

BI Policy:

Pausing to let the uncertainty train pass

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Executive Summary

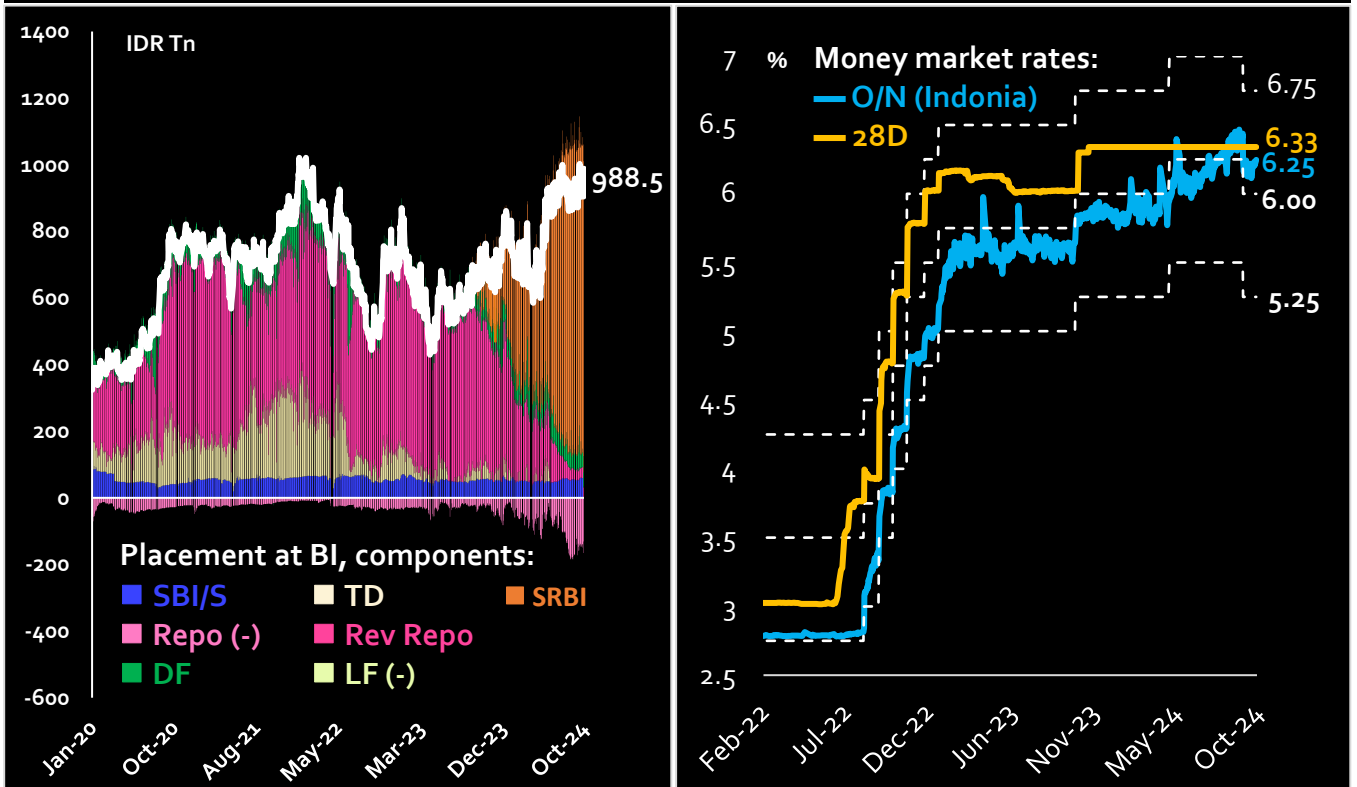
- Bank Indonesia maintained its policy rate of 6%, mainly due to more hawkish market expectations caused by escalation in the Iran-Israel conflict, China's uncertain stimulus size, better than expected U.S. data, and the looming U.S. presidential election.
- BI's belief that Rupiah's fundamental value was more accurately reflected in August and September may complicate their exit plan from SRBI.
- BI has realigned KLM to focus more on labor-intensive industries, as well as extending 0% MDR for all QRIS transactions up to Rp 500k.
- The lack of a cut this month is likely to be temporary stoppage on a dovish road, but uncertainty about the global market slowdown, much less a soft landing represents many speedbumps ahead.

- BI decided to keep the BI Rate at 6.00%, in line with the recent shift in market expectations of late – and a weaker Rupiah as a result. This shift was driven by recent shocks that has thrown the “soft landing” thesis into doubt.
- The first shock, of course, was the escalation of the Israel-Iran conflict, which has led to fears over oil supply. As a result, crude oil price has risen by 8.5% from its pre-FOMC low, and even briefly topped USD 80/bbl. Meanwhile, recent unemployment and inflation data show that the US economy is not weakening as quickly as previously expected. Furthermore, it is now becoming clear that most of the slowdown in inflation in the last four months was driven by lower oil price (which is now reversing) and oversupply in China.
- Speaking of China, its stimulus may now be seen as the main X-factor for global rate trajectory going forward. And after a sharp rally late in September, the size and cautiousness of China's stimulus package has begun to disappoint some investors. It is clear that a bolder program would be needed to revive China's consumer demand and credit impulse, but this very success may lead to the abatement of the current deflationary global environment, driven as it is by the gap between strong supply growth and weak demand growth in China.
- The recent sharp downturn in Rupiah's value becomes another reason for BI to keep its interest rates. Initially fluctuating at Rp 15,100 – Rp 15,500/USD in September, Rupiah has now fallen to Rp 15,500 - Rp 15,600/USD at the time of writing. BI has indicated belief that Rupiah's September exchange rate was closer to its “fundamental value” than its current exchange rate in October, and that less geopolitical uncertainty would restore the Rupiah at a stronger position.
- But while we agree that reduced uncertainty would benefit Rupiah, we would argue that the current level may be closer to Rupiah's fundamentals. We should remember that – outside of

the rate cut euphoria in August and September – Rupiah has mostly been weaker, and that the current exchange rate is partly buttressed by net issuance of SRBI. We see BI's comments, as such, as a sign of its limited tolerance to IDR depreciation, which would complicate its exit from what was initially intended to be a short-term strategy (SRBI).

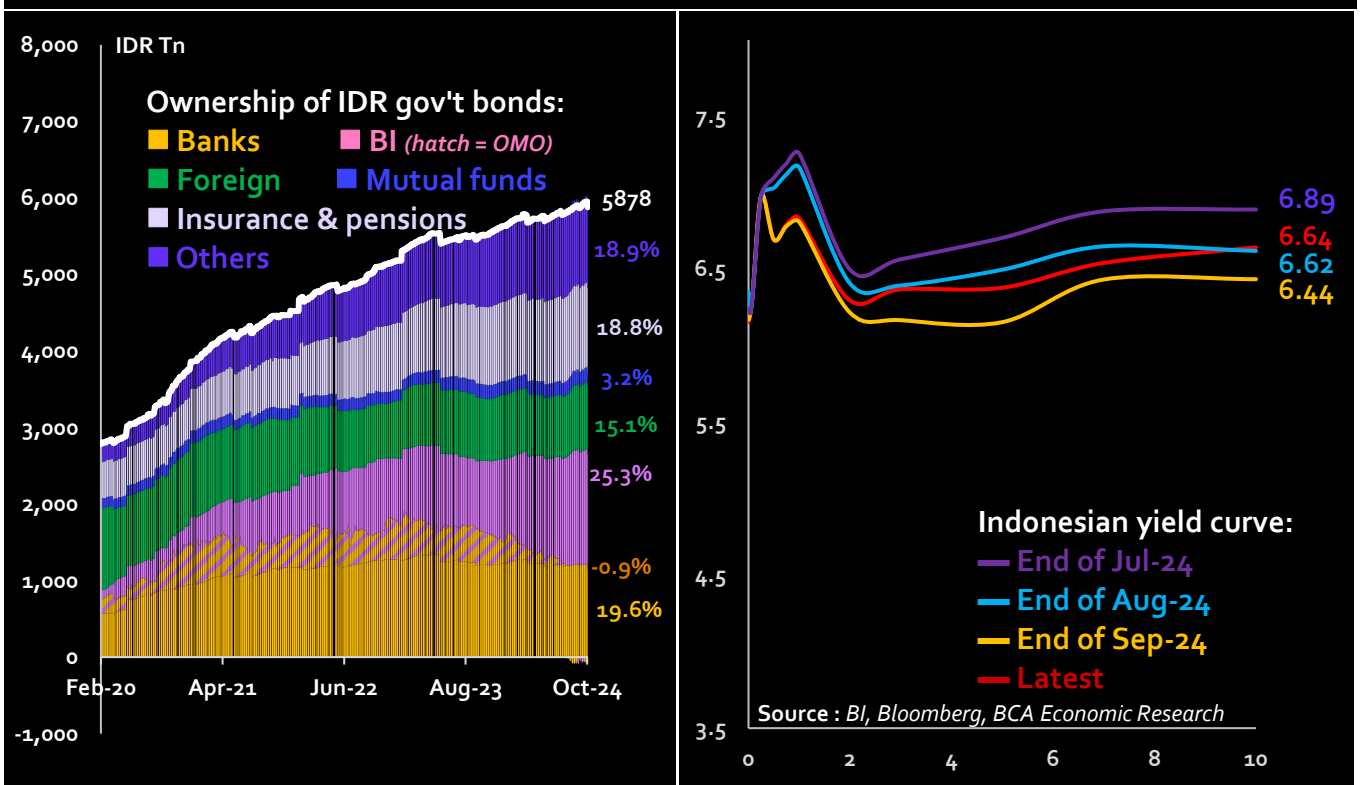
- Despite no rate cut, BI has kept its pro-growth stance elsewhere. Macroprudential Liquidity Incentive Policy (referred to as "KLM") has been realigned to focus on labor intensive industries, down streaming, MSMEs, and green investment, although we are yet to see signs of bigger incentives yet. This realignment may be driven by the recent slowdown in loan growth (to 10.85% YoY), albeit still within BI's target range (10-12%), and the gap in loan growth between capital-intensive and labor-intensive sectors. For example, loan growth for Agriculture (7.4%), retail (8.4%), and MSME (5.04%) are much lower than the growth on mining (26.7%), electricity, gas, and water (15.9%), and transport, telecoms, and tourism (17.5%).
- KLM acts as by reducing reserve requirement ratio (GWM/RRR) for banks, and is therefore a more specific/targeted liquidity boost. Thanks to KLM, large banks probably already enjoy much lower effective RRR (closer to 5-6%) rather than the *de jure* level of 9%. Given this gap between official RRR and effective RRR, the room to use RRR as an expansionary monetary instrument is more limited.
- BI has also expanded the threshold for 0% MDR (Merchant Discount Rate) to transactions of up to IDR 500k, which would take effect on 1 December 2024. At present, QRIS would take a 0.3% transaction fee from the merchant for transactions above Rp 100k, while transactions below Rp 100k would have no transaction costs. This change may be of some benefit for MSMEs and mid-sized corporates, especially those in the F&B industry that makes up the largest sector of QRIS merchants. However, it is too hasty to conclude that this will be a strong boost for demand, as the main problem seems to be the relatively weak purchasing power of Indonesian consumers rather than high transaction costs.
- Interestingly, while data on bank deposits (third-party loan funds or referred to as "DPK") has not been published in recent months, we can surmise a weakening trend from other sources (with August growth at only 6.8% YoY). This slower pace of growth (and even contraction) unfortunately isn't too surprising, seeing as the massive government spending in Q1-24 leave the government with too few bullets to spend in Q2-24. However, we may expect some improvement on DPK going forward, due to rising commodity prices and higher spending from Regional Elections and new government programs.
- Overall, the decision to not cut interest rates likely only represent a temporary stoppage on a dovish road, not a reversal in policy. It is important to note that a global slowdown (much less a gradual, well-engineered "soft landing") is not a given, and there will be speedbumps along the way. Indeed, we have not even mentioned the US Elections and the potential bout of uncertainty that a return to Trump presidency could engender – whether on geopolitical, tariff, or low rates/weak USD policies – especially since it appears that he is now a slight favourite for the November 5th vote.

Panel 1. SRBI growth has slowed down but is still positive.



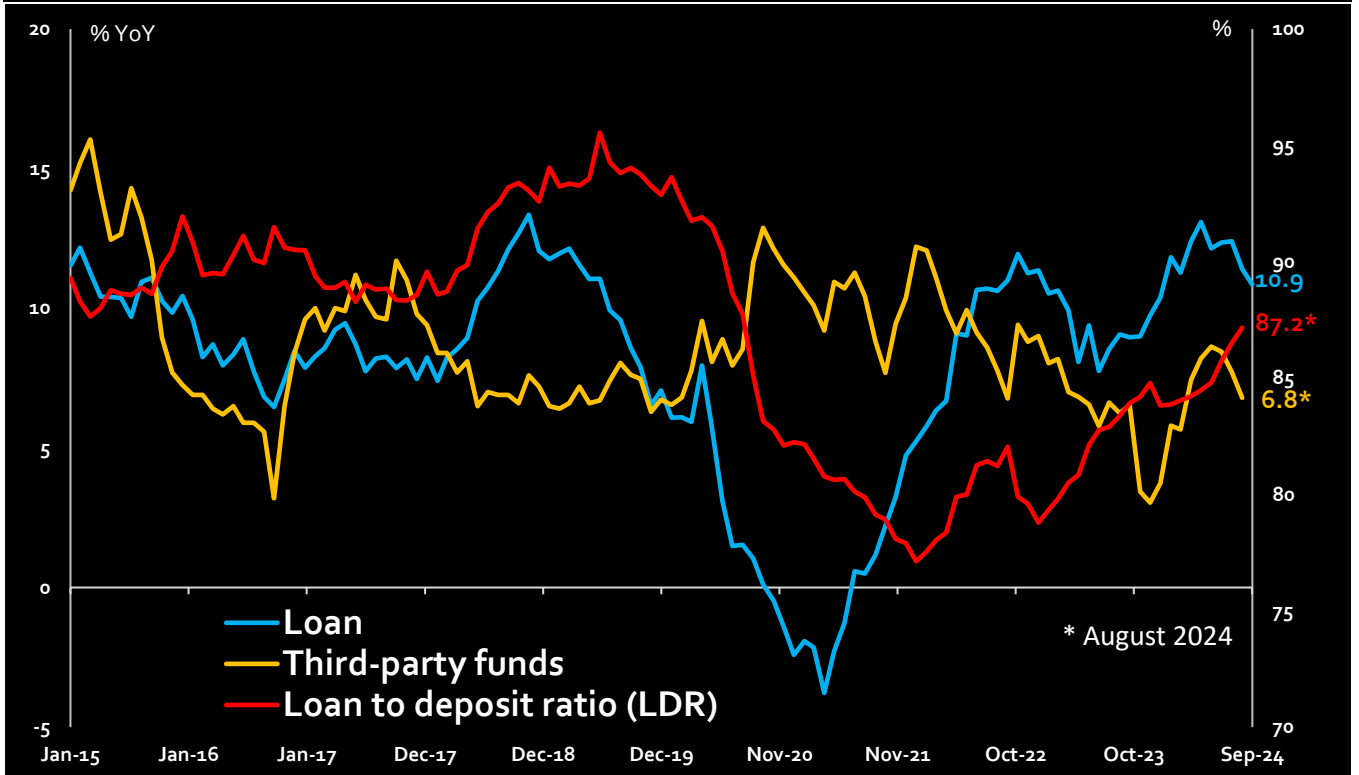
Source: BI, Bloomberg, BCA Economist

Panel 2. The benchmark SBN yield is going back up again



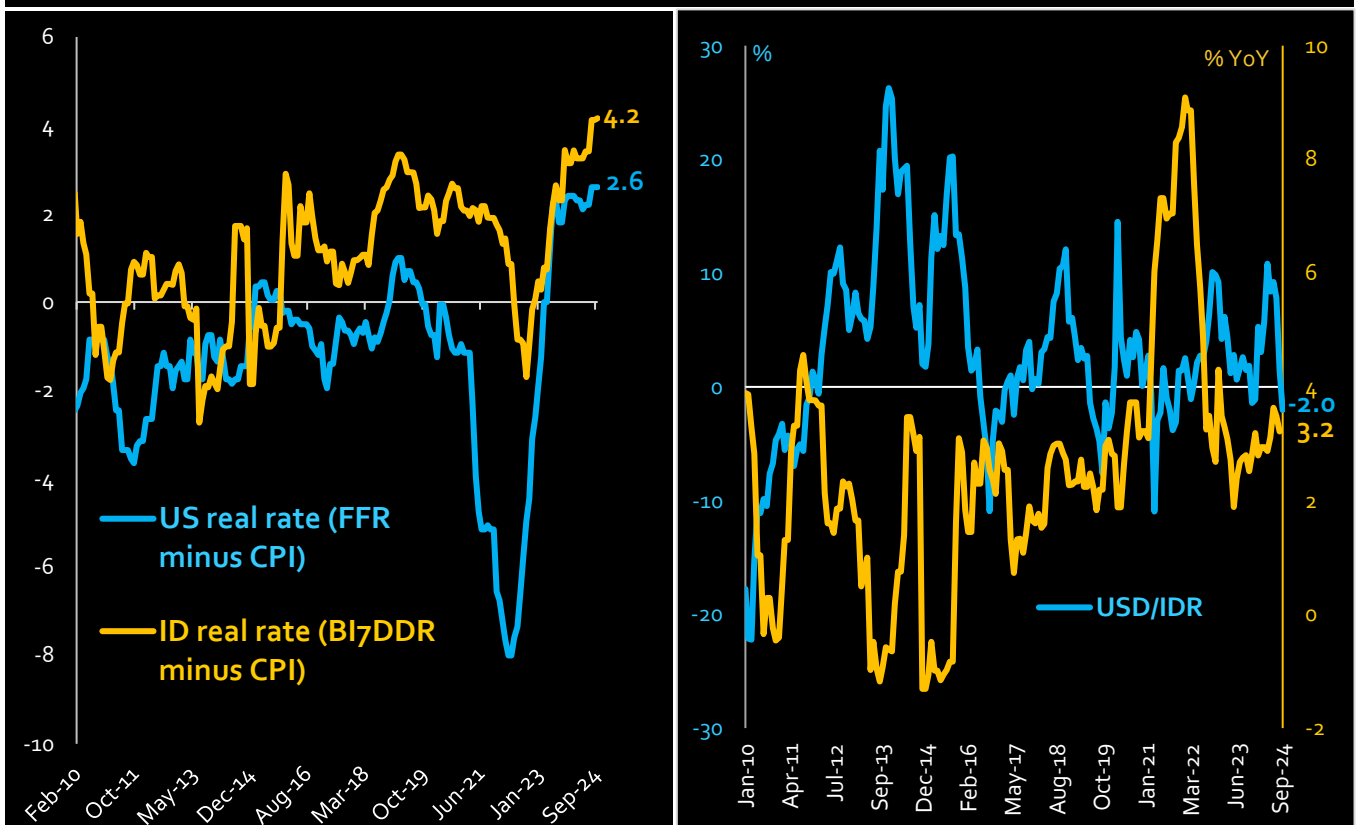
Source: MoF, BI, Bloomberg, BCA Economist

Panel 3. Both loan and third-party funds have decreased this month



Source: MoF, Bloomberg, BCA Economist

Panel 4. The IDR has tumbled down from it's high



Source: BI, Bloomberg, BCA Economist

Selected Macroeconomic Indicators

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)	Trade & Commodities	16-Oct	-1 mth	Chg (%)
US	5.00	Sep-24	2.60	Baltic Dry Index	1,676.0	1,890.0	-11.3
UK	5.00	Aug-24	3.30	S&P GSCI Index	536.1	519.1	3.3
EU	3.65	Sep-24	1.85	Oil (Brent, \$/bbl)	74.2	71.6	3.6
Japan	0.25	Jul-24	-3.10	Coal (\$/MT)	147.4	136.3	8.2
China (lending)	2.00	Sep-24	3.95	Gas (\$/MMBtu)	2.21	2.26	-2.1
Korea	3.25	Oct-24	1.65	Gold (\$/oz.)	2,673.8	2,577.7	3.7
India	6.50	Feb-23	1.01	Copper (\$/MT)	9,418.8	9,189.2	2.5
Indonesia	6.00	Sep-24	4.16	Nickel (\$/MT)	17,019.9	15,709.7	8.3
Money Mkt Rates	16-Oct	-1 mth	Chg (bps)	CPO (\$/MT)	1,022.2	928.8	10.1
SPN (3M)	4.06	5.91	-185.6	Rubber (\$/kg)	2.00	1.89	5.8
SUN (10Y)	6.66	6.56	9.7	External Sector	Sep	Aug	Chg (%)
INDONIA (O/N, Rp)	6.16	6.34	-18.1	Export (\$ bn)	22.08	23.44	-5.80
JIBOR 1M (Rp)	6.64	6.90	-26.6	Import (\$ bn)	18.82	20.67	-8.91
Bank Rates (Rp)	Jul	Jun	Chg (bps)	Trade bal. (\$ bn)	3.26	2.78	17.37
Lending (WC)	8.81	8.82	-1.72	Central bank reserves (\$ bn)*	149.9	150.2	-0.21
Deposit 1M	4.78	4.70	7.49	Prompt Indicators	Sep	Aug	Jul
Savings	0.65	0.67	-1.66	Consumer confidence index (CCI)	123.5	124.4	123.4
Currency /USD	16-Oct	-1 mth	Chg (%)	Car sales (%YoY)	-9.1	-14.2	-7.8
UK Pound	0.770	0.762	-1.02	Motorcycle sales (%YoY)	3.7	7.4	24.1
Euro	0.921	0.903	-1.92	Manufacturing PMI	Sep	Aug	Chg (bps)
Japanese Yen	149.6	140.9	-5.87	USA	47.3	47.9	-60
Chinese RMB	7.120	7.097	-0.31	Eurozone	45.0	45.8	-80
Indonesia Rupiah	15,513	15,400	-0.73	Japan	49.7	49.8	-10
Capital Mkt	16-Oct	-1 mth	Chg (%)	China	49.3	50.4	-110
JCI	7,648.9	7,812.1	-2.09	Korea	48.3	51.9	-360
DJIA	43,077.7	41,393.8	4.07	Indonesia	49.2	48.9	30
FTSE	8,329.1	8,273.1	0.68				
Nikkei 225	39,180.3	36,581.8	7.10				
Hang Seng	20,286.9	17,369.1	16.80				
Foreign portfolio ownership (Rp Tn)	Sep	Aug	Chg (Rp Tn)				
Stock	3,558.2	3,684.6	-126.37				
Govt. Bond	870.6	852.3	18.28				
Corp. Bond	6.9	7.0	-0.02				

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	1.9
BI 7-day Repo Rate (%)	5.00	3.75	3.50	5.50	6.00	5.50
USD/IDR Exchange Rate (end of the year)*	13,866	14,050	14,262	15,568	15,397	15,650
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

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