Indonesia Outlook

OCBC Bank

The easing starts for BI

Thursday, July 18, 2019

Highlights

- **Bank Indonesia (BI) cut the benchmark rate by 25bps to 5.75%, in line with our expectations.**
- **Conditions have been favorable for BI to start easing amid a stronger IDR, moderate inflation and a global easing cycle.**
- **BI mentioned they believe that there is still space for monetary accommodation.**
- **Going forward, we believe BI may cut the benchmark rate one more time this year by 25bps, possibly within 3Q 2019, making it a total of 50bps of easing in 2019.**

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Bank Indonesia (BI) cut the benchmark rate by 25bps to 5.75%, in line with our expectations. The central bank noted that the cut was done in line with the lower expected inflation and the need to boost growth. Governor Perry Warjiyo also mentioned that the cut was done now as the impact of it may only be felt next year. He further warned that without the cut, the effects of the trade war could see economic growth slip below 5.2% yoy.

As a whole, BI painted a more subdued picture of both global and domestic growth in their statement. They expect the global trade environment to be affected by trade tensions and a slowing global economy. Meanwhile, they see that Indonesia's 2Q 2019 growth may be about the same as 1Q 2019 (5.1% yoy). For the entire year, they see that growth may come out below the midpoint of the range of 5.0 – 5.4%, with our own forecast being 5.1% yoy. They also expect that 2019 headline inflation would come out below the mid-range of 2.5 – 4.5% and our own expectation is 3.2% yoy. The IDR in their view would remain stable in line with market mechanisms. They also expect the current account deficit to be in the range of 2.5- 3.0% of GDP.

Conditions have become favorable for BI to start an easing cycle. The IDR is now stronger, hovering below the 14,000 level against the USD for the first time since early this year, supported by both bond and equity inflows. A global easing cycle has also set in with the Fed increasingly likely to cut by 25bps at the July FOMC. Meanwhile, headline inflation is also moderate and it is no constraint to monetary easing.

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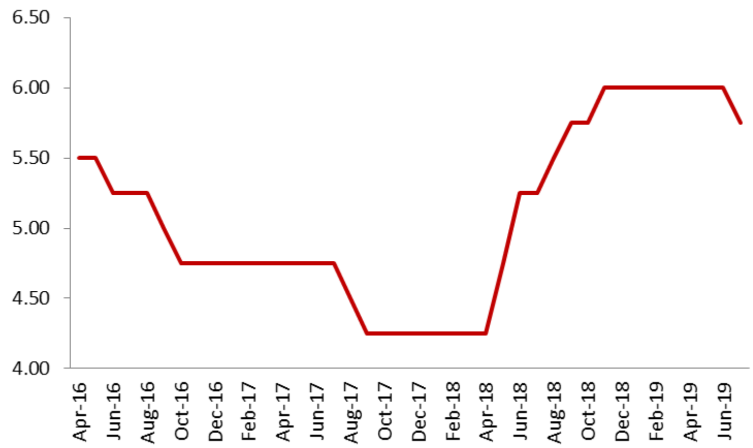
Hence, going forward, we believe BI may cut the benchmark rate one more time this year by 25bps, possibly within 3Q 2019, making it a total of 50bps of easing in 2019. After all, there appears to be strong hints of another cut as BI mentioned that they believe there is still space for monetary accommodation.

Chart 1: 7-Day Reverse Repo Rate, %



Source: CEIC, Bloomberg and OCBC