

BI Policy:

A waiting period

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Executive Summary

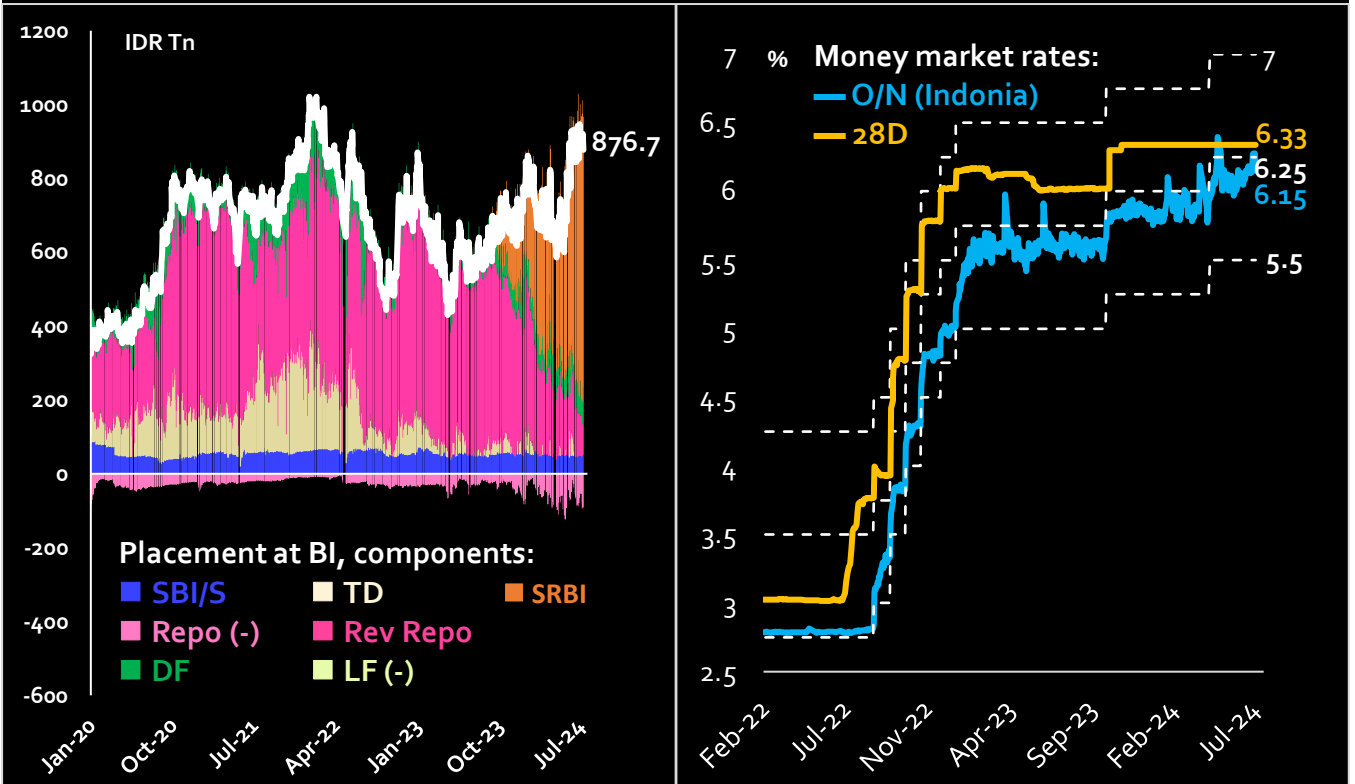
- BI has kept the BI7DRR at 6.25%, following the slight recovery of the Rupiah throughout the month.
- But compared to the beginning of the year, the Rupiah remains relatively weak due to the widening deficit in the saving-investment gap.
- BI is likely to adopt a more cautious approach towards rate cuts, as declining commodity prices makes Indonesia more vulnerable to capital market fluctuations.
- Timeline of Fed cuts is still highly uncertain and will depend on developments in US politics and macro data.

- Bank Indonesia (BI) has maintained its benchmark rate (BI7DRR) at 6.25%. This decision was widely anticipated following the strengthening of the Rupiah throughout the month due to signs of a weakening US economy.
- However, the Rupiah continues to remain relatively weak compared to the beginning of the year, and this is likely due to fiscal issues rather than monetary ones. As we wrote in a recent report, the deficit in our domestic net bank balance (NBB) was a key factor behind Rupiah's weakness. In turn, this was driven by robust government spending, strong loan growth in the SME segment, and high corporate CAPEX despite slowing domestic growth and exports. Unfortunately, there are no signs that the NBB would reverse soon, given the still-strong private sector expansion and stable credit growth at 12.36% YoY in Jun-24.
- The best way to shift the NBB into surplus is for the government to issue bonds at attractive enough yields for foreign investors, which would also ease the "crowding out" problem as retail investors absorb a larger share of SBN. Unfortunately, this may entail higher rates on the long-end ("bear steepening"), which BI has been keen to avoid as seen from its recent market operations (issuing short-term SRBI, acquiring long-term SBN).
- In theory, then, higher long-term yields could allow BI to reduce its short-term yields, including the BI Rate. But this is not the only bar that has to be cleared. While developed nations have begun to cut rates ahead of the Fed (at the cost of weaker exchange rate), Indonesia does not have quite the same flexibility.
- Similar dilemmas are faced by Indonesia's peer countries, although there are indications that they are becoming more comfortable easing before the Fed. For instance, the central bank governor of the Philippines recently suggested that a rate cut in August is still on the table. However, we anticipate that BI will adopt a more conservative approach, since growing weakness in the commodity market makes Indonesia even more vulnerable to capital market

fluctuations. As such, BI will likely wait for the Fed to cut rates first before committing to its own rate cut.

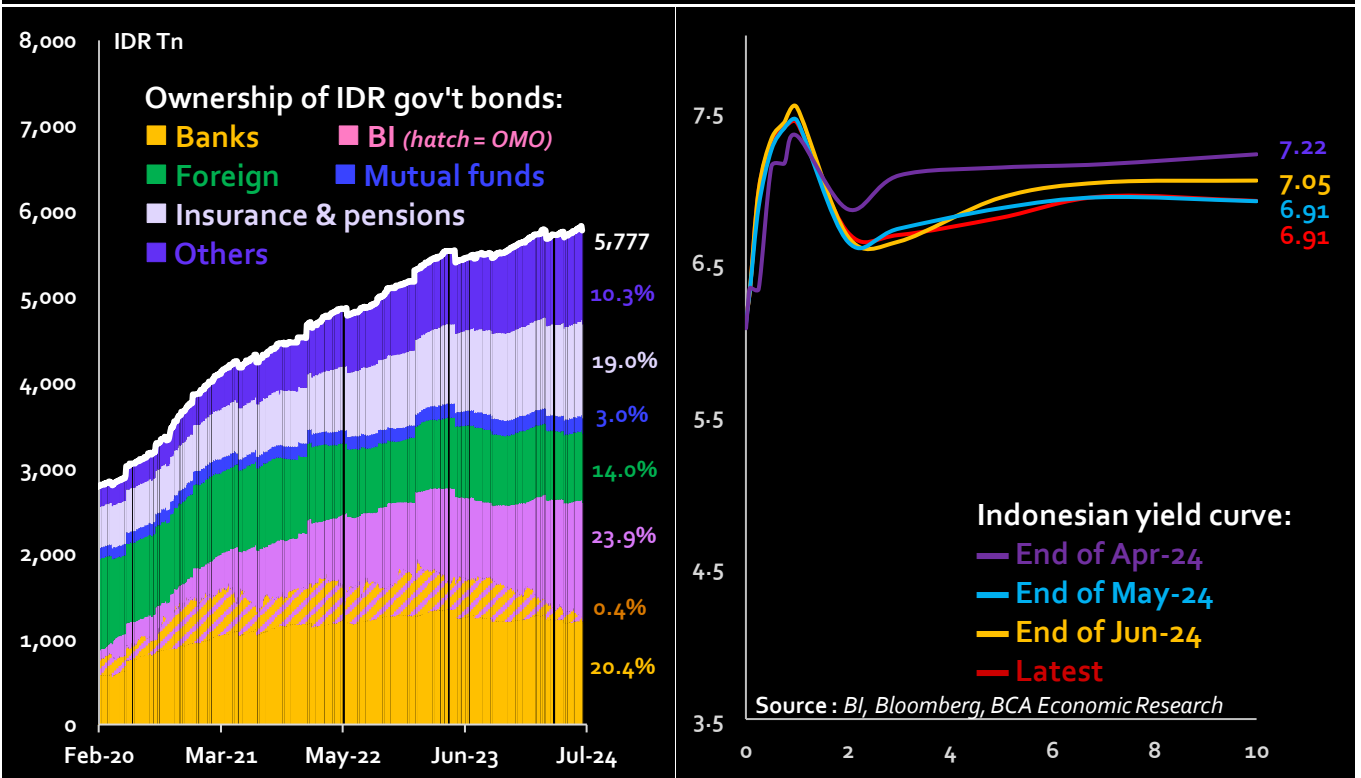
- And the Fed's timeline itself is still highly uncertain. Despite recent comments from Fed Chair Jerome Powell acknowledging that the job market has "cooled considerably", the market is still not entirely convinced about a rate cut in September. Indeed, the Fed fund futures for the end of Sep-24 have remained stable around the 5.2% range in recent weeks.
- Additionally, a rate cut before the US election in November could be perceived as politically motivated. Neither is the weakening trajectory of the US economy a one-way street. The latest estimates from GDPNow showed Q2 growth at a still-robust 2.5% growth (QoQ SAAR). This third quarter, then, is set to be a tense waiting period, where the market anxiously awaits every new development in US politics and macro data.

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



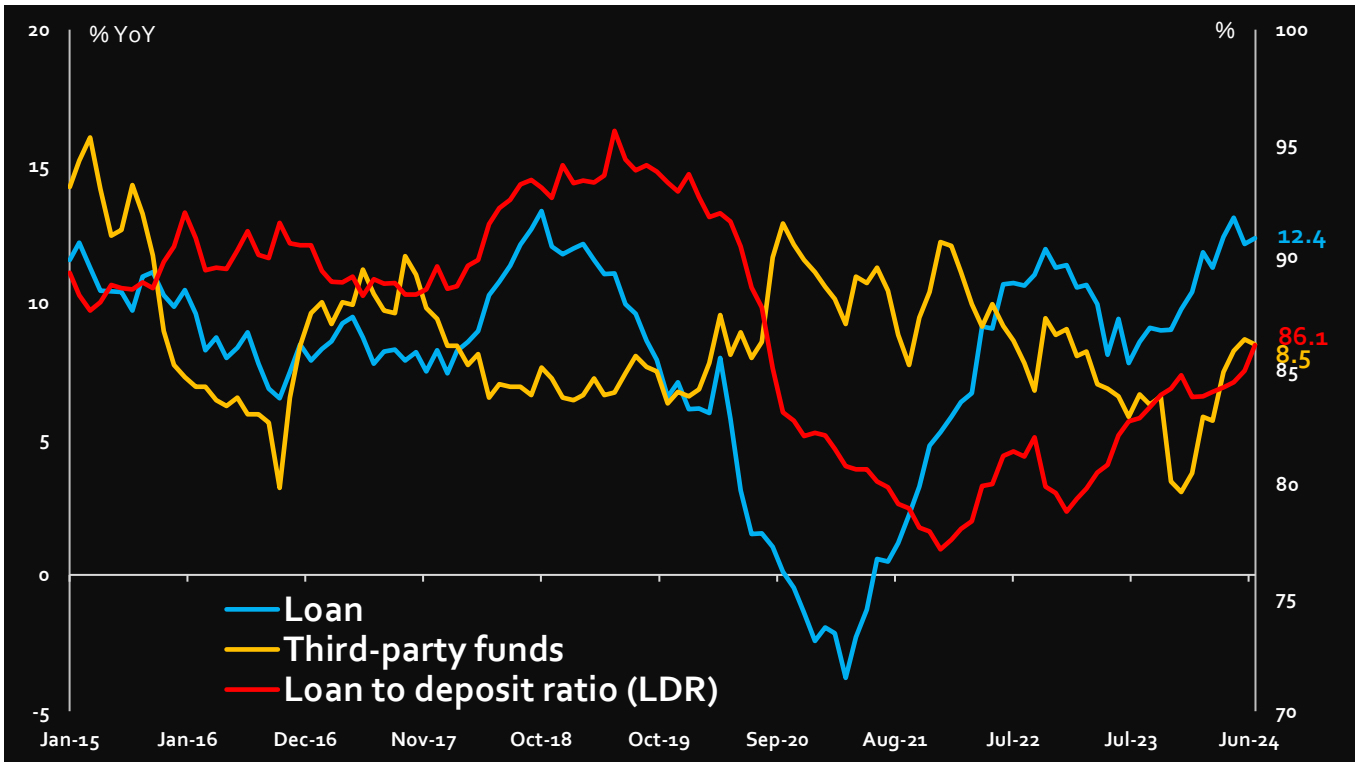
Source: BI, Bloomberg, BCA Economist

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



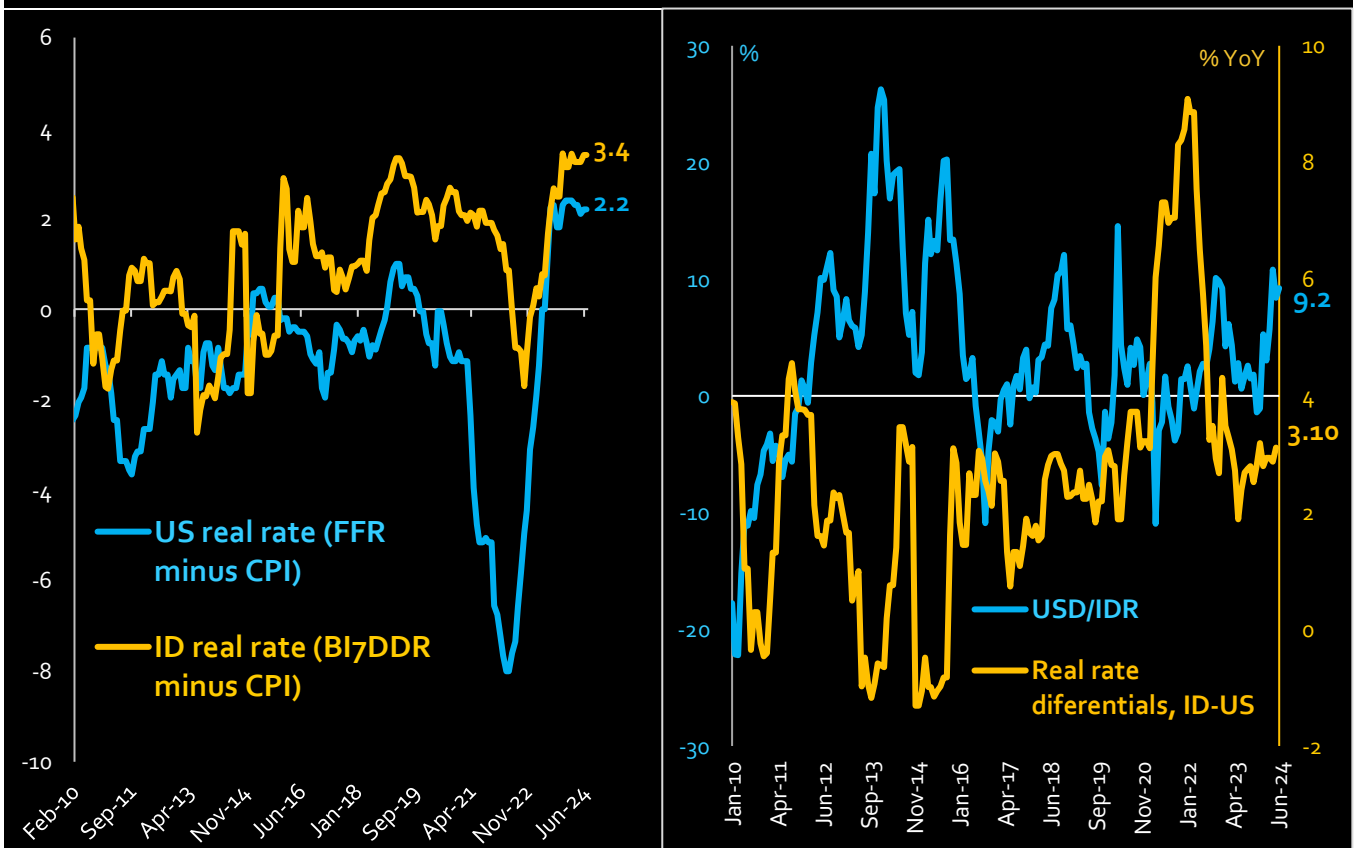
Source: MoF, BI, Bloomberg, BCA Economist

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



Source: MoF, Bloomberg, BCA Economist

Panel 4. The IDR posted a slight recovery, but it is still at a much weaker level compared to the beginning of the year



Source: BI, Bloomberg, BCA Economist

Selected Macroeconomic Indicators

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)	Trade & Commodities	16-Jul	-1 mth	Chg (%)
US	5.50	Jul-23	2.50	Baltic Dry Index	1,942.0	1,948.0	-0.3
UK	5.25	Aug-23	3.25	S&P GSCI Index	564.2	575.1	-1.9
EU	4.25	Jul-23	1.75	Oil (Brent, \$/bbl)	83.7	82.6	1.3
Japan	-0.10	Jan-16	-2.90	Coal (\$/MT)	138.3	138.5	-0.2
China (lending)	2.50	Aug-23	4.15	Gas (\$/MMBtu)	2.10	2.74	-23.4
Korea	3.50	Jan-23	1.10	Gold (\$/oz.)	2,469.1	2,333.0	5.8
India	6.50	Feb-23	1.42	Copper (\$/MT)	9,505.3	9,615.5	-1.1
Indonesia	6.25	Apr-24	3.74	Nickel (\$/MT)	16,304.4	17,328.2	-5.9
				CPO (\$/MT)	852.6	837.4	1.8
				Rubber (\$/kg)	1.64	1.74	-5.7
Money Mkt Rates	16-Jul	-1 mth	Chg (bps)	External Sector	Jun	May	Chg (%)
SPN (1M)	5.88	5.80	7.6	Export (\$ bn)	20.84	22.33	-6.66
SUN (10Y)	6.94	7.17	-22.5	Import (\$ bn)	18.45	19.40	-4.89
INDONIA (O/N, Rp)	6.15	6.15	-0.1	Trade bal. (\$ bn)	2.39	2.93	-18.36
JIBOR 1M (Rp)	6.90	6.90	0.0	Central bank reserves (\$ bn)*	140.2	139.0	0.87
Bank Rates (Rp)	Apr	Mar	Chg (bps)	Prompt Indicators	Jun	May	Apr
Lending (WC)	8.85	8.83	2.01	Consumer confidence index (CCI)	123.3	125.2	127.7
Deposit 1M	4.65	4.62	3.47	Car sales (%YoY)	-11.8	-13.2	-17.4
Savings	0.68	0.68	0.22	Motorcycle sales (%YoY)	3.5	-4.5	18.3
Currency/USD	16-Jul	-1 mth	Chg (%)	Manufacturing PMI	Jun	May	Chg (bps)
UK Pound	0.771	0.788	2.26	USA	51.6	51.3	30
Euro	0.918	0.934	1.83	Eurozone	45.8	47.3	-150
Japanese Yen	158.4	157.4	-0.60	Japan	50.0	50.4	-40
Chinese RMB	7.269	7.256	-0.18	China	51.8	51.7	10
Indonesia Rupiah	16,180	16,400	1.36	Korea	52.0	51.6	40
Capital Mkt	16-Jul	-1 mth	Chg (%)	Indonesia	50.7	52.1	-140
JCI	7,224.3	6,734.8	7.27				
DJIA	40,954.5	38,589.2	6.13				
FTSE	8,164.9	8,146.9	0.22				
Nikkei 225	41,275.1	38,814.6	6.34				
Hang Seng	17,728.0	17,941.8	-1.19				
Foreign portfolio ownership (Rp Tn)	Jun	May	Chg (Rp Tn)				
Stock	3,273.1	3,115.0	158.05				
Govt. Bond	805.6	807.0	-1.38				
Corp. Bond	8.2	8.2	-0.06				

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	6.25
USD/IDR Exchange Rate (end of the year)*	13,866	14,050	14,262	15,568	15,397	16,218
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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