

## Poised to Pause

Wellian Wiranto

+65 6530 6818

[WellianWiranto@ocbc.com](mailto:WellianWiranto@ocbc.com)

### Why Bank Indonesia will hold its policy rate for now

- Indonesia's central bank will announce the decision from its meeting tomorrow – the second last for 2019 – and we expect it to be on pause, after four consecutive rate cuts worth 100bps in aggregate.
- Inflation prints are contained, current account gap is in check, and most importantly, Rupiah has been broadly well-behaved. Together, this should technically still give BI some room to ease further – if it so chooses.
- However, given the increasingly binary outcome of US-China trade negotiations, prudence is BI's top operative word from now. The last thing it wants is to be forced into a sharp U-turn later. Best to take it easy from here.

### Mulling the middle

Having eased its policy rate four times this year, Bank Indonesia has earned the right to pause in the upcoming meeting, and our sense is that it will indeed hold rate unchanged at 5.0% for the rest of the year.

Let's start with the consideration on whether there is a strong need to ease further. While the recent Q3 GDP data has a lacklustre air to it, the momentum has not slowed enough to justify another rate cut this week. As mentioned in our [Nov 5<sup>th</sup> report](#), boosting growth on a more sustainable basis has less to do with further monetary support and a lot more to do with structural reforms by the government, particularly on [labour law changes](#) to address a key FDI impediment.

In other words, BI has done what it can in putting a floor on growth through its 100bps cut already. Opting for further easing would have limited beneficial effect on growth. Moreover, the marginal cost of further easing is starting to be higher from here, given that the current policy rate setting leaves it in the relative sweet spot of maximizing future manoeuvrability on three counts.

Measure	Latest	From 2017 to latest		
		Average	Min	Max
Nominal Rates	5.00	5.10	4.25	6.00
Real Rates	1.87	1.73	0.38	3.52
Rate Differential	3.38	3.46	2.63	4.13

*Note: Real rates refer to the difference between BI's 7-day reverse repo policy rate and contemporaneous headline CPI inflation rate. Rate differential refers to the gap between Indonesia's policy rate and the midpoint of US Fed Funds rate.*

To start with, in nominal terms, the current level of 5.0% is broadly in the middle of the range of the policy rate since 2017, encompassing the period before the central bank was compelled to start hiking rate in May 2018 from

## Indonesia

20 November 2019

4.25% all the way to 6.0%, due to broader emerging market concerns as the Fed's tightening cycle gathered pace.

Taking the view that the policy rate setting might have been relatively too loose before the onset of 2018 market concerns – necessitating the dramatic tightening response – and that, at its height, the monetary policy might have been overly tight, the halfway point might be an useful rule of the thumb.

The same thinking applies when we look at how the prevailing policy rate fares against domestic inflation rate and versus the Fed funds rate. Both the real rates and differential against the US policy rate are now close to the period average. The former signals that the current rate setting is “just nice” in curbing domestic inflation pressure, and the latter in anchoring interest rate differential that is attractive enough to foreign investors.

In particular, with rates differential preservation in mind, given that the Fed has been actively telegraphing to the market that it is not in a hurry to trim rates further after its 3 rate cuts this year, there is a compelling reason for Bank Indonesia to follow suit with a pause as well at this juncture.

Being in the middle on all three counts maximizes the room for Bank Indonesia to manoeuvre going forward.

If growth momentum slumps significantly enough in 2020 to necessitate further monetary action, it can be more assured that it has preserved this space. On the flip side, in the (unlikely) case of sizable pick-up in domestic inflation or the (less unlikely) case of global market volatility which might require sudden rate hikes to anchor currency stability, the degree of upward policy rate reversal that it has to stomach will be contained, as well. In short, a pause now is very much in the order.



Source: OCBC, Bloomberg.

## Treasury Research & Strategy

### Macro Research

**Selena Ling***Head of Research & Strategy*[LingSSSelena@ocbc.com](mailto:LingSSSelena@ocbc.com)**Tommy Xie Dongming***Head of Greater China Research*[XieD@ocbc.com](mailto:XieD@ocbc.com)**Wellian Wiranto***Malaysia & Indonesia*[WellianWiranto@ocbc.com](mailto:WellianWiranto@ocbc.com)**Terence Wu***FX Strategist*[TerenceWu@ocbc.com](mailto:TerenceWu@ocbc.com)**Howie Lee***Thailand, Korea & Commodities*[HowieLee@ocbc.com](mailto:HowieLee@ocbc.com)**Carie Li***Hong Kong & Macau*[carierli@ocbcwh.com](mailto:carierli@ocbcwh.com)**Dick Yu***Hong Kong & Macau*[dicksnyu@ocbcwh.com](mailto:dicksnyu@ocbcwh.com)

### Credit Research

**Andrew Wong***Credit Research Analyst*[WongVKAM@ocbc.com](mailto:WongVKAM@ocbc.com)**Ezien Hoo***Credit Research Analyst*[EzienHoo@ocbc.com](mailto:EzienHoo@ocbc.com)**Wong Hong Wei***Credit Research Analyst*[WongHongWei@ocbc.com](mailto:WongHongWei@ocbc.com)**Seow Zhi Qi***Credit Research Analyst*[ZhiQiSeow@ocbc.com](mailto:ZhiQiSeow@ocbc.com)

This publication is solely for information purposes only and may not be published, circulated, reproduced or distributed in whole or in part to any other person without our prior written consent. This publication should not be construed as an offer or solicitation for the subscription, purchase or sale of the securities/instruments mentioned herein. Any forecast on the economy, stock market, bond market and economic trends of the markets provided is not necessarily indicative of the future or likely performance of the securities/instruments. Whilst the information contained herein has been compiled from sources believed to be reliable and we have taken all reasonable care to ensure that the information contained in this publication is not untrue or misleading at the time of publication, we cannot guarantee and we make no representation as to its accuracy or completeness, and you should not act on it without first independently verifying its contents. The securities/instruments mentioned in this publication may not be suitable for investment by all investors. Any opinion or estimate contained in this report is subject to change without notice. We have not given any consideration to and we have not made any investigation of the investment objectives, financial situation or particular needs of the recipient or any class of persons, and accordingly, no warranty whatsoever is given and no liability whatsoever is accepted for any loss arising whether directly or indirectly as a result of the recipient or any class of persons acting on such information or opinion or estimate. This publication may cover a wide range of topics and is not intended to be a comprehensive study or to provide any recommendation or advice on personal investing or financial planning. Accordingly, they should not be relied on or treated as a substitute for specific advice concerning individual situations. Please seek advice from a financial adviser regarding the suitability of any investment product taking into account your specific investment objectives, financial situation or particular needs before you make a commitment to purchase the investment product. OCBC Bank, its related companies, their respective directors and/or employees (collectively "Related Persons") may or might have in the future interests in the investment products or the issuers mentioned herein. Such interests include effecting transactions in such investment products, and providing broking, investment banking and other financial services to such issuers. OCBC Bank and its Related Persons may also be related to, and receive fees from, providers of such investment products.

This report is intended for your sole use and information. By accepting this report, you agree that you shall not share, communicate, distribute, deliver a copy of or otherwise disclose in any way all or any part of this report or any information contained herein (such report, part thereof and information, "Relevant Materials") to any person or entity (including, without limitation, any overseas office, affiliate, parent entity, subsidiary entity or related entity) (any such person or entity, a "Relevant Entity") in breach of any law, rule, regulation, guidance or similar. In particular, you agree not to share, communicate, distribute, deliver or otherwise disclose any Relevant Materials to any Relevant Entity that is subject to the Markets in Financial Instruments Directive (2014/65/EU) ("MiFID") and the EU's Markets in Financial Instruments Regulation (600/2014) ("MiFIR") (together referred to as "MiFID II"), or any part thereof, as implemented in any jurisdiction. No member of the OCBC Group shall be liable or responsible for the compliance by you or any Relevant Entity with any law, rule, regulation, guidance or similar (including, without limitation, MiFID II, as implemented in any jurisdiction).