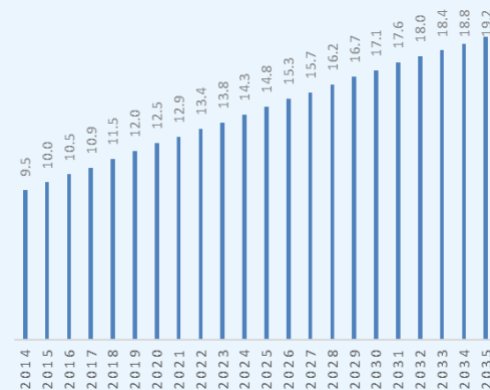


CONSTRUCTION

Construction Sector | Indonesia | November 26, 2021

KEY INDEX

Graph 1: Construction Industry Spending Worldwide from 2014 to 2019, with forecast from 2020 to 2035 (in trillion U.S. dollars)



Source: Statista

Table 1: Contribution to GDP Indonesia 2020, by industry (%)

Manufacturing	19.88
Agriculture, forestry and fishing	13.7
Wholesale and retail trade, etc	12.93
Construction	10.71
Mining and quarrying	6.44
Information and communication	4.51
Financial and insurance activities	4.51
Transportation and storage	4.47
Public administration and defence, etc	3.76
Education	3.56
Real estate activities	2.94
Accommodation and food service activities	2.55
Other services activities	1.96
Business activities	1.91
Human health and social work activities	1.3
Electricity and gas	1.16
Water, sewage and waste management	0.07

Source: Statista

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Despite Pandemic, Construction Activity Increased

- Roads, dam, zone, train, and energy projects will be built in the next period in Indonesia based on National Strategic Projects which contain 245 projects.
- More funds from the Government to support the industry.
- Relocation of capital city will begin in 2022.

Global Construction Outlook 2021

Before the coronavirus (COVID-19) pandemic, the annual spending value of the construction industry reached USD12 Tn (see Graph 1) and is expected to increase by 3%. Given the huge economic and social shock of COVID-19, the market may experience a periodic slowdown. The market size of this industry is expected to more than double in just 20 years, and by 2035 it will exceed USD 19 Tn. Similarly, the scale of the global construction equipment market is expected to continue to grow. The market size will grow by 25% in just five years.

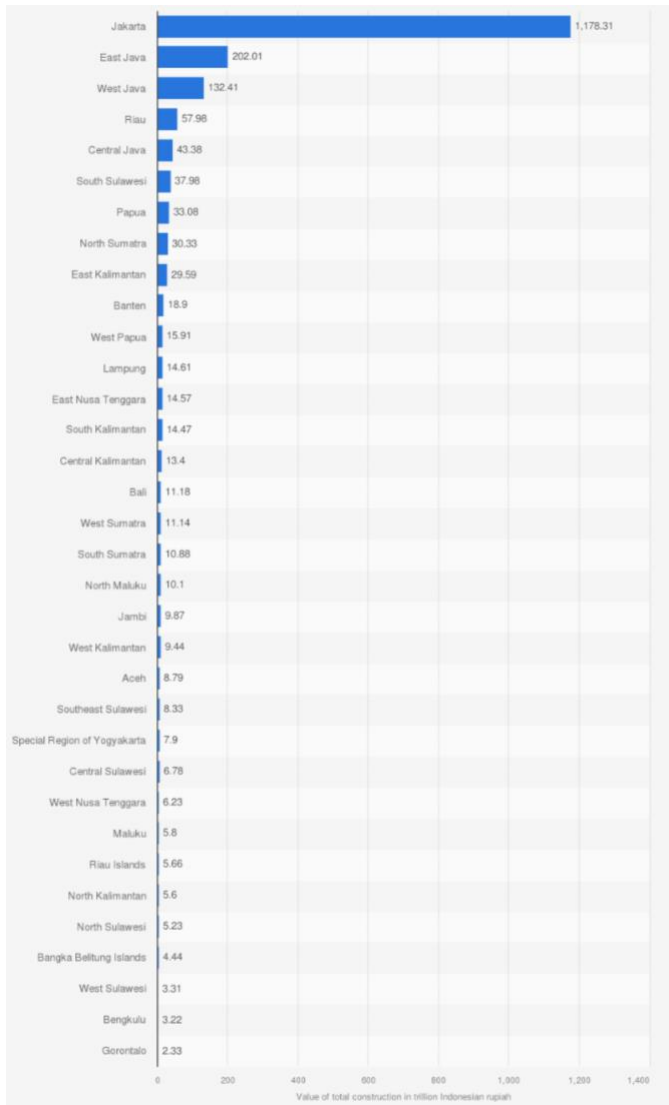
Public Sector Pushing Construction Visibility

Roads, dam, zone, train, and energy projects will be built in the next period in Indonesia based on National Strategic Projects. There are 245 projects and 2 programs, electricity and airplane industry. The total 245 projects will require around IDR 4,197 Tn that will be funded by the state budget, state-owned enterprises and public-private partnerships.

Indonesia's Construction Sector Epicenter is in Java

The construction sector is the fourth-largest contributor to Indonesia's GDP (see Table 1). Over the past few decades, Indonesia's infrastructure development has focused on Java, the most populous island and home to its current capital city, Jakarta. Despite growth on other islands, the total value of the completed construction in Java is more than 100 times that of Bali and more than 30 times that of Papua. In recent years, the Indonesian government has been trying to reduce development inequality by building toll roads nationwide. In 2015, Indonesia started its biggest infrastructure project, the Trans-Sumatra Toll Road, to connect the northern part to the southern part of Sumatra, the second-largest island in the archipelago and the six-largest island globally.

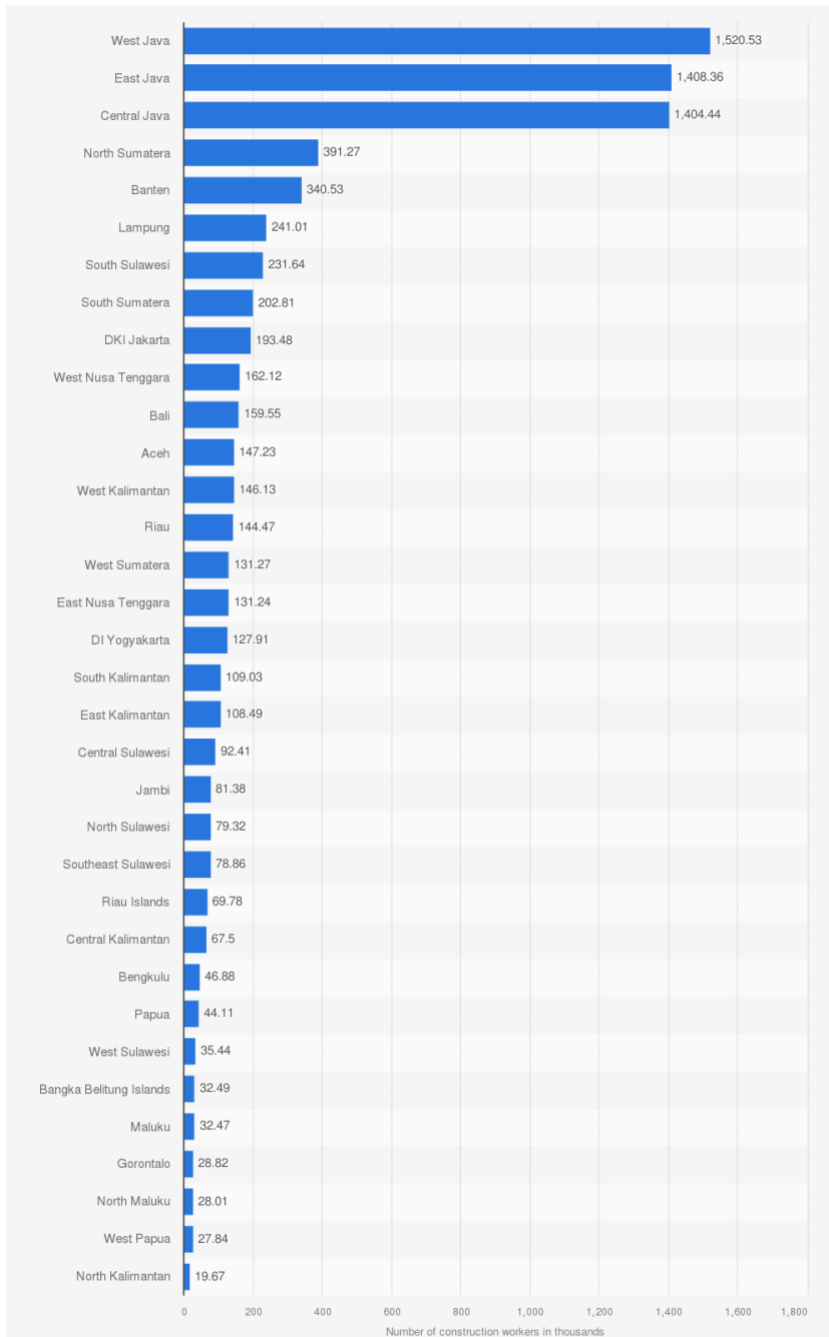
Graph 2: Value of Total Construction Completed in Indonesia in 2019, by province (in trillion Indonesian Rupiah)



Source: Statista

More than 80% of Indonesian construction sites are small businesses and rely heavily on local workers. By far, West Java has the largest number of construction workers in Indonesia. Becoming a permanent construction worker in Indonesia today is still rare, as most workers are ordinary day-to-day wage workers with no certifications or high formal education. In recent years, the Indonesian government has helped these workers obtain official certifications to enhance their skills.

Graph 3: Number of Construction Workers in Indonesia as of August 2020, by Province (in 1,000s)

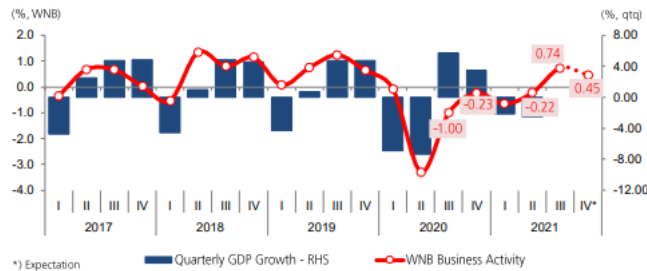


Source: Statista

Construction Activity in Indonesia Increased

Several National Strategic Projects (PSN) and regional infrastructure projects are still being completed, thus helping to improve the construction sector. As domestic demand has grown and some projects have restarted, construction activity increased in the third quarter of 2021, and weighted net balance (WNB) increased from 0.22% in the previous quarter to 0.74%. With the increase in construction activities, respondents confirmed that the labor utilization decreased slightly from 0.39% to 0.34%.

Graph 4: Business Activity of Construction Sector



Source: Bank Indonesia

Graph 5: Labor Utilization of Construction Sector



Source: Bank Indonesia

Relocation of Capital City

The latest news is that the construction of the capital city will begin in 2022. The military, police, and civil servants will start to relocate in 2023. The contractor has not yet received a list of projects for the new capital city. Parliamentary debates are unpredictable and we may not know the outcome until 1Q22. The capital city project budget is IDR 466 Tn and is funded by the state budget and public-private partnerships.

Jakarta-Bandung High-Speed Railway (HSR) Project

The government recently issued Presidential Decree 93/2021, which allows the HSR project to be financed by state budget and appointing Kereta Api Indonesia (KAI – non-listed) as the project’s lead consortium, replacing WIKA. KAI would receive IDR 4.3 Tn state capital injection from the outstanding budget 2021 in order to speed up the project. At Wailini, the HSR’s management team also cut one transit station, bringing the total number of transits to four. Meanwhile, there is still no clarification on how to finance USD 1.9 Bn cost overrun, which was mostly caused by delays in land acquisition and pandemic. The current construction progress is around 80%, and the HSR is targeted to start operation in 4Q22.

More Funds from the Government to Upgrade Infrastructure

The Government has approved a state capital injection of IDR 52 Tn for eight state-owned enterprises. Hutama Karya will get IDR 15.2 Tn to accelerate works on the Trans-Sumatra Toll Road. Adhi Karya is also likely to benefit from these funds, and its work on the Sigli-Banda Aceh Toll Road can be expected to be at least IDR 3.1 Tn. Meanwhile, Waskita Karya will be allocated about IDR 7.9 Tn and will continue to work on seven existing toll road projects (one in Sumatra and six in Java).

Figure 2: State Capital Injections In 2021

State-Owned Enterprise		Total (IDR Tn)	Details
Phase 1	Hutama Karya	3.1	Sigli - Banda Aceh
		2.7	Lubuk - Linggau Curup - Bengkulu
		0.4	Kuala Tanjung - Tebing Tinggi - Parapat
	Pelindo	1.2	Port development
	Indonesia Tourism Development Corporation	0.5	Basic infrastructure
	Kawasan Industri Wijayakusuma	1.0	Industrial estate
	PAL Indonesia	1.3	Submarine
	PLN	5.0	Substation transmission
	Indonesia Financial Group	20.0	N/A
2021 -	Waskita Karya	7.9	Working capital improvement
Phase 2	Hutama Karya	9.0	Most Trans Sumatra Tollroad
	Total	52.0	

Source: Various Sources

Challenges Facing the Indonesian Construction Industry

In August 2019, Indonesia’s President Joko Widodo officially announced that its capital city will be relocated to East Kalimantan. The infrastructure projects for the relocation were planned to start in 2021. However, in 2020, the Indonesian government had to put many projects, including the capital city relocation, on hold due to the COVID-19 pandemic. In that year, the revenues of Indonesia’s largest construction companies such as Waskita Karya, Wijaya Karya, and PT PP also declined for the first time in the past few years.

Even before the pandemic, most of the small-sized construction companies in Indonesia were already struggling to keep sustaining their businesses and competing against the large contractors. Smaller construction companies lack heavy equipment and capital which the large-scale infrastructure development projects required. However, as long as the Indonesian government is focusing on improving the archipelago’s infrastructure to strengthen its economy, Indonesia’s construction sector is projected to continue growing, supported not just by the government but also by foreign investments and the private sector.

Construction Sector is Expected to Continue Improving

Future improvements in the construction sector are expected to continue throughout 2021, but not as strong as expected due to the delay in many projects in some regions. The performance of the regional construction sector will be supported by the achievement of many PSN project goals in 2021, which was higher than the previous year. In addition, a higher central government infrastructure spending allocation in 2021 will further elevate construction sector performance, along with completion of several large-scale infrastructure projects, such as the Trans-Sumatra Toll Road (JJTS) in Sumatra, Phase II Jakarta MRT project, Jabodebek LRT project, Patimban toll road in Java, projects to support tourism activity in the Balinusra region, including the Singaraja Mengwitani road, national tourism strategic areas (KSPN) in East Nusa Tenggara (Puncak Waringan, Batu Cermin, Bukit Pramuka) and supporting infrastructure in Mandalika, West Nusa Tenggara. Meanwhile, accelerating post-earthquake reconstruction in West Sulawesi will support Sulawesi's construction sector with the completion of national strategic and electricity projects. Several incentive policies for residential real estate purchases, such as lower loan-to-value (LTV) ratios and value-added tax exemptions, are also expected to increase property demand. Nonetheless, the relentless COVID-19 pandemic and delays in completing some regional infrastructure projects have resulted in lower performance improvements in the construction sector than previously estimated, partly due to the refocusing of government budgets.