Automotive Financing Industry in the Medium Term Remains Positive; The Impact of Down Payment Regulatory is Limited

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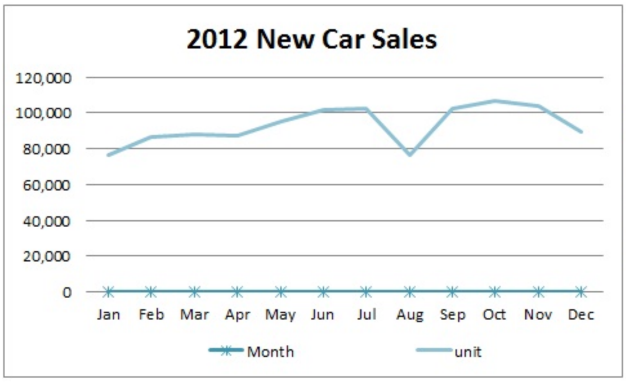
PEFINDO views that the policy of minimum down payment (DP) is expected to have a limited impact on the Indonesian vehicle financing industry in the medium to long term, especially in the segment of car financing. Although the finance industry will face further challenges in the form of equalization minimum DP rules of sharia to conventional financing, fiduciary rules and the possible increase in fuel and electricity basic tariff (TDL), we view that the car financing segment will still be able to record a positive growth in 2013. However, motorcycle financing segment, in our opinion, will continue to experience a contraction until the first half of 2013 as compared to the same period last year. Finance companies in our portfolio which focus only on motorcycle financing, such as FIF and Summit Oto Finance might be further affected by the new policy depends on what action will be taken by the company to address this situation. However, we have not yet taken a rating action on those companies. In the long run, we expect the minimum DP policy will improve the industry's asset quality profile so that the finance industry will be more healthy and profitable.

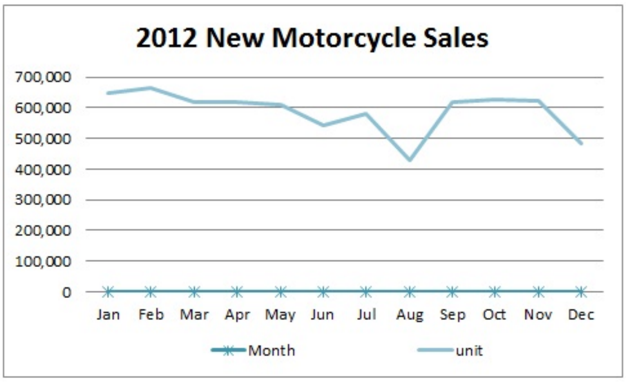
The expansion of the motor vehicle industry is supported by steady economic growth in the range of 6-7% per year, growing middle class population thereby increasing the purchasing power, and also low interest rates to support the sale of motor vehicles on credit. The number of people categorized as "middle class" segment in Indonesia has grown by 8 million to 9 million annually. They are regarded as the consumer class that has become a target market for various industrial sectors. With a stable national economic condition, consumer credit segment in the national banking system is able to grow in the range of 19% - 22% year on year (yoy) growth in 2012. However, the policy of fuel subsidy restrictions that may be implemented in 2013 is likely to be one of the factors inhibiting sales of motor vehicles, primarily cars. The increase in fuel prices will boost inflation and ultimately increase the level of interest rates. The increase in electricity rates that are expected to happen in the 2013 is also a limiting factor as it will increase production costs of automotive industry.

The new regulations announced by the central bank, Bank Indonesia (BI) with Circular Letter No. 14/10/DPNP and by Capital Market and Financial Institution Supervisory Agency (Bapepam-LK) with the Finance Minister Decree No. 43/PMK.010/2012 related to minimum down payment for motor vehicles has contributed to the decline in vehicle sales in August 2012. As shown in the two graphs below, the lower demand generally has affected the finance company's ability to finance new booking in the period, particularly in the motorcycle financing.

Graph 1:



Graph 2:



Source: Gaikindo and AISI

As a result of the minimum DP requirement, motorcycle sales fell by 12% year-on-year (yoy) in 2012 from 8 million units in the previous year. Finance companies, such as PT Federal International Finance (FIF) that focuses only on motorcycle financing has experienced deep contraction of its new booking up to 30% in that year. On the other hand, companies which have cars and motorcycles financing in their portfolios including PT Adira Dinamika Multifinance, PT Indomobil Finance Indonesia and PT BFI Finance Indonesia are less affected, while the ones that focus solely on car financing, such as PT BCA Finance and PT Astra Sedaya Finance were even able to enjoy a thin positive growth of their new booking. Pefindo estimates that the contraction in the motorcycle market to continue in 2013. The government imposed the same policy of minimum down payment in both conventional and sharia financing segments at the end of 2012, which is likely to weaken further the sales of motorcycle in the near term. Currently, sharia credit accounts for about 75% of the total motorcycle loans.

Nevertheless, the middle class segment, in our view, is unlikely to be affected by the new regulation. Unlike the lower income segment, the middle income group is less dependent on credit financing for motor vehicles. Currently, about 70 percent of motorcycle purchases are made on credit. Out of USD4.8 billion or equivalent to around IDR46.6 trillion investment in the automotive sector during the year 2012, about USD2.3 billion or nearly 48% is allocated for the car assembly industry. Around USD2.0 billion have been invested for the automotive components (auto parts) industry, which is mainly car components, and only a small portion disbursed for the motorcycle industry. Pefindo views that the motorcycle sector is likely to remain under pressure given the lack of additional production capacity in that segment.

We project that car sales are expected to grow moderately in the range of 5% - 10% in 2013 supported by higher production capacity of factories owned by sole agent (ATPM). The growth of this industry is highly dependent on a number of factors, such as the readiness of the infrastructure, government policies, tax incentives and incentives for research and development, as well as ease in obtaining raw materials such as steel, aluminum, rubber and plastic. The multi-purpose vehicle (MPV) is projected to be the engine of growth in the next year car sales. The government policy to encourage environmentally friendly cheap car or low cost green car (LCGC) will shift the use of motorcycles to switch to the use of low-cost cars. This policy will not impose taxes on luxury goods for cheap car that will provide incentives for companies that sell LCGC. The rising of commodity prices will be a factor inhibiting growth of car sales in addition to the threat of the weakening exchange rate of the rupiah against the U.S. dollar.

Overall, we view that the automotive financing industry is still positive in 2013 and will be able to record at least the same level of new financing as in 2012. Car financing will be the driver of industry performance in addition to the used vehicles financing either two-wheel or four-wheel. The recent regulations regarding auto financing minimum down payment implemented since mid-June 2012 has led to a decrease in the motorcycle market, but less affecting the car market. The automotive industry and automotive financing sector have proven to have ability to withstand economic shocks, such as rising fuel prices in 2005 and the tightening of liquidity in the year 2008 to 2009. The long term demand for motor vehicles will still be high in line with poor transport facilities. The finance companies, in our view, will find a solution to mitigate the decrease in volume due to higher down payment. We consider that the industry will likely to benefit from the policy in which the regulation will raise the finance companies' asset profile along with the increasing portion of high DP in their financing portfolios.

in IDR billion

BALANCE SHEET	2011		2012									
	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct
Financing Receivables:	**241,911**	**245,298**	**261,067**	**263,071**	**267,778**	**273,189**	**282,820**	**283,743**	**290,348**	**294,010**	**297,238**	**298,414**
a. Leasing	75,320	76,592	91,145	91,313	93,150	96,039	102,100	101,504	104,470	106,101	107,503	106,989
Growth	*5.31%*	*1.69%*	*19.00%*	*0.18%*	*2.01%*	*3.10%*	*6.31%*	*-0.58%*	*2.92%*	*1.56%*	*1.32%*	*-0.48%*
b. Factoring	3,447	3,915	3,876	3,817	3,893	3,992	3,901	3,993	4,048	4,139	4,075	4,076
Growth	*11.34%*	*13.58%*	*-1.00%*	*-1.52%*	*1.99%*	*2.54%*	*-2.28%*	*2.36%*	*1.38%*	*2.25%*	*-1.55%*	*0.02%*
c. Consumer Financing	163,144	164,791	166,046	167,941	170,735	173,158	176,819	178,246	181,830	183,770	185,660	187,349
Growth	*1.04%*	*1.01%*	*0.76%*	*1.14%*	*1.66%*	*1.42%*	*2.11%*	*0.81%*	*2.01%*	*1.07%*	*1.03%*	*0.91%*

Source: APPI or IFSA

Despite our view on limited impact of the regulation of minimum down payment to consumer financing industry risk profile in overall, PEFINDO will closely monitor further development within the automotive and consumer financing sectors, particularly consumer financing companies within our portfolio. We will monitor the performance of finance companies that focus primarily on motorcycle financing to see the impact of the regulation on its risk profile. We believe impact to each consumer financing company will be different depending on their business characteristics, and necessary rating action will be taken if we believe that the impact may substantially weaken the companies' credit risk profiles.