance are (1) overreliance on

natural resources export, (2) relatively less welcoming regulatory regime in Indonesia for FDI, and (3) the protectionist measures that hinder the ability. As the result, Indonesia become less attractive as manufacturing base compared to other ASEAN countries such as Thailand and Vietnam, despite offering access to the largest domestic market in Southeast Asia.

This relatively low attractiveness of Indonesia as investment destination and manufacturing base is at full display in recent months following the escalation of trade war between US and China. Facing the possibility of not being able to access US markets without being levied steep tariffs and rising wage costs in China, many Chinese firms and other foreign firms that previously set up manufacturing bases in China have started to invest in other countries that remain neutral as new manufacturing bases. As the result FDI flows from China to the benefits of several Southeast Asian countries, such as Thailand, Vietnam, and Malaysia.

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Unfortunately, Indonesia has not received much windfall in terms of FDI. In fact, FDI to Indonesia has gone down in Q2 2018, as previously noted, which suggests that investors see Indonesia not as a cost-competitive manufacturing base. Vietnam has persistently beaten Indonesia in head-to-head competition for FDI, given that Vietnam has less protectionist barriers, relatively more investor-friendly regulatory regime compared to Indonesia, and has competitive wage level. This phenomenon is also evident from excerpt of various news that are related to windfall to Southeast Asia following trade war between China and US; Indonesia is very rarely mentioned as potential beneficiaries of ongoing trade war.

As we pointed out before, we see sets of regulatory reforms to make Indonesia more open, removing unnecessary bureaucratic processes, and making Indonesia labor market more dynamic as important steps that should be implemented in order to attract more FDI in manufacturing sectors but have not been carried out by Government of Indonesia so far. This lack of push for more regulatory reforms, relative to what have been carried out in other countries, has also caused Indonesia to rank one notch lower in Ease of Doing Business.

Lower FDI realization in Indonesia also come at less opportune moment, as negative external factors may become more apparent in 2019. While there are signs that US growth rate has peaked, there are no signs that Federal Reserve will reverse its path toward more monetary policy tightening in 2019. More US rate hikes will be a big problem for Bank Indonesia, as it has to reluctantly hike interest rate further despite the obvious contractionary effect of such moves. Additionally, full-scale trade war between US and China will affect Indonesia indirectly through possibility of shrinking export market. As US and China cumulatively account for 39.3% of global GDP and 24.2% of total Indonesian export market, reduced trade between the two will negatively impact their respective value chains. This will reduce demand for some intermediate goods or components that are produced in Indonesia, and slower GDP growth due to trade war will negatively affect Indonesian export further by dampening price of key commodities prices in 2019.