Indonesia Market Color

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FX & Interest Rate

Bank Indonesia moderates tightening pace. BI hiked BI 7D RRR by 25 bps to 5.50% in its December meeting, after three consecutive 50 bps rate hikes in the past three months. The decision was on the back of easing headline inflation as well as moderating pressure to IDR since the Fed has shifted to smaller rate hikes in Dec-22. However, Fed members are expecting higher terminal rate of 5.25%, compared to its initial 4.75% back in September. On domestic economy, core inflation still has room to escalate further. Latest inflation figure in reflected a stronger festive season, with core inflation at 3.4% yoy as of Dec-22, up from 3.3% in previous month. PMI manufacturing input cost has also shown moderation, albeit still at high level. We still see that producers will continue to adjust their output prices by normalizing margin. We project headline inflation at 4.5% yoy at the end of 2023, while core inflation increases to 4.0% yoy. As such, there's still room for BI to impose further hikes, which we expect to reach a terminal rate of 6.25% by March.

Pressure to IDR has receded. From the end of Nov-22 to the end of Dec-22, IDR appreciated by 0.8%, after experiencing a tough headwind from Fed's monetary policy tightening. However, compared to other peer currencies, the level of appreciation was milder. JPY, PHP, CNY, THB have appreciated by around 2% to 4% in the same period (Table 1). Looking at portfolio flows, bond market posted some inflows worth USD 3 bn within the same period, while equity booked net outflows of USD 1 bn. The limited number of inflows to bond market and outflows from equity has restrained IDR to appreciate further. In our view, IDR will remain fragile to external pressure since the margin between Fed Fund Rate and BI 7D RRR narrowed to 100 bps in December (Chart 1).

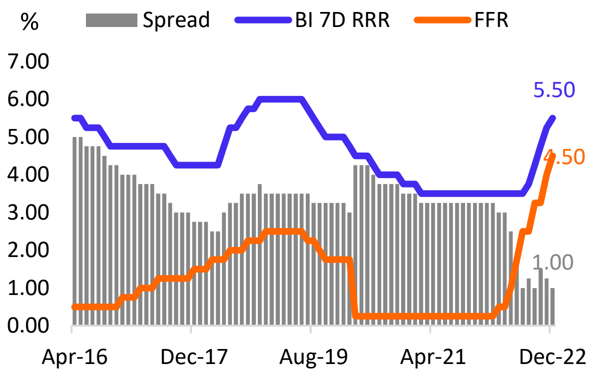
Trade surplus posted at USD 49 bn in 11M22. Export grew by 28.2% yoy to USD 267 bn during 11M22, while import grew by 24.5% yoy to USD 218 bn. Heading towards year-end, export growth has been moderating, due to lower prices and volumes of commodities.

Table 1. Peer Currencies Comparison

2022	FOMC Meeting				
	Dec'19 to Mar'22	Mar'22 to Jun'22	Jun'22 to Sep'22	Sep'22 to Dec'22*	Nov'22 to Dec'22*
JPY	-5.8%	-11.5%	-6.6%	8.8%	4.4%
PHP	-1.5%	-6.2%	-6.7%	5.8%	2.3%
EUR	-2.8%	-5.6%	-7.0%	7.9%	2.2%
KRW	-1.9%	-7.2%	-10.2%	9.7%	2.0%
CNY	0.3%	-5.7%	-6.2%	2.2%	1.9%
THB	0.4%	-6.3%	-6.7%	8.0%	1.6%
SGD	-0.4%	-2.7%	-3.2%	5.9%	0.8%
IDR	-0.8%	-3.7%	-2.2%	-2.5%	0.8%
MYR	-0.9%	-4.9%	-5.2%	4.5%	0.3%
BRL	15.0%	-10.9%	-3.0%	4.0%	-0.2%
ZAR	8.3%	-11.4%	-11.1%	4.3%	-0.6%
INR	-1.9%	-4.2%	-3.0%	-1.7%	-1.6%

Source: Bloomberg as of 20-Dec-2022, Danamon

Chart 1. Interest Rate Differential



Source: The Fed, Bank Indonesia, Danamon

Meanwhile, import has gradually picked up, with consumptive goods remaining on the sideline. We expect this trend to sustain, along with recovering domestic demand that will induce imported consumer goods in 2023.

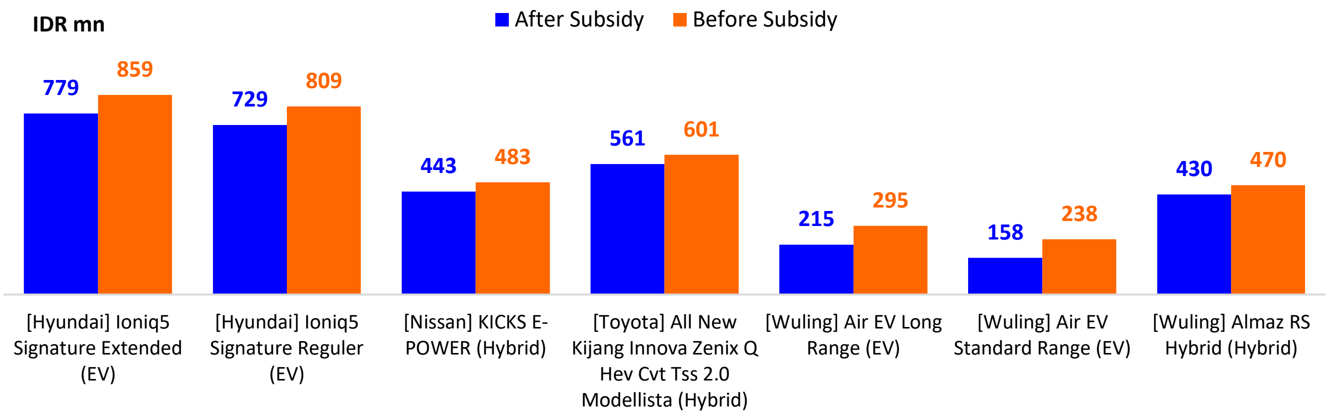
BI prepared supplementary policies to attract more FX flows. Within the press release that followed their meeting in December, BI announced a plan to issue new FX monetary operation instrument for exported natural resources. The instrument will be issued with competitive yield and equipped with tax incentives. Details on the instrument is not out yet. On top of that, BI will continue its operation twist, to push short tenor yield higher, in order to attract portfolio flows to domestic market. From the macroprudential perspective, BI also added incentives for banks to disburse more credit to MSME and green projects. Incentives of RRR for banks that disburse loan for MSMEs was doubled to 1%, new incentive for green project financing at 0.3% max, and higher RRR incentives to 280 bps max, from 200 bps previously for financing to priority sectors.

Automotive Industry

The automotive industry is getting stronger. It was reflected in higher car sales as it grew 4.2% yoy in November, reaching 91,086 units. Throughout 2022, car sales increased 19.2% yoy by selling 942,499 units compared to the same period last year. Growth is also seen in motorcycle sales. A total of 588,269 motorcycles were sold during Nov-22, which increased significantly by 26.9% yoy compared to Nov-21. The automotive industry is and will be prospective, especially with the government's effort to promote and develop the EV ecosystem in Indonesia.

The latest government plan is to subsidize electric vehicle sales. The amount is estimated to be IDR 80 mn for Battery Electric Vehicle (BEV) and IDR 40 mn for hybrid cars. The subsidy will only be applied to vehicles that are produced domestically. As for cars, there are at least eight vehicles, which come from Hyundai, Nissan, Toyota, and Wuling. Chart 2 shows that such subsidy will decrease prices by 15% on average; Wuling AIR EV gets the most significant price cut by 27-34%, whereas other models get 7-10%. With this subsidy scheme and EV tax incentives, the government is optimistic about the future of EVs in Indonesia. However, rising interest rate poses as a challenge, since 70% of vehicle sales are on credit schemes. In addition, the government also needs to secure domestic production to balance out the possible increase in EV demand.

Chart 2. 4W Electric Vehicle Prices



Source: Gaikindo, Katadata.com

Indonesia's Selected Economic Indicators

	2019	2020	2021	2022E	2023E
National Accounts					
Real GDP (% y-o-y)	5.0	-2.1	3.7	5.1	5.3
Domestic demand ex. inventory (% y-o-y)	3.6	-3.1	2.8	5.0	5.2
Real Consumption: Private (% y-o-y)	5.0	-2.7	2.0	5.0	6.1
Real Gross Fixed Capital Formation (% y-o-y)	4.4	-4.9	3.8	4.5	3.5
GDP (USD bn) — nominal	1,119	1,059	1,186	1,212	1,296
GDP per capita (USD) — nominal	4,193	3,917	4,350	4,422	4,593
Open Unemployment Rate (%)*	5.3	7.1	6.0	5.9	5.5
External Sector					
Exports (% y-o-y, BoP Basis)	-6.8	-3.0	42.5	30.7	4.3
Imports (% y-o-y, BoP Basis)	-8.9	-18.1	39.9	31.1	13.2
Trade balance (USD bn, BoP Basis)	3.5	28.2	43.8	56.0	36.9
Current account (% of GDP)	-2.7	-0.4	0.3	-0.5	-1.0
Central government debt (% of GDP)	30.5	38.1	41.0	37.8	35.8
International Reserves –IRFCL (USD bn)	129.2	135.9	144.9	130.2	135.7
Reserve Cover (Months of imports & ext. debt)	7.3	9.8	7.8	5.8	6.2
Currency/USD (Year-end)*	13,901	14,050	14,253	15,573	15,090
Currency/USD (Average)*	14,146	14,529	14,296	14,855	15,450
Other					
BI 7-Day Reverse Repo rate (% year end)*	5.00	3.75	3.50	5.50	6.25
Consumer prices (% year end)*	2.72	1.68	1.87	5.51	4.50
Fiscal balance (% of GDP; FY)	-2.20	-6.09	-4.65	-3.92	-2.71
S&P's Rating – FCY	BBB	BBB	BBB	BBB	BBB

Source: CEIC, E = Danamon Estimates, *FY22 actual data

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