

Omnibus Law and Impact Construction Industry

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On October 5, 2020, the Indonesian government and the House of Representatives (Dewan Perwakilan Rakyat) passed the Job Creation Law (Omnibus law) intended to simplify 79 laws consisting of 1,244 articles related to investment in Indonesia. PEFINDO is of the view that the implementation of Omnibus Law will significantly affect many industries, construction among others. PEFINDO views the impact of the Omnibus Law to the construction industry is through speeding up land acquisition process and the establishment of a sovereign wealth fund (SWF), which will help mitigate risks in the industry's growth and stability as well as its financial profile.

Based on the Omnibus Law chapter VIII, the government accelerates land acquisition process through three regulations, namely: acceleration of land acquisition process; acceleration of land compensation process; and procurement of landbank for national development. Land acquisition process will be accelerated in terms of approval process, through a clause stating that entitled party and/or users of state/regional property is deemed to have approved the development plan if they do not attend the public discussion after having been invited three times. The process of land compensation will also be expedited through the implementation of the Omnibus Law, as compensation fund will be deposited with the district court if the entitled party refuses the stipulated form and amount of the compensation. The Omnibus Law also regulates about the provision on land bank agency to carry out planning, procurement management, acquisition, utilization, and distribution of land. The agency will ensure the availability of land for infrastructure purposes and prevent cost overrun of the project by speeding up land acquisition process. Previously, 40% of national projects had been stalled due to land acquisition problem, according to the Committee for Acceleration of Priority Infrastructure Delivery (KPPIP). The slow progress leads to contractor companies' revenues falling short of their targets. The Omnibus Law, contains, inter alia, regulations addressing land acquisition problems which will facilitate contractor companies to meet their revenue targets. Therefore, the implementation of the Omnibus Law is expected to accelerate land acquisition and alleviate risks in the construction industry. Speedier process of land acquisitions from the government will provide more certainty for contractor companies in terms of achieve targeted revenue and margin from the project. In line with the more sustainable business growth, the financial risk of construction companies is also expected to lessen, as contractors can meet their revenue targets with greater certainty, hence improving their capital structure and cash flow protection.

In accordance with the Job Creation law chapter X part 1, paragraph 2 articles 165-172, the Indonesian government plans to establish a sovereign wealth fund (SWF) under the name of Lembaga Pengelola Investasi (LPI). LPI is an organization with the objective to finance infrastructure projects, increase and optimize assets value in the long term. Its statute provides the minimum initial capital from the government of IDR 15 trillion in the form of cash. Furthermore, LPI will be provided with IDR75 trillion capital from the government with the expectation to attract investors up to three times from the government's shares or around IDR225 trillion. It is expected that LPI will provide alternative fund for financing infrastructure projects in Indonesia. LPI will generate positives contribution to state-owned construction companies, especially for those holding infrastructure concessions and its cash flow is generated from asset liquidation, by selling its shares in special purpose vehicle (SPV). LPI can be a solution, as it can acquire those SPV shares, hence easing the construction company's balance sheet. Without LPI, the construction company will find it difficult to liquidate its asset with the right price, particularly if the asset is still in the early operation phase with limited cash flow generation. The longer it holds the asset, the heavier the balance sheet burden. In addition, another type of state-owned construction company that focuses its operation on construction works will also derive benefit from LPI by working in a project purchased by LPI. The company will get certainty for payment from the projects, as the payment is sourced from cash settlement from transaction with LPI. For both types of construction company, LPI contributes to alleviate risk in financial profile. It strengthens the cash flow of construction company of which its business model is recycled asset with invest-build-divest and gets certainty for the source of payment for a construction company focusing on construction work.

Despite the potential positive impact from the Omnibus Law and the establishment of LPI, PEFINDO maintains the view that the construction industry risk profile is regarded as moderately high with a stable outlook. Furthermore, we view that most construction companies are heavily impacted by the pandemic, as the government reallocate its infrastructure budget in 2020 for the abatement of the pandemic by reducing infrastructure budget from IDR423.4 trillion to IDR281.1 trillion in 2020. Accordingly, delays in the government project tender from 2020 to 2021 is inevitable, resulting in lower new contract achievement in the first nine months of 2020 (9M2020) compared to the previous year. In addition, the pandemic has reduced the operational activities of construction companies, mainly attributable to delays in the progress of the project and payment due to social distancing policy resulting in lower revenue in 9M2020 compared to the same period in the previous year. We expect a potential recovery in the industry, with the increasing infrastructure budget for fiscal year 2021 by 48.6% to IDR417.7 trillion and the vaccination program starting in early 2021 as the contributing factors. As of December 31, 2020, PEFINDO rated five state-owned contractors including PT Pembangunan Perumahan (Persero) Tbk (PTPP, *id*A+/Negative), PT Wijaya Karya (Persero) Tbk (WIKA, *id*A/Stable), PT Hutama Karya (Persero) (PTHK, *id*A/Negative), PT Adhi Karya (Persero) Tbk (ADHI, *id*A-/Negative), PT Waskita Karya (Persero) Tbk (WSKT, *id*BBB/Stable). Among those contractors, PTPP has the highest rating due to more conservative financial leverage and stronger cash flow protection measures compared to its peers.

Information	PTPP		WIKA		WSKT		ADHI	
	9M2020	9M2019	9M2020	9M2019	9M2020	9M2019	9M2020	9M2019
Revenue (IDR Bn)	10,236.83	16,214.84	10,726.02	18,883.38	11,833.56	22,206.77	8,539.91	9,152.92
EBITDA (IDR Bn)	1,276.44	2,036.10	994.86	2,732.21	724.08	4,040.31	796.75	1,180.53
Debt to EBITDA (x)	11.51	6.09	17.44	5.97	71.54	15.44	8.99	7.06
DER (x)	1.51	1.02	1.47	1.19	3.17	3.05	1.71	1.70
FFO to Debt (%)	3.2%	8.1%	(0.6)%	9.0%	(3.9)%	2.4%	0.0%	5.1%
EBITDA to IFCCI (x)	2.01	3.99	1.04	3.21	0.24	1.56	1.25	2.16
New Contract (IDR Tn)	11.8	22.03	6.8	25.7	12.2	15	6.2	7.6

Sources: various financial statements and sources

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