FX Reserves:

Ample war chest for the battles to come

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Executive Summary

- BI's FX reserves decreased by USD 0.3 Bn to USD 149.9 Bn in September, driven by the decline in bank's FX placement on Bank Indonesia, which might have reflected increased FX demand by the private sector amid strong Rupiah.
- Rupiah has normalized recently from its overvaluation, hastened by geopolitical escalation in the Middle East, better data in the US, and a lack of stable forward guidance from the Fed.
- BI has slowed down its SRBI issuance (IDR 58.0 Tn) to the point it barely kept up with maturity (51.2 Tn), but an outright exit from SRBI could be trickier amid heightened global uncertainty.

- BI's FX reserves decreased to USD 149.9 Bn in September, slightly off its all-time high (150.2 Bn) the previous month. Interestingly, this decline happened despite September being quite a good month for the Rupiah, with faster-than-expected rate cuts by both BI and the Fed spurring net inflows into both bonds (USD 1.34 Bn) and equities (USD 1.42 Bn). These easily offset any potential decline from SRBI, whose issuance in September (IDR 58.0 Tn) barely kept up with maturity (51.2 Tn).

- Part of the decline can be attributed to repayment of external debt, including those by SOEs (PLN's JPY-bond of about USD 0.17 Bn). But again, these numbers are eclipsed by new issuance of USD- and EUR-denominated bonds by the government, which amounted to about USD 2.5 Bn (versus 1.5 Bn in maturing bonds). BI's reserves also continued to benefit from valuation (mark-to-market) effect, due to rising prices of gold and bonds.

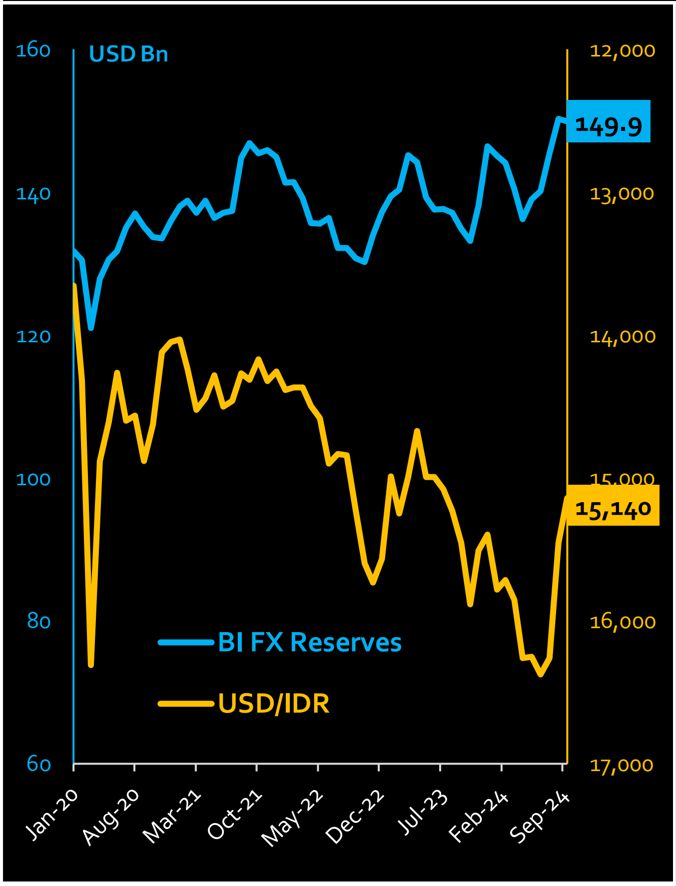
- What, then, explains the decline? Worsening trade balance (or current account deficit) could be the culprit, although this would have to await future data for confirmation. One intriguing signal that we already saw in September, however, was the decline in banks' FX placement at BI – outside of SVBI and SUVBI (which are the FX equivalents of SRBI). Notably, FX swaps, which forms the bulk of such placement, has declined by USD 1.25 Bn.

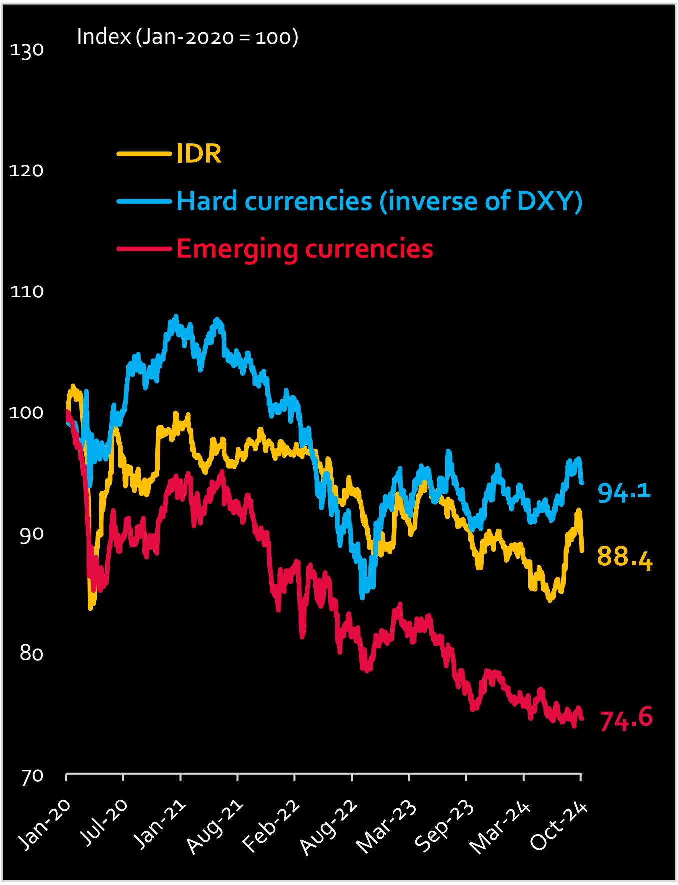
- This could be a sign, then, that the strong Rupiah has encouraged demand for USD, be it for actual use (e.g. imports) or speculative purposes (e.g. customers expecting USD to strengthen vs. IDR). As we have forewarned previously, an overly-strong Rupiah – as was the case in September – could incentivize behaviors that worsens Indonesia's external balance, leading eventually to a new and weaker equilibrium for the currency.

- The sharp Rupiah depreciation of late (with USD/IDR exceeding 15,600 as of this writing) seems to vindicate our view – but only up to a point. Global factors, most notably military escalation in the Middle East and strong job numbers in the US, are the dominant factor behind the USD's rally. And then there is also the matter of China's stimulus, which has diverted EM flows away from Indonesia since the last week of September.

- Unfortunately, this "rollercoaster ride" may not end anytime soon. On the political front, investors await the swearing-in and cabinet announcement for the Prabowo administration (Oct 20th), as well as the US Elections (Nov 5th). We do not fail to see how the latter deadline could influence some of the decision-making in Israel and Iran lately, leading to a heightened risk of escalation.
- Meanwhile, the Fed has all but abdicated its forward guidance of late, and act in a more reactive, data-dependent manner. This could lead to pleasant surprises like its 50-bps cut last month, but it equally could imply sensitivity to inflation (oil price) shocks and other gyrations in the economic data. And even if the Fed can follow through with several cuts in the short-term, there may be a host of inflationary pressure building up which could prevent further cuts next year – from rising oil prices to (potential) new Trump tariffs to the aftershocks from China's stimulus.
- Amid this uncertainty, BI's abundant reserves appear to be a good stabilizer for the Rupiah – but not without its vulnerability. The reserves have been buttressed by inflows into new instruments (about USD 16.1 Bn for SRBI, and 4.2 Bn for SVBI/SUVBI) and banks' FX placement (about 19.4 Bn), meaning that BI's net reserves is only about USD 110.2 Bn. As it stands, BI cannot really afford to phase out SRBI without strong corresponding inflows into government bonds, and it may have to roll over most of the IDR 344 Tn that will mature between October and January. This is unfortunate, since SRBI is today the single largest sink of banks' liquidity, and BI rate cuts might not be as effective without SRBI reduction.
- Despite its big "war chest", then, BI needs to deploy it more sparingly and strategically. Defending the Rupiah at high valuations would deplete its ammo prematurely, while there are still plenty of battles (market volatility) to come. A more realistic assessment of Rupiah's fundamental value, taking into account peer currencies, our real (effective) exchange rates, and our saving-investment (S-I) gap, would be needed in order to best utilize BI's resources.

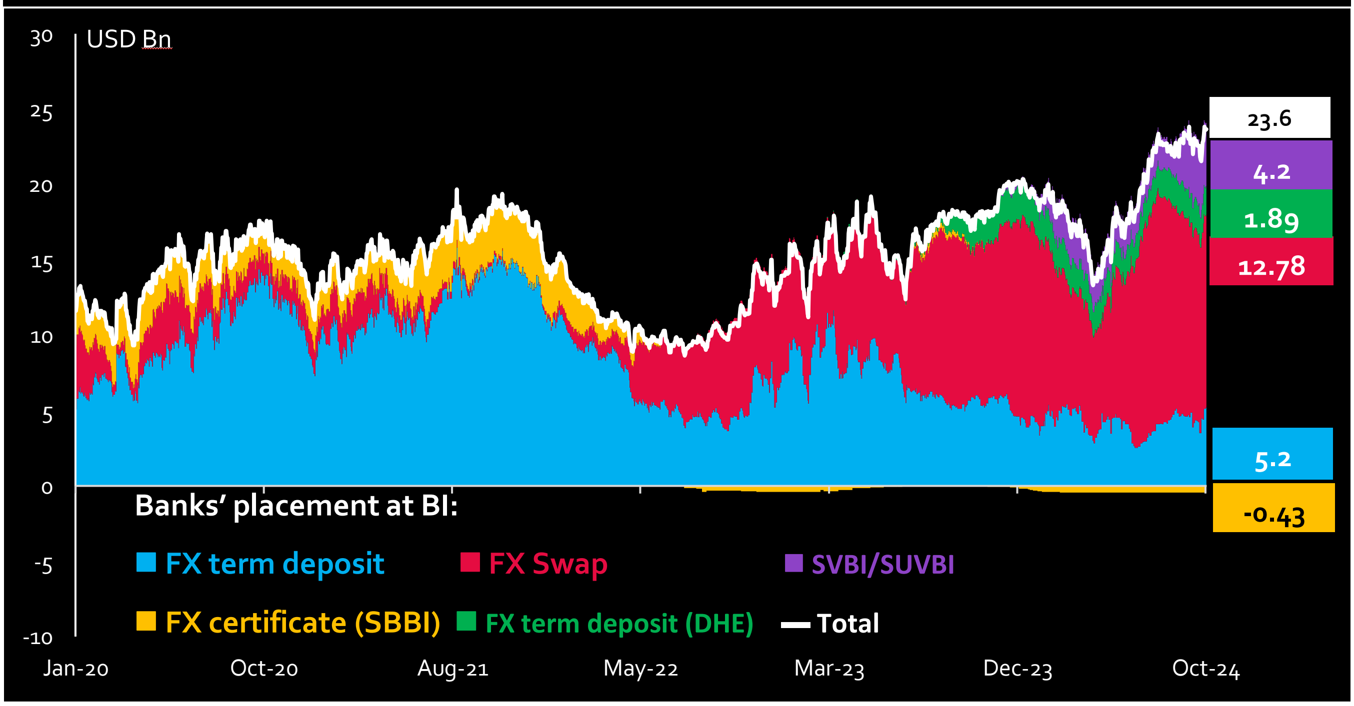
Panel 1. FX reserves decreased as SRBI issuance barely keeping up with maturity





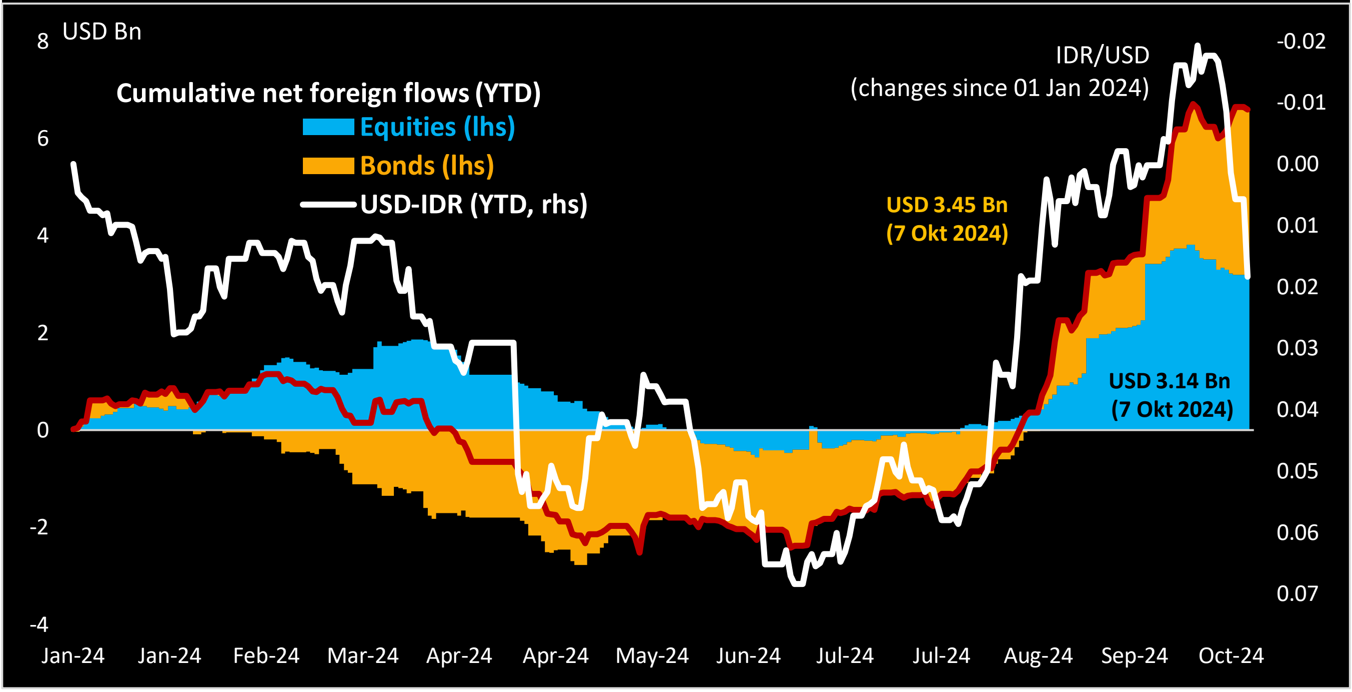
Source: Bloomberg

Panel 2. Banks' placement at BI declines further with FX swap leading the charge



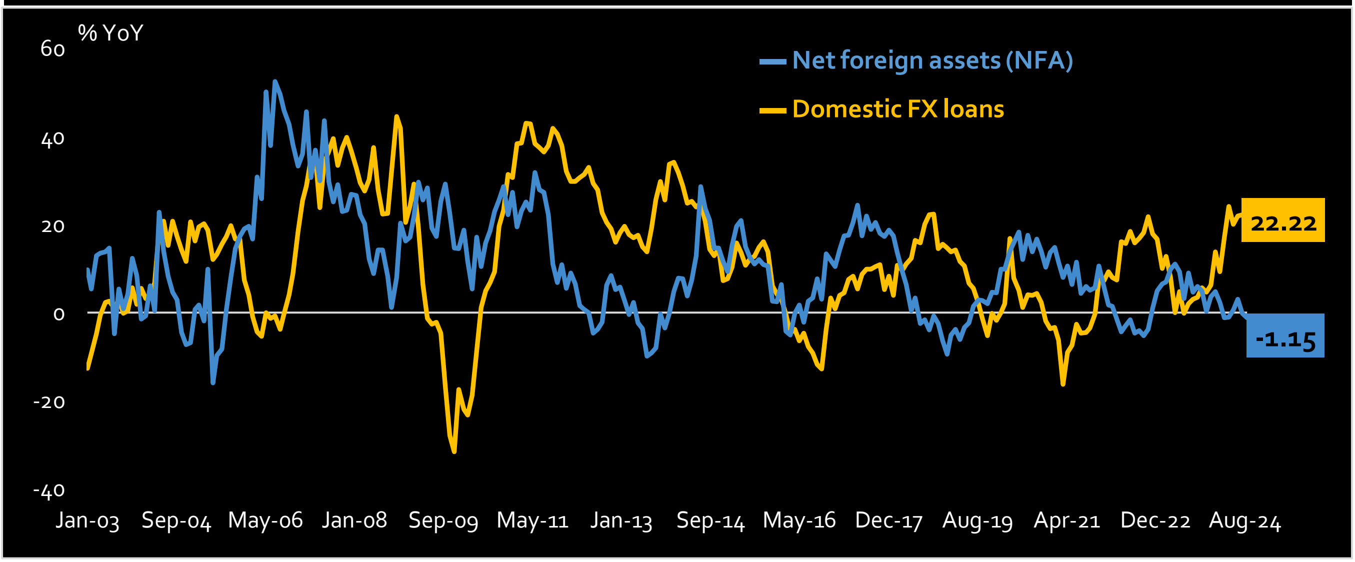
Source: BI

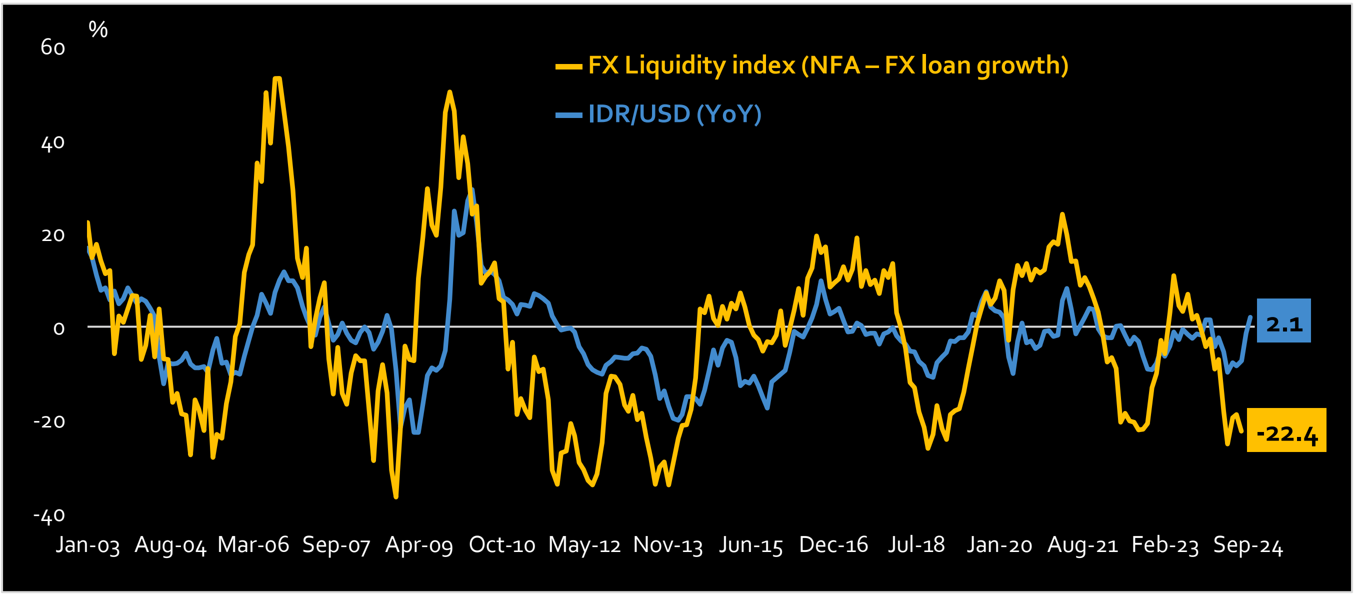
Panel 3. Increased capital inflow in both equities and bonds in September



Source: Bloomberg

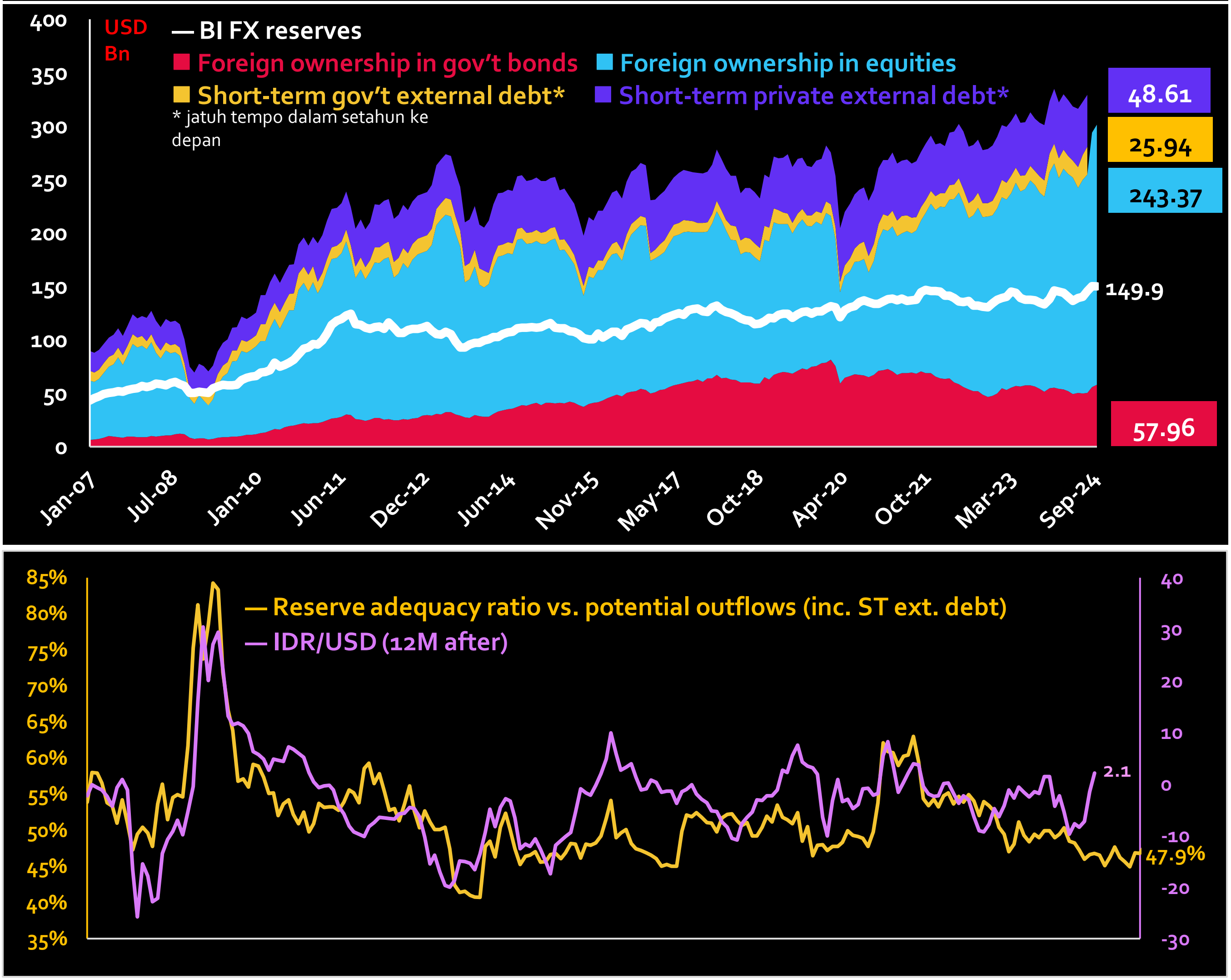
Panel 4. Demand for FX liquidity continue to pick up





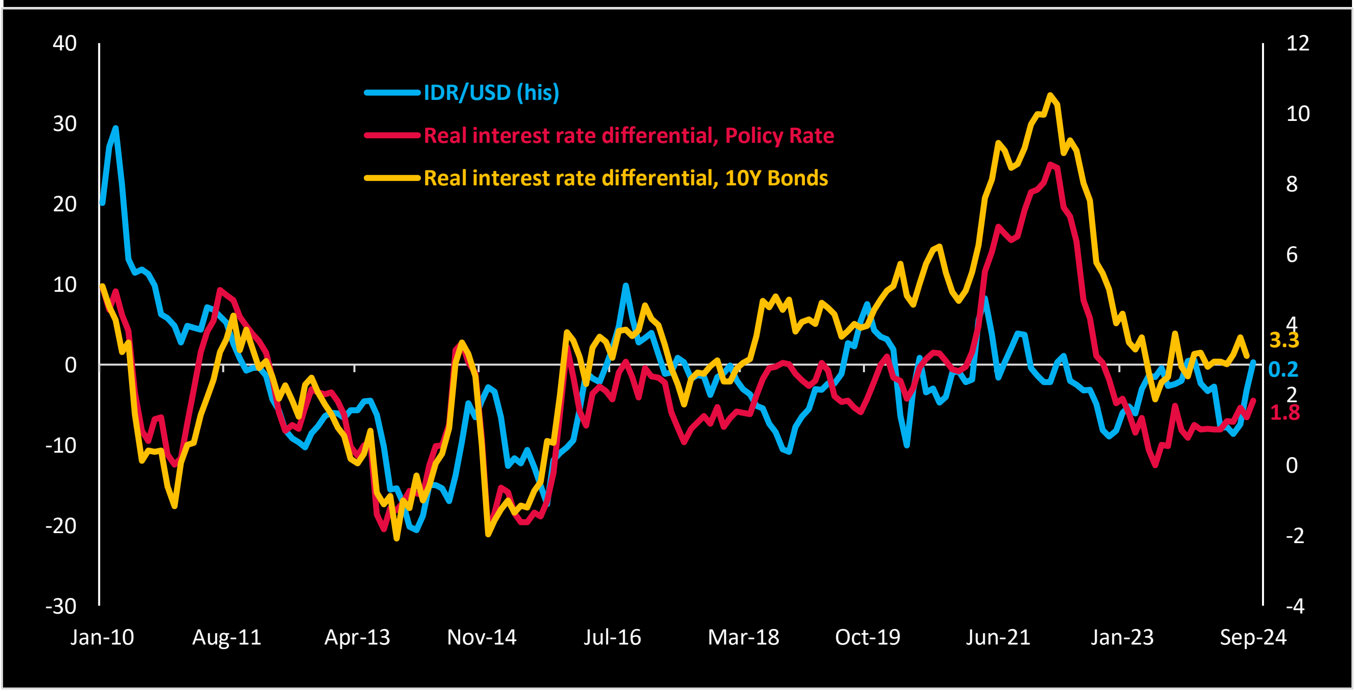
Source: BI, Bloomberg

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



Source: BI, Bloomberg

Panel 6. Still narrow real rate differentials has not hindered Rupiah's rise



Source: Bloomberg

Selected Macroeconomic Indicators

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)
US	5.00	Jul-23	2.50
UK	5.00	Aug-23	2.80
EU	3.65	Jul-23	1.85
Japan	-0.10	Jan-16	-3.10
China (lending)	2.00	Aug-23	3.75
Korea	3.50	Jan-23	1.90
India	6.50	Feb-23	2.85
Indonesia	6.00	Sep-24	4.16

Money Mkt Rates	7-Oct	-1 mth	Chg (bps)
SPN (3M)	5.60	5.91	-31.5
SUN (10Y)	6.71	6.60	11.1
INDONIA (O/N, Rp)	6.21	6.31	-10.6
JIBOR 1M (Rp)	6.65	6.90	-25.3

Bank Rates (Rp)	Jul	Jun	Chg (bps)
Lending (WC)	8.81	8.82	-1.72
Deposit 1M	4.78	4.70	7.49
Savings	0.65	0.67	-1.66

Currency/USD	7-Oct	-1 mth	Chg (%)
UK Pound	0.764	0.762	-0.35
Euro	0.911	0.902	-0.97
Japanese Yen	148.2	142.3	-3.97
Chinese RMB	7.019	7.098	1.13
Indonesia Rupiah	15,680	15,365	-2.01

Capital Mkt	7-Oct	-1 mth	Chg (%)
JCI	7,504.1	7,721.8	-2.82
DJIA	41,954.2	40,345.4	3.99
FTSE	8,303.6	8,181.5	1.49
Nikkei 225	39,332.7	36,391.5	8.08
Hang Seng	23,099.8	17,444.3	32.42

Foreign portfolio ownership (Rp Tn)	Sep	Aug	Chg (Rp Tn)
Stock	3,558.2	3,684.6	-126.37
Govt. Bond	870.6	852.3	18.28
Corp. Bond	6.9	7.0	-0.02

Trade & Commodities	7-Oct	-1 mth	Chg (%)
Baltic Dry Index	1,907.0	1,941.0	-1.8
S&P GSCI Index	566.6	511.1	10.9
Oil (Brent, $/brl)	80.9	71.1	13.9
Coal ($/MT)	153.0	142.5	7.4
Gas ($/MMBtu)	2.51	2.01	24.8
Gold ($/oz.)	2,642.6	2,497.4	5.8
Copper ($/MT)	9,777.7	8,875.5	10.2
Nickel ($/MT)	17,792.9	15,637.1	13.8
CPO ($/MT)	1,023.2	925.2	10.6
Rubber ($/kg)	2.10	1.84	14.1

External Sector	Aug	Jul	Chg (%)
Export ($ bn)	23.56	22.24	5.97
Import ($ bn)	20.67	21.74	-4.93
Trade bal. ($ bn)	2.90	0.50	478.90
Central bank reserves ($ bn)*	150.2	145.4	3.32

Prompt Indicators	Aug	Jul	Jun
Consumer confidence index (CCI)	124.4	123.4	123.3
Car sales (%YoY)	-14.2	-7.8	-9.7
Motorcycle sales (%YoY)	7.4	24.1	3.5

Manufacturing PMI	Sep	Aug	Chg (bps)
USA	47.3	47.9	-60
Eurozone	45.0	45.8	-80
Japan	49.7	49.8	-10
China	49.3	50.4	-110
Korea	48.3	51.9	-360
Indonesia	49.2	48.9	30

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$)	4175	3912	4350	4784	4920	5149
Consumer Price Index Inflation (% YoY)	2.7	1.7	1.9	5.5	2.6	1.9
BI 7 day Repo Rate (%)	5.00	3.75	3.50	5.50	6.00	5.50
USD/IDR Exchange Rate (end of year)**	13,866	14,050	14,262	15,568	15,397	15,650
Trade Balance (US$ 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

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