Macro Brief

Office of Chief Economist

BI 7-DAY (REVERSE) REPO RATE

19 October 2023

Bank Indonesia Unexpectedly Raised BI-7DRRR to 6.00% in Oct-23 Board of Governors Meeting.

Economic Indicators	2022	2023 Prognosis
Real GDP (% yoy)	5.31	5.04
Inflation (% yoy, eoy)	5.51	3.00
Inflation (% yoy, avg)	4.21	3.79
IDR/USD (eoy)	15,568	15,000-15,300
CA (% of GDP)	0.96	-0.65
BI 7-day RR Rate (%)	5.50	6.00

F = OCE BMRI forecast
yoy = year-on-year
eoy = end of year
avg = average

Key Rates (%)	Dec-22	Oct-23*
BI 7-day RR Rate	5.50	6.00
Deposit Facility Rate	4.75	5.25
Lending Facility Rate	6.25	6.75
IDR 10Y Bond Yield	6.92	7.05
Fed Funds Rate	4.50	5.50
ECB Rate	2.50	4.50
BoE Rate	3.50	5.25
BoJ Rate	-0.10	-0.10

**) as of 19-Oct-23*

Source: Bloomberg

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The decision was to ensure financial stability and that Indonesia has a robust external resilience amidst rising uncertainties in the global market.

- In Oct-23 governor meeting, Bank Indonesia (BI) unexpectedly raised its benchmark interest rate, the BI 7-Day Reverse Repo Rate (BI-7DRRR), by 25 bps to 6.00%. BI also raised the deposit facility rate by 25 bps to 5.25% and the lending facility rate to 6.75%, respectively.
- The increase is to strengthen and stabilize the financial market from the impact of rising global uncertainties. As of 18-Oct-23, Indonesia government 10 year bond yield was reaching to 6.92%, marking a 12.3 bps increase on mtd. Capital outflow in stock market was recorded at IDR 1.7 tn mtd, while outflow in government bond was even bigger, specifically reaching IDR 10.1 tn mtd.
- This decision was also a pre-emptive and forward-looking measures to mitigate risks of rising global energy and food prices which could influence imported inflation to domestic economy. By this being done, Bank Indonesia is making sure that domestic inflation remains under control within the target of 3.0±1% in 2023 and 2.5±1% in 2024.

Bank Indonesia also announced several measures to strengthen the stability of the financial market and the resilience of the economy.

- Amid the rising pressure on the currency, BI will continue the triple intervention measures I.e. intervention in the foreign exchange market in spot transactions, Domestic Non-Deliverable Forward (DNDF), and purchase of Government Securities (SBN) in the secondary market;
- Sekuritas Rupiah Bank Indonesia (SRBI) has showed progress in absorbing liquidity. Until the last auction on 13-Oct-23, nine auctions have been held, showing that nominal won on the auctions reached IDR 113.7 tn. Foreign investors also took participation as shown from foreign ownership recorded at 7% of the total (as of Sep-23).
- **Bank Indonesia announce new monetary instruments, Sekuritas Valuta Asing Bank Indonesia (SVBI) and Sukuk Valuta Asing Bank Indonesia (SUVBI) aimed to deepen the money market and support efforts to attract portfolio inflows.** These are foreign currency securities issued by BI with short-term tenor (≤1 year) using underlying assets in the form of foreign currency securities owned by Bank Indonesia. These instruments will begin to be implemented on 21-Nov-23. SVBI will be issued in tenors of 1, 3, 6, 9 and 12 months. The Sukuk Valuta Asing Bank Indonesia (SUVBI) is relatively similar in fashion, but using sharia principles. The SUVBI will be issued with tenors of 1, 3, and 6 months. Similar to SRBI, these instruments can also be transferred and owned by non-banks (residents or non-residents) in the secondary market.
- **BI will also continue to strengthen the implementation of liquidity incentive** I.e. the Macroprudential Liquidity Incentive Policy (KLM) to encourage bank credit/financing to priority sectors, including downstream (mineral and coal, agriculture, plantations, and fisheries), housing (including public housing), tourism and creative economy, MSMEs, KUR, Micro, and green which has been in effect since October 1, 2023. The measure is expected to add IDR50 tn of liquidity in the banking system. As of now, around 120 banks have utilized the incentives which create additional liquidity of IDR28.79 tn.

- **BI also issued liquidity easing policy by reducing the Macroprudential Liquidity Buffer (PLM) ratio** by 100 bps from 6% to 5% for Conventional Commercial Banks (BUK) with repo flexibility of 5%; and Islamic PLM ratio by 100 bps from 4.5% to 3.5% for Sharia Commercial Banks/Sharia Business Units (BUS/UUS), with repo flexibility of 3.5%. The policy is expected to bring an estimated additional liquidity of IDR81.5 tn and will be effective from December 1, 2023.
- **Other macroprudential measures maintaned** i.e. the Countercyclical Capital Buffer (CCyB) Ratio at 0% and the Macroprudential Intermediation Ratio (RIM) in the range of 84-94%.
- **Continuation of the relaxation of the Loan to Value/Financing to Value (LTV/FTV) ratio which was supposed to be completed by the end of 2023, extended until December 31, 2024;** for property loans to a maximum of 100% for all types of properties (landed houses, flats, and shop houses) for banks that meet certain NPL/NPF criteria, to encourage property sector credit growth. Down payment requirements for motor vehicle loans/financing to at least 0% for all types of new motor vehicles, to encourage credit growth in the automotive sector with the aim of driving economic growth from the banking and financing institutions.

Volatility and uncertainty in the global markets will remain high, hence Indonesia need to strengthen domestic economy.

- Bank Indonesia is cautious on several global conditions that need to be monitored: (1) Global economic growth is expected to experience slowdown in 2023, with a widening gap of growth divergence between countries. (2) Rising and unpredictable geopolitical risk, potentially causing an increase in world crude oil prices, as well as food prices, which can cause pressure on global inflation. (3) Higher for longer global policy rates especially in the US. Bank Indonesia sees there is a 40% probability that the Fed will raise interest rates in Dec-23 and may start to cut in the second half of 2024. (4) In the midst of this high uncertainty, there is a risk that investors will tend to be risk averse and switch to US Dollar. This will put pressure on capital outflows from emerging countries, including Indonesia.

Indonesia's economic growth so far remains robust, and inflation is effectively managed within the specified target range.

- **Credit in September 2023 grew 8.96% yoy,** slightly weaker compared to the previous month at 9.06% yoy. **Banking liquidity during September 2023 remained stable, with deposits growing at 6.54% yoy** or slightly higher compared to the previous month of 6.24%.
- **Domestic inflation remains well within Bank Indonesia's target and at a low level though facing some inflationary risk** particularly coming from the energy and food price. BI is currently collaborating with the government to ensure food price stability, particularly rice and beef. It is estimated that rice supply will be sufficient until the first quarter of 2024 in line with the government's efforts to secure supply through import, which will help maintain price stability until Lebaran. BI's forecast for inflation by the end of 2023 is around 3%.

OUR VIEW: BI's decision to raise rate along with other macroprudential measures will support financial stability which is needed for a resilient economy.

- Market volatility may remain high in the short term amid lingering concerns on global economic slowdown, *higher-for-longer* interest rates and the ongoing geopolitical tension in the middle east. The next key event to watch is the FOMC Meeting at Nov 23. Market consensus broadly expect the FFR to be unchanged, but hinted at a possible rate hike at the end of the year. Market also expects a rate cut can happen in the second half next year.

- On the domestic front, Indonesia's inflation rate has declined and consistently resides within the target range of 2 – 4%. Therefore, we think BI's main focus is now on the currency. Going forward, we think the current BI Rate should be sufficient to maintain the attractiveness of the Rupiah assets and attract capital flows, though this will still depend especially on Fed's monetary policy and the recent development of the geopolitical risk, particularly on the escalation of conflict between Israel and Hamas.

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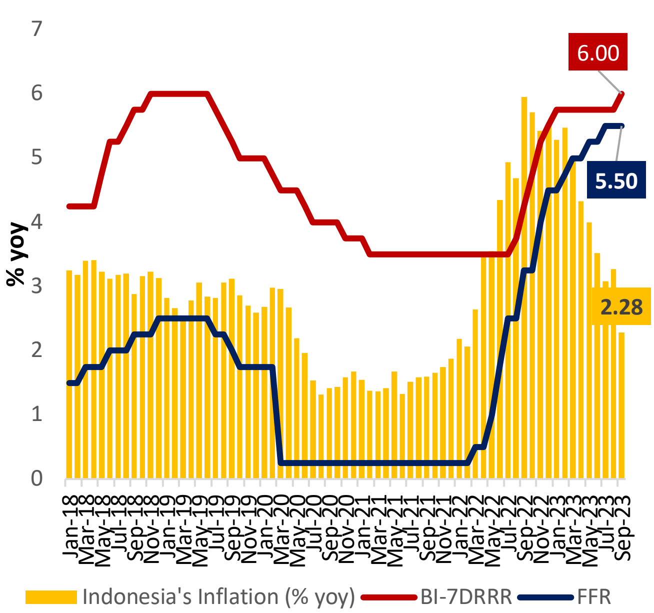
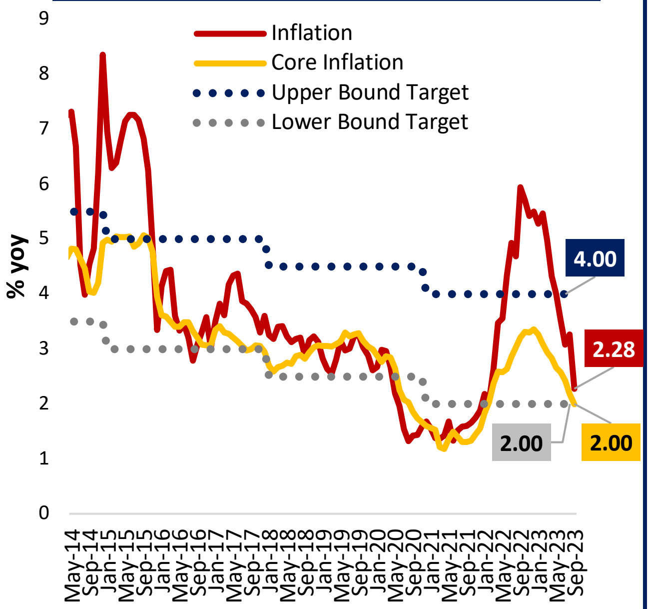


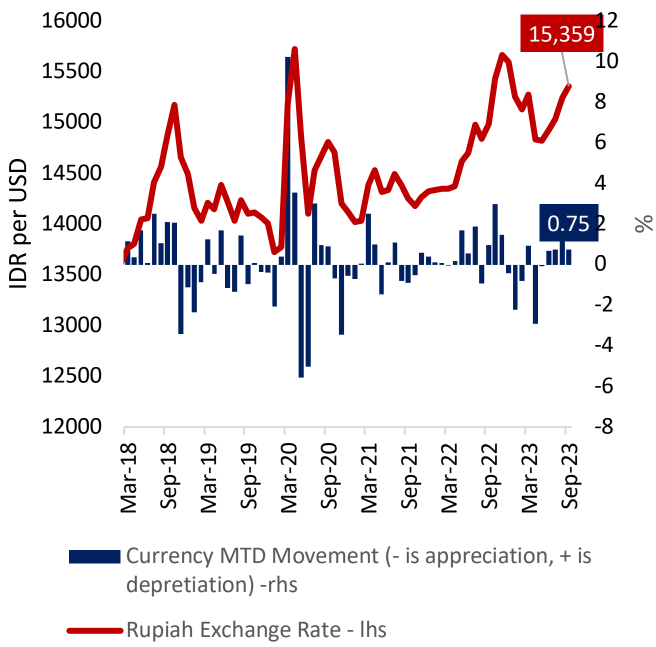
Source: Bank Indonesia, BPS, & the Fed

Inflation Rate Target



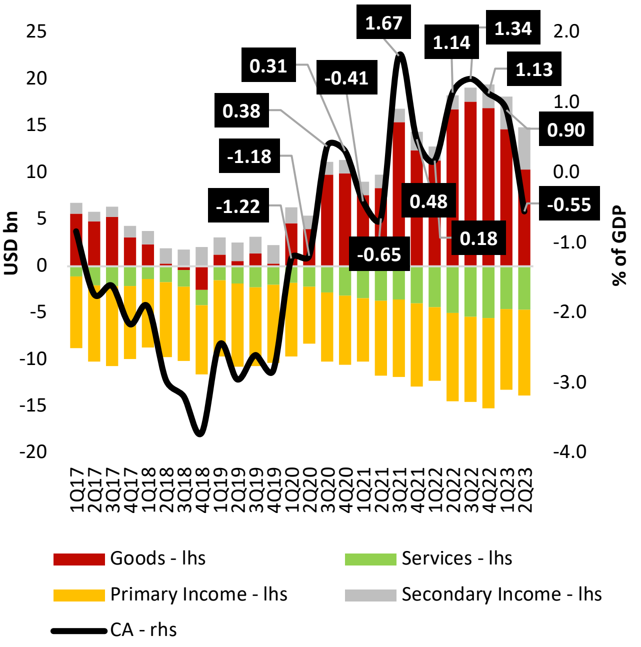
Source: Bank Indonesia & BPS

Rupiah Exchange Rate



Source: Bloomberg (as of 21-Sep-23)

Current Account Balance



Source: Bank Indonesia

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