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FX & Interest Rate

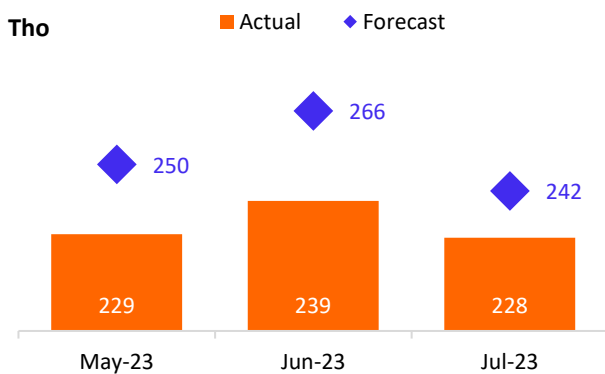
A data dependent monetary policy. In line with consensus, the Federal Reserve raised its policy rate by 25 bps to 5.50% p.a. in July. The press release indicated that the Fed will rely more on data to determine future direction of the policy rate. Monetary policymakers are not in a hurry to hike again, but they are prepared if needed. The latest CPI inflation data for Jun-23 showed a substantial decline in headline inflation to 3.0% yoy, down from 4.0% yoy in the previous month. However, core inflation remained high at 4.8% yoy, reflecting stronger than anticipated economic data. The US economy exhibited robust growth, surpassing market expectations, with growth rate of 2.4% yoy in 2Q23. Furthermore, the labor market demonstrated resilience, as jobless claims consistently fell below expectations over the past three months. Demand for labor continues to outpace supply, as reflected in the unemployed person to vacancy ratio, which stood at 0.6 in Jun-23.

Headwinds for IDR. Since FOMC, the IDR has depreciated by 0.8%, reaching IDR 15,113/USD at month end. This is attributed to the possibility of another monetary tightening and the increase of financing needs in relation to debt ceiling, which lead to higher UST yields. In contrast, the Indonesian government bond yields have significantly declined due to potential supply cut. Yield differential then narrows and exerts pressure to the IDR amid dwindling USD liquidity. We have also observed a gradual increase in onshore demand for USD, along with import awakening. Looking forward, election and energy-related spendings are expected to further boost demand for USD. We anticipate that the IDR will continue to depreciate throughout 3Q23, with a projected quarterly average movement of IDR 15,352/USD.

Diverging external and internal balances. In Jul-23, headline inflation marked five consecutive months of moderation, reaching 3.1% yoy (0.2% mom).

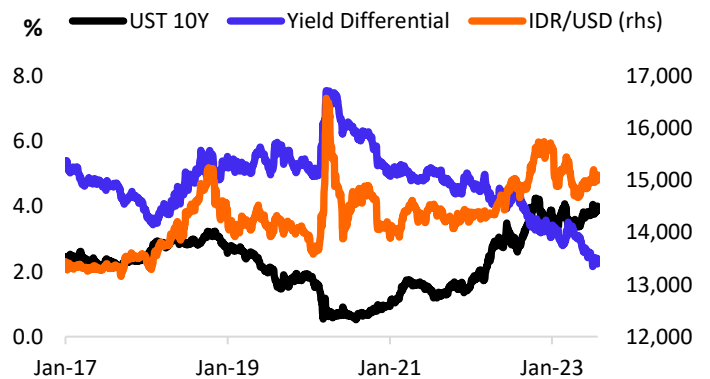
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Chart 1. US Jobless Claims



Source: US Labor Department

Chart 2. Yield Differential vs IDR/USD



Source: Bloomberg per 28-Jul-23. Yield differential is 10Y INDOGB minus 10Y UST

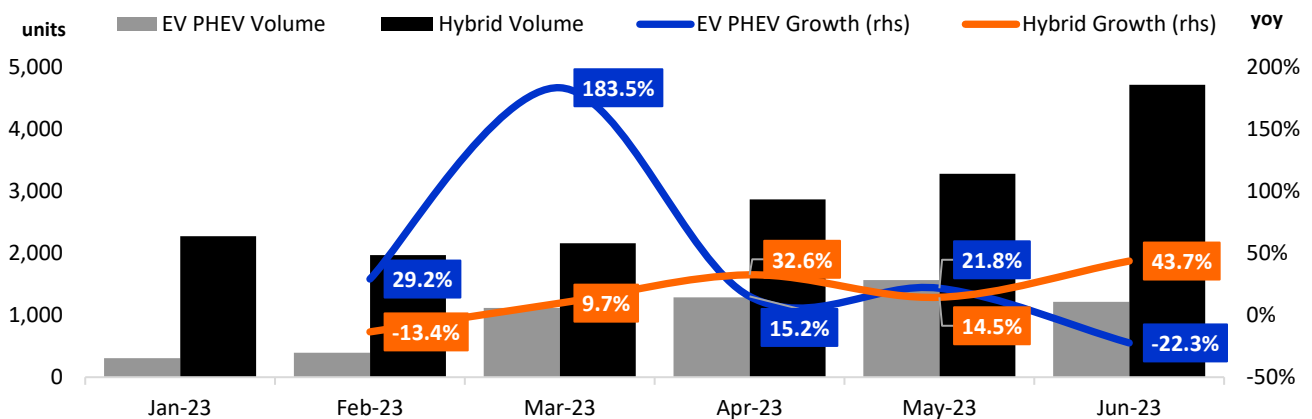
The decline in headline inflation was primarily driven by volatile foods, which experienced a deflation of 0.03% yoy. Furthermore, core inflation and administered prices both eased to 2.4% yoy and 8.4% yoy, respectively, with moderation observed across most segments. As disinflation continues at a faster pace than expectation, there is likelihood of headline inflation dipping below 3.0% in the fourth quarter of 2023. This can be attributed to the high base effect resulting from last year's subsidized fuel price adjustments. The trajectory of inflation has been favorable for authorities thus far, especially considering a lower target range of 1.5% to 3.5% in the following year, as opposed to the current range of 2.0% to 4.0%. On the other hand, external balance indicators, such as the current account and portfolio flows, have shown signs of deterioration. Given these circumstances, it is expected that BI will prioritize managing IDR volatility as a primary focus for policy direction.

Automotive Industry

Automotive industry's notable strides. In the first half of 2023, Indonesia's automotive industry has made significant improvements, rebounding from the challenges posed by the pandemic in previous years. Notably, 4W sales increased by 6.5% yoy, reaching 505,985 units, which already represents 48% of the 2023 target. Equally remarkable, 2W sales saw a staggering 42.5% yoy increase, totaling 3,201,930 units. These positive indicators point to a recovering consumer demand and a renewed momentum in the industry. Manufacturers have played an active role in this progress, introducing new models, and integrating advanced technologies to meet the evolving needs of consumers, particularly in the hybrid and electric vehicle segment.

Hybrid cars still lead the sales. For 1H23, the sales of electric vehicles (EV), plug-in hybrid electric vehicles (PHEV), and hybrid electric vehicles (HEV) reached 23,167 units, making up 4.6% of total 4W sales. Although this is a relatively small contribution, it has already surpassed the combined sales of all EV, PHEV, and HEV throughout 2022, which amounted to 20,681 units. Hybrid cars are still the preferred choice among Indonesian buyers, outselling EVs almost three times over. This preference is attributed to the perceived convenience and familiarity associated with hybrid technology, giving buyers a sense of comfort and confidence in adopting this eco-friendly alternative. As the industry continues to progress, it is likely that consumer attitudes towards EVs may shift further in the future.

Chart 3. EV, PHEV, HEV Sales



Source: Gaikindo

Indonesia's Selected Economic Indicators

	2020	2021	2022	2023E
National Accounts				
Real GDP (% y-o-y)	-2.1	3.7	5.3	5.3
Domestic demand ex. inventory (% y-o-y)	-3.1	2.8	3.8	5.2
Real Consumption: Private (% y-o-y)	-2.7	2.0	4.9	6.1
Real Gross Fixed Capital Formation (% y-o-y)	-4.9	3.8	3.9	3.5
GDP (USD bn) — nominal	1,059	1,186	1,391	1,475
GDP per capita (USD) — nominal	3,917	4,350	4,783	5,267
Open Unemployment Rate (%)	7.1	6.0	5.9	5.3
External Sector				
Exports (% y-o-y, BoP Basis)	-3.0	42.5	25.6	8.5
Imports (% y-o-y, BoP Basis)	-18.1	39.9	21.6	17.2
Trade balance (USD bn, BoP Basis)	28.2	43.8	62.7	47.9
Current account (% of GDP)	-0.4	0.3	1.0	-0.4
Central government debt (% of GDP)	38.1	41.0	39.6	37.3
International Reserves –IRFCL (USD bn)	135.9	144.9	137.2	141.2
Reserve Cover (Months of imports & ext. debt)	9.8	7.8	5.9	6.2
Currency/USD (Year-end)	14,050	14,253	15,573	14,839
Currency/USD (Average)	14,529	14,296	14,855	15,090
Other				
BI 7-Day Reverse Repo rate (% year end)	3.75	3.50	5.50	6.00
Consumer prices (% year end)	1.68	1.87	5.51	3.53
Fiscal balance (% of GDP; FY)	-6.09	-4.65	-2.38	-2.18
S&P's Rating – FCY	BBB	BBB	BBB	BBB

Source: CEIC, E= Danamon Estimates

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