

Trade:

Continued global slowdown: BI at the crossroads

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Executive Summary

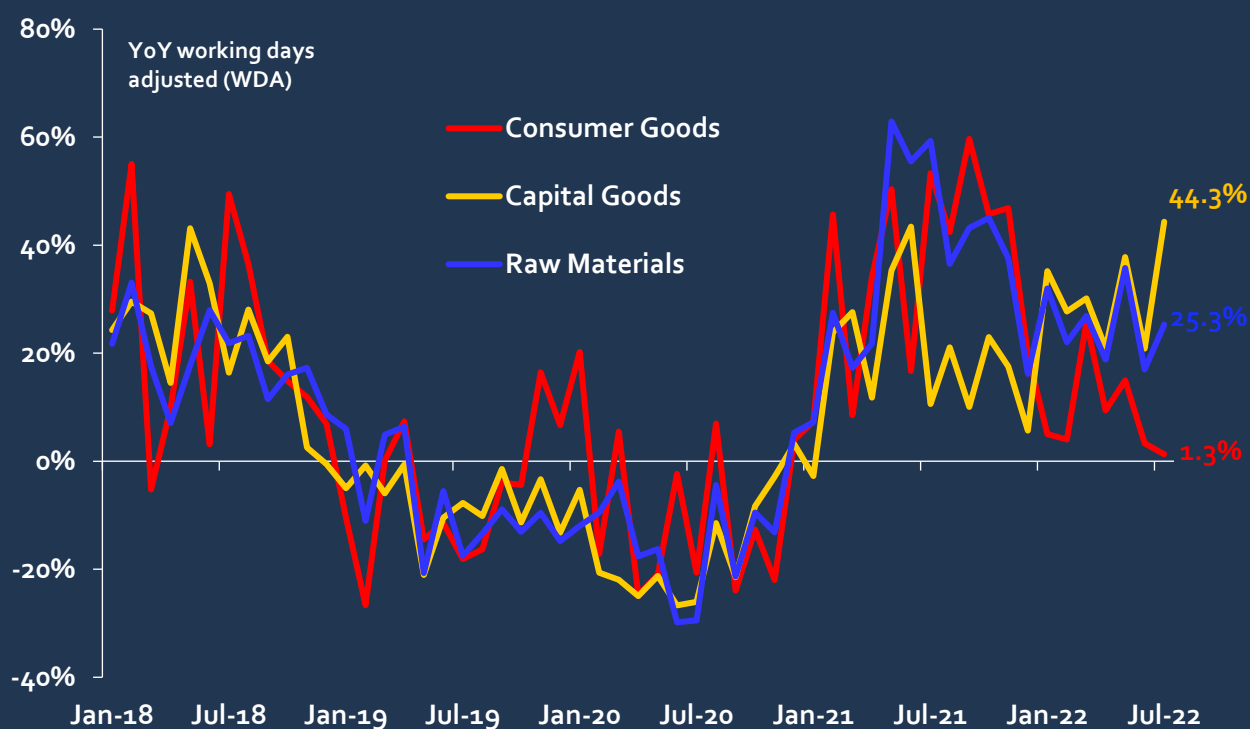
- Indonesia record trade balance of USD 4.23 billion, slight decline from June's figures but still above market expectations.
- Exports grew faster than expectations, driven by higher price and volume of coal exports. Imports grew mostly due to re-stocking of fuel and oil and rising business-related imports of capital and raw materials. Meanwhile imports of consumer goods decline as consumers remain wary of rising inflation despite strong confidence.
- The risk of global slowdown remains large. US inflation data shows signs of softening, raising possibility of "Fed Pause" scenario. China's zero Covid-19 policy, continued crackdown on property sector and further tensions with Taiwan risk disrupting global value chain and suppress domestic demand.
- Indonesia's reduced trade surplus will likely put BI under pressure to pursue more aggressive monetary policy, including raising its signature 7 day repo rate. However if the "Fed Pause" scenario, materialize, Indonesia will be ahead of the curve and reap benefits.

- Indonesia's trade balance decline slightly to USD 4.23 billion, with imports (39.86% YoY) rising much faster than exports (32.03% YoY). The surplus and its corresponding parts (exports & imports) defied market expectations as the surplus was larger (expectation USD 3.9 billion vs USD 4.23 billion) and both imports (expectation 31.02% vs reality 39.86%) and exports (expectation 28.7% vs reality 32.03%).
- Overall Indonesia's export and import data reflect the ongoing global and domestic slowdown seen in the previous months. Prices of staple exports (CPO & metals) all decline in the past month due to global consumption slowdown, fears of global recession and weaker than expected Chinese economic growth. Exports of coal increased slightly due to modest increase of volume and stable price of coal, even increasing 13% from the previous month as European energy crunch replace declining Chinese demand for coal.
- Meanwhile imports grew mostly due to re-stocking of fuel and oil products by state owned Pertamina, taking advantage of lower global oil price in July. The trend of rising business consumption, instead of consumer spending continues in July as imports of consumer goods further slows (1.3% YoY) compared to imports of capital (44.3%) and raw materials (25.3% YoY) (**Chart 1**). This is further vindication from our previous report that consumers do not

have much leeway for imported goods, although there is still considerable desire to consume as shown by rising core inflation, positive credit growth and solid consumer confidence.

- Moving ahead, the risk of a global slowdown and recession remains large. US inflation data suggest inflationary pressures are softening. This leads to market speculation on a rapid Fed “pause” or even reversal of its aggressive monetary tightening policy. However Fed officials have rebuked this possibility, due to still historically high core inflation and elevated inflation expectations in the short run and long run.
- Another major risk is China, which has been showing signs of continued weakness. Strict zero Covid-19 policy and crackdowns and restructuring in its property and “shadow banking” sector depressed consumer spending and overall growth. Meanwhile the authorities seem weary of launching any stimulus effort that might increase aggregate demand and create new bubbles. For the time being, the Chinese central bank PBoC cut its policy rates by 10bps and maintain liquidity in its banking system. Adding to this is further tensions with Taiwan that can exacerbate slowdown in the global value chain.
- In light of these risks, we believe that Indonesia’s trade surplus will continue to decline due to weak commodity prices and reduced export volumes to China. Fortunately the upcoming fuel prices may reduce demand for imported oil and consumer goods. Nevertheless it can still put substantial pressure on the Rupiah, especially if yield differentials between Indonesian and risk free US treasury rise and global investors are reluctant to return to emerging market bonds.
- Indonesian policy makers, including the fiscal authorities seem to have this in mind when discussing the 2023 budget as it projects lower revenues from commodity windfall and weaker Rupiah. It plans on greater expenditures on infrastructure and various projects such as the new capital and salary increments for civil servant. Subsidies remain the wildcard as it can reduce the government’s fiscal space substantially. This means growth in 2023 will be heavily supported by state budget in absence of commodity related sectors.
- For Bank Indonesia, recent developments unveils an interesting possibility. If the global outlook deteriorate rapidly-coupled with softening inflation expectations- cause the Fed gives away to “pause” scenario, it will put Indonesia ahead of the curve and possibly benefit in the short run. But the alternative, and the more likely scenario of continued Fed tightening, BI might need to finally use its signature 7 day policy repo rate to defend the Rupiah and slow increasing inflation pressures, sacrificing domestic recovery from the depths of the Covid-19 pandemic.

Chart 1. Business spending driving imports while consumer spending weaken



Source: BPS, BCA Research Team

Indonesia – Economic Indicators Projection

	2017	2018	2019	2020	2021	2022E
Gross Domestic Product (% YoY)	5.1	5.2	5.0	-2.1	3.7	5.1
GDP per Capita (US\$)	3877	3927	4175	3912	4350	4564
Consumer Price Index Inflation (% YoY)	3.6	3.1	2.7	1.7	1.9	5.2
BI 7 day Repo Rate (%)	4.25	6.00	5.00	3.75	3.50	4.50
USD/IDR Exchange Rate (end of year)**	13,433	14,390	13,866	14,050	14,262	15,070
Trade Balance (US\$ billion)	11.8	-8.5	-3.2	21.7	35.3	36.9
Current Account Balance (% GDP)	-1.6	-3.0	-2.7	-0.4	0.3	0.5

** Estimation of Rupiah's fundamental exchange rate

Selected Macroeconomic Indicator

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)	Trade & Commodities	12-Aug	-1 mth	Chg (%)
US	2.50	Jul-22	-6.00	Baltic Dry Index	1,477.0	2,013.0	-26.6
UK	1.25	Jun-22	-8.15	S&P GSCI Index	672.7	657.7	2.3
EU	0.50	Jul-22	-8.40	Oil (Brent, \$/bbl)	98.2	99.5	-1.3
Japan	-0.10	Jan-16	-2.50	Coal (\$/MT)	403.0	427.2	-5.7
China (lending)	4.35	Oct-15	1.65	Gas (\$/MMBtu)	8.75	6.81	28.5
Korea	2.25	Jul-22	-4.05	Gold (\$/oz.)	1,802.4	1,726.0	4.4
India	5.40	Aug-22	-1.31	Copper (\$/MT)	8,085.0	7,335.0	10.2
Indonesia	3.50	Feb-21	-1.44	Nickel (\$/MT)	22,963.5	21,320.0	7.7
				CPO (\$/MT)	999.4	957.2	4.4
				Rubber (\$/kg)	1.50	1.59	-5.7
Money Mkt Rates	12-Aug	-1 mth	Chg (bps)	External Sector	Jul	Jun	Chg (%)
SPN (1M)	1.91	2.66	-75.6	Export (\$ bn)	25.57	26.09	-2.0
SUN (10Y)	6.96	7.26	-29.3	Import (\$ bn)	21.35	21.00	1.6
INDONIA (O/N, Rp)	2.80	2.78	1.8	Trade bal. (\$ bn)	4.23	5.09	
JIBOR 1M (Rp)	3.77	3.54	23.3	Central bank reserves (\$ bn)*	132.2	136.4	-3.06
Bank Rates (Rp)	Apr	Mar	Chg (bps)	Prompt Indicators	Jul	Jun	May
Lending (WC)	8.49	8.59	-10.53	Consumer confidence index (CCI)	123.2	128.2	128.9
Deposit 1M	2.84	2.85	-1.17	Car sales (%YoY)	29.4	8.5	-9.3
Savings	0.62	0.63	-0.57	Motorcycle sales (%YoY)	-13.3	-30.9	-2.5
Currency/USD	12-Aug	-1 mth	Chg (%)	Cement sales (%YoY)	#N/A	-41.1	7.6
UK Pound	0.824	0.841	2.09	Capital Mkt	12-Aug	-1 mth	Chg (%)
Euro	0.975	0.996	2.21	JCI	7,129.3	6,718.3	6.12
Japanese Yen	133.4	136.9	2.59	DJIA	33,761.1	30,981.3	8.97
Chinese RMB	6.743	6.725	-0.27	FTSE	7,500.9	7,209.9	4.04
Indonesia Rupiah	14,668	14,988	2.18	Nikkei 225	28,547.0	26,336.7	8.39
				Hang Seng	20,175.6	20,844.7	-3.21
Foreign portfolio ownership (Rp Tn)	Jul	Jun	Chg (Rp Tn)	Manufacturing PMI	Jul	Jun	Chg (bps)
Stock	2,442.4	2,388.2	54.28	USA	52.8	53.0	-20
Govt. Bond	751.2	780.2	-28.98	Eurozone	49.8	52.1	-230
Corp. Bond	16.7	17.9	-1.14	Japan	52.1	52.7	-60
				China	50.4	51.7	-130
				Korea	49.8	51.3	-150
				Indonesia	51.3	50.2	110

Source: Bloomberg, BI, BPS

Notes:

^Data for January 2022

*Data from earlier period

For changes in currency: **Black indicates appreciation against USD, **Red** otherwise

***For PMI, >50 indicates economic expansion, <50 otherwise

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