

BI holds and rolls out accommodative measures

Thursday, April 25, 2019

Highlights

- The central bank held the benchmark rate at 6.00% and appeared positive on the domestic economy in the last quarter.
- BI also recognized that financial market uncertainties have receded, but they remain wary of the global economic situation.
- BI announced several accommodative measures that they said would be aimed at boosting domestic demand.
- These measures may also help the liquidity situation whilst supporting longer – term IDR stability.
- There remain potential upcoming risks related to the IDR such as the possible outflow of tax amnesty funds and/or the monthly trade data not turning a surplus.
- Hence, we stick to our view that BI may only cut the benchmark rate by 50bps in 4Q 2019 as they may want to observe first if any of these risks may materialize.

BI held rates at 6.00% following today's policy meeting and refrained from any dovish hints. Instead the central bank was focused on announcing a slew of accommodative measures (see table 1) that focused on deepening the financial markets and easing the liquidity situation. **The central bank sees that these measures as helping to boost domestic demand. These measures could also help strengthen longer term IDR stability.**

The central bank appeared rather optimistic of the domestic economy in the last quarter but remained wary of the global economic situation. They also recognized that financial market uncertainties have receded. BI sees that 1Q 2019 GDP growth could come out at 5.2% yoy and see that the 1Q 2019 balance of payments would be positive. Hence there is no immediate need for a rate cut, but BI is likely to remain vigilant of the economic situation in the next couple of months.

The central bank also recognized that the currency has been supported by inflows. Indeed, interest in Indonesia has been strong for this year and hence provided some form of stability for the IDR as it remains fairly sticky in the low 14,000s against the USD. Yield seeking investors have been attracted by the country's high bond yields (see chart 1) relative to peers especially as the external pressures on the country recedes (particularly with the Fed turning dovish this year). The equity market also initially rallied at the start of this year before range trading ahead of the election. It looks like political uncertainty has abated somewhat as quick count results show Jokowi may have achieved a fairly comfortable margin of victory of around 10% over his opponent Prabowo.

A large margin of victory by Jokowi also makes it harder for Prabowo to undertake a material challenge of the results.

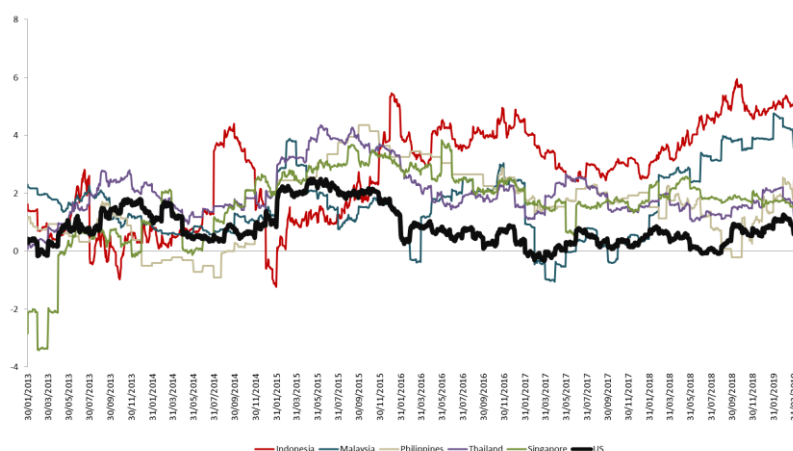
However, there remain some risks to monitor ahead. These include the potential outflow of the earlier repatriated funds from the tax amnesty program, the question if the monthly trade surplus is able to sustain, and the slower-than-expected global growth leading to weaker appetite for emerging market (EM) assets. The first phase of the tax amnesty program had ended around September 2016 and the lock – up period reportedly is three years, which would mean that the risk related to an outflow of the funds would come in the second half of 2019. The outflow probability would depend on whether Indonesian assets can still remain attractive in the second half of 2019 vis-à-vis its peers, the availability of investment instruments and government policies to encourage the funds to stay within the country. Indonesia has reported two months of a trade surplus but exports have been affected by the global trade slowdown and weak commodity prices, and there is a risk that the import declines would slow as the country enters the festive period when the demand for consumable items such as fuel may rise. BI also expects the current account deficit to be at 2.5% of GDP for 2019. In terms of the global growth situation, there may be limited signs of green shoots at the moment but whilst data continues to point an expected slowdown, the recession risk has also declined. In the short-term, one risk is that of broad USD strength.

Overall, we stick to our view that BI may only cut the benchmark rate by 50bps in 4Q 2019 as they monitor economic developments and risks in coming months and the impact of the newly announced measures.

Table 1: Measures unveiled by Bank Indonesia

No	Measure
1	Increase the availability of liquidity and support financial market deepening through strengthening monetary operations strategy.
2	Improve the efficiency of retail payments through the expansion of the Bank Indonesia National Clearing System (SKNBI), namely through additional time and acceleration of settlement, increase in nominal value of transactions, and reduction in tariffs.
3	Increasing the supply of Domestic Non-Deliverable Forward (DNDF), in particular by simplifying the regulations concerning underlying transaction.
4	Implementing market operator regulation in the money market and foreign exchange market.
5	Develop the market for Commercial Securities (SBK) as an alternative short-term funding source for corporations.
6	Drive the expansion of electronification of non-cash social assistance, village funds, transportation sector, and fiscal operations.

Source: Bank Indonesia

Chart 2: 10 Year Real Rates of Indonesia against Regional Peers, %

Source: CEIC, Bloomberg and OCBC

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