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Investing next door in Indonesia

China and India mostly fill the headlines on where to invest abroad, but Australia's neighbor Indonesia is actually worth to look at because it could be the next China, only younger and like Australia, a democracy.

Former Australian Prime Minister Paul Keating noted that Indonesia was vital to Australia's future and built a relationship that future Prime Minister's and governments have continued.

There is no other country more important to Australia than Indonesia and now it's time for its super funds to recognize the important investment opportunities in Indonesia's stock market and infrastructure.

Three years ago Morgan Stanley stated that Indonesia would be the next member of the "elite" BRIC developing nations comprising Brazil, Russia, India, and China (BRIC). Yet since that time Indonesia has taken several strides further as an emerging economic power widely regarded as having an enviable demographics and natural resources profile and resilient economy.

Post-2008 rebound

During the 2008 global crisis, when all major economies and many smaller ones were in recession, Indonesia recorded 4.6% growth. Reinforcing all the improvements that occurred following the Asian Financial Crisis in 1997, these healthy numbers helped Indonesia earlier this year win back its investment grade rating from Fitch Ratings and Moody's Investors Service.

The ratings upgrade now puts the largest economy in Southeast Asia on par with India, Malaysia and Thailand.

The stock market tells the same story. In 2011 with uncertainties lingering in the global market, the Jakarta Composite Index (JCI) managed to climb 2.84%, outperforming the share markets in BRIC countries which all fell in varying degrees. This made Indonesia the second best performing share market in the Asia Pacific region.

In fact, over the past decade the JCI has grown by an average of 24% pa. Bloomberg notes the country's local-currency bonds have returned 28% in the past year, the best performance among 10 Asian debt markets tracked by HSBC Holdings Plc. Meanwhile its dollar bonds gained 9% in the same period, the second-best out of 11 markets in the region.

Growth drivers

Strong domestic consumption is one of the key factors driving the country's economy. In line with Indonesia's very favorable demographic structure, last year private consumption

accounted for 55% of GDP. With a population of 240 million, the world's fourth largest, 60% of Indonesians are of productive age. And the middle class is quickly making its presence felt. In 2003 only 35% of Indonesians spent \$2 – \$20 a day, while in 2010 the figure had expanded to 57 percent.

The young and growing middle class population signals support for long-term growth. In addition to that, the country's strength also inheres in its abundant resources.

Indonesia is currently the world's largest CPO, tin, thermal coal and natural gas producer. Investment in these resources has boosted foreign direct investment into the country to a record A\$12.8 billion in 2010, outpacing the growth of portfolio investment.

In terms of political stability, Indonesia is in a better position than many emerging Asian nations. After the end of the Soeharto era in 1998, growth in the number of political parties has been one sign of a strengthening democracy. In addition, more provinces and municipalities have succeeded in transitioning away from a centralistic system to regional autonomy.

Yes there are some risks

There remain security problems in some of the regions (eg, Papua), but overall it does not much affect national economic stability and Indonesia has become a secure place for foreign investment.

There remain market and economic risks, however. Indonesia remains fairly insulated from an EU economic malaise with Europe only accounting for around 12% of Indonesian trade but of course would have to negotiate the accompanying market turmoil and capital flows back to safe-haven countries.

As regards an internal perspective, Indonesia is known for having inadequate infrastructure in some areas of the economy, red tape, and corruption. The World Bank Logistic Performance Index, an indicator of trade logistics efficiency, ranks it 75th, or below peers in the region like Thailand, Philippines, and Malaysia.

The government is aware of these problems and last year deployed an accelerated program for nationwide infrastructure development involving Rp 4 quadrillion (A\$407 billion) with more than half the funding to come from the private sector.

Open for business

During a meeting with Prime Minister Julia Gillard in July, President Susilo Bambang Yudhoyono invited Australian investors to participate in the plan. Indonesia is open for business for Australian institutional investors.

Australian superannuation funds and invest-

ment consultants are encouraged to visit Jakarta meet with local investment houses, experts and the Indonesian regulators. These visits and meetings help to build knowledge and understanding.

It's important to learn about the high standards of compliance and regulation in the Indonesian market. Mandiri Investasi together with its Australian front office, AFM Investment Partners, have seen this as crucial in developing confidence in investing in Indonesia and the local regulator, Bapepam & LK (Capital Market and Financial Institutions Supervisory Agency), has hosted Australian delegations.

Bapepam will be presenting to the inaugural Investing in Asia conference to be held in Melbourne with the Australian Centre for Financial Studies on September 4th to discuss compliance and regulation.

Potential foreign infrastructure investors have in the past held back due to concerns over the decision making framework. Much of this concern has its origins in things long resolved. However, the constellation of legal and other issues involved is being addressed by the new land bill passed last year.

With the new land acquisition law, landowners are obliged to release land needed by the state for projects. Price disputes are settled by the court but construction activity may continue in the meantime. Moreover, the government is also considering several sweeteners – such as tax incentives – that are sure to lure more foreign investors to the infrastructure sector in Indonesia.

Accessing the market

Mandiri Investasi, as the largest national investment manager in Indonesia that has been extending its reach to provide a channel to Australian investors interested in investing in Indonesia-based portfolios, sees that the relationship between Indonesia's economy and Australia's can be seen as similar as between Canada and the US in the early 1980's – [when that trading relationship was poised to boom].

Indonesia's natural resource-based economic profile is almost identical to that of Australia, except without the modern technology and infrastructure.

Reflecting these opportunities it is also pleasing to see that funds and consultants are visiting Jakarta to review the opportunities in Indonesia including the equities market.

Driven by consumption and commodities, and continued investment in infrastructure, the Indonesian economy has ploughed forward as one of the world's more stable emerging market economies and one of most preferred investment destination in Asia Pacific. **FS**



The quote

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