



# Indonesia and India - Upcoming Elections Provide Food for Thought

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*Recent research trips to India and Indonesia provide valuable insight ahead of upcoming elections*

It's an election heavy-year for many emerging market countries, with elections in progress in Ukraine and voters due to go to the polls in Nigeria, Indonesia, India, South Africa and Argentina over the course of 2019.

Elections in India and Indonesia are due this month. In Indonesia, around 190 million are expected to participate, although this is significantly overshadowed by India where around 900 million people are eligible to vote in what is the largest election on the planet which takes over a month to complete.<sup>1</sup>

Both elections have similarities. Incumbents are running, and at this point there is a strong likelihood both could be re-elected. The agenda of each is also heavily skewed towards economic reform, something which investors are anxious to encourage.

Indonesian President Joko Widodo ('Jokowi') is pitched against Prabowo Subianto. The latest polling data surveys carried out in March show that Jokowi has a 13-point lead over Prabowo, at 56.5-43.5. In July 2014, Jokowi won by 53-47 and, at this point, we expect a similar outcome.<sup>2</sup>

In India, polls have moved more in favour of Narendra Modi although suggest that the ruling Bharatiya Janata Party may not have enough to command an overall majority.<sup>3</sup> In our view, the recent Modi majority government was a rarity for India, a country which is more used to coalitions. We believe setbacks in the state elections were viewed more as protest votes rather than a trend that looks set to continue into the general election. While the opposition is seen as united in its anti-Modi sentiment, beyond that we believe there does not appear to be a coherent policy agenda.

1. <https://www.nst.com.my/world/2019/04/477360/indonesias-presidential-election-jokowi-or-prabowo>; <https://edition.cnn.com/2019/02/16/asia/india-election-numbers-intl/index.html>
2. <https://www.roymorgan.com/findings/7934-indonesian-vote-april-2-2019-201904020627>
3. <https://www.timesnownews.com/india/article/times-now-vmr-opinion-poll-for-lok-sabha-election-2019-bjp-narendra-modi-congress-rahul-gandhi/396628>



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There are also similarities in both Jokowi and Modi's economic reform agendas in that so far, both appear to have had mixed results.

### Indonesia - Reform Likely to Continue

We believe the reaction to the free trade agreement with Australia (the Indonesia-Australia Comprehensive Economic Partnership Agreement or IA-CEPA) can be highlighted as an example of the general acceptance of a reform agenda. In the past, such an agreement might have been politicized by the opposition but in our view, it was not the case this time.

It could be argued that the reform agenda is likely to continue whoever wins the election. However, if it is the opposition, market pressure will likely mean that they will quickly need to establish their own reform credentials to instil market confidence in the new leadership.

Monetary policy appears to have had some success. Since early 2016, inflation has been low, around the 3% target, although growth has consistently disappointed at the 5 - 5.5% level.<sup>4</sup> Recent trade tensions and interventionist policies also led to imports to fall faster than exports, resulting in a current account surplus in February.<sup>5</sup>

We have also seen evidence of the government focusing on strengthening its relationships with China, including increasing dialogue with large industrial groups to encourage them to relocate production to Indonesia. We believe closer ties between these two countries are likely to benefit both countries and highlight China's increasing recognition of the need to transition its economy into higher-skilled activities, especially as the population is aging (and is expected to decline from 2030).

The country has also highlighted tourism as a key source of local currency inflows, with its '10 New Balis' strategy, launched in 2016, to boost tourism in the country. In our view, despite recent tragic setbacks due to natural disasters, the development of some of these sites would be a catalyst for additional spending on infrastructure such as airports, roads and power generation.

### India - A Growing Interest in Renewables

Headline policies such as the 2016 banknote demonetisation and the 2017 Goods and Services Tax (GST) have, arguably, not been implemented that well. However, anecdotal evidence from individual companies suggests significant improvements because of those policies.<sup>6</sup> For example, post the GST, the inter-state transportation of goods is now seamless, whereas before there were delays at state borders.<sup>7</sup>

A cited weakness in the Indian economy however is disappointing jobs growth, although we acknowledge there is a measurement problem as jobs are moving from the informal sector to the formal sector.<sup>8</sup>

Meanwhile the higher scrutiny on cash transactions has helped commercial leasing companies, with one bank reporting financing penetration of new commercial vehicle purchases increasing from 20% to 40%.<sup>9</sup> This comes on top of strong commercial vehicle sales in calendar year 2018 of 27.28%.<sup>10</sup>

Inflation was 2.5% in March 2019,<sup>11</sup> around the lows for Modi's Premiership and growth for FY20 (year ending 31 March 2020) is forecast to be c.7%, all of which appears to be good news for the bulk of the Indian fixed income issuers which are geared to domestic demand conditions.<sup>12</sup>

An interesting development is in the country's the renewable energy sector. India has a public policy commitment to 175GW of renewable capacity (100GW of solar, 60GW of wind, 15GW of other) by March 2022 and solar and wind power are becoming more prominent participants.<sup>13</sup>

We believe they are likely to be long-term players in the sector, although acknowledge they are still significantly behind their developed market counterparts. For example, issues such as how best to ensure solar panels remain clear of dust to maintain operational efficiency in a dry, gritty and hot climate, is something that the solar companies are still struggling to resolve. The case for automated solutions suffers against an abundant, affordable local workforce, but has an increasing appeal when thinking about water conservation, with some automated solutions requiring no water.

### Outlook for Corporates

Political uncertainty can drive idiosyncratic sentiment amongst investors in those countries - at both the sovereign and corporate level.

In our view, Indian companies appear to be less affected by election noise. Domestic demand is a key driver for many Indian issuers (e.g. steel, infrastructure, power generation, petrochemicals), although other issuers are more export-orientated (e.g. generic drug manufacturers, business process outsourcing).

We currently see value in some lower-rated investment grade names within Indian power companies as well as interesting opportunities in some high yield companies within India's renewable energy sector.

The overall tone amongst the Indonesian companies we visited was largely constructive, with the probability of a shock election result being relatively low. However, many companies, such as those in the property sector, are likely to postpone issuance in our opinion, with buyer interest likely to be limited before the 17<sup>th</sup> April elections. In addition, with reference to the property sector, we believe it is unlikely that there will be any major new project launches until the second half of this year, which we believe should generate marketing sales and encourage companies to replenish land banks.

While we will be closely watching the outcome of both elections, they are not the determining factor behind our investment decisions. Nevertheless, policy feeds through into the corporate environment and, with both countries likely to continue their market-friendly reform programmes post the elections, we believe they are likely to be an ongoing source of interesting opportunities for credit investors.

4. <https://tradingeconomics.com/indonesia/gdp-growth-annual>

5. <https://www.ft.com/content/0b664b70-46c9-11e9-b168-96a37d002cd3>

6. Source: Muzinich research trip

7. Source: Muzinich research trip

8. <https://tradingeconomics.com/india/unemployment-rate>

9. Source: Muzinich research trip.

10. <https://auto.economicstimes.indiatimes.com/news/industry/complete-india-auto-sales-analysis-2018-cv-sales-crosses-a-million-mark/67549073>

11. <https://tradingeconomics.com/india/inflation-cpi>

12. <https://economicstimes.indiatimes.com/news/economy/indicators/indias-economic-growth-to-slow-to-7-3-in-2019-moodys/articleshow/66542777.cms>

13. <https://india.mongabay.com/2018/03/will-india-be-able-to-meet-its-renewable-energy-targets-by-2022/>

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