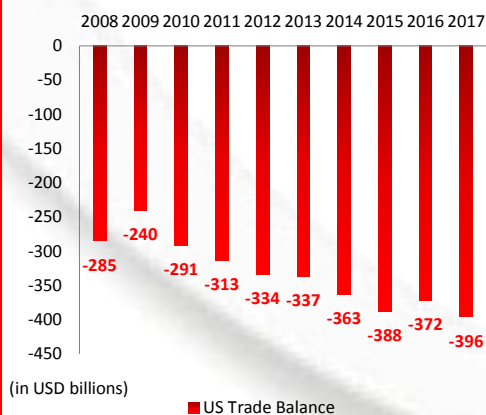


Macroeconomic Review

THE U.S. HAS STARTED 'THE BIGGEST TRADE WAR' IN HISTORY .

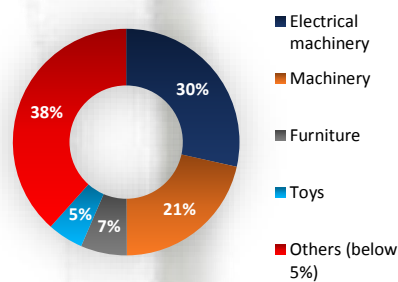
On July 6, 2018, U.S. President Donald Trump's administration began imposing a US\$ 34 billion tariff on goods imported from China, including flat-screen televisions, spare parts and medical equipment. The items that marked for the current rate will face a 25% border tax when exported to the U.S. Responding to the U.S. policy, China will reply to the U.S. by imposing the same tariff of 25% on the U.S. imported goods that valued at US\$ 34 billion, including soybeans, milk, beef, machinery, autos and US-made spare parts. In the next two weeks, the United States is expected to impose more border taxes on the additional of Chinese goods that valued at US\$ 16 billion. The US trade deficit in 2017 with China reached US\$ 396 billion, while China had a trade surplus of US\$ 276 billion.

US-China trade balance, 2008 – 2017



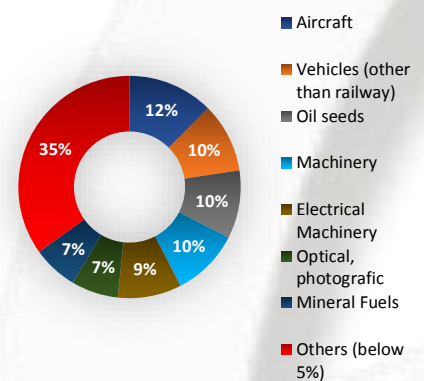
Source: Bloomberg, VMI estimates

US imports from China (2017)



Source: Bloomberg, VMI estimates

China imports from US (2017)



Source: Bloomberg, VMI estimates

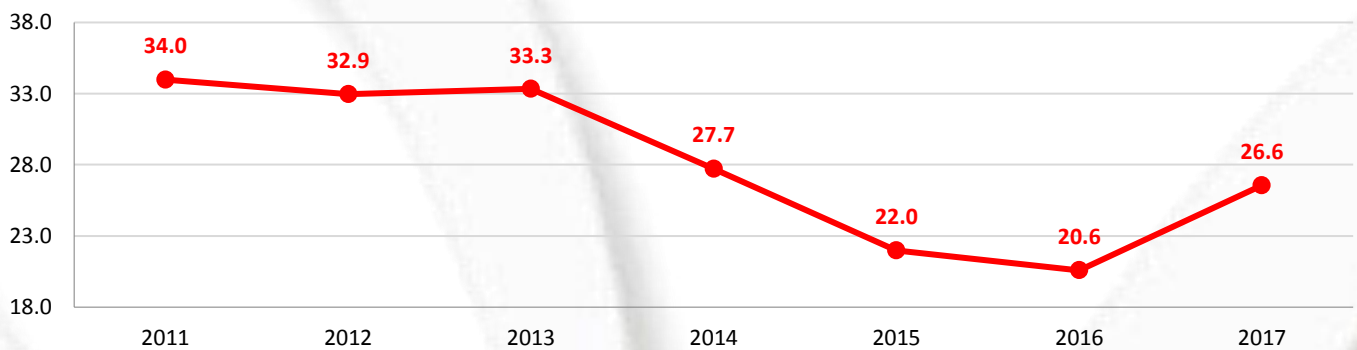
Impacts on Crude Oil.

The policy of increasing import duty by China will have a significant impact on crude oil trade flows between the U.S. and China. U.S. crude oil exports to China are in the range of 300,000 barrels per day (bpd) in the first quarter of 2018, or about 20% more than U.S. total crude oil exports. This shows that China is a major destination for significant crude oil exports for the United States. Even crude oil exports are indicated to be even greater in the second quarter of 2018. The amount of U.S. crude oil exports to China is in line with the declining crude oil production of China, as well as increased oil refining capacity in the world's most populous country. Along with the establishment of crude oil import duties by China, it is certain that U.S. crude oil exports to China will decline in the future. The reason is because China still can find an alternative source from West Africa that has crude oil quality similar to the U.S. On the other hand, the U.S. will find it difficult to find a market alternative that has the same size as China.

Impacts on Coal.

In our opinion, the impact of U.S. - China trade war on coal is less significant, on a scale. In the first quarter of 2018, China imported only 400,000 tonnes of coal from the U.S. or only about 2.6% of China's total coal imports and 1.7% of U.S. total coal exports. Historically, the contribution of U.S. coal to China is the highest at only 4.0% in 2012. Prior to the increase, China's import duty for the U.S. was only 3 - 6%, while Australia and Indonesia were free. Considering higher shipping costs, the U.S. has never been a cost competitive coal supplier to China, unless there is an unexpected large supply disruption from Australia. In fact, with weak domestic consumption, U.S. coal producers will be more triggered to supply coal to the Pacific market, let alone the price of coal is currently on an upward trend. But with higher import duties from China, the U.S. may have to steer coal shipments elsewhere such as India or EMEARC (Europe, Middle East, Africa, Russia, and Caspian) in the longer term, to get better margins.

Indonesia Coal Exports 2011 - 2017 (USD billion)



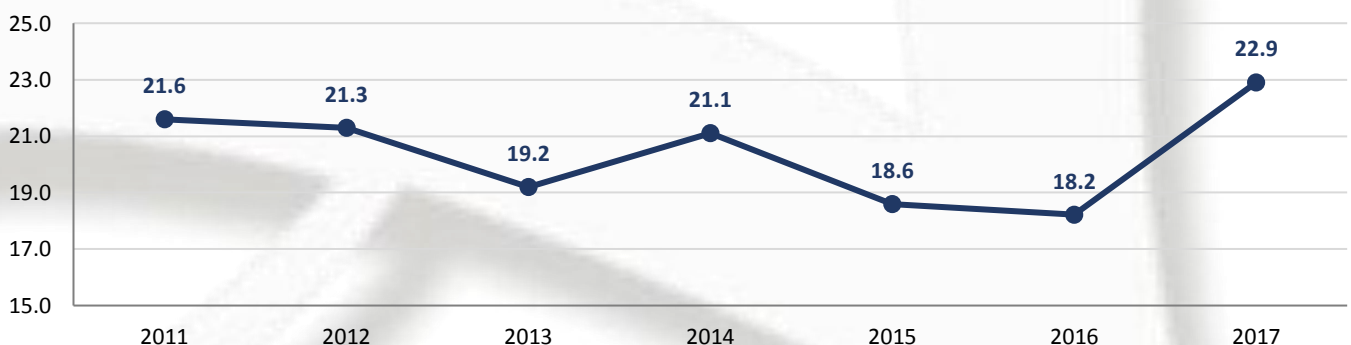
Source: Bloomberg, VMI estimates

- Impacts on Crude Palm Oil (CPO).**

We see the palm oil industry and its derivative products, especially crude palm oil (CPO), which will benefited from this trade war. This is because the CPO is a substitution of soybean oil and China fixes tariffs on imports of all soy products and derivatives originating from the U.S. However, the impact of trade war on listed plantation companies in Indonesia today is not very large. Therefore, palm oil products exported by Indonesia to the U.S. and China are not many. Referring to the datas from Indonesian Palm Oil Entrepreneurs Association (GAPKI), the export of Indonesia's crude palm oil (CPO) and palm kernel oil (PKO) to the U.S. is only about 62,160 tons per April. This number dropped 67.87% compared to the exports at the beginning of the year which reached about 193,470 tons. Meanwhile, until April, CPO and PKO exports to China were about 234,420 tons. This figure is also down 23.76% compared to January exports which reached 307,490 tons. In addition, the plantation companies must remain vigilant, because recently the U.S. President Donald Trump sent a warning to Indonesia and began to re-evaluate products from Indonesia that are exported to the U.S.

Outside of the trade war, the plantation companies are still facing the challenge from anti-oil campaign launched by Europe. Indeed, the Europe has lifted the ban on the use of CPO until 2030. However, the plantation companies do not necessarily sleep well. In addition, India also plans to raise CPO import tariffs. Political sentiment is also helped make world CPO prices weakened to about 6.4% during the first half year. In addition to losses due to the falling commodity prices, listed companies are also threatened to lose their market share. Not only that, currently the Indonesian government is planning to expand the replanting program of oil palm plantations in Indonesia. The target this time is as much as 185,000 hectares for this year. In fact, the government's target was only 4,400 ha for last year. We consider this replanting program will cause palm oil players in Indonesia difficult to obtain their new land in the future.

Indonesia Palm Oil Exports 2011 - 2017 (USD million)

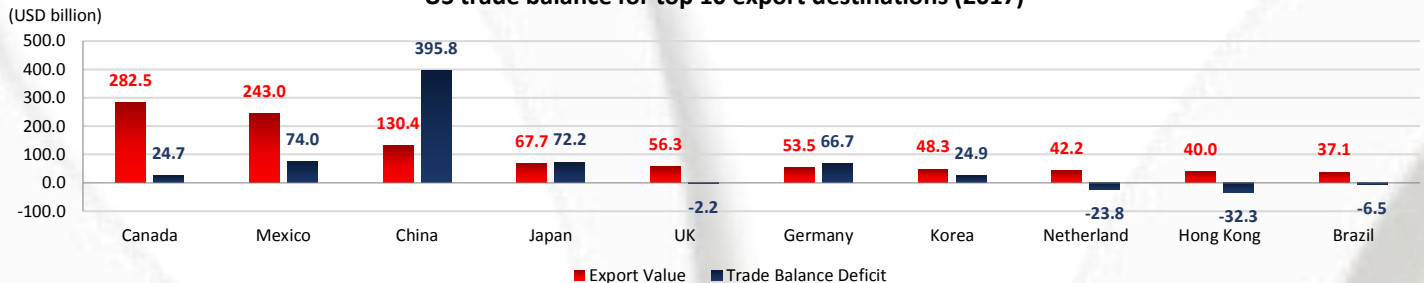


Source: Bloomberg, VMI estimates

HOW IS THE IMPACT OF THE TRADE WAR ON ASIA ECONOMIC GROWTH?

As a result of the ongoing trade war, we project the economic growth of Asian countries to decline slightly this year, some of which are expected to decline by 0.40 percent for South Korea, Malaysia and Taiwan could lose 0.60 percent, Singapore 0.80 percent, while Indonesia only lost 0.13 percent. Many other APEC economies are vulnerable to the losses from the U.S. - China trade war because of East Asia's integrated manufacturing supply chain, and China plays an important role as an export market for other APEC economies.

US trade balance for top 10 export destinations (2017)

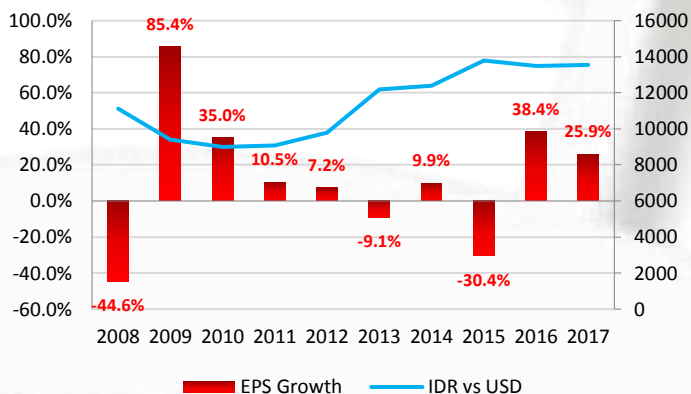


Source: Bloomberg, VMI estimates

THE BIGGEST ISSUE IS NOT COMING FROM TRADE WAR, BUT...

Any negative effects on the companies in Indonesia resulting from the U.S. - China trade war will not happen immediately. So far, the nervousness of the Indonesian people has been higher for the fact that the current rupiah is much weaker than the USD (-6.2% YTD), which could potentially reduce the earnings of some companies in 3Q18 as the trade war increases. The effect will worsen if global growth momentum stops, leading to lower-potential exports, as well as lower FDI to Indonesia. We do not see any positive benefits from market replacement, as Indonesia may not have substitutes for most of the traded Chinese goods. If the U.S. imposes a direct tariff on all goods exported from Indonesia, given the US\$ 9 billion surplus in 2017 (the highest contribution of 44% from clothing), then the adverse impact on the Indonesian economy will certainly be somewhat noticeable, but the likelihood is very small for now.

Indonesia EPS Growth vs IDR weakening



Source: Bloomberg, VMI estimates

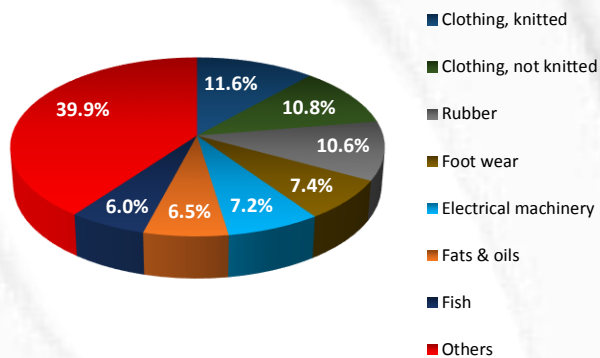
US-Indonesia trade balance 2008 - 2017



Source: Bloomberg, VMI estimates

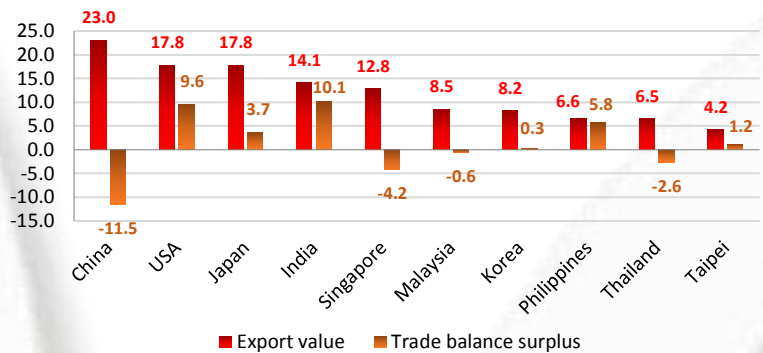
The majority of the companies in Indonesia are still safe from the early phases of the trade war, due to their domestic-oriented sales. A double impact will be seen in the coal sector at higher coal prices as import replacements will be positive for the short term, which is ultimately offset by lower demand, if China's own economic growth declines. We identified that apparel companies, as the largest contributors to exports, would be potentially adversely affected by the trade wars, along with the players of textiles, rubber and electronic machinery.

Indonesia exports to US, by product



Source: Bloomberg, VMI estimates

Indonesia trade balance for top 10 export destinations (2017)



Source: Bloomberg, VMI estimates

	% of Sales	% of COGS	% of Debt
Coal	100.0%	28.0%	0.0%
Heavy Equipment	100.0%	10.0%	19.4%
Metal & Mining	73.6%	46.9%	46.0%
Plantation	9.5%	0.0%	7.7%
Automotive	8.2%	11.5%	40.8%
Telecommunication	5.8%	0.0%	2.2%
Consumer Goods	4.2%	63.6%	19.3%
Cement	2.9%	18.0%	33.3%
Retails	1.2%	27.8%	0.0%
Cigarette	1.1%	0.7%	1.5%
Industrial Estate	0.0%	0.0%	2.2%
Media	0.0%	12.5%	40.0%
Poultry	0.0%	25.0%	28.8%
Property Residential	0.0%	0.0%	37.4%

Source: Bloomberg, VMI estimates

WARNING AND SOLUTION.

Despite from the indirect impacts of current trade war condition, the greatest concern remains in the weakening of our currency, as it may hinder the momentum of domestic recovery as projected in 2Q18. As for the effects of the trade war itself, we see the impact is not so great on Indonesia's current economic growth, which is only reducing 0.13% of our GDP. We recommend an accumulative approach, focusing on companies that can continue to provide robust revenue growth amid market volatility. We see, coal commodities will be the best investment for such situations, while telecommunications and mature consumer goods companies can remain a long-term defensive investment. And of course, we advise investors to avoid first the industries that have the largest export to the U.S. and the most disadvantaged due to the weakening of the rupiah which is the textile industry, rubber, automotive and electronic goods.

Our Investment Team :

Putu Wahyu Suryawan

Fund Manager

Rudy Fenji

Fund Manager

PT VICTORIA MANAJEMEN INVESTASI

Panin Tower Lantai 8, Senayan City., Jl. Asia Afrika Lot.19
Jakarta Pusat 10270
P: 021-72781861
F: 021-72781860

DISCLAIMER: This report is issued by PT. Victoria Manajemen Investasi, a member of the Indonesia Stock Exchanges (IDX) and PT. Victoria Manajemen Investasi is registered and supervised by the Financial Services Authority (OJK). Although the contents of this document may represent the opinion of PT. Victoria Manajemen Investasi, deriving its judgement from materials and sources believed to be reliable, PT. Victoria Manajemen Investasi or any other company in the Victoria Group cannot guarantee its accuracy and completeness. PT. Victoria Manajemen Investasi or any other company in the Victoria Group may be involved in transactions contrary to any opinion herein to make markets, or have positions in the securities recommended herein. PT. Victoria Manajemen Investasi or any other company in the Victoria Group may seek or will seek investment banking or other business relationships with the companies in this report. For further information please contact our number: 62-21-72781861.

ANALYSTS CERTIFICATION: Each contributor to this report hereby certifies that all the views expressed accurately reflect his or her views about the companies, securities and all pertinent variables. It is also certified that the views and recommendations contained in this report are not and will not be influenced by any part or all of his or her compensation.