

CPI: A Tug of War

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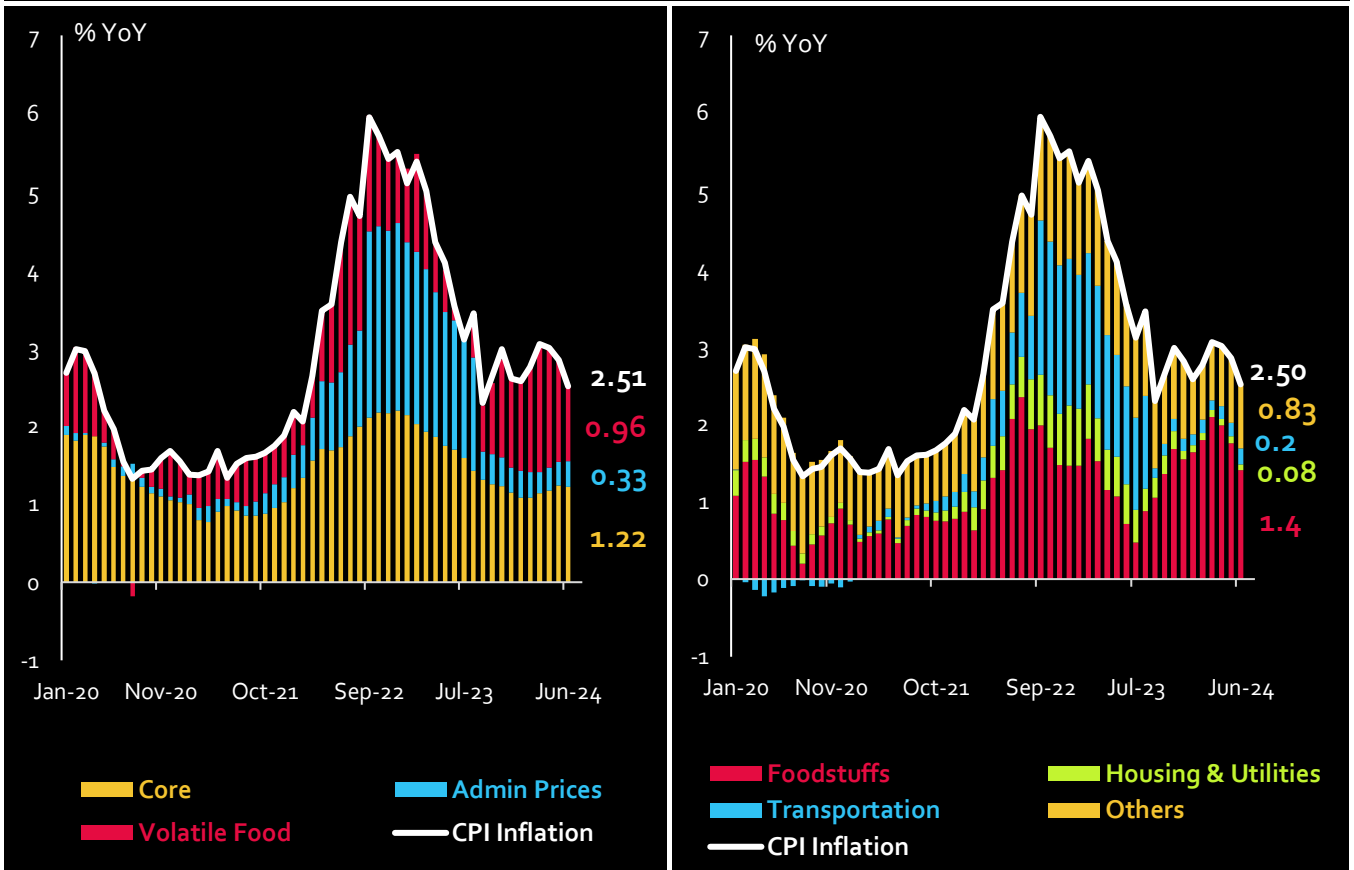
Executive Summary

- Indonesia's inflation further slowed down to 2.51% YoY in May (-0.08% MoM), with foodstuffs deflation led by chicken and shallots. However, food inflation remains a risk going forward with rice being the primary risk.
 - While import prices are pulling core inflation upward, weaker consumer demand may be pulling things in the opposite direction.
 - Low inflation and weak consumption dissuade BI against hiking rates, but possibility of 25 bps hike remains in the event of extreme pressure on Rupiah.
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- Annual inflation slowed down further to 2.51% YoY in June, with a deflation of 0.08% MoM (the second consecutive month of deflation). Foodstuffs deflation – for the third straight month – was the main driver behind this slowdown, and June saw the sharpest deflation yet.
 - This was dominated by chicken and shallots, with the latter benefiting from a bumper harvest season (“panen raya”). And while the price of chilis did rise at the same time, it did not add too much to inflation with rice prices still relatively stable after recent harvests.
 - Core inflation slightly increased in monthly terms (0.1% MoM) but declined annually (from 1.93% to 1.90% YoY). Unlike previously, gold was not a major contributor to core inflation as gold prices stabilized at the global level.
 - Imported items, on the other hand, may be a major driver considering Rupiah depreciation in recent months. While imported WPI softened in May (during which the Rupiah did strengthen slightly), the trend for imported inflation remains upwards, and it is very possible that the acceleration would resume in June.
 - If, as we surmise, import prices are pulling core inflation upwards, then there might be an opposite force downwards – namely slowing consumer demand – that is keeping core inflation relatively stable. Our Big Data flags a decline in consumer spending in June, following a slight rebound in May.
 - Overall, Q2 consumption numbers are likely to underperform versus Q1, which benefited from social spending and rice imports around the Elections. But would Q3 see a rebound, or just a continuation of this slowing trend?
 - Food inflation may, once more, hold the key. Despite food deflation in Q2, worries about rice production persists as the turn towards cooler, wetter La Nina conditions is happening more slowly than expected. Indeed, this is one rationale behind the recent increase of maximum

retail price (*harga eceran tertinggi* or HET) of rice, which is to incentivize rice production amid rising risks and thinning margins.

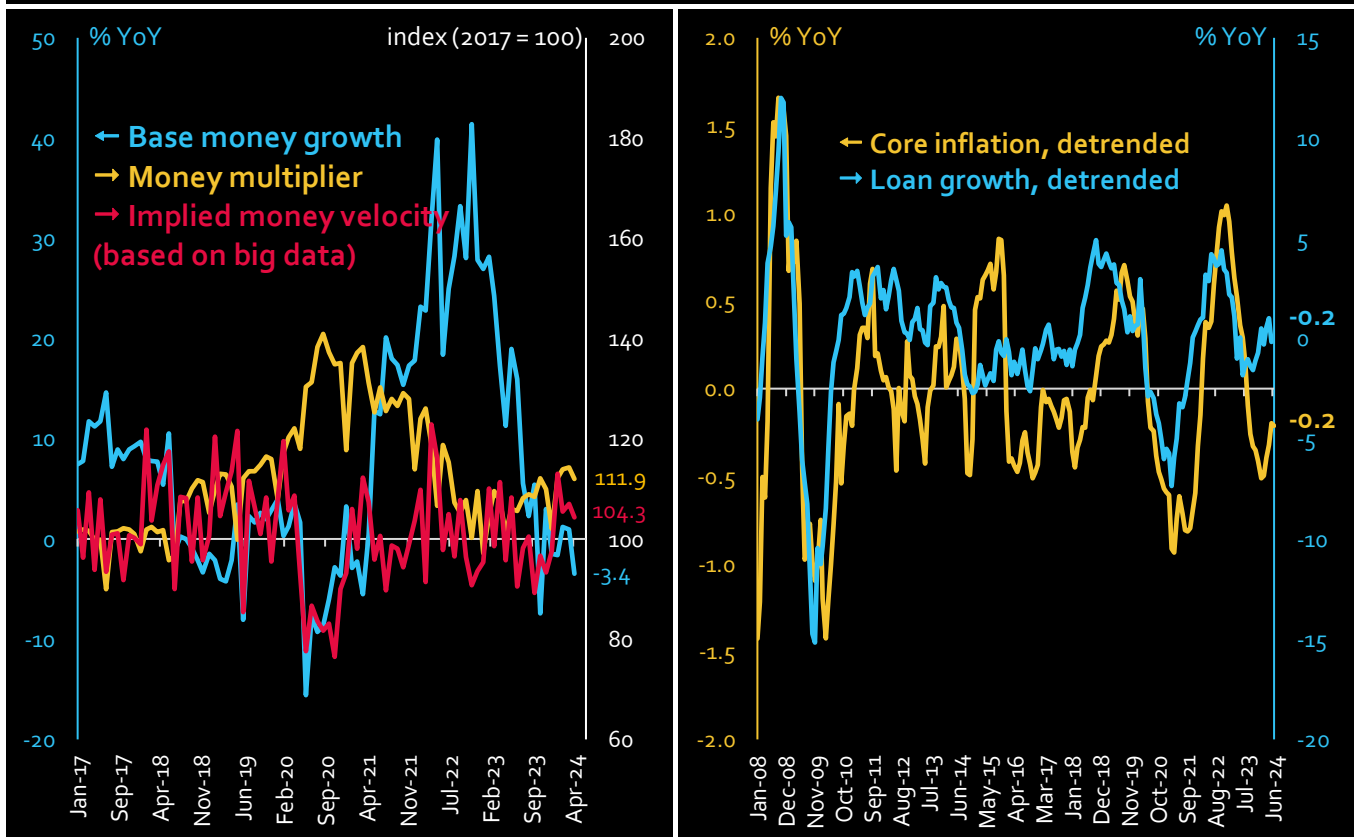
- In addition to rice, there is also the perennial worry of tuition fee inflation (around Jul-Aug), as well as the increase in oil price amid recent escalation in the Middle Eastern conflict (this time, involving Lebanon).
- Still, while there were rumors that the government would raise fuel prices in accordance with weaker Rupiah and higher oil prices, the latest MoF presscon did not give any indication of such a plan, and (at least for 2024) the extra fuel subsidy burden remains manageable.
- There is also continuing uncertainty on trade policies, as the government vacillated between import restriction (Permendag 36/2023) and relaxation (Permendag 8/2024). In recent days, there has been rumors about a new safeguard tariff of up to 200% against an influx of items such as clothing, steel, and textiles coming from China. This uncertainty could, in itself, add to the cost of doing business for importers.
- The low inflation and potentially weakening consumption should dissuade BI against hiking rates, and yet the possibility of 25 bps hike at some point in the next six months remains (if only very slightly) alive in the event of extreme pressures on the Rupiah.
- Nonetheless, we are sharply downgrading the chances of such a hike for several additional reasons. With US inflation and growth momentum on a downward trajectory and Trump now emerging as clear favorite for the November election, the upside for the Dollar may not be as high as it had been.
- Furthermore, we view it as inevitable that the government would issue more bonds in H2, given its limited cash balances by the end of May. Extra FX liquidity from global/Euro bonds could add extra steel to BI's reserve cushion. In this scenario, a stronger Rupiah does not require an increase in short-term rates, but rather long-term yields – which may be fine if long-term UST yields continue to inch downwards.

Panel 1. Food inflation experienced another slowdown, while core inflation remains stable



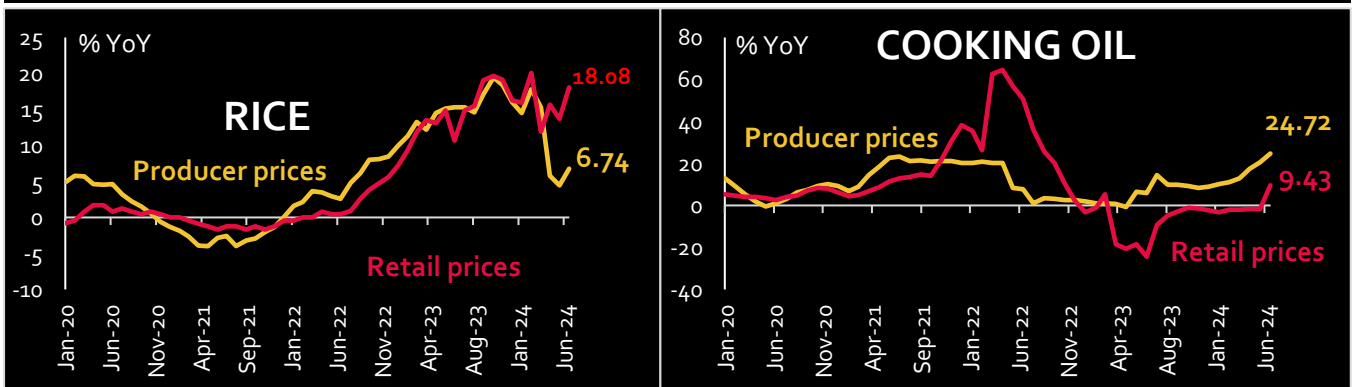
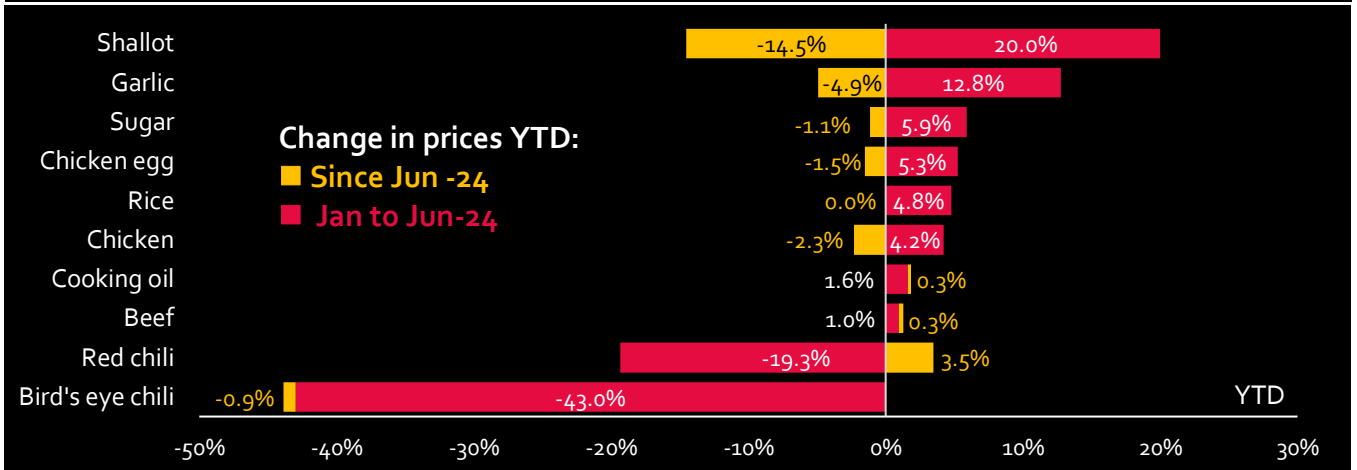
Source: BPS, calculation by BCA Economic Research

Panel 2. Strong loan growth may start to raise core inflation



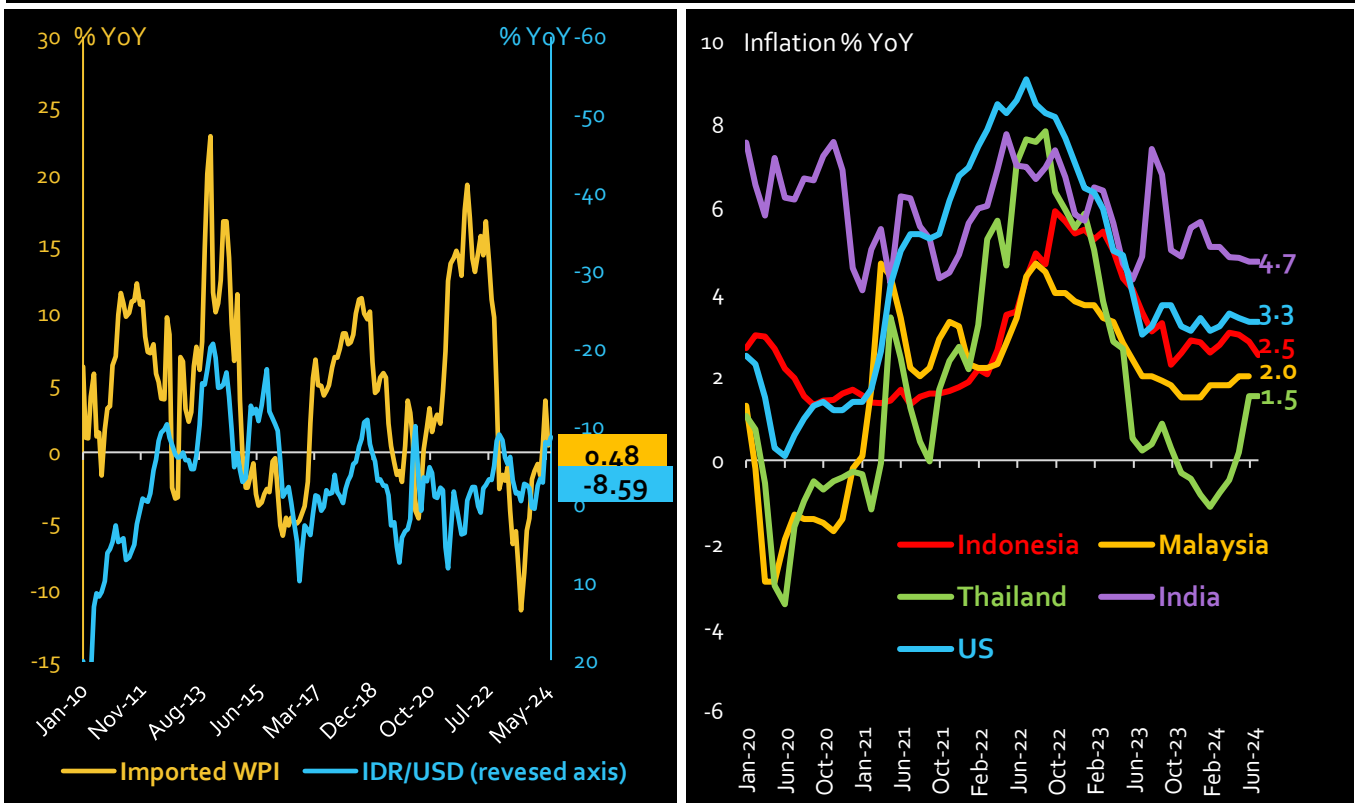
Source: BI, OJK, BCA big data, calculation by BCA Economic Research

Panel 3. Rice prices remain stable while shallots price decrease due to harvest season



Source: Ministry of Trade, BPS

Panel 4. Imported inflation might goes up again because of Rupiah's weakening



Source: BI, Bloomberg

Selected Macroeconomic Indicators

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)	Trade & Commodities	28-Jun	-1 mth	Chg (%)
US	5.50	Jul-23	2.20	Baltic Dry Index	2,050.0	1,784.0	14.9
UK	5.25	Aug-23	3.25	S&P GSCI Index	578.4	592.4	-2.4
EU	4.25	Jul-23	1.65	Oil (Brent, \$/bbl)	86.4	84.2	2.6
Japan	-0.10	Jan-16	-2.90	Coal (\$/MT)	133.2	142.0	-6.2
China (lending)	2.50	Aug-23	4.05	Gas (\$/MMBtu)	2.55	2.29	11.4
Korea	3.50	Jan-23	0.80	Gold (\$/oz.)	2,326.8	2,361.3	-1.5
India	6.50	Feb-23	1.75	Copper (\$/MT)	9,456.0	10,380.8	-8.9
Indonesia	6.25	Apr-24	3.74	Nickel (\$/MT)	17,040.2	20,217.7	-15.7
Money Mkt Rates	28-Jun	-1 mth	Chg (bps)				
SPN (1M)	5.88	5.80	7.6	CPO (\$/MT)	847.0	839.6	0.9
SUN (10Y)	7.05	6.86	18.7	Rubber (\$/kg)	1.66	1.77	-6.2
Bank Rates (Rp)	Apr	Mar	Chg (bps)	External Sector	May	Apr	Chg (%)
Lending (WC)	8.85	8.83	2.01	Export (\$ bn)	22.33	19.62	13.82
Deposit 1M	4.65	4.62	3.47	Import (\$ bn)	19.40	16.90	14.82
Savings	0.68	0.68	0.22	Trade bal. (\$ bn)	2.93	2.72	7.61
Currency/USD	28-Jun	-1 mth	Chg (%)	Central bank reserves (\$ bn)*	139.0	136.2	2.04
UK Pound	0.791	0.784	-0.92	Prompt Indicators	May	Apr	Mar
Euro	0.933	0.921	-1.33	Consumer confidence index (CCI)	125.2	127.7	123.8
Japanese Yen	160.9	157.2	-2.31	Car sales (%YoY)	-13.3	-17.5	-26.2
Chinese RMB	7.267	7.244	-0.32	Motorcycle sales (%YoY)	-4.5	18.3	-7.8
Indonesia Rupiah	16,375	16,090	-1.74	Manufacturing PMI	Jun	May	Chg (bps)
Capital Mkt	28-Jun	-1 mth	Chg (%)	USA	51.7	51.3	40
JCI	7,063.6	7,253.6	-2.62	Eurozone	45.6	47.3	-170
DJIA	39,118.9	38,852.9	0.68	Japan	50.0	50.4	-40
FTSE	8,164.1	8,254.2	-1.09	China	51.8	51.7	10
Nikkei 225	39,583.1	38,855.4	1.87	Korea	52.0	51.6	40
Hang Seng	17,718.6	18,821.2	-5.86	Indonesia	50.7	52.1	-140
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				

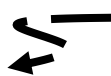
Source: Bloomberg, BI, BPS

Notes:

*Data from 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	6.50
USD/IDR Exchange Rate (end of 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

* Estimated Number

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