



# 2025 Mid-Year Macro Letter

## 2H 2025

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## **Summary of 2H 2025 Macro Letter:**

### **1. Indonesia's Economic Conundrum: Government Spending, Where Is It?**

- Fiscal support remains critical, but stimulus rollout has been slow. June spending surged, yet overall absorption remains weak.
- Revenue underperformed due to VAT hike cancellation and SOE dividend reallocation to Danantara.
- Free Meal Program met only 4% of its target; the budget cut reflects poor execution capacity.
- Fiscal deficit ceiling revised to 2.8% of GDP, with cautious spending to stay under the 3% legal limit.

### **2. Bond Market Resilience Driven by BI Intervention**

- BI's interventions (bond purchases, SRBI issuance, liquidity ops) have anchored yields and reduced volatility.
- Heavy BI buying (IDR 145 trillion YTD) distorts price discovery and dampens auction appetite among institutional investors.
- Investors are rotating into corporate bonds, especially SOEs and banks, amid compressed sovereign yields.
- Monetary easing bias, low inflation, and credit growth need support duration and modest steepening of the curve.

### **3. Foreign Outflows and Domestic Resilience in Indonesia's Equity Market**

- Over USD 3 billion in YTD foreign outflows, driven by policy uncertainty, subsidy reforms, and social unrest.
- Domestic institutions (e.g., Danantara, BPJS) and corporate buybacks have stabilized equity prices.
- Retail flows rotate into small- and mid-caps, driving volume and alpha outside blue chips.
- Foreign-heavy stocks see low liquidity and weak price discovery; local investors now lead market direction.
- Foreign re-entry depends on improved policy clarity, global rate stabilization, and stronger fiscal execution.

### **4. US Exceptionalism Through Crises: Still Standing Strong**

- US markets remain top global performers despite shocks (COVID legacy, Fed hikes, tariffs, geopolitics).
- DXY down more than 10% YTD. Yet, the USD-IDR remains elevated, indicating Rupiah strength through contained depreciation, rather than gains. US assets outperform even with a weaker dollar, supported by innovation, policy credibility, and market depth.
- Recession unlikely; growth moderates amid weak consumer health and low savings.
- Inflation easing; economists expect rate cuts starting September, totaling ~200 bps through 2027.

## **Key Takeaways from our previous 1H 2025 Macro Letter:**

### **1. Indonesia 2025: Fragile Growth, Rising Risks**

- Economic recovery relies on government spending, FDI, and fiscal reforms. While consumer demand remains weak, especially in lower-income segments.
- BI's rate cuts may trigger capital outflows and Rupiah depreciation.
- Domestic investment remains robust, but import-driven inflation is a concern. Manufacturing faces margin pressure due to weak demand and high input costs.

### **2. Foreign Flows Drive Investment Decisions**

- BI's policy pivot favours growth, steepening the sovereign yield curve. Short-term yields stay high; long-term yields rise with fiscal spending.
- AAA/AA corporate bond spreads are narrowing; we remain selective in allocation.
- Indonesian equities look undervalued; focus on blue-chip and momentum plays.

### **3. Trump Policies Fuel Growth, But Pose Risks for Indonesia**

- US growth strong under Trump via deregulation, tariffs, and tax reform.
- Domestic energy policies may boost supply, easing inflation pressures.
- Potential Fed rate cuts ahead, but Indonesia faces trade and currency risks.
- US protectionism may hurt Indonesia's commodity exports and trade balance.

### **4. USD Private Credit Continues to Outperform**

- USD Indonesian Sovereign Bonds offer yields comparable to investment-grade USD bonds and a premium over U.S. Treasuries.
- Yield advantage may shrink over time with global rate cuts.
- USD Private Credit expected to offer stronger, more consistent returns than USD-based bonds.

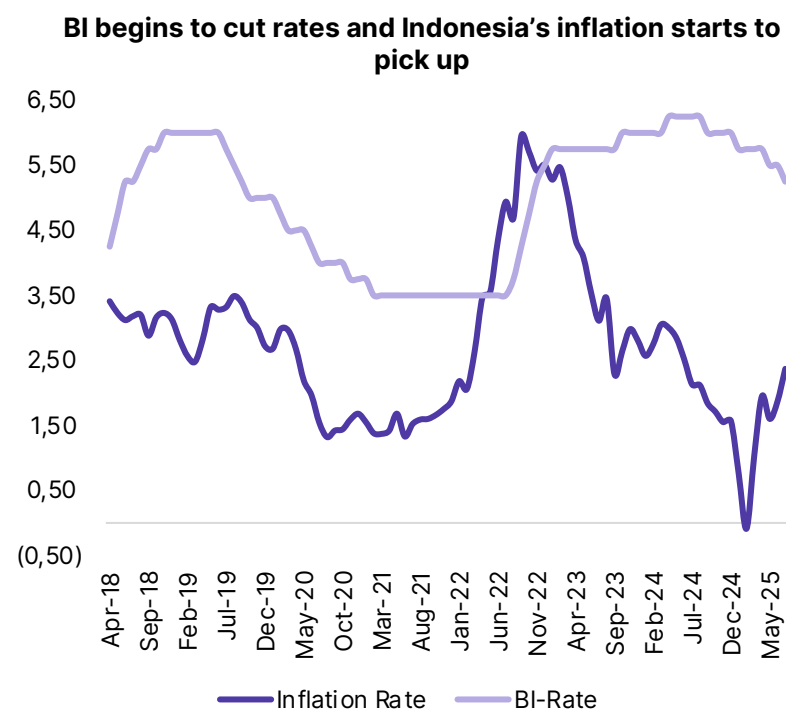
## 1. Indonesia's Economic Conundrum: Government Spending, Where Is It?

**As Indonesia enters the second half of 2025, it finds itself in a policy paradox: macroeconomic fundamentals remain weak, inflation is subdued, yet the government's fiscal momentum has been underwhelming.** In 1H25, the fiscal deficit stood at IDR 204 trillion, equivalent to -0.8% of GDP. While there has been a modest increase in public expenditure from both central and regional, most of the growth stemmed from a 2.9% YoY rise in social spending, totaling IDR 79 trillion. This partially reflects the initial rollout of the government's fiscal stimulus programs.

June saw a significant spike in government expenditure, surging 54.2% YoY. The Ministry of Finance (MoF) cited three main drivers: the acceleration of fiscal stimulus disbursements, backdated subsidy compensations to Pertamina and PLN (covering Q4 2024), and the unblocking of budget allocations for line ministries. With full-year GDP growth now forecast at 4.7–5.0%, the government is aiming for the upper end of the range, making further stimulus disbursement likely in the second half. One of the implementation challenges is the flagship *Free Meal Program*, which has only achieved 4% of its annual target. Due to these bottlenecks, the government has reduced the maximum budget for the program from IDR 171 trillion to IDR 116 trillion, raising concerns over underutilization and absorption capacity.

On the revenue front, the Ministry of Finance ("MOF") reported a disappointing performance. Cumulative tax collections for the period reached IDR 978 trillion, down -4.8% YoY, while non-tax revenue declined by -22.7% YoY to IDR 223 trillion. The shortfall was largely attributed to the cancellation of the planned VAT hike and the reallocation of state-owned enterprise (SOE) dividends to the newly established sovereign wealth fund, Danantara.

**In response to this, the MOF revised the fiscal deficit ceiling for 2025 to 2.8% of GDP, up from the initial target of 2.5% and higher than 2024's realization of 2.3%. At the same time, spending plans were scaled back to avoid breaching the critical 3% fiscal rule.**



## Danantara: Catalyzing Strategic Growth through Sovereign Capital

Danantara was established in March 2025 as Indonesia's sovereign wealth fund, representing a pivotal shift in the country's long-term economic strategy. Backed by redirected dividends from state-owned enterprises (SOEs), Danantara now holds significant capital reserves, positioning it as a powerful vehicle for financing high-impact national projects.

While the fund's economic impact is yet to be fully realized, Danantara has the potential to emerge as a central orchestrator of Indonesia's industrialization drive. Beyond capital deployment, we see an opportunity for Danantara to partner with the private sector through co-investment schemes. This collaborative model would not only accelerate infrastructure and industrial development but also generate meaningful value-add across strategic sectors, ranging from green energy and digital infrastructure to downstream processing.

**If deployed efficiently and transparently, Danantara could serve as a key enabler in Indonesia's pursuit of long-term growth, anchoring the economy on a path toward its ambitious 8% GDP growth target over the coming decade.**

## 2. Bond Market Resilience Driven by BI Intervention

**Amid global volatility and localized risks, Indonesia's bond market has exhibited remarkable resilience through the first half of 2025.** This stability has been largely underpinned by Bank Indonesia's (BI) proactive stance anchored by direct bond purchases, liquidity injections, and issuance of SRBI (reverse repo instruments), all designed to manage yields and anchor investor confidence.

In practice, BI has become an increasingly dominant buyer in the government bond market. While this intervention has successfully contained volatility and supported yields, it has also begun to distort natural price discovery, particularly along the mid-to-long end of the yield curve. **The crowding-out effect has reduced incentives for both foreign and domestic institutional investors, resulting in more tactical, volume-sensitive participation in government bond auctions. As of mid-July, BI's cumulative bond purchases reached IDR 145 trillion, up from IDR 124 trillion just a month earlier, underscoring the scale of its ongoing support.**

These dynamics have influenced the broader bond market. With sovereign yields appearing increasingly compressed, investors have gradually shifted towards higher-yielding corporate debt. Demand has been strong for investment-grade issuers, especially state-owned enterprises (SOEs) and large financial institutions, where credit spreads remain attractive relative to underlying risk. Corporate bond issuance is expected to pick up meaningfully in 2H25, driven by pre-election financing needs and refinancing cycles, creating a favorable backdrop for the asset class.

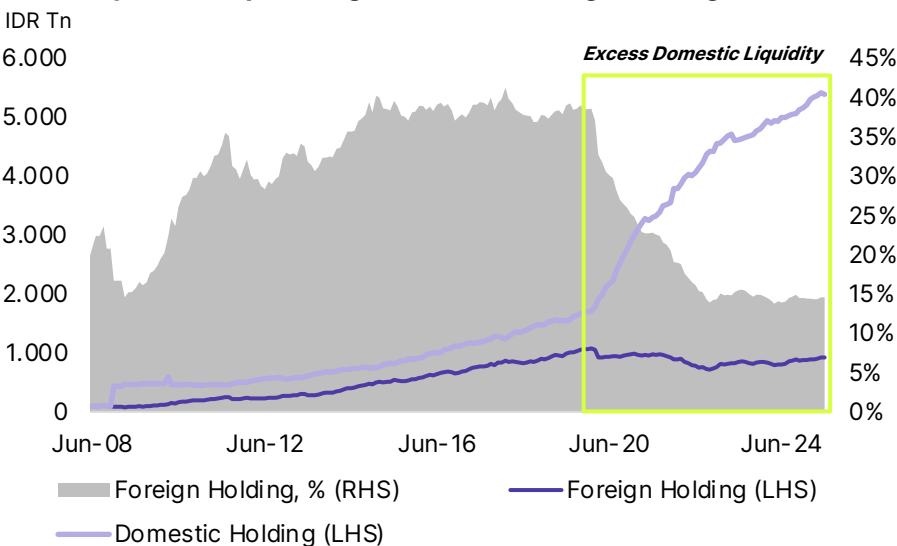
**Monetary policy expectations are further supporting duration assets.** BI has signaled a growing scope for monetary easing, underpinned by subdued inflation and a softer growth outlook. Governor Perry Warjiyo reaffirmed the central bank's dual commitment to maintaining Rupiah stability while stimulating economic activity, highlighting that broader credit expansion will require a sustained accommodative stance. In response to these dovish signals, the previously flat yield curve began to steepen modestly by mid-year, as market participants priced in reduced future intervention and awaited firmer policy guidance.

Source: Simpan Asset Management, Central Agency of Statistics Indonesia (BPS), Bank Indonesia (BI), Ministry of Finance (MoF), Bloomberg. Data as of 30 June 2025

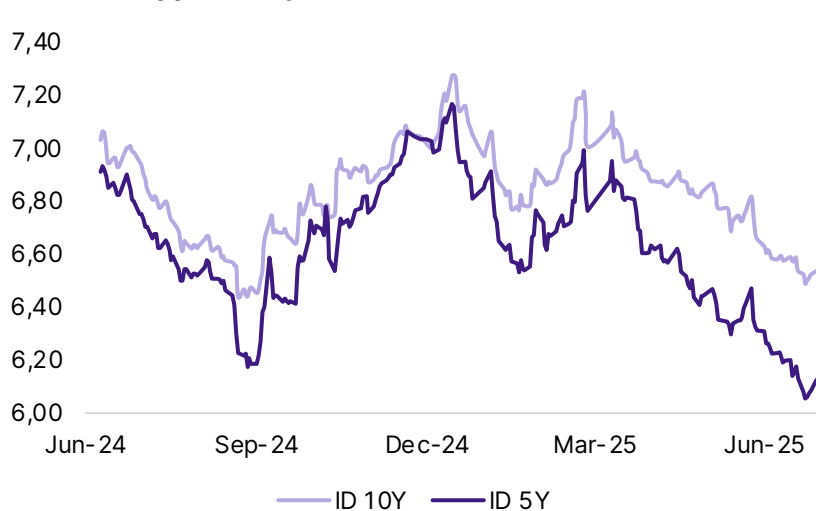
However, there are emerging constraints. BI's balance sheet has absorbed a rising share of sovereign issuance, potentially limiting its flexibility to respond to future shocks, be it currency volatility or inflation surprises. In light of these structural shifts, we maintain a more cautious stance on government bonds and see relatively better value in corporate debt, where spreads remain favorable and yield pickup compensates for the incremental credit risk.

**Looking ahead to the second half of 2025, we expect BI to maintain a steady hand, balancing its commitment to currency stability with the need to support growth.** Against this backdrop, Indonesia's bond market is likely to remain a key anchor of financial market resilience, albeit with a shifting composition in investor preference.

## Domestic intervention, particularly from BI has supported Bond yields despite a significant low foreign holding



## Indonesia's 5Y and 10Y bond yields continue its decline, supported by resilient domestic flows



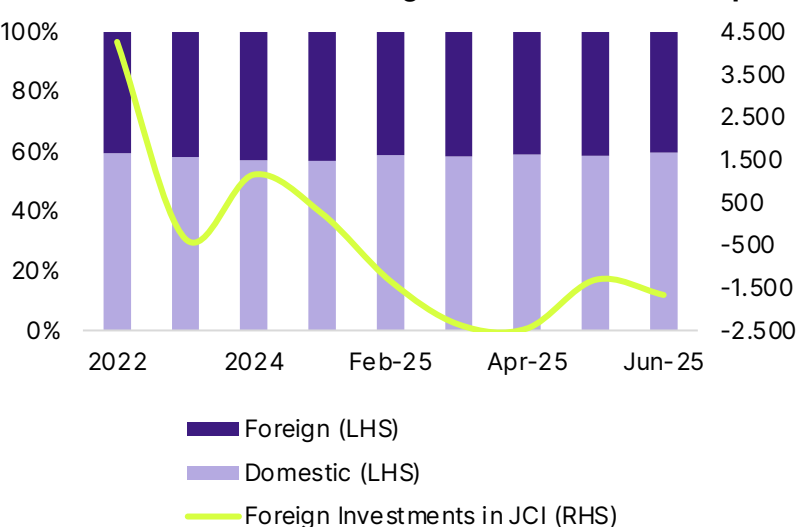
## 3. Foreign Outflows and Domestic Resilience in Indonesia's Equity Market

**Sustained foreign outflows on one side and growing domestic resilience on the other have been the driving forces that shaped Indonesia's equity market in the first half of 2025.** Foreign investors have cumulatively pulled over **USD 3 billion on a Year-to-Date (YTD) basis from the domestic equity market, reflecting concerns over political risk, policy clarity, and a challenging global macro backdrop.** Contributing factors include uncertainty surrounding Danantara's governance, government budget cuts, and episodes of social unrest tied to fuel subsidy reforms and labor protests. These have collectively dampened risk appetite, particularly for large-cap stocks traditionally favored by foreign investors.

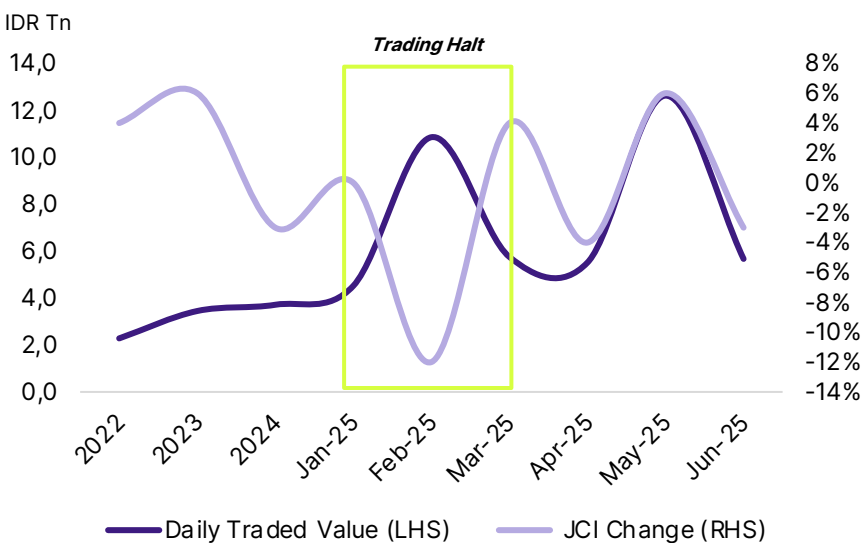
In stark contrast, **domestic institutional investors have stepped in to fill the gap,** helping to cushion equity prices from steeper declines. Major players such as Danantara and BPJS Ketenagakerjaan (Indonesia's national pension fund) have selectively allocated capital into equities, while corporate share buybacks funded by ample cash reserves have added another layer of support. At the same time, retail investors and local fund houses have actively rotated into under-owned, higher-beta segments of the market. Conglomerate-owned and small-cap stocks have seen a notable surge in price and trading volume, driven by liquidity hunting behavior and the search for alpha outside the conventional blue-chip universe. This reflects a broader market change where local capital is increasingly driving price action. **These shifts contribute to a structural transformation in Indonesia's equity market.** With foreign ownership now at multi-year lows, trading volumes have declined in many foreign-heavy names, leading to reduced price discovery and liquidity.

**While we remain constructive on the long-term value of Indonesia's large-cap equities, near-term momentum has rotated toward the domestic side of the market.** Looking ahead, a foreign re-entry is contingent on several key catalysts: improved policy visibility, stabilization of global rates, particularly US Treasury yields, and a more pronounced increase in fiscal disbursement. Until then, local investors are likely to continue playing a dominant role in shaping market direction.

## Ownership in Indonesian Equities continues to be dominated by domestic investors as foreign remain to withdraw capital



## Investor flows continue to drive volatility in the JCI



Source: Simpan Asset Management, Bank Indonesia (BI), Ministry of Finance (MoF), Bloomberg. Data as of 30 June 2025

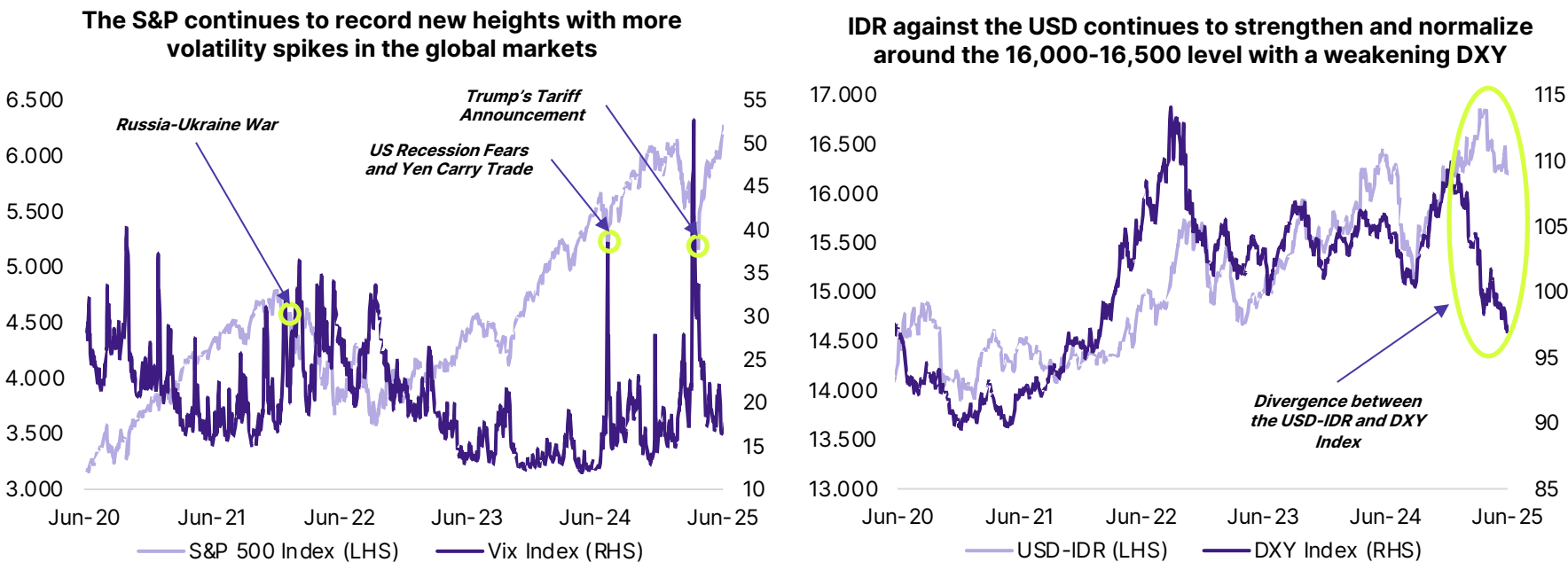
## 4. US Exceptionalism Through Crises: Still Standing Strong

The US economy continues to demonstrate exceptional resilience in the face of cumulative shocks. Despite the lingering effects of the COVID-19 pandemic, global supply chain disruptions, aggressive Fed tightening, trade tariffs, and geopolitical flashpoints in Eastern Europe and the Middle East, US financial markets remain among the best-performing globally.

A notable divergence has occurred between the US dollar and US assets. The DXY has declined more than 10% YTD, its worst start since 1973, typically a tailwind for emerging market currencies. Yet the Indonesian Rupiah has shown only modest strength, with USD/IDR remaining relatively elevated. This divergence suggests that while global USD weakness is clear, domestic factors such as central bank policy, USD demand, and capital flows have kept the Rupiah's movement more contained. In other words, the Rupiah has been resilient not because of appreciation, but because of controlled, limited depreciation amid a weakening USD backdrop. This reflects deep structural advantages: innovation leadership, capital market depth, policy credibility, and investor confidence. For global allocators, US exposure remains a core component. Even in a weaker dollar environment, US assets continue to deliver better risk-adjusted returns. The paradox of US exceptionalism, where the capital markets outperform while the currency underperforms, underscores the ongoing attractiveness of the US as an investment destination.

Looking ahead, we continue to expect the US economy to avoid a recession, even as GDP growth moderates. The recent surge in tariffs introduced in early April has increased risks on both the inflation and recession fronts, but a broader slowdown was already in view. Key factors include an overstretched consumer sector and a persistently low household savings rate, which remains below pre-pandemic levels. Inflation, while still above target, is gradually easing, and we expect a declining trend in the years ahead. In this context, we anticipate substantial monetary easing. Economists project the first rate cut in September, followed by another in December. **Beyond that, it is projected that an additional three rate cuts will occur in 2026 and three more in 2027, totaling 200 basis points of easing through the cycle.**

**In summary, despite short-term headwinds, the United States continues as a beacon of stability, performance, and resilience through its exceptionalism.**





# Appendix: Macro Dashboard

Indicators (as of 30 June 2025)	Indication	Data
Global Indicators		
Dollar Currency Index	Strong	96.88
US GDP Growth (Y/Y)	Strong	4.70
US CPI (Y/Y)	Strong	2.70
UST 10Y vs. UST 2Y	Narrow Spread	0.51
UST 2Y vs. UST 3M	Narrow Spread	-0.75
UST 10Y - US CPI	Wide Spread	1.53
MSCI World P/E	Expensive	23.25
MSCI World Earnings Yield	Expensive	4.30
MSCI World Earnings Yield vs UST 10Y	Narrow Spread	0.07
Indonesia Macro Indicators		
Indonesia GDP (Y/Y)	Weak	4.87
Indonesia CPI (Y/Y)	Weak	1.87
Current Account as a % of GDP	Strong	0.00%
Trade Balance as a % of GDP	Strong	0.08%
M2 Supply (Y/Y)	Weak	4.88
Retail Sales	Weak	2.05
Unemployment Rate	Strong	4.76
Government Expenditure as a % of GDP	Neutral	0.60
Government Revenue as a % of GDP	Weak	0.49
Government Debt as a % of GDP	Strong	39.60
Consumer Credit as a % of GDP	Strong	0.40
Growth Indicators		
BI Consumer Confidence Index	Strong	117.80
Indonesia Industrial / Manufacturing Index	Strong	51.92

Indicators	Indication	Data
Real Returns		
Indonesia GDP - CPI (Y/Y)	Wide Spread	3.00
IDR 10Y Bond Yield - Indonesia CPI (Y/Y)	Wide Spread	4.76
IDR 2Y Bond Yield - Indonesia CPI (Y/Y)	Wide Spread	4.18
IDR 1M Deposit Rates - Indonesia CPI (Y/Y)	Wide Spread	2.17
Bond Characteristics		
Central Bank' Government Bonds Ownership	Strong	25%
Banks' Government Bonds Ownership	Weak	19%
Non-Banks' Government Bonds Ownership	Neutral	56%
Foreign' Government Bonds Ownership	Weak	15%
Bonds Inflow 12M (USD, Million)	Strong	7,009
Bond Spreads		
IDR 10Y - IDR 2Y Bond Yield	Narrow Spread	0.42
IDR 10Y - UST 10Y	Narrow Spread	-0.05
IDR 2Y - IDR 1M Deposit	Wide Spread	-0.77
Stock Valuation		
JCI P/E	Cheap	-1.79
JCI Earnings Yield	Cheap	0.01
LQ45 Earnings Yield	Cheap	-0.31
IDX 20 High Dividend, Dividends Yield	Cheap	1.94
IDR 10Y - JCI Earnings Yield	Narrow Spread	-0.37
MSCI Indonesia Earnings Yield	Cheap	0.01
Stock Inflow 12M (USD, Million)	Weak	-1,909
Banking Sector		
Loan Growth (Y/Y)	Weak	-0.90
Loan to Deposit Ratio	High	0.13
Net Interest Margins	Neutral	0.01
Return on Asset	High	0.10
Non-Performing Loan	Good	-0.01

Source: Simpan Asset Management, BLS, Morgan Stanley Capital International (MSCI), Central Agency of Statistics Indonesia, Ministry of Finance Indonesia, Bank Indonesia, Federal Reserve System, Bloomberg.

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