FX Reserves: A tricky maneuver

08 Aug 2024

Nicholas Husni
Economist/Analyst

Barra Kukuh Mamia
Senior Economist

Executive Summary

- Bank Indonesia's FX reserves increased by USD 5.2 Bn to USD 145.4 Bn in July 2024, driven by a combination of net global bond issuance, inflows to SRBI, and inflows into equities and secondary bond markets.
- Bank Indonesia issued another USD 8.6 billion of SRBI in July 2024, with around 30% of them bought by foreign investors.
- The recent unwinding of Yen carry trade has led to a global sell-off in risk assets, causing a setback for stocks, but a surge of inflows into government bonds (SBN).
- Bank Indonesia's continued issuance of SRBI is now being supported by repo lending to banks, but this eventually would have to be normalized as pressure on Rupiah subsides.

- Bank Indonesia's FX reserves saw a strong increase of USD 5.2 Bn in July, to USD 145.4 Bn. The surge was due to a combination of net global bond issuance (USD 1.26 Bn), inflows to SRBI (USD 2.6 Bn), and inflows into equities and secondary bond markets totaling USD 0.7 Bn.

- Bank Indonesia continued to issue large amounts of SRBI, totaling USD 8.6 Bn in July. About 30% of these recently-issued SRBI were bought by foreigners, raising foreign ownership of the instrument to about 28%. This increased demand allowed for lower SRBI yields, while coupons on the newly-issued global bond series were also ~30 bps lower compared to last year's issuance.

- July, of course, were a favorable month for Indonesian (and global) markets, as expectations of Fed rate cuts ratcheted up. But August has been a different story entirely. The diverging trajectories of US and Japanese rates (after a surprising 15 bps hike by the Bank of Japan) had unwound the Yen carry trade, which led to a dramatic sell-off in risk assets across the globe. For Indonesia, this meant a setback to stocks, but there has been a silver lining in the form of inflows into government bonds (SBN), amounting to USD 0.25 Bn in the first week of August.

- The sharp increase in reserves and favorable conditions (so far) for bonds support our bullish turn towards Rupiah since late June/early July. The higher amount of banks' FX placement at BI (particularly FX swaps) also indicates that FX liquidity among the private sector has been improving.

- Part of this improvement might be attributable to the mini-commodity boom in Q2, even though metal prices had since slumped. It is also possible that companies are becoming more cautious and opt to conserve their FX liquidity, rather than using it for import or CAPEX. The waning CAPEX cycle, as such, should serve as a positive for Rupiah despite its negative impact on growth.

- With everything seemingly going well for the Rupiah, then, why does BI continue issuing SRBI at high volumes? Since May, BI has issued IDR 140 – 160 Bn (net) each month, of which about 25 – 30% have been absorbed by foreign investors. Much of the remainder, however, has had to be bought by banks, further contributing to the tightening liquidity that banks experience due to strong loan growth (vis-à-vis deposits).

- Last month, we argued that BI may have to slow down net SRBI issuance, since banks are increasingly having to finance their purchase of SRBI by unwinding their reverse repo with BI, which had dwindled to less than IDR 100 Tn by mid-July. Further SRBI issuance may force BI to choose between letting SBN yields rise or neutralizing it by buying SBN outright.

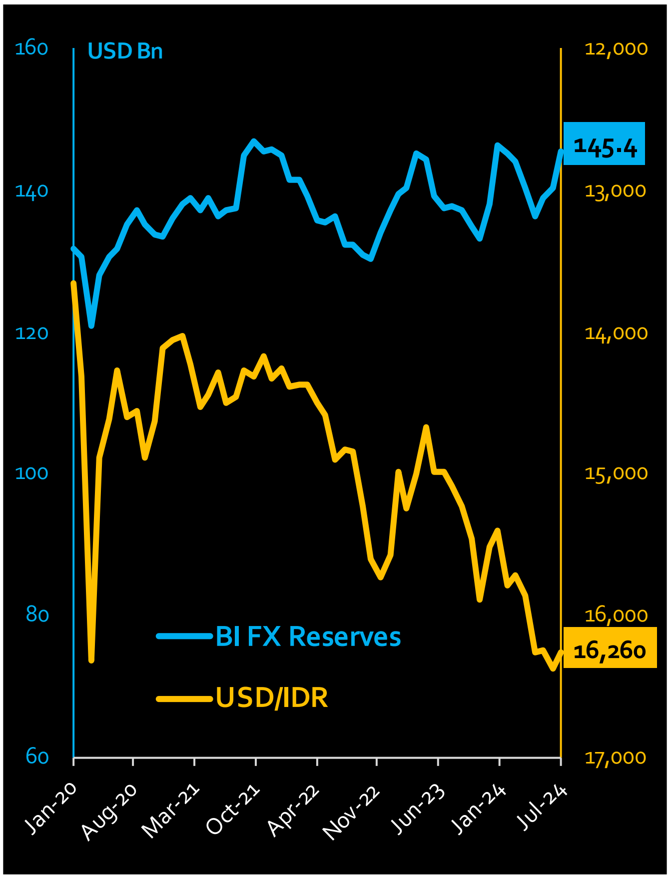
"Strong foreign demand has allowed for a lower SRBI yield"

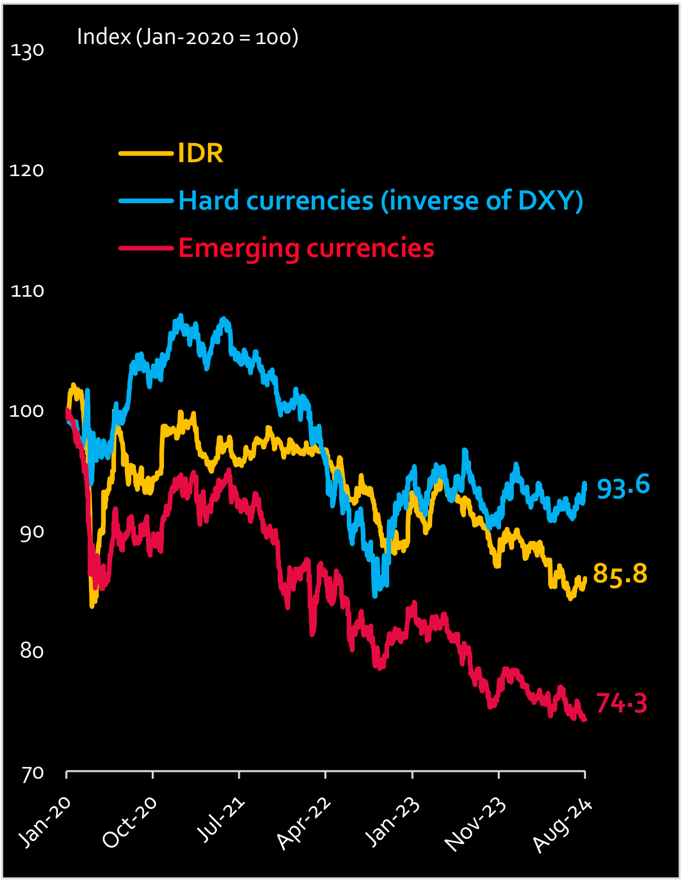
- But BI still has a trick up its sleeve. It is now ramping up repo transactions, essentially lending money to banks so that they would buy SRBI. This also means that BI is now acquiring SBN again, but this only adds to its net holdings (now at 24.5% of total) rather than gross. All these amount to a rather tricky maneuver, whereby BI tries to support the Rupiah while easing monetary conditions at home.

- Could these contradictory stances be a problem down the road? Probably not, especially if the Fed does cut rates quite aggressively in the coming months. In that scenario, capital inflows would improve banks' liquidity and reduce pressure on the Rupiah, allowing BI to gradually phase out SRBI issuance.

- But the road ahead may prove to be bumpier, in which case BI may continue issuing SRBI at or near current volumes. This would be a short-term boon for the Rupiah, but a considerable risk in the long-run, since the IDR liquidity that BI is injecting might eventually "chase" the USD. Furthermore, increased BI holdings of SBN (albeit only in net value) does not make for good optics when markets are volatile and investors' conviction on EMs continue to ebb and flow.

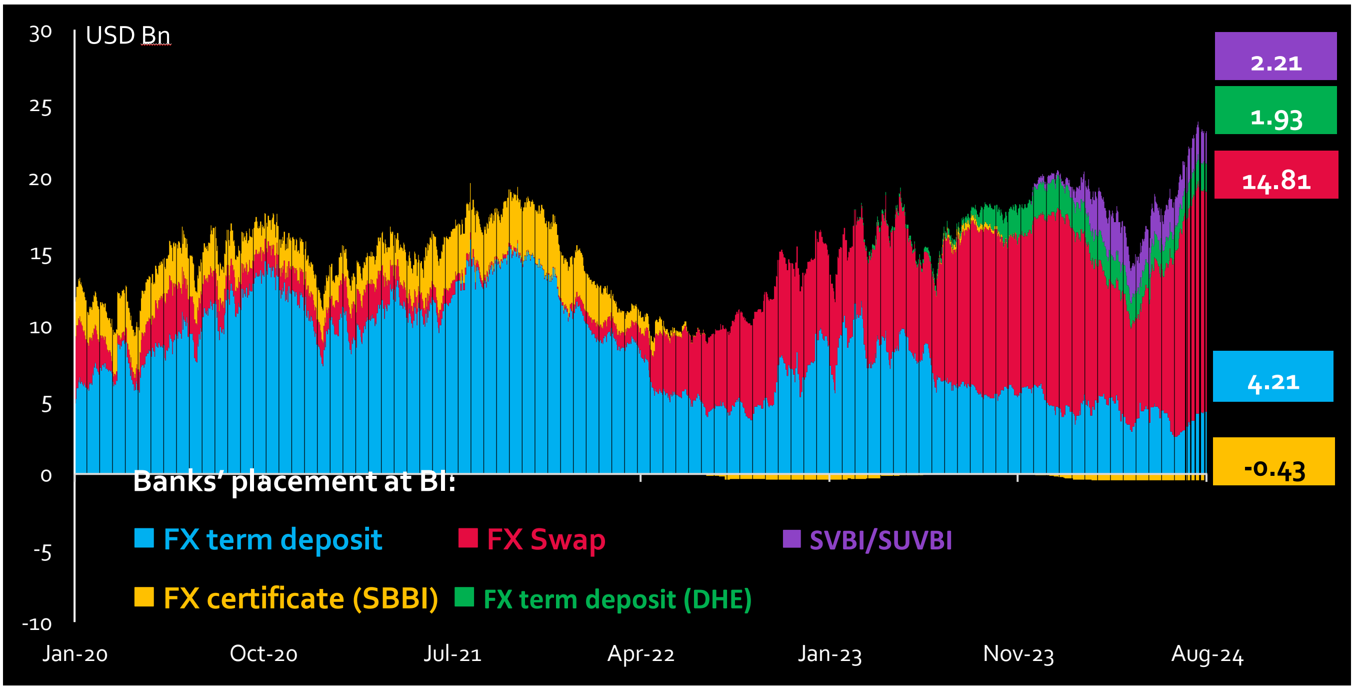
Panel 1. FX reserves increased due to SRBI and net global bond issuance





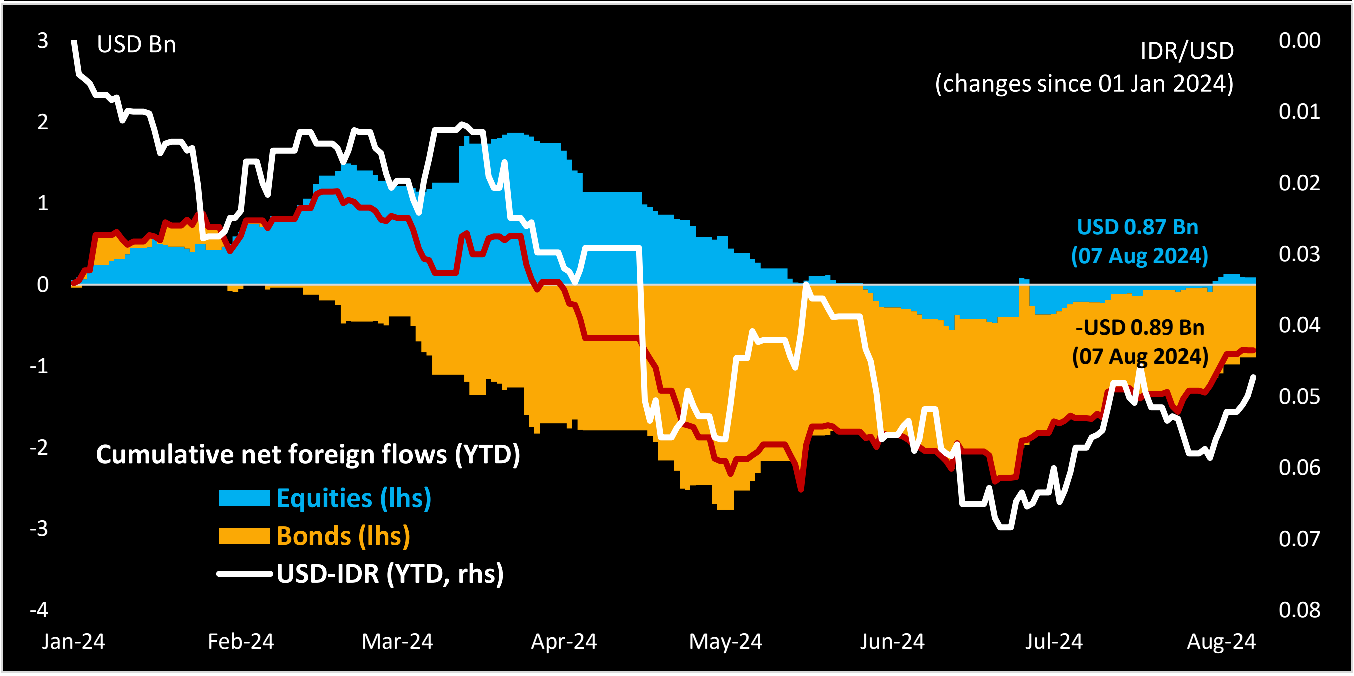
Source: Bloomberg

Panel 2. Banks' placement at BI increased, driven mainly by FX swap



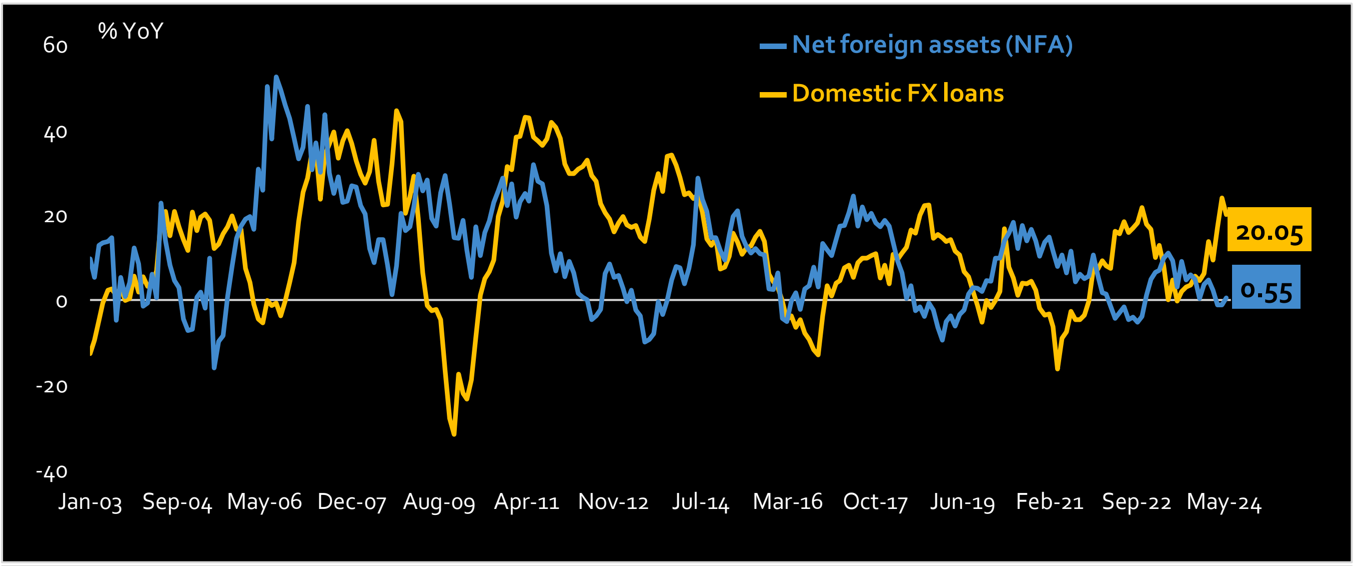
Source: BI

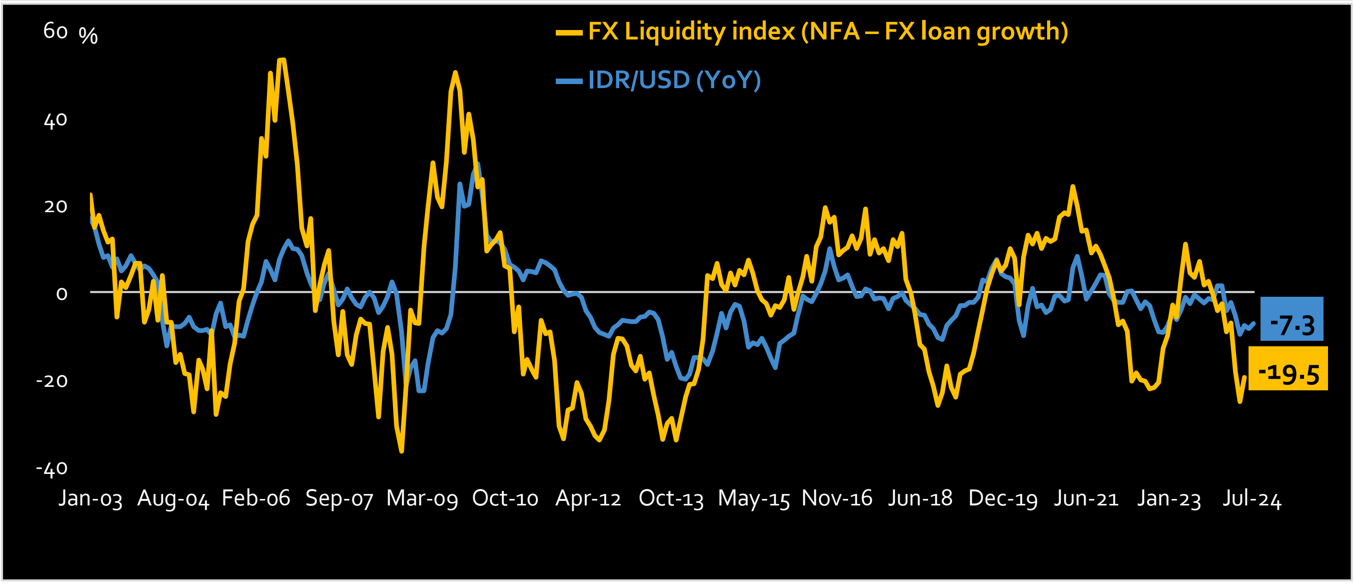
Panel 3. Increased capital inflow in both equities and bonds



Source: Bloomberg

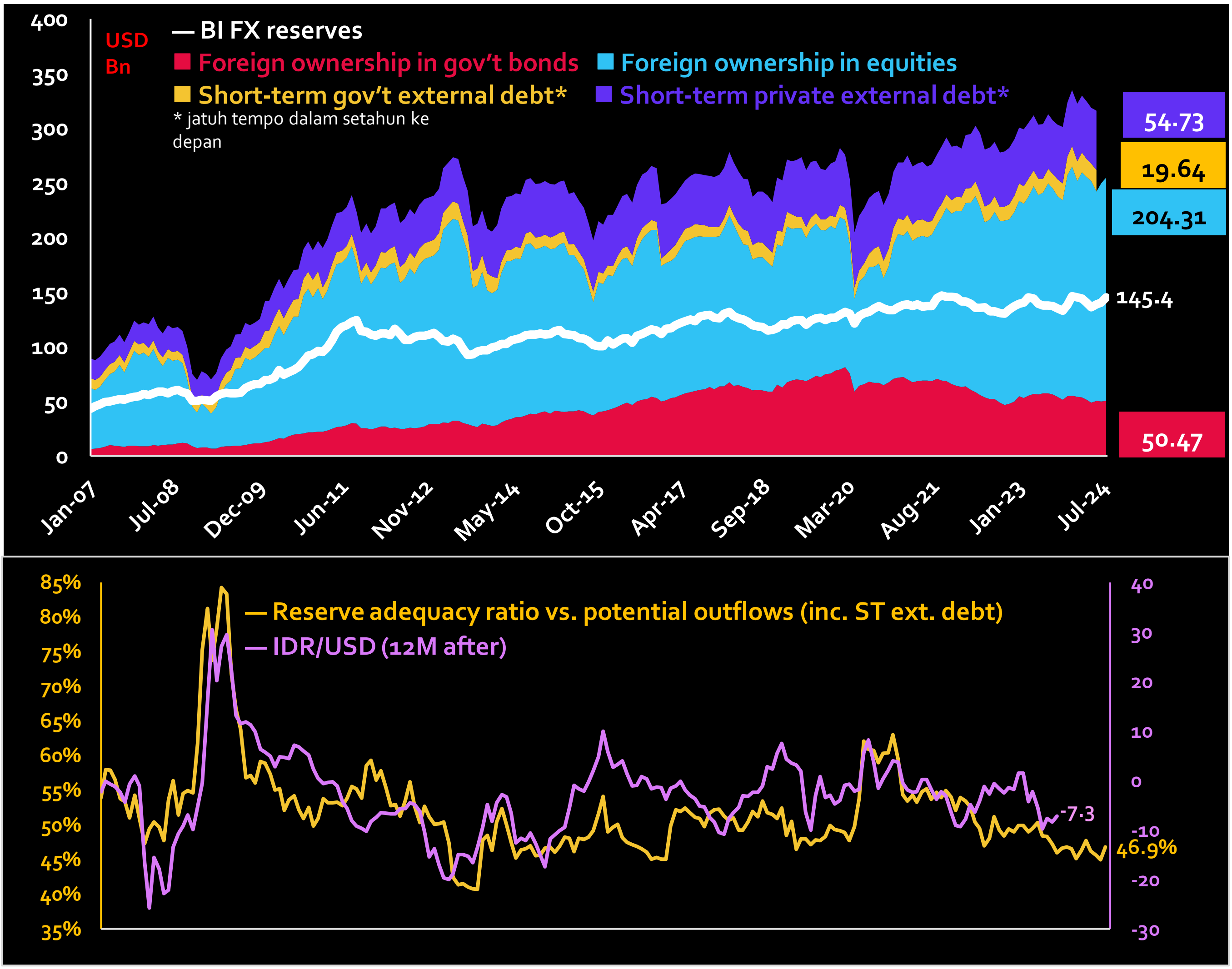
Panel 4. Demand for FX liquidity continue to pick up





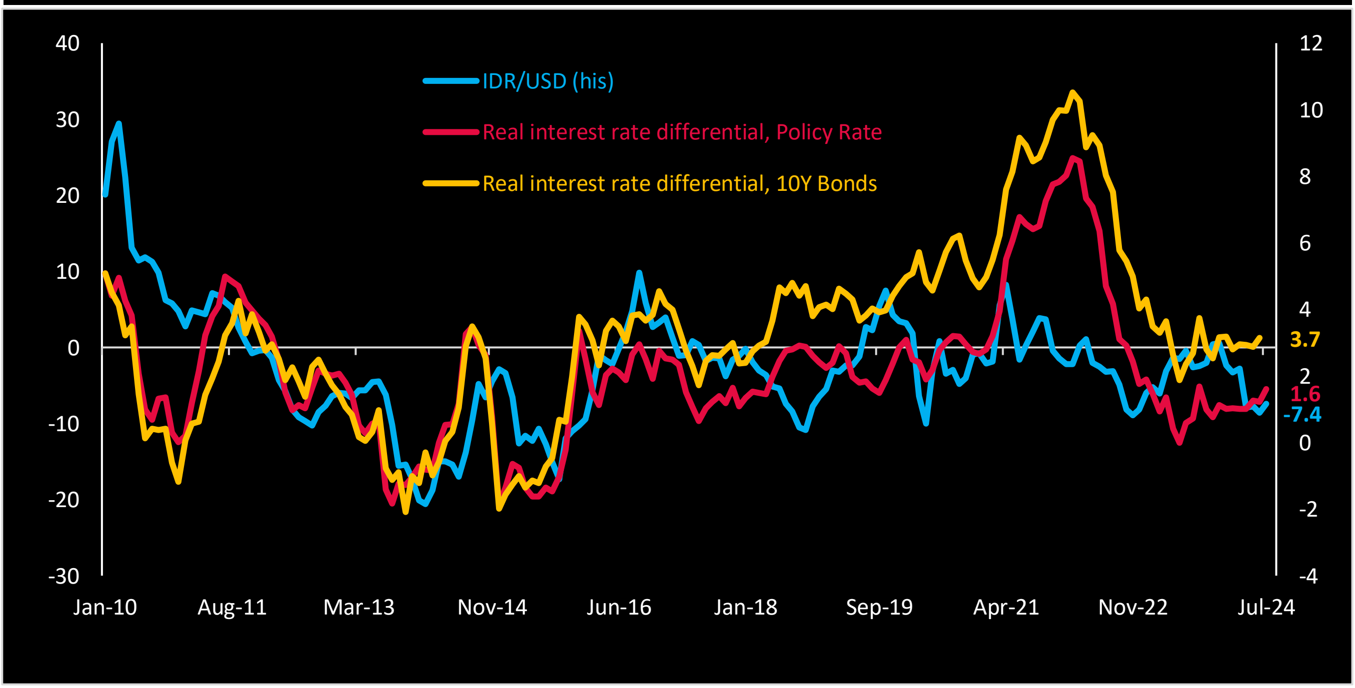
Source: BI, Bloomberg

Panel 5. Reserves adequacy ratio might be worsening in the coming months



Source: BI, Bloomberg

Panel 6. Still narrow real rate differentials may add pressure on the Rupiah



Source: Bloomberg

Selected Macroeconomic Indicators

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)
US	5.50	Jul-23	2.50
UK	5.00	Aug-23	3.00
EU	4.25	Jul-23	1.65
Japan	-0.10	Jan-16	-2.90
China (lending)	2.30	Aug-23	4.15
Korea	3.50	Jan-23	0.90
India	6.50	Feb-23	1.42
Indonesia	6.25	Apr-24	4.12

Money Mkt Rates	7-Aug	-1 mth	Chg (bps)
SPN (1M)	5.88	5.80	7.6
SUN (10Y)	6.80	7.04	-24.4
INDONIA (O/N, Rp)	6.24	6.13	10.5
JIBOR 1M (Rp)	6.90	6.90	0.0

Bank Rates (Rp)	May	Apr	Chg (bps)
Lending (WC)	8.86	8.85	1.37
Deposit 1M	4.68	4.65	2.54
Savings	0.67	0.68	-1.07

Currency/USD	7-Aug	-1 mth	Chg (%)
UK Pound	0.788	0.780	-0.96
Euro	0.916	0.923	0.76
Japanese Yen	146.7	160.8	9.59
Chinese RMB	7.177	7.268	1.28
Indonesia Rupiah	16,035	16,278	1.52

Capital Mkt	7-Aug	-1 mth	Chg (%)
JCI	7,212.1	7,253.4	-0.57
DJIA	38,763.5	39,375.9	-1.56
FTSE	8,166.9	8,203.9	-0.45
Nikkei 225	35,089.6	40,912.4	-14.23
Hang Seng	16,877.9	17,799.6	-5.18

Foreign portfolio ownership (Rp Tn)	Jul	Jun	Chg (Rp Tn)
Stock	3,322.0	3,273.1	48.98
Govt. Bond	813.1	808.1	4.97
Corp. Bond	7.6	8.2	-0.60

Trade & Commodities	7-Aug	-1 mth	Chg (%)
Baltic Dry Index	1,698.0	1,966.0	-13.6
S&P GSCI Index	537.4	587.1	-8.5
Oil (Brent, $/brl)	78.3	86.5	-9.5
Coal ($/MT)	149.0	138.6	7.5
Gas ($/MMBtu)	1.85	2.02	-8.4
Gold ($/oz.)	2,382.9	2,392.2	-0.4
Copper ($/MT)	8,640.9	9,795.2	-11.8
Nickel ($/MT)	16,031.3	17,082.2	-6.2
CPO ($/MT)	862.3	873.2	-1.3
Rubber ($/kg)	1.71	1.64	4.3

External Sector	Jun	May	Chg (%)
Export ($ bn)	20.84	22.32	-6.65
Import ($ bn)	18.45	19.40	-4.89
Trade bal. ($ bn)	2.39	2.92	-18.30
Central bank reserves ($ bn)*	140.2	139.0	0.87

Prompt Indicators	Jun	May	Apr
Consumer confidence index (CCI)	123.3	125.2	127.7
Car sales (%YoY)	-11.8	-13.2	-17.4
Motorcycle sales (%YoY)	3.5	-4.5	18.3

Manufacturing PMI	Jul	Jun	Chg (bps)
USA	49.6	51.6	-200
Eurozone	45.8	45.8	0
Japan	49.1	50.0	-90
China	49.8	51.8	-200
Korea	51.4	52.0	-60
Indonesia	49.3	50.7	-140

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

Scan for the link to Subscribe or **click here**

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$)	4175	3912	4350	4784	4920	5149
Consumer Price Index Inflation (% YoY)	2.7	1.7	1.9	5.5	2.6	2.87
BI 7 day Repo Rate (%)	5.00	3.75	3.50	5.50	6.00	6.00
USD/IDR Exchange Rate (end of year)**	13,866	14,050	14,262	15,568	15,397	16,172
Trade Balance (US$ 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 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: 1007431

Thierris Nora Kusuma
Economist / Analyst
thierris_kusuma@bca.co.id
+6221 2358 8000 Ext: 1071930

Nicholas Husni
Economist / Analyst
nicholas_husni@bca.co.id
+6221 2358 8000 Ext: 1079839

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