FX Reserves:

The storm has passed for the Rupiah

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Executive Summary

- BI's FX reserves are finally rising again (to USD 134.0 Bn), as domestic FX liquidity is replenished by capital inflows amid rising expectations of an upcoming Fed pivot.
- The combination of global disinflation and China's reopening could provide a more favorable environment for the Rupiah.
- Nonetheless, there is ceiling as to how high the Rupiah could rebound, as many of the issues that have led to persistent domestic FX shortage remains in place.

- Bank Indonesia's foreign exchange reserves are finally rebounding, from USD 130.2 Bn in Oct-22 (a 30-month low) to USD 134.0 Bn in November. The increase is proximately attributed to FX revenues earned by the government and SOEs, but there are plenty of signs that point to a broader replenishment of FX supply in the whole economy.

- One indication is the increase in commercial banks' holdings of FX instruments issued by BI, which functions as an absorber of excess FX liquidity and add to BI's total reserves. The total amount outstanding rose by USD 2.4 Bn, which accounts for 62% of the increase in November, and shows that tight FX liquidity in the banking sector – a particular concern of ours since the start of the year – may be alleviated at last.

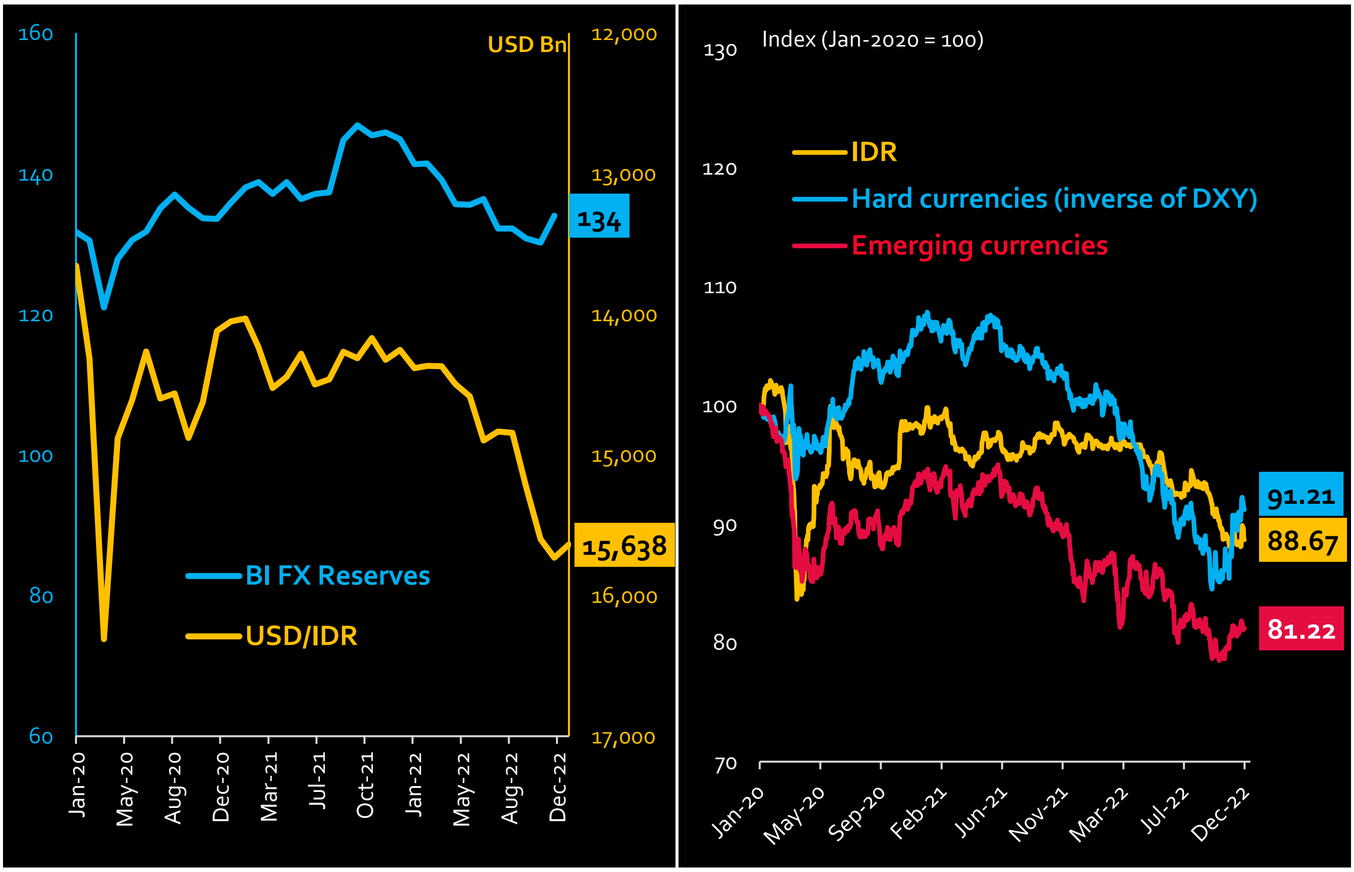
- To be sure, many of the issues involved are still there: overt dependence on the commodity terms-of-trade; export receipts not fully repatriated; yield gap between FX deposits at home and abroad; irregular reimbursement of subsidies that causes periodic tightness in the FX market as the two energy SOEs (Pertamina and PLN) look for financing. The first issue might in fact be worsening, as falling coal prices begin to weigh down on Indonesia's substantial trade surplus.

- But two things combined to attract foreign capital back into Indonesia. The first is a feverish expectations of a Fed pivot ahead of the FOMC's December meeting. The other is Indonesia's lower-than-expected inflation, which put it at the forefront of the global disinflation story – although, fortunately, still at the back of the global recession story.

- The impact of this abrupt shift in macro outlook was obviously more pronounced for bonds, which saw USD 1.5 Bn in net inflows compared to only USD 45 Mn for equities. And its positive impact was more visible on FX reserves rather than the USD/IDR exchange rate, as BI has pared down the scale of its interventions from earlier in the year.

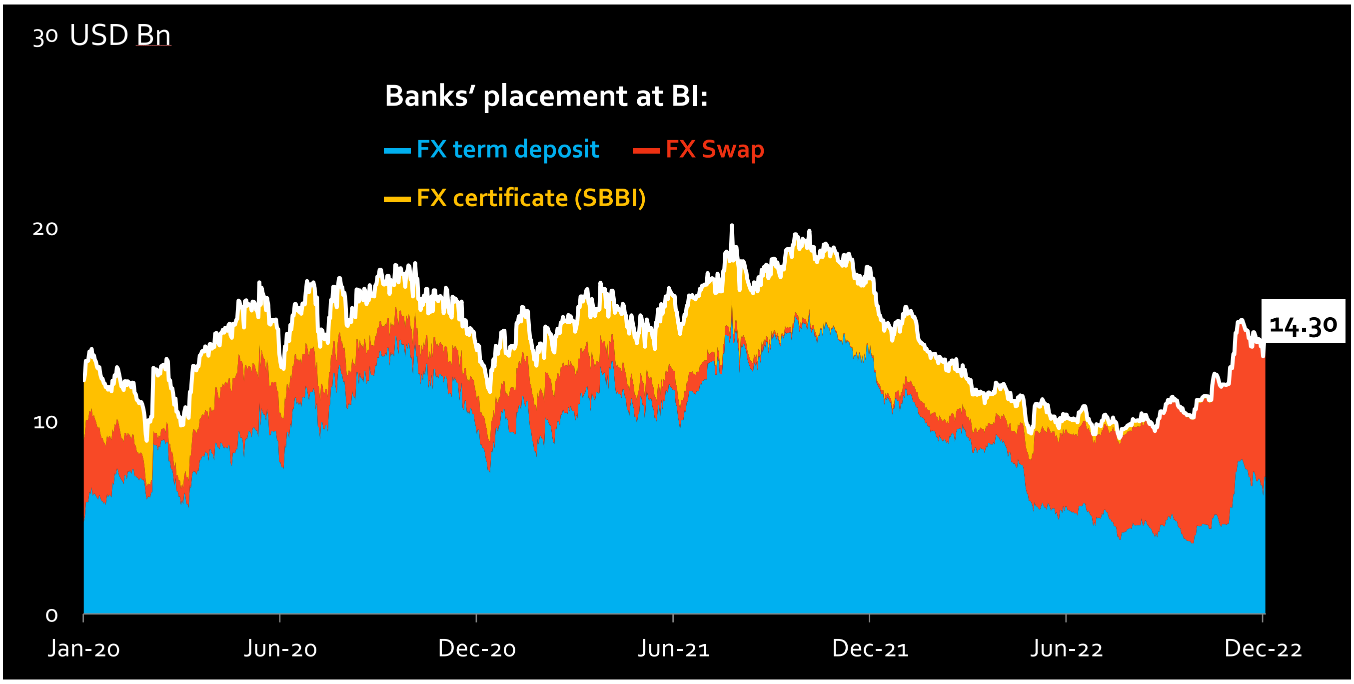
- Looking back, it does seem that the worst has passed for the Rupiah, following the joint pressure from an aggressive Fed and falling coal prices in October and early November. The current pivot narrative is a good start, but there are signs that the global economy could be slowing more drastically than currently expected – a hard landing rather than a soft one. In that scenario, commodities could fall further, but the Fed might also start to ease rather than simply keeping rates near current levels.
- For the Rupiah, this may well be the more favorable scenario. China's reopening should provide support for coal and CPO prices, while providing some uplift for other Asian economies. And perhaps more importantly, 2022 has proven that capital inflows are the more potent tonic for the Rupiah than current account surplus – especially since, as we mentioned, much of the export revenues are not repatriated to begin with.
- But there is also a ceiling as to how high the Rupiah could rebound. Our fundamental models, based on the balance of FX demand and supply, have been showing an FX shortage for quite some time, which makes the sharp depreciation in October seem "preordained" rather than the product of a temporary market mood swing. Unless there is a clear improvement in these fundamentals, we expect the Rupiah to remain near its current levels and BI to persist in its mildly cautious rate path.

***Panel 1.* The Rupiah and FX reserves have regained ground as the USD begins to weaken**



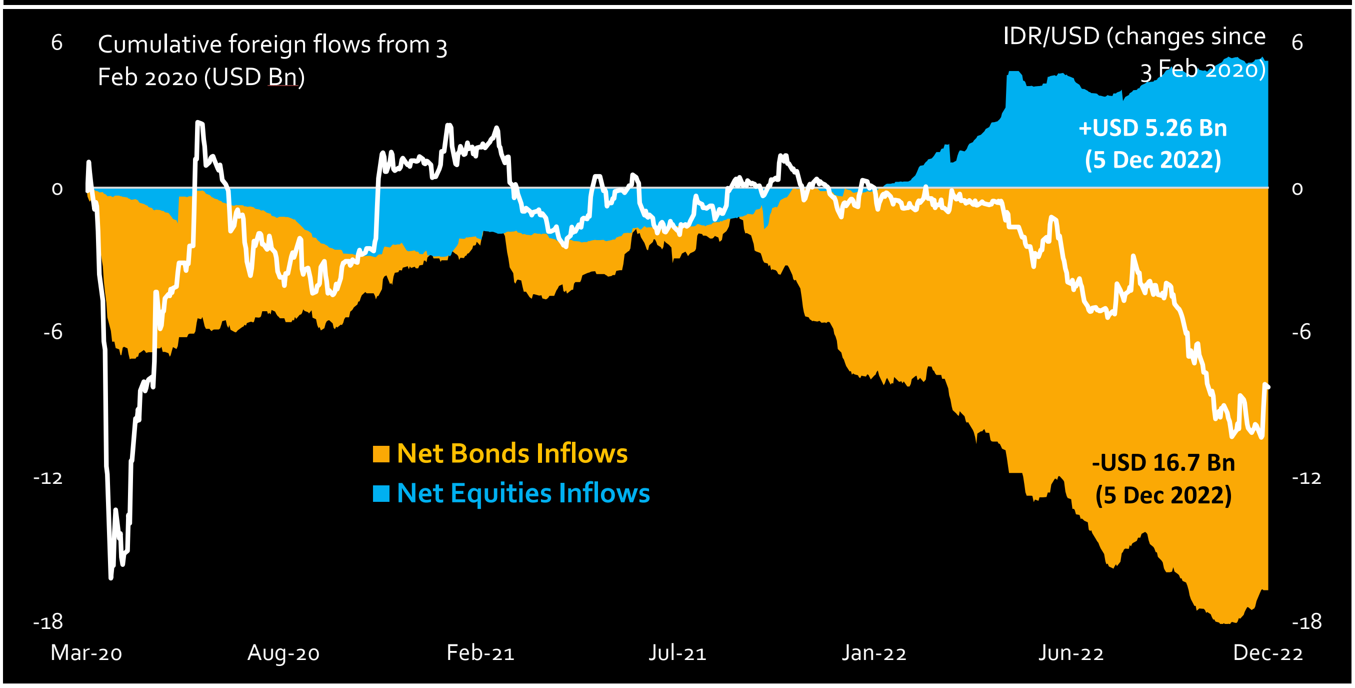
Source: Bloomberg

Panel 2. FX liquidity in the banking sector is starting to recover



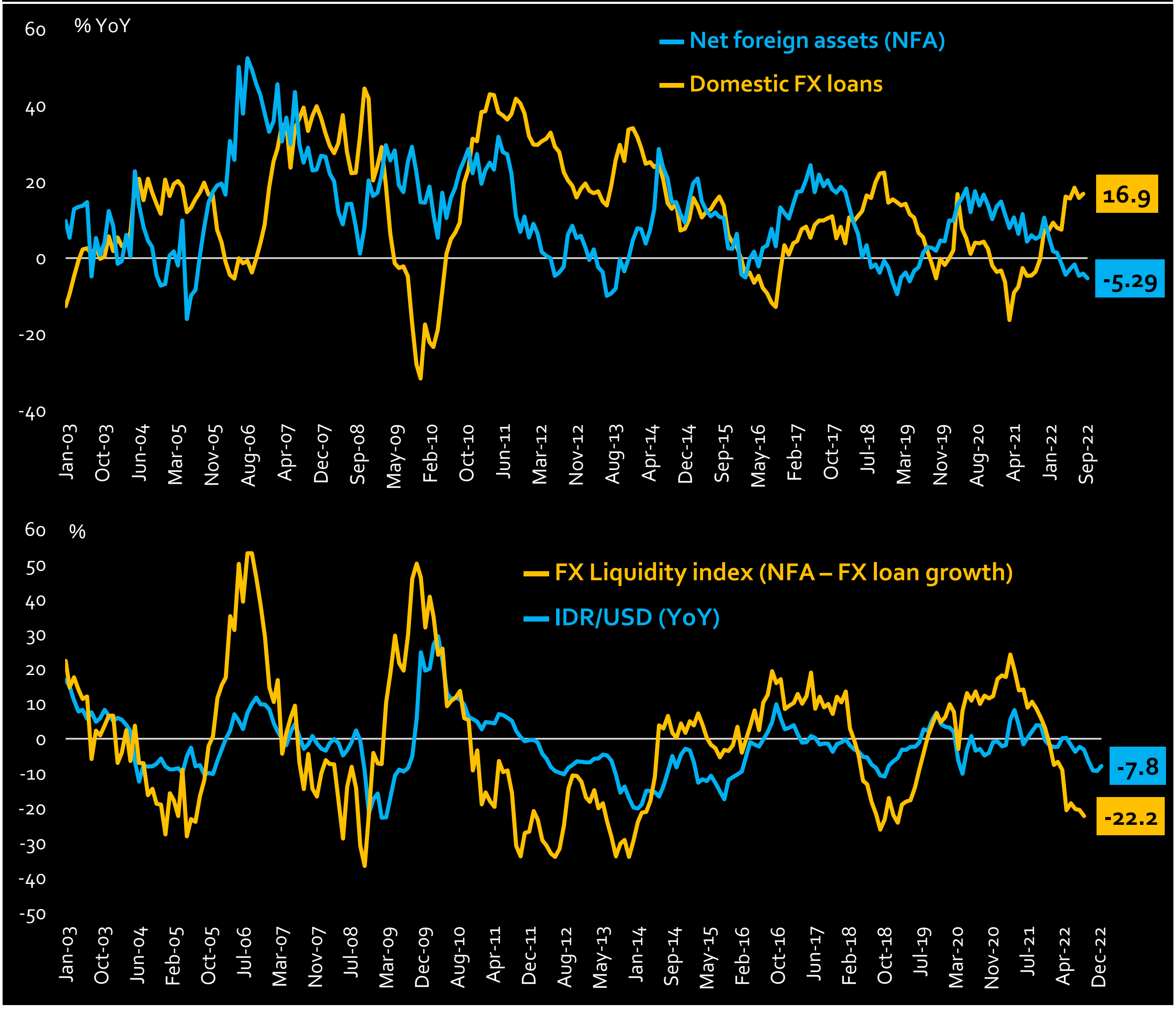
Source: BI

Panel 3. Bond inflows return as Fed pivot narratives take hold



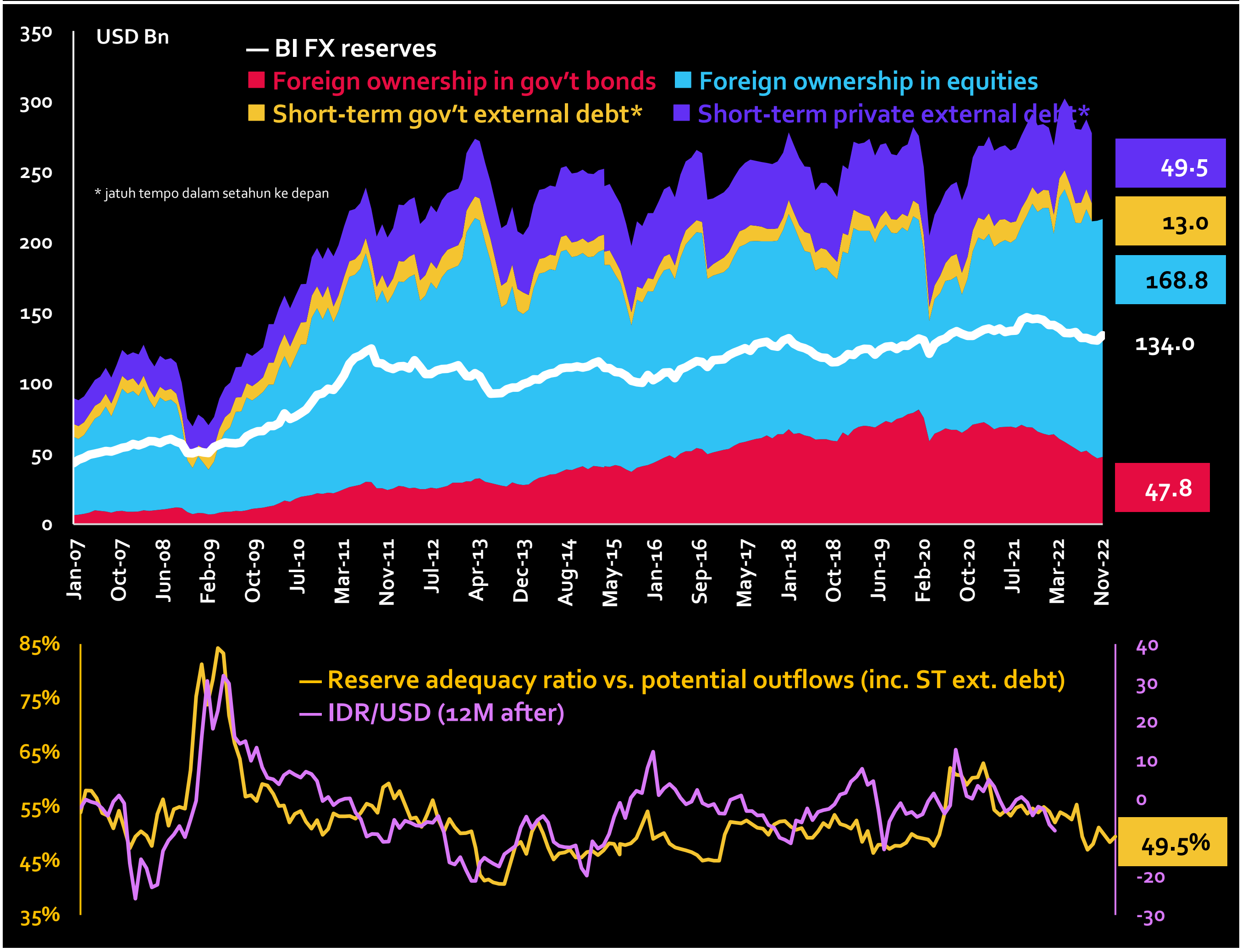
Source: Bloomberg

Panel 4. **Persistent FX shortage means the Rupiah's earlier plunge was always on the cards**



Source: BI, Bloomberg

Panel 5. **Despite the rebound, FX reserves still far from adequate to cover potential outflows**



Selected Macroeconomic Indicator

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)
US	4.00	Nov-22	-3.70
UK	3.00	Nov-22	-8.10
EU	2.00	Nov-22	-8.00
Japan	-0.10	Jan-16	-3.80
China (lending)	4.35	Nov-22	2.25
Korea	3.25	Nov-22	-1.75
India	6.25	Dec-22	-0.52
Indonesia	5.25	Nov-22	-0.17

Money Mkt Rates	6-Dec	-1 mth	Chg (bps)
SPN (1M)	4.11	4.96	-85.0
SUN (10Y)	6.93	7.44	-51.4
INDONIA (O/N, Rp)	4.82	4.30	52.2
JIBOR 1M (Rp)	5.95	5.43	51.7

Bank Rates (Rp)	Aug	Jul	Chg (bps)
Lending (WC)	8.42	8.42	-0.03
Deposit 1M	2.87	2.83	3.57
Savings	0.65	0.64	0.98

Currency/USD	6-Dec	-1 mth	Chg (%)
UK Pound	0.824	0.879	6.63
Euro	0.955	1.004	5.12
Japanese Yen	137.0	146.6	7.02
Chinese RMB	6.995	7.185	2.72
Indonesia Rupiah	15,618	15,738	0.77

Capital Mkt	6-Dec	-1 mth	Chg (%)
JCI	6,892.6	7,045.5	-2.17
DJIA	33,596.3	32,403.2	3.68
FTSE	7,521.4	7,334.8	2.54
Nikkei 225	27,885.9	27,199.7	2.52
Hang Seng	19,441.2	16,161.1	20.30

Foreign portfolio ownership (Rp Tn)	Nov	Oct	Chg (Rp Tn)
Stock	2,656.0	2,630.5	25.56
Govt. Bond	736.9	713.2	23.70
Corp. Bond	14.5	15.4	-0.86

Trade & Commodities	6-Dec	-1 mth	Chg (%)
Baltic Dry Index	1,340.0	1,323.0	1.3
S&P GSCI Index	579.2	665.9	-13.0
Oil (Brent, $/brl)	79.4	98.6	-19.5
Coal ($/MT)	402.0	345.8	16.3
Gas ($/MMBtu)	4.01	4.39	-8.5
Gold ($/oz.)	1,771.0	1,681.9	5.3
Copper ($/MT)	8,384.8	8,136.0	3.1
Nickel ($/MT)	29,142.0	23,721.0	22.9
CPO ($/MT)	888.0	883.2	0.5
Rubber ($/kg)	1.34	1.24	8.1

External Sector	Oct	Sep	Chg (%)
Export ($ bn)	24.81	24.78	0.1
Import ($ bn)	19.14	19.81	-3.4
Trade bal. ($ bn)	5.67	4.97	14.2
Central bank reserves ($ bn)*	134.0	130.8	2.46

Prompt Indicators	Oct	Sep	Aug
Consumer confidence index (CCI)	120.3	117.2	124.7
Car sales (%YoY)	23.3	18.9	16.4
Motorcycle sales (%YoY)	20.9	10.7	11.6

Manufacturing PMI	Nov	Oct	Chg (bps)
USA	49.0	50.2	-120
Eurozone	47.1	46.4	70
Japan	49.0	50.7	-170
China	49.4	49.2	20
Korea	49.0	48.2	80
Indonesia	50.3	51.8	-150

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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Indonesia – Economic Indicators Projection

	2017	2018	2019	2020	2021	2022E
Gross Domestic Product (% YoY)	5.1	5.2	5.0	-2.1	3.7	5.3
GDP per Capita (US$)	3877	3927	4175	3912	4350	4564
Consumer Price Index Inflation (% YoY)	3.6	3.1	2.7	1.7	1.9	5.6
BI 7 day Repo Rate (%)	4.25	6.00	5.00	3.75	3.50	5.5
USD/IDR Exchange Rate (end of year)**	13,433	14,390	13,866	14,050	14,262	15,584
Trade Balance (US$ billion)	11.8	-8.5	-3.2	21.7	35.3	52.8
Current Account Balance (% GDP)	-1.6	-3.0	-2.7	-0.4	0.3	0.9

** Estimation of Rupiah's fundamental exchange rate

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