Indonesia Outlook

OCBC Bank

Expect a hold but what about easing horizon?

Thursday, June 20, 2019

Highlights

- **Bank Indonesia (BI) is still likely in our view to keep the benchmark rate on hold today.**
- **The timing may appear favorable for a cut as global easing expectations have set in and the IDR appears firmer but BI may still likely wish to continue to monitor capital outflow risks, possibly even related to the expiry of the lock – up period of the repatriated tax amnesty funds before pulling the trigger.**
- **For today, watch closely for further views from BI on the external environment, which can give us more understanding on the easing horizon.**

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Bank Indonesia (BI) will be concluding its June monthly policy meeting today with our expectations that they will still likely be on hold. Governor Perry Warjiyo sounded cautious just before this meeting as he stated that "global financial market condition is still full of uncertainties" which he sees "can lead to capital flows reversal and bring risks in financing the current-account deficit." However, Perry did state, "If we take into account low inflation and economic growth that needs to be pushed, indeed, we already know that there's room to lower interest rate." In our opinion, such a statement strongly indicates that BI keeps rate cuts in their view though they may possibly still be patient about it and only undertake it when the believe the time is right. At the moment, we see that Indonesia's economic conditions does not merit an urgent need for a cut with GDP growth still ticking above 5.00% (even if slowing) and inflation remains comfortably within BI's range of 2.5% – 4.5%.

It can be seen though, that the timing appears favorable for a cut at this point. Indeed, this may be the case as the IDR has been firmer in June as global expectations of a Fed rate cut began to set in, providing a boost for Asian sovereigns too. Country specific wise, there was also the positive news of S&P upgrading Indonesia sovereigns from BBB- to BBB. Foreign reserves may have fallen to USD120.3bn in May from USD124.3bn in the prior month but it is still sufficient as it is equivalent to 6.7 months of imports and servicing of government external debt. The conclusion of the FOMC on the 19th June 2019 saw the Fed's median dot plot for 2020 turn lower than the 2019 median dot plot whilst at the same time, the "patient" reference was also dropped. Other regional central banks have also begun cutting including Bangko Sentral Ng Pilipinas, Reserve Bank of Australia, Bank Negara Malaysia and the Reserve Bank of New Zealand.

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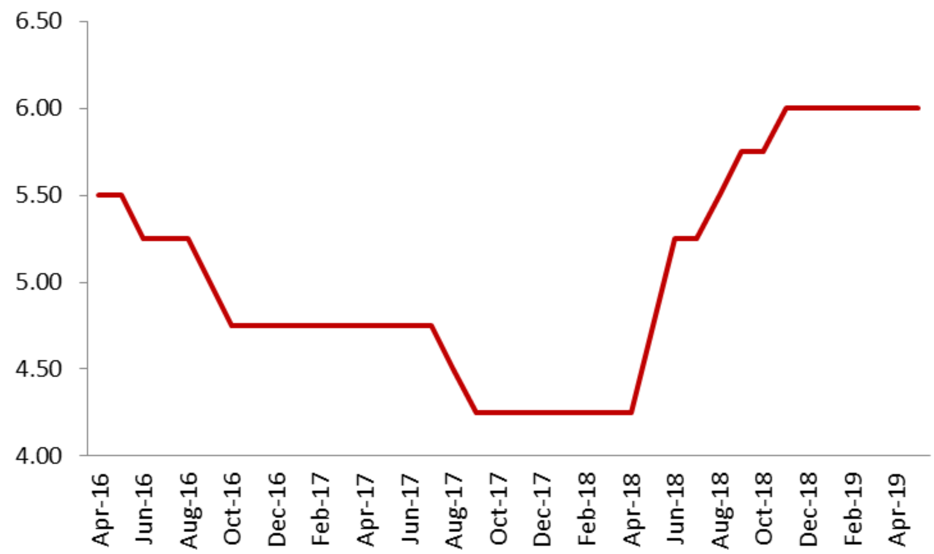
Even so, we believe BI may still be keen to continue to monitor certain capital outflow risks such as whether there is a likelihood of a substantial amount of the repatriated tax amnesty fund flowing out upon expiry of the lock – up period. As a note, the first phase of the tax amnesty period had ended back in September 2016 and the lock – up is meant to last for three years. That said, according to a news report from

Reuters, the government has announced that the income tax rate for infrastructure-related securities would be cut to 5% from 15%.

For today, continue to watch closely for further views from BI on the external environment, which can gives us more understanding on the easing horizon.

Chart 1: Bank Indonesia 7 – Day Reverse Repo Rate, %



Source: CEIC, Bloomberg and OCBC

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