Macro Economy

Global upswing

Global growth was at the lowest in 2016 since the global financial crisis at 3.2% YoY and is predicted to rise to 3.6% YoY in 2017 as the Euro Area, Russia, Japan, and emerging Asia recorded better than expected results in the first three quarters of 2017.

Stronger domestic demand in China and continued recovery in emerging economies supported this growth. Brazil had a strong export performance which helped the economy to return to positive growth in the first three quarters of 2017.

Growth in the first half was also supported by an increasing private consumption, investment and external demand in Japan and Euro Area. Recovery in the energy sector contributed to a better business investment in the United States.

Stable domestic economy

During the third quarter of 2017, GDP grew 5.06% YoY better than growth of the same period in 2016 of 5.01% YoY. It is predicted that GDP will expand by 5.1% YoY for the full year, an improvement from 2016 of 5.02% YoY.

Variable	2013	2014	2015	2016	9M2016	9M2017
GDP (IDR trillion)	9,084	10,095	11,541	12,407	9,251	10,096
GDP growth (%)	5.78	5.02	4.79	5.02	5.02	5.06
Inflation (%)	8.38	8.36	3.35	3.02	3.07	3.72
Export (USD billion)	182.55	175.98	150.37	145.19	105.11	123.36
Import (USD billion)	186.63	178.18	142.69	135.65	98.69	112.49
Trade balance (USD billion)	(4.08)	(2.20)	7.68	9.53	6.41	10.87
Current Account Deficit (%of GDP)	3.19	3.09	2.03	1.80	2.09	1.65

Robust economic growth is boosted by the strong export performance and investment. Export was sustained by rising commodity prices such as coal and crude palm oil and stronger global demand. As a result of stronger exports value and volume, the current account deficit decreased compared to the previous year at 1.65% of GDP. Investment increased strongly due to the continuous government infrastructure construction and non-structural investment such as investing in supplies and machineries.

Growth by Expenditure	2013	2014	2015	2016	9M2017	2017E	2018E
HH Consumption	5.3	5.1	5.0	5.0	4.9	5.1	5.1-5.2
Government Spending	4.9	2.0	5.4	(0.1)	3.5	4.6	3.8-4.0
Investment	4.7	4.1	5.1	4.5	7.1	5.4	6.0-6.6
Export	5.3	1.0	(2.0)	(1.7)	17.3	4.8	5.0-5.5
Import	1.2	2.2	(5.8)	(2.3)	15.1	3.9	4.4-4.8
	5.78	5.02	4.79	5.02	5.06	5.20	5.2-5.6

** based on APBNP 2017*
** based on OJK's forecast*

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2018 Outlook

The domestic economy is forecasted to grow in the **5.1 – 5.3%** range driven by domestic consumption. Inflation is projected within the **3.5± 1%** window. Current account deficit is expected to remain **below 3%** of GDP.

In the banking sector, loan growth is projected to be in the **9-11%** range, inline with the deposit growth.

Domestic Consumption

Consumption	Share (%)	3Q'16	2Q'17	3Q'17
F&B	39.01	5.23	5.24	5.04
Apparel, Footwear	3.49	2.24	3.47	2.00
Equipment	12.76	4.17	4.13	4.14
Health & Edu	6.73	5.36	5.33	5.38
Trans. Kom	23.33	6.08	5.34	5.86
Hotel Resto	9.99	5.01	5.86	5.52
Other	4.69	2.15	2.05	2.17

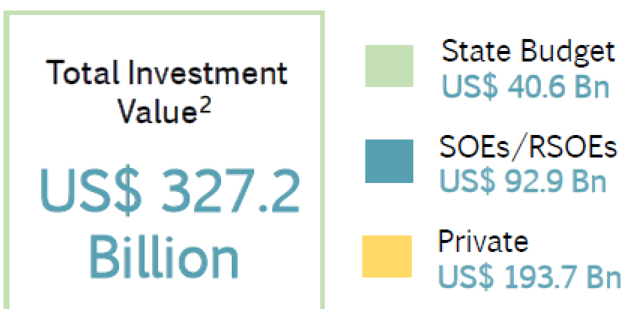
Domestic consumption was lower in 2017, however we expect this to be temporary as an adjustment from last year's increase in electricity tariffs, which is shown by modest decline in food and beverage consumption.

We also noticed that there were shifting in consumers' preference, where leisure industries (hotel, restaurants, transportations and communications) experienced a pick up trend.

Government Infrastructure Development

To accelerate economic growth, in five years the Government has 245 projects and 2 programs (35 GW Electricity Infrastructure and Small and Medium Airplane industry) listed as National Strategic Projects.

These projects and programs are spread across nationwide and covers 15 sectors which will approximately cost Rp4.4tn in investment.



As of 19th December 2017, 26 projects of Rp 73tn have been completed, 145 projects are under construction, 9 projects are in transaction, while 86 projects are still in the preparation phase.

Banking Industry

Slower loan growth, easing liquidity pressure

- Liquidity in the industry improved during the third quarter of 2017 at 88.74%. Loan grew at a slower pace of 7.86% in September 2017 compared to deposit which grew 11.69%.
- Banks were not very aggressive to disburse loans due to weak demand and therefore still focus on improving the loan quality. NPL at 2.93% showed a slight decrease compared to September last year at 3.1%.
- NIM decreased by 32 bps YoY to the level of 5.32%, as an adjustment toward lower benchmark (7 days repo) rate by 75bps YoY.

2018 Outlook

Better environment than 2017

GDP growth is projected to be stronger next year supported by:

- Improving export performance, as we expect better economic growth for Indonesia's trading partner.
- Increase in private investment, following increasing IPOs in 2017 which covers 35 companies raising proceeds of Rp9.03tn, and bond issuance of Rp251.4tn, or increased in outstanding bonds by Rp171.8tn from Rp478.1tn in Dec 2016 to Rp649.9tn in Dec 2017.
- Stable domestic consumption during political year.

Stable inflation is expected in 2018, thus with slightly improving GDP growth, we expect industry loan growth to slightly accelerate. Concerns on credit quality has eased as banks continued to show better performance on loan quality and big banks are predicted to have reached the peak of credit cost in 2017.

A likely FFR hike may cause temporary Rupiah depreciation, as we expect that the market have already been priced in. However, we do not expect further rate cut by Bank Indonesia, at least in the first semester of 2018.

Source: BPS, Bloomberg, IDX and Bank Indonesia

Strategy in 2018

Growth

Pushing Micro and Consumer

BRI plans to remain focus on growing the Micro and Consumer segments as these two are the biggest ROE contributors. In the micro segment, we still largely rely on KUR to support growth. Nevertheless, we want to maintain robust growth in commercial Kupedes, as we have seen 15% yoy growth in November 2017.

Ultimately, we are looking forward to see 13-15% yoy loan growth in Micro, with similar target in the commercial Kupedes alone. With this kind of growth, we expect that KUR proportion to total micro to be maintained below 30%.

Digital Banking Plan

Developing the "Faster" value for our customer

We expect 2018 will be interesting year for digital banking business as we have witnessed several strong fintechs acquiring financial players.

In order to remain competitive, we need to be faster, better and cheaper. Thus, we plan to implement new initiatives, especially to generate faster turn-around-time loan processing for our customers in the Micro and Consumer segments.

NIM

Lower NIM in 2017 mostly mechanical

During 2017, we changed the components of NIM. Previously, we exclude deposit insurance (Lembaga Penjamin Simpanan) fee and KUR insurance premium (to Askrindo and Jamrkindo) in the NIM calculation. However since 2017, we added deposit insurance fee into interest expense, and we deducted interest income by the amount of insurance premium. Hence NII and NIM are lower, but PPOP remained intact.

Going forward to 2018, we expect that NIM will be slightly lower due to compression on the loan yield, as competitions on salary loan are getting stronger.

Operating Efficiency

Improving efficiencies without losing the human touch with our BRILink agents

In 2018, we plan to remain robust on BRILink agents acquisition by developing BRILInk Mobile platform, hence, agents may use their own smartphone to provide banking services. This initiatives also part of our effort to accelerate the acceptance and growth of transactions in mobile platform.

Provisioning Policy

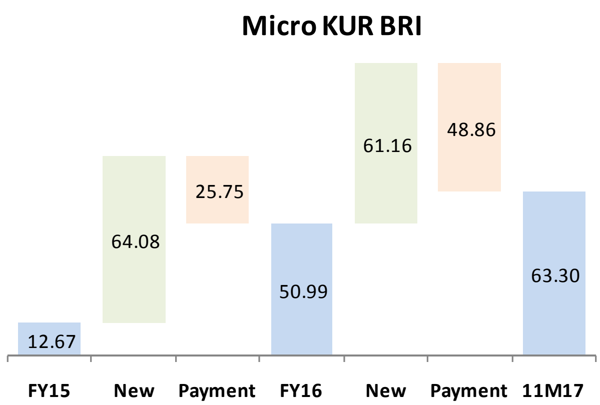
Maintain reserves for Loan at Risk

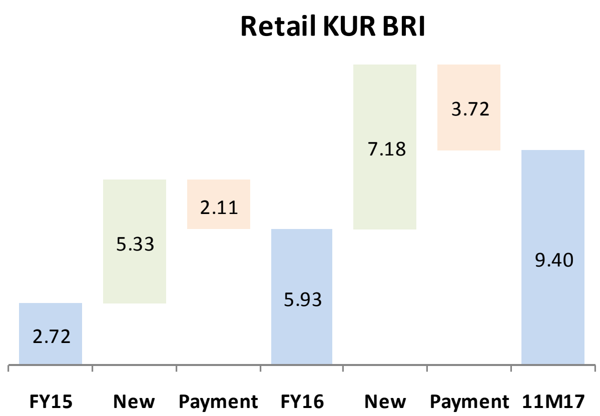
With current trend on Loan at Risk, we expect that the peak of credit cycle already behind us. Hence, we are relatively comfortable with current provisioning coverage of above 40% to Loan at Risk. With such assumptions, we expect credit cost to be lower in 2018.

KUR Update

High repayments ratio in 2017 lead to stable proportion to Micro loan

Until November 2017, BRI have disbursed KUR amounted to Rp 68.3tn or 96.3% of 2017 target to 3.7mio borrowers. However, KUR loan outstanding only grew by Rp 15.8tn, showing that most of the growth comes from existing borrowers maturing in 2017. Hence, proportion of KUR increased from 24% in Dec 2016 to 26.8% in Nov 2017.





KUR Sustainability

Changes in external and internal conditions

KUR is the most massive government program for micro, and small entrepreneurs. However, we acknowledge some concerns on KUR, especially comparing to the previous government program, which ended-up unsuccessful.

Looking at major improvements that have happened both internally and externally, we are quite optimistic that the KUR program will be better than other government subsidized loan program.

These improvements include:

- Banks have the freedom to select borrowers
- BRI's GCG and Risk Management standards, especially loan underwriting in Micro has improved significantly. Every loan is being assessed based on 5Cs.
- BRI imposed NPL ratio as part of loan officers' KPI.
- Central Bank provides credit bureau data
- Government requires banks who disburse KUR to have NPL below 5%.

KUR 2018: Lower rate by 2% is compensated by an increase in subsidy by 1%

Based on the press release from Coordinating Ministry for Economic Affairs on 8th December, 2017, KUR 2018 features will include:

- Lower interest rate for borrowers to 7% from 9% in 2017
- Higher subsidy by 1% (Micro KUR: 10.5%, Retail KUR: 5.5%)
- Increase in disbursement target from 110tn in 2017 to Rp120tn in 2018
- Increase in productive sector (non-trading) target from 40% to 50% of total disbursement.

KUR 2018: Impact to NIM and profitability

With such pricing structure, we expect an overall impact of lower interest income of 400bio (assuming target of disbursement increased from 71.2tn in 2017 to 80tn in 2018). This number will be translated into both lower NIM and ROA by approximately 4bps.