



## **Australian Government**

National Interest Statement:

Loan Agreement between the Australian Government and  
the Government of Indonesia

NOVEMBER 2020

## **NATIONAL INTEREST STATEMENT**

### **Loan Agreement between the Australian Government and the Government of Indonesia for a bilateral loan of A\$1.5 billion**

#### **Summary**

This document is a national interest statement for the recent bilateral loan agreement between the Australian Government and the Government of Indonesia for A\$1.5 billion, signed on 12 November 2020. The national interest statement is tabled in compliance with the requirements of the *International Monetary Agreements Act 1947 (Cth)* (IMA Act).

On 12 November 2020, Australia entered into a loan agreement with Indonesia to provide A\$1.5 billion. This agreement is part of a multilateral action to support Indonesia led by the Asian Development Bank (ADB) and including the Asian Infrastructure Investment Bank (AIIB), the Japan International Cooperation Agency (JICA) and the German state-owned development bank (KfW).

This loan is designed to support Indonesia's COVID-19 response financing task. COVID-19 has precipitated a health and humanitarian crisis in Indonesia, threatening economic prosperity. The economic impacts of COVID-19 are being felt. Indonesia experienced the first year on year contraction since the Asian Financial crisis in the second quarter of 2020. The economy contracted 5.3 per cent through the year to the June quarter marking the first contraction since the 1997-98 Asian Financial Crisis. Following its response to COVID-19, the fiscal deficit is forecast to widen from 2.2 per cent in 2019 to 6.3 per cent in 2020.

Escalation of the health crisis will further undermine the economic and fiscal position. While the Indonesian Government is responding to the crisis through increased expenditure and has taken steps to manage fiscal pressures, further assistance is required. Indonesia's ability to raise revenue quickly is constrained, given its narrow tax base and financial market conditions mean that raising capital is expensive.

The funds will be used to support Indonesia's COVID-19 response, including social protection initiatives and health system development. Indonesia's response has expanded social protections for the most vulnerable and strengthened the health system.

It is in Australia's interest, as we have in the past, to offer direct support to Indonesia during challenging times. An economically strong Indonesia is critical to the recovery and prosperity of Australia and the rest of the region.

The Australian Government previously provided standby loans to Indonesia in both 2008 (US\$1 billion) and again between 2013 and 2015 (A\$1 billion). While neither loan was taken up, their existence provided confidence to markets, which assisted Indonesia to access international capital. Providing this loan to Indonesia enhances Australia's diplomatic and economic interests, through strengthening the important relationship between the two countries, and by supporting the economic stability of Indonesia and the region.

## **Legislative requirements**

This National Interest Statement relating to the Loan Agreement was tabled pursuant to the requirements of sections 8CA-8F of the IMA Act. The IMA Act requires the Treasurer to table a statement as soon as practicable after entering into such an agreement, indicating the reasons why the loan agreement is in Australia's national interest, along with a description of its nature and terms.

The IMA Act also prescribes that Australia can enter into an agreement for a loan that provides financial assistance in support of ADB programs to another country if: the ADB requests Australia's assistance; and the Treasurer is satisfied that at least one other government or organisation will be providing similar assistance.

These requirements have been fulfilled. The ADB has formally requested Australia's participation in support of its US\$1.5 billion countercyclical support facility loan under the COVID-19 pandemic response option (CPRO) for the COVID-19 Active Response and Expenditure Support Program (CARES), approved by the ADB board of Directors on 23 April 2020. The AIIB, JICA and KfW have also announced similar lending arrangements in support of this program to the value of US\$750 million, US\$480 million and EUR250 million respectively.

## **National Interest Assessment**

It is in Australia's interest, as we have in the past, to offer direct support to Indonesia during challenging times. An economically strong Indonesia is critical to the recovery and future prosperity of Australia and the region.

Australia's bilateral relationship with Indonesia is based on important political, economic, strategic and social connections. The Australian Government's continued support through this bilateral loan will strengthen this relationship with the Indonesian Government. It will also help promote the long-term economic prosperity of Indonesia and the region, which will in turn benefit Australia. Providing this loan will assist Indonesia in its health response and economic recovery from COVID-19.

Australia has previously provided support to Indonesia through two standby loan facilities. The first was established in 2008 and the second was in place between 2013 and 2015. While neither of these standby loan facilities were drawn down, they were considered by Indonesia to have played a role in boosting market confidence in Indonesia's economic prospects.

Australia has significant trade and investment links to Indonesia, which is the largest economy in Southeast Asia and 16th largest economy in the world. In 2019, two-way trade (goods and services) totalled approximately A\$17.7 billion, making it Australia's 13th largest bilateral trading relationship, while two-way investment in 2019 totalled A\$9 billion. Indonesia is expected to experience continued strong growth over the medium term. The entry into effect of the Indonesian-Australia Comprehensive Economic Partnership Agreement (IA-CEPA) on 5 July 2020 and the soon to be concluded Regional Comprehensive Economic Partnership (RCEP) negotiations will support and develop the trade and investment relationship in the years ahead.

## **Nature and terms of the Loan Agreement**

On 12 November 2020, the Treasurer announced that Australia would provide a bilateral loan of A\$1.5 billion to Indonesia, to provide timely support to the Government of Indonesia's public expenditure and fiscal management for urgent public health measures and for the expansion of social and economic assistance.

The subsequent Loan Agreement was entered into by the Australian Government and the Government of Indonesia on 12 November 2020. The availability of the loan for drawdown by Indonesia will be up and until 12 May 2021. The availability period reflects the Indonesia Government's careful cash flow management. Indonesia is working hard to constrain interest costs from the multiple bilateral loans they are receiving, with varying rates of conditionality. The Loan Agreement ensures additional flexibility so that the Indonesian Government can draw down on our loan in one instalment anytime within six months of the date of agreement.

In line with our Cabinet negotiation mandate, the interest rate is fixed to match the yield on 10-year Australian Government Securities (AGS) as at the date of drawdown by the Indonesian Government, with an additional 0.5 per cent margin to cover administrative costs associated with the loan. Instalments on the loan principal and interest are repayable over fifteen years every six months in Australian Dollars. The loan will have an A\$9.996 million impact on the Underlying Cash Balance from 2020-21 to 2023-24.

The 10-year bond is the Australian Office of Financial Management (AOFM) target weighted average term to maturity across all bond lines. It serves as the best reflection of the Government's cost of borrowing. It is also consistent with the approach undertaken for setting the base rate for other loans and concessional lending arrangements with state and territory governments. It is a simple and transparent option for approximating Australia's cost of borrowing, and avoids the administrative burden of periodically resetting the interest rate as would be the case for a variable rate.

The interest rate is scheduled for review 10 years after drawdown, at which time the rate can be modified if it no longer aligns with the Australian Government's cost of borrowing. This will ensure Australia's underlying cash balance will not be negatively impacted as a result of the loan being drawn down.

Stakeholder consultation committees under the ADB CARES Program, members of which include Australian representatives, will meet quarterly to monitor the Government of Indonesia's overall COVID-19 response measures. Indonesia will report ongoing progress of managing COVID-19 and mitigating the economic and social damage from the outbreak.