CPI:
Short-term surge, fundamental problem

Thierris Nora Kusuma
Economist/Analyst

Barra Kukuh Mamia
Senior Economist

01 Apr 2024

Executive Summary

- Inflation surged to 3.05% YoY (0.52% MoM) in Mar-24, primarily driven by food prices (rice, eggs, and chicken) due to supply issues exacerbated by heightened demand during Ramadan and upcoming Lebaran festivities.
- Core inflation experienced a slight uptick to 1.77% YoY, indicating strong consumption among low-income groups, amid concern over weak durable consumption that probably reflects the pattern of upper- and middle-class conservative spending.
- BI is anticipated to adopt additional measures to boost growth, possibly by expanding macroprudential incentives (KLM). However, weak deposit growth resulting from low commodity prices suggests that overt easing through the BI Rate is unlikely until the Fed initiates rate cuts.

- Inflation surged to 3.05% YoY (0.52% MoM) in Mar-24, substantially higher than consensus (2.91%). As has been the case in recent months, foodstuffs were the primary driver of inflation, contributing nearly 80% of the monthly increase in prices.

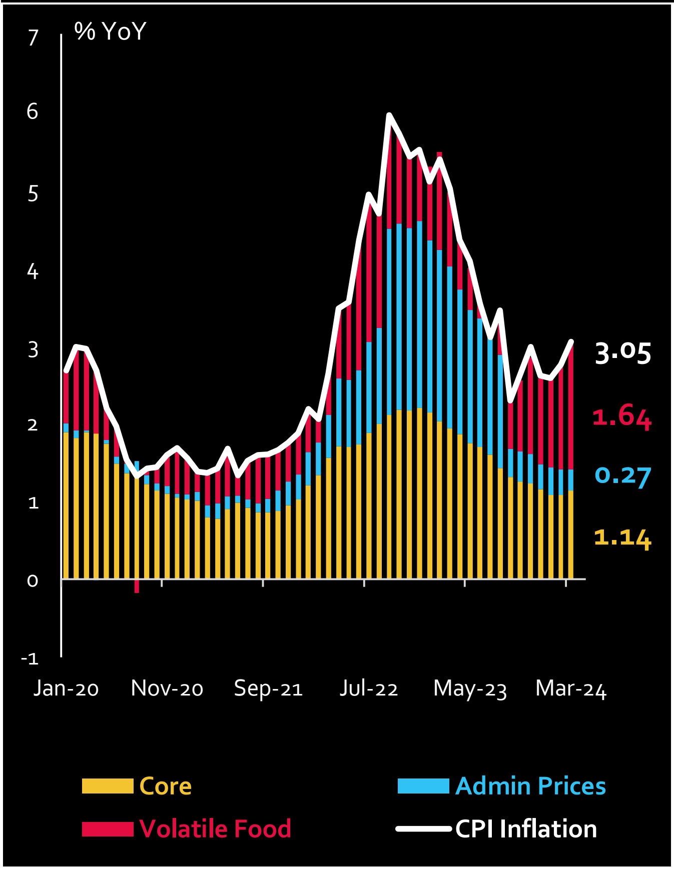
- Of this, about two-thirds came from rice, eggs, and chicken, where the unfortunate supply problems collided with the heightened demand during Ramadan and the upcoming Lebaran festivities. This was almost in line with the worst-case scenario that we envisioned a while ago, although fortunately things are likely to improve from here on out. The harvest season ("panen raya") is finally commencing after some delay, while El Niño conditions – which led to the delay in the first place – is finally abating.

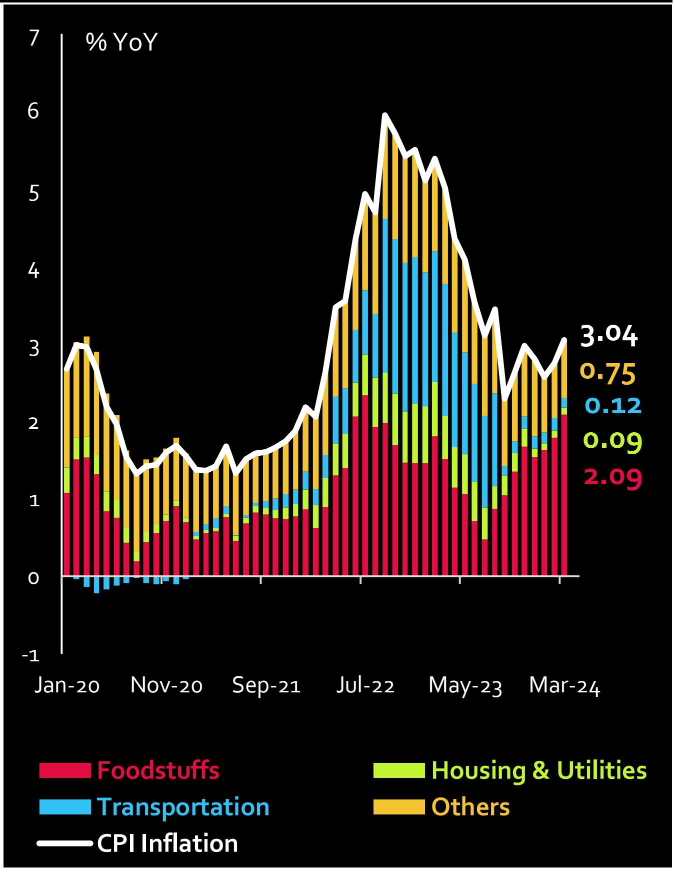
- Core inflation also experienced a slight uptick to 1.77% YoY (Feb-24: 1.68% YoY), albeit still on the low side compared to a few months ago. The media is usually quick to attribute this increase in core inflation to improved consumption, but the reality might be more nuanced than that. Indeed, depending on how one looks at it, consumption might be a half-full or a half-empty glass.

- On the "half-full" side: consumption by low-income groups – chiefly consisting of basic needs and secondary items such as new clothing for Lebaran – appear to be robust. This is boosted by the large amounts of cash in circulation, thanks to government social assistance and the recent disbursement of seasonal bonuses (THR). Strong demand for cash can also be seen from the still-large spread between overnight money market rates (Indonia) and the "floor" of BI's monetary corridor (deposit facility/DF).

- On the "half-empty" side, however, there has been a lot of hand-wringing over the weakness of durable goods consumption, which also suppressed the growth in consumer loans. This probably reflects the pattern of upper- and middle-class spending, which has become a lot more conservative since the second half of 2023. Recent reporting has often focused on the decline in small-size savings account as a sign of weakening purchasing power; in our view, however, the growth in large accounts – and especially time deposits – are equally (if not more) revealing about the nature of the consumption slowdown.
- Given the implications on growth, BI should favor more stimulus in the short-term. However, this bumps up against the reality of heightened inflation (however temporary) and stronger US Dollar, as the market continues to downgrade the chances of Fed easing this year, making an early BI Rate cut a dicey proposition. The easiest path – as we have often argued before – is for BI to loosen the reserve requirement ratio (RRR), given the wide gap between bank lending and deposit growth rates.
- As it turns out, BI seems likely to choose an even cleverer solution – widening its existing macroprudential incentives (KLM) such that the effective RRR is much lower than the 9% rate that is currently in place. Under KLM, banks are allowed certain discounts on their RRR if they successfully meet BI's lending target in areas such as mineral downstreaming or SME loans, which are in line with government priorities.
- Last year, BI reported that its KLM incentives had led to roughly 2% of bank deposits being "freed" from reserve requirement – which banks can then utilize to lend or to purchase government debt (SBN). This year, it is quite likely that these incentives would be widened further, meaning that the effective RRR would probably lie between 5-6%. We expect this policy to be announced in the upcoming BI policy meeting(s), and it is likely to be an easy "win-win" solution – for lending and GDP growth, for bank profits, and for SBN demand.
- Still, there is no quick fix to the fundamental problem, namely the weak deposit growth which – as we hinted in today's The Focal Point – can largely be attributed to declining corporate revenues due to weak commodity prices. The bitter truth, of course, is that Indonesia remains a commodity-dependent economy, but the impact of low commodity prices was typically mitigated by lower global interest rates which allows BI to ease policy accordingly.
- As long as the Fed persists with its tight(-ish) policy, however, the commodity cloud contains little silver linings for Indonesia. For this reason, we cannot expect any overt easing (via BI Rate) until the Fed begins to cut rates, and macroprudential tools such as KLM remains BI's best bet to bolster growth in the short-term.

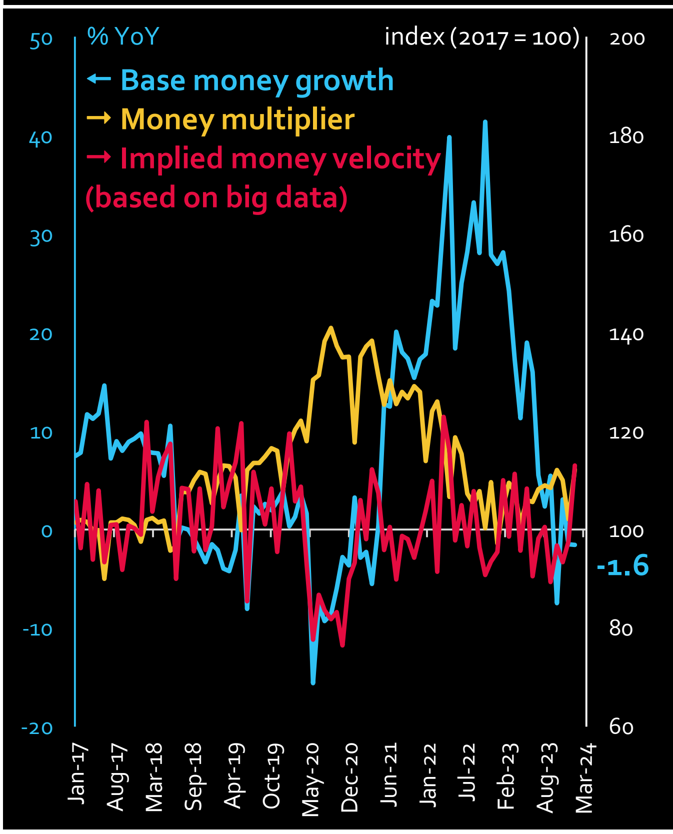
Panel 1. Inflation increased mainly due to the foodstuffs category

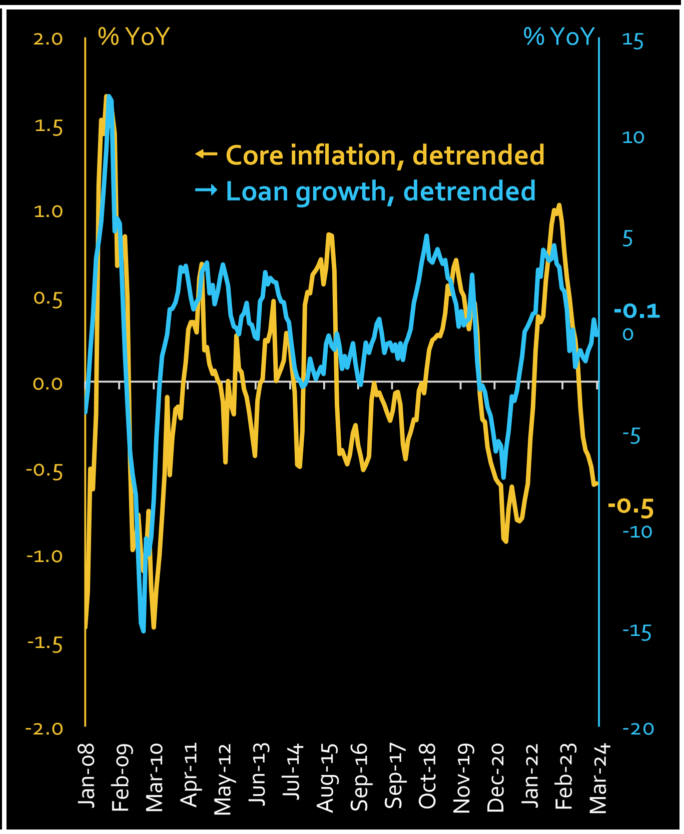




Source: BPS, calculation by BCA Economic Research

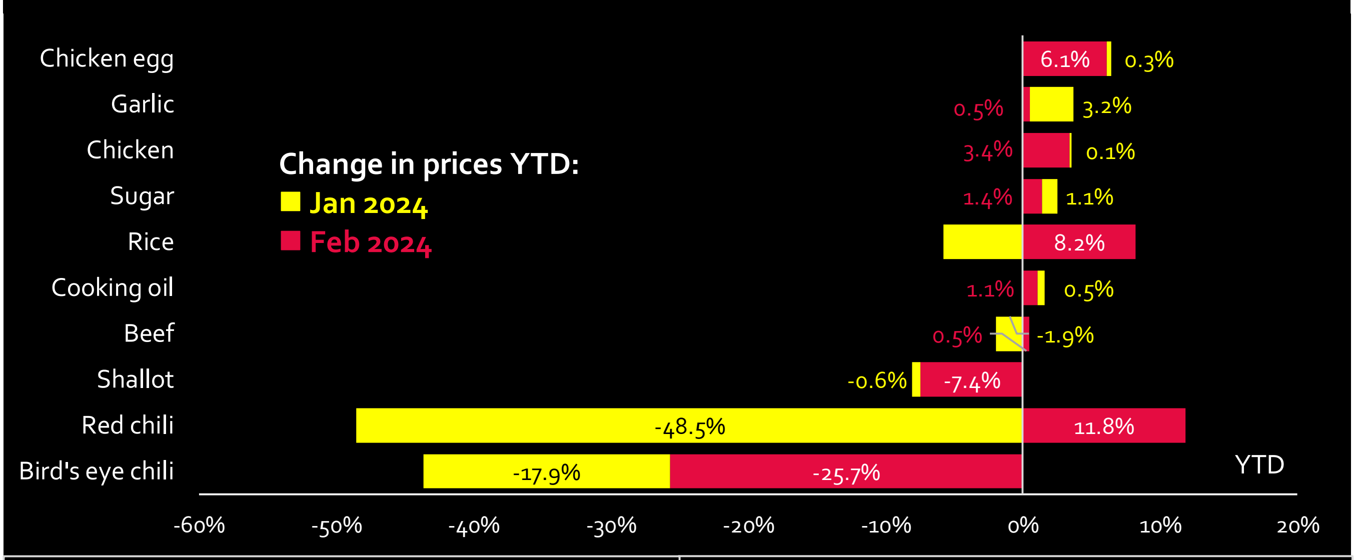
Panel 2. Core inflation posted a limited gain, and is expected to increase further

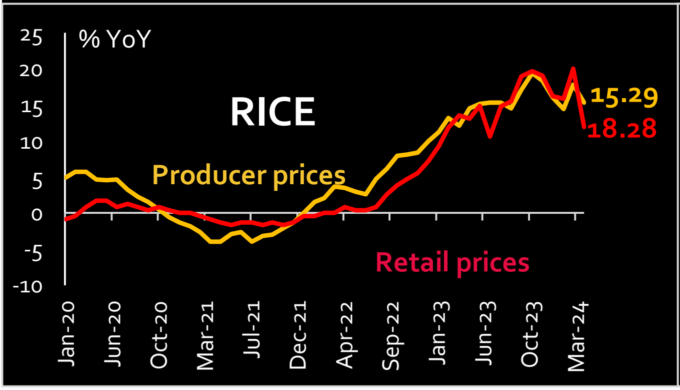


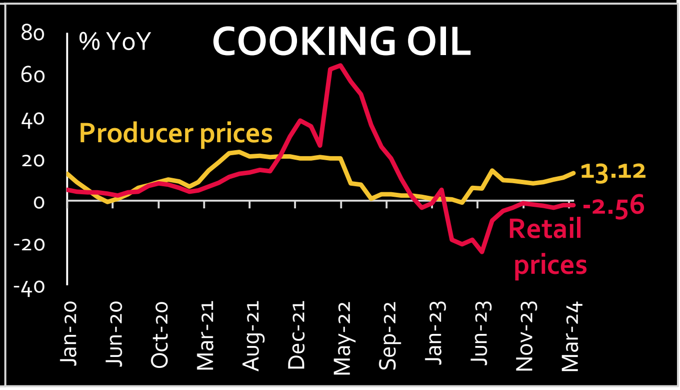


Source: BI, OJK, BCA big data, calculation by BCA Economic Research

Panel 3. **Among the foodstuffs category, rice prices increased the most**

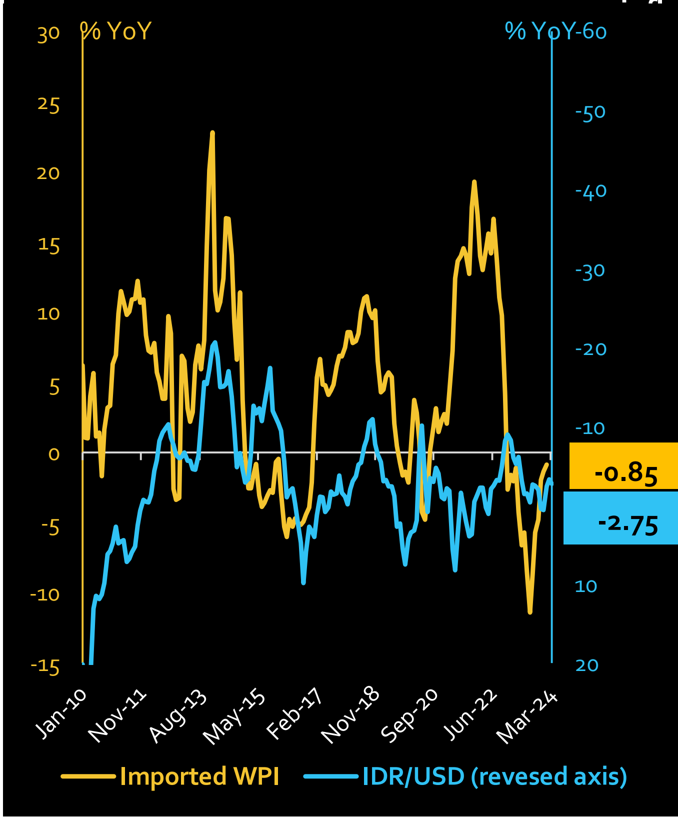


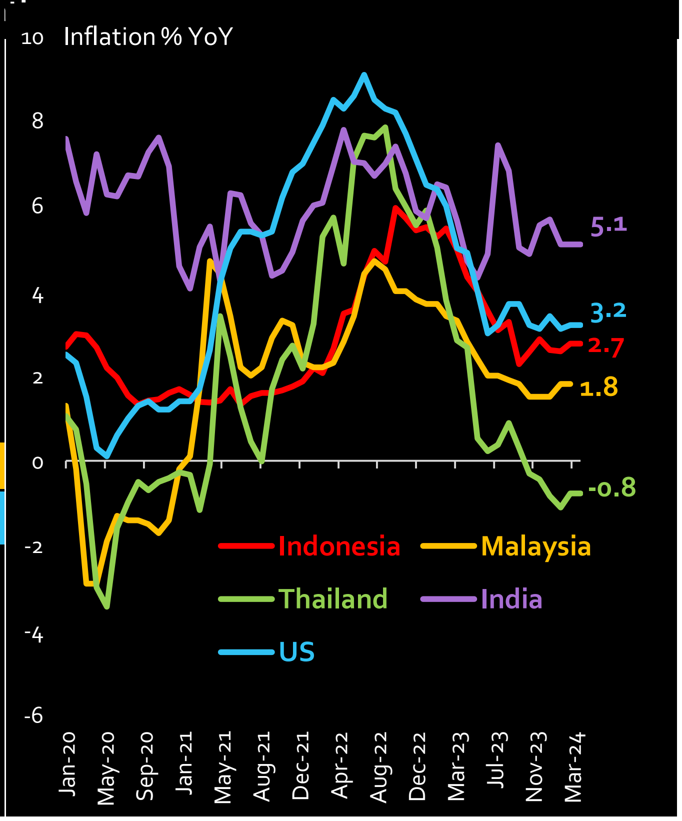




Source: Ministry of Trade, BPS

Panel 4. **Slower global disinflation is evident in the rising trend of Indonesia's imported WPI inflation**





Source: BI, Bloomberg

Selected Macroeconomic Indicators

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)
US	5.50	Dec-23	2.30
UK	5.25	Dec-23	1.85
EU	4.50	Dec-23	1.90
Japan	-0.10	Jan-16	-2.90
China (lending)	2.50	Dec-23	3.65
Korea	3.50	Nov-23	0.40
India	6.50	Dec-23	1.41
Indonesia	6.00	Nov-23	2.95

Money Mkt Rates	28-Mar	-1 mth	Chg (bps)
SPN (1M)	5.88	5.80	7.6
SUN (10Y)	6.69	6.56	12.9
INDONIA (O/N, Rp)	5.91	5.96	-5.2
JIBOR 1M (Rp)	6.65	6.64	0.8

Bank Rates (Rp)	Dec	Nov	Chg (bps)
Lending (WC)	8.86	8.91	-4.93
Deposit 1M	4.76	4.52	24.61
Savings	0.69	0.67	1.94

Currency/USD	28-Mar	-1 mth	Chg (%)
UK Pound	0.792	0.788	-0.48
Euro	0.927	0.922	-0.57
Japanese Yen	151.4	150.7	-0.45
Chinese RMB	7.227	7.198	-0.40
Indonesia Rupiah	15,855	15,630	-1.42

Capital Mkt	28-Mar	-1 mth	Chg (%)
JCI	7,288.8	7,283.8	0.07
DJIA	39,807.4	39,069.2	1.89
FTSE	7,952.6	7,684.3	3.49
Nikkei 225	40,168.1	39,233.7	2.38
Hang Seng	16,541.4	16,634.7	-0.56

Foreign portfolio ownership (Rp Tn)	Feb	Jan	Chg (Rp Tn)
Stock	3,236.2	3,115.8	120.46
Govt. Bond	837.1	841.9	-4.76
Corp. Bond	9.5	10.4	-0.89

Trade & Commodities	28-Mar	-1 mth	Chg (%)
Baltic Dry Index	1,821.0	1,871.0	-2.7
S&P GSCI Index	582.5	555.9	4.8
Oil (Brent, $/brl)	87.5	82.5	6.0
Coal ($/MT)	132.0	128.5	2.7
Gas ($/MMBtu)	1.54	1.65	-6.7
Gold ($/oz.)	2,229.9	2,031.2	9.8
Copper ($/MT)	8,766.5	8,361.5	4.8
Nickel ($/MT)	16,568.0	16,930.8	-2.1
CPO ($/MT)	905.2	834.2	8.5
Rubber ($/kg)	1.60	1.58	1.3

External Sector	Feb	Jan	Chg (%)
Export ($ bn)	19.31	20.49	-5.79
Import ($ bn)	18.44	18.49	-0.29
Trade bal. ($ bn)	0.87	2.00	-56.64
Central bank reserves ($ bn)*	144.0	145.1	-0.72

Prompt Indicators	Feb	Jan	Nov
Consumer confidence index (CCI)	123.1	125.0	123.6
Car sales (%YoY)	-18.8	-26.1	-7.5
Motorcycle sales (%YoY)	-2.9	-3.7	-2.8

Manufacturing PMI	Feb	Jan	Chg (bps)
USA	52.2	50.7	150
Eurozone	46.5	46.6	-10
Japan	47.2	48.0	-80
China	50.9	50.8	10
Korea	50.7	51.2	-50
Indonesia	52.7	52.9	-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$)	4175	3912	4350	4784	4920	5149
Consumer Price Index Inflation (% YoY)	2.7	1.7	1.9	5.5	2.6	3.2
BI 7-day Repo Rate (%)	5.00	3.75	3.50	5.50	6.00	5.50
USD/IDR Exchange Rate (end of the year)*	13,866	14,050	14,262	15,568	15,397	16.037
Trade Balance (US$ 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

* Estimated 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: 1074310

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

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