First Key Rates Cut Since October 2016

23 August 2017

Evan Lie Hadiwidjaja
Head of Research
+62 21 392 5550 ext. 610
evan.hadiwidjaja@sinarmassekuritas.co.id

BI cuts key rates by 25 bps yesterday, as BI sees easing monetary policy seems to be appropriate given the current economic condition. In the August meeting, BI has decided to lower 7DRRR to 4.50%, while keeping the 150 bps corridor between lending and deposit facility rates, which currently stand at 5.25% and 3.75% respectively. BI had also indicated that the 25 bps cut also applies to longer tenor policy rates. Meanwhile, during the press conference yesterday evening, BI stated that there are four main reasons behind the 25 bps cut, 1) lower-than-expected inflation: 4.0% with electricity tariff increases and 3.0% without electricity tariff increases, 2) strong CAD position: BI sees FY17E CAD to stand within 1.5-2.0% of GDP and FY18F CAD to stand within 2.0-2.5% of GDP or still below the regulatory 3.0% of GDP, 3) less external forces: BI sees the pressure from FFR hike in December has lessened given the much lower odds for a rate hike in December as inflation stands below initial projection, 4) soft credit growth in 1H17: BI sees that easing monetary policy is appropriate in order to stimulate credit demand and domestic economy.

While 25 bps cut seems to be a positive driver for credit demand, BI lowered credit growth forecast for FY17E by 200 bps. In the August meeting, BI had lowered credit growth forecast for FY17E from previously 10-12% to 8-10%, while keeping the FY18F guidance unchanged at 10-12%. Meanwhile, BI keeps the deposit growth forecast for FY17E and FY18F unchanged at 9-11%. BI sees that there are still pressure from NPL that causes banks to be more conservative in disbursing loans.

Which sectors are benefited? Normally during the event of easing monetary policy, four sectors are benefited; Banks, Property, Automotive, and Consumer. While we agree on Property, Automotive, and Consumer sectors, we view that the impact on Indonesian banks will be muted this time, as market may prefer wait-and-see stance to anticipate upcoming announcement on OJK's relaxation which supposedly ends on August 24th. OJK had recently announced that they do not plan to extend the one-pillar relaxation program as they see the economy is getting better and local banks have sufficient CAR to anticipate the asset quality movement it may cause. However, we may see margin expansion on the banking sector as policy rate cut tends to benefit banks as it is more correlated to CoF than to lending rate; from January 2016 to July 2017, BI had cut key rates as much as 150 bps, meanwhile CoF declined by 145 bps (97% correlation) whereas lending rate only declined by 110 bps (73% correlation).

As for other sectors, we prefer Property as it is the most laggard sector with attractive valuation and outlook. Not to mention that BI had imposed a new tool called "LTV Spatial" that they are currently preparing. While they have not given any clear picture on what the ratio will be like, the LTV Spatial is intended to stimulate property demand in an area where demand is considered to be lackluster, thus the LTV ratio per region may vary depending on certain factors such as economic condition, land price, etc. Thus, we see the 25 bps cut to be a positive catalyst for the sector (BSDE, SMRA, CTRA). We choose BSDE for its having the biggest landbank and focus on the mid segment, SMRA's attractive valuation due to its close to 70% discount to NAV, while CTRA has the most dispersed locations which will be benefited by the LTV spatial, not to mention customer profile who tend to use mortgages.

As for Automotive sector, while we see policy rate cut will benefit the sector, we see that 4W market is quite disruptive right now with new players entering the market. Although 2W sales has been a breath of fresh air lately as it shows a sign of recovery in the lower end consumer (Jun'17+Jul'17 2W sales went up by 11.4% YoY). Nevertheless, we remain neutral on Automotive for the time being.

As for Consumer sector, we see there will be indirect impact from the rate cut. We remain optimistic on the sector, although we prefer to be selective as during lower growth environment, defensive sector such as Consumer may appear to be expensive. We choose INDF for the sector given the attractive valuation and holding discount from ICBP.

All in all, we recommend to add BSDE, SMRA, CTRA and INDF on your portfolio given the changes in policy rates.

SINARMAS SEKURITAS INVESTMENT RATINGS GUIDE

BUY: Share price may rise by more than 15% over the next 12 months.
ADD: Share price may range between 10% to 15% over the next 12 months.
NEUTRAL: Share price may range between −10% to +10% over the next 12 months.
REDUCE: Share price may range between −10% to −15% over the next 12 months.
SELL: Share price may fall by more than 15% over the next 12 months.

DISCLAIMER

This report has been prepared by PT Sinarmas Sekuritas, an affiliate of Sinarmas Group.

This material is: (i) created based on information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon as such; (ii) for your private information, and we are not soliciting any action based upon it; (iii) not to be construed as an offer to sell or a solicitation of an offer to buy any security.

Opinions expressed are current opinions as of original publication date appearing on this material and the information, including the opinions contained herein, is subjected to change without notice. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. The analyst(s) responsible for the preparation of this publication may interact with trading desk personnel, sales personnel and other constituencies for the purpose of gathering, integrating and interpreting market information. Research will initiate, update and cease coverage solely at the discretion of Sinarmas Research department. If and as applicable, Sinarmas Sekuritas' investment banking relationships, investment banking and non-investment banking compensation and securities ownership, if any, are specified in disclaimers and related disclosures in this report. In addition, other members of Sinarmas Group may from time to time perform investment banking or other services (including acting as advisor, manager or lender) for, or solicit investment banking or other business from companies under our research coverage. Further, the Sinarmas Group, and/or its officers, directors and employees, including persons, without limitation, involved in the preparation or issuance of this material may, to the extent permitted by law and/or regulation, have long or short positions in, and buy or sell, the securities (including ownership by Sinarmas Group), or derivatives (including options) thereof, of companies under our coverage, or related securities or derivatives. In addition, the Sinarmas Group, including Sinarmas Sekuritas, may act as market maker and principal, willing to buy and sell certain of the securities of companies under our coverage. Further, the Sinarmas Group may buy and sell certain of the securities of companies under our coverage, as agent for its clients.

Investors should consider this report as only a single factor in making their investment decision and, as such, the report should not be viewed as identifying or suggesting all risks, direct or indirect, that may be associated with any investment decision. Recipients should not regard this report as substitute for exercise of their own judgment. Past performance is not necessarily a guide to future performance. The value of any investments may go down as well as up and you may not get back the full amount invested.

Sinarmas Sekuritas specifically prohibits the redistribution of this material in whole or in part without the written permission of Sinarmas Sekuritas and Sinarmas Sekuritas accepts no liability whatsoever for the actions of third parties in this respect. If publication has been distributed by electronic transmission, such as e-mail, then such transmission cannot be guaranteed to be secure or error-free as information could be intercepted, corrupted, lost, destroyed, arrive late or incomplete, or contain viruses. The sender therefore does not accept liability for any errors or omissions in the contents of this publication, which may arise as a result of electronic transmission. If verification is required, please request a hard-copy version.

Additional information is available upon request.

Images may depict objects or elements which are protected by third party copyright, trademarks and other intellectual properties.