

To the edge with SRBI

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Summary

- Indonesia still enjoys net foreign capital inflows thanks to SRBI, although the SRBI-driven inflows do not seem to resonate with the Rupiah's value.
- The robust foreign demand for SRBI seems to reflect investors' demand for a higher rate rather than the improving optimism on the Indonesian market.
- An accelerated SRBI issuance may intensify the crowding-out effect from others to the SRBI market, which may compel BI to increase its presence in the SBN market.

- The short trading week due to the Juneteenth holiday the news flow from the US market and economy in the past week, but policy uncertainty remains the name of the game for the global economy. In Europe, for example, results from the recent European parliamentary election have led to French President Macron calling a snap election, joining the UK in holding a midsummer election. On the monetary policy side, two major European central banks, the Bank of England and the Swiss National Bank, have also taken sharply different policy decisions, with the BoE opting to keep its bank rate at 5.25% while the SNB leads other global central banks by cutting its policy rate by a total of 50bps (from 1.75% to 1.25%) so far in 2024.
- Given its relative size, the SNB's policy decision does not seem to have a significant effect on the global financial market. Neither does it may inspire other major central banks to follow

suit, given the different economic reality (low 1.50% YoY headline inflation and 6.83% YTD increase in CHFUSD exchange rate) Swiss central bankers faced, especially compared to their American counterparts.

- Asian financial markets may not have much to expect from the increasing rate-cut sentiment held by central bankers in Europe. For instance, the Bloomberg "Asia Dollar" index (ADXY) suffered from a 0.13% depreciation in the past week, while the lower interest rate on the CHF breath strength to the USD and the Euro. Meanwhile, the Indonesian financial market remains unable to escape from the heat wave of bad sentiment that continues to hit some of its Asian counterparts, although foreign capital outflows from the stock market seem to have moderated to a slim USD 86.4 Mn amidst the short trading days in the past week.

Toward the banks of the Rubicon

- While foreign capital outflows from the domestic stock and bond market have been a constant theme in 2024, **the Indonesian financial market still enjoys substantial net foreign capital inflows during the year, all thanks to BI’s experiment with SRBI.** Citing BI’s capital inflow data, net foreign purchases of SRBI throughout the year have now reached USD 2.26 Bn per last week, substantially higher than the USD 0.18 Bn outflows from the SBN and the stock market.
- Unfortunately, **unlike foreign capital inflows from the more traditional stock and SBN market, substantial inflows to the SRBI market do not seem to have the same positive impact on the Rupiah’s value (see Chart 1).** Indeed, the decline in the Rupiah’s value against the USD appears to have accelerated since May 2024, the period when foreign investors doubled their SRBI holdings from IDR 75.15 Tn to IDR 152.18 Tn.
- The downward trend in the USDIDR exchange rate, of course, is driven by a host of internal factors far unrelated to the SRBI, ranging from the higher external payments in Q2 2024, limited improvement in the CA outlook, and the uncertain policy outlook that is typical of a transitory period. However, given the peculiar relationship (or lack of it) between foreign purchases of SRBI and the USDIDR exchange rate, could it be that torrents of net foreign capital inflows to the SRBI market reflect a starker reading for the short-term outlook of the Rupiah’s value?

“The higher tax on SRBI returns and the depreciating Rupiah means that foreign demand for SRBI may be driven by factors other than its higher yield”

- The answer stems from the original design of the instrument itself. **As a liquidity absorption tool, BI has been adding supply to the supply of SRBI in congruence with the ebb and flow in the IDR’s value,** expanding when the Rupiah weakens and vice versa (*see Chart 2*). Hence, the central bank’s decision to issue more SRBI and let foreign investors accumulate around USD 2.74 Bn of the instrument since May 2024 may highlight the intensifying challenge faced by BI to stabilise the Rupiah during the period, rather than a vote of confidence from foreign investors on the attractiveness of the Indonesian financial market.

▪ But why do foreign investors seem eager to buy more SRBI? Our main thesis is that SRBI provides a way for foreign investors to avoid short-term volatility in the Indonesian market. Higher real interest rate differentials between SRBI and its corresponding US short-term debt securities (compared to the longer-tailed segment of the market) further highlight SRBI’s advantage over other Rupiah assets. However, given the higher tax on SRBI returns (20% compared to 10% for SBN) and the lower dollar returns due to the -6.7% YTD decline in the Rupiah’s value, we ponder whether the high foreign demand for SRBI may stretch beyond the calculus of profits and losses.

- Indeed, we argue that apart from its relatively attractive features, **the recent spike in foreign interest in SRBI may also stem from foreign investors’ demand for a higher policy rate in**

Indonesia. SRBI, of course, is a costly tool (although, is not as costly as its FX-denominated siblings SVBI/SUVBI), meaning that reliance on SRBI may lead to higher costs the central bank would need to bear to stabilise the Rupiah. The higher cost of defending the Rupiah using SRBI (and other form of market operations) may thus lead to the speculation that BI may eventually need to taper the supply of SRBI in the market, explaining the recent spike in foreign capital inflows to the SRBI market.

- Whether BI can continue to rely on SRBI to stabilise the Rupiah is not only a function of the central bank's ability to bear the higher policy costs. **The decision to issue more SRBI may also be considered in the context of its connection with the SBN market**, given that a higher SRBI issuance may continue to crowd out foreign investors to the SRBI market thus exacerbating the sell-off pressure in the SBN market.
- This crowding-out effect from the SBN to the SRBI market is more visible when we observe the change in banks' placement of their IDR liquidity. Unlike foreign investors, who sell SBN outright to free up the liquidity to buy SRBI, **banks have insofar opted to reduce the use of other BI instruments to facilitate their SBN purchases.** The now lower utilisation of BI instruments outside of SRBI, including reverse repo, thus far keeps BI's gross ownership of SBN stable (*see Chart 3*), reducing the concern of debt monetisation.
- The problem, however, may potentially arise if the central bank doubles down on SRBI as the

primary tool to protect the Rupiah's value. **The depleted SBN used in monetary operations may force banks to follow foreign investors' path, selling SBN outright to free up liquidity to purchase more SRBI.** BI may thus eventually find itself on the bank of the Rubicon; either the central bank crosses the river by continuing to issue more SRBI and simultaneously increasing its presence in the SBN market, thus vindicating the debt monetisation concern.

- Alternatively, similar to what happened in October 2023, **the higher cost of market interventions may encourage BI to turn around and opt for a more conservative measure to stabilise the Rupiah's value**, letting the yield on SBN float closer to yields offered by SRBI being one of the examples. These costs and market signalling considerations mean that there remains a limit to how far BI could rely on SRBI as the primary tool to defend the Rupiah, leading us to maintain our call on the possibility of a further adjustment to the BI rate should the uncertain global monetary policy landscape and the weakening domestic growth impulse continue to put downward pressure on the Rupiah.

"Costs and market signalling concerns may limit BI's ability to rely on SRBI as its primary exchange rate stabilisation tool"

Chart 1

More inflows, less protection

Net capital inflows to the Indonesian financial market due to SRBI do not stop the IDR from its ongoing downward trend

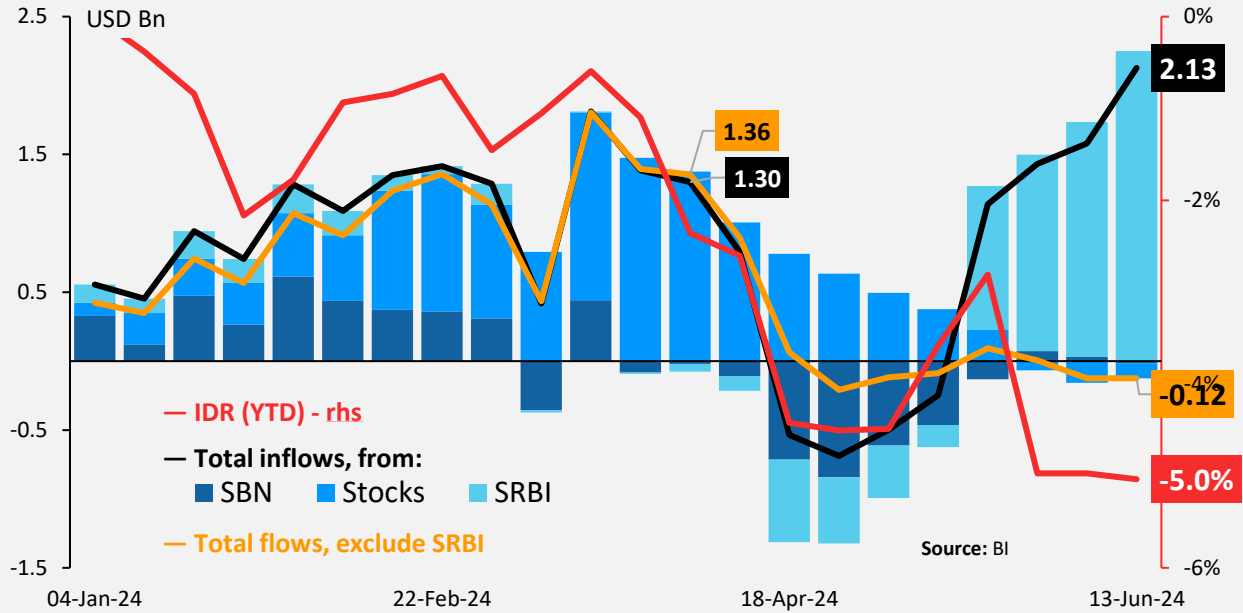


Chart 2

Goes where the Rupiah goes

Apart from its early auctions, SRBI issuances have largely followed the ebb and follow in the USDIDR's exchange rate

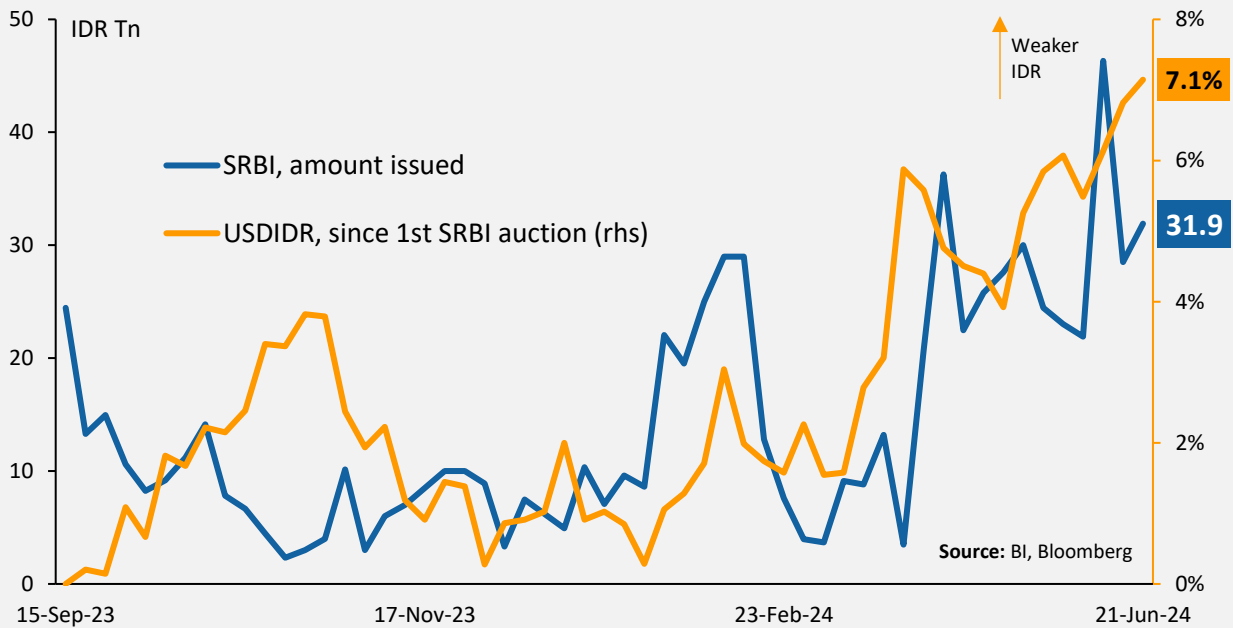
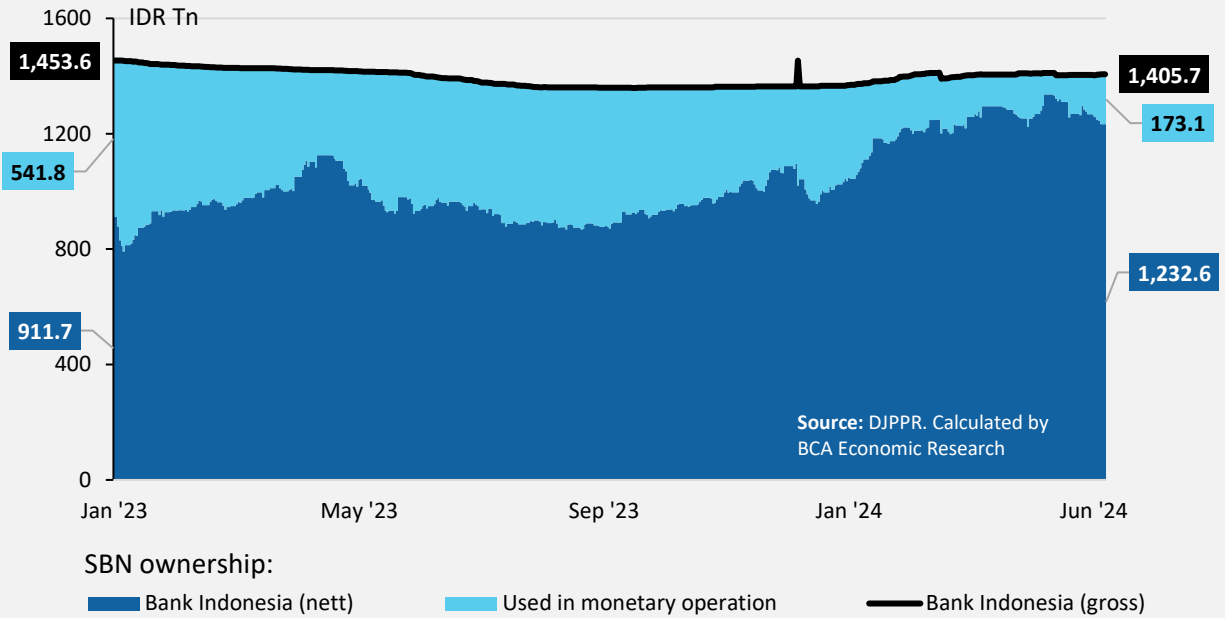


Chart 3

No to debt monetisation

BI's gross ownership of SBN has not change much as banks move from RR to SRBI, but further SRBI issuance may justify BI purchasing more SBN outright



Economic Calendar				
		Actual	Previous	Forecast*
11 June 2024				
ID	Retail Sales YoY, %	-2.7	9.3	11
ID	Car Sales YoY, %	-13.3	-17.5	-
12 June 2024				
CN	Inflation rate YoY, %	0.3	0.3	0.2
US	Inflation rate YoY, %	3.3	3.4	3.4
ID	Motorbike Sales YoY, %	-4.5	-2.5	-
13 June 2024				
US	Fed Interest Rate Decision, %	5.5	5.5	5.5
14 June 2024				
EU	Balance of Trade, (Bn)	15	23.7	16.0
17 June 2024				
CN	Retail Sales YoY, %	3.7	2.3	2.6
CN	Unemployment Rate, %	5	5	5
18 June 2024				
EU	Inflation rate YoY, %	2.6	2.4	2.6
US	Retail Sales YoY, %	2.3	3	2.8
19 June 2024				
ID	Balance of Trade, (Bn)	2.93	2.72	2.5
20 June 2024				
ID	Interest Rate Decision, %	6.25	6.25	6.25
01 July 2024				
ID	S&P Global Manufacturing PMI (Bn)		52.1	51
ID	Inflation rate YoY, %		2.84	2.26
02 July 2024				
US	JOLTs Job Openings, (Mn)		8.05	-
EU	Inflation rate YoY, %		2.6	2.4
EU	Unemployment Rate, %		6.4	-
3 July 2024				
US	Balance of Trade, (Bn)		-74.6	-
05 July 2024				
ID	Foreign Exchange Reserves, (Bn)		139	148
US	Unemployment Rate, %		4	4
US	Non Farm Payrolls, (Th)		272	160

*Forecasts of some indicators are simply based on market consensus

Bold indicates indicators covered by the BCA Monthly Economic Briefing report

Selected Macroeconomic Indicator

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)	Trade & Commodities	24-Jun	-1 mth	Chg (%)
US	5.50	Jul-23	2.20	Baltic Dry Index	1,973.0	1,797.0	9.8
UK	5.25	Aug-23	3.25	S&P GSCI Index	582.2	581.7	0.1
EU	4.25	Jul-23	1.65	Oil (Brent, \$/brl)	86.0	82.1	4.7
Japan	-0.10	Jan-16	-2.90	Coal (\$/MT)	139.2	146.7	-5.1
China (lending)	2.50	Aug-23	4.05	Gas (\$/MMBtu)	2.58	2.22	16.2
Korea	3.50	Jan-23	0.80	Gold (\$/oz.)	2,334.7	2,333.8	0.0
India	6.50	Feb-23	1.75	Copper (\$/MT)	9,513.3	10,204.6	-6.8
Indonesia	6.25	Apr-24	3.41	Nickel (\$/MT)	17,060.5	20,018.5	-14.8
				CPO (\$/MT)	837.5	829.4	1.0
				Rubber (\$/kg)	1.68	1.73	-2.9
Money Mkt Rates	24-Jun	-1 mth	Chg (bps)	External Sector	May	Apr	Chg (%)
SPN (1M)	5.88	5.80	7.6	Export (\$ bn)	22.33	19.62	13.82
SUN (10Y)	7.09	6.86	22.9	Import (\$ bn)	19.40	16.90	14.82
INDONIA (O/N, Rp)	6.05	6.11	-6.4	Trade bal. (\$ bn)	2.93	2.72	7.61
JIBOR 1M (Rp)	6.90	6.90	0.0	Central bank reserves (\$ bn)*	139.0	136.2	2.04
Bank Rates (Rp)	Mar	Feb	Chg (bps)	Prompt Indicators	May	Apr	Mar
Lending (WC)	8.83	8.84	-1.69	Consumer confidence index (CCI)	125.2	127.7	123.8
Deposit 1M	4.62	4.62	-0.76	Car sales (%YoY)	-13.3	-17.5	-26.2
Savings	0.68	0.67	0.26	Motorcycle sales (%YoY)	-4.5	18.3	-7.8
Currency/USD	24-Jun	-1 mth	Chg (%)	Manufacturing PMI	May	Apr	Chg (bps)
UK Pound	0.788	0.785	-0.40	USA	51.3	50.0	130
Euro	0.932	0.922	-1.05	Eurozone	47.3	45.7	160
Japanese Yen	159.6	157.0	-1.65	Japan	50.4	49.6	80
Chinese RMB	7.259	7.244	-0.22	China	51.7	51.4	30
Indonesia Rupiah	16,394	15,993	-2.45	Korea	51.6	49.4	220
				Indonesia	52.1	52.9	-80
Capital Mkt	24-Jun	-1 mth	Chg (%)				
JCI	6,889.2	7,222.4	-4.61				
DJIA	39,411.2	39,069.6	0.87				
FTSE	8,281.6	8,317.6	-0.43				
Nikkei 225	38,804.7	38,646.1	0.41				
Hang Seng	18,027.7	18,608.9	-3.12				
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 an earlier period

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

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

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

*Estimation of the Rupiah's fundamental exchange rate

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