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## FX & Interest Rate

**Hawkish stance, despite a pause.** In the most recent FOMC meeting, the Fed decided to maintain the policy rate target range at 5.00% - 5.25%. However, it is worth noting that half of the FOMC members now anticipate a higher FFR terminal of 5.75%, compared to the 5.25% projection from the March meeting. This adjustment aligns with the latest macro indicators, which highlight a strong labor market. In May 2023, non-farm payroll figures exceeded market expectations, reaching 339,000, compared to the consensus estimate of 190,000. On the other hand, there is a continued disinflationary trend, with headline inflation declining to 4.0% in May 2023, down from 4.9% in the previous month. However, core inflation remains persistent at 5.3% in May 2023, despite high base effect from previous year.

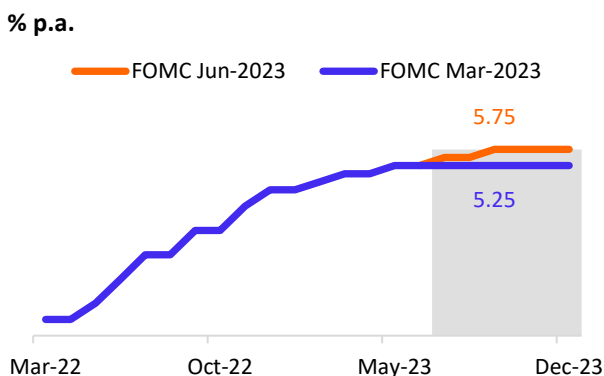
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**Headwinds blow for EM currencies.** Since the June FOMC meeting, several EM currencies, including IDR, have experienced depreciation due to capital outflows. As of 23-Jun, the IDR depreciated by approximately 0.6%, which is relatively moderate compared to other currencies like MYR, THB, KRW, and JPY. The IDR's resilience can be attributed to robust economic fundamentals, such as disinflationary trend and sustainable growth recovery. However, there are risks looming for IDR, primarily stemming from the diminishing trade surplus. Indonesia's trade surplus significantly narrowed in May-23, amounting to USD 440 million, driven by lower export growth due to declining commodity prices. Consequently, we anticipate that Indonesia's trade surplus for 2Q23 will only reach USD 5 billion, down from USD 16 billion in 2Q22. As a result, there is a possibility that the current account could shift from a surplus to a deficit in the near future.

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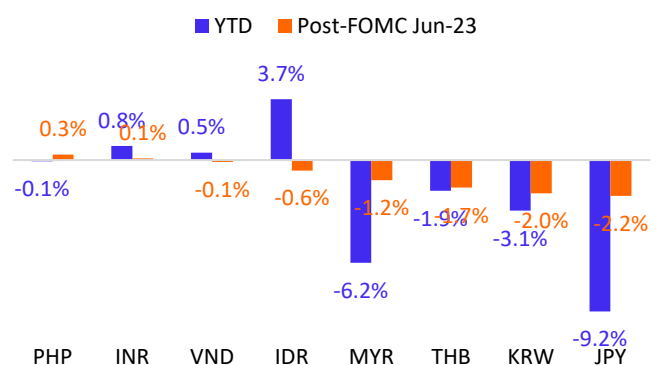
**Inflation is approaching BI's midpoint target.** In Jun-23, headline inflation decreased to 3.5% yoy, from 4.0% yoy in a month prior. The primary factors contributing to this decline in inflation were the costs associated with volatile foods and transportation.

Chart 1. Trajectory of Fed Fund Rate



Source: The Federal Reserve

Chart 2. Currency Comparison



Source: Bloomberg as of 23-Jun-2023

Volatile food inflation moderated to 1.2% yoy in Jun-23, significantly lower than the 3.3% yoy recorded in May-23. Meanwhile, administered inflation also decreased to 9.25 yoy in Jun-23, down from 9.5% yoy in the previous month, due to downward adjustments in unsubsidized fuel prices.

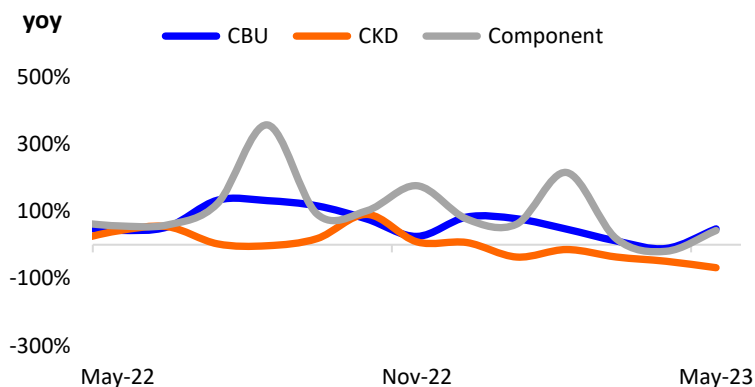
**BI expressed vigilance amid external risks.** In its June MPC meeting, BI decided to keep the policy rate unchanged at 5.75%, citing the return of inflation to the central bank's target range ahead of expectations. However, Governor Perry emphasized the importance of strengthening policy responses in emerging markets, including Indonesia, to mitigate potential spillover effects from external factors. This concern was not explicitly stated during the May-23 MPC meeting, indicating a shift in BI's stance. These developments suggest that BI is likely to maintain its current policy rate for the remainder of the year unless IDR faces significant pressure amid a hawkish monetary policy from the Federal Reserve. In such a scenario, there is a possibility of a 25 basis points hike in the policy rate.

**Automotive Industry**

**Dynamic growth fueling the automotive industry.** In May 2023, the automotive industry in Indonesia witnessed a dynamic and promising landscape, further solidifying its growing prominence in the global economy. The domestic sales exhibited a significant increase of 65.2% yoy, driven by robust domestic demand. Notably, even after accounting for the seasonality associated with the Eid festivities, domestic sales still demonstrated a noteworthy growth of 4.0% in May-23 compared to Jun-22, which represents the first month following Eid. This remarkable sales surge can be attributed to several contributing factors, including an upward trend in the current income index and the successful introduction of new 4W models.

**Automotive's trade boom.** Furthermore, Indonesia has showcased a robust trade performance, underscoring its potential as a global market leader. The country experienced a substantial upswing in the export of vehicles and their accessories, with an increase of 60.2% yoy in May-23. Remarkably, the exports of completely built-up vehicles (CBU) and components experienced impressive year-on-year growth rates of 47.3% and 42.2% respectively. Key export destinations for Indonesian automotive products include countries such as Thailand, Singapore, and the Philippines.

**Chart 3. Auto Export Growth**



Source: Gaikindo

## Indonesia's Selected Economic Indicators

	2020	2021	2022	2023E
<b>National Accounts</b>				
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
<b>External Sector</b>				
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
<b>Other</b>				
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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