



MARKET INSIGHTS

FOCUS ON INDONESIA: A JOKOWI WIN WILL BE GOOD FOR INVESTORS

JULY 2014



The apparent victory of Joko “Jokowi” Widodo in Indonesia’s third-ever direct presidential election will likely boost the country’s stock market and currency in the short term. But the widely popular Jokowi, who is favoured by the investment community, is not yet out of the woods.

He and his opponent, ex-general Prabowo Subianto, each claim an election victory by virtue of “quick counts,” unofficial polls conducted by private organizations. Although the Jokowi ticket seems to be backed by a greater number of quick counts, Indonesia’s Election Commission will not declare an official winner for two weeks.

JOKOWI: A LEADER WITH A WILL TO EXECUTE

Jokowi is the governor of Jakarta and a former mayor of Surakarta, or Solo, a city in central Java. Infrastructure and public welfare schemes thrived under his administrations. Jokowi’s popularity sprang from his common-man personality and hands-on approach, which helped him break through a number of bottlenecks.

As governor of Jakarta, he focused on infrastructure by kick starting mass rapid transit and monorail projects. If Jokowi becomes president, a national thrust in infrastructure and public welfare spending is likely.

Jokowi has advocated reforming fuel subsidies and bureaucracy to increase transparency and reduce corruption. His proposed elimination of fuel subsidies in Jakarta suggests that he can overhaul the national fuel subsidy scheme. A reduction of fuel subsidies would save the government a significant amount of taxpayer money, which could be diverted to infrastructure.

While all this stands him in good stead to lead the country, Jokowi may face challenges in Parliament. His opponent, Prabowo, is backed by a coalition that already controls nearly two-thirds of Parliament. This can make it difficult for Jokowi and his team to push through his reform agenda.

However, coalition members have switched sides in the past after final election results were announced. Signs of potential switching have emerged already among senior members of a key Prabowo coalition partner. Such moves can work in Jokowi’s favour.

WHAT WILL A JOKOWI VICTORY MEAN FOR INDONESIA?

A Jokowi victory would come at a key moment for Indonesia’s economy, currency and investment climate. Jokowi’s reform agenda looks promising and, if implemented efficiently, can help Indonesia achieve longer-term growth.

The political guard is changing as Indonesia progresses at mending macro imbalances. This includes containing the troubled current account deficit, persistent inflation and weak currency that had chilled investor sentiment in the second half of 2013.

The current account deficit has improved significantly after peaking in the second quarter of 2013. Headline inflation also moderated while the Indonesian Rupiah strengthened 2.5% against the US dollar in the year to date.



Fig. 1. Table of Reforms

Jokowi's Nine Priority Agenda	
1	Return state to providing security to citizens, ensuring national sovereignty and strengthening Indonesia's regional/global role;
2	Develop clean, effective, trusted and democratic governance;
3	Develop Indonesia's rural areas and strengthen effectiveness of local governments;
4	Reform law enforcement agencies and reduce corruption;
5	Improve quality of life via programs in education, healthcare, social welfare and land reform and land ownership;
6	Raise productivity and competitiveness via infrastructure, streamlined business procedures and research technology;
7	Promote economic independence by developing domestic strategic sectors such as food/energy;
8	Overhaul character of the nation via civic education and;
9	Strengthen the spirit of "unity in diversity".

Source: Morgan Stanley Research, as at July 2014.

SECTORS LIKELY TO BENEFIT

If a Jokowi reform agenda is implemented, we believe that the shares of banks and select real estate companies, already attractively valued, will do especially well.

Further steps to contain fiscal and current account deficits may deter the central bank from raising interest rates. This could lift sentiment towards financial sector companies. Equally, an infrastructure thrust should underpin the real estate sector. Our strategies are poised to benefit from these possibilities.

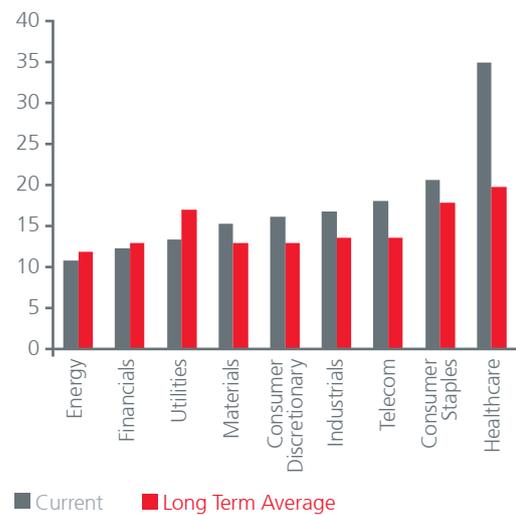
Indonesia's stock market is trading within the fair value range. Pushing through key reforms could result in an overall market rerating. Irrespective of this, the consensus estimates that company profits on aggregate will grow faster than in the past, rising in double digits over the next three years.

THE LONG-TERM INVESTMENT STORY

Attractive long-term fundamentals underpin Indonesia's investment story.

Indonesia is among the fastest growing economies in the G20 Group. It is the world's fourth most populous country and Southeast Asia's largest economy. Strong domestic demand and a low reliance on exports have made the economy resilient when faced with a challenging external

Fig.2. Price to Earnings Ratio for Indonesian Sectors



Source: IBES, MSCI, Indonesian Sector data from Thomson Reuters Datastream, as at 9 July 2014.

environment, such as economic slowdown elsewhere in the world. Rising investments are emerging as the new growth engine of Indonesia's economy.

We expect Indonesia's growing middle class and relatively young working population to underpin a structural consumption boom in the coming years.



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