

A darker cloud does not mean an end to a sunny day

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Summary

- The ongoing debt-ceiling crisis may translate to some adverse impact on the US economy, especially if the government decided to cut spending on healthcare. Intensifying partisanship have elevated the debt ceiling debacle into a regular event.
- The market remains sanguine over the prospect of the US government defaulting on its debt as the Treasury has developed strategies to avoid default while the Fed had shown capabilities to restore the normal functioning of the market.
- Continuous improvement in China's economic activity and the upcoming earnings season may help to strengthen the still-positive sentiment for Indonesian assets.

- Markets continue to breeze along in the fourth week of 2023. This time around, however, the good news largely comes from Asia. The Bank of Japan had successfully defended its YCC policy from another round of attacks from bond vigilantes, while China broke the internet with colourful economic data from Q4-2022. China's GDP in Q4-2022 grew above market expectations (2.9% YoY actual vs 1.8% YoY consensus), driven by strong industrial production growth that signals strengthening domestic aggregate demand (albeit still negative, but weaker retail sales growth). Continuing the trend, foreign capital flowed into Indonesia's bond market to the tune of USD 789.6 million last week, while the domestic stock market also recorded around USD 64.2 million in capital

inflow. Improving FX liquidity condition, of course, help the Rupiah to stabilise following a steep rally a couple of weeks ago.

- Unfortunately, however, brighter skies in Asia mean darker clouds brewing elsewhere; this time on top of Capitol hill in the US. US Treasury Secretary Janet Yellen broke the news last week that the US government would be unable to raise new debt after breaching the USD 31.4 trillion debt ceiling on 19 January 2023. We should recall, of course, that the split congress after the 2022 mid-term elections make it hard for the US government to raise the debt ceiling without giving some concessions to the Republicans. In hindsight, House Republicans want a smaller budget in return for a higher debt ceiling. The Democrat-controlled White

House, however, wants to deliver on their campaign promises that require continuous fiscal expansion. No sides want to lose, locking them in a game of brinkmanship that may risk the US government default on its debt.

- We have to consider, however, that the ongoing debt ceiling debacle is likely a short-term problem. Even in the height of the game of brinkmanship during the 2011 and 2019 episodes, the two political sides were always able to (eventually) reach a consensus to lift the debt ceiling. Alas, **a slight threat to US treasuries’ “moneyness” may bring volatility to the now calm and optimistic market, and the increasing partisanship may have locked the debt ceiling problem into a built-in feature of US politics.** Fortunately, multiple episodes of bipartisan infighting over the debt ceiling has led the US Treasury (and the Fed) to develop their ‘how-to-cope-with-the-bickering-over-the-debt-ceiling’ playbook. The first option, and the most discussed one, is for the US Treasury to prioritise the payment of debt-servicing obligations. This mean, however, that the government would have to deliver some form of fiscal contraction, at a time when the private sector is slowing.
- **Payment prioritisation, then, is not exactly ideal for a government fighting to avoid a short-term recession risk.** More astute US political observers have noted that the Biden administration may face political difficulty if they choose to moderate the budget that has been appropriated for the IRA act of 2022

“Despite the ongoing debt ceiling debacle is not a primary source of concern for those in the market”

(President Biden’s flagship bill), which leaves military and healthcare spending as expenses most likely to be re-appropriated. Moderating aid for Ukraine is straightforward; spending on foreign grants offers little multiplier for the domestic economy, and many in the Republican party have questioned the merit of foreign aid when the US economy is not in an ideal shape. But lower spending on healthcare, which largely targets low-income group (and hence, offer a higher fiscal multiplier) would reduce US consumers’ disposable income, worsening sentiment that may hasten the coming of the next recession.

- If the debt ceiling problem is indeed a short-term (but regular) problem, the US government may look for another option.

The US Treasury could choose to pay off treasury bills to increase the headroom in the short-term, prioritising issuance of longer-dated treasury notes **(see Chart 1)**. This option, however, may only isolate volatility to one segment of

the market, namely the bill market as bill investors such as money market funds would be deprived of their favourite investments. In this regard, then, the Fed’s intervention may still be needed. The central bank’s decision to double the reverse repurchase agreement (RRP) counterparty limit to USD 160 billion last September may be enough to accommodate increasing demand from bill investors, deflating volatility in the bill market. In the short run, however, **this intervention could translate to a slower pace of the Fed’s balance sheet reduction,**

as the ongoing QT necessitates banks and MMFs to shift their liquidity from the central bank's liabilities to the government's (and private) ones.

- Letting the market feel the pain (to an extent) of market volatility may be productive to entice Congress to react and lift the debt ceiling. But **apart from some manoeuvre out of Treasury bills that would mature around the X-date (which some belief would be around June 2023), many in the market remain relatively sanguine (see Chart 2 & 3).** Indeed, tools developed after the 2008 financial crisis has provided the Fed with ample capabilities to maintain liquidity and deflate volatility in the market. For instance, even if the US government cannot avoid defaulting on some treasury bills, some have speculated that the Fed could accept

the defaulted assets as collateral, restoring the normal functioning of the market.

- It is safe to say, then, despite some probable adverse impact on the US real economy, the ongoing debt ceiling debate is not a primary source of concern for those in the financial market. FOMC members' still-hawkish talks ahead of the February FOMC meeting have not hampered the enthusiasm of those in the 'Fed pivot' camp as the projected 25 bps in the next meeting has largely been priced in. **Industrial commodity prices had also begun to creep up as the Chinese market gets busier, strengthening the sentiment for commodity-exporting markets such as Indonesia.** Indeed, the stage is set for Indonesian assets to continue its rally, and the upcoming earnings season may help to provide another boost to the now-effervescent sentiment.

Chart 1

Careful planning is the key

The US Treasury could avoid default by paying off shorter-tailed treasury bills in favour of longer-tailed treasury notes

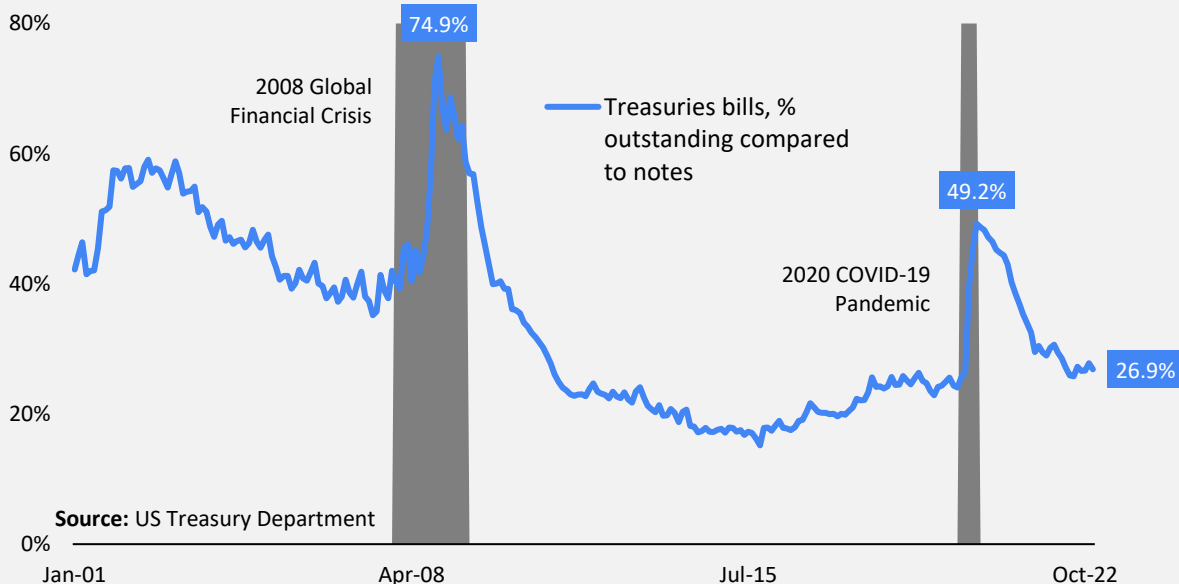


Chart 2

Evasive manoeuvre

The yield on US 6M treasury bills rose higher as investors are avoiding bills that would mature around the hypothetical June 2023 X-date while trading for treasuries of other maturities

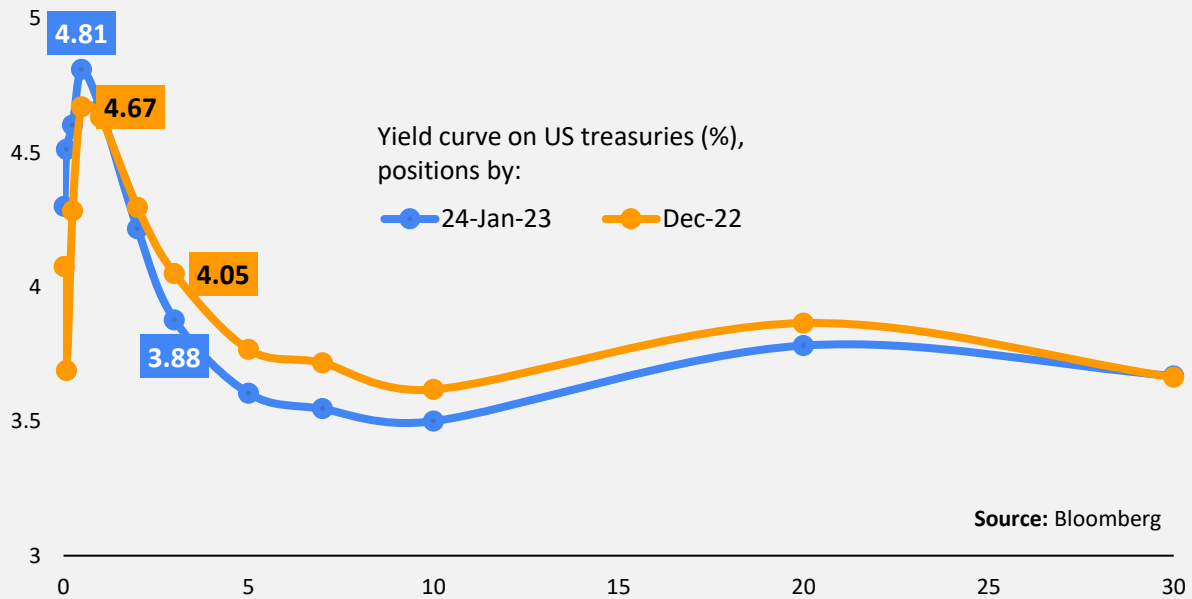
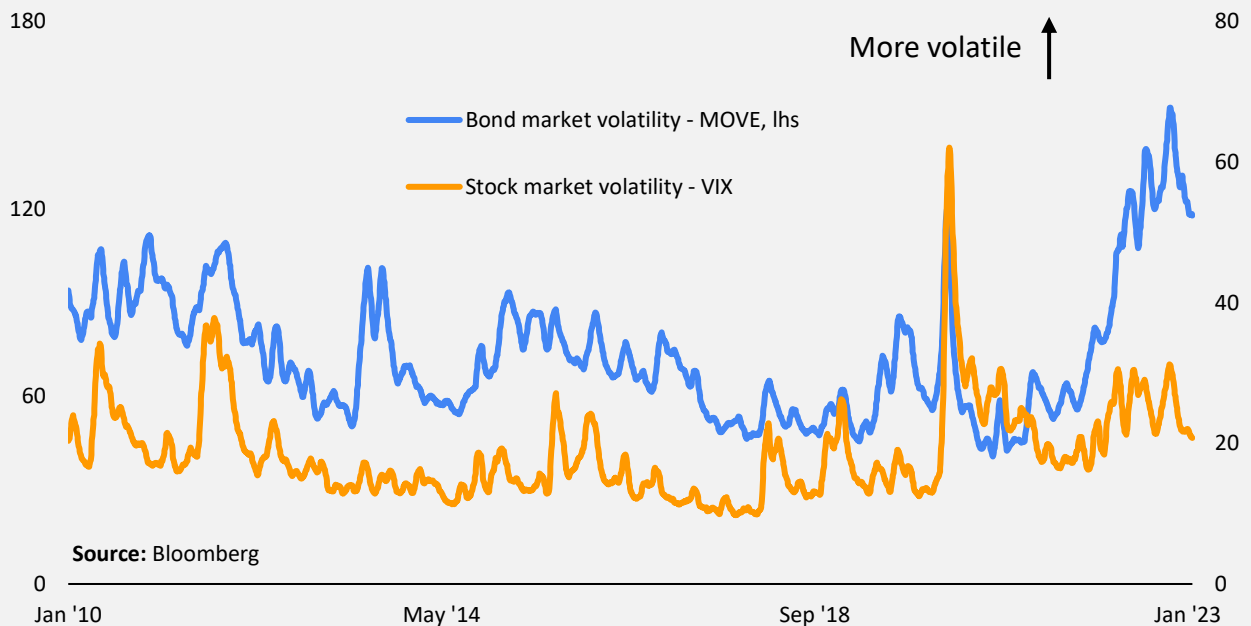


Chart 3

Calm and steady

Bond market volatility continue to decline despite the prospect of default, courtesy of the Fed's credibility in restoring the normal functioning of the market



Economic Calendar				
		Actual	Previous	Forecast*
9 January 2023				
ID	Consumer confidence	119.9	119.1	115
10 January 2023				
ID	Retail sales YoY	1.3%	3.7%	-
12 January 2023				
CN	CPI Inflation YoY	1.8%	1.6%	2%
US	CPI Inflation YoY	6.45%	7.1%	6.7%
13 January 2023				
CN	Balance of trade (USD Bn)	78.0	69.8	80
16 January 2023				
ID	External debt (USD Bn)	392.6	390.2	-
ID	Balance of trade (USD Bn)	3.89	5.1	3.57
17 January 2023				
CN	Industrial Production	-	2.2%	3.8%
CN	GDP Growth Q4 2022 (YoY)			
18 January 2023				
US	Producer Price Index	-	0.3%	0.3%
US	Retail Sales	-	-0.6%	0.3%
19 January 2023				
ID	Bank Indonesia policy announcement	5.75%	5.5%	5.75%
24 January 2023				
ID	Foreign and Domestic Direct Investments Q4 2022 (YoY)	43.3%	63.6%	
ID	M2 Money Supply (YoY)	8.3%	9.5%	
27 January 2023				
US	Personal income MoM	-	0.4%	0.3%
US	Personal spending MoM	-	0.1%	0.1%

*Forecasts of some indicators are simply based on market consensus

Bold indicates indicators covered by the BCA Monthly Economic Briefing report



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Selected Macroeconomic Indicator

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)	Trade & Commodities	23-Jan	-1 mth	Chg (%)
US	4.50	Jan-23	-2.00	Baltic Dry Index	740.0	1,515.0	-51.2
UK	3.50	Jan-23	-7.00	S&P GSCI Index	618.9	605.8	2.2
EU	2.50	Jan-23	-6.70	Oil (Brent, \$/bbl)	88.2	83.9	5.1
Japan	-0.10	Jan-16	-4.10	Coal (\$/MT)	273.8	313.6	-12.7
China (lending)	4.35	Jan-23	2.55	Gas (\$/MMBtu)	3.42	7.49	-54.3
Korea	3.50	Jan-23	-1.50	Gold (\$/oz.)	1,931.0	1,798.2	7.4
India	6.25	Dec-22	0.53	Copper (\$/MT)	9,330.8	8,328.0	12.0
Indonesia	5.75	Jan-23	0.24	Nickel (\$/MT)	27,895.0	29,377.0	-5.0
Money Mkt Rates	23-Jan	-1 mth	Chg (bps)				
SPN (1M)	3.41	4.37	-96.1				
SUN (10Y)	6.61	6.90	-28.7				
INDONIA (O/N, Rp)	5.19	4.97	22.3				
JIBOR 1M (Rp)	6.43	6.18	24.4				
Bank Rates (Rp)	Sep	Aug	Chg (bps)				
Lending (WC)	8.46	8.42	3.71				
Deposit 1M	2.97	2.87	10.38				
Savings	0.66	0.65	0.76				
Currency/USD	23-Jan	-1 mth	Chg (%)				
UK Pound	0.808	0.830	2.70				
Euro	0.920	0.942	2.40				
Japanese Yen	130.7	132.9	1.71				
Chinese RMB	6.785	6.990	3.03				
Indonesia Rupiah	15,075	15,593	3.44				
Capital Mkt	23-Jan	-1 mth	Chg (%)				
JCI	6,874.9	6,800.7	1.09				
DJIA	33,629.6	33,203.9	1.28				
FTSE	7,784.7	7,473.0	4.17				
Nikkei 225	26,906.0	26,235.3	2.56				
Hang Seng	22,044.7	19,593.1	12.51				
Foreign portfolio ownership (Rp Tn)	Dec	Nov	Chg (Rp Tn)				
Stock	2,699.4	2,656.0	43.37				
Govt. Bond	762.2	736.9	25.26				
Corp. Bond	12.5	14.5	-2.05				
				External Sector	Dec	Nov	Chg (%)
				Export (\$ bn)	23.83	24.09	-1.1
				Import (\$ bn)	19.94	18.96	5.2
				Trade bal. (\$ bn)	3.89	5.13	-24.2
				Central bank reserves (\$ bn)*	137.2	134.0	2.39
				Prompt Indicators	Dec	Nov	Oct
				Consumer confidence index (CCI)	119.9	119.1	120.3
				Car sales (%YoY)	9.0	4.4	23.3
				Motorcycle sales (%YoY)	24.6	26.9	20.9
				Manufacturing PMI	Dec	Nov	Chg (bps)
				USA	48.4	49.0	-60
				Eurozone	47.8	47.1	70
				Japan	48.9	49.0	-10
				China	49.0	49.4	-40
				Korea	48.2	49.0	-80
				Indonesia	50.9	50.3	60

Source: Bloomberg, BI, BPS

Notes:

^Data for January 2022

*Data from an earlier period

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

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

Indonesia – Economic Indicators Projection

	2018	2019	2020	2021	2022	2023E
Gross Domestic Product (% YoY)	5.2	5.0	-2.1	3.7	5.3*	4.6
GDP per Capita (US\$)	3927	4175	3912	4350	4564*	4525
Consumer Price Index Inflation (% YoY)	3.1	2.7	1.7	1.9	5.5	4.4
BI 7-day Repo Rate (%)	6.00	5.00	3.75	3.50	5.50	6.00
USD/IDR Exchange Rate (end of the year)**	14,390	13,866	14,050	14,262	15,568	16,292
Trade Balance (US\$ billion)	-8.5	-3.2	21.7	35.3	55.8*	43.2
Current Account Balance (% GDP)	-3.0	-2.7	-0.4	0.3	0.9*	-0.2

*Estimated number

** Estimation of the Rupiah's fundamental exchange rate

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