

BI Policy:

Saddle up for the rodeo

Nicholas Husni
Economist/Analyst

Barra Kukuh Mamia
Senior Economist

22 August 2024

Executive Summary

- BI maintained the policy rate at 6.25%, as it awaits rate cut actions by the Fed. The room remains open for potential BI Rate cuts in Q4.
- Recent Rupiah appreciation has been driven by euphoric expectations over Fed cuts, rather than improvement in domestic fundamentals.
- BI has three options to add liquidity and revive growth momentum: cutting the BI Rate, reducing the GWM, or unwinding SRBI.
- Unwinding SRBI could release the most liquidity into the market, but unwinding must be done gradually to avoid market disruption.

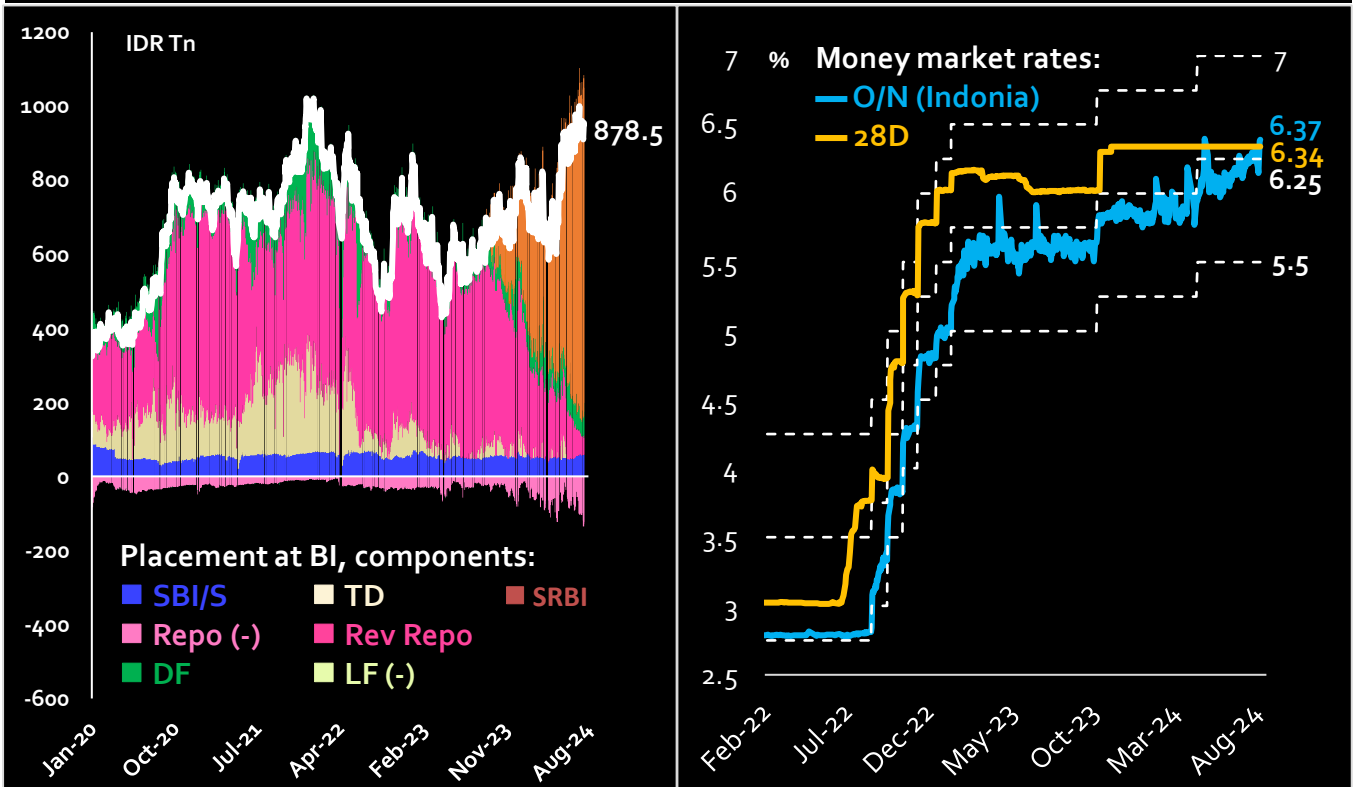
- Bank Indonesia (BI) kept its benchmark rate (BI7DRR) at 6.25%, amid recent appreciation of the Rupiah and declining bond yields. While most analysts anticipated this, a small but vocal minority are starting to see rate cuts on the horizon, especially after the Bangko Sentral ng Pilipinas (BSP) cut its benchmark rate last week.
- So why did BI stay put? Based on BI's own statements, it remains cautious regarding recent improvements in the capital market – which reflects expectations of aggressive Fed rate cuts – and would like to await actual moves by the Fed before starting to ease policy. Gov. Perry Warjiyo commented that BI expects (as baseline scenario) two FFR cuts this year, with the first potentially coming in September. This would open the room for a potential BI rate cut some time in Q4.
- We should also note that the Rupiah's rapid ascent may prove unsustainable, especially when compared to more modest appreciation of other emerging currencies in general. Moreover, it is common historically for the Rupiah to strengthen in August, only to fall in September or October. Given this seasonal pattern and sundry uncertainty about US economy and politics, we would expect BI to defer its first rate cut until at least November.
- Any accommodative action by BI would, of course, be welcome given the softening growth outlook and tightening liquidity. While GDP growth exceeded expectations in Q2 at 5.05%, much of this growth was driven by seasonal factors and legacy government projects, while private CAPEX cycle has been winding down. Meanwhile, manufacturing data and domestic demand are also weakening, with our Consumer Spending Index (Intrabel BCA) in negative territory in July and August (MTD).
- And lack of liquidity may have something to do with this situation. Domestic savings has been inadequate relative to investment, as can be seen from our net bank balance (NBB) data and

the current account deficit (0.9% in Q2). If anything, deposit growth (7.72% in July) are slowing down further vis-à-vis loan growth (12.4% YoY), and a significant part of liquidity is now locked up in government bonds (SBN) and SRBI – effectively kept out of circulation. BI, as such, will have to play a major role in alleviating this liquidity drought.

- But is BI Rate cut the best way to achieve this goal? Keep in mind that monetary policy transmission is a protracted and messy affair, and typically takes 2-4 quarters to be fully felt. We should also note that banks had not really raised their rates on consumer loans during the latest BI rate hike cycle (2022-24), and BI has effectively used its macroprudential tools (base loan rates/SBDK reference) to maintain favorable loan rates. These suggest relatively muted effect from rate cuts, unless/until BI embarks on a more aggressive easing cycle next year.
- The other alternative would be cutting the reserve requirement ratio (Giro Wajib Minimum/ GWM) from the current 9%. Keep in mind, however, that effective GWM rates are actually less than that for most major banks (closer to 5-6%), thanks to BI's incentive system (the Macroprudential Liquidity Buffer/KLM). This suggest that BI may, at best, cut GWM by a further 1-2%, which would inject approximately IDR 90 – 180 Tn into the system.
- But BI still has a third option: unwinding its use of SRBI. As we have noted previously, SRBI has been pivotal in BI's defense of Rupiah, but only about 30% of it is acquired by foreign investors. The need to absorb SRBI, then, increasingly falls to banks, who hold IDR 538 Tn by the end of July. This use of funds for SRBI is such that BI is now resorting to repo facilities (lending to banks) in order that they would be able to buy SRBI.
- But although unwinding SRBI would unleash a lot more liquidity than GWM or even BI Rate cut, it is something that BI would have to do in a measured, deliberate manner. For starters, it may start to reduce the yields on offer – something we are starting to see in recent weeks – and begin to offer smaller and less frequent auctions. Finally, it may let maturing SRBI (about IDR 285 Tn until year-end) expire without issuing replacements.
- The countdown to BI easing has thus started, although the stars are not aligned just yet. For this reason, we maintain a still-cautious outlook for GDP growth and Rupiah until the end of 2024, but a mildly optimistic one for 2025. Fresh injection of liquidity could finally revive the growth momentum, which is becoming dependent on a narrow base of government spending and a few capital-intensive sectors (mining, smelters, chemicals) this year. Of course, the timing and dosage between the potential easing mechanisms (BI Rate cut, GWM cut, SRBI unwinding) would be critical as BI strives to balance liquidity provision with macroeconomic stability.

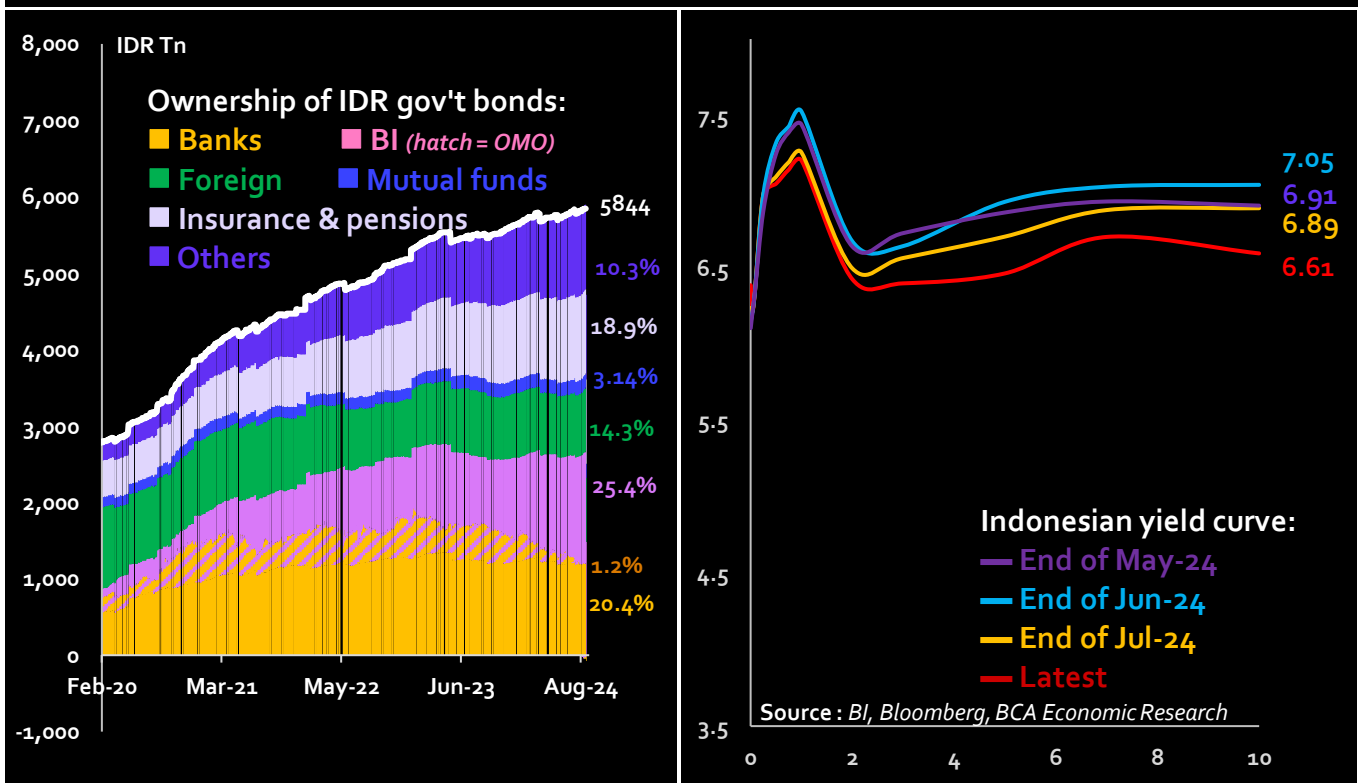
"Timing and dosage of potential easing mechanism would be critical as BI strives to balance liquidity provision with macroeconomic stability."

Panel 1. Domestic banks are stashing their cash almost exclusively in SRBI



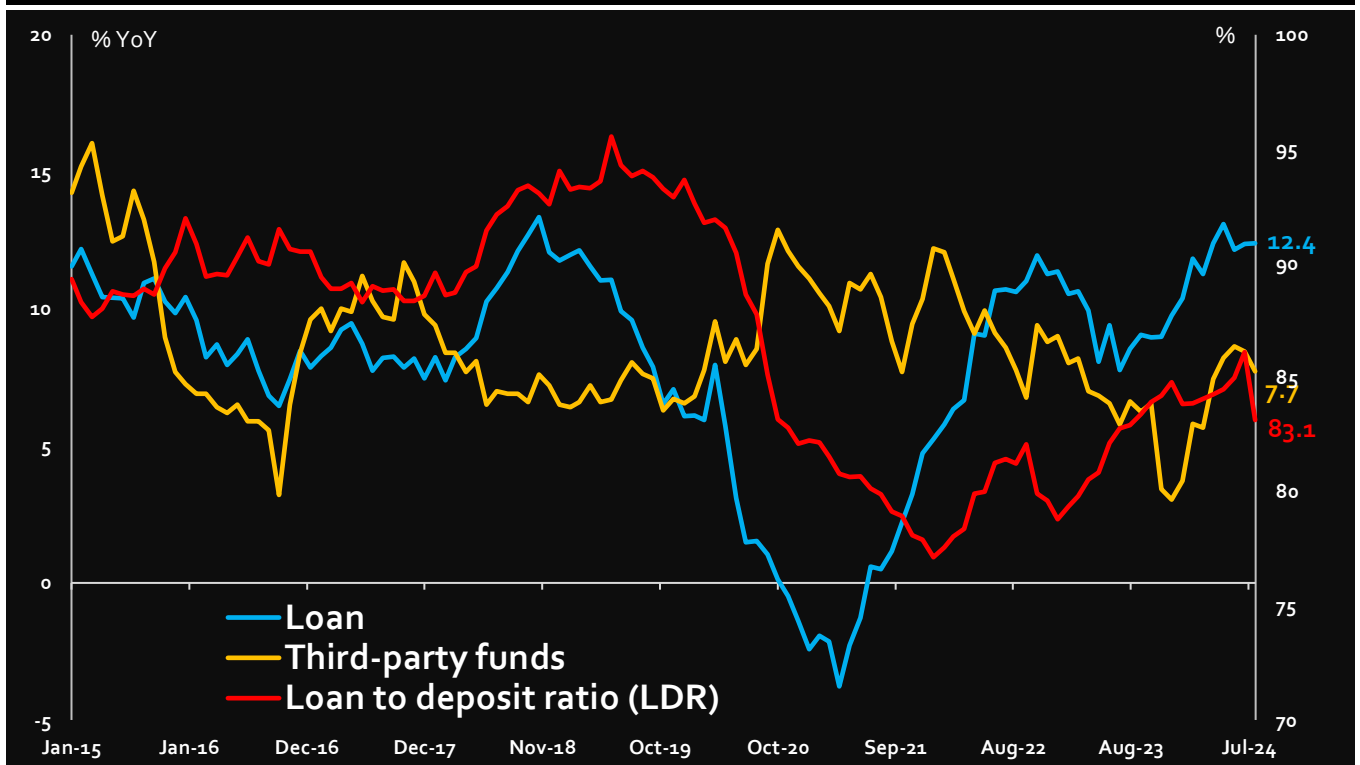
Source: BI, Bloomberg, BCA Economist

Panel 2. The benchmark SBN yield is starting to decline, due to calmer global financing conditions



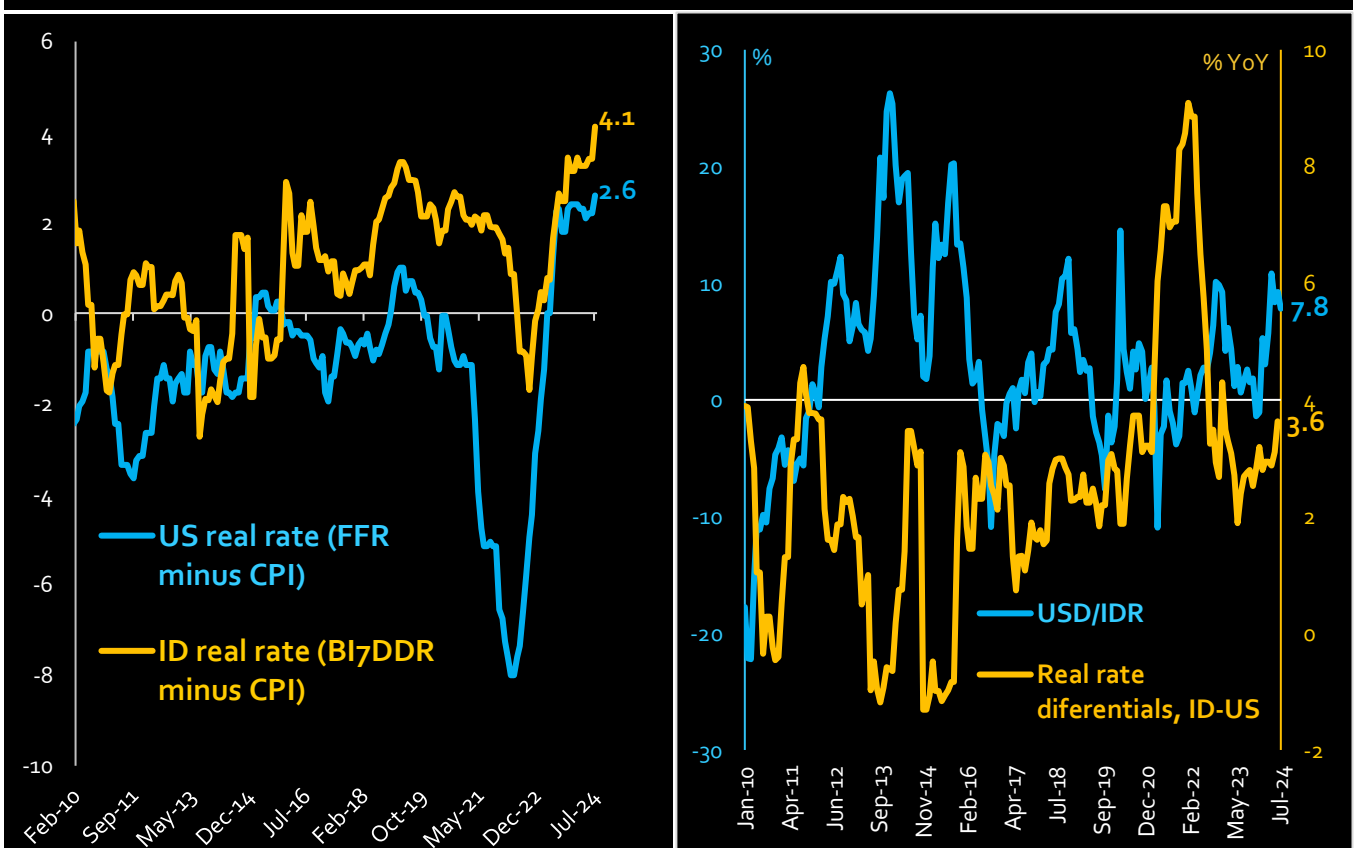
Source: MoF, BI, Bloomberg, BCA Economist

Panel 3. Private sector expansion is still going strong, evident from the persisting loan growth in Jul-24



Source: MoF, Bloomberg, BCA Economist

Panel 4. The IDR posted a decent recovery, but remains fundamentally weak



Source: BI, Bloomberg, BCA Economist

Selected Macroeconomic Indicators

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)	Trade & Commodities	21-Aug	-1 mth	Chg (%)
US	5.50	Jul-23	2.60	Baltic Dry Index	1,759.0	1,902.0	-7.5
UK	5.00	Aug-23	2.80	S&P GSCI Index	530.5	555.8	-4.6
EU	4.25	Jul-23	1.65	Oil (Brent, \$/bbl)	76.1	82.6	-8.0
Japan	-0.10	Jan-16	-2.90	Coal (\$/MT)	148.1	139.6	6.1
China (lending)	2.30	Aug-23	3.85	Gas (\$/MMBtu)	2.14	1.79	19.4
Korea	3.50	Jan-23	0.90	Gold (\$/oz.)	2,512.6	2,400.8	4.7
India	6.50	Feb-23	2.96	Copper (\$/MT)	9,136.1	9,179.3	-0.5
Indonesia	6.25	Apr-24	4.12	Nickel (\$/MT)	16,665.8	15,985.5	4.3
Money Mkt Rates	21-Aug	-1 mth	Chg (bps)	CPO (\$/MT)	889.6	855.8	4.0
SPN (3M)	6.47	6.56	-8.2	Rubber (\$/kg)	1.78	1.66	7.2
SUN (10Y)	6.59	6.94	-34.2	External Sector	Jul	Jun	Chg (%)
INDONIA (O/N, Rp)	6.37	6.13	23.3	Export (\$ bn)	22.21	20.85	6.55
JIBOR 1M (Rp)	6.90	6.90	-0.1	Import (\$ bn)	21.74	18.45	17.82
Bank Rates (Rp)	May	Apr	Chg (bps)	Trade bal. (\$ bn)	0.47	2.39	-80.29
Lending (WC)	8.86	8.85	1.37	Central bank reserves (\$ bn)*	145.4	140.2	3.74
Deposit 1M	4.68	4.65	2.54	Prompt Indicators	Jul	Jun	Apr
Savings	0.67	0.68	-1.07	Consumer confidence index (CCI)	123.4	123.3	127.7
Currency/USD	21-Aug	-1 mth	Chg (%)	Car sales (%YoY)	-7.9	-11.8	-17.4
UK Pound	0.764	0.774	1.37	Motorcycle sales (%YoY)	26.0	3.5	18.3
Euro	0.897	0.919	2.46	Manufacturing PMI	Jul	Jun	Chg (bps)
Japanese Yen	145.2	157.5	8.45	USA	49.6	51.6	-200
Chinese RMB	7.131	7.270	1.94	Eurozone	45.8	45.8	0
Indonesia Rupiah	15,485	16,190	4.55	Japan	49.1	50.0	-90
Capital Mkt	21-Aug	-1 mth	Chg (%)	China	49.8	51.8	-200
JCI	7,554.6	7,294.5	3.57	Korea	51.4	52.0	-60
DJIA	40,890.5	40,287.5	1.50	Indonesia	49.3	50.7	-140
FTSE	8,283.4	8,155.7	1.57				
Nikkei 225	37,951.8	40,063.8	-5.27				
Hang Seng	17,391.0	17,417.7	-0.15				
Foreign portfolio ownership (Rp Tn)	Jul	Jun	Chg (Rp Tn)				
Stock	3,322.0	3,273.1	48.98				
Govt. Bond	813.1	808.1	4.97				
Corp. Bond	7.6	8.2	-0.60				

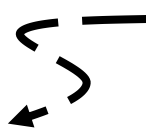
Source: Bloomberg, BI, BPS

Notes:

*Data from earlier period

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

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



Scan for the link to our report depository or click:

https://s.id/BCA_REI

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	2.87
BI 7-day Repo Rate (%)	5.00	3.75	3.50	5.50	6.00	6.00
USD/IDR Exchange Rate (end of the year)*	13,866	14,050	14,262	15,568	15,397	16,172
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

Nicholas Husni

Economist / Analyst

nicholas_husni@bca.co.id

+6221 2358 8000 Ext: 1079839

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

DISCLAIMER

This report is for information only, and is not intended as an offer or solicitation with respect to the purchase or sale of a security. We deem that the information contained in this report has been taken from sources which we deem reliable. However, we do not guarantee their accuracy, and any such information may be incomplete or condensed. None of PT. Bank Central Asia Tbk, and/or its affiliated companies and/or their respective employees and/or agents makes any representation or warranty (express or implied) or accepts any responsibility or liability as to, or in relation to, the accuracy or completeness of the information and opinions contained in this report or as to any information contained in this report or any other such information or opinions remaining unchanged after the issue thereof. The Company, or any of its related companies or any individuals connected with the group accepts no liability for any direct, special, indirect, consequential, incidental damages or any other loss or damages of any kind arising from any use of the information herein (including any error, omission or misstatement herein, negligent or otherwise) or further communication thereof, even if the Company or any other person has been advised of the possibility thereof. Opinion expressed is the analysts' current personal views as of the date appearing on this material only, and subject to change without notice. It is intended for the use by recipient only and may not be reproduced or copied/photocopied or duplicated or made available in any form, by any means, or redist ted to others without written permission of PT Bank Central Asia Tbk.

All opinions and estimates included in this report are based on certain assumptions. Actual results may differ materially. In considering any investments you should make your own independent assessment and seek your own professional financial and legal advice. For further information please contact: (62-21) 2358 8000, Ext: 1020451 or fax to: (62-21) 2358 8343 or email: eri_tristanto@bca.co.id