Balance of payments:
Heights come before a fall

Barra Kukuh Mamia
Senior Economist

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Executive Summary

- The balance of payment (BoP) recorded a large surplus of USD 4.7 Bn in Q4-22, thanks to a USD 4.3 Bn current account (CA) surplus and a narrow USD 0.5 Bn financial account (FA) deficit.
- The CA surplus for the whole year amounted to 1.0% of the GDP, but this is likely to flip into a deficit in 2023 due to the decline in coal prices, an increase in import of services, and the still-strong financing into SMEs and consumers.
- The FA deficit improved thanks to bond inflows and a crackdown on un-repatriated export receipts, but FDI inflows continues to lag reported FDI realization – meaning that support for the Rupiah remains dependent on global liquidity conditions and portfolio flows.

- The current account (CA) picture in Q4-22 was pretty much a redux of Q3-22, and with almost identical results too. The CA surplus, at 1.30% of the GDP (USD 4.3 Bn), was only marginally lower than Q3's 1.34%; and it solidified 2022 as the year when Indonesia's CA returned to its past glories during the 2000's.

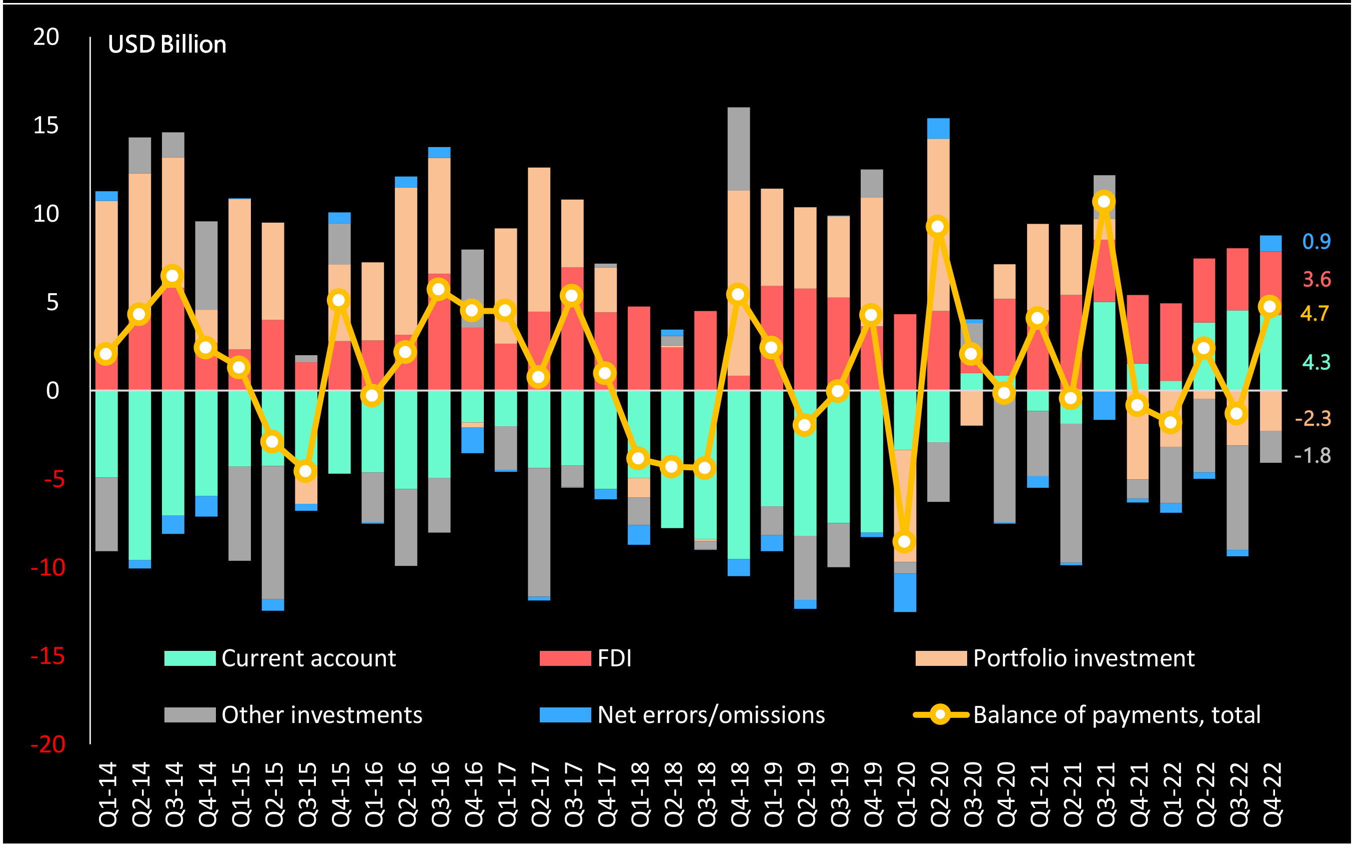
- Except that this might be a blip rather than a trend. As we have noted in our report on trade, it is nigh impossible for Indonesia to retain CA surplus at current coal prices, and a deficit of about 1.0% of the GDP – much wider than our initial forecast of -0.2% – could beckon for 2023.

- Two other things strengthen our argument of a wider-than-expected deficit this year. The first is that loan growth has remained strong, particularly for the mostly import-oriented SMEs and consumers. This burgeoning loan growth has hitherto been offset by robust deposit growth, driven in part by producers of coal (and other commodities). With this liquidity source removed, however, we may see a rapid increase in loan-to-deposit ratio (LDR), which almost always go hand-in-hand with a wider CA deficit.

- The second factor is the services deficit, which Indonesia has always suffered from to an extent, but which could be a bigger problem after the pandemic. As international shipping recovered, payments to foreign shipping lines and freight insurance naturally follows. Furthermore, the pandemic has spurred demand for new digital services – from Zoom to Netflix to crypto exchanges – which shows up as rapid growth in "telecommunication and IT imports" and also potentially in "other business service imports" during the past two years.

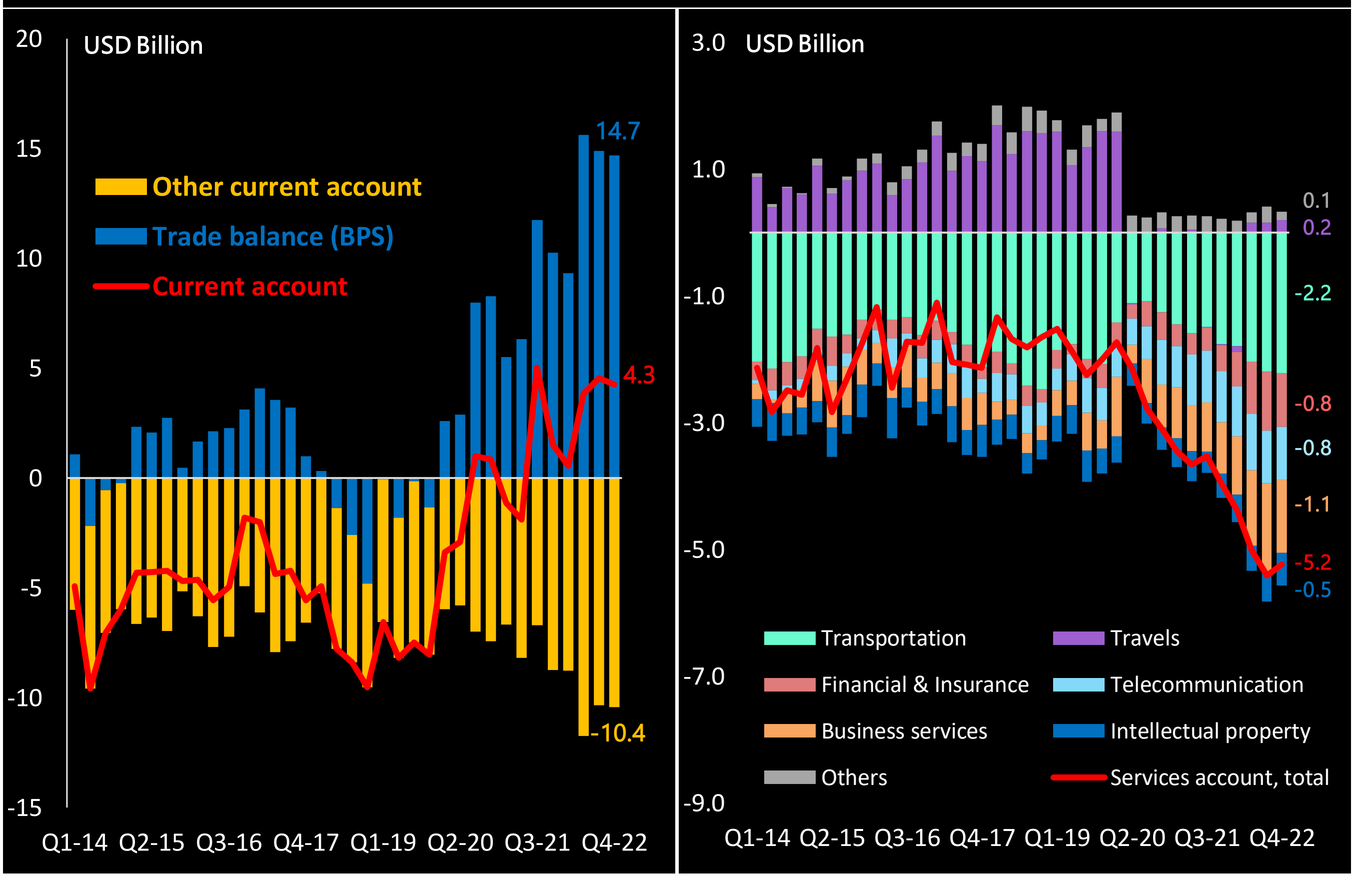
- One thing we can look forward to which could improve the services deficit is tourism. Prior to the pandemic, Indonesia made around USD 1.4 Bn per months in earnings, out of roughly 1.2 Mn foreign visitors coming in monthly. By Q4-22, the numbers stood at USD 0.8 Mn and 740 thousands, respectively – i.e. at half strengths – and the surplus was unfortunately offset by a sharp increase in outbound tourism. As the situation normalizes over the coming 1-2 years, we expect this corner of the surplus from tourism to return in full strength.
- But if CA is about to worsen next quarter, then at least the financial account (FA) is doing better, right? And indeed, the FA deficit in Q4-22 (at USD 0.5 Bn) was already much better compared to the previous quarters in 2022, thanks to the return of foreign inflows into bonds and the decline in outflows from "other assets".
- These "other assets", we should clarify, covers all the non-FDI, non-portfolio outflows from Indonesia. As such, it includes nostro bank accounts (foreign bank accounts registered to Indonesian nationals) as well as other items that could be used to retain export receipts abroad.
- Its decline, coupled with a similar trend for net errors and omissions (NEO) – a well-known proxy of illicit flows – could be a sign that BI's crackdown on exporters that fail to repatriate their earnings ("the stick") is working. Now we just have to wait if "the carrot", i.e. incentives on repatriated export receipts (effective March 1st), would work similarly well.
- With bond inflows returning, illicit outflows curbed, and FX reserves recovering, there remains only one of the "four gaps" that we identified in our previous report about the BoP: that between FDI as reported by BKPM and the actual FDI-related inflows as recorded by BI. This may well be a long-term issue given its persistence and its widening gap, and it does mean that portfolio inflows are still required to stabilize the Rupiah – especially now that the CA is turning towards a deficit.
- With this in mind, we think that the end of BI's rate hike cycle is not yet the end of its conservative tilt, with neither the BI 7-day Repo Rate nor the reserve requirement ratio likely to be lowered in the near future. Some interventions in the bonds and FX market could also return if needed.

Chart 1. **Current account surplus in 2022 had been offset by financial account deficit**



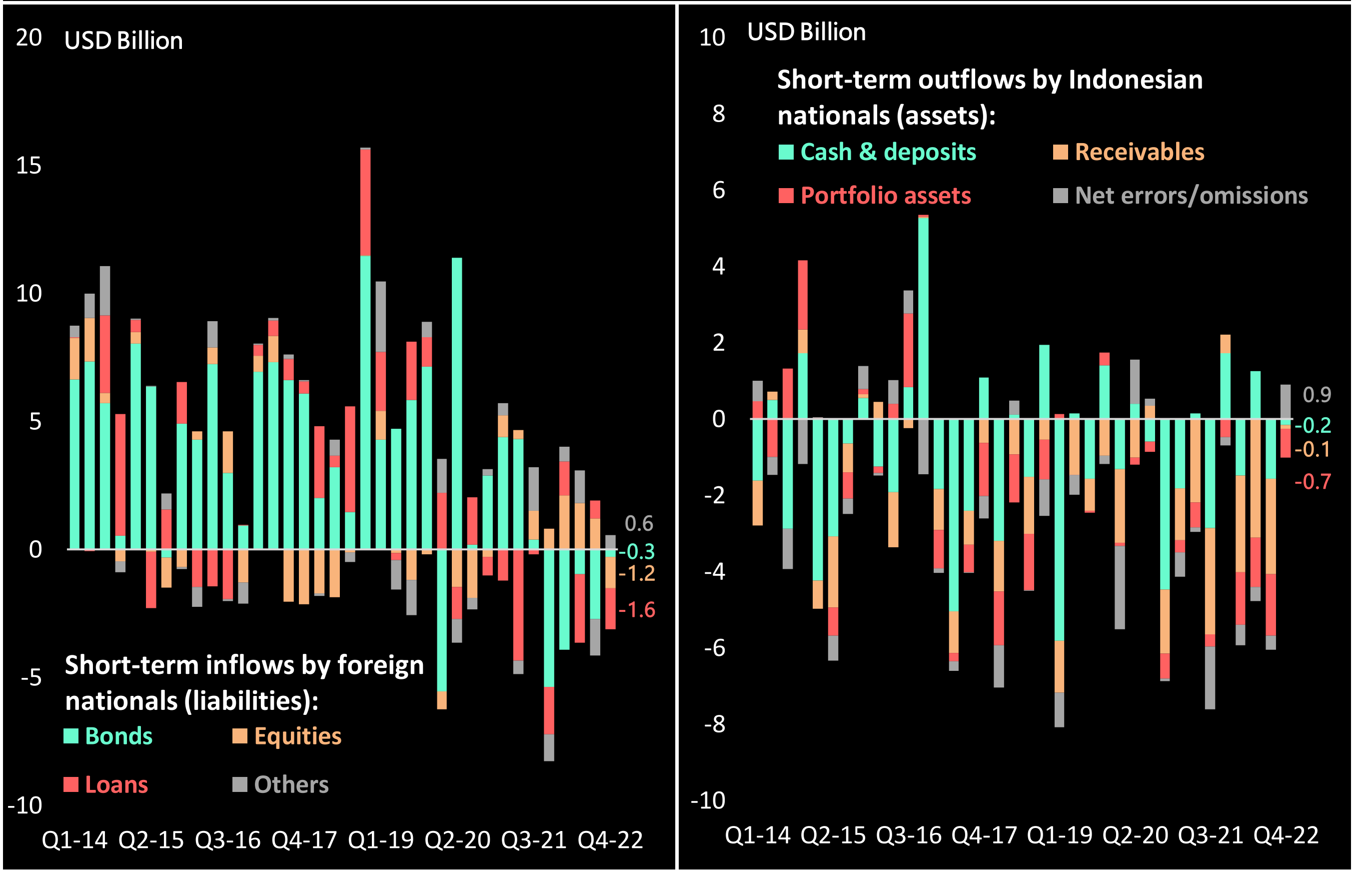
Source: Bank Indonesia

Panel 1. **Widening trade surplus concealed a similar widening of services deficit**



Source: Bank Indonesia, BPS

Panel 2. Tighter global liquidity had suppressed foreign inflows, while outflows peaked amid the commodity boom



Source: Bank Indonesia

Selected Macroeconomic Indicators

Table 1. Balance of payments (current USD Million)

	Q4-21	Q1-22	Q2-22	Q3-22	Q4-22	2020	2021	2022
CURRENT ACCOUNT	***1,511***	***550***	***3,858***	***4,544***	***4,265***	***-4,433***	***3,511***	***13,216***
(as % of GDP)	***7.77***	***6.97***	***6.41***	***5.73***	***5.90***	***-0.42***	***7.77***	***5.90***
A. Goods	12,433	11,301	16,797	17,623	16,961	28,301	43,806	62,682
- Non-Oil/Gas	18,128	17,210	24,445	25,160	22,958	29,954	57,804	89,773
- Oil/Gas	-5,045	-5,694	-7,187	-6,481	-5,405	-5,386	-12,965	-24,767
B. Services	-3,962	-4,379	-5,014	-5,413	-5,235	-9,755	-14,599	-20,041
C. Income	-8,910	-7,866	-9,449	-9,075	-9,392	-28,911	-31,961	-35,782
D. Current Transfers	1,950	1,494	1,523	1,409	1,931	5,932	6,264	6,357
CAPITAL TRANSACTIONS	**63.07**	**0.88**	**3.04**	**2.43**	**54.10**	**36.91**	**80.15**	**60.44**
FINANCIAL TRANSACTIONS	**-2,195**	**-1,833**	**-1,102**	**-5,492**	**-489**	**7,884**	**12,492**	**-8,916**
A. Direct Investment	3,891	4,397	3,604	3,514	3,605	14,142	17,286	15,120
B. Portfolio Investment	-5,023	-3,182	-450	-3,118	-2,272	3,369	5,086	-9,023
C. Derivative Instruments	26.65	136.76	-86.05	8.55	-10.90	17.73	332.71	48.36
D. Other Investment	-1,089	-3,185	-4,170	-5,896	-1,811	-9,645	-10,212	-15,062
NET ERRORS AND OMISSIONS	**-223.67**	**-534.28**	**-369.15**	**-358.10**	**900.83**	**-891.30**	**-2,622.30**	**-360.71**
BALANCE OF PAYMENT *(= change in BI international reserves)*	**-844**	**-1,817**	**2,389**	**-1,304**	**4,730**	**2,597**	**13,461**	**3,999**

Source: Bank Indonesia

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Indonesia – Economic Indicators Projection

	2018	2019	2020	2021	2022	2023E
Gross Domestic Product (% YoY)	5.2	5.0	-2.1	3.7	5.3	4.7
GDP per Capita (US$)	3927	4175	3912	4350	4784	5011
Consumer Price Index Inflation (% YoY)	3.1	2.7	1.7	1.9	5.5	4.3
BI 7 day Repo Rate (%)	6.00	5.00	3.75	3.50	5.50	5.75
USD/IDR Exchange Rate (end of year)**	14,390	13,866	14,050	14,262	15,568	15,647
Trade Balance (US$ billion)	-8.5	-3.2	21.7	35.3	54.5	43.2
Current Account Balance (% GDP)	-3.0	-2.7	-0.4	0.3	0.9*	-0.2

** Estimation of Rupiah's fundamental exchange rate

Economic, Banking & Industry Research Team

David E.Sumual
Chief Economist
david_sumual@bca.co.id
+6221 2358 8000 Ext:1051352

Agus Salim Hardjodinoto
Head of Industry and Regional Research
agus_lim@bca.co.id
+6221 2358 8000 Ext: 1005314

Barra Kukuh Mamia
Senior Economist
barra_mamia@bca.co.id
+6221 2358 8000 Ext: 1053819

Victor George Petrus Matindas
Senior Economist
victor_matindas@bca.co.id
+6221 2358 8000 Ext: 1058408

Gabriella Yolivia
Industry Analyst
gabriella_yolivia@bca.co.id
+6221 2358 8000 Ext: 1063933

Lazuardin Thariq Hamzah
Economist / Analyst
lazuardin_hamzah@bca.co.id
+6221 2358 8000 Ext: 1071724

Keely Julia Hasim
Economist / Analyst
keely_hasim@bca.co.id
+6221 2358 8000 Ext: 1071535

Elbert Timothy Lasiman
Economist / Analyst
Elbert_lasiman@bca.co.id
+6221 2358 8000 Ext: 1074310

Thierris Nora Kusuma
Economist / Analyst
thierris_kusuma@bca.co.id
+6221 2358 8000 Ext: 1071930

Arief Darmawan
Research Assistant
arief_darmawan@bca.co.id
+6221 2358 8000 Ext: 20364

Firman Yosep Tember
Research Assistant
firman_tember@bca.co.id
+6221 2358 8000 Ext: 20378

PT Bank Central Asia Tbk

Economic, Banking & Industry Research of BCA Group

20th Grand Indonesia, Menara BCA

Jl. M.H Thamrin No. 1, Jakarta 10310, Indonesia

Ph : (62-21) 2358-8000 Fax : (62-21) 2358-8343