∂Ri/884/pi/2007

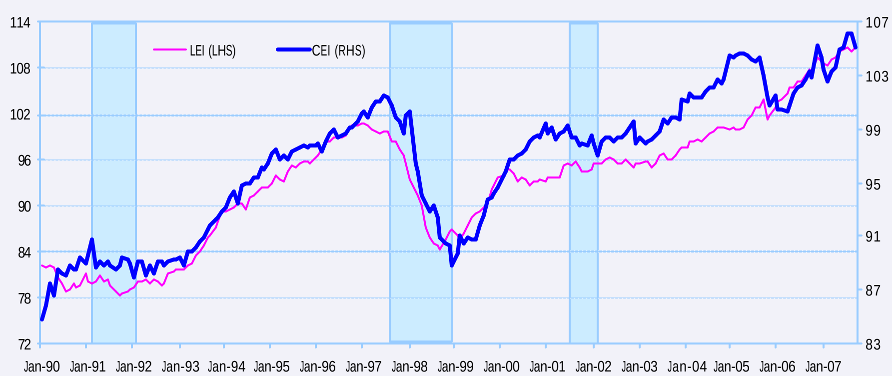
November 2007

EARLY ECONOMIC INDICATORS

Strong Growth[1]

- **In September 2007, the dRi Coincident Economic Index (CEI), which tracks the current state of the economy, fell to 105.1 (down by 1.0% month-on-month) from 106.2 in August 2007. This is the first time the CEI has fallen in seven months. As such, it is too early to conclude that the uptrend in the CEI has been broken. Indeed, the fall in the CEI is only temporary we believe, and the CEI is likely to rebound in the coming months.**
- **The latest data shows that the Indonesian economy grew by 6.5% year-on-year (YoY) in Q3 2007, slightly up from the 6.3% YoY growth pace in Q2 2007. As such, the Indonesian economy is picking up its growth pace.**
- **The dRi Leading Economic Index (LEI) that moves ahead of the Coincident Index (around 6 to 12 months) rose to 110.7 in September from 110.3 in August 2007 (up by 0.4% m-o-m). The LEI had increased from March 2007 till July 2007, but declined in August 2007. The rebound in the LEI in September suggests that the economic recovery is likely to be sustainable and that the economy is likely to continue to pick up its growth pace in the near term.**
- **Improving purchasing power, combined with relatively low interest rates, have spurred domestic demand. Investment activities have also increased significantly. As a result, the engine of economic growth is more balanced than before, thus meaning that the current economic expansion is more sustainable than before.**
- **Against this backdrop, we reiterate our forecast that the Indonesian economy will grow by 6.23% in 2007. The expansion is expected to continue in 2008, in which year the economy is expected to grow by 6.33%.**

Graph 1. Coincident Index: Current Economic Activity Fell in September2007



[1] The previous months' index may be slightly different from the published index in the previous month due to data revision. As such, CEI and LEI data in previous publications cannot be used in conjunction with the data in the current and future publications.

Forecast for 2007

GDP growth (%YoY)	6.23
Inflation (%YoY)	6.25
SBI 1M (%p.a)	8.25

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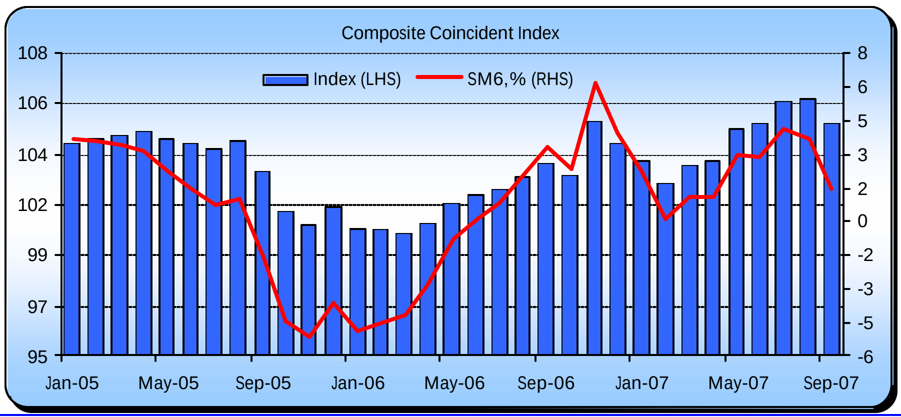
I. Coincident Index[2]: Down on Seasonality Factors

In September 2007, the dRi Coincident Economic Index (CEI), which tracks the current state of the economy, fell to 105.1 (down by 1.0% month-on-month) from 106.2 in August 2007. This is the first time the CEI has fallen in seven months. Hence, it is too early to conclude that the uptrend in the CEI has been broken. Indeed, the fall in the CEI is only temporary we believe (due to the impact of Ramadhan and Idul Fitri) and, as such, the CEI will resume its upward trend in the near future.

Graph 2. Composite Coincident Index and its SM6 Annualized Growth Rate



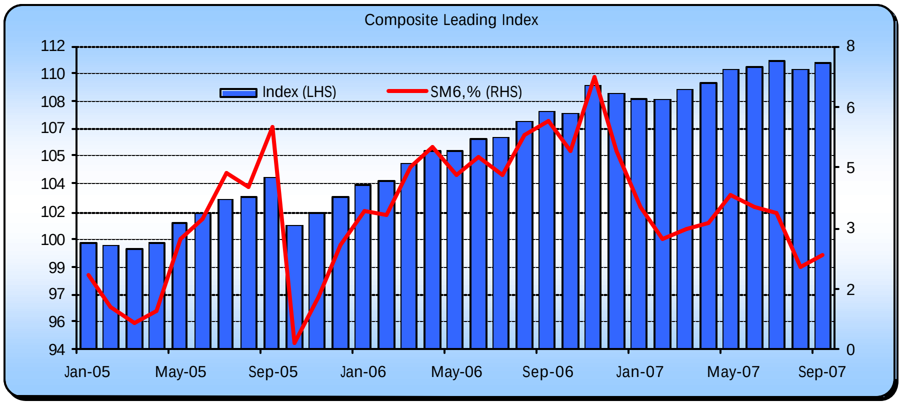
In September 2007, all of the CEI components fell: the deflated imports index dropped to 143.0 from 146.4 in August (down by 2.3% m-o-m), the domestic car sales index fell to 120.5 from 125.8 in August (down by 4.2% m-o-m), the cement consumption index retreated to 123.5 from 138.7 in August (down by 11.0% m-o-m), the real money supply index edged down to 159.9 from 164.1 in August (down by 2.6% m-o-m), and the retail sales index fell to 66.8 from 68.1 in August (down by 1.8% m-o-m).

II. Leading Index: Rebounded

The dRi Leading Economic Index (LEI) that moves ahead of the Coincident Index (around 6 to 12 months) rose to 110.7 in September 2007 from 110.3 in August 2007 (up by 0.4% m-o-m). The LEI had increased from March 2007 till July 2007, but declined in August 2007. Hence, the rebound in the LEI in September suggests that the economic recovery is likely to be sustainable and that the economy is likely to continue to pick up its growth pace in the near term.

[2] We have rebased the CEI and LEI data. As such, the current 2005-based CEI-LEI is different from the previous CEI-LEI data that were published before May 2006.

Graph 3. Composite Leading Index and its SM6 Annualized Growth Rate



Four components of the LEI rose in September 2007: the building permits index rose to 77.0 from 76.9 in August (up 0.2% m-o-m), the number of foreign tourist arrivals index rose to 98.2 from 92.9 in August (up by 5.8% m-o-m), the Jakarta Composite Index (JCI) index rose to 389.1 from 357.7 in August (up by 8.8% m-o-m), the real effective exchange rate index rose to 103.0 from 99.7 in August (up by 3.3% m-o-m). Three components of the LEI fell, however, in September 2007: the foreign investment approvals index fell to 242.7 from 242.9 in August (down by 0.1% m-o-m), the total real exports index fell to 175.6 from 190.4 in August (down by 7.8% m-o-m), and the CPI services index fell to 2.62 from 2.63 in August (down by 0.4% m-o-m).

Table 1. Summary of Composite Indexes

	Aug-07	Sep-07	%MoM
Coincident index	**106.2**	**105.1**	**-1.0**
Domestic car sales index	125.8	120.5	-4.2
Cement consumption index	138.8	123.5	-11.0
Deflated import index	146.4	143.0	-2.3
Real money supply index	164.2	159.9	-2.6
Retail sales index	68.1	66.8	-1.8
Leading index	**110.3**	**110.7**	**0.4**
Building permits index	76.9	76.9	0.2
Number of foreign tourist arrivals index	92.9	98.2	5.8
Foreign investment approvals index	242.9	242.7	-0.0
Real effective exchange rate index	99.7	102.9	3.3
JCI index	357.7	389.1	8.8
Total real exports index	190.4	175.6	-7.8
CPI services index	2.6	2.6	-0.4

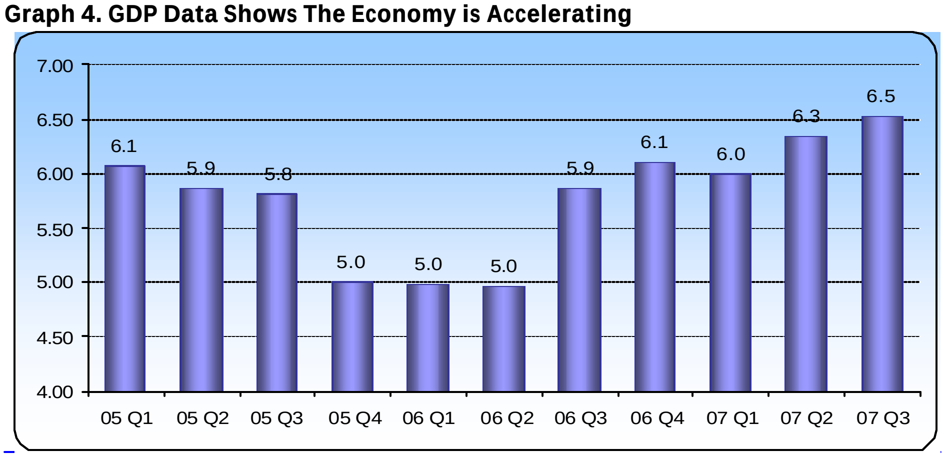
Source: Danareksa Research Institute (DRI)

III. The Near Term Economic Outlook: Prospects Remain Bright

The CEI fell slightly in September. The decline, however, does not necessarily mean that the economy is moving into a slower growth phase. We believe Lebaran and the Idul Fitri holidays were the main reasons behind the drop in the CEI. And going forward, the economy is very likely to continue expanding and even to grow at a faster rate as suggested by the increasing trend in the LEI.

Indeed, the GDP data recently published by the Central Bureau of Statistics (BPS) shows that the Indonesian economy is picking up its growth pace. The huge fuel price hikes in October 2005 had previously slowed down the economy: Indonesia's economic growth rate had dropped sharply from 5.8% YoY in Q3 2005 to 5.0% YoY in Q4 2005. Yet in the second half of 2006, however, economic activities started to pick up significantly. Indeed, the Indonesian economy grew by 5.9% YoY in Q3 2006, and has continued to grow at a brisker pace since (see graph 4).

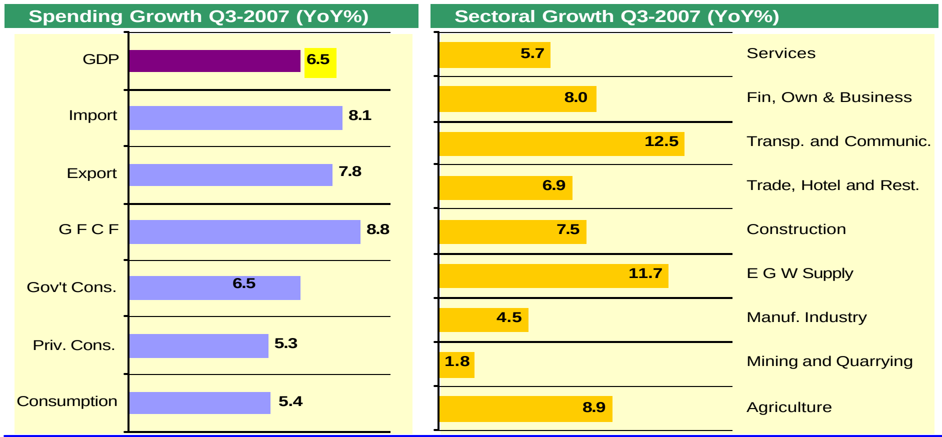
Graph 4. GDP Data Shows The Economy is Accelerating



In Q3 2007, the Indonesian economy grew by 6.5% YoY, or faster than the 6.3% YoY growth seen in Q2 2007. In the third quarter of 2007, nearly all of the components of GDP posted strong growth. Household consumption, for instance, grew by 5.3% YoY, or higher than the 4.7% YoY growth seen in the second quarter of 2007. Government spending rose by 6.5% YoY, compared to 3.8% YoY in the second quarter of 2007. Imports climbed 8.1% YoY in the third quarter of 2007, or slightly higher than the 7.3% YoY figure in the previous quarter, with investments growth reaching 8.8% YoY, up from 7.0% YoY in the second quarter of 2007. Meanwhile, exports grew by 7.8% YoY in the third quarter of 2007, slightly down from 9.8% YoY in the previous quarter (graph 5).

By sector, in the third quarter of 2007, the Manufacturing sector grew by 4.5% (vis-à-vis 5.1% in Q2 2007), the Electricity and Gas sector by 11.7% (vis-à-vis 10.5% in Q2 2007), the Construction sector by 7.5% (vis-à-vis 7.9% in Q2 2007), the Trade and Hotels sector by 6.9% (vis-à-vis 7.3% in Q2 2007), the Transportation and Communications sector by 12.5% (vis-à-vis 11.8% in Q2 2007), the Financial sector by 8.0% (vis-à-vis 7.9% in Q2 2007), and the Agriculture sector by 8.9% (vis-à-vis 4.8% in Q2 2007). See graph 5.

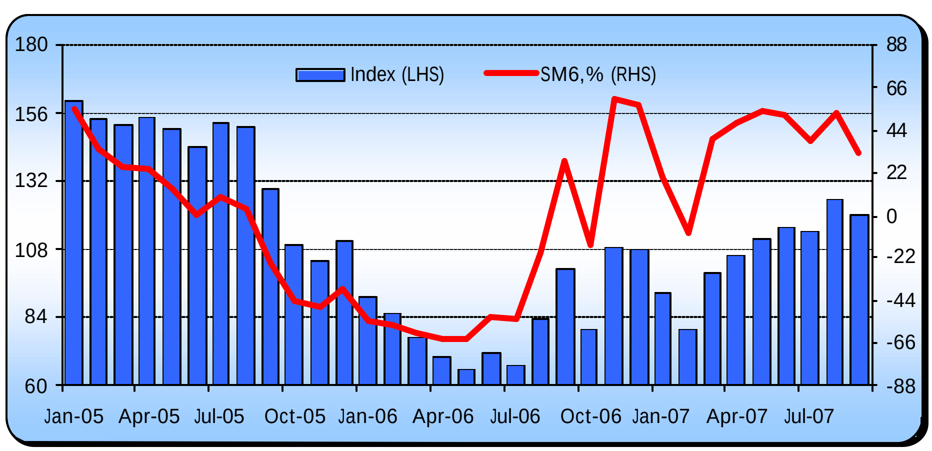
Graph 5. Q3 2007 GDP Indonesian GDP Growth



The pattern of growth suggests an improvement in the balance of the engines of growth compared to the previous year. In 2006, for example, economic growth was mainly driven by consumption and exports. Investment, in contrast, only grew by 2.9 percent in the whole of 2006. Thus, the increase in investment in 2007, especially in the third quarter of the year, suggests that the growth engine for the Indonesian economy is more balanced now; that is the country's economic growth is no longer solely fueled by consumption; and thereby meaning the current economic expansion is more sustainable.

Nevertheless, household consumption did increase in the third quarter of 2007, reflecting strong domestic demand. Improving purchasing power, combined with relatively low interest rates, certainly have spurred domestic demand. Among other things, the strong domestic demand is reflected in the increasing trend in car sales. Back in February 2007, car sales were at a low level. Weak purchasing power (on the back of high rice prices) combined with major flooding had dented car sales in the first two months of 2007. Yet since March 2007, car sales have risen consistently. And low interest rates and improving purchasing power have given an additional boost to car sales. Such strong growth in car sales explains why the car sales index had risen consistently since March 2007 (graph 6). And although this index did see a fall in September due to the impact of Lebaran, we believe the index shall soon recover given the favorable economic environment previously mentioned.

Graph 6. The Domestic Car Sales Index Is In An Uptrend



In addition, the imports data also depicts a condition of strong domestic demand. As shown by the latest GDP data, imports posted strong growth of 8.1% YoY in the third quarter of 2007 vis-à-vis 7.3% YoY in the previous quarter. Furthermore, Indonesian imports have been consistently above US$ 6 billion since May 2007. And in August 2007, imports reached an historic high of US$ 6.85 billion. And although imports did indeed fall in September 2007, this month was still the second highest month for imports on record. As a result, imports grew by 17.43% in the first nine months of 2007, or significantly more than the paltry 4.21% growth rate in the same period of 2006. Please note, however, that since exports also grew significantly in the same period (up by 12.88%), the current account balance did not come under pressure. The latest data shows that the Indonesian trade balance in the first nine months of 2007 reached US$ 29.35 billion, or up from US$ 27.85 billion in the same period of 2006 (table 2).

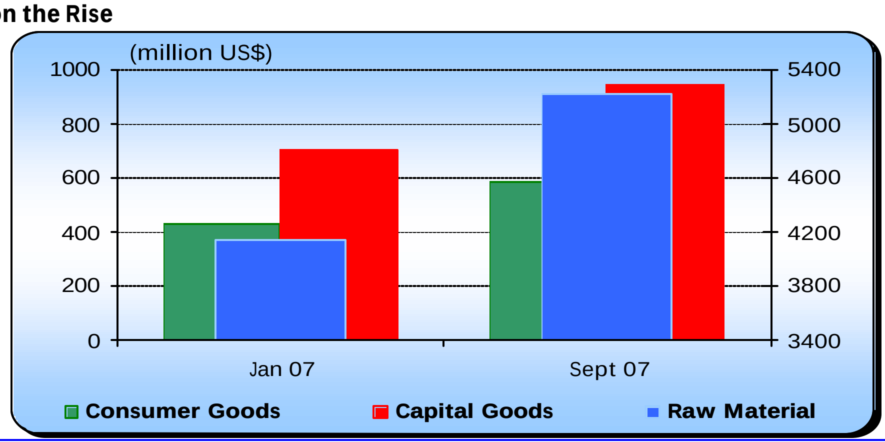
Imports have risen for all types of goods. For example, imports of consumption goods rose from US$ 434.9 million in January to US$ 586.0 million in September 2007 (up by 34.7%). Imports of capital goods rose from US$ 702.2 million in January to US$ 944.5 million in September 2007 (up by 34.5%) and imports of raw materials rose from US$ 4.15 billion in January to US$ 5.22 billion in September 2007 (up by 26.0%) (graph 7). The rise in imports suggests that domestic demand is increasing, thus also suggesting an improvement in purchasing power and brisker economic activity.

Table 2. Imports Posted Strong Growth

(billions of US$)	Dec-06	Jan-07	Feb-07	Mar-07	Apr-07	May-07	Jun-07	Jul-07	Aug-07	Sep-07	2006	2007
											YTD(Jan-Sep)	
Export	**9.61**	**8.32**	**8.19**	**9.06**	**8.91**	**9.81**	**9.56**	**10.04**	**9.61**	**9.52**	**73.56**	**83.03**
Oil & Gas	1.90	1.52	1.47	1.57	1.54	1.79	1.83	1.83	1.85	1.98	15.97	15.38
Non-Oil & Gas	7.72	6.80	6.73	7.49	7.38	8.02	7.73	8.21	7.75	7.54	57.59	67.65
Import	**4.97**	**5.28**	**4.66**	**5.65**	**5.64**	**6.46**	**6.01**	**6.36**	**6.85**	**6.76**	**45.71**	**53.67**
Oil & Gas	1.37	1.39	1.10	1.70	1.63	1.91	1.65	1.77	1.78	2.24	14.49	15.17
Non-Oil & Gas	3.60	3.89	3.56	3.95	4.02	4.54	4.36	4.59	5.07	4.52	31.22	38.51
Tade Balance	**4.64**	**3.04**	**3.53**	**3.42**	**3.27**	**3.35**	**3.54**	**3.68**	**2.76**	**2.76**	**27.85**	**29.35**
Oil & Gas	0.53	0.13	0.37	-0.12	-0.09	-0.12	0.18	0.06	0.08	-0.26	1.48	0.21
Non-Oil & Gas	4.11	2.91	3.17	3.54	3.36	3.47	3.37	3.62	2.68	3.03	26.37	29.14
YoY Growth (%)												
Export	18.81	10.11	10.77	20.93	16.64	17.18	13.05	13.05	7.80	7.64	17.31	12.88
Import	3.75	20.38	2.99	28.04	18.08	26.64	5.06	17.24	20.07	19.63	4.21	17.43

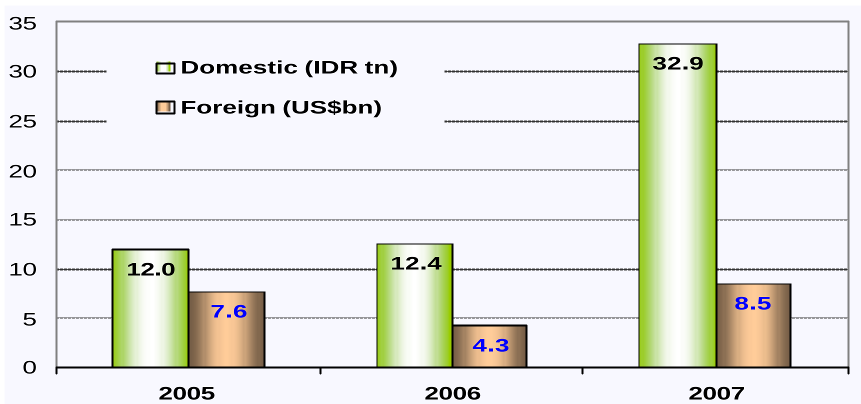
Source: Cdentral Bureau of Statistic (BPS)

Graph 7. Imports of Consumption Goods, Capital Goods, and Raw Materials are on the Rise

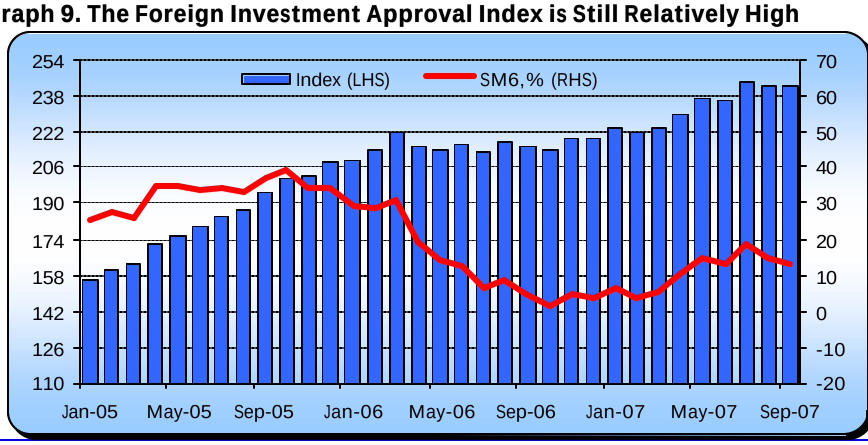


Against this backdrop, investment has also increased significantly. The latest GDP data shows that investment grew by 8.8% YoY in the third quarter of 2007, or up from 7.0% YoY in the second quarter of the year. And the latest data on realized investment also points toward stronger investment activities (graph 8). In the first nine months of 2007, realized domestic investment reached 32.9 trillion rupiah (up by around 164% from 12.4 trillion rupiah in the same period of 2006), while foreign realized investment reached US$ 8.5 billion (up by around 99% from US$ 4.3 billion in the same period of 2006). And, going forward, foreign investment is likely to remain strong, as depicted by the high level of the Foreign Investment Approvals index (graph 9). Also, on the back of relatively low interest rates, domestic investment activities are likely to remain firm.

Graph 8. Domestic and Foreign Realized Investment (January-September)

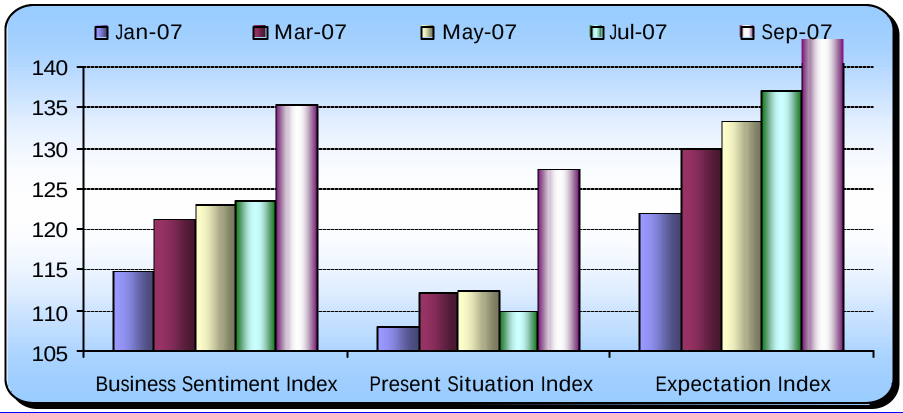


Graph 9. The Foreign Investment Approval Index is Still Relatively High



The expectation of a rosier economic outlook is confirmed by our business sentiment survey. Every other month we survey CEOs of companies operating in Indonesia. From the survey's findings, we construct a Business Sentiment Index (BSI). The reading of the index is quite simple: a reading above 100 indicates that the CEOs are optimistic (which often means that economic conditions are improving), while a reading below 100 indicates that CEOs are pessimistic (usually a reflection of deteriorating economic and business conditions). Based on our surveys, the BSI has increased consistently since January 2007, thereby indicating that the CEOs' businesses are doing better (graph 10). From a reading of 115.0 in January the BSI rose to 135.3 in September 2007; this improving trend suggesting that the economy is picking up its growth pace.

Graph 10. The Business Sentiment Index in on the Rise

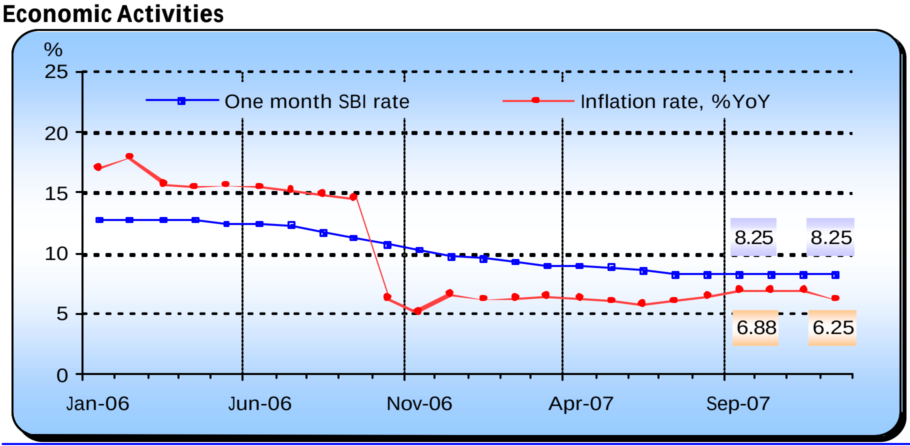


Looking ahead, we believe the Indonesian economy will grow at an even faster rate than before. The dRi Leading Economic Index (LEI) rose to 110.7 in September from 110.3 in August 2007. Over the last seven months, the LEI has risen on six occasions, suggesting brighter prospects for the Indonesian economy in the near term.

Several favorable factors are likely to give an additional push to Indonesian economic growth in the near future. First of all, we believe that inflation will remain in check, as the government will not increase the fuel prices further in the near future. With benign inflationary pressure, we believe that the Indonesian central bank will keep the interest rates at a low level. Thus, consumer purchasing power should improve. By the end of 2007, the inflation rate is expected to stand at 6.25% with the BI rate at 8.25 percent (see graph 11). Furthermore, on the back of seasonality factors, government spending will also increase in the fourth quarter of 2007. And, in addition, government plans to increase civil servants' salaries by up to 20% will also boost household spending if implemented.

Moreover, global economic conditions still remain supportive it seems. Although we expect a slowdown in the economies of some of Indonesia's main trading partners, the economic growth rates in these countries are expected to remain high enough to result in additional demand for Indonesian exports. Also, the Organization of Petroleum Exporting Countries (OPEC) has reiterated its readiness to raise oil production to meet the rising demand for oil in Asia. This will help keep producers' cost pressures under control.

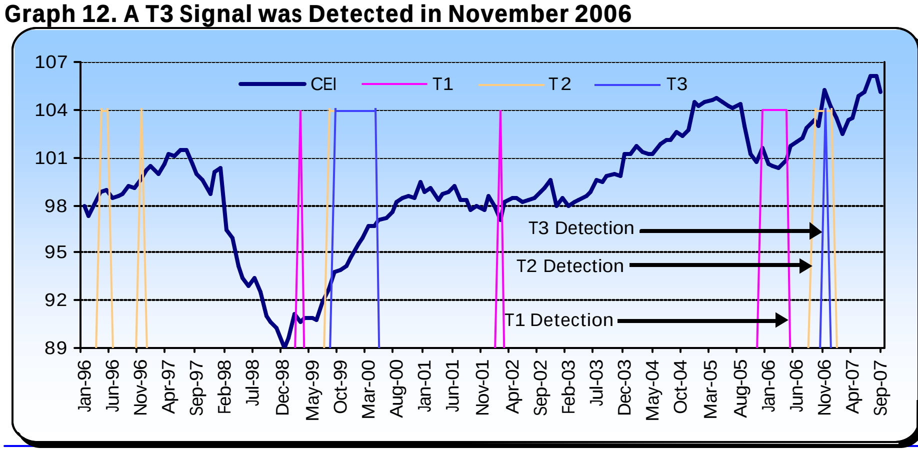
Graph 11. Low Interest Rate and Benign Inflation are Helping to Boost Economic Activities



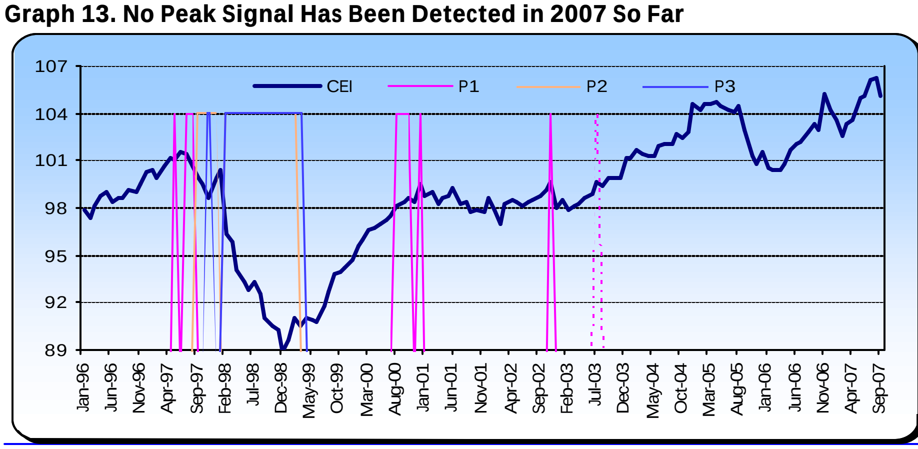
Furthermore, our business cycle indicators also suggest that the Indonesian economy is currently accelerating. To determine the position of the Indonesian economy in its business cycle, we use the sequential signaling method[3]. The sequential signaling method employed confirms that the Indonesian economy has reached the bottom of its business cycle (graph 12) and that it is currently growing at full speed. A T1 (trough) signal was detected in January 2006, suggesting that the economy had stopped slowing. And a T2 signal indicates that the expansion has moved onto the next stage; that is, the economy is not only expanding, but that it is expanding at a much faster pace. Finally, a T3 signal was detected in November 2006, suggesting that the Indonesian economy is currently well into the expansion phase of its business cycle.

Meanwhile, no peak signal has been detected in 2007 so far, suggesting that the likelihood of the economy entering into a slowdown phase is remote (graph 13). As such, the Indonesian economy is likely to remain on its growth path.

Graph 12. A T3 Signal was Detected in November 2006



Graph 13. No Peak Signal Has Been Detected in 2007 So Far



[3] We use "the sequential signalling" developed by Zarnowitz and Moore (1982). In short, this method tells that detection of P1, followed by P2 and P3 indicate that a recession is looming. However, if the detection of P1 is not followed by detection of P2, then the economy is only slowing down, and recession is unlikely to occur in the upcoming months. The business cycle trough was detected by the detection of a T1 signal, followed by T2, then by T3. However, the time span between T1 and T2 and T3 detections was quite long. Since, historically, the Indonesian LEI data shows that the detection of a T1 signal was almost always followed by T2 and T3, it is, therefore, quite safe to assume that each T1 detection can be considered as a trough in the business cycle.

All in all, we believe the current economic recovery is sustainable. And we maintain our forecast that the Indonesian economy is likely to continue picking up its growth pace for the rest of 2007. As such, we reiterate our forecast that the Indonesian economy will grow by 6.23% in 2007. The expansion is expected to continue in 2008, in which year the economy is expected to grow by 6.33%.

TABLE 3. FORECAST OF INDONESIAN ECONOMIC GROWTH

Sectors	2007F	2008F	Y-o-Y 2008F: % YoY				Q-o-Q 2008F: % QoQ			
			Q1	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**	**Q4**
1. Agriculture	2.4	3.8	4.6	2.9	4.1	3.4	19.2	2.6	7.9	-21.6
2. Mining and Quarrying	2.6	2.0	-1.5	3.2	4.7	1.5	-6.0	2.6	3.0	2.1
3. Manufacturing	5.8	6.4	7.0	6.1	6.1	6.5	0.4	1.1	4.0	0.9
4. Electricity, Gas, and Clean Water	8.1	8.4	7.3	8.4	9.5	8.3	0.0	3.8	4.0	0.3
5. Construction	9.1	8.5	9.0	8.5	8.9	7.5	-0.3	3.0	3.9	0.6
6. Trade, Hotel, and Restaurant	7.6	7.3	7.4	7.0	6.5	8.3	0.5	2.0	3.7	1.8
7. Transportation and Communication	12.6	12.8	16.7	11.0	11.4	12.4	2.1	2.4	3.9	3.4
8. Finance, Leasing, and Business Services	7.7	7.9	7.7	8.4	7.1	8.2	1.6	2.4	3.2	0.8
9. Services	6.0	4.9	3.8	5.8	5.8	4.3	0.3	2.5	1.7	-0.4
GROSS DOMESTIC PRODUCT	**6.2**	**6.3**	**6.4**	**6.2**	**6.3**	**6.4**	**2.2**	**2.1**	**4.1**	**-2.0**
1. Consumption Expenditures: Household	4.1	3.9	3.7	3.7	4.2	4.2	-0.7	0.9	2.4	1.7
2. Consumption Expenditures: Government	9.5	7.2	14.3	12.6	2.4	2.6	-30.8	21.3	-4.5	28.1
3. Gross Fixed Capital Formation	12.7	10.0	17.1	10.1	8.6	5.5	-2.5	3.1	3.6	1.3
4. Export of Goods and Services	8.9	9.3	9.4	9.1	9.6	9.0	0.1	2.4	4.8	1.4
5. Import of Goods and Services	8.2	8.7	9.3	8.5	7.4	9.7	-0.8	7.1	5.4	-2.0
6. Total Consumption	4.8	4.3	4.7	4.7	3.9	4.0	-5.3	3.1	1.5	4.9
7. Domestic Demand	6.7	5.8	7.8	6.1	5.2	4.4	-4.6	3.1	2.1	3.9

Source: Danareksa Research Institute (DRI)

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