Indonesia Market Color

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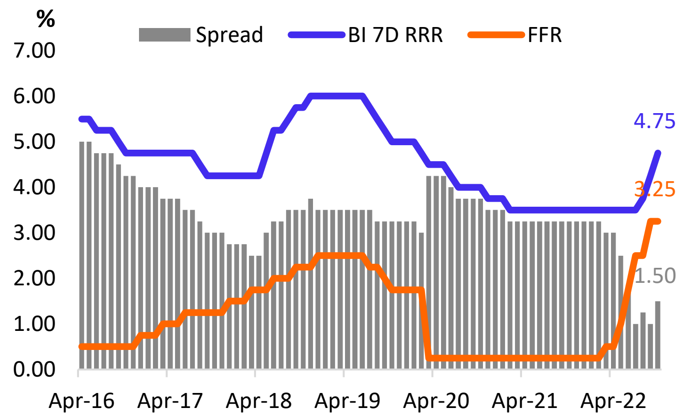
FX and Interest Rate

- **A piping hot inflation.** Inflation spiked to 5.95% yoy in Sep-22, the highest level since Oct-15, as a result of the first-round impact from subsidized fuel price increase. In October, inflation moderated to 5.71% yoy on the back of a decline in food prices amid harvest season. Such moderation would be transitory, until the second-round impact of fuel price adjustment fully kicks in. We expect headline inflation to climb to 6.49% yoy at year-end.

- **Trade surplus remained aloft.** Indonesia reported USD5.0bn worth of trade surplus in Sep-22, narrowing from USD5.7bn in a month prior. Export grew by 20.3% yoy to USD25bn, moderating from 30.2% yoy in Aug-22, as prices of palm oil and iron-steel plunged by 23.0% yoy and 19.9%, respectively. Meanwhile, import was recorded at USD20bn, decelerated to 22.0% yoy, from 32.8% yoy in Aug-22. The lag in import recovery was attributed to consumption goods, which was contracted by 11.2% yoy. With the improvement in domestic indicators and the moderation in commodity prices, we expect that the trade surplus will narrow, going forward.

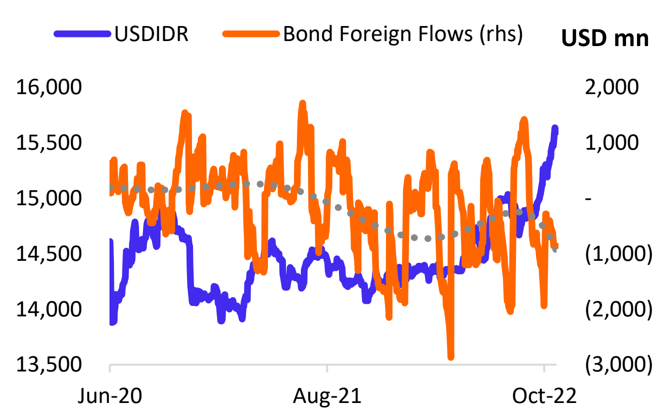
- **Capital flew from domestic bond market as UST jumped**. Along with the Fed's hawkish policy stance during their last FOMC meeting, 10Y US Treasury (UST) yield jumped by 100 bps to 4.04% at the end of October. This had pulled capital out from domestic bond market as much as USD1.0bn in Oct-22. The Rupiah depreciated to IDR 15,598/USD at the end of October, from IDR 15,228/USD in previous month. As a response, monetary policy makers raised its policy rate by 50 bps in October, after their initial 50 bps hike in September. The Fed will hold another meeting on Nov 2nd, where we expect another 75 bps increase of benchmark rate, before easing the pace of tightening to 50 bps in Dec-22.

Chart 1. Interest Rate Differential



Source: The Fed, Bank Indonesia

Chart 2. USD/IDR vs INDOGB Flows



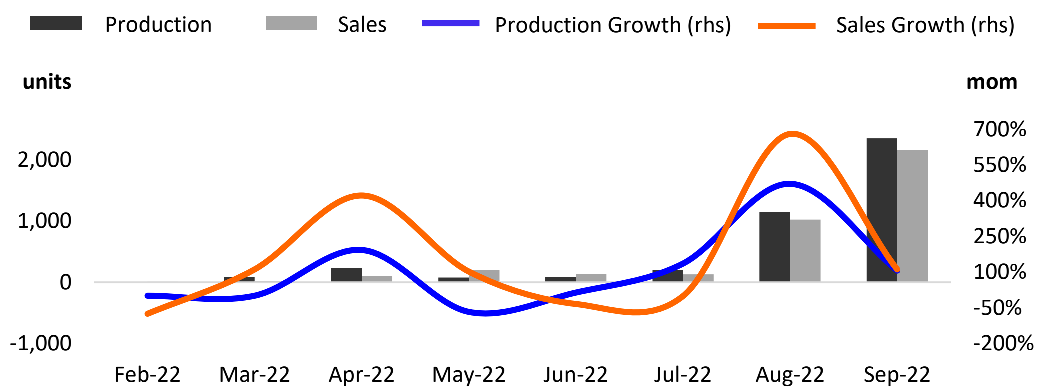
Source: Bank Indonesia, MoF

- **Bank Indonesia to protract its pre-emptive measures**. Having inflation on-track to climb, coupled with recent pressure towards the Rupiah, BI will need to pick-up its pace on policy tightening. Interest rate differential between BI's policy rate and Fed Fund Rate would narrow further if BI does not catch-up, while the spread was already at record low. Thus, bold and limpid signals on BI's policy stance are necessary, to build confidence in the market amid strong IDR fundamentals. Having said that, we believe there is more space for BI to front load its rate hikes, reaching a terminal rate of 6.25% in the beginning of 2Q23.

Automotive Industry

- **Indonesia goes hefty on EV.** Soaring and fluctuating fuel prices contributed to consumers' automotive preference towards electric vehicles (EV) in Sep-22. Its sales accounted for 2.2% of all vehicles' sales, selling 2,154 units and growing 111% from Aug-22. The sales were dominated by Wuling AIR EV (1,887 units) and Hyundai IONIQ (261 units). As President Jokowi plans for Indonesia to have two million EVs by 2025, the government is looking for ways to accelerate EV purchases inside the country. In boosting demand, the government implements tax incentives, only paying 10% of the vehicle tax. In addition, subsidies are being considered for next year to ease the conversion and be more cost-competitive. The Ministry of Transportation has stated that it is possible to reallocate the fuel subsidy for EVs. Nonetheless, the policy is expected to majorly impact domestic sales. These promising incentives and low car ownership ratio give the automotive industry great potential to grow and developing the EV ecosystem might be the catalyst for growth.

Chart 3. Electric Vehicles Wholesales & Production



Source: Gaikindo

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	5.7	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	14,820	14,890
Currency/USD (Average)	14,146	14,529	14,296	14,738	14,927
Other					
BI 7-Day Reverse Repo rate (% year end)	5.00	3.75	3.50	5.25	6.25
Consumer prices (% year end)	2.72	1.68	1.87	6.49	5.73
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

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