

MILLIMAN RESEARCH REPORT

Employee benefit obligations of Indonesian LQ45 companies

An analysis of employee benefit obligations in financial statements published in 2017 by companies included on the Indonesia Stock Exchange LQ45 Index

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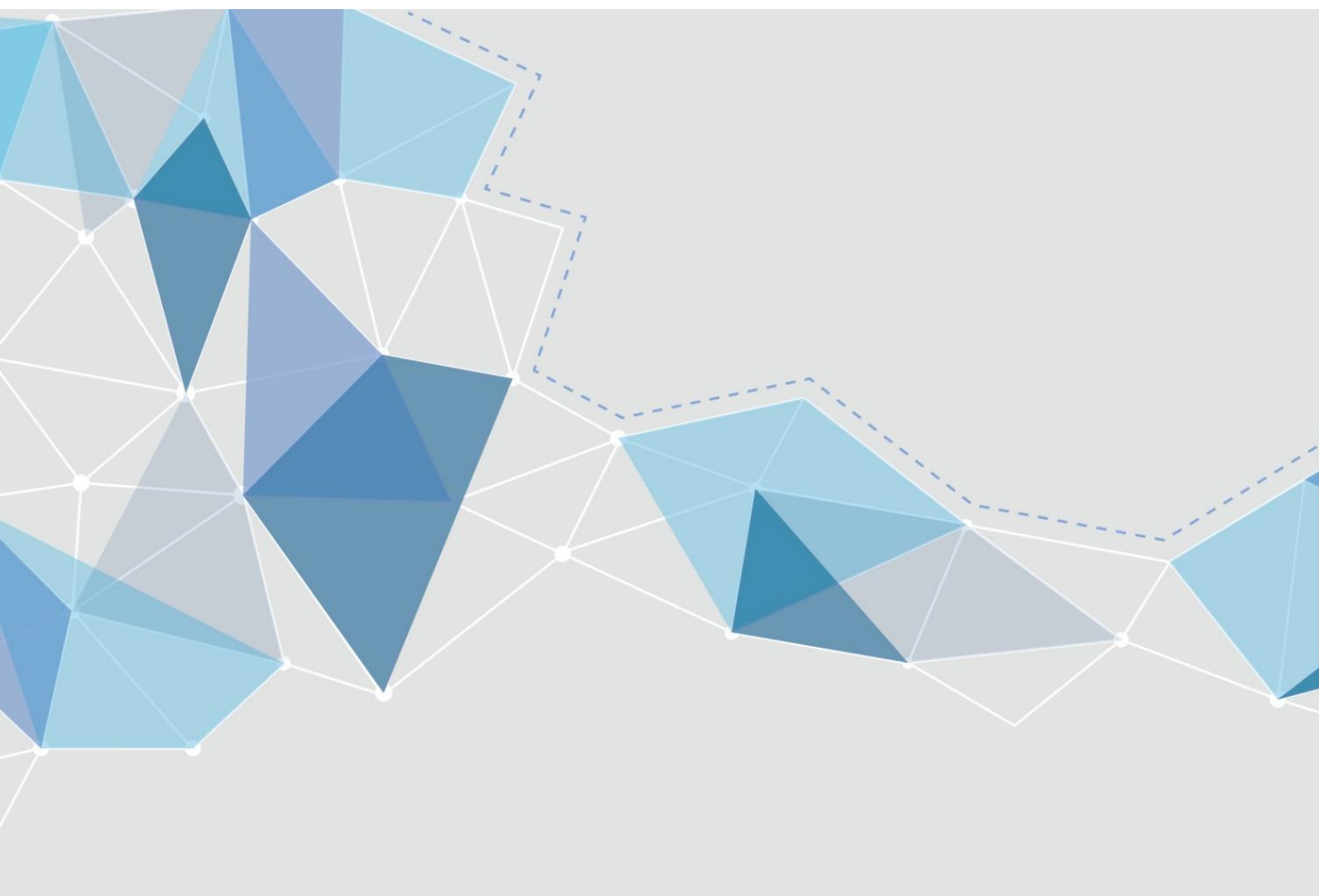




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Scope of review

With over 300 clients in Indonesia, Milliman conducts continual and extensive research on issues related to the employee benefits offered by companies there.

This report presents Milliman's 2017 analysis of employee benefit obligations based on the financial statements published by companies included on the Indonesia Stock Exchange LQ45 Index. The LQ45 Index represents the 45 companies with the largest market capitalisation and most significant trading volumes on the Indonesia Stock Exchange. This is Milliman's second annual review of employee benefit obligations in Indonesia.

As required by Indonesia Statement of Financial Accounting Standard No. 24 (PSAK24), all companies in Indonesia should report their liabilities in respect of their post-employment and other long-term employee benefit plans in accordance with the standard. This study considers the balance sheet liabilities and profit or loss costs in respect of employee benefits presented in the 2016 year-end statements, and looks at changes since the previous year. It also reviews the key assumptions disclosed in deriving the liabilities and costs.

The main aim of this study is to create awareness about the state of employer-sponsored long-term employee benefit programs and to foster a dialogue amongst policy makers, employers, employees and the public about the future of such plans in Indonesia.

The companies included in the LQ45 Index are reviewed every six months. The constituents of the LQ45 Index considered in this study are those included in the index during the period August 2017 to February 2018, as set out below:

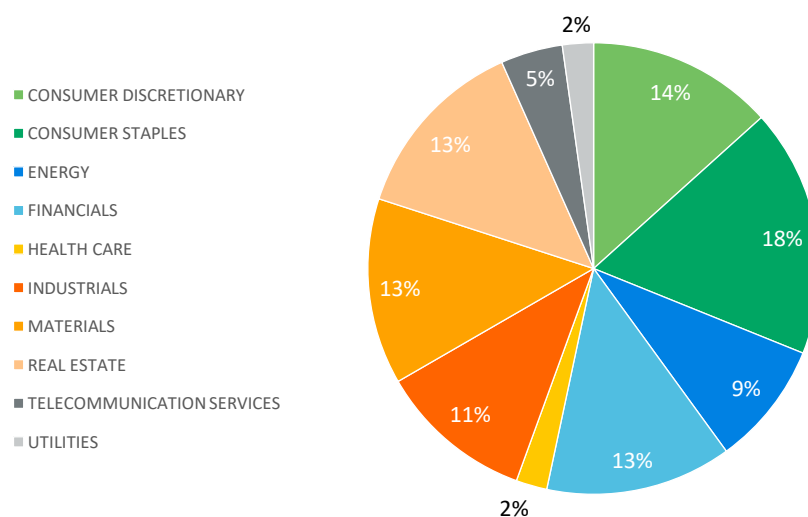
FIGURE 1: COMPANIES AND THEIR SECTORS INCLUDED IN THE LQ45 INDEX

COMPANY NAME	SECTOR
ADARO ENERGY TBK.	ENERGY
ADHI KARYA (PERSERO) TBK.	INDUSTRIALS
AKR CORPORINDO TBK.	MATERIALS
ANEKA TAMBANG PERSERO (PERSERO) TBK.	MATERIALS
ASTRA AGRO LESTARI TBK.	CONSUMER STAPLES
ASTRA INTERNATIONAL TBK.	CONSUMER DISCRETIONARY
BANK CENTRAL ASIA TBK.	FINANCIALS
BANK MANDIRI (PERSERO) TBK.	FINANCIALS
BANK NEGARA INDONESIA (PERSERO) TBK.	FINANCIALS
BANK RAKYAT INDONESIA (PERSERO) TBK.	FINANCIALS
BANK TABUNGAN NEGARA (PERSERO) TBK.	FINANCIALS
BARITO PACIFIC TBK.	MATERIALS
BPD JAWA BARAT DAN BANTEN TBK.	FINANCIALS
BUMI RESOURCES TBK.	ENERGY
BUMI SERPONG DAMAI TBK.	REAL ESTATE
GLOBAL MEDIACOM TBK.	CONSUMER DISCRETIONARY
GUDANG GARAM TBK.	CONSUMER STAPLES
HM SAMPOERNA TBK.	CONSUMER STAPLES
HANSON INTERNATIONAL TBK.	REAL ESTATE
INDOCEMENT TUNGGAL PRAKASA TBK.	MATERIALS
INDOFOOD CBP SUKSES MAKMUR TBK.	CONSUMER STAPLES
INDOFOOD SUKSES MAKMUR TBK.	CONSUMER STAPLES
JASA MARGA (PERSERO) TBK.	INDUSTRIALS
KALBE FARMA TBK.	HEALTH CARE
LIPPO KARAWACI TBK.	REAL ESTATE

FIGURE 1: COMPANIES AND THEIR SECTORS INCLUDED IN THE LQ45 INDEX (CONTINUED)

COMPANY NAME	SECTOR
MATAHARI DEPARTMENT STORE TBK.	CONSUMER DISCRETIONARY
MEDIA NUSANTARA CITRA TBK.	CONSUMER DISCRETIONARY
PAKUWON JATI TBK.	REAL ESTATE
PERUSAHAAN GAS NEGARA (PERSERO) TBK.	UTILITIES
PP (PERSERO) TBK.	INDUSTRIALS
PP LONDON SUMATRA INDONESIA TBK.	CONSUMER STAPLES
PP PROPERTI TBK.	REAL ESTATE
TAMBANG BATU BARA BUKIT ASAM TBK.	ENERGY
SAWIT SUMBERMAS SARANA TBK.	CONSUMER STAPLES
SEMEN INDONESIA (PERSERO) TBK.	MATERIALS
SRI REJEKI ISMAN TBK.	CONSUMER DISCRETIONARY
SUMMARECON AGUNG TBK.	REAL ESTATE
SURYA CITRA MEDIA TBK.	CONSUMER DISCRETIONARY
TELEKOMUNIKASI INDONESIA (PERSERO) TBK.	TELECOMMUNICATION SERVICES
UNILEVER INDONESIA TBK.	CONSUMER STAPLES
UNITED TRACTORS TBK.	ENERGY
VALE INDONESIA TBK.	MATERIALS
WASKITA KARYA (PERSERO) TBK.	INDUSTRIALS
WIJAYA KARYA (PERSERO) TBK.	INDUSTRIALS
XL AXIATA TBK.	TELECOMMUNICATION SERVICES

FIGURE 2: COMPANIES BY INDUSTRY



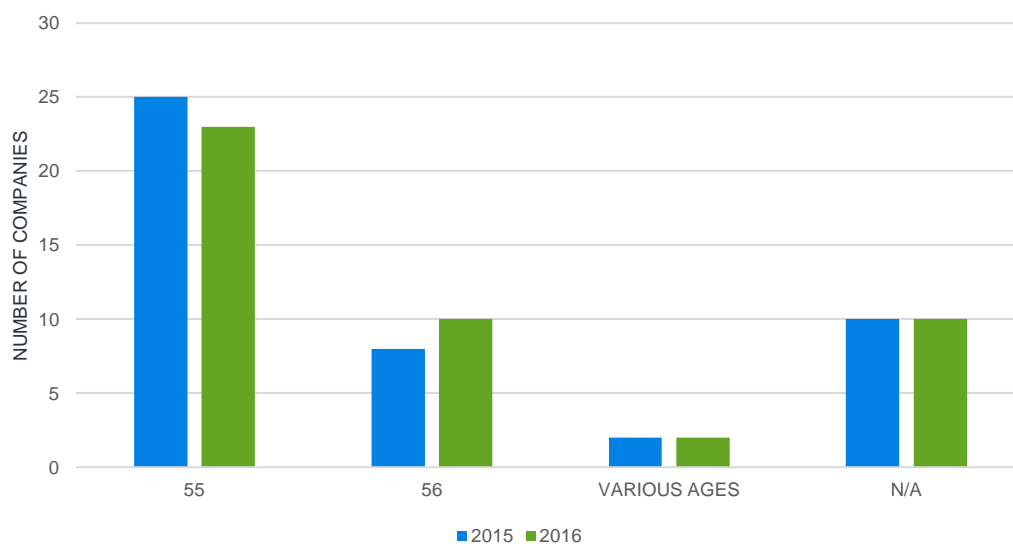
Disclosure information on employee benefits has been extracted from companies' published annual reports as at 31 December 2016. Where annual reports were in respect of group companies, reference has only been made to the obligations relating to the main company, rather than considering the consolidated disclosures for the combined undertakings of the company and its subsidiaries. Corresponding information for 2015 has been extracted from companies' published annual reports as at 31 December 2015.

Normal retirement age

In Indonesia, normal retirement age should be defined in a company's internal policies. Typically it is specified in a company's regulations, collective labour agreements or employment contracts.

In line with typical company practice in Indonesia, most companies defined normal retirement age as age 55 at the end of 2016. Of the 35 companies that disclosed their retirement ages, 23 companies (66%) set normal retirement age at 55, whilst 10 companies (28%) set it at age 56. Two companies (6%) set a range of normal retirement ages depending on the category of employee. Ten companies did not disclose their normal retirement ages.

FIGURE 3: NORMAL RETIREMENT AGE



Two companies changed their normal retirement ages during 2016 from 55 to 56 years. This reflects alignment with the age under the revised social security system (BPJS Ketenagakerjaan), which came into effect in 2015. Increases in retirement age are planned under BPJS Ketenagakerjaan in the future, to move the retirement age for social security benefits to age 65 by 2043. It is therefore anticipated that normal retirement ages for companies in Indonesia will also increase over time.

Post-employment and other long-term employee benefits

All companies in Indonesia must provide post-employment benefits as regulated under Labour Law no.13/2003 (LL13). LL13 provides for benefits on retirement, death, disability or involuntary termination. The benefits depend on service, with a maximum of 32.2 times monthly wages after 24 years' service.

Some companies also offer pension plans which are either defined benefit (DB) or defined contribution (DC) in nature. The pension plan proceeds relating to company contributions are typically used to fund the mandatory LL13 obligation at retirement either in full or in part. Of the 45 companies included in the LQ45 Index, 42 companies (93%) provide a pension plan—of these, 14 companies (33%) provide a DB plan and 28 companies (67%) provide a DC plan.

Apart from the mandatory LL13 benefit and pension plans, some companies also provide other post-employment benefits such as post-retirement healthcare benefits and paid leave for retirement preparation (Masa Persiapan Pensiun or MPP). Five companies (11%) provided post-retirement healthcare benefits and two companies (4%) provided MPP.

There were 17 companies (38%) that offered other long-term benefits such as long service awards or long service leave.

Defined benefit obligations at year-end 2016

WHAT IS A DEFINED BENEFIT OBLIGATION?

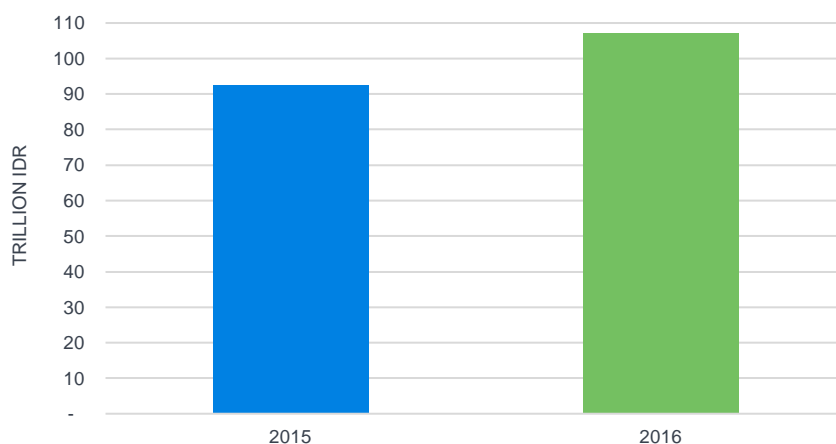
The defined benefit obligation (DBO) for an employee benefit scheme is the present value of all benefits under that scheme attributed to service completed by employees up to the balance sheet date.

The PSAK24 accounting standard prescribes that the Projected Unit Credit cost method is used to evaluate the DBO. Under this method, a projected accrued benefit is calculated based on employees' service up to the balance sheet date, but where the benefit payable is based on levels of future salary, using assumptions about the growth in salaries up to the point when an employee is entitled to benefits under the arrangement.

HIGHER OBLIGATIONS FOR EMPLOYEE BENEFITS RECORDED AT YEAR-END 2016

From year-end 2015 to year-end 2016, the aggregate DBO for employee benefits (combining post-employment and other long-term employee benefits) amongst LQ45 companies increased by 16%, from approximately IDR 92.5 trillion to approximately IDR 107.1 trillion.

FIGURE 4: DEFINED BENEFIT OBLIGATION



Changes in the DBO relating to a benefit scheme can be attributed to the following factors:

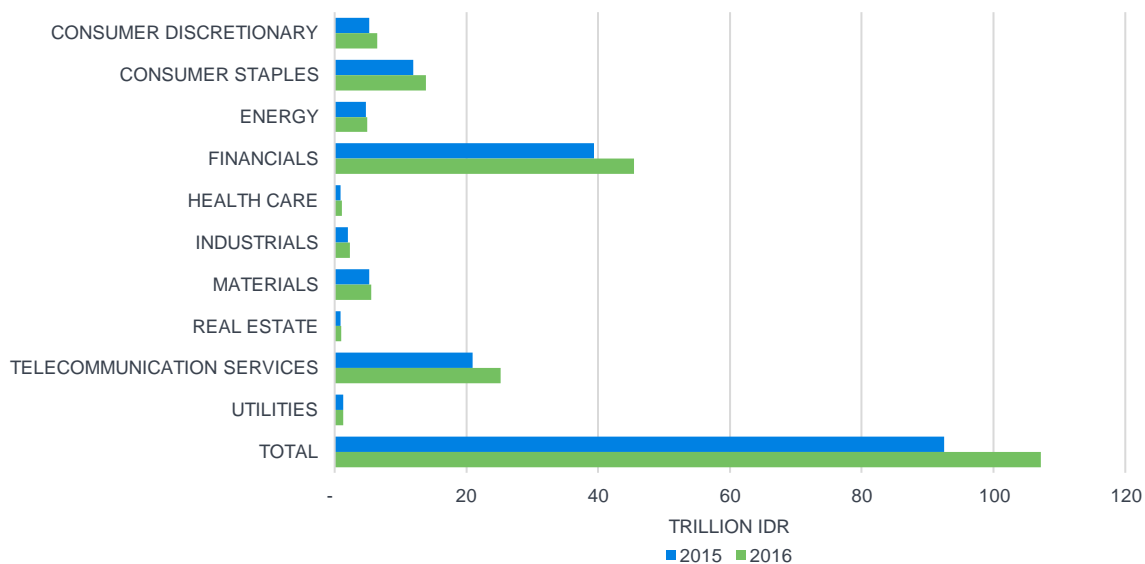
- Accrual of an additional year of service by members of the scheme
- Ageing of the scheme population (so that benefits are one year closer to expected payment)
- Experience of the scheme relative to the actuarial assumptions used in the calculation of the DBO (such as salary increases being higher or lower than assumed)
- Changes in the assumptions used to value the liabilities.

As discussed later, median discount rates were 0.5% per annum (pa) lower at year-end 2016 compared to year-end 2015. This would have contributed towards some of the increase in the aggregate DBO.

MOVEMENT IN OBLIGATIONS BY INDUSTRY SECTOR

The movement in the DBO between year-end 2015 and year-end 2016 varied by company and by industry sector. By sector, the biggest absolute increase was approximately IDR 6.1 trillion in the financials sector. The biggest change in relative terms was in the consumer discretionary sector, with a rise of around 24% from approximately IDR 5.3 trillion to approximately IDR 6.4 trillion. There was a small reduction in the utilities sector.

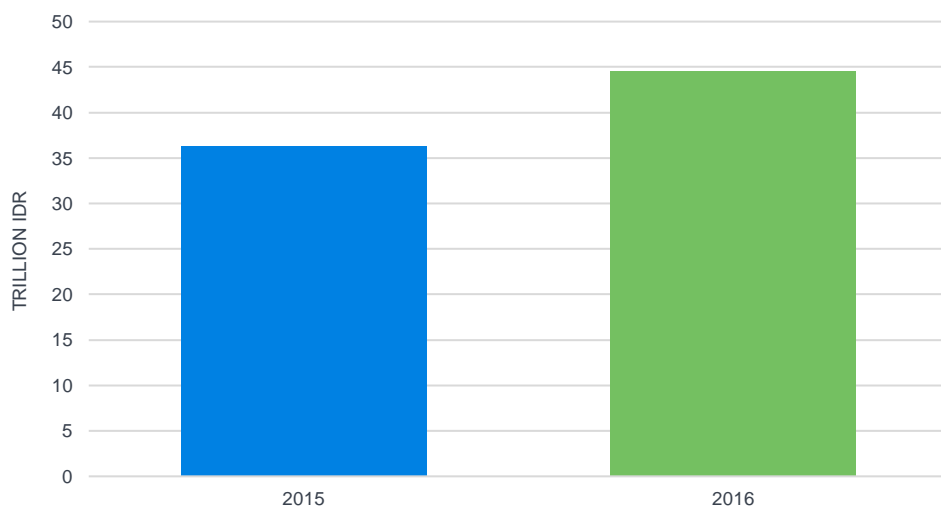
FIGURE 5: DBO BY INDUSTRY SECTOR



MOVEMENTS IN NET LIABILITY

In aggregate the LQ45 companies registered an increase of IDR 8.2 trillion in their net liability (which nets off the DBO by attributable scheme assets). Between year-end 2015 and year-end 2016, the aggregate net liability rose by 23%, from approximately IDR 36.3 trillion to approximately IDR 44.5 trillion.

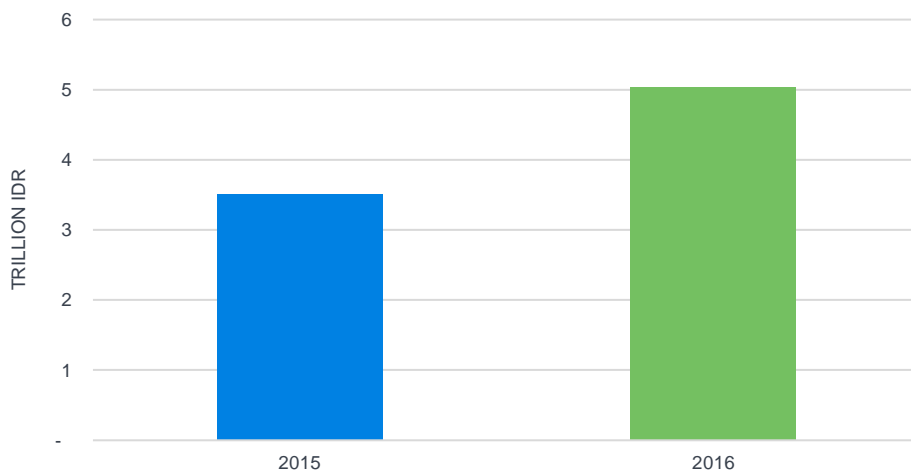
FIGURE 6: NET OBLIGATION (DBO LESS SCHEME ASSETS)



HIGHER OBLIGATIONS FOR OTHER LONG-TERM EMPLOYEE BENEFITS AT YEAR-END 2016

For those companies that disclosed obligations for other long-term employee benefits, there was an overall increase in obligations from the prior year. From 2015 to 2016, their aggregate obligations rose by 44%, from approximately IDR 3.5 trillion to approximately IDR 5 trillion.

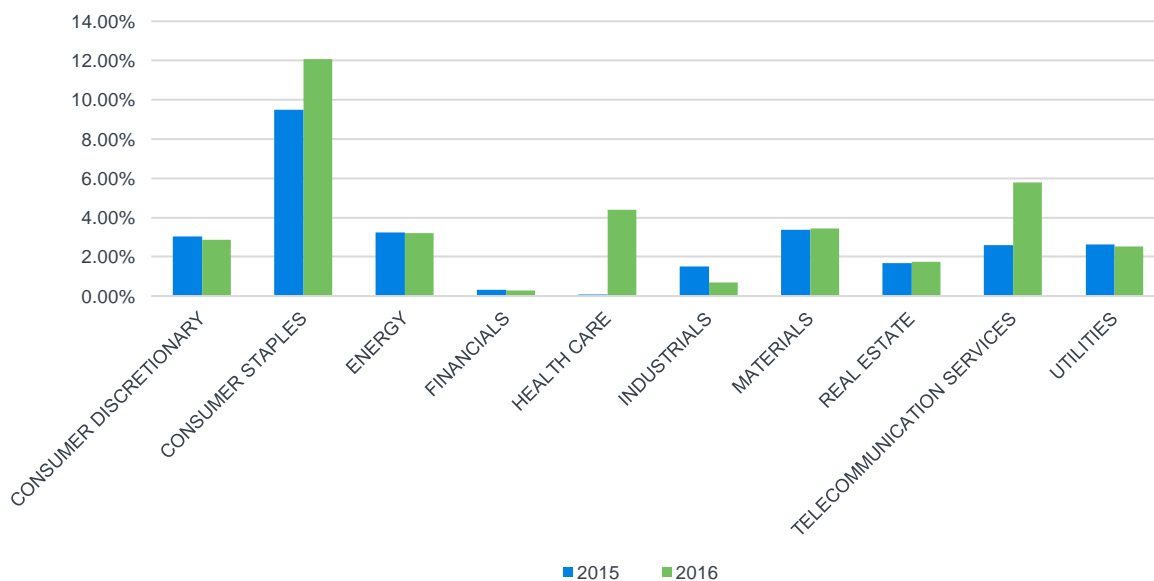
FIGURE 7: OTHER LONG-TERM BENEFIT LIABILITIES



RATIO OF EMPLOYEE BENEFIT LIABILITIES TO TOTAL LIABILITIES

Typically the net liabilities for employee benefits represented less than 5% of the total balance sheet liabilities of the LQ45 companies. The exception however was the consumer staples sector, which saw employee benefit obligations make up some 12% of the total balance sheet liabilities. This may be reflective of the relatively generous retirement and other long-term benefits offered by companies in this sector.

FIGURE 8: RATIO OF TOTAL EMPLOYEE BENEFIT LIABILITIES TO TOTAL LIABILITIES



Costs in profit or loss in 2016

WHAT IS THE COST IN PROFIT OR LOSS?

The cost recognised in profit or loss for an employee benefit scheme is made up of a number of components. The two key items are the service cost and net interest or income. The service cost includes the current service cost, which reflects the accrual of an additional year of benefits in the scheme, as well as any past service cost or settlement gains or losses arising from changes to the scheme or scheme membership during the year. The net interest or income reflects the application of the discount rate on the net balance sheet liability adjusted for cash flows during the year.

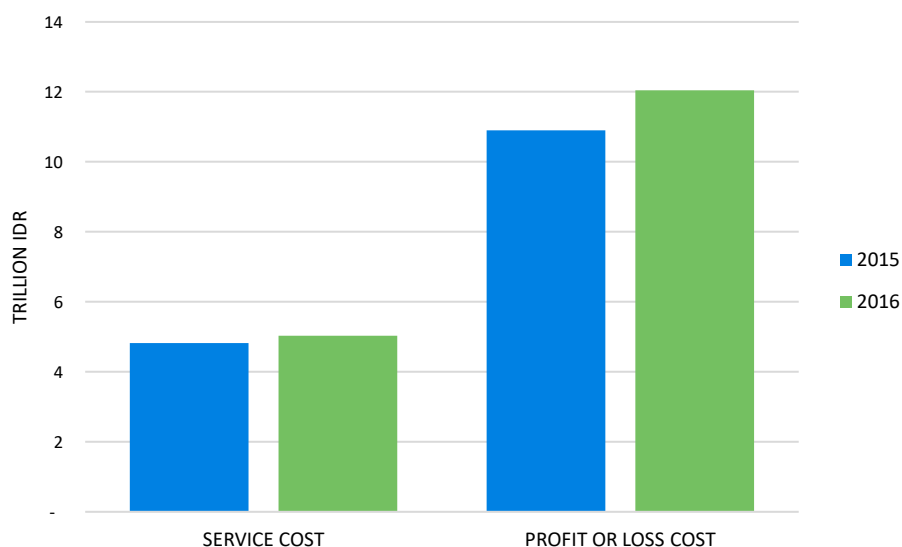
For other long-term employee benefits, any actuarial gains or losses arising at the balance sheet date are also recognised immediately in the profit or loss cost.

Not all companies disclosed the profit or loss cost explicitly. In these cases, inference was made about the cost from other disclosure items in the accounts.

HIGHER COSTS FOR EMPLOYEE BENEFITS RECOGNISED IN PROFIT OR LOSS IN 2016

Considering the two main elements of the profit or loss cost—service cost and net interest or income—LQ45 companies registered an increase in their profit or loss costs from the prior year. Between 2015 and 2016, the aggregate cost for employee benefits (combining both post-employment and other long-term employee benefits) increased by around 11%, from approximately IDR 10.8 trillion to approximately IDR 12.0 trillion. Within these figures, the aggregate service cost recorded in 2016 was approximately IDR 5 trillion, compared to IDR 4.8 trillion in 2015, an increase of around 4%.

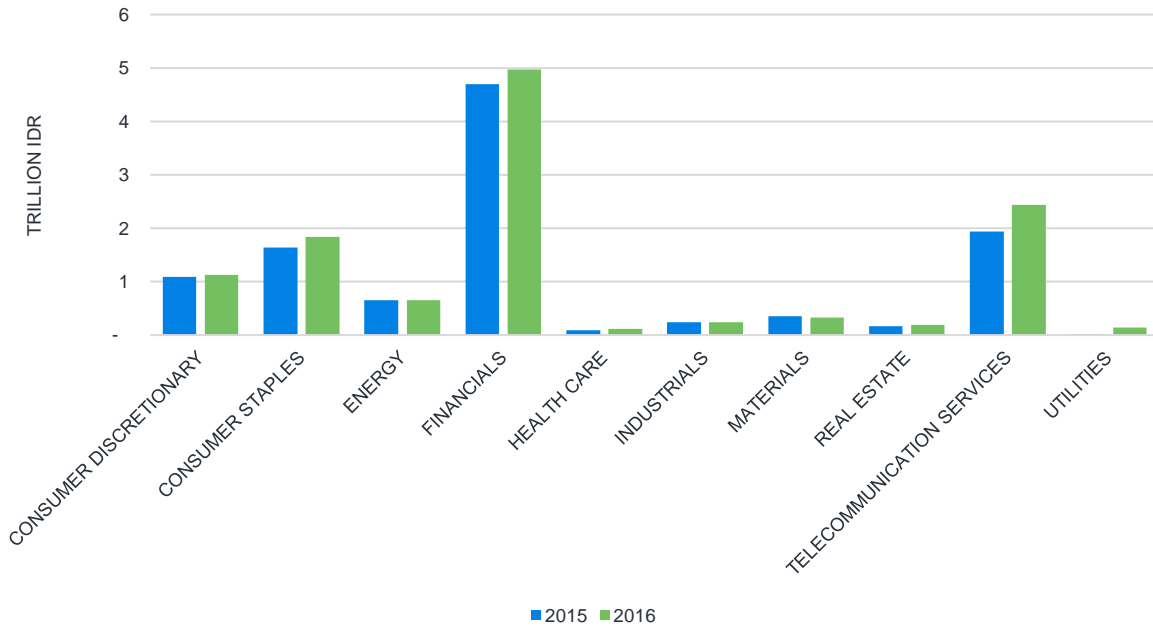
FIGURE 9: SERVICE COST AND PROFIT OR LOSS COST



MOVEMENTS IN PROFIT OR LOSS COST BY INDUSTRY SECTOR

All industry sectors saw an increase in their profit or loss costs between 2015 and 2016 with the exception of the materials sector, which saw a slight decline. The most significant increases in percentage terms were in the telecommunication services and utilities sectors.

FIGURE 10: COST IN PROFIT OR LOSS BY INDUSTRY SECTOR



Actuarial assumptions as at year-end 2016

BASIS FOR ACTUARIAL ASSUMPTIONS

In estimating employee benefit obligations and costs, companies must make certain assumptions regarding the future experience of the benefit scheme. These assumptions should reflect a company's best estimate of future experience. The assumptions that usually have the biggest impact on the calculations are:

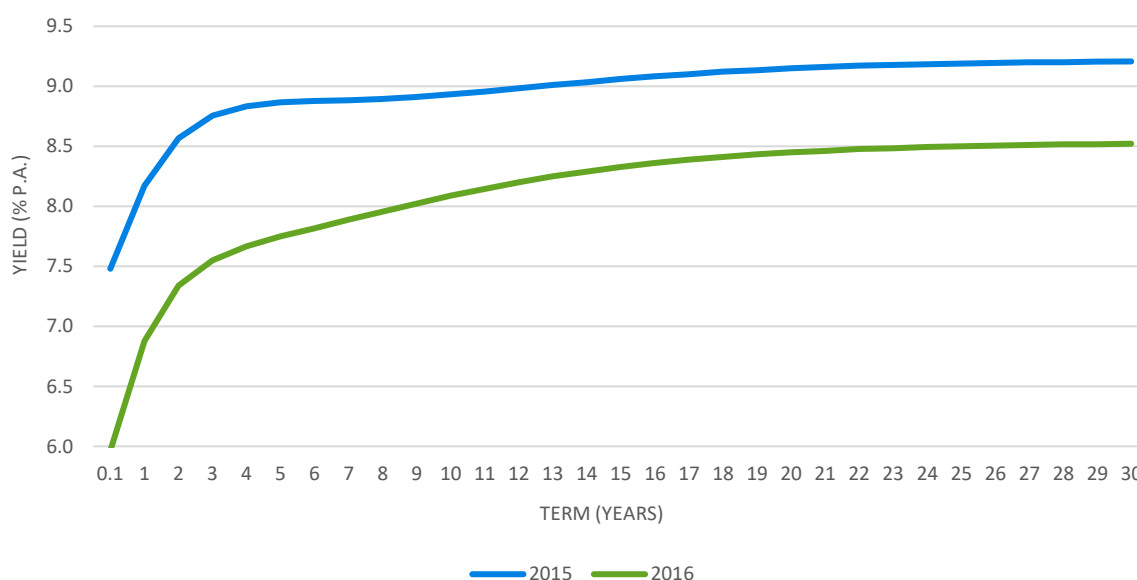
- Discount rate
- Future salary increases
- Employee turnover rates
- Mortality rates.

SELECTION OF THE DISCOUNT RATE

In Indonesia, the primary reference point for setting the discount rate is the yield on Indonesian government bonds. The rate chosen should reflect the notional yield at the balance sheet date on a bond with the same duration as the weighted average expected future working lifetime of the employees covered by the benefit scheme.

Figure 11 shows the yield curves on Indonesian government bonds as at the end of 2015 and 2016.

FIGURE 11: INDONESIA GOVERNMENT BONDS AT THE END OF 2015 AND 2016



Source: [<http://www.ibpa.co.id/>]

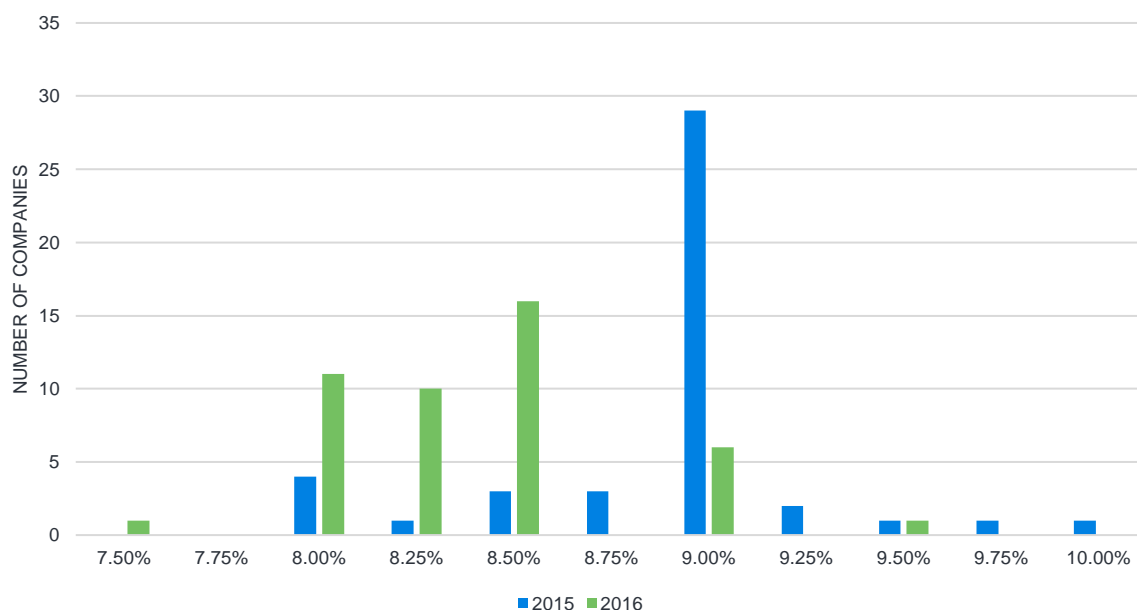
There was reduction in bond yields across the durations between the end of 2015 and 2016—from around 1.5% at very short durations to around 0.7% at the longer terms. A lower discount rate results in a higher benefit obligation.

DISCOUNT RATES FELL AT YEAR-END 2016

Many of the companies stated a range of discount rates for 2016, typically because different discount rates were selected for different benefit schemes and the results were sometimes presented on a consolidated basis.

Taking the representative discount rate to be the midpoint of the specified range, there was a reduction in discount rates between year-end 2015 and 2016 for 35 companies (78%) and an increase in discount rates for four companies (9%), with the remainder (13%) unchanged. Overall, the median discount rate fell by 0.5% pa, from 9.0% pa in 2015 to 8.5% pa in 2016.

FIGURE 12: DISCOUNT RATE



Discount rates at year-end 2016 ranged between 7.5% pa and 9.5% pa. Whilst a spread of discount rates would be expected as a result of differences in the profiles of the liabilities and resulting different durations, some of the variance also arises as a result of the different approaches that are taken to setting the discount rate.

The Indonesian government bond yield curve shown in Figure 11 is a coupon yield curve. Some companies in Indonesia reference these yields directly when setting the discount rate. Other companies reference spot yields (i.e., yields imputed on a zero-coupon bond) in line with the duration of the liabilities. Alternatively, some companies take a more complex approach, where the projected cash flows in each year are discounted at the reference spot yield for that particular year.

Applying a single spot rate approach for a long-term liability with a duration of more than 20 years (where the coupon bond yield was 8.5% pa at year-end 2016) would result in a discount rate of around 9% pa.

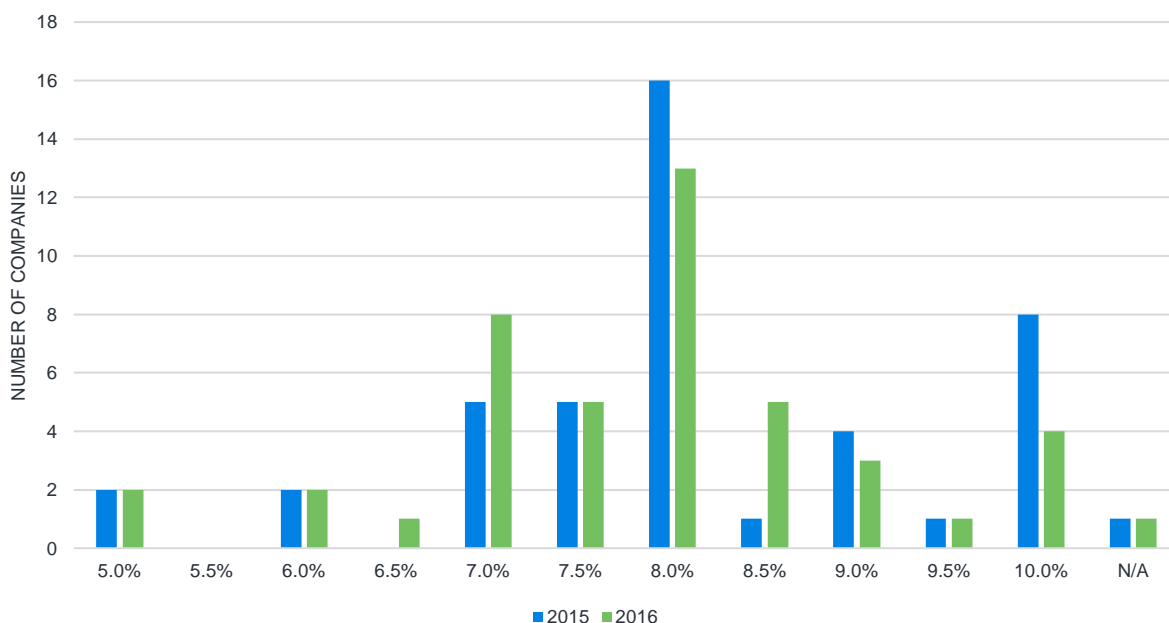
Variation could also arise depending on what date the company used to determine the discount rate. In order to ensure that the actuarial calculations are completed in time for the closing of a company's accounts, discount rates are sometimes referenced at a date within the last three months of the year. The yield curve at the longer terms varied by around 1% pa over the last few months of 2016.

EXPECTED SALARY INCREASES REMAINED UNCHANGED AT YEAR-END 2016

In measuring the obligation for a benefit that depends on an employee’s salary when the employee leaves the company, an assumption is made about the expected long-term rates of increase in employees’ salaries.

In the same way as the discount rate, some companies disclosed a range of salary increases for 2016. Taking the representative salary increase assumption as the midpoint of the specified range, there was a rise in the salary increase assumption between 2015 and 2016 for three companies (7%), a fall in the salary increase assumption for 14 companies (31%), and the remainder (62%) were unchanged. Overall, the median salary increase assumption was 8.0% pa at year-end 2015 and 2016.

FIGURE 13: SALARY INCREASES



TURNOVER RATES AT YEAR-END 2016

Employee turnover rates can have a significant impact on the liabilities and costs in respect of long-term employee benefits. This is particularly true for the LL13 benefit, under which no benefit is payable on voluntary resignation. Very few LQ45 companies disclose the turnover assumption used however.

Disclosure of this assumption should be encouraged given its impact on the results and that the purpose of such disclosures is to enable readers of a company’s accounts to form a view as to the reasonableness of the liabilities booked by the company.

MORTALITY RATES AT YEAR-END 2016

The majority of the LQ45 companies used mortality rate table TMI III (2011), the most recent insured lives table available in Indonesia. However, there were still a few companies making reference to US tables such as CSO 1980, CSO 1958, and GAM 1971.

Whilst this assumption is less significant in the valuation of the statutory LL13 benefit, which provides for benefits to be paid in lump sum form, it is significant for pension plans that provide lifetime annuities and for self-funded post-retirement healthcare benefits.

About this study

2017 MILLIMAN REVIEW OF INDONESIAN EMPLOYEE BENEFIT OBLIGATIONS

This study considers the 45 companies featured in the LQ45 Index during the period August 2017 to February 2018.

The results of this study are based on the employee benefit accounting information disclosed in companies' annual reports for the 2015 and 2016 fiscal years as reported under Indonesia Statement of Financial Accounting Standard No. 24.

This is Milliman's second annual review of employee benefit obligations in Indonesia.



Milliman is among the world's largest providers of actuarial and related products and services. The firm has consulting practices in life insurance and financial services, property & casualty insurance, healthcare, and employee benefits. Founded in 1947, Milliman is an independent firm with offices in major cities around the globe.

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