

BI Policy:

A balancing act

Keely Julia Hasim
Economist/Analyst

Barra Kukuh Mamia
Senior Economist

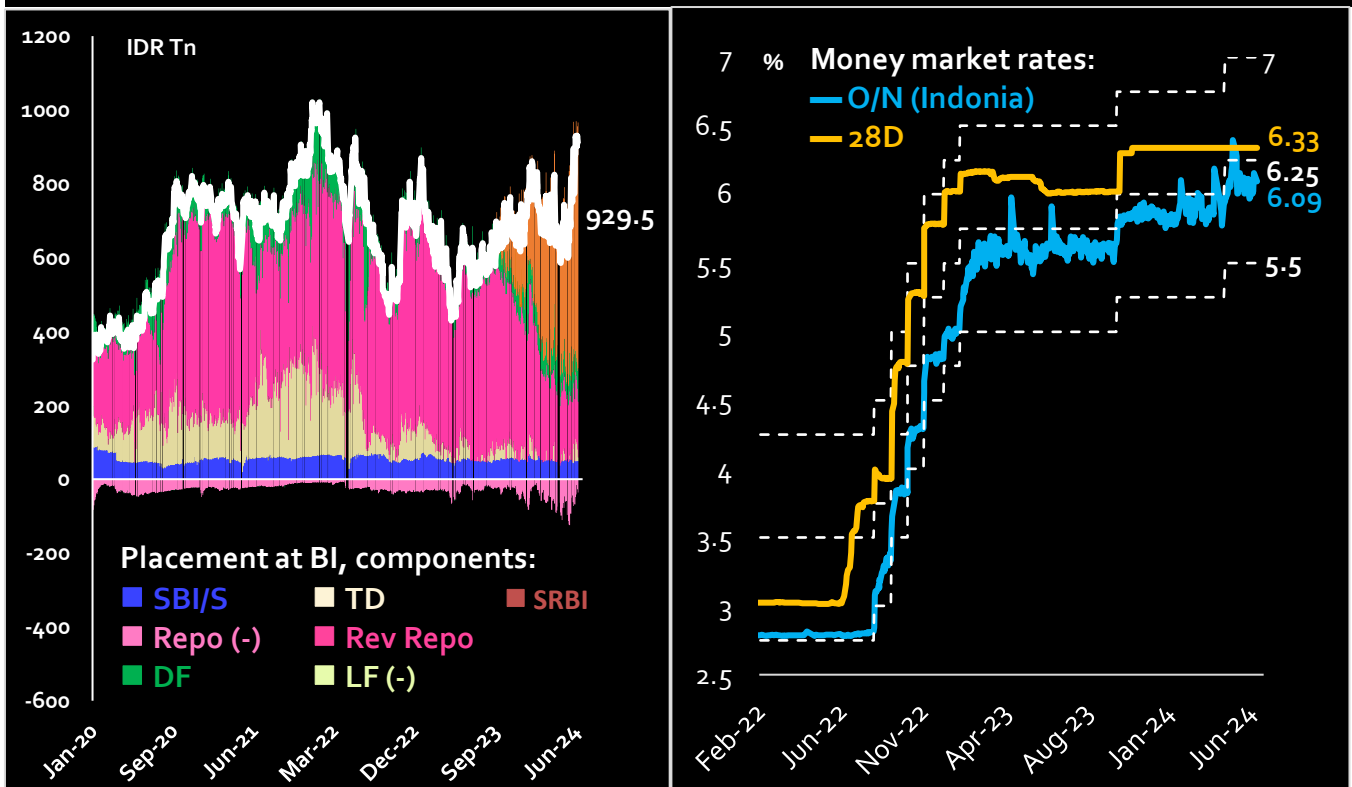
20 June 2024

Executive Summary

- BI has kept the BI7DRR at 6.25% in its latest meeting, despite significant depreciation of the IDR throughout the month.
 - The depreciation of IDR is driven by worsening sentiment of foreign investors towards Indonesia, as seen from the continued foreign outflows from the stock market.
 - Due to the increasing FX risks, BI has issued the Rasio Pendanaan Luar Negeri (RPLN) policy for banks, which indirectly helps keep import from the real sector under control.
 - BI still has room to increase interest rates by 25 bps this year, but the timing of the hike is difficult to predict.
- Bank Indonesia (BI) decided to maintain its benchmark policy rate (BI7DRR) at 6.25% in its latest meeting, following a significant depreciation of the Rupiah throughout the month. This depreciation is not surprising given the continued foreign outflows from the stock market in June (USD 131.2 million MTD).
 - Despite being hailed as a growth haven last year, foreign investors are becoming increasingly pessimistic about Indonesia's short-term outlook, with several high-profile foreign banks downgrading their ratings for the Indonesian market due to concerns over credit risks, weaker demand, and generally slowing growth. Additionally, dividend distributions by some publicly listed companies in June have further driven capital outflows from Indonesia.
 - Meanwhile, FX inflows from trade are likely declining, especially since there are indications that China's inventory of coal, nickel, and copper is starting to exceed industrial needs. On the flip side, Indonesia's imports will likely increase in the coming months due to the new government ruling to loosen import restrictions, allowing cheap goods from China to enter more freely into Indonesia. The relatively limited upside for Indonesia's trade surplus also suggests that domestic liquidity would likely be more constricted in the short-term.
 - The increasing FX risks have led BI to introduce a new policy (RPLN) to limit banks' short-term external debt to a maximum of 30% of their total capital, effective from August 1, 2024. Additionally, BI has imposed stricter requirements for banks with regards to managing foreign funding. This policy will likely have limited short-term impact, as the total external debt of banks was still relatively low at around 10% as of Q1-24. But it's important to note that the real issue with banks' external debt lies in the domestic demand for FX from the private sector and SOEs. Since banks merely cater to this demand, this policy could limit FX borrowing from the real sector and indirectly help keep imports under control.

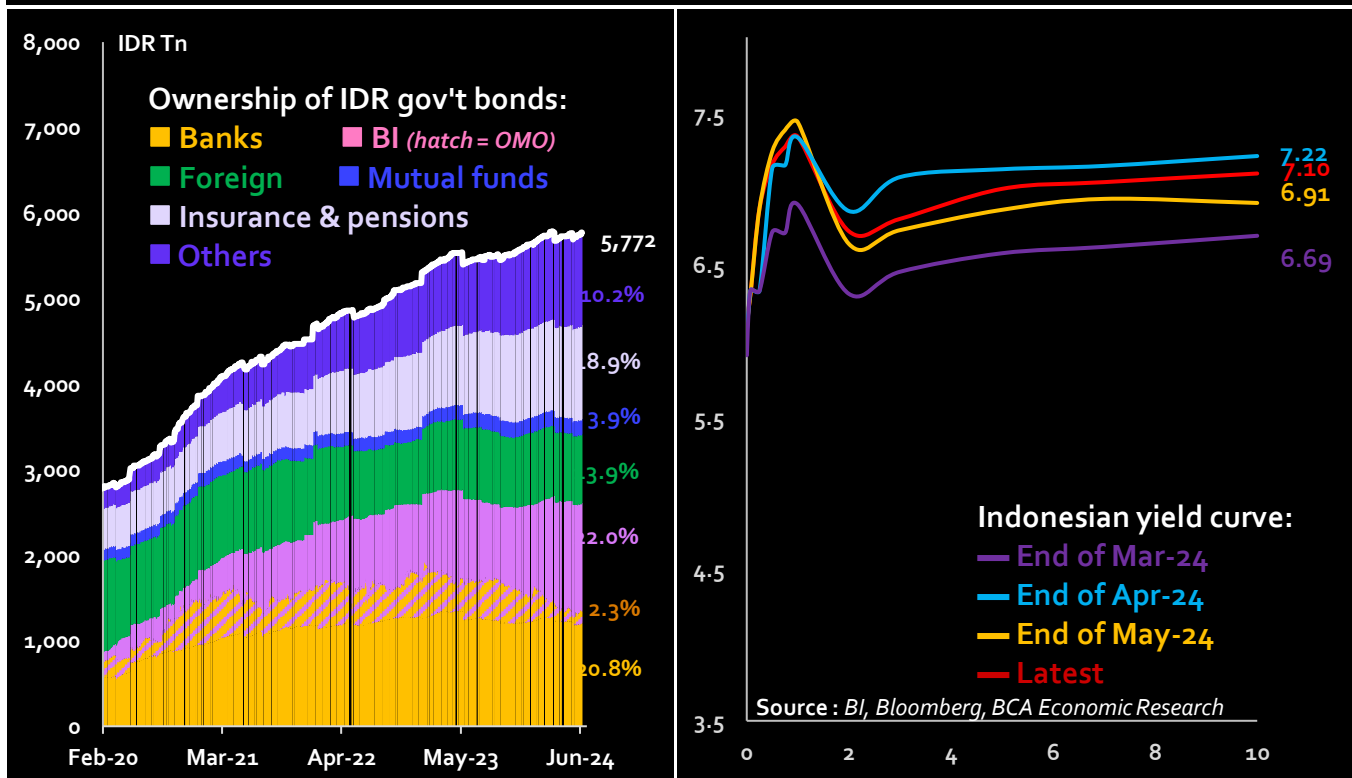
- Despite the worsening macroeconomic landscape, the IDR still receives some support from BI's issuance of the SRBI, which has managed to attract substantial foreign liquidity. Indeed, net foreign purchases of SRBI reached Rp 8.9 trillion (~USD 500 million) between June 10-13, 2024, suggesting that the return offered by the SRBI is attractive to foreign investors (despite risks of investing in Indonesia).
- This brings us to the question of whether BI should adjust its benchmark rate to more closely match the yield offered by the SRBI? Given concerns about slowing growth at home, BI is likely reluctant to raise rates further. However, we still see a potential for another 25 bps hike this year, depending on the Rupiah's performance in the coming months. Moreover, BI cannot solely depend on SRBI issuance to maintain IDR stability, as too much issuance of the SRBI may result in an excessive tightening of domestic liquidity.
- There is a possibility of relief if the Fed decides to cut rates earlier than expected, particularly since recent US data has been weaker than anticipated. However, we cannot rely too heavily on this scenario as the Fed will likely require convincing evidence of slowing inflation before beginning its rate cuts. Therefore, we still maintain our base case for the earliest Fed rate cut to occur in Q4-24.

Panel 1. Domestic banks' placement in BI is increasingly skewed towards SRBI



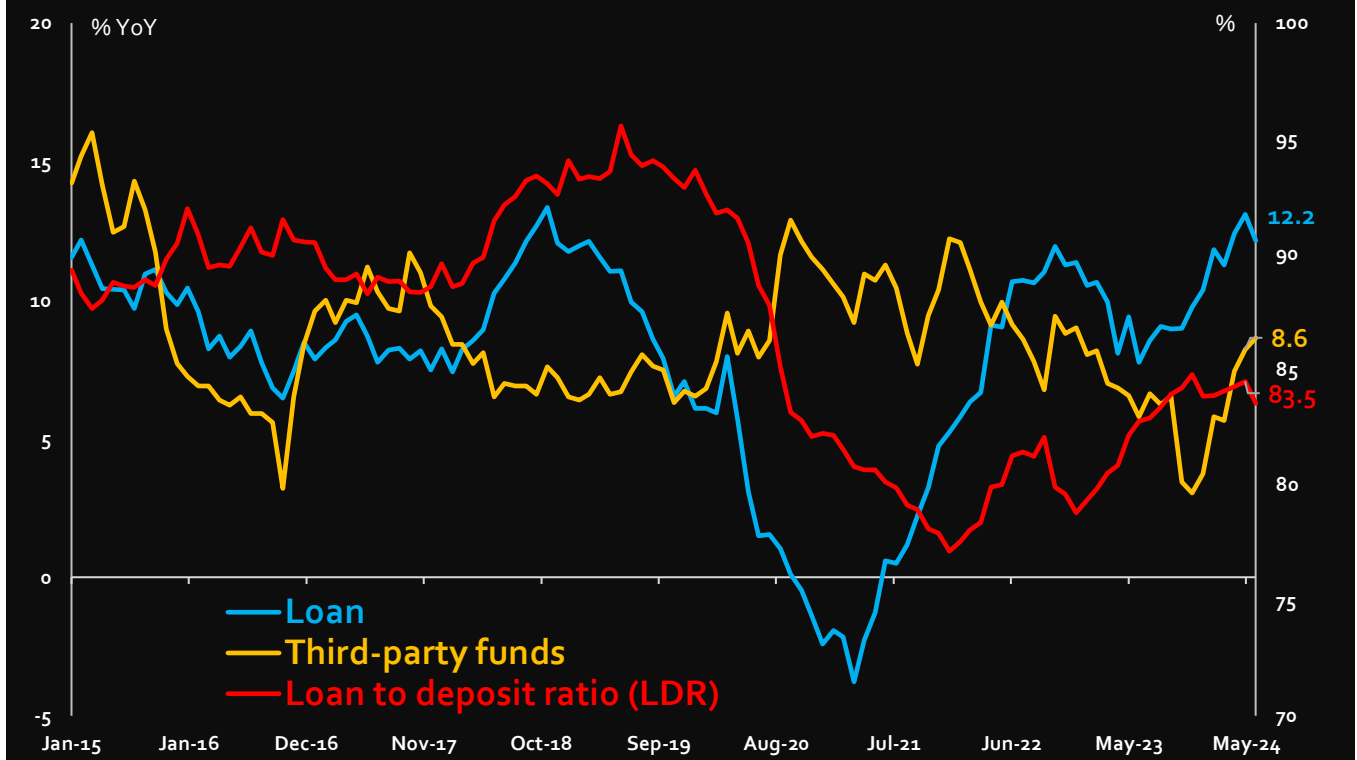
Source: BI, Bloomberg, BCA Economist

Panel 2. The benchmark SBN yield is starting to rise again, despite BI's larger presence in the SBN market



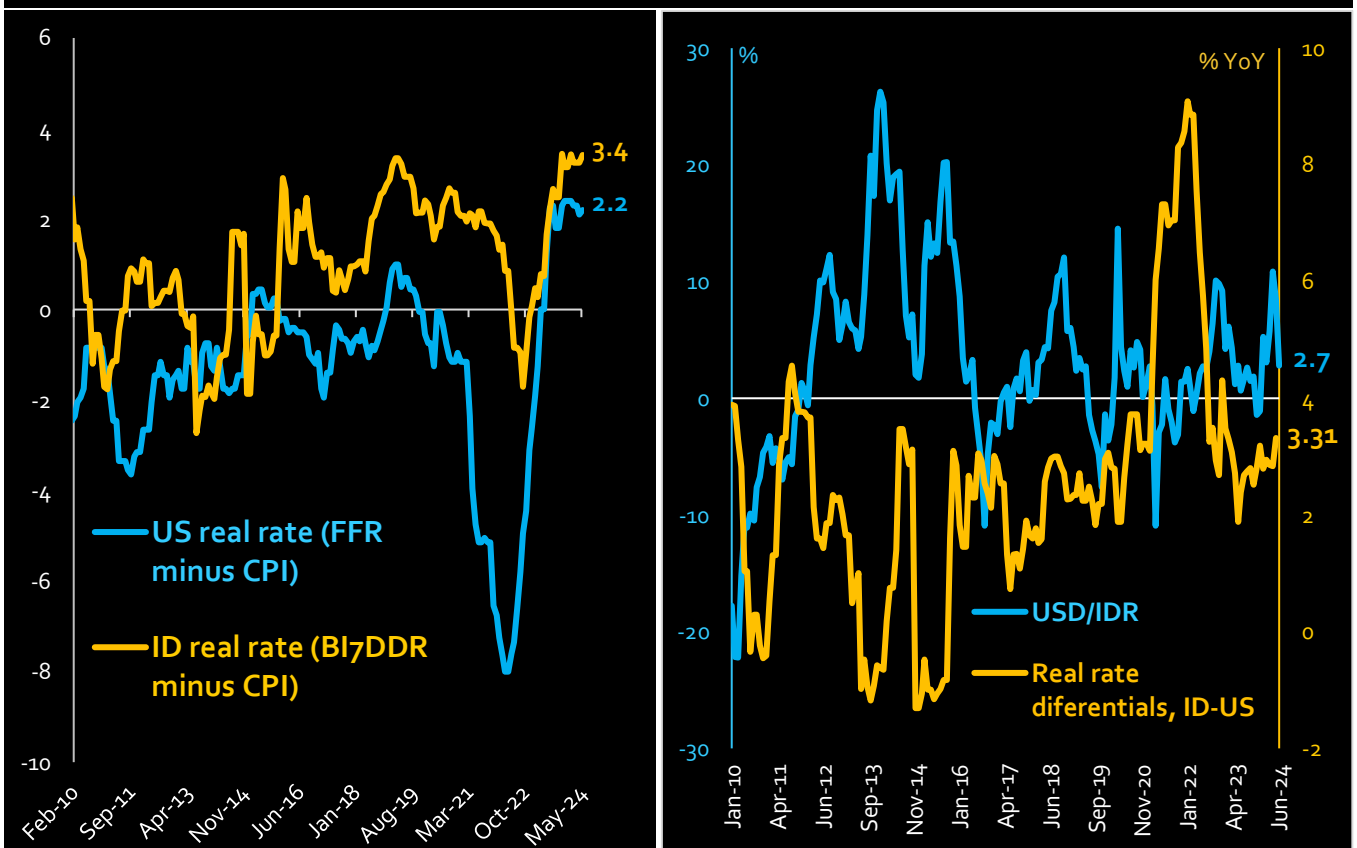
Source: MoF, BI, Bloomberg, BCA Economist

Panel 3. Domestic liquidity has improved in recent months, evident from the stabilization in the LDR



Source: MoF, Bloomberg, BCA Economist

Panel 4. The IDR has continued to depreciate despite rising US – Indonesia real rate differentials



Source: BI, Bloomberg, BCA Economist

Selected Macroeconomic Indicators

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)	Trade & Commodities	19-Jun	-1 mth	Chg (%)
US	5.50	Jul-23	2.20	Baltic Dry Index	1,943.0	1,844.0	5.4
UK	5.25	Aug-23	3.25	S&P GSCI Index	582.3	587.5	-0.9
EU	4.25	Jul-23	1.65	Oil (Brent, \$/bbl)	85.1	84.0	1.3
Japan	-0.10	Jan-16	-2.60	Coal (\$/MT)	140.0	142.4	-1.7
China (lending)	2.50	Aug-23	4.05	Gas (\$/MMBtu)	2.43	2.44	-0.4
Korea	3.50	Jan-23	0.80	Gold (\$/oz.)	2,328.2	2,415.2	-3.6
India	6.50	Feb-23	1.75	Copper (\$/MT)	9,647.2	10,597.9	-9.0
Indonesia	6.25	Apr-24	3.41	Nickel (\$/MT)	17,107.0	20,829.8	-17.9
Money Mkt Rates	19-Jun	-1 mth	Chg (bps)	CPO (\$/MT)	844.0	831.1	1.5
SPN (1M)	5.88	5.80	7.6	Rubber (\$/kg)	1.70	1.67	1.8
SUN (10Y)	7.12	6.86	25.7	External Sector	May	Apr	Chg (%)
INDONIA (O/N, Rp)	6.09	6.01	8.6	Export (\$ bn)	22.33	19.62	13.82
JIBOR 1M (Rp)	6.90	6.90	0.0	Import (\$ bn)	19.40	16.90	14.82
Bank Rates (Rp)	Mar	Feb	Chg (bps)	Trade bal. (\$ bn)	2.93	2.72	7.61
Lending (WC)	8.83	8.84	-1.69	Central bank reserves (\$ bn)*	139.0	136.2	2.04
Deposit 1M	4.62	4.62	-0.76	Prompt Indicators	May	Apr	Mar
Savings	0.68	0.67	0.26	Consumer confidence index (CCI)	125.2	127.7	123.8
Currency/USD	19-Jun	-1 mth	Chg (%)	Car sales (%YoY)	-13.3	-17.5	-26.2
UK Pound	0.786	0.787	0.15	Motorcycle sales (%YoY)	-4.5	18.3	-7.8
Euro	0.931	0.920	-1.15	Manufacturing PMI	May	Apr	Chg (bps)
Japanese Yen	158.1	155.7	-1.54	USA	51.3	50.0	130
Chinese RMB	7.257	7.224	-0.45	Eurozone	47.3	45.7	160
Indonesia Rupiah	16,365	15,955	-2.51	Japan	50.4	49.6	80
Capital Mkt	19-Jun	-1 mth	Chg (%)	China	51.7	51.4	30
JCI	6,726.9	7,317.2	-8.07	Korea	51.6	49.4	220
DJIA	38,834.9	40,003.6	-2.92	Indonesia	52.1	52.9	-80
FTSE	8,205.1	8,420.3	-2.56				
Nikkei 225	38,570.8	38,787.4	-0.56				
Hang Seng	18,430.4	19,553.6	-5.74				
Foreign portfolio ownership (Rp Tn)	May	Apr	Chg (Rp Tn)				
Stock	3,115.0	3,294.9	-179.85				
Govt. Bond	807.0	789.9	17.11				
Corp. Bond	8.2	8.4	-0.20				

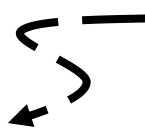
Source: Bloomberg, BI, BPS

Notes:

*Data from earlier period

For changes in currency: **Black indicates appreciation against USD, **Red** otherwise

***For PMI, **>50** indicates economic expansion, **<50** otherwise



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Indonesia – Economic Indicators Projection

	2019	2020	2021	2022	2023	2024E
Gross Domestic Product (% YoY)	5.0	-2.1	3.7	5.3	5.0	5.0
GDP per Capita (US\$)	4175	3912	4350	4784	4920	5149
Consumer Price Index Inflation (% YoY)	2.7	1.7	1.9	5.5	2.6	3.2
BI 7-day Repo Rate (%)	5.00	3.75	3.50	5.50	6.00	6.50
USD/IDR Exchange Rate (end of the year)*	13,866	14,050	14,262	15,568	15,397	16,304
Trade Balance (US\$ billion)	-3.2	21.7	35.3	54.5	37.0	32.6
Current Account Balance (% GDP)	-2.7	-0.4	0.3	1.0	-0.1	-0.5

*Actual number

** Estimation of Rupiah's fundamental exchange rate

Economic, Banking & Industry Research Team

David E.Sumual

Chief Economist

david_sumual@bca.co.id

+6221 2358 8000 Ext:1051352

Agus Salim Hardjodinoto

Head of Industry and Regional

Research agus_lim@bca.co.id

+6221 2358 8000 Ext: 1005314

Barra Kukuh Mamia

Senior Economist

barra_mamia@bca.co.id

+6221 2358 8000 Ext: 1053819

Victor George Petrus Matindas

Senior Economist

victor_matindas@bca.co.id

+6221 2358 8000 Ext: 1058408

Gabriella Yolivia

Industry Analyst

gabriella_yolivia@bca.co.id

+6221 2358 8000 Ext: 1063933

Lazuardin Thariq Hamzah

Economist / Analyst

lazuardin_hamzah@bca.co.id

+6221 2358 8000 Ext: 1071724

Keely Julia Hasim

Economist / Analyst

keely_hasim@bca.co.id

+6221 2358 8000 Ext: 1071535

Elbert Timothy Lasiman

Economist / Analyst

Elbert_lasiman@bca.co.id

+6221 2358 8000 Ext: 1007431

Thierris Nora Kusuma

Economist / Analyst

thierris_kusuma@bca.co.id

+6221 2358 8000 Ext: 1071930

Aldi Rizaldi

Research Assistant

aldi_yanto@bca.co.id

+6221 2358 8000 Ext: 1020451

Fikri Adam Zaqi

Research Assistant

Fikri_zaqi@bca.co.id

+6221 2358 8000 Ext: 20378

Eri Tristanto

Research Assistant

eri_tristanto@bca.co.id

+6221 2358 8000 Ext: -

PT Bank Central Asia Tbk

Economic, Banking & Industry Research of BCA Group

20th Grand Indonesia, Menara BCA

Jl. M.H Thamrin No. 1, Jakarta 10310, Indonesia

Ph : (62-21) 2358-8000 Fax : (62-21) 2358-8343

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