

Indonesian Economic Outlook 2025

Glass half-empty, or glass half-full?

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Executive Summary

- The root of Indonesia's current economic paradoxes lies in a structural change in its manufacturing industry. Capital-intensive, commodity-related industries—driven by “downstreaming” program—have thrived, while labor-intensive, final goods industries have come under pressure.
- Downstreaming has successfully bolstered exports but also increases Indonesia's vulnerability to fluctuations in commodity prices and Chinese demand. This puts it under considerable risk in 2025 amid a stronger USD, deflation in China, and re-escalation of the trade war.
- Layoffs in the formal manufacturing sector have cut into the purchasing power of the lower/middle-class and the earning of SMEs. Other segments of the economy—large corporations, the plantation sector, white-collar and wealthier households—are relatively insulated, but tend to adopt a more cautious posture.
- Government spending has greatly influenced the business cycle recently, and BCA Big Data have pointed towards more moderate growth since after the General Elections in Feb-24. Most indications point towards subdued nominal growth and money velocity in 2025, unless the new government can quickly realize their spending goals.
- Expansive fiscal policy, CAPEX needs from capital-intensive industries, and tight global liquidity have caused a scramble for liquidity at the expense of the rest of the private sector (including households). This has been exacerbated by high real rates as BI mounts a strong defense of the Rupiah. Ultimately, a more pragmatic monetary approach might become necessary to sustain robust private spending amid continued global pressure.

Glass half-empty, or glass half-full?

- At first glance, 2024 seemed to be an ordinary (even quite good) year for the Indonesian economy. The GDP grew close to its long-term average of 5%, supported by double-digit loan growth and a healthy trade surplus. Inflation, meanwhile, slowed to just 1.55%—the lowest outside of the COVID-19 pandemic.
- In theory, this should have been a great time to be an Indonesian consumer, particularly given the extra social assistance doled out during an Election year. Take a look at the news and social media, however, and one will get a very different view.
- News of mass layoffs were frequently on the headlines, while low inflation is seen not as a boon, but rather a sign of weak demand. Indeed, a quite unfortunate portmanteau (*'mantab'*, from *'makan tabungan'* i.e. using up one's savings) has entered the lingo, as a shorthand for the plight of middle-class households.
- There is thus a widespread feeling of malaise, which nonetheless cannot be captured by the usual topline indicators. Answering this puzzle—whether the Indonesian economy is a “glass half-empty” or “half-full”—is key to our outlook of the economy in 2025.
- We will start ([Ch. 1](#)), however, not on consumption but at the root of the issue—a reorientation of the economy's productive forces in the years after the pandemic. The result of this is a fall in formal employment and increased pressure on household liquidity, the consequences of which will be explored in [Ch. 2](#).
- The new government under President Prabowo has come up with an ambitious spending agenda to bolster growth ([Ch. 3](#)). But the massive financing needs that it entails, amid high global rates and the need to maintain a defensive monetary posture ([Ch.4](#)), might add further pressure on the liquidity situation.
- Liquidity, then, is the key bottleneck to our long-term growth, and we lay out several areas for improvement in [Ch. 5](#). In the short-term, however, we opt for a more cautious *projections*, especially against the backdrop of heightened global uncertainty in 2025.

I

THE SUPPLY SIDE

II

THE DEMAND SIDE

III

FISCAL
POLICY

IV

MONETARY
POLICY



GLASS HALF-EMPTY:

**Decline in labor-intensive,
final goods industries**



GLASS HALF-EMPTY:

**Decline in households'
purchasing power**



GLASS HALF-EMPTY:

**Gov't financing needs may
exacerbate liquidity issues**



GLASS HALF-FULL:

**Growth in capital-intensive,
commodity-based industries**

GLASS HALF-FULL:

**Widening income disparity,
but room for consumption
growth remains**

GLASS HALF-FULL:

**New government programs
to boost economic activities**

V

FINAL NOTE

THE ULTIMATE QUESTION:

**Can we solve the liquidity
constraint to growth?**

Swimming downstream and upstream

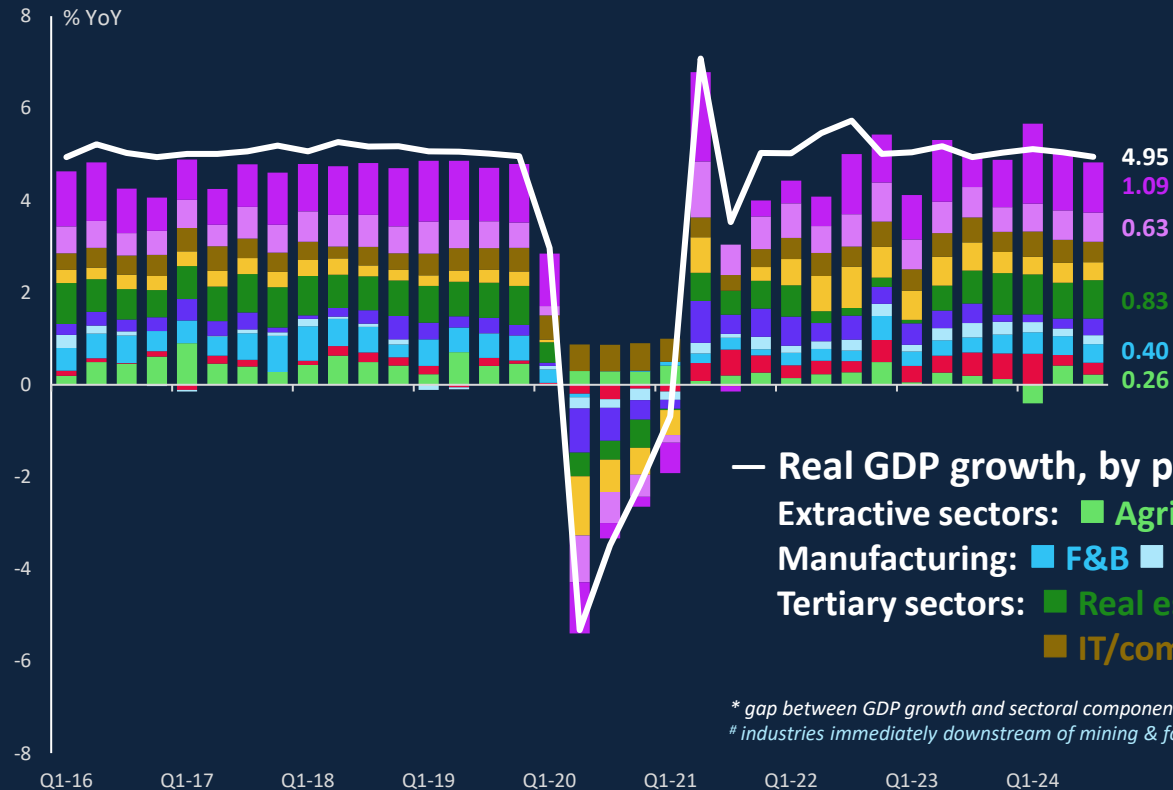
- If infrastructure had been the main focus during the first term of former President Jokowi, “downstreaming”—i.e. the push to build mineral, specifically nickel, processing facilities at home—was the key to his second. And it worked like a charm.
- Between 2021 and 2023, FDI into metal processing doubled, while the value of nickel-derived exports jumped 2.5 times. Accordingly, mining and metals became bigger contributors to GDP growth [7].
- But this success did not catapult Indonesia to a higher growth trajectory, as it was offset by a decline in other manufacturing industries [8]. Many of these industries are labor-intensive, and they also tend towards the end of the supply chains (*final goods* such as clothing, footwear, and electronics).
- Some of the declines seem connected to the influx of imported goods from China, whose real estate crisis has forced it to double down on its export-oriented strategy. Indeed, among final goods industries, only foods and pharmaceuticals are spared [9]—likely due to significant non-tariff barriers (*halal*, safety, sanitary).
- The upshot, then, is that Indonesia’s role in the global value chains may have shifted *upstream* rather than *downstream* as intended. Thanks to nickel derivatives, Indonesia now exports more to China (“the world’s factory”), but exports to the US (the world’s biggest consumer market) have long been stagnant [10].
- Indonesia’s positioning—mostly upstream of China—thus puts it in a different boat to Vietnam, India, or Mexico, which emerge as alternative hubs for manufacturing, assembly, and re-export amid the ongoing “divorce” between China and America.
- As an industrial strategy, this seems to be a low-reward, high-risk bet. Although downstreaming certainly allows us to capture more value compared to exporting raw materials, final goods industries tend to capture an even larger share of value [11].
- Downstreaming also shares the same drawback as exporting the raw materials itself—namely, sensitivity to the commodity cycle. This has been a problem since nickel prices fell back to earth in 2023 [18], amid an ongoing oversupply in China.

Putting on an ill-fitting suit

- The shift from labor-intensive sectors to largely capital-intensive basic industries is also rather ill-suited to Indonesia, which has a huge labor force but limited capital. Financing these investments, as such, would put a strain on domestic liquidity, unless there is significant external support.
- There was ample support in 2021-23, both from FDI and from the surplus generated by high commodity prices. This surplus allowed companies to massively ramp up their CAPEX [12], until it eventually slowed in the latter half of 2023 as commodity revenue dried up [13].
- Indeed, so closely tied up is our “animal spirit” with commodities, that corporate liquidity *and* borrowing both follow a cycle mirroring the commodity boom-and-bust [14]. Unsurprisingly, then, the appetite for financing—both debt and equity—had cooled down markedly in 2024 [19].
- But despite this more cautious turn, there are a couple of green shoots for 2025. One is the strong borrowing trend among China-linked corporates [20], which could signal greater FDI. Amid the twin pressures of US tariffs and deflation in China itself, Indonesia could emerge as a new place to invest for Chinese companies.
- The other is a nascent recovery in commodity revenues, as Indonesia’s commodity terms of trade shows a modest recovery [15]. Much of this improvement has come from higher CPO prices [16], which has bolstered the trade surplus in recent months.
- CPO’s revival—coupled with nickel’s waning fortune—could have significant implications on the regional income distribution. While Eastern Indonesia (Sulawesi, Maluku, Papua) has been the shining star in the past few years, Sumatra—a relative laggard recently—stands to enjoy a renewed windfall.
- Still, there is a caveat to this good news, since the increase in CPO prices is part of a general trend of rising prices for tropical crops relative to temperate ones [17]. If this is driven by climate-related supply disruptions, the boost from better terms of trade might be outweighed by a decline in agricultural productivity.

Same façade, different interior

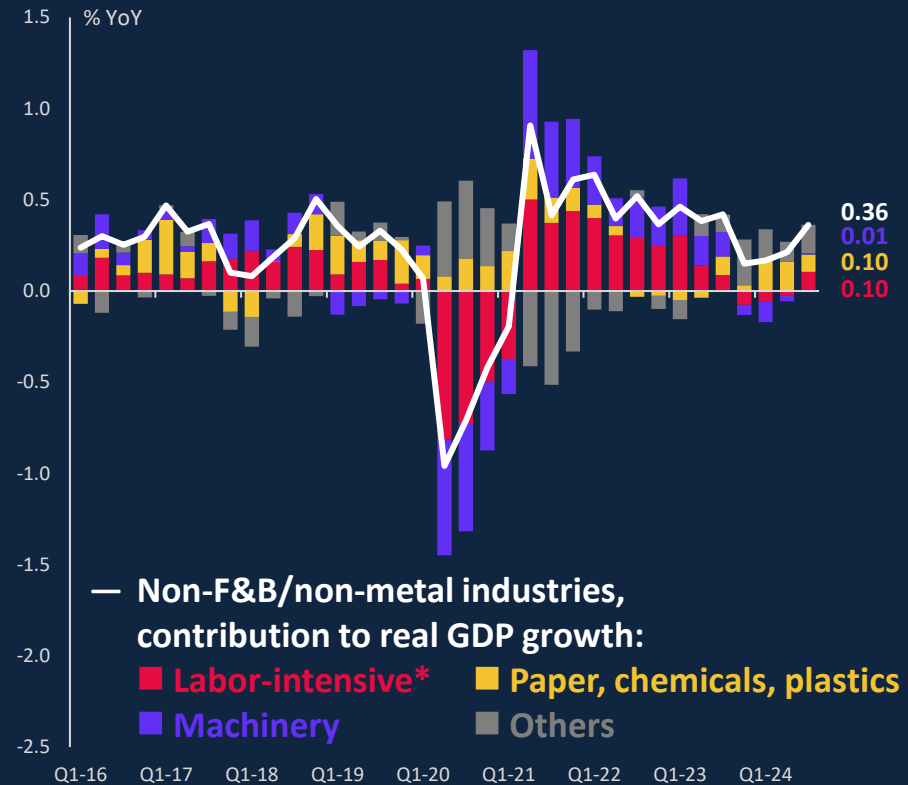
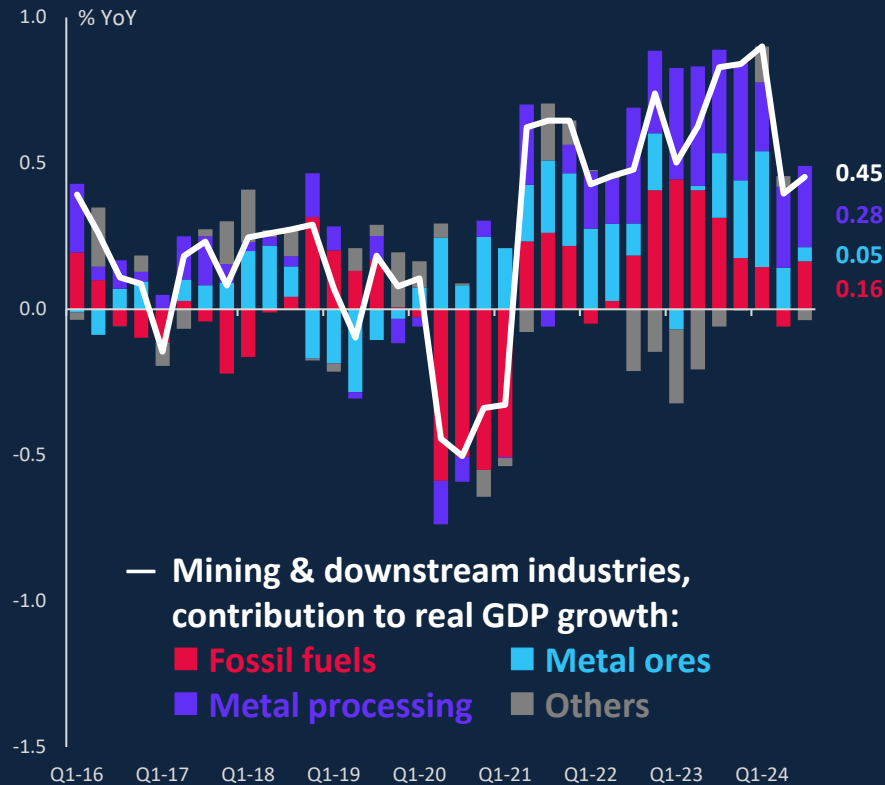
While GDP growth remains steady at around 5%, there has been a notable shift in its sectoral composition relative to pre-pandemic times



- **Mining & downstream industries** used to add about 0.2% to annual growth prior to the pandemic; now it contributes up to 0.9% at its peak (Q1-24)
- Contributions from **logistics** and **services** (esp. healthcare and tourism) have likewise increased

Metalhead with feet of clay

The government's "downstreaming" program has been a massive success, but it is offset by a decline in several other industries

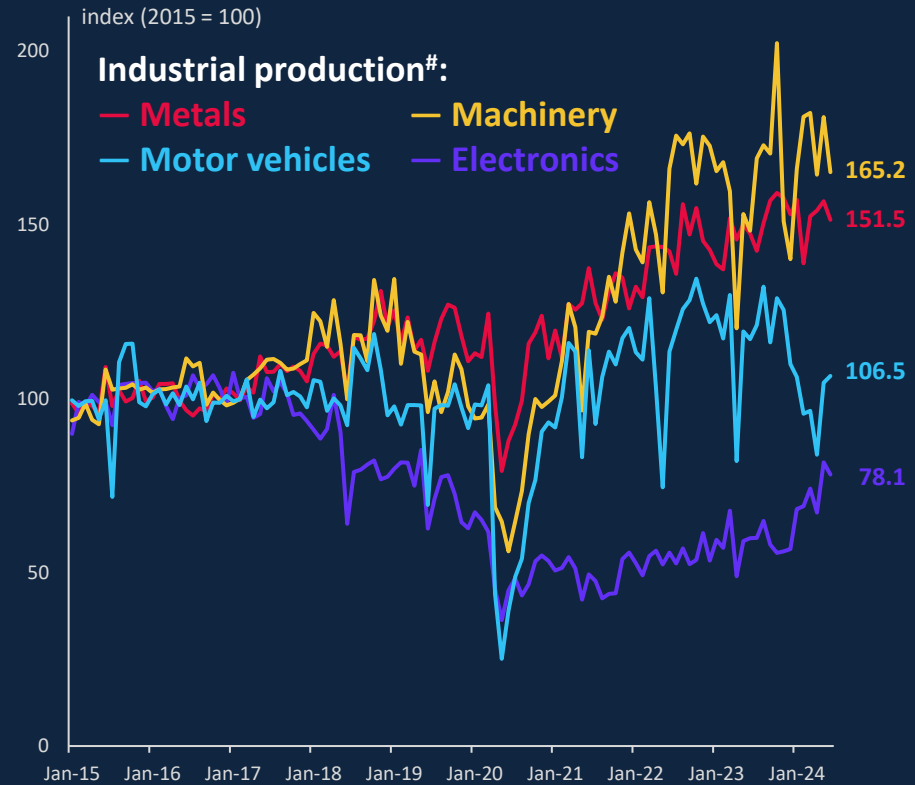
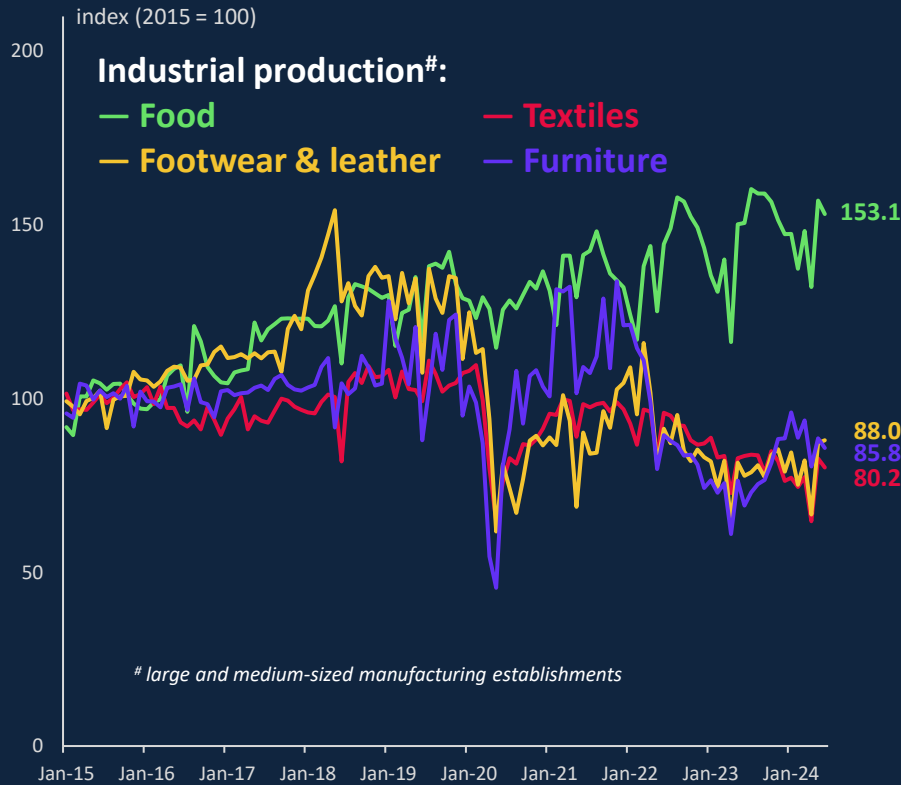


Source: BPS, calculations by BCA Economic Research

* textiles, footwear, leather products, and furniture industries

Back to basic

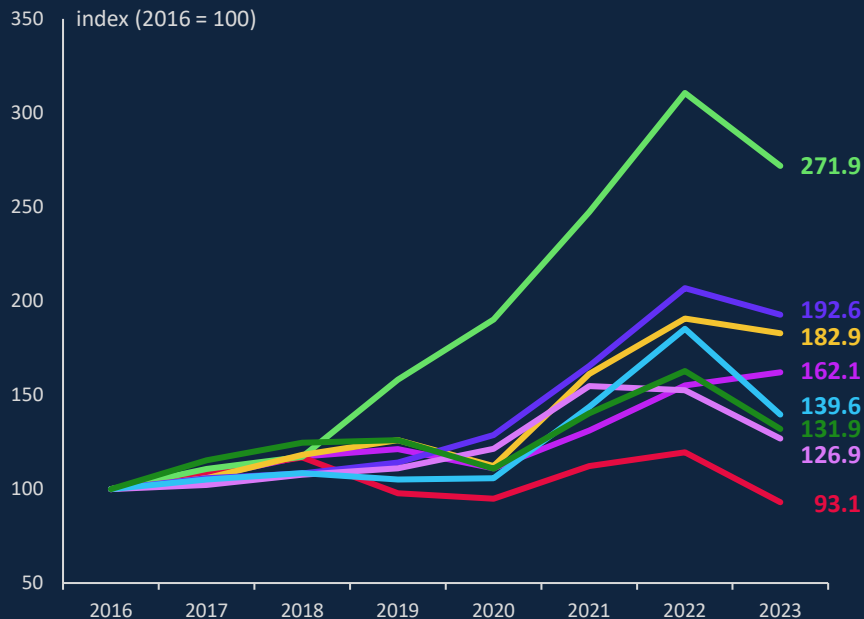
Basic, upstream industries have been thriving, but—other than food and pharma*—industries making final goods are mostly struggling



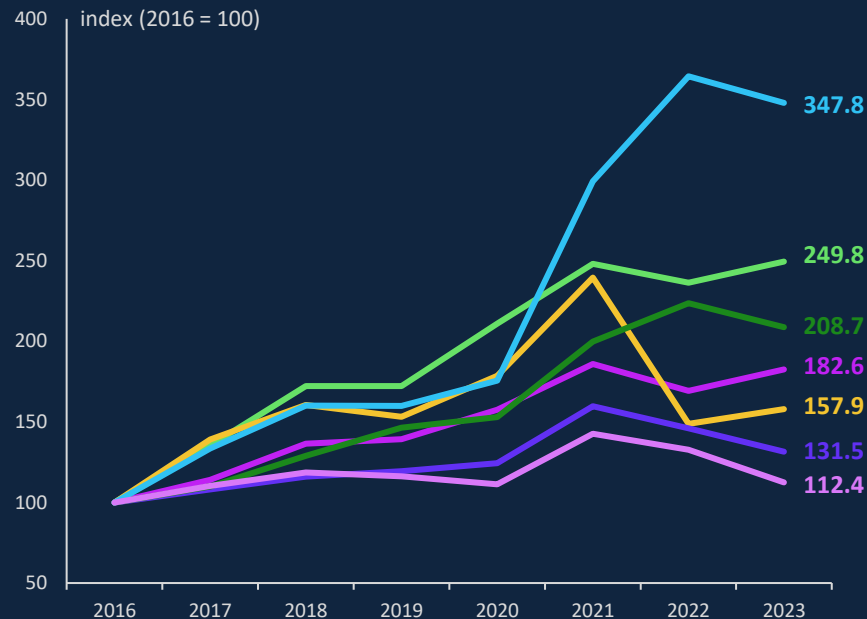
The Orient Express

Amid US-China fallout, Vietnam and Mexico are playing both sides—whereas Indonesian exports are becoming more orientated towards China

Exports to United States



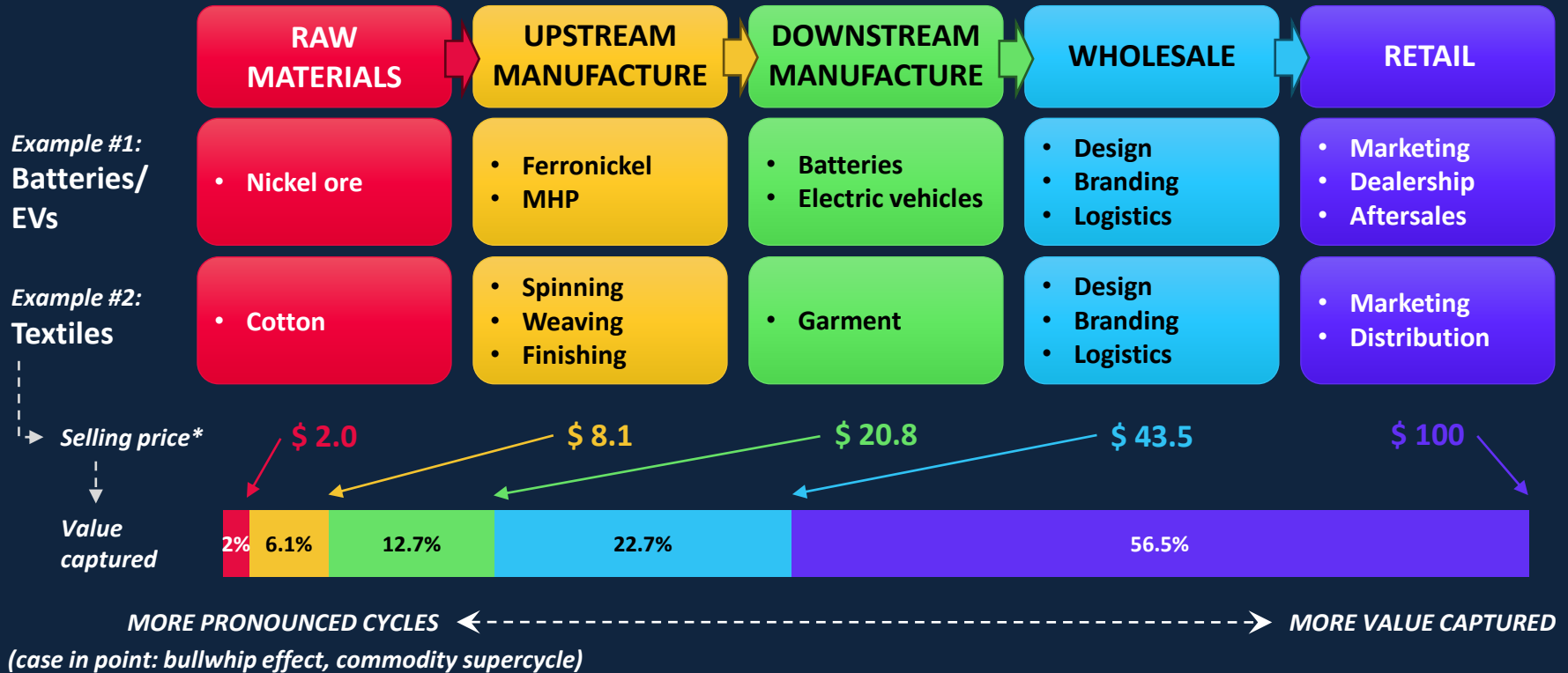
Exports to China



— Indonesia — Malaysia — Thailand — Philippines — Vietnam — India — Mexico — China

Turn off, relax, and float downstream?

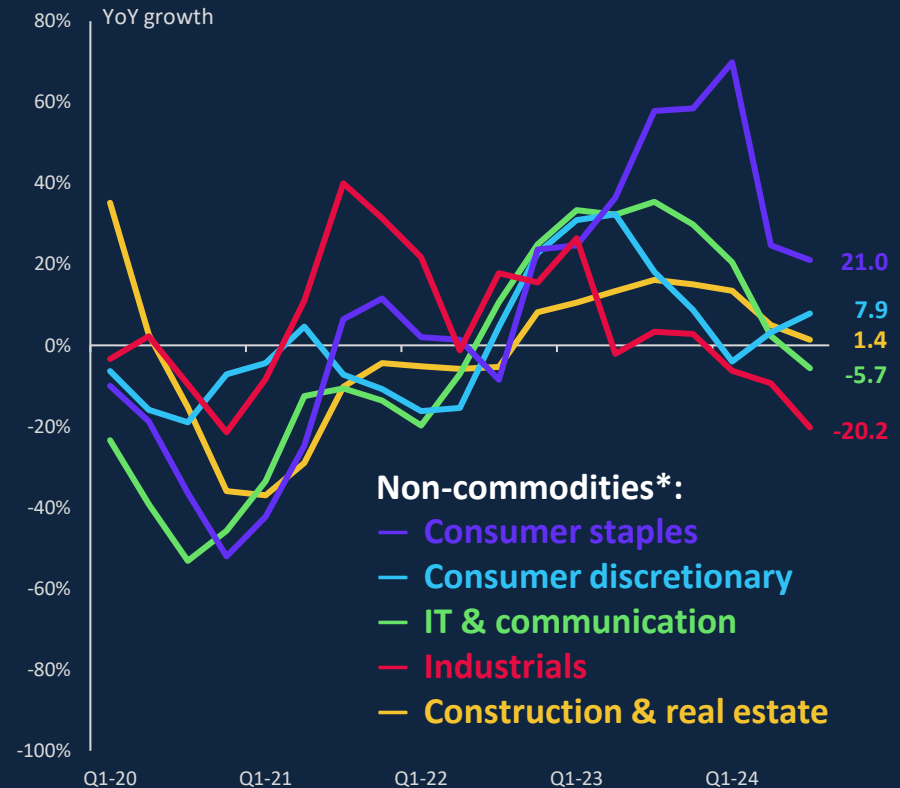
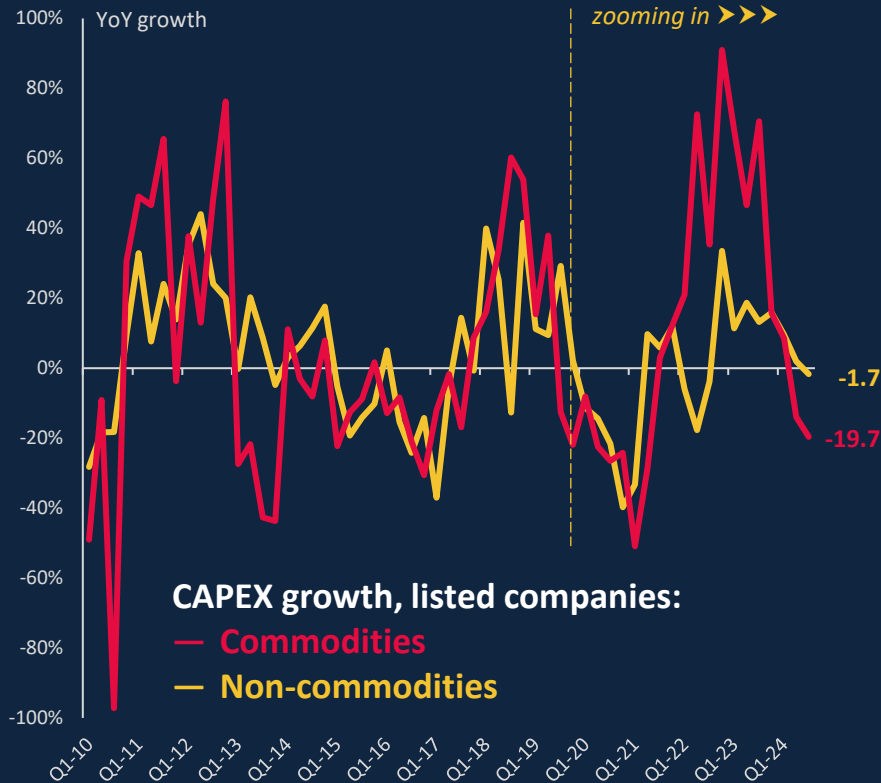
Indonesia is moving down the metal supply chain, but losing its edge in multiple final goods industries is a substantial blow nonetheless



* selling prices along the textile value chain are based on ILO (2017) and Reddy (2013); final retail price is rounded to \$ 100, and prices upstream are expressed proportionally to that final price

Feast and famine

Businesses spent aggressively coming out of the pandemic, but the CAPEX cycle has since begun to wane

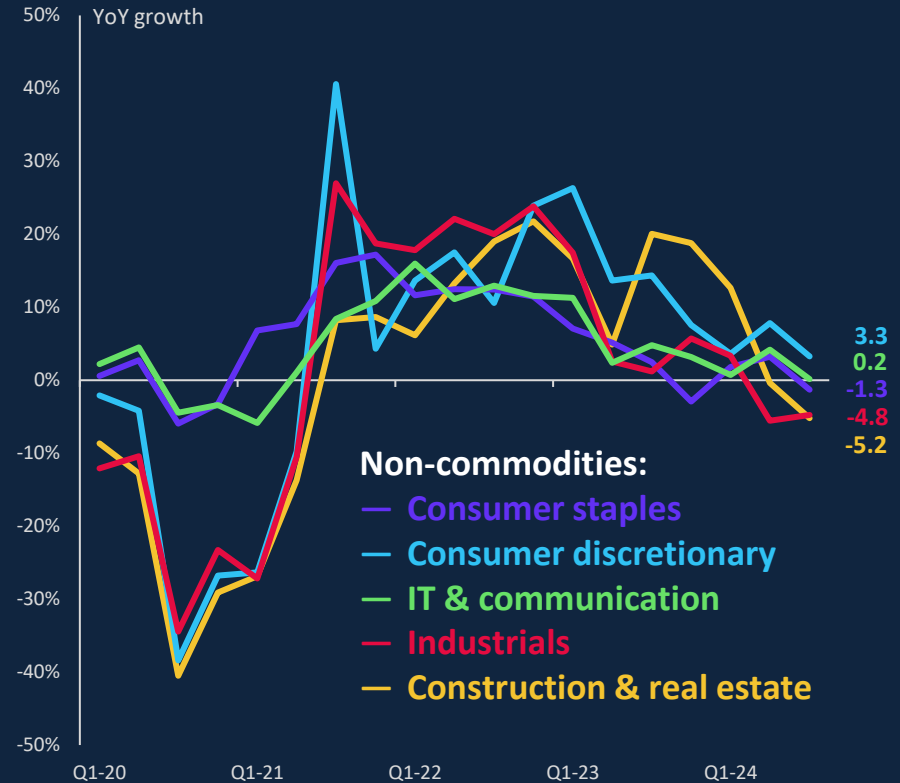
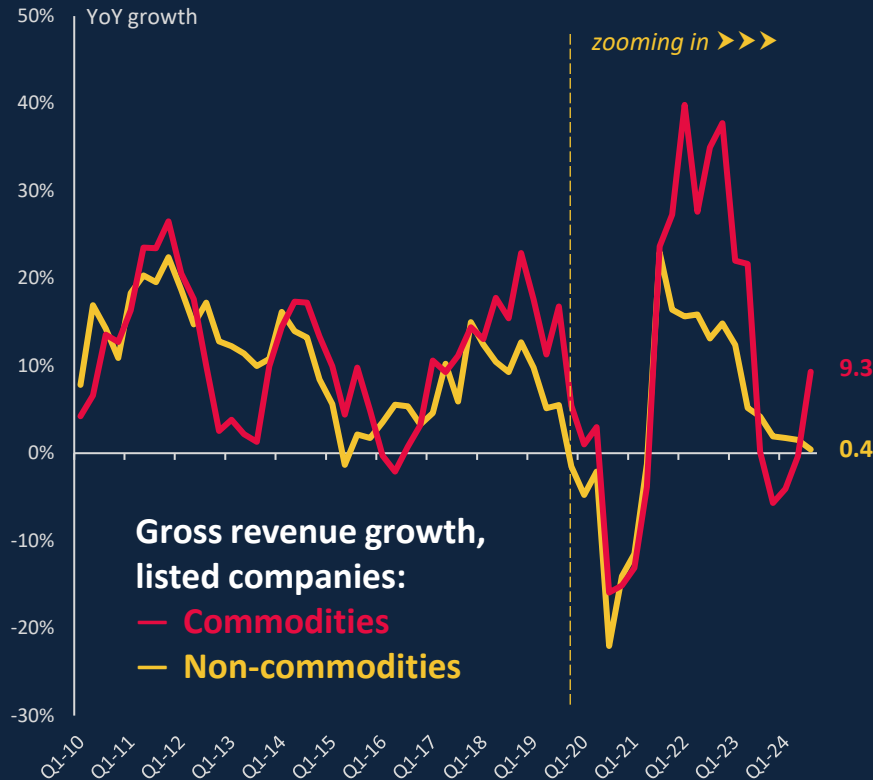


Source: Bloomberg, calculations by BCA Economic Research

* 3-mth centered moving average (3M-CMA)

Cavalry to the rescue

Revenue in most sectors is still slowing down, but recovery among commodity exporters could support domestic liquidity

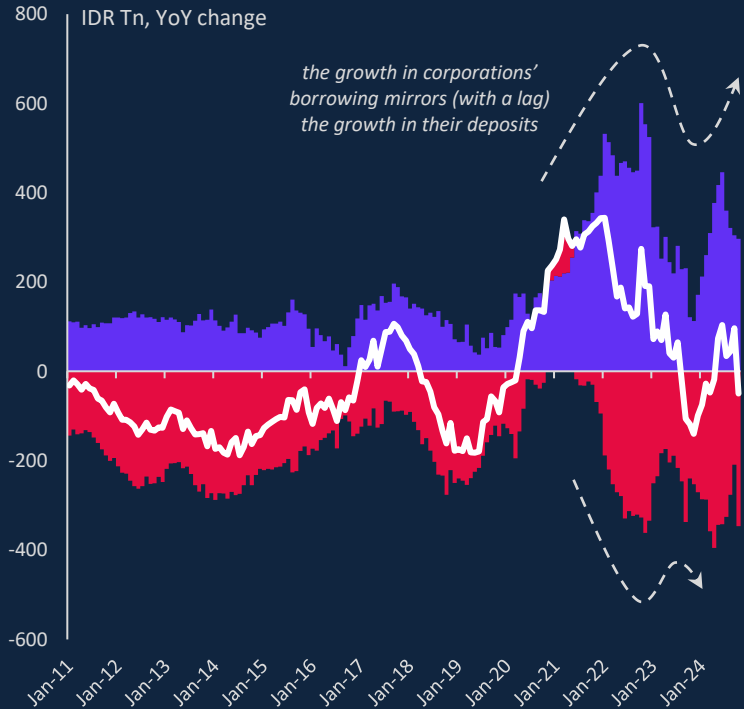


Source: Bloomberg, calculations by BCA Economic Research

Refreshed and replenished?

Private corporations' net liquidity declined as commodity prices fell in 2023, although there has been some recovery in 2024

Net bank balance: Private corporates*



— **Net bank balance (NBB), YoY change as reflected in the balance sheets of BI & commercial banks:**

■ **Change in deposits**

■ **Change in loans and bonds**

How to read this visualization:

In the past year (Oct-23 to Oct-24), deposits by private corporations grew by IDR 296.8 Tn...

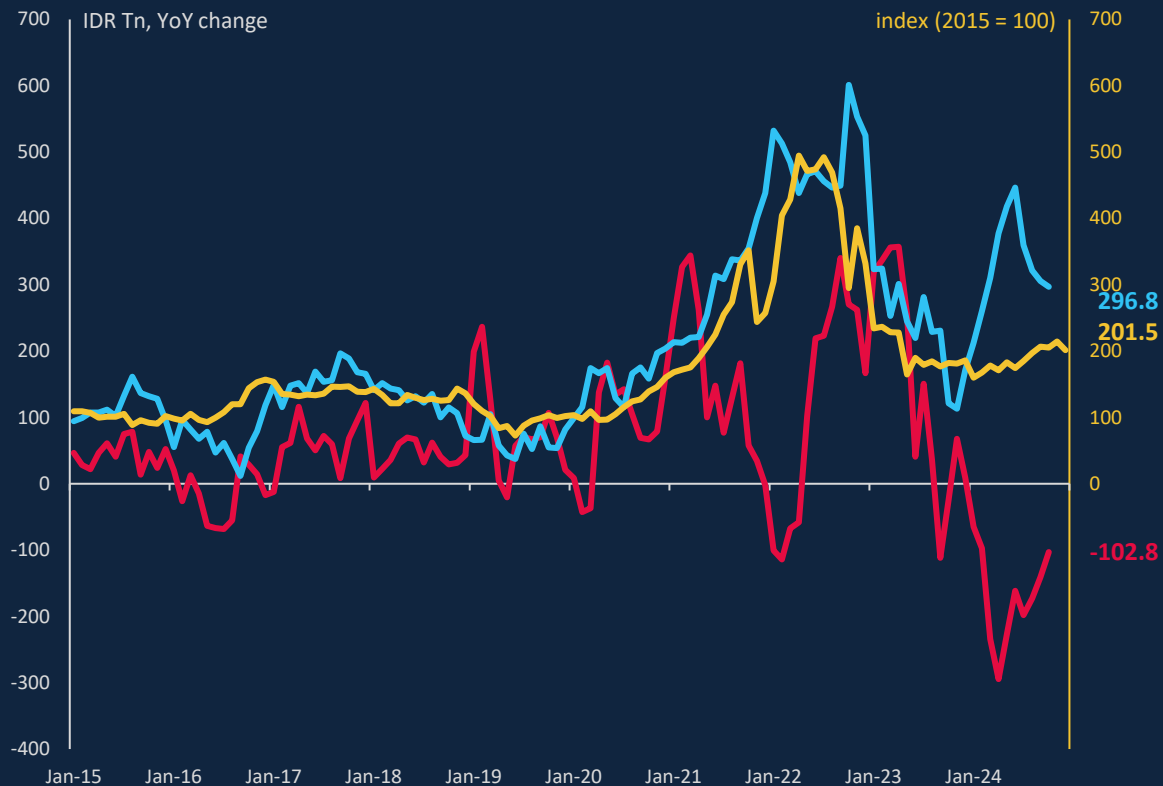
... while their borrowing (both loans and bonds) grew by IDR 346.6 Tn

Net bank balance[#] (or net liquidity) is simply the change in deposits minus the change in loans and bonds, which therefore decreased by **IDR 49.8 Tn** during that period

[#] the term "net bank balance" is chosen because it is essentially a proxy for net financial balance in Flow-of-Funds statistics, albeit a partial one based only on the balance sheets of BI & commercial banks

Exogenous growth theory

For private corporations, liquidity is largely a function of commodity prices and government dissaving

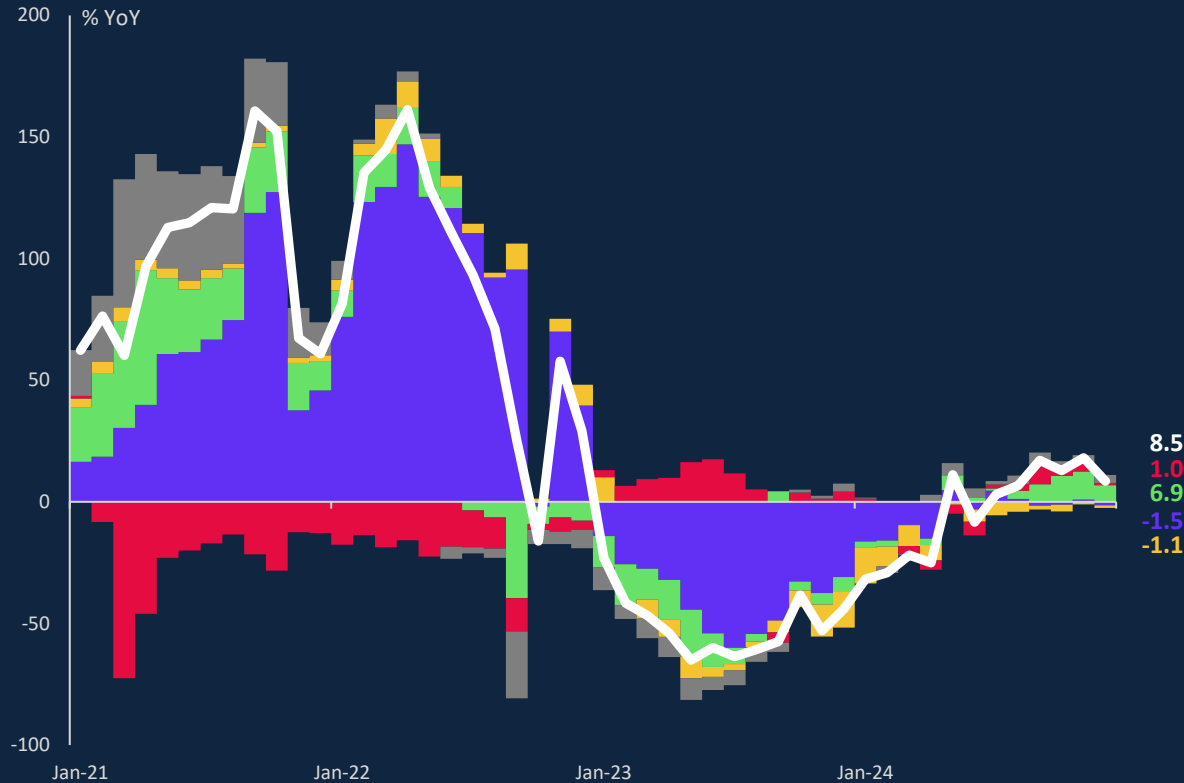


- The peak in **government spending (dissaving)** in early 2024 led to 18% YoY growth in **deposits by private corporations**
- However, the more modest improvement in **terms of trade** suggests that corporate deposit growth will eventually normalize to the high single-digits

- ◀ **Change in private corp. deposits**
- ◀ **Change in government deposits**
- **BCA Inacott index (Indonesian commodity terms of trade)**

Greasing the wheels

High palm oil prices and low crude oil prices accounted for most of the terms of trade improvement in 2024



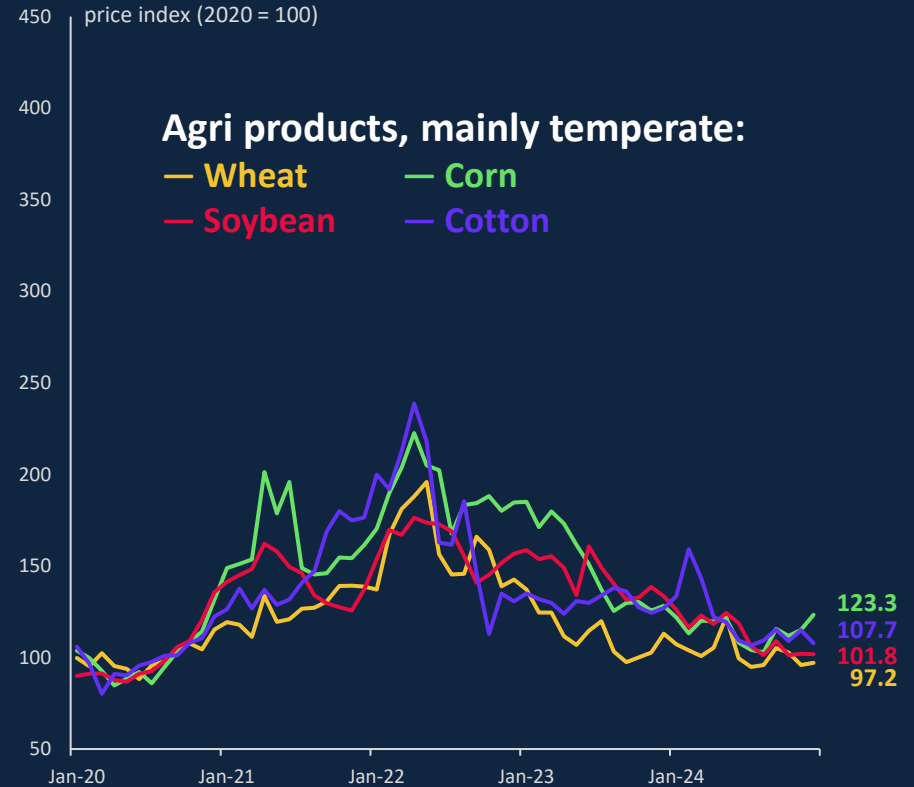
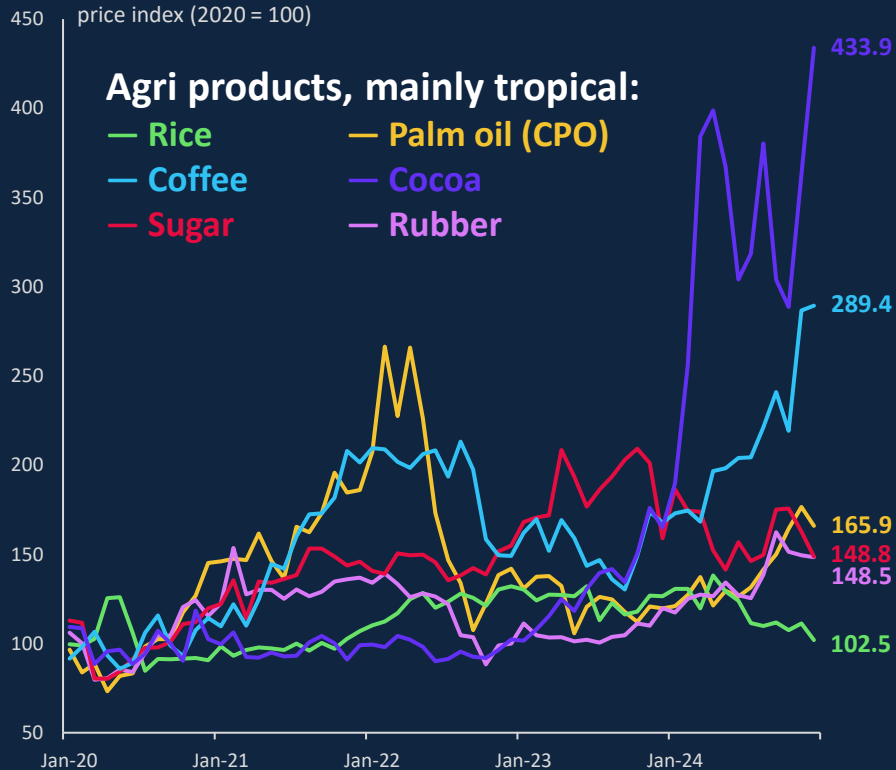
- The 2022 commodity boom was exceptional as it involved all three of our main export commodities: **coal**, **CPO**, and **nickel**
- Being a net importer, Indonesia benefits from subdued **oil prices** for most of 2024

BCA Inacott index, YoY change by component:

- Coal
- Palm oil (CPO)
- Oil
- Nickel
- Other commodities

Heat wave

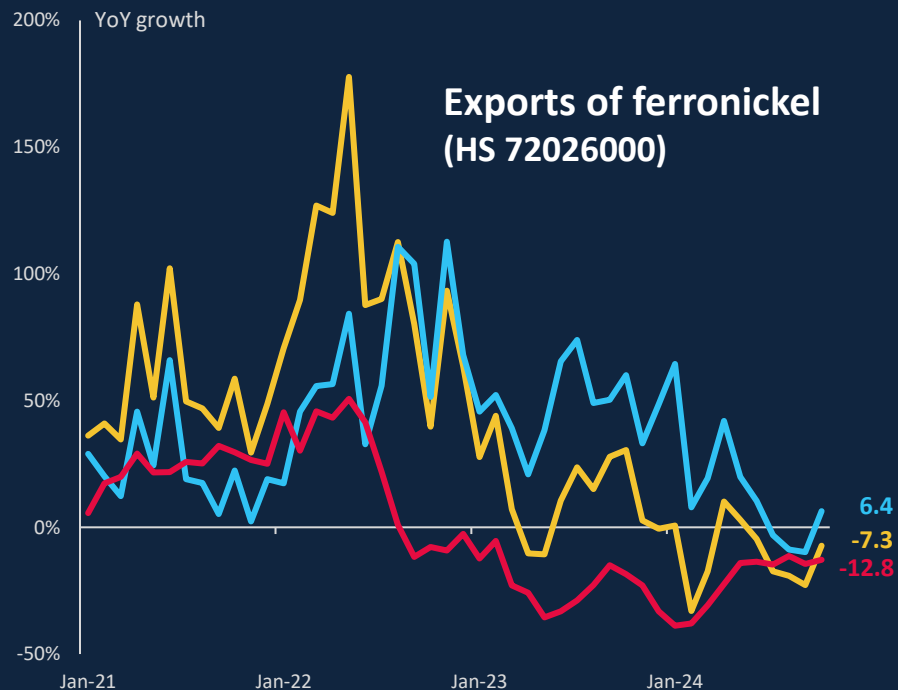
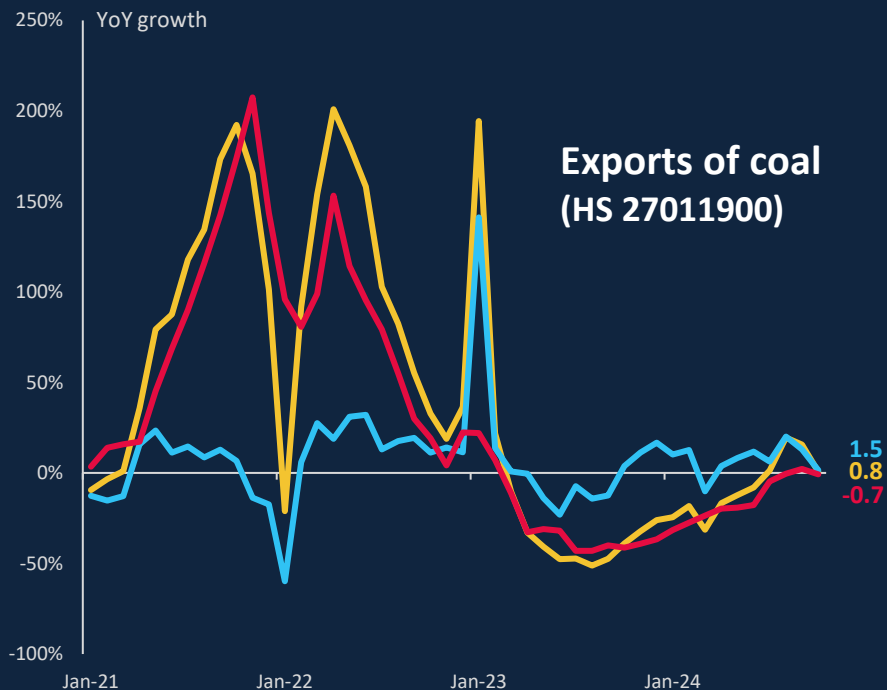
Prices of tropical products are (mostly) rising, while temperate crops have stabilized after the initial shock of the Russia-Ukraine War



Source: Bloomberg, BCA Economic Research

Hold the line

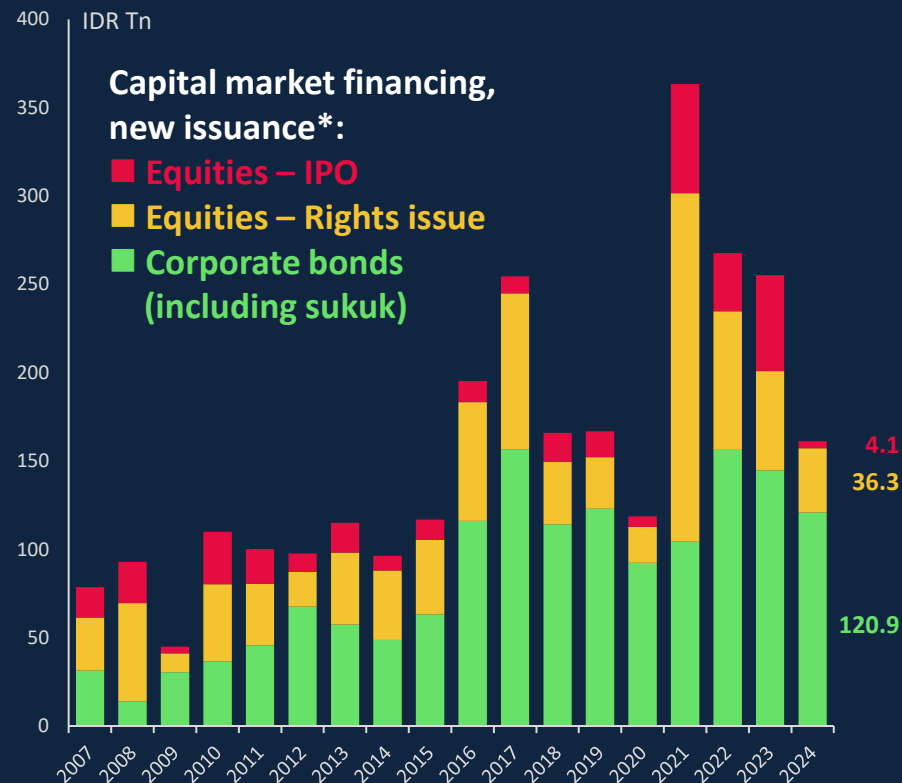
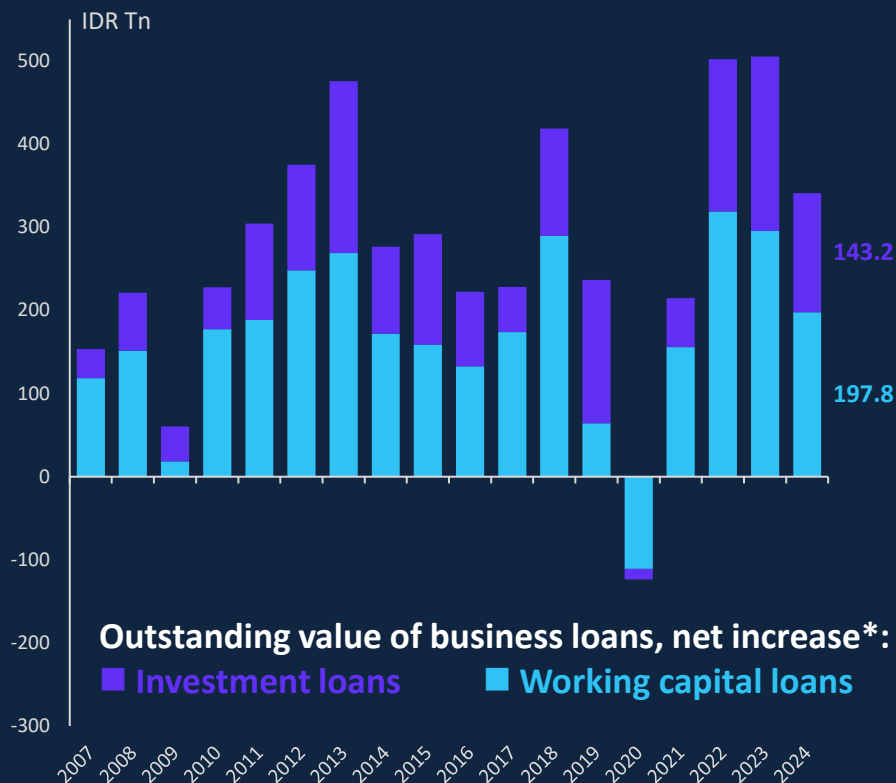
Indonesian miners have been forced to curb output in a bid to stabilize prices amid weak global demand



Commodity exports: — Value (USD) — Volume (kg) — Unit price (USD/kg)

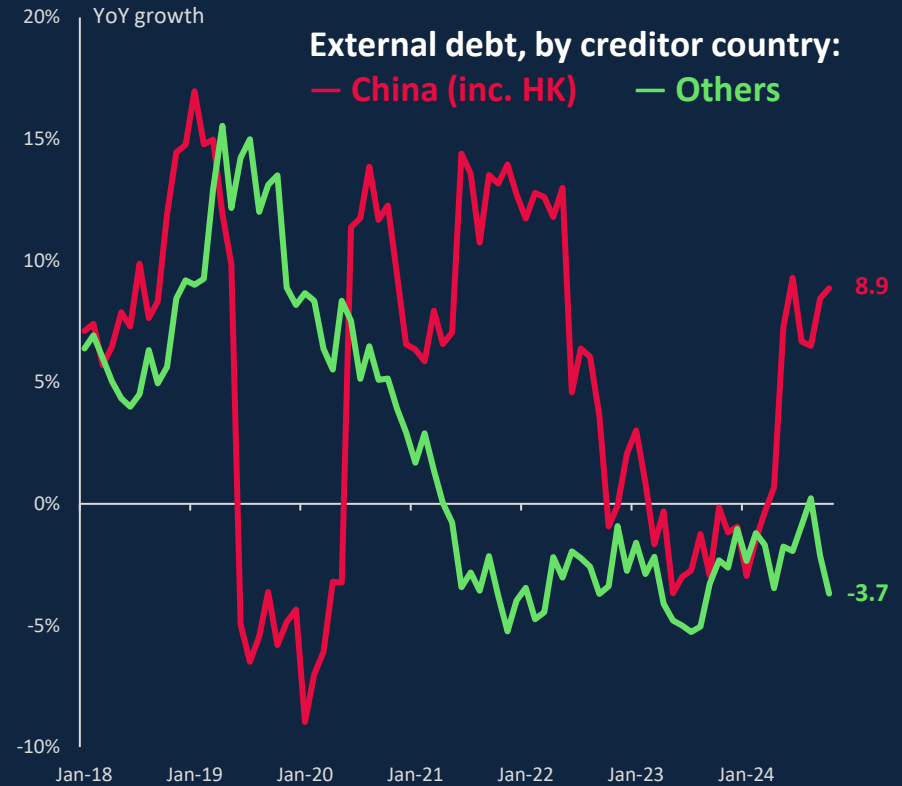
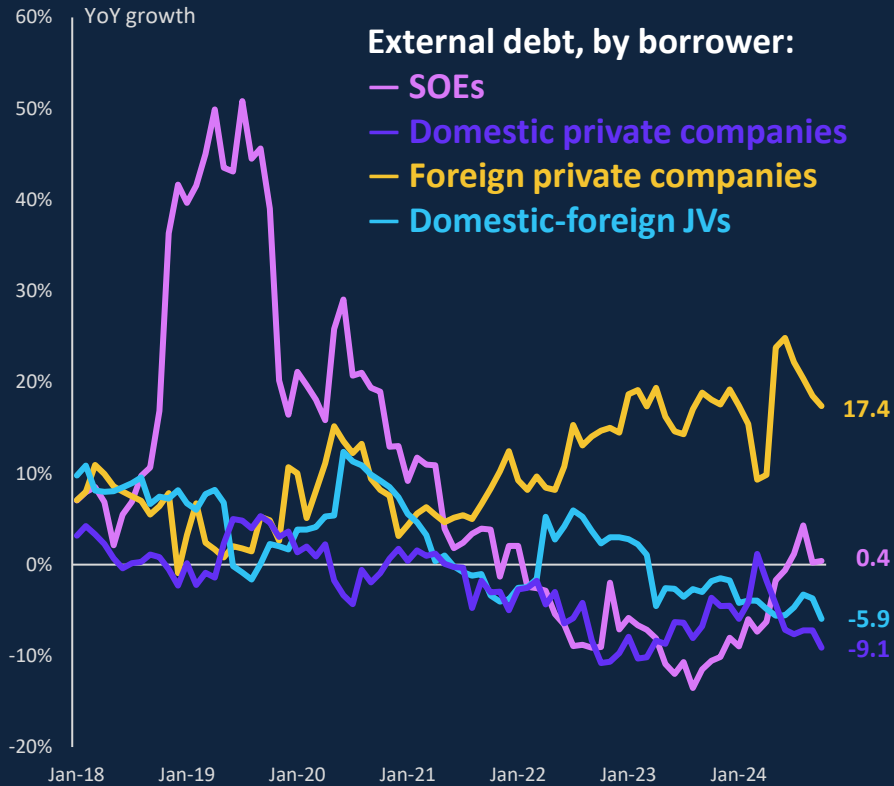
Cooling down

Debt financing peaked in 2022-23, while new equity issuance has fallen far from its heyday in 2021



Low ebb, red tide

Local companies are becoming reluctant to borrow from abroad, but China-linked companies are bucking the trend



II

THE DEMAND SIDE

Informality trap all over again

- The decline in Indonesia’s labor-intensive industries appears to be a slow-moving process—a few bankruptcies here, a thousand laid off there—but the cumulative effect is immense. Since 2020, the formal manufacturing sector has shed 1.34 Mn jobs, with 471k of those happening just between H1-23 and H1-24 [24].
- Many of these laid-off workers shift to informal activities in retail trade, food service, and logistics—all of which have profited from digitalization in recent years. Others—mostly those who lost their jobs during the pandemic—return to farming.
- Regardless, these new jobs often offer low and irregular income, which is why the rate of *underemployment* has risen sharply [23]. Indeed, given the prevalence of low-paying informal work in Indonesia, we argue that underemployment—not unemployment—is the preferred gauge of labor market conditions.
- The declining income has crimped retail sales, even as consumer sentiment remains above-par [25]. A closer look, however, shows that consumption has not declined uniformly across the board.
- Big-ticket items like housing, vehicles, and appliances have slowed considerably [26], with an associated rise in credit delinquency to boot [28]. On the other hand, “affordable luxuries” like eating out and domestic travels [27] have been more resistant to decline.
- The top of the income distribution, including white-collar workers outside of manufacturing, also seems to be holding up better—as indicated by sales of larger houses [29] and high-end cars [30].
- Indeed, while there is a clear case of *mantab* among households as a whole, its effect disappears once we include the ownership of government bonds (SBN) [31]. Wealthier households, as such, may just be shifting their savings from plain-old time deposits at banks to SBN amid an uncertain, high-yield environment.
- This distributional problem hits SMEs especially hard, given their mostly low/middle-income customer base. Indeed, their liquidity position has continued to worsen [32] despite much support from the authorities since the pandemic. Informal work, then, seems to be no substitute to the losses in formal employment.

II

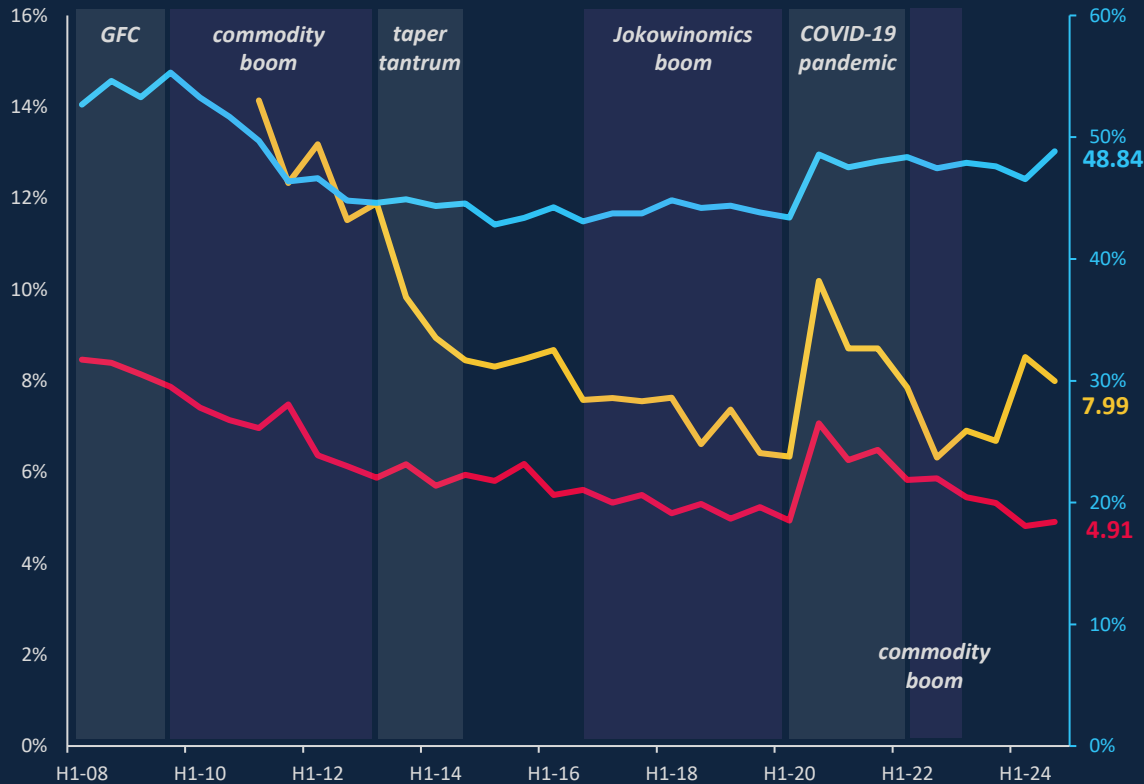
THE DEMAND SIDE

Flying on one engine

- As household consumption—which still makes up 54% of the GDP—grew shakier while investment and exports ebbed along with commodity prices, government spending seemed to be the only source of demand left intact [33].
- If anything, the fiscal engine was playing an outsized role in 2024. The General Elections saw a flurry of activities, from electoral logistics to the disbursement of social assistance. The latter provided a significant buffer for households, leading to a temporary peak in consumption in Q1-24.
- Construction by the public sector, particularly legacy projects like the new capital city (IKN) and other “national strategic projects” (PSN), also ramped up in 2024. Nonetheless, these did not make up for the decline in private construction since the pandemic [34].
- But this fiscal push did not last, and activities—as seen from BCA’s big data—hit a lull in mid-2024 [35]. A late-year push, coinciding with Regional Elections, provided only a limited boost, in line with a modest rise in consumer and capital goods imports [36].
- Food inflation, a persistent issue since 2022 [37], is another area where the government has made substantial headway, thanks to imports [38] and higher production (since April). The ensuing disinflation mitigated some of the losses in purchasing power—quite contrary to the dim view that weak demand is *solely* to blame.
- We agree, however, that demand problems has contributed to a slower money velocity [39]. As a result, the relatively robust loan disbursement—especially in early 2024—did not result in higher income growth.
- This low-inflation, low-nominal growth trend may persist in 2025, with loan growth seemingly slowing and China set to “export” its deflation further [40]. This will likely offset the inflationary effect from higher VAT rate (from 11% to 12%), which we expect to add about 0.4% to the annual inflation rate.

Look under the hood

Despite record-low unemployment, higher levels of underemployment and informality show deeper underlying issues in the labor market



- In general, **underemployment rate** is more volatile—and more highly responsive to macro conditions—than **unemployment rate**
- **Informality** increased during the pandemic, and has not declined appreciably (scarring effect)

- ◀ **Unemployment rate** (as % of workforce)
- ◀ **Underemployment rate*** (as % of working population)
- ▶ **Non-farm informal workers** (as % of non-farm workers)

* underemployment refers to workers who work less than 35 hrs per week and wish to increase their working hours

Downwardly mobile

Almost 1% of the workforce have lost formal jobs in manufacturing, forcing them to shift into small/family businesses in (e-)commerce and food service



* all numbers are pct of population aged 15+

H2-19 to H1-23

Formal workers
Own business
Freelance workers
Family business
Formal entrepreneurs

	Agriculture	Mining	Manufacturing	Utilities	Construction	Trade & Repair	Logistics	Hotel & Resto.	IT & Comm.	Finance	Real Estate	Biz. Services	Government	Education	Health & Social	Other Services	Unemployed	Not in LF*
Formal workers	0.05%	-0.69%	-0.08%	-0.07%	-0.22%	0.01%	-0.03%	-0.05%	-0.19%	-0.01%	-0.07%	-0.23%	-0.08%	-0.07%	-0.19%			
Own business	0.05%	0.08%	0.03%	0.08%	-0.27%	-0.15%	0.20%	0.03%	0.02%	0.02%	0.02%	0.00%	0.02%	0.06%	0.00%			
Freelance workers	1.61%	-0.02%	-0.11%	0.00%	-0.19%	0.12%	0.00%	0.00%	0.01%	0.00%	0.00%	0.01%	0.00%	0.01%	0.01%	-0.14%	0.24%	-1.77%
Family business	0.01%	0.13%	0.06%	0.00%	0.72%	0.11%	0.39%	0.09%	0.04%	0.01%	0.04%	0.00%	0.04%	0.15%	0.17%			
Formal entrepreneurs	0.00%	-0.04%	0.00%	-0.06%	0.03%	-0.01%	-0.02%	0.03%	0.00%	0.00%	0.00%	0.02%	0.00%	0.00%	0.03%	0.01%		

H1-23 to H1-24

Formal workers
Own business
Freelance workers
Family business
Formal entrepreneurs

Formal workers	-0.02%	-0.28%	0.08%	0.00%	0.27%	0.04%	0.20%	0.12%	0.06%	-0.02%	0.06%	0.33%	0.22%	0.22%	-0.13%			
Own business	0.00%	0.00%	-0.03%	0.01%	-0.09%	-0.10%	-0.02%	-0.03%	-0.01%	0.01%	-0.01%	0.00%	0.03%	-0.04%	-0.01%			
Freelance workers	-0.20%	0.00%	0.07%	0.00%	-0.10%	0.01%	0.01%	0.01%	0.00%	0.00%	0.01%	0.00%	0.00%	-0.02%	0.18%	-0.41%	-0.51%	
Family business	0.02%	0.11%	-0.04%	0.00%	0.10%	-0.01%	0.14%	-0.06%	-0.04%	0.01%	0.01%	0.00%	-0.04%	-0.14%	-0.04%			
Formal entrepreneurs	-0.01%	0.03%	-0.01%	0.05%	-0.03%	0.06%	0.06%	-0.03%	0.00%	0.01%	0.00%	0.00%	0.00%	-0.03%	-0.03%			

Total: H2-19 to H1-24

Formal workers
Own business
Freelance workers
Family business
Formal entrepreneurs

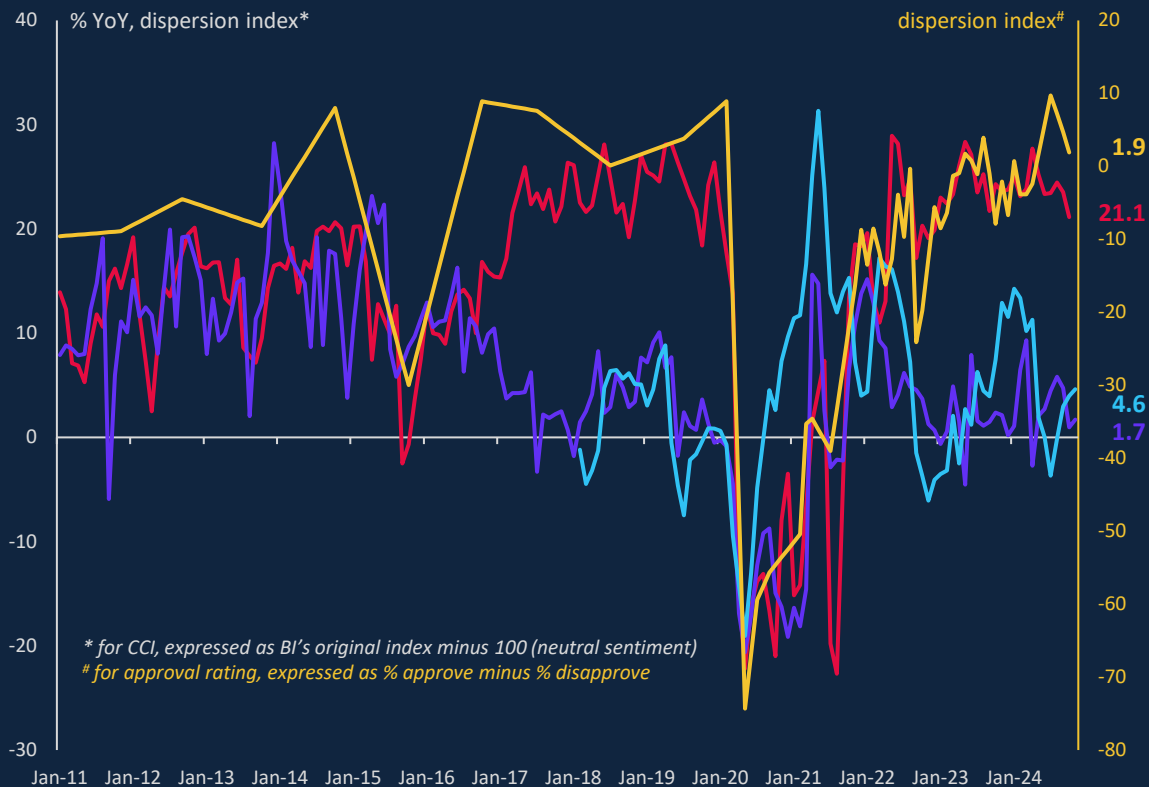
Formal workers	0.03%	-0.97%	0.01%	-0.07%	0.05%	0.05%	0.17%	0.07%	-0.13%	-0.03%	-0.01%	0.09%	0.14%	0.15%	-0.32%			
Own business	0.05%	0.07%	0.00%	0.09%	-0.35%	-0.26%	0.18%	0.00%	0.01%	0.03%	0.01%	0.00%	0.05%	0.02%	-0.01%			
Freelance workers	1.41%	-0.01%	-0.05%	-0.01%	-0.28%	0.14%	0.01%	0.01%	0.01%	0.00%	0.00%	0.01%	0.00%	0.01%	0.04%	-0.17%	-2.27%	
Family business	0.02%	0.23%	0.01%	0.00%	0.82%	0.10%	0.53%	0.04%	0.00%	0.01%	0.04%	0.00%	0.01%	0.01%	0.13%			
Formal entrepreneurs	0.00%	-0.01%	-0.01%	0.00%	-0.01%	0.04%	0.04%	0.00%	0.00%	0.01%	0.02%	0.00%	0.00%	0.00%	-0.02%			

Source: BPS, calculations by BCA Economic Research

* not in labor force, for reasons of education, housework, or others (NEET)

Feels over reals

Consumer sentiment ebbs albeit still on a high baseline—in line with presidential approval—but is now decoupled from actual retail sales

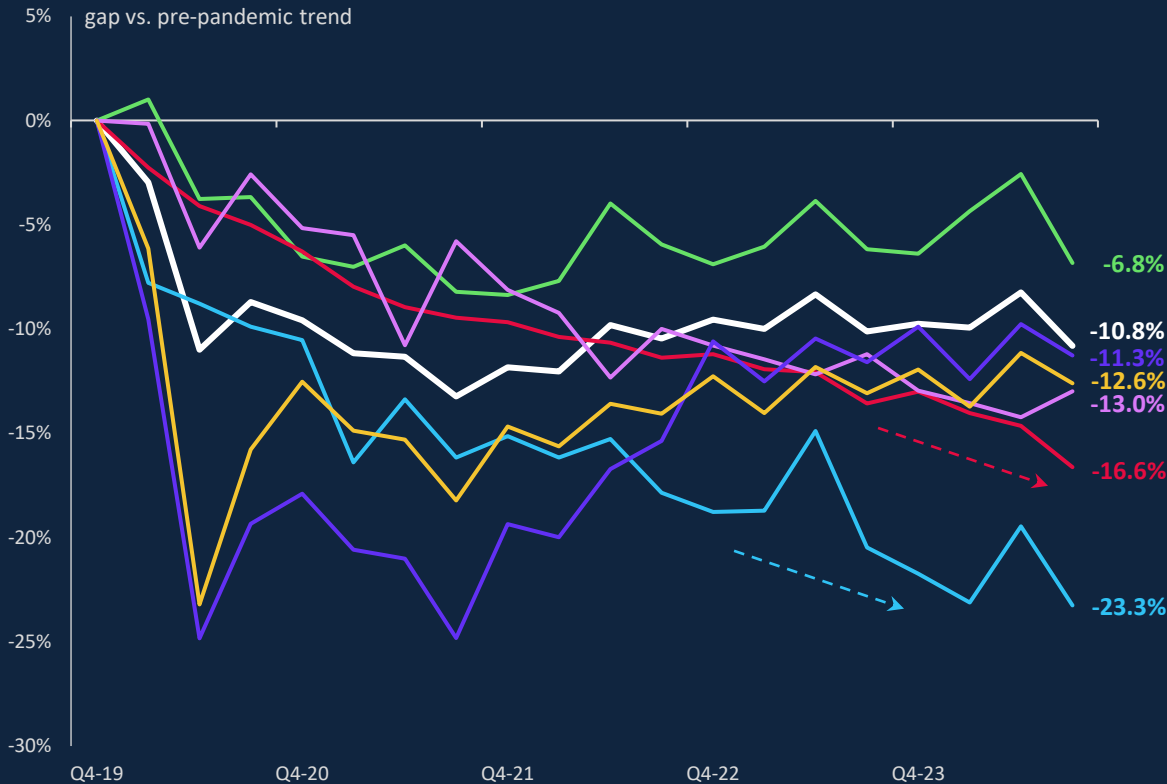


- Retail sales growth broadly mirrors BCA's big data index for consumer spending (see [35])
- Strong correlation between economic and political sentiments is, by now, a well-established phenomenon—e.g. partisan flips between Republican/Democratic administrations in the US

- ◀ Consumer confidence index (CCI)
- ◀ Real retail sales growth
- ◀ BCA Intrabel [35]
- ▶ Presidential approval, economic

Most wounds heal, but some fester

Despite some output loss, consumption has returned to its pre-pandemic growth rate—except for clothing and housing/appliances

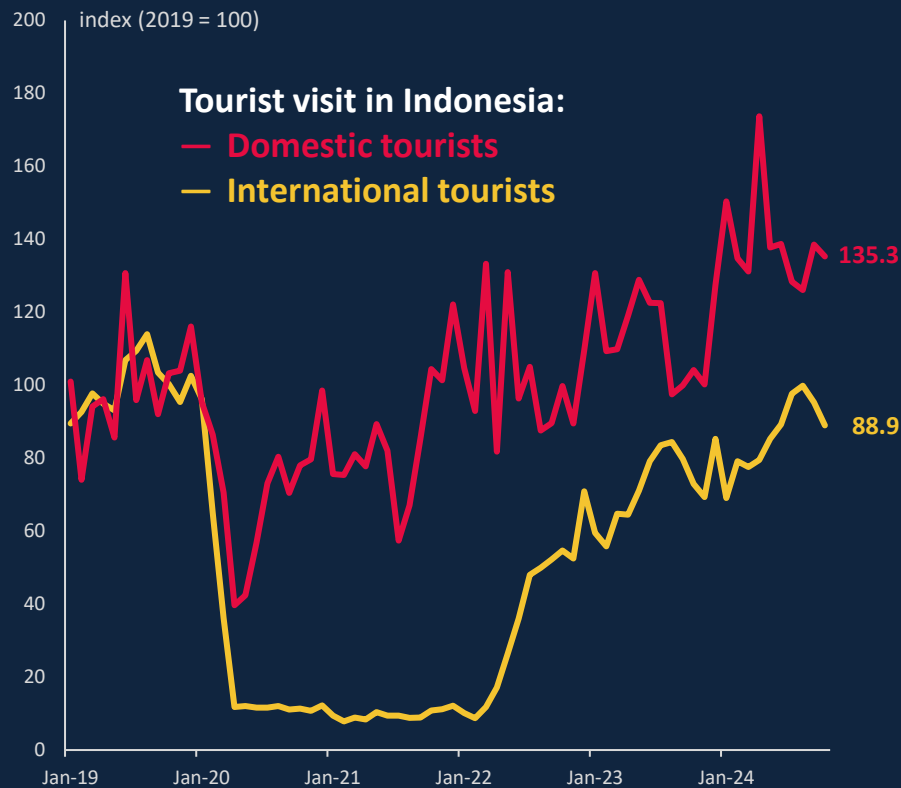


Source: BPS, calculations by BCA Economic Research

- Household consumption is ~10% lower than it should be, had there not been a pandemic
- Declining income makes big ticket items (**housing & appliances**) less affordable, but spending on more “affordable luxuries” (**travel & dining out**) has held up better
- Nominal household consumption, gap vs. pre-pandemic trendline:
 - **F&B ex-restaurant**
 - **Clothing & footwear**
 - **Hotel & restaurant**
 - **Housing & appliances**
 - **Health & education**
 - **Transport & communication**

Traveling without moving (countries)

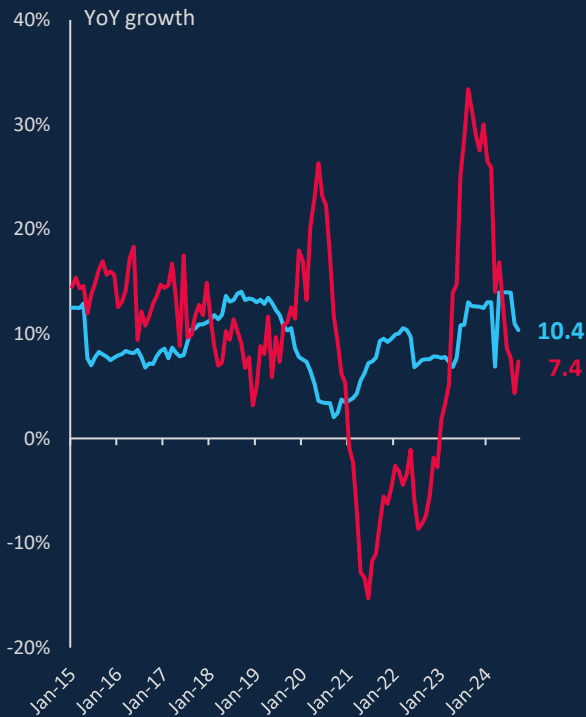
International tourism has not fully recovered, but this has been offset by increased travel within Indonesia



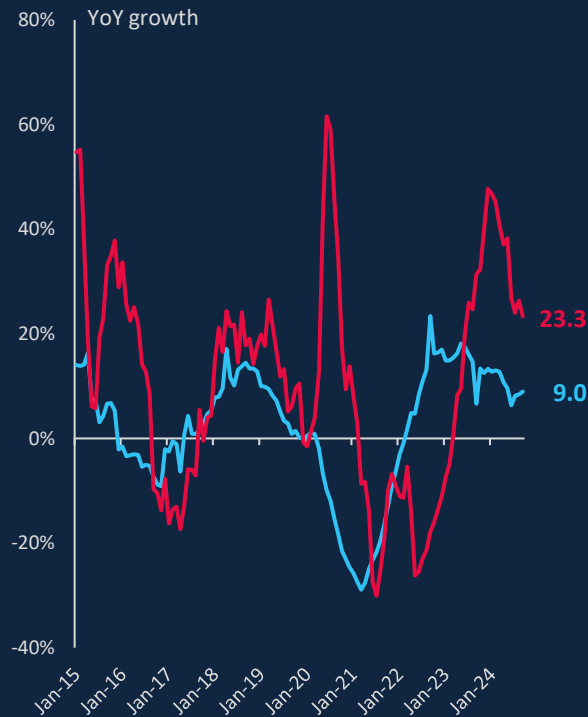
Risk(y) appetite

Consumer loan delinquency skyrocketed in the past year, which persists especially for smaller ticket-size loans

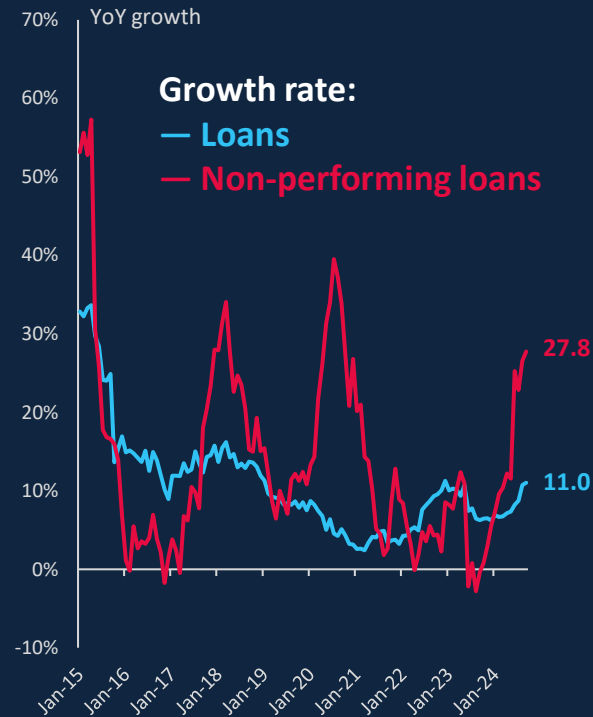
Loans: Landed house



Loans: Motor vehicles

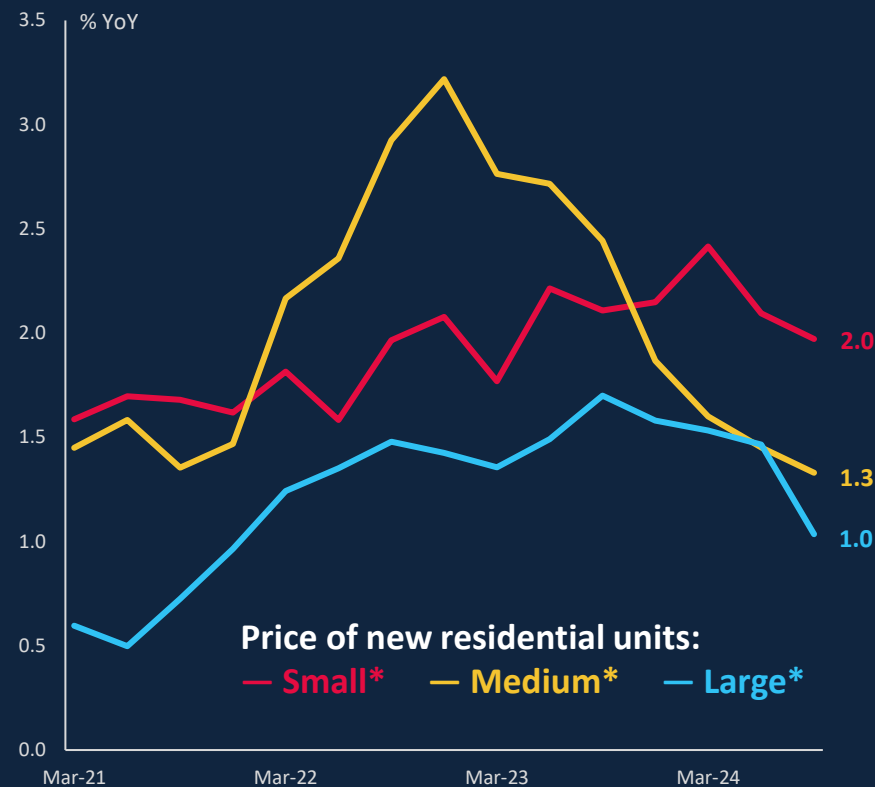
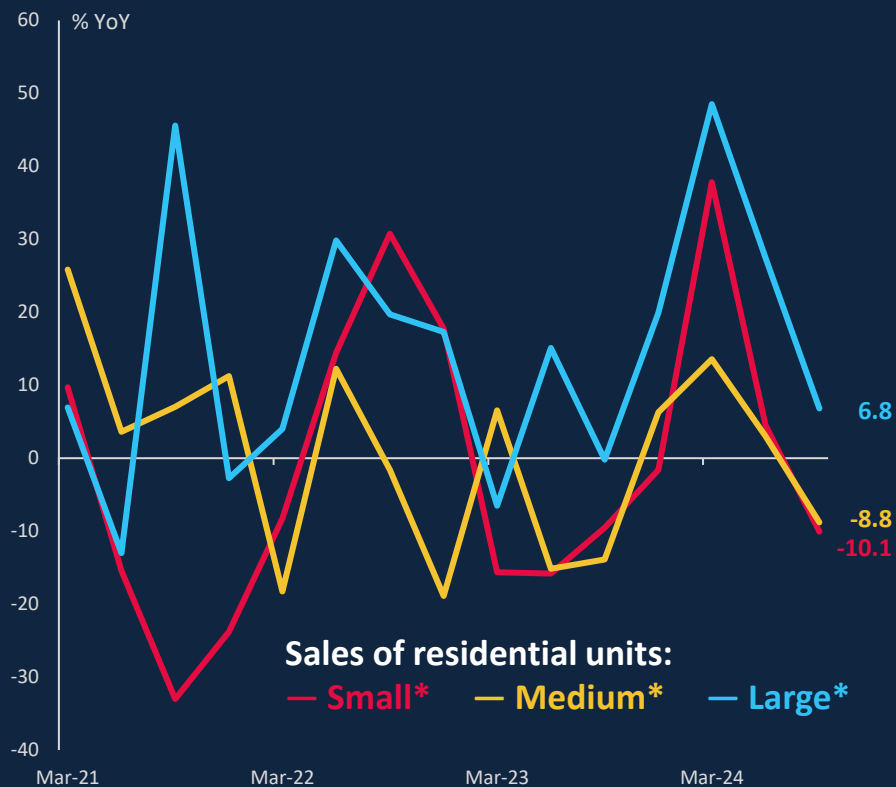


Loans: HH appliances



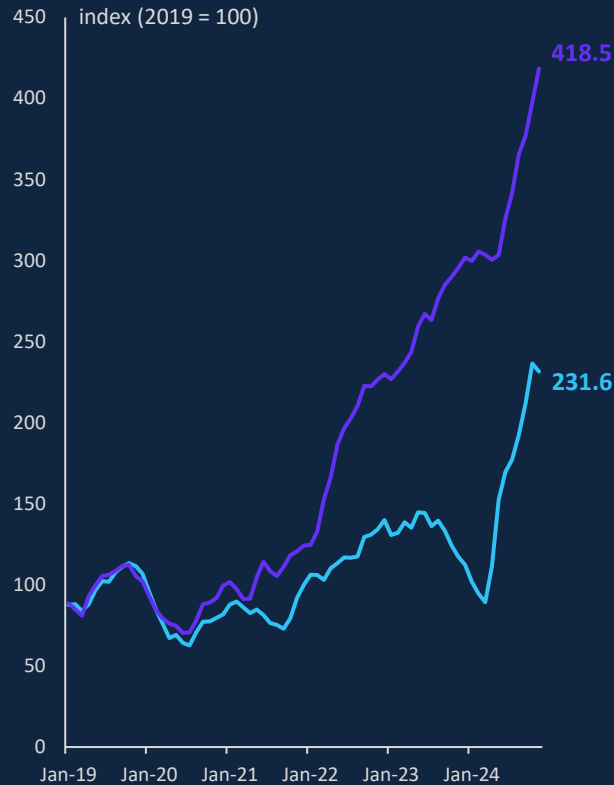
Missing middle #1: Housing

Sales of mid-sized homes have struggled since the pandemic, while larger homes have seen stronger demand but also slower price increase



Missing middle #2: Vehicles

Bifurcated market for motor vehicles may be another symptom of growing income disparity



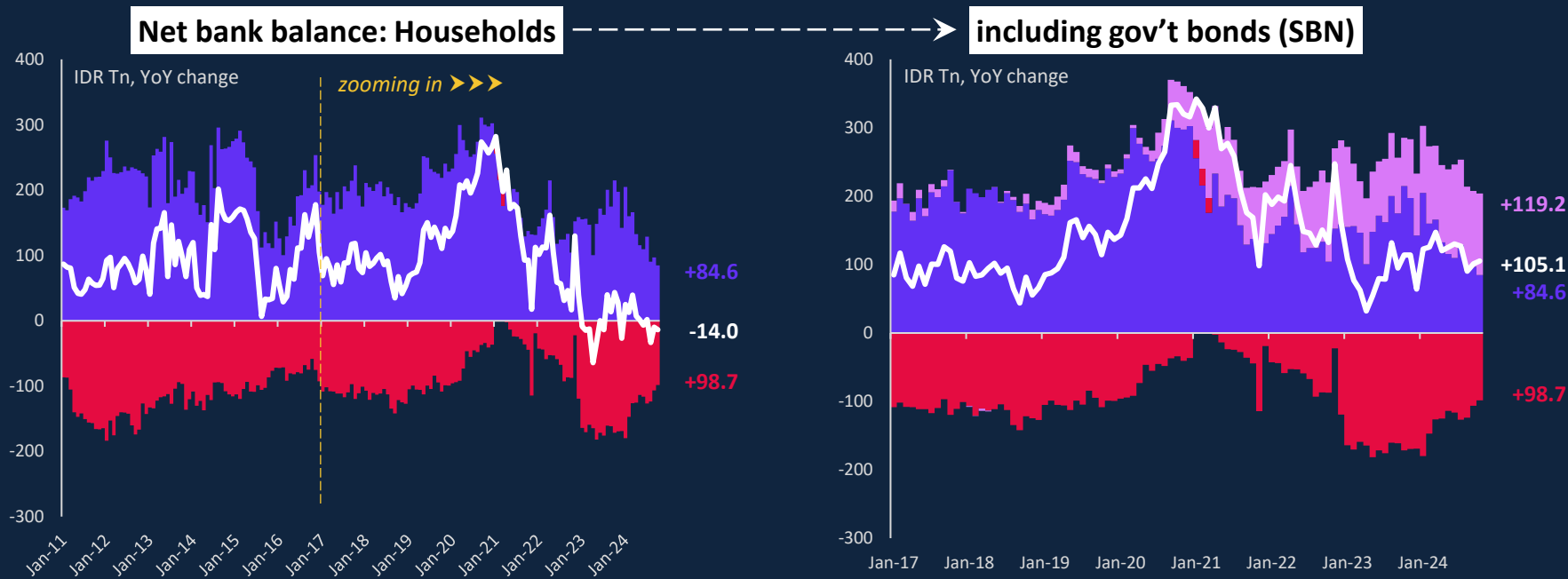
- Low-end and mid-range cars (LCGC and most 4x2) that traditionally accounts for the bulk of car sales are declining
- Recent growth is mostly seen for motorcycle and high-end cars (sedan & 4x4), plus demand from commodity-producing areas (motorcycle and 4x4/offroad cars)

Vehicles sales:

- Motorcycle
- 4x2 cars
- LCGC ("low-cost green cars")
- Commercial (bus, truck, etc.)
- Sedan
- 4x4 cars

Dissaving and disparity

Households appear to no longer be a net saver—but the increase in SBN holdings suggests that wealthier households merely shift their savings



— Net bank balance (NBB), YoY change:

■ Change in deposits

■ Change in loans

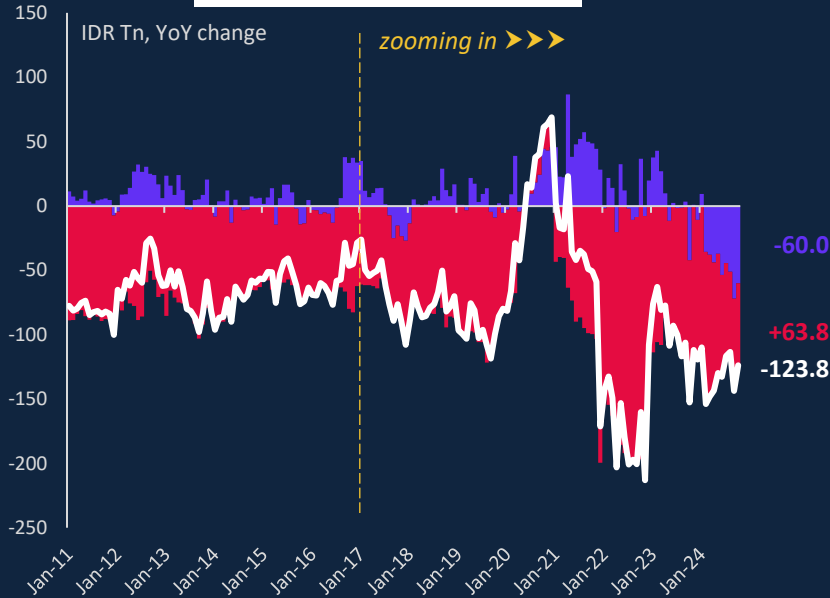
■ Change in government bonds (SBN) held

Source: BI, OJK, MoF, calculations by BCA Economic Research

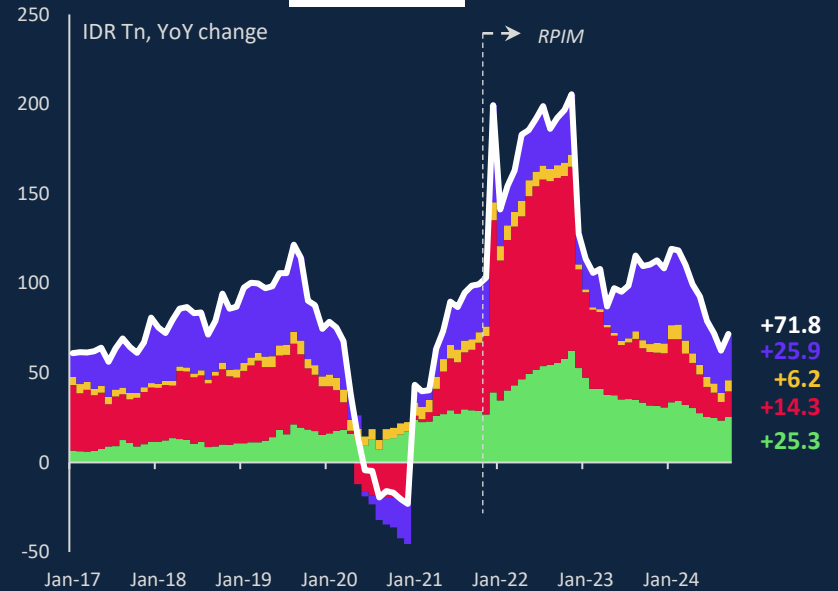
Double trouble

SMEs' cashflow deteriorates, just as growth in SME loans moderates following policy-driven salvos in 2022-23

Net bank balance: SMEs



SME loans



— **Net bank balance (NBB), YoY change:**
■ Change in deposits* ■ Change in loans

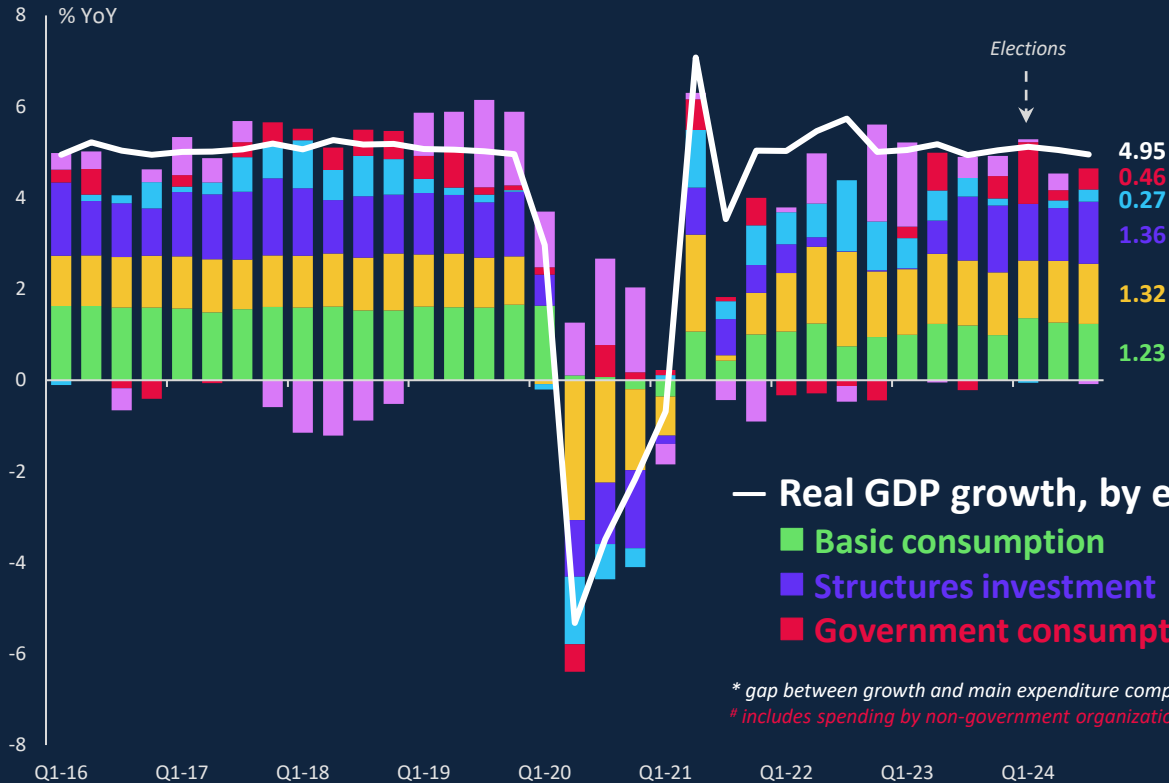
— **SME loans, YoY change, by sector:** ■ Agriculture ■ Trade & repair ■ Hotel & restaurant ■ Others

Source: BI, OJK, MoF, calculations by BCA Economic Research

* checking accounts with individual holders

Relying on largesse

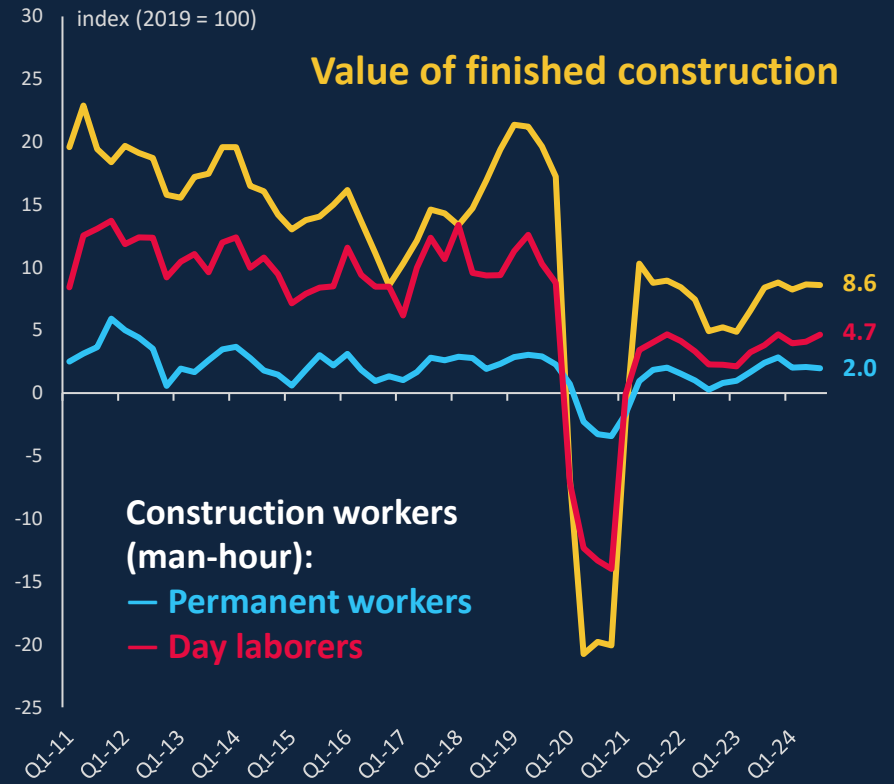
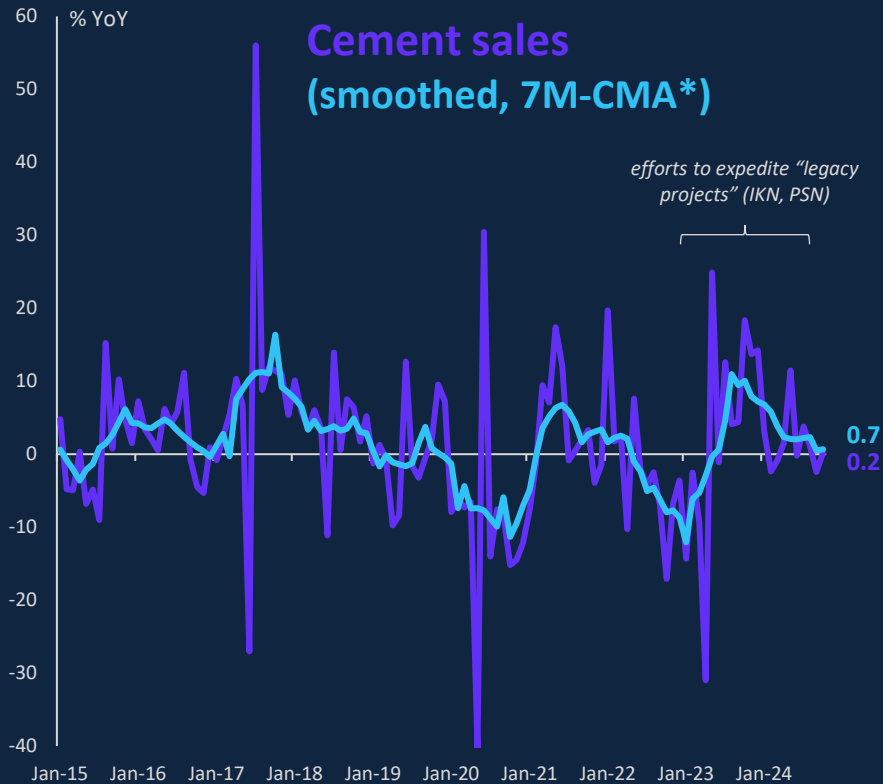
GDP growth in 2024 depended substantially on government support—both for consumption and investment



- **Gov't spending** contributed to growth not just directly as during the Elections (Q1-24) ...
- ... but also indirectly by adding to **basic consumption** (via social aid) and **investment in buildings** (via new capital city and other legacy projects)

New normal

Construction activities improved in recent quarters, but are still considerably lower than their pre-pandemic baselines

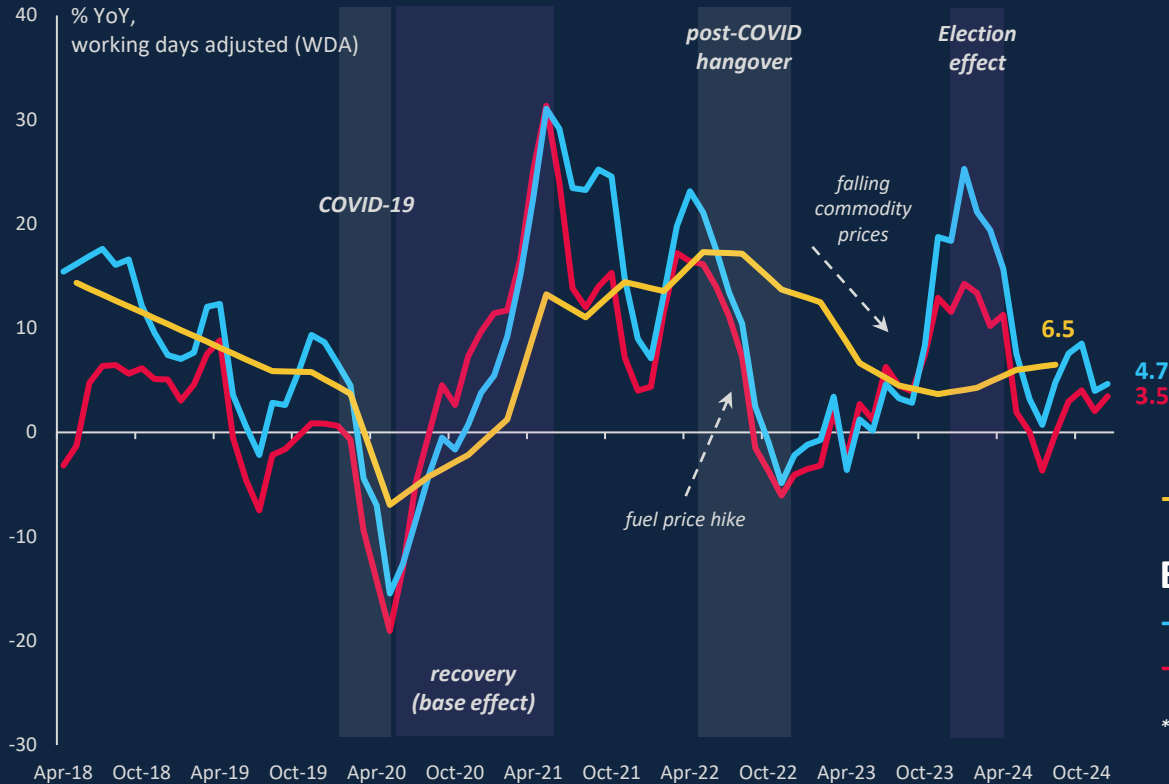


Source: CEIC, BPS, BCA Economic Research

* 7-mth centered moving average

Out of steam?

The economy lost momentum after the Elections, although there has been some limited improvement at the back end of 2024



- Both of our big data indices (on the **business** and **consumer** sides) generally align with **nominal GDP growth** ...
- ... although there were disparities in 2022 to early 2024, due to large swings in commodity prices (and thus export revenues)

— **Nominal GDP growth**

BCA big data indices*:

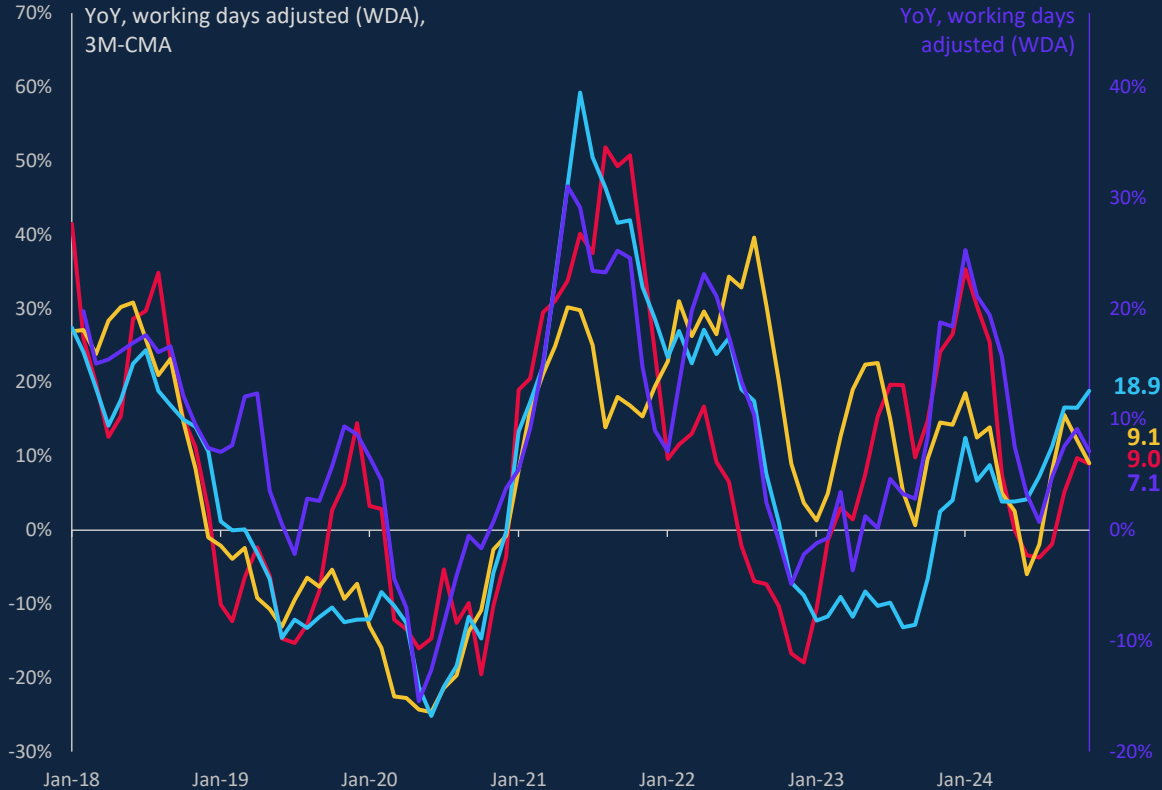
— **Business transaction index ("Intrabiz")**

— **Consumer spending index ("Intrabel")**

* 3-mth centered moving average (3M-CMA)

Defensive rebound

Imports of raw materials are rebounding nicely, but things are otherwise pointing towards softer domestic demand



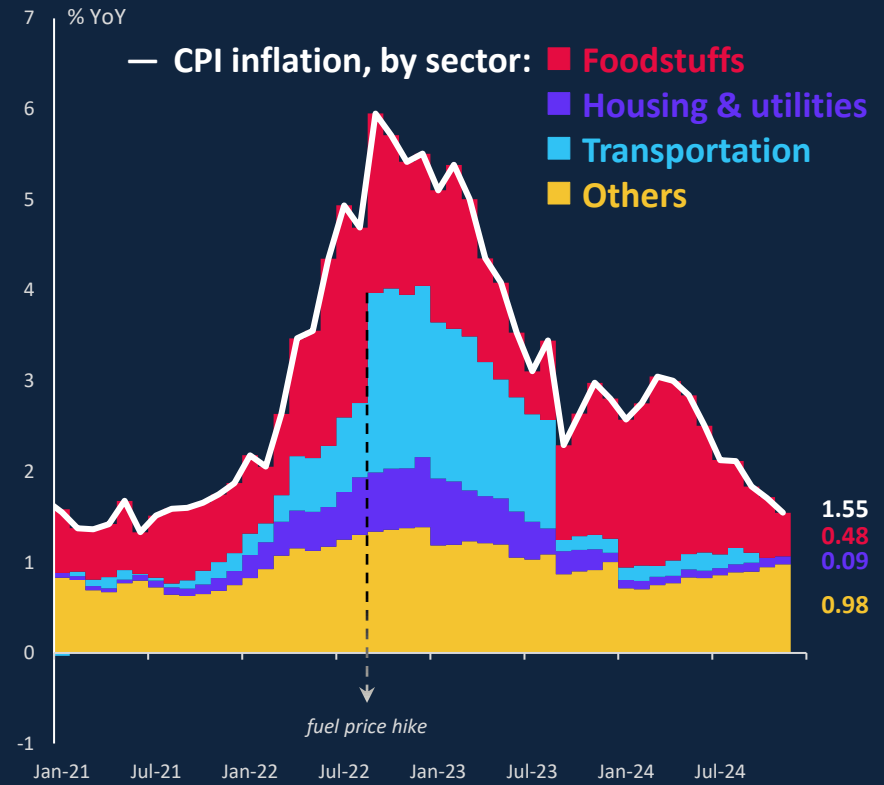
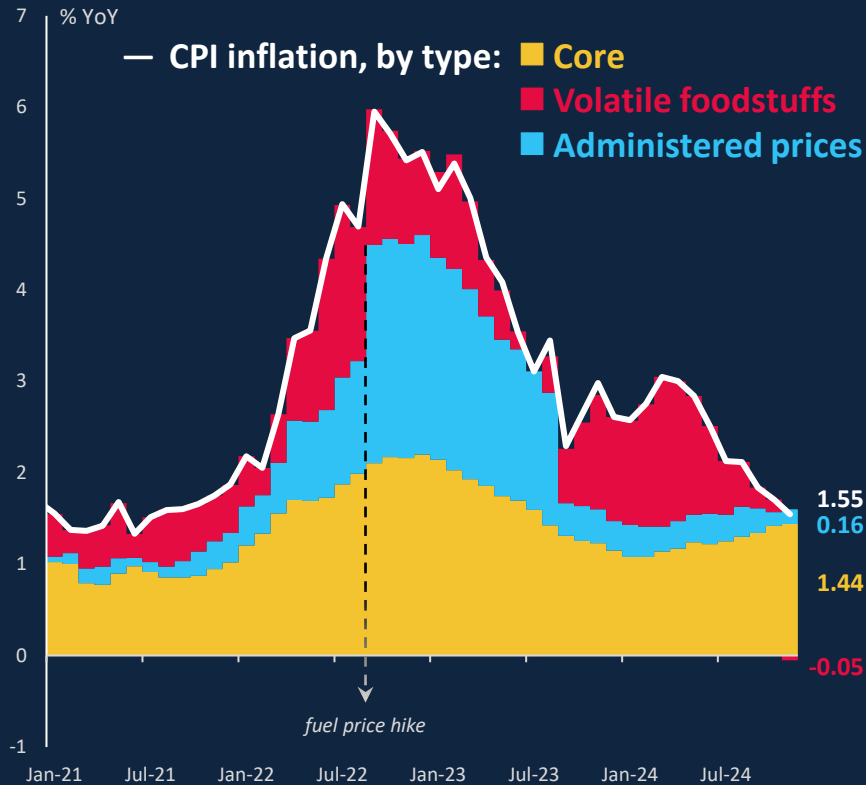
Source: BPS, calculations by BCA Economic Research

- **Import growth broadly mirrors BCA's big data indices on business revenue (see [35])**
- **High raw material imports seem to largely reflect government effort to stabilize food prices, i.e. through rice imports**

- **BCA Intrabiz [35]**
- ◀ **Imports by category:**
 - **Consumer goods**
 - **Capital goods**
 - **Raw materials ex-oil/gas**

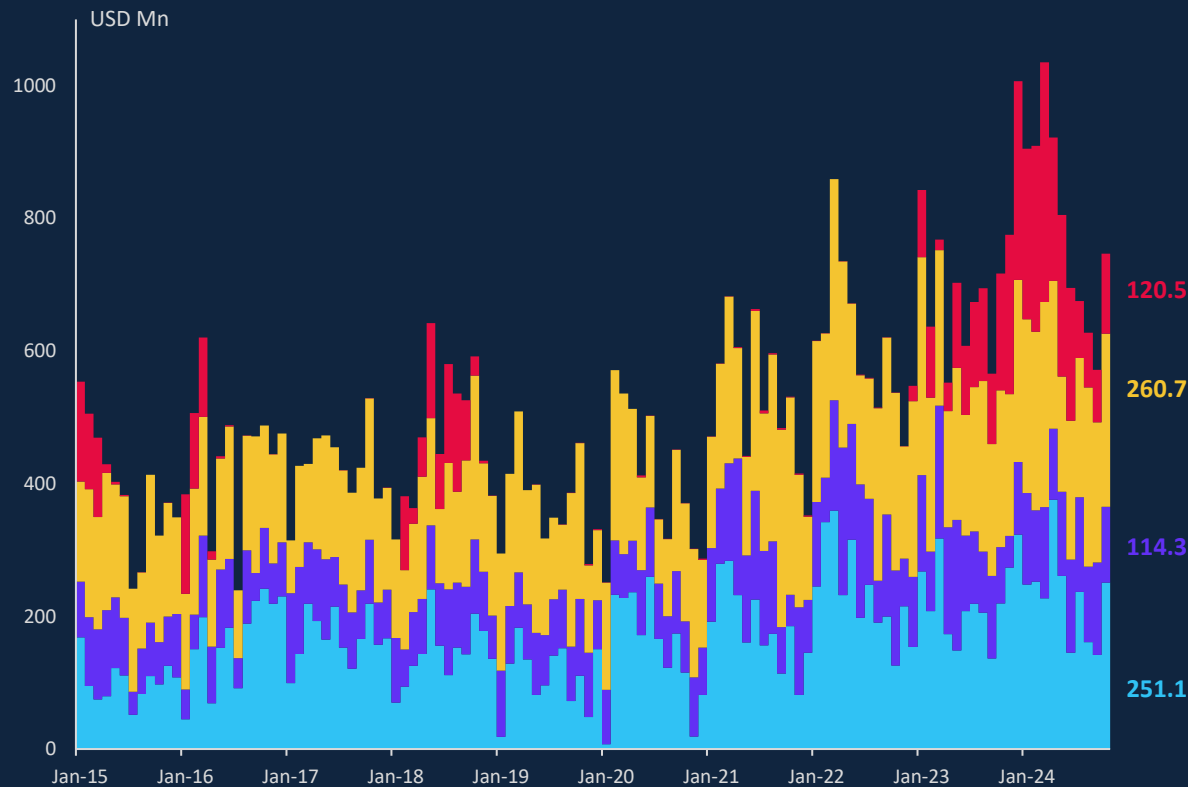
Disinflation is good, actually

Slowing inflation raises concern about weakening demand, but most of the recent disinflation has come from the supply-side (foodstuffs)



Turning the tap back on

Increased rice imports have been crucial in taming the rampant food inflation of 2023-24



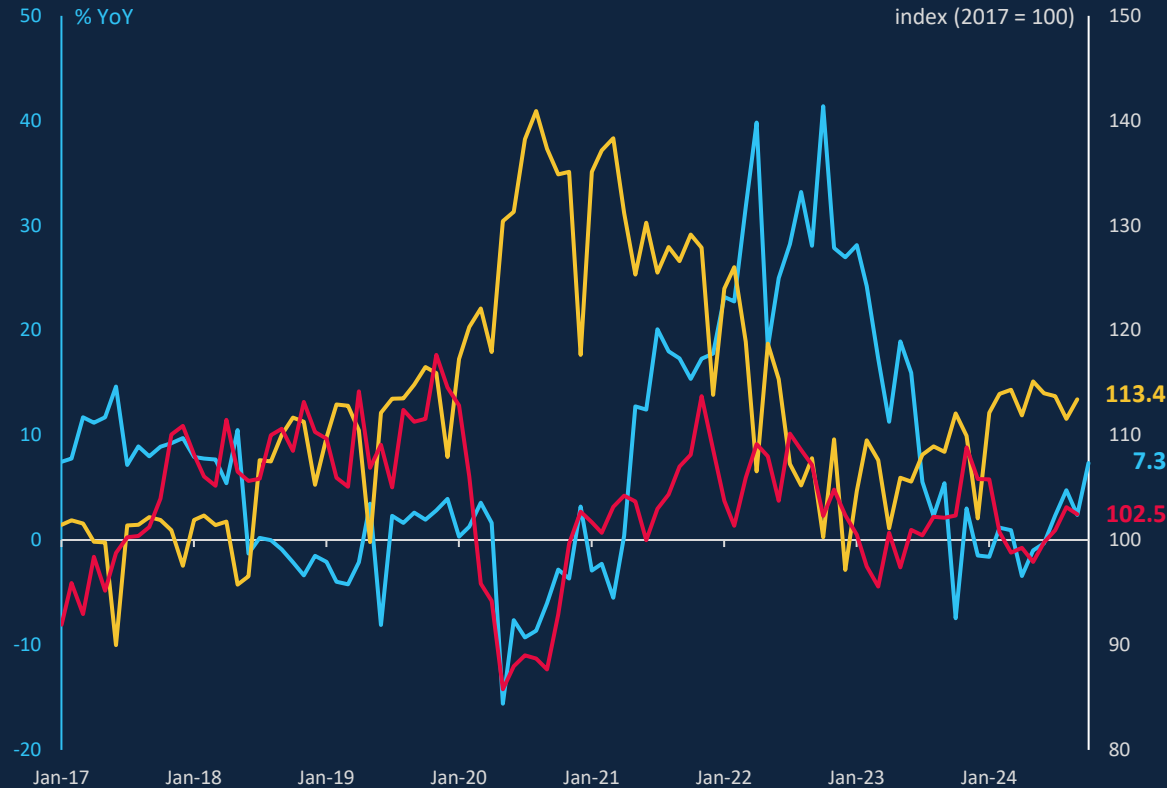
- Private **rice imports** are controlled by a quota system, but the government can also import to refill its strategic reserves
- Drastic increase in imports (2018, 2023-24) tends to be driven by the government, to anticipate or relieve supply shortage

Import of foodstuffs,
top 4 commodities:

- Rice (HS 10063099)
- Wheat (HS 10019912)
- Soybean (HS 12019000)
- Sugar (HS 17011400)

Need for speed

Money supply grows at similar rates as during the late *Jokowinomics* boom (2018-19), but it currently circulates at much slower rates



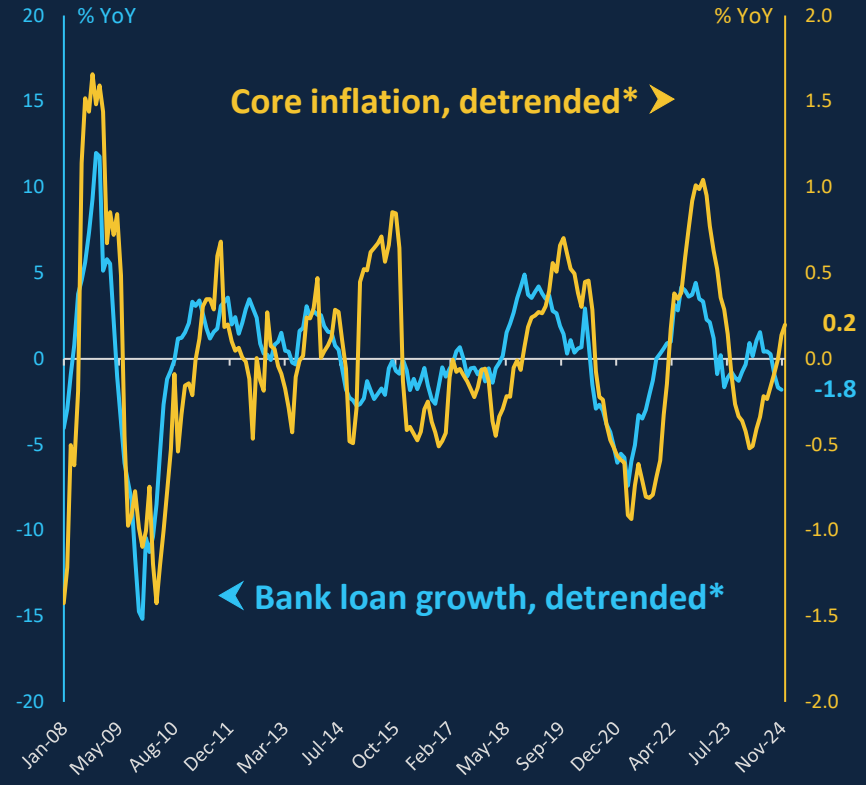
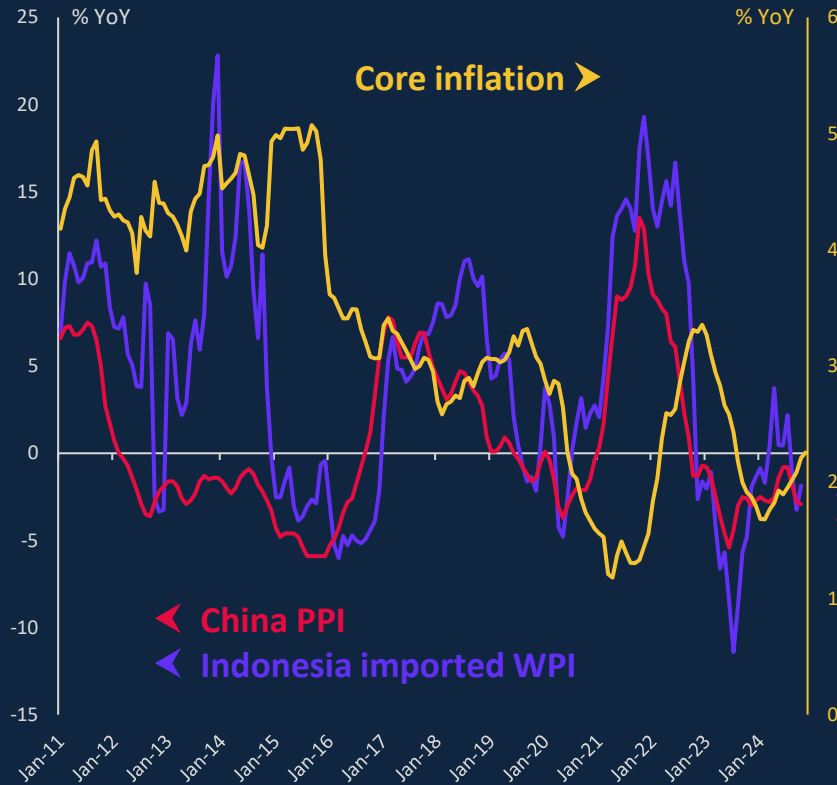
- With this chart, we break down nominal GDP growth—according to the quantity theory of money—into three drivers, in monetary terms:

- **Monetary policy by BI (M0)**
- **Credit by the financial sector (money multiplier)**
- **Money circulation in the real economy (money velocity)**

- ◀ **Base money (M0) growth**
- **Money multiplier (M2/M0)**
- **Implied velocity of money (based on BCA big data)**

Not so hard-core

Core inflation has risen of late due to gold price, but two key determinants—imported inflation and loan growth—hint at future moderation



Source: BPS, BI, OJK, Bloomberg, calculations by BCA Economic Research

* using H-P filter to retain only the cyclical component

Slouching towards utopia

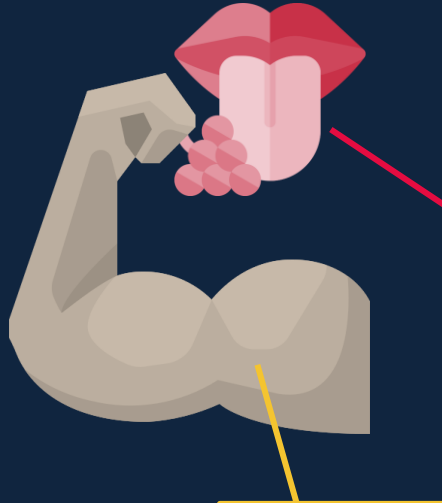
- Pres. Prabowo's rise to power was premised on the continuation of Pres. Jokowi's "Golden Indonesia" vision, which aimed to make Indonesia a high-income economy by 2045. To this end, he set an ambitious growth target of 7-8%, to be attained by the end of his first term in 2028-29.
- However, the President's programs [43] do depart substantially from his predecessor's. For one, instead of infrastructure, there is more emphasis on welfare programs such as free school meals.
- On the supply-side, meanwhile, "*Prabowonomics*" largely revolves around natural resources. This includes replicating the success of downstreaming of nickel ores on other commodities, as well as a "food estate" project to expand agricultural output.
- All these programs, however, are large-scale undertakings, which face considerable hurdles before they can get off the ground [44]. Food estate, for example, has the potential to address the issue of agricultural land conversion [45], but it also requires extraordinary efforts to boost agricultural productivity in Papua [46].
- For all the potential bureaucratic and economic hurdles, however, the main bottleneck in the short-term lies in financing. The state's fiscal capacity is limited, with low tax ratio (10.3% of GDP in 2023) and revenue that depends greatly on the commodity cycle [48].
- High global rates add more difficulties, with interest payment now eating up over 2% of the GDP—which, since the deficit is legally capped at 3%, leaves very little room for fiscal discretion [49]. As such, accommodating the new government programs necessitates a cut to the infrastructure (CAPEX) budget [50].
- Even a more modest fiscal push, as in 2024, had forced the state to utilize some of its accumulated savings [51]. We should note, however, that the use of these funds [52] was in part a tactical choice to keep borrowing costs stable, by reducing SBN issuance.
- Such tactics, unfortunately, might not be adequate in 2025, given increased financing needs partly to refinance maturing debt [53]. The authorities, as such, would have to get more creative in their quest for financing.

Financing beyond frontiers

- In recent months, the government has floated several proposals to bridge this financing gap [47], only one of which looks certain to be implemented in 2025 (12% VAT rate). Some, like the establishment of a new state investment company (*BP Danantara*), might take time, while others could face political resistance.
- The crux of the issue, however, is that it is not just fiscal capacity that is limited—the *national* financing capacity is also increasingly limited. We can visualize this by adding up the net liquidity (NBB) of all the sectors within the economy—government, corporations, households, etc.—as we do in [54].
- As we can see, there has been a consistent liquidity deficit *at the national level* since mid-2023, with uses of funds (investment) far exceeding the sources of funds (savings) that could finance it.
- Therefore, we are probably close to the limit as to how much the government could divert private funds for public uses. Additional taxes or levies, then, will—more likely than not—force a cutback in private spending, dragging growth lower.
- The more feasible path for Pres. Prabowo is to draw liquidity from abroad, in the form of FDI. His diplomatic tour, which began mere weeks upon assuming office, is likely informed by this reality. FDI, however, is likely limited to profitable projects—primarily those on the supply-side.
- Tax amnesty and *BP Danantara* are also interesting for a similar reason—that they can draw foreign funds, via repatriation for the former, or external debt (levering up its jumbo balance sheet) for the latter.
- Indeed, there is clear parallel between today and the early years of Pres. Jokowi, when a fiscal-focused first attempt at financing infrastructures floundered. The breakthrough was only achieved in 2016-17 [55], with tax amnesty and asset revaluation of SOEs that enabled them to take on larger debt.

Gotta catch 'em all

Pres. Prabowo's welfare programs grab most of the headlines, but (commodity-oriented) supply-side programs require even greater financing



DEMAND-SIDE (WELFARE) PROGRAMS

SCHOOL MEAL PROGRAM	<ul style="list-style-type: none"> • 2025 Budget = IDR 71 Tn (early trial/pilot) • Ideal budget = IDR 400 Tn (82.9 Mn children @ IDR 15,000)
NAT'L FOOD RESERVES	<ul style="list-style-type: none"> • 2025 Budget = IDR 15 Tn/yr
AFFORDABLE HOUSING	<ul style="list-style-type: none"> • Estimated need = IDR 53.6 Tn (to build 3 Mn house/yr)
SCHOOL UPGRADE	<ul style="list-style-type: none"> • 2025 Budget = IDR 22 Tn/yr (school renovations, integrated high-quality schools)
HEALTHCARE SPENDING	<ul style="list-style-type: none"> • 2025 Budget = IDR 13 Tn/yr (eradication of TB, upgrade of hospitals, free medical check-up)

SUPPLY-SIDE PROGRAMS

FOOD SECURITY	<ul style="list-style-type: none"> • 2025 Budget = IDR 124.4 Tn (food estate & other supporting activities)
ENERGY SECURITY	<ul style="list-style-type: none"> • Estimated need = at least USD 235 Bn to 2040 (100 GW power generation, bioethanol, CCUS)
DOWNSTREAMING	<ul style="list-style-type: none"> • Estimated need = USD 618 Bn to 2040 (for 28 commodities)

Additional financing needs per annum:

Demand-side = IDR 170 – 500 Tn (0.7 – 2.1% of GDP)

Supply-side = IDR 1,000 – 1,200 Tn (4 – 5% of GDP)

Base investment rate = 32% of GDP (average 2013-23 excl. pandemic)

Hurdle race

The new administration has to contend with several obstacles to ensure the impact and sustainability of its programs



FINANCING

- Lack of fiscal space (3% deficit limit)
- Public sector (gov't & SOEs) control plenty of assets, but only limited *liquid assets*
- Financing of public sector competes against private consumption & private CAPEX (*crowding-out effect*)
- *Weak global liquidity* hampers FDI & portfolio inflows

BUREAUCRATIC

- Unclear/overlapping regulations
- Coordination issues across multiple *(new) ministries & institutions*
- Slow or irregular fiscal disbursement, causing *liquidity issues* among gov't contractors/sub-contractors
- Weak execution capacity at lower levels of government
- *Inefficiencies & cost overruns*

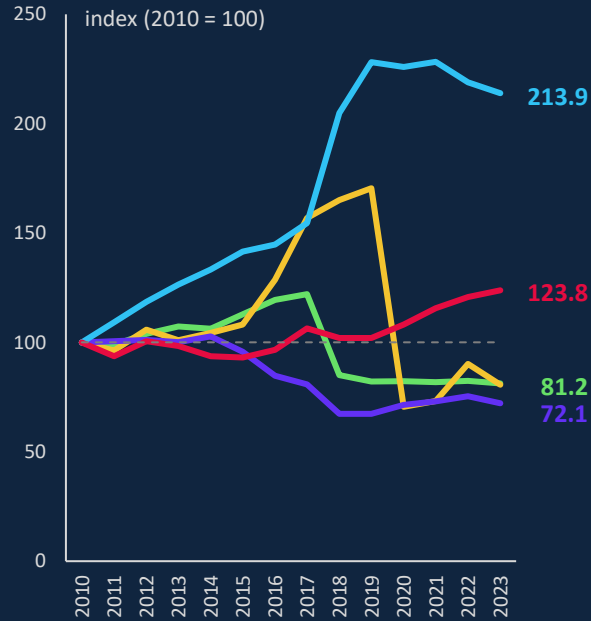
ECONOMIC

- Projects are inefficient (*high ICOR*) or lacking in economic case
- Economic benefits are *only realized in the long-run* (e.g. higher HDI)
- Economic benefits are externalized by the private sector, gov't & SOEs unable to recoup investment
- Investments fail to generate national savings (i.e. improve CA balance), thus *increasing dependence on external financing for future projects*

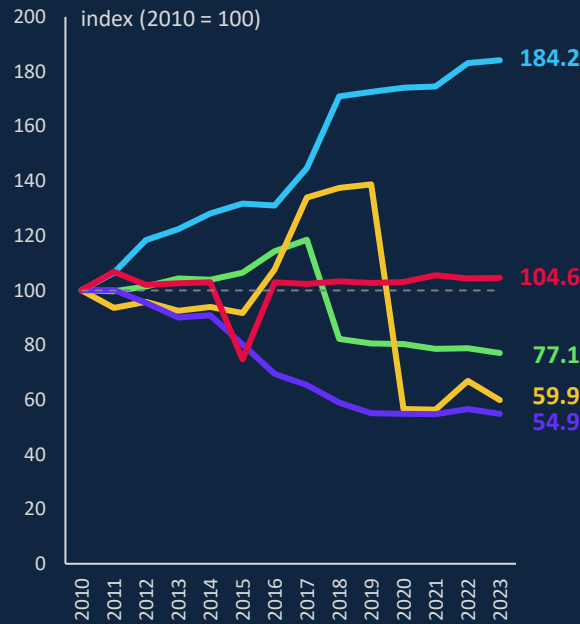
Hungry for land

Agricultural output has been kneecapped by conversion of farmlands to development—which is to be remedied by the “food estate” program

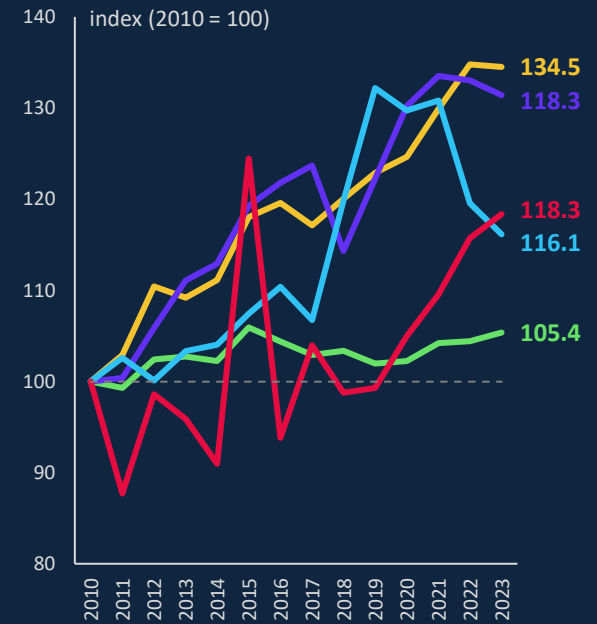
Production



Area harvested



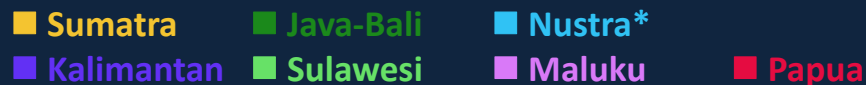
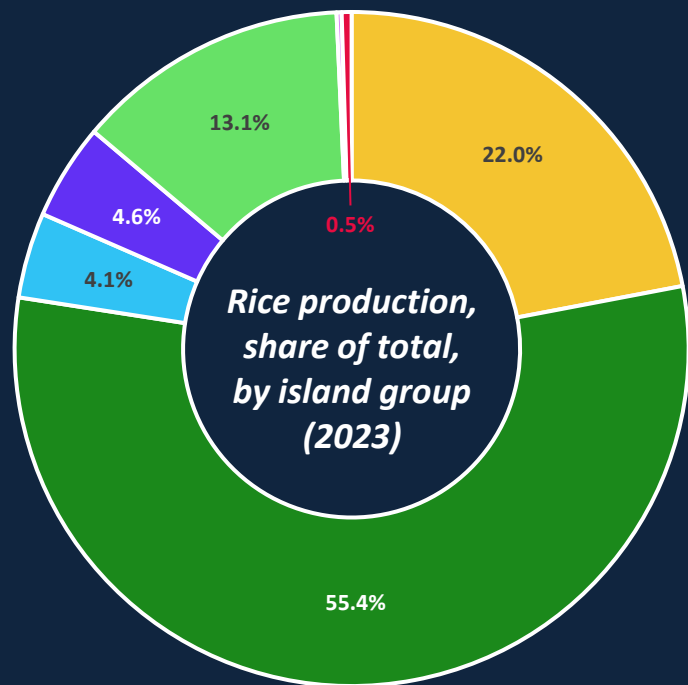
Productivity per unit area



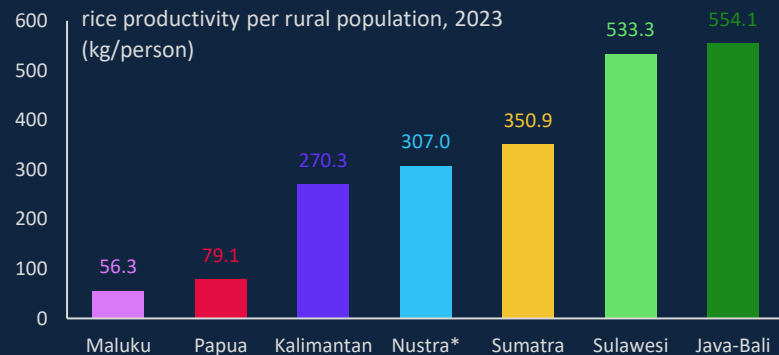
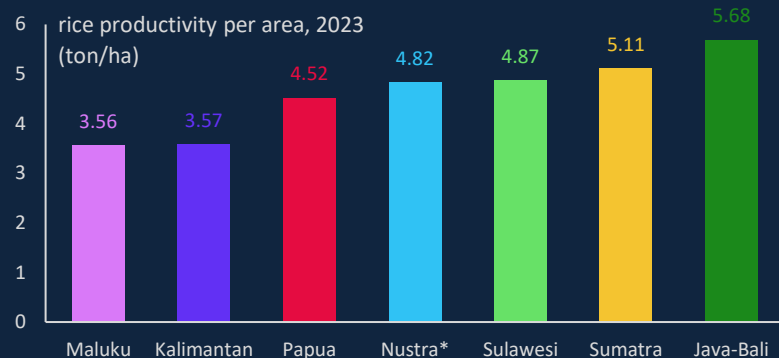
Agricultural commodities: — Rice — Maize — Cassava — Oil palm — Coffee

Colossal task

Raising Papua's agricultural productivity will be a challenge—and may require large-scale transmigration from Java



Source: BPS, calculations by BCA Economic Research



* Nusa Tenggara (Southeastern Islands), excluding Bali

Knife to a gunfight?

In general, the proposals to raise public sector liquidity are rather inadequate to address the financing gap



VAT to 12% (partly offset by stimulus*)

Liquidity raised: Around 0.3-0.4% of GDP (recurrent)

Drawback: Some decline in consumption growth, probably towards 4.6-4.8% YoY (vs. typically 4.9-5.0%)

Tax amnesty (3rd round)

Liquidity raised: One-time influx, about 0.3% of GDP (TA-1 in 2016-17 raised 1.2% of GDP, but diminishing returns are likely in repeated amnesties)

Drawback: Minimal, except for long-term moral hazard

Tapera levy (postponed)

What it is: Compulsory contribution to the Housing Fund, at 3% of wages

Liquidity raised: About 0.2-0.3% of GDP (recurrent)

Drawback: Slower consumption for the middle class (forced savings)

BP Danantara

What it is: State-owned investment firm (*à la* Temasek), comprised of 7 major SOEs

Liquidity raised: Potentially 5-10% of GDP over the next 5-10 years

Drawback:

- Will take time to set up
- Uncertainty on structure & governance
- Potential disruptions & worsening risk perception on the SOEs involved

Limiting distribution of Pertalite[#]

Liquidity raised: Up to 0.3-0.4% of GDP (recurrent)

Drawback:

- Slower consumption (partly compensated by cash transfers)
- Modest impact on CPI inflation

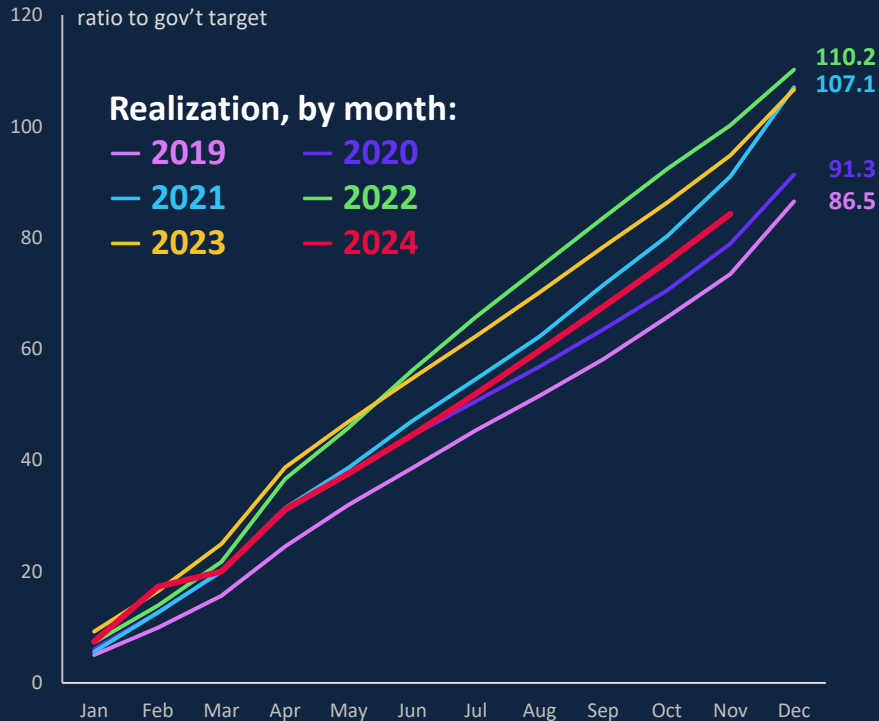
* New fiscal package to help consumers & SMEs, announced December 16th

[#] Pertamina's RON 90 gasoline: formally non-subsidized, but the price is usually fixed below production cost (for which the government compensates for the shortfall)

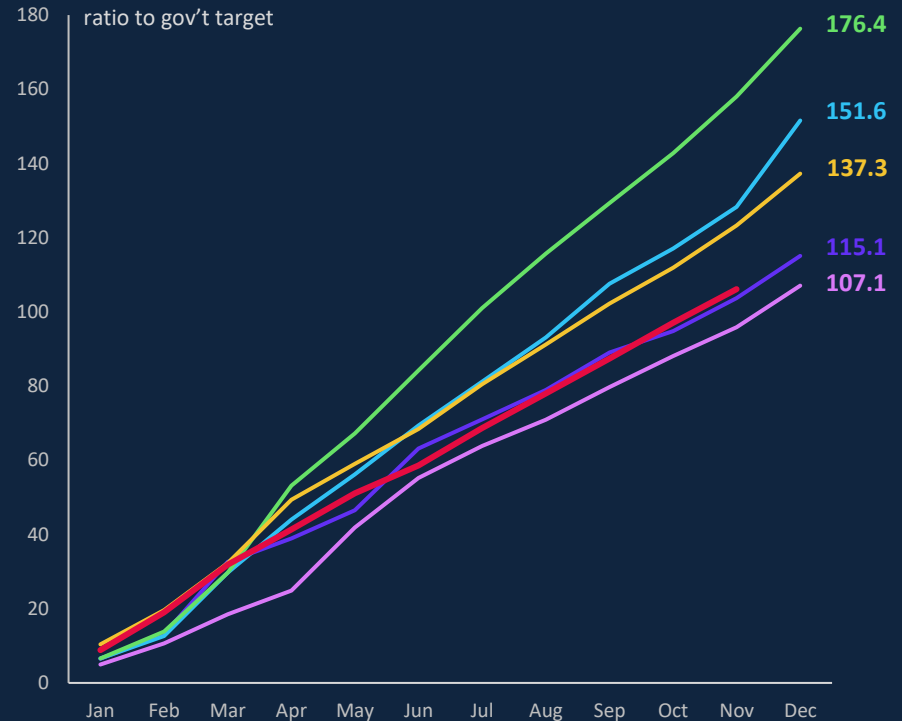
Nice run while it lasted

Government revenue greatly depends on commodity prices, and so the “pleasant surprises” of 2021-23 are not exactly replicable

Tax revenue

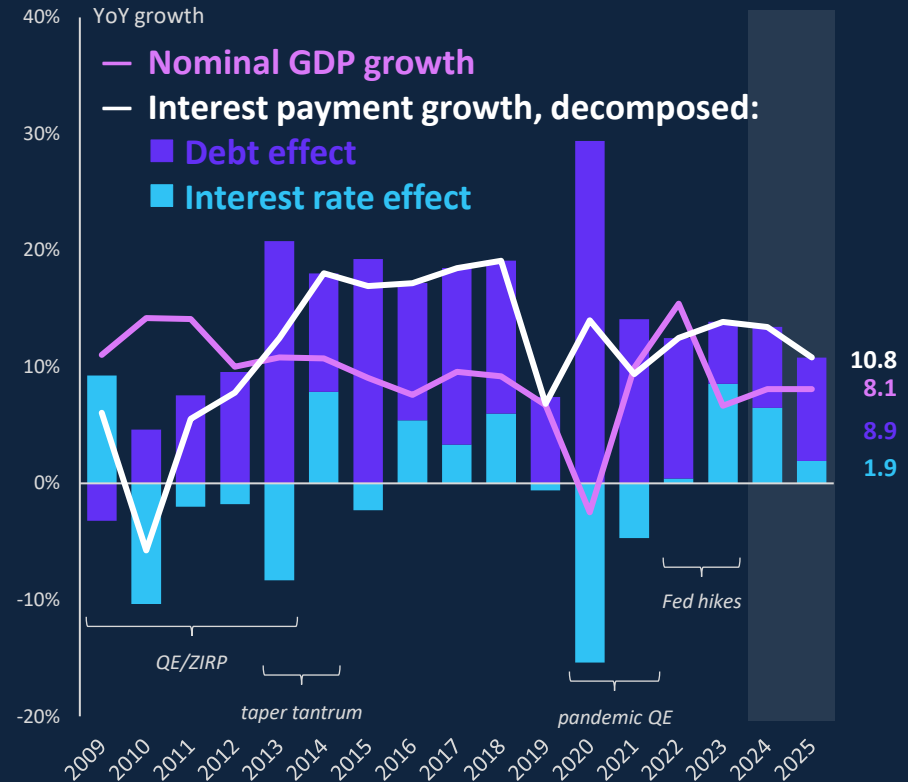
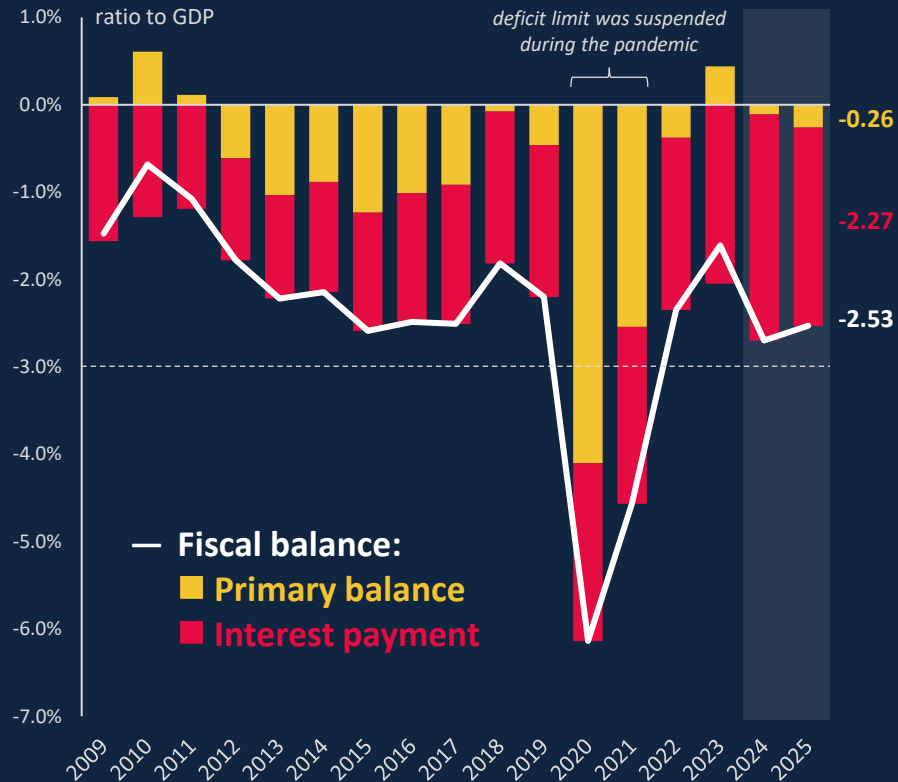


Non-tax revenue (commodity & others)



Stay positive

If global rates remain elevated, the government will have to maintain a primary surplus (or close to it) to stay within the fiscal deficit limit

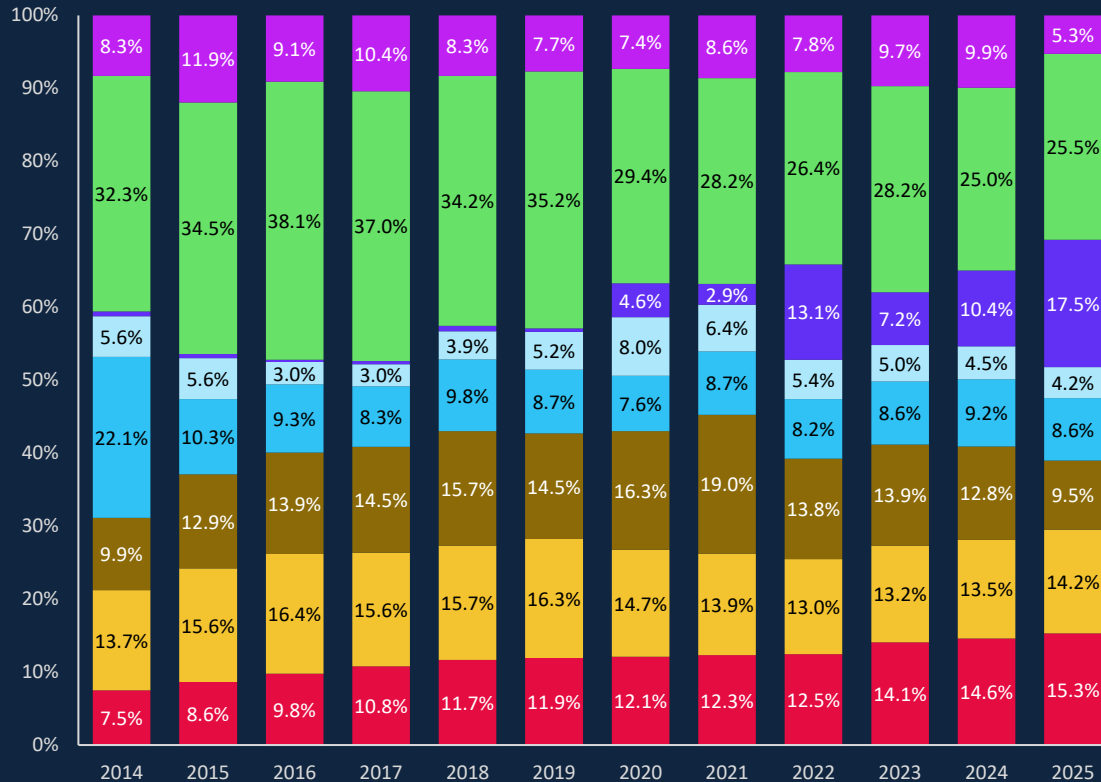


Source: MoF, BPS, calculations by BCA Economic Research

* figures for 2024-25 are based on MoF forecasts

Smaller headroom

Amid growing interest burden and “other spending”, the portion of State Budget allocated towards capital expenditure shrinks



- The sharp rise in “other spending” anticipates new programs by the Prabowo administration (e.g. free school meal) as well as a potential increase in energy compensation (for fuel and electricity)

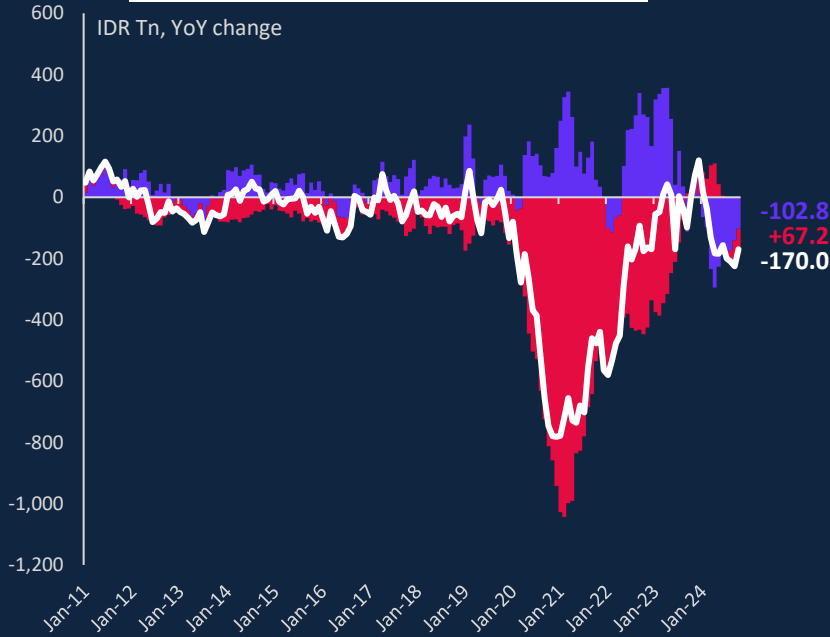
State Budget allocation:

- Interest payment
- Employee compensation
- Goods expenditure
- Subsidies
- Social assistance
- Other (uncategorized) spending
- Regional transfers
- CAPEX

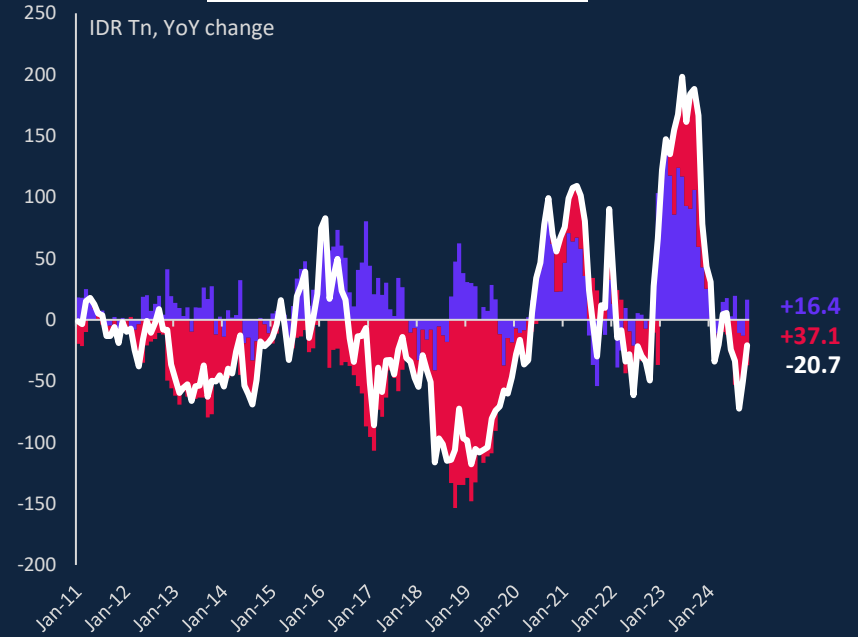
Digging deep

The public sector's liquidity needs in 2024 has necessitated dissaving by the government, while SOEs require bridging loans

Net bank balance: Government*



Net bank balance: SOEs



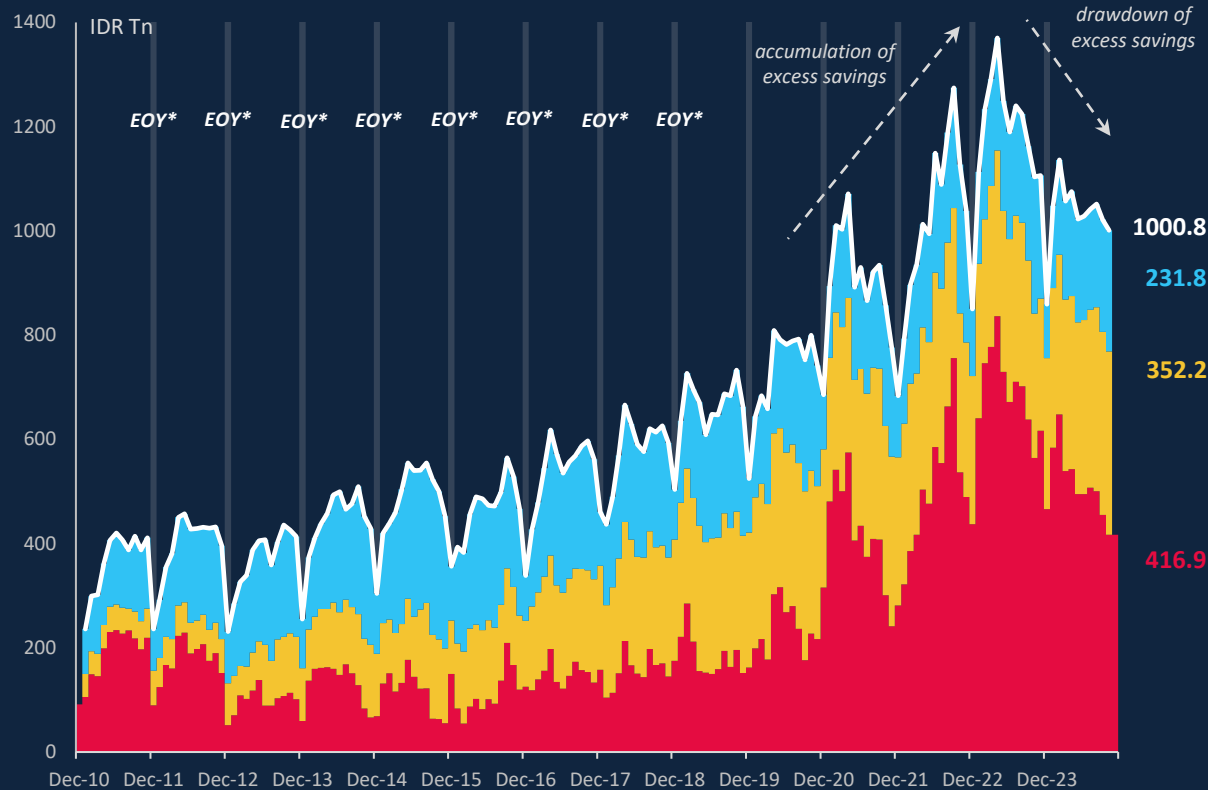
— Net bank balance (NBB), YoY change: ■ Change in deposits ■ Change in loans and bonds

Source: BI, OJK, MoF, calculations by BCA Economic Research

* central and regional governments combined

Savings for a rainy day

Excess financing during the pandemic has been a valuable buffer amid challenging conditions in 2023-24



- Gov't spending tends to be concentrated at year-ends, leading to a cyclical pattern for growth and liquidity
- MoF is allowed to use **excess financing** (*saldo anggaran lebih – SAL*) to finance current deficit, subject to legislative approval

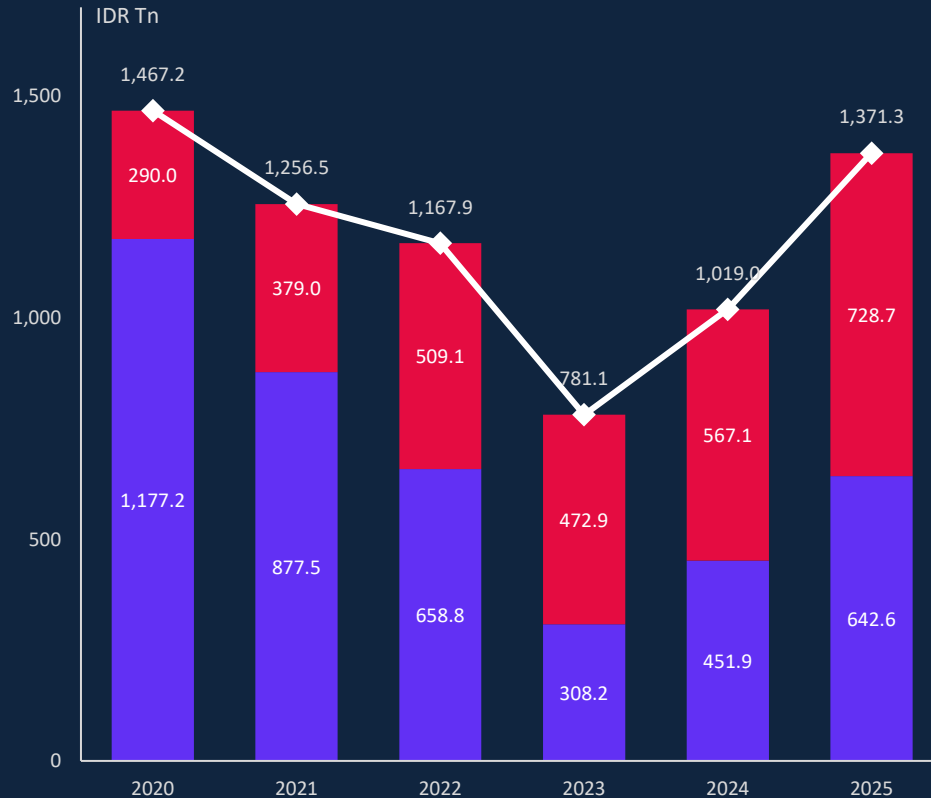
- Gov't deposits, by type:
 - Central gov't at BI
 - Central gov't at commercial banks
 - Regional gov't at commercial banks

Source: BI, calculations by BCA Economic Research

* EOY marks end of year periods, when government spending tends to accelerate, resulting in lower savings

Sheer volume

Maturing bonds and growing budget deficit is likely to push gross issuance of sovereign bonds (SBN) to its highest level since 2020



- Issuance in 2024 would have been significantly higher, were it not for the strategy to take up more multilateral loans—and also to utilize excess funds from previous years

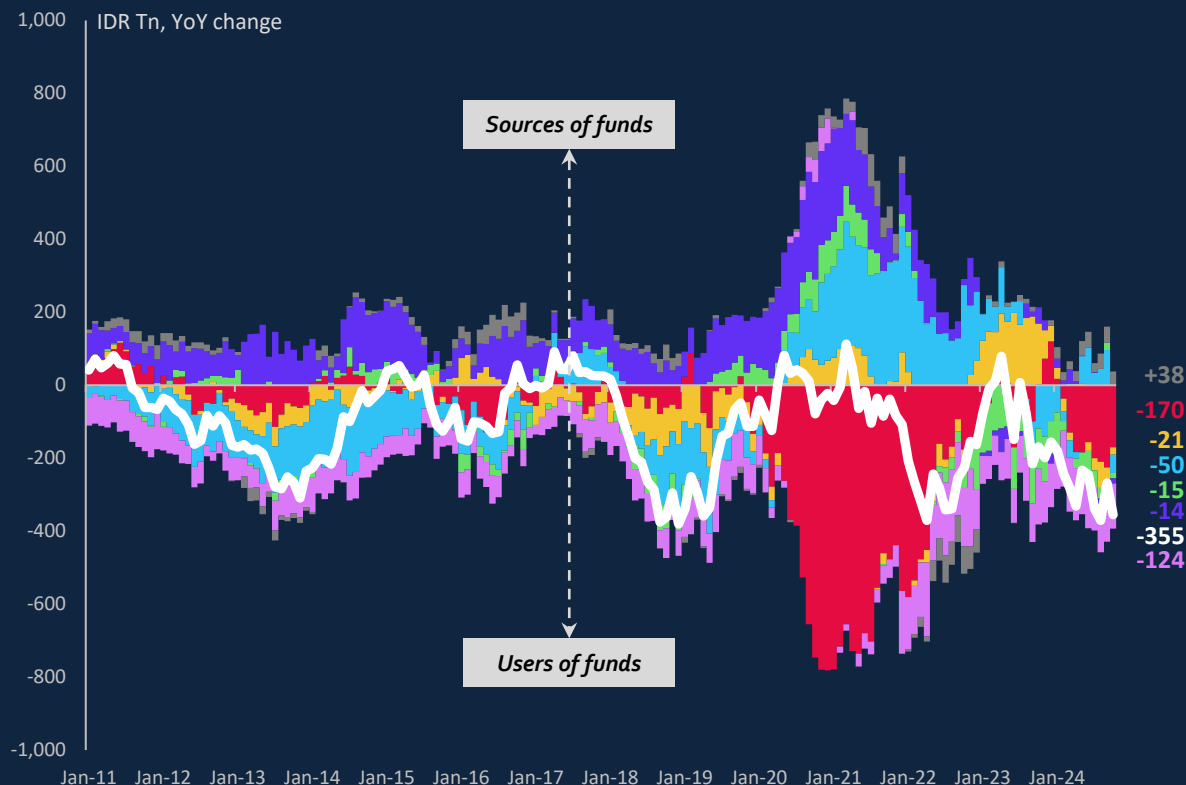
— SBN gross issuance (estimated)

■ Net issuance

■ Refinancing of maturing SBN

The pegs are larger than the pole*

Nearly all sectors of the economy are now net borrowers rather than net savers, making external financing an urgent necessity

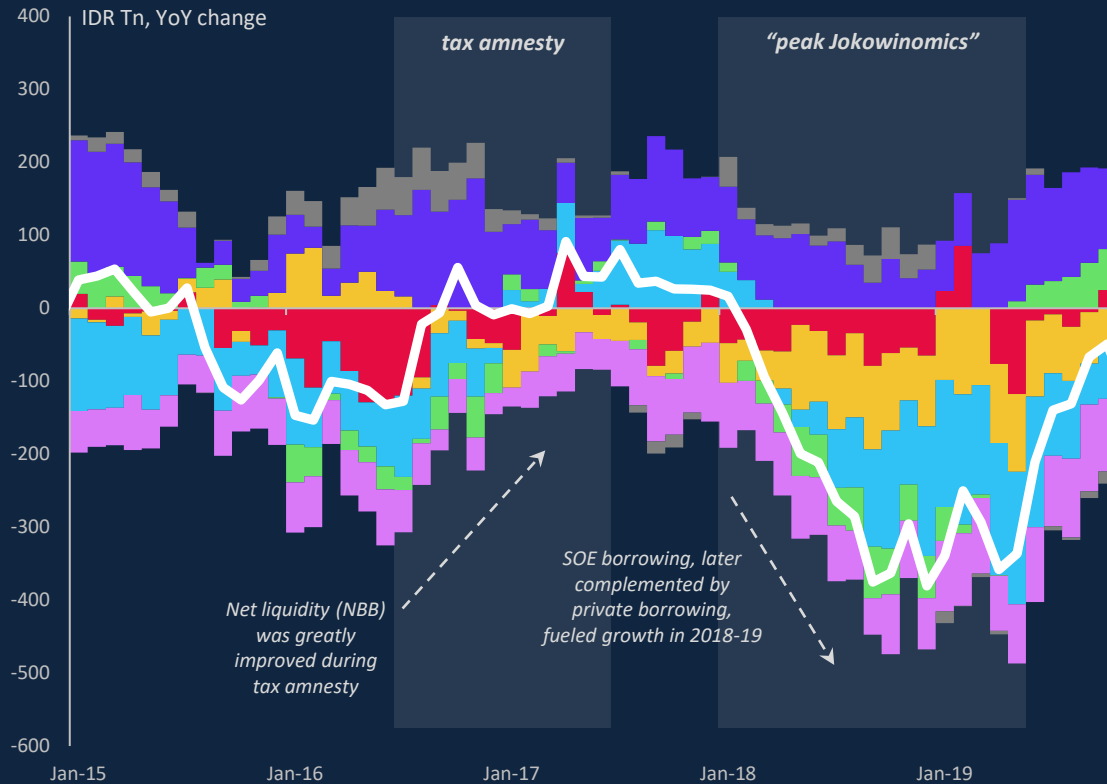


- Indonesia suffers from periodic bouts of financing deficit, but this has become a near-constant since 2022—largely due to the deterioration of **government**, **household**, and **SME** liquidity

- **Net bank balance (NBB), YoY change:**
 - Government**
 - SOEs**
 - Private corporations**
 - NBFIs**
 - Households**
 - SMEs**
 - Others (foundations, etc.)**

Flanking maneuvers

Faced with a lack of fiscal space, the Jokowi admin resorted to tax amnesty and SOE borrowing—a tactic to be repeated by the Prabowo admin?



- The 1st tax amnesty (2017) increased private deposits by about IDR 150 Tn
- Larger SOE borrowing was facilitated by asset revaluations beginning in 2016, plus increased activities by the MoF’s special mission vehicles*

— Net bank balance (NBB), YoY change:

- Government
- SOEs
- Private corporations
- NBFIs
- Households
- SMEs
- Others

Source: BI, OJK, MoF, calculations by BCA Economic Research

* LMAN, PII, SMI, and IIF (providing additional financing, loan guarantees, and helping with land acquisition)

IV

MONETARY POLICY

Painkiller but no panacea

- The net liquidity (NBB) deficit, as described in [Ch. 3](#), has obvious implications on monetary policy, since it connects to the country’s external balance [\[59\]](#). In fact, NBB strongly predicts the USD/IDR movement [\[60\]](#), and the persistent liquidity deficit suggests that the Rupiah was overdue for depreciation.
- The fact that it has not, until quite recently, is attributable to SRBI—the new certificate issued by BI as derivative of its SBN holdings. Its high yields and short durations are attractive to domestic and foreign investors [\[61\]](#) alike, and it effectively made our yield curve a mirror of its inverted US counterpart, without hiking the BI Rate.
- SRBI, then, has been a crucial “band-aid” that covers some of our issues. Without SRBI, for instance, the FX reserves would not be nearing all-time highs [\[62\]](#), while money market spreads—which signal liquidity tightness—could be even more elevated [\[63\]](#).
- But a band-aid could only help so much. For one, a sizable amount of SRBI will mature in mid-2025 [\[64\]](#). Far from attracting inflows, then, BI may be mostly concerned with preventing outflows.
- Additionally, SRBI tends to shift banks’ asset allocation away from loans and even from SBN. Given still-muted foreign appetite for SBN, the onus to absorb them thus falls to private individuals and corporations, along with BI interventions [\[65\]](#).
- Ideally, the US yield curve would bull-steepen as the Fed cut rates, which would induce foreign inflows to SBN and allow BI to unwind SRBI safely, without negative impact on the Rupiah. Instead, the long-end of the US yield curve has risen (bear steepening) due to fears over Pres. Trump’s policies [\[66\]](#).
- This seems to push BI into further intervention, as seen from its recent plan to buy IDR 150 Tn worth of SBN in 2025—ostensibly to offset maturing pandemic-era bonds. This may add further to the cost of BI’s monetary operations, due to the negative carry between SBN and SRBI.

IV

MONETARY POLICY

Bend but not break

- Concerns about the Rupiah also informed BI's decision to keep its policy rate at 6.00%—25 bps hike in April cancelled by 25 bps cut in September. This puts BI in line with the central banks of India, Vietnam, and Malaysia, but behind Thailand and the Philippines which have lowered rates in 2024.
- BI appears to be sensitive to market sentiment surrounding Fed policy [67]. Such cautious tendency, however, is balanced by pro-growth macroprudential policies, which promote lending to SMEs, consumers, and labor-intensive sectors.
- This two-track approach seems to be quite successful thus far, but there are signs of diminishing returns. Credit growth is starting to slow, precisely for SME and consumer loans which enjoy the most incentives.
- This brings us back to the BI Rate, which is actually at record highs *in real terms* [68], thanks to slowing inflation. Historically, higher real BI Rate tends to improve the NBB—via less borrowing and/or more savings—and thereby support the IDR.
- But two things complicate the current situation. Firstly, as we saw in [Ch. 2](#), household and SME incomes are declining. This means that they are actually using up their savings [69], and the only way to improve their NBB is through lower borrowing [70].
- Meanwhile, government dissaving as well as corporate borrowing—much of it from capital-intensive industries—continue apace, preventing improvement in overall NBB. High real rates, as such, have done little to allay the pressure on the Rupiah.
- One potential way out of this impasse is to accept that some NBB deficit—and thus some degree of *controlled* depreciation—is an unavoidable price to pay for greater fiscal spending and corporate CAPEX.
- This more flexible approach (“*bend*”) is preferable to the alternative, where BI makes a valiant attempt to defend the Rupiah at a high psychological level, only to be overtaken by external events which cause a more drastic depreciation (“*break*”). And the year ahead may have a few of such breaking points ...

IV

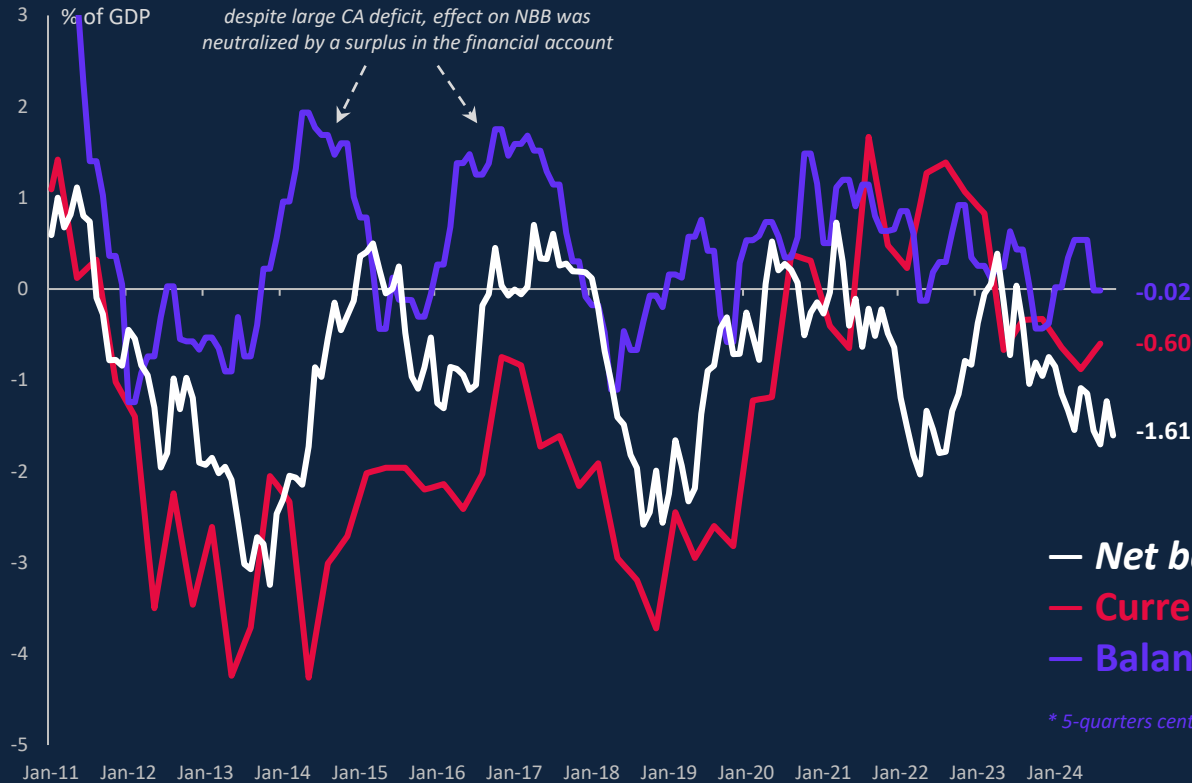
MONETARY POLICY

Bend but not break (cont'd)

- The most obvious point, perhaps, is Pres. Trump's tariffs on China. Past experience (2018) suggests that this would be accompanied by a depreciation of the Yuan, with significant contagion on other Asian currencies.
- Indonesia may be particularly vulnerable here, as the Rupiah has become overvalued against the Yuan [71]. Moreover, Indonesian imports from China—far more so than exports—are increasingly being paid in CNY, resulting in a widening Yuan shortage [72].
- An aggressive defense of the Rupiah, then, might be quite costly and potentially counterproductive. Strong IDR vs. CNY would drive imports further—heaping more pressure on final goods industries as we saw in *Ch. 1*. Neither will it help narrow our Yuan shortage, which will have to be addressed through Chinese FDI.
- Furthermore, we might be entering (however briefly) a period of strong USD but weak commodity prices [73], which is not exactly ideal for Indonesia's growth model. This runs counter to what is until recently the prevailing wisdom—that the Fed will soon cut rates and that commodities still have plenty of runway.
- Our *Projections*, then, reflects our belief that a more flexible and pragmatic approach will eventually prevail. This implies moderate adjustments in the exchange and interest rates, and a fiscal strategy that strikes relative balance with private spending.
- We acknowledge, however, that downside risks are substantial, especially on the metal sector which has been *the* big bet in the last few years. Some deterioration of the current account, then, may be necessary to keep GDP growth at relatively robust levels.

Cash is king

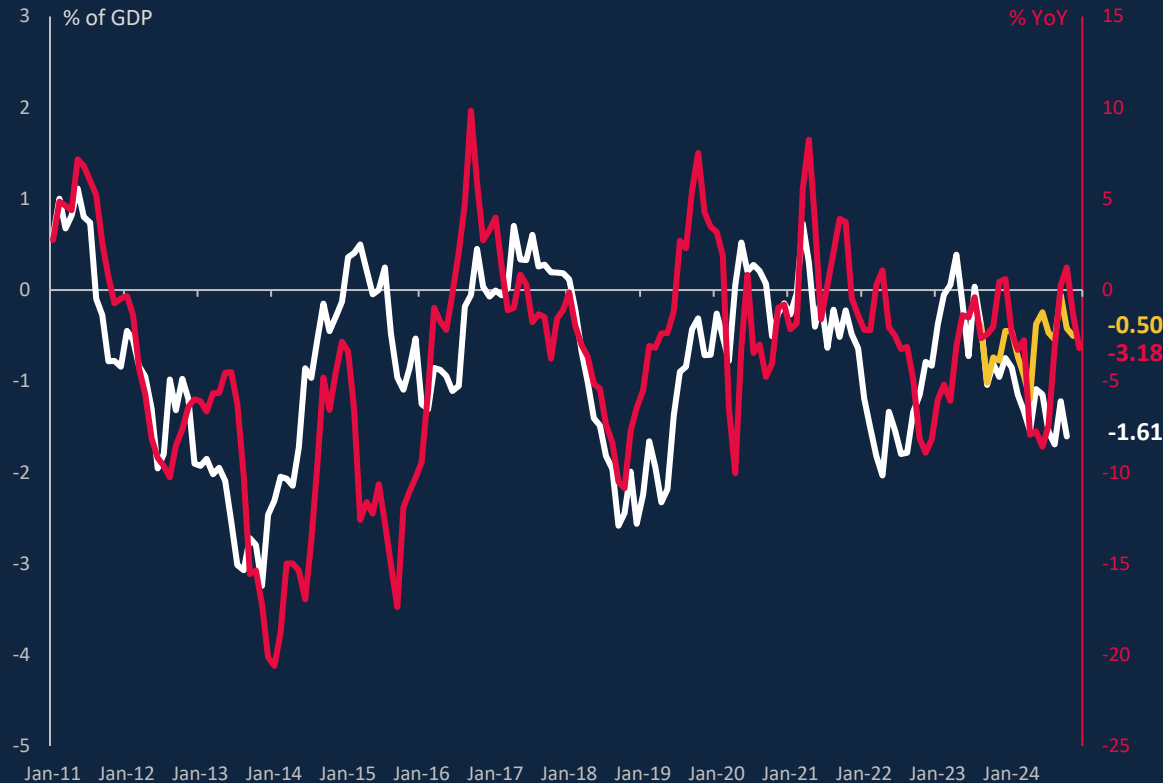
Despite a narrower CA deficit, the relative decline in financial inflows has put domestic liquidity under a sustained pressure



- NBB is a partial measure of the savings-investment (S-I) gap— one that specifically measures cash (i.e. bank deposits) rather than less liquid assets
- Accordingly, NBB is a “bridge” between bank liquidity metrics (e.g. LDR) and traditional measures of external balance (CA and BoP)

Under pressure

Persistent NBB deficit predicts Rupiah depreciation against the USD—albeit partially remedied by SRBI issuance

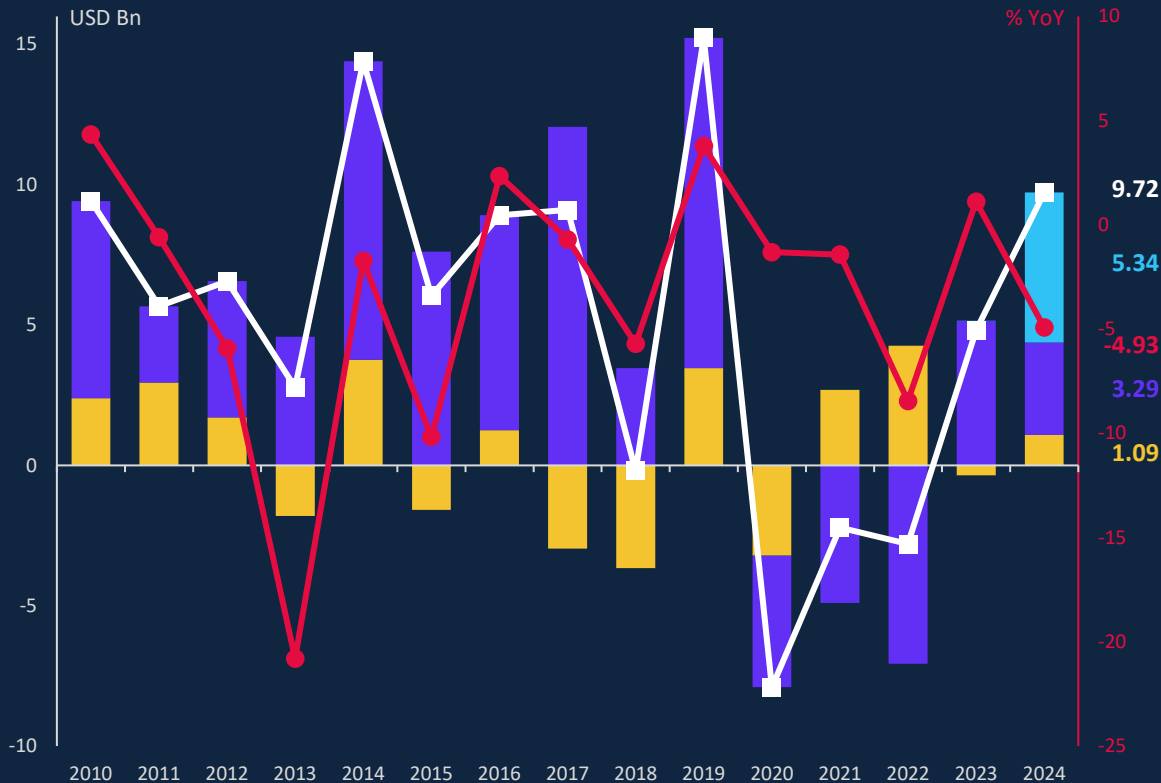


- NBB is a better predictor* of the exchange rate, as compared to either CA balance or BoP
- Without foreign SRBI purchase, we reckon that the Rupiah would have fallen by 6-8% YoY to the USD, instead of just 3%

- ◀ Net bank balance (NBB), YoY change
- ◀ NBB plus foreign-owned SRBI
- ▶ IDR/USD

Shiny new tool

SRBI managed to attract substantial inflows to Indonesia, despite still-lukewarm appetite for bonds and equities



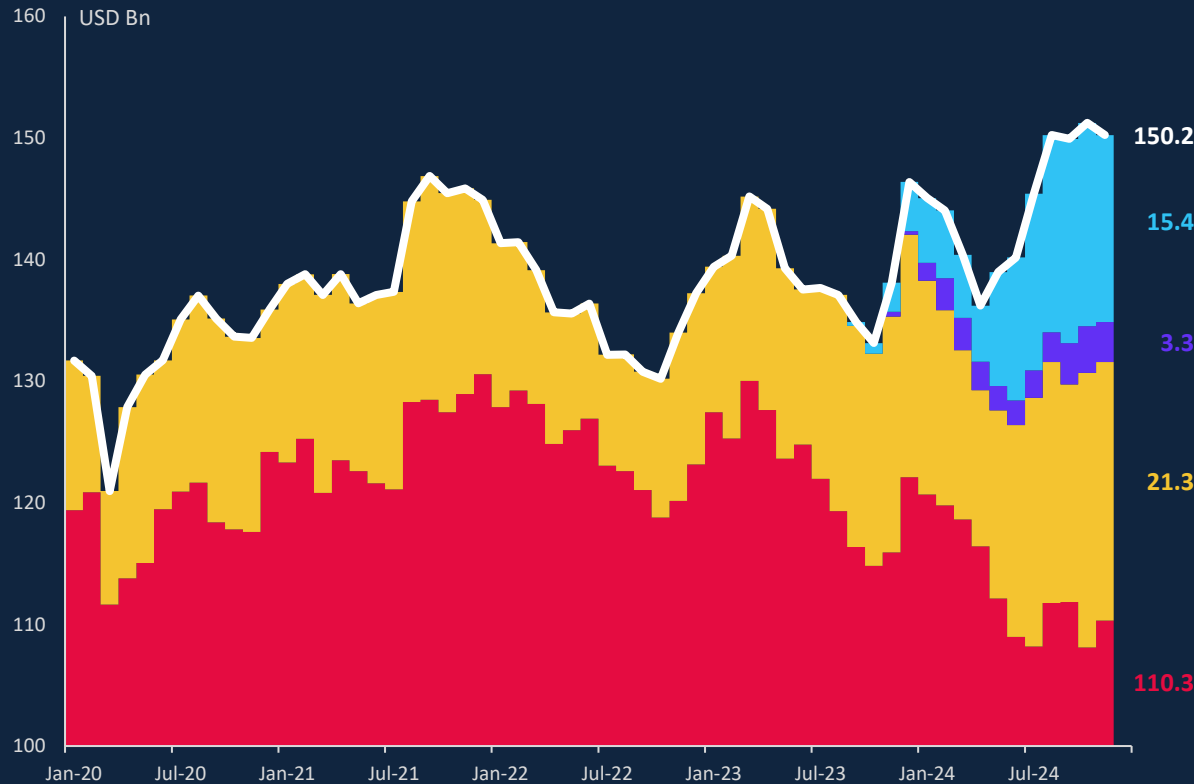
- **SRBI** was first issued in Sep-23, but issuance ramped up in 2024 as the Rupiah came under pressure
- Before 2020, the **USD/IDR** moved in line with financial flows ...
- ... but since then, it seems to deviate—an indication that the current account and domestic liquidity (i.e. S-I gap) are the more limiting factor for the Rupiah

◀ Net foreign purchase, by asset:
■ Equities ■ SBN ■ SRBI
➤ IDR/USD

Source: Bloomberg, BI, calculations by BCA Economic Research

Buffer and fitter?

BI's FX reserves are near all-time highs, largely thanks to new instruments (SRBI and SVBI/SUVBI)



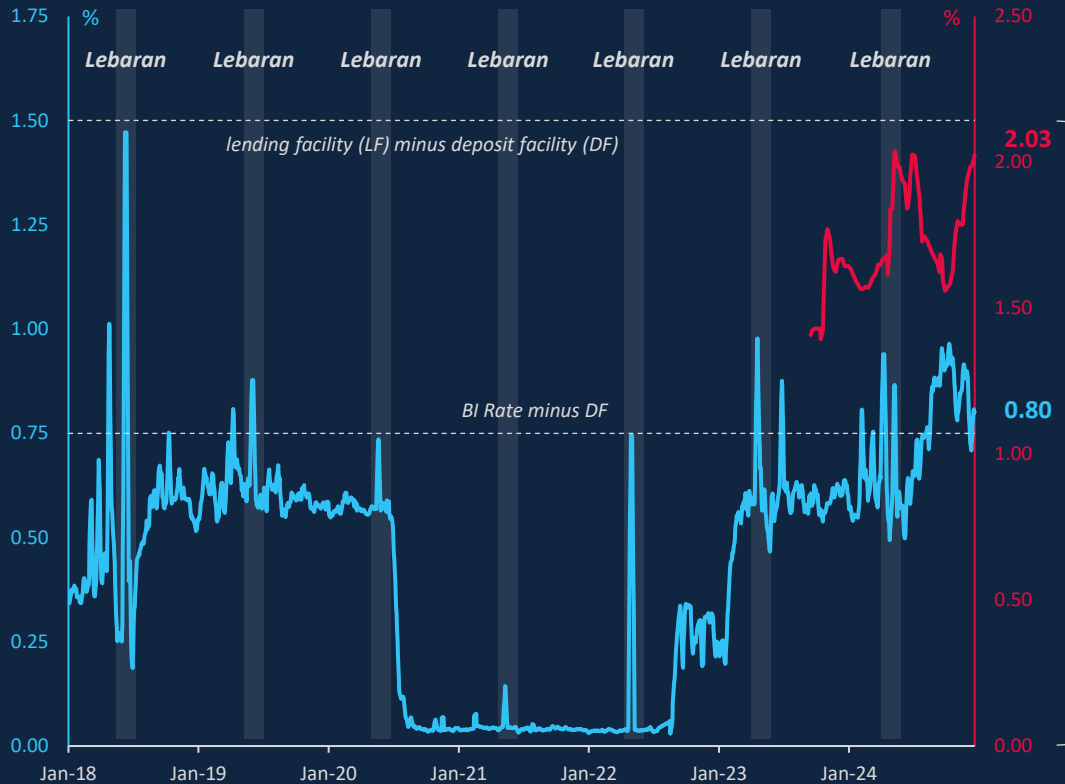
- **FX placements at BI** consists of swaps, certificate (SBBI), term deposits, and special deposits for FX receipts (TD-DHE)
- **SRBI, SVBI/SUVBI, and FX placements** are all BI liabilities —ergo, their issuance is limited only by BI's willingness to bear their costs

— BI's FX reserves, by drivers:

- SRBI (foreign-owned)
- SVBI/SUVBI
- Banks' FX placements at BI
- Net reserves

Relief valve

Money market tightness persists throughout 2024, but higher SRBI yields—and the ensuing foreign inflows—provide periodic relief



- **Indonesia (O/N money market rate) is usually 50-65 bps above the “floor” of the monetary corridor ...**
- **... but there is seasonal widening of the spread during Lebaran holidays, when demand for cash peaks**
- **Larger Indonesia spreads recently (similar to 2018) signals tighter liquidity, which is partially relieved by foreign inflows into SRBI**

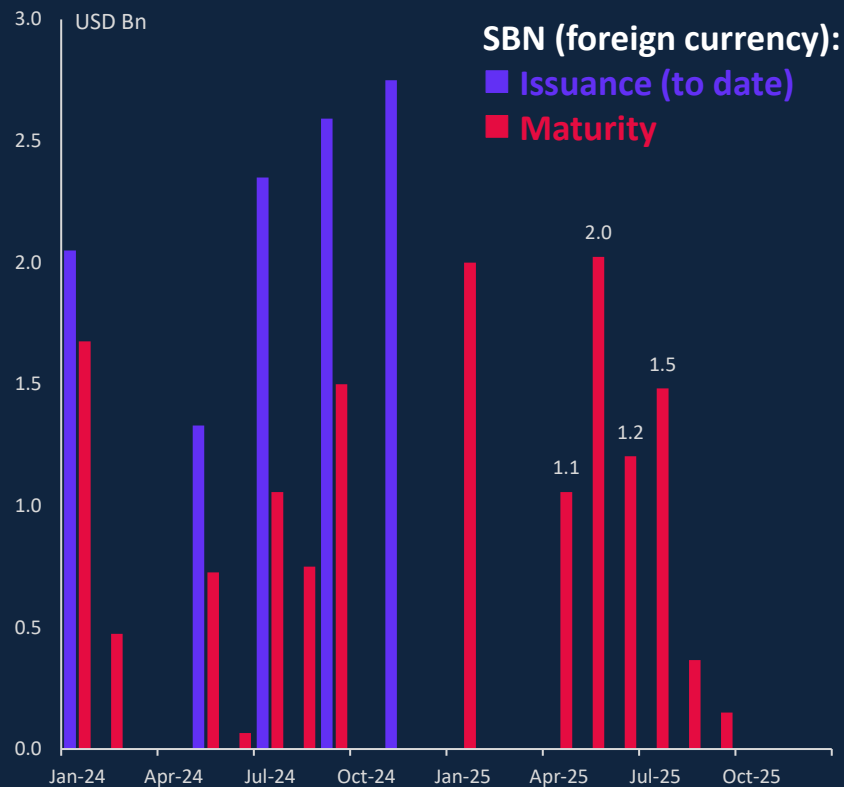
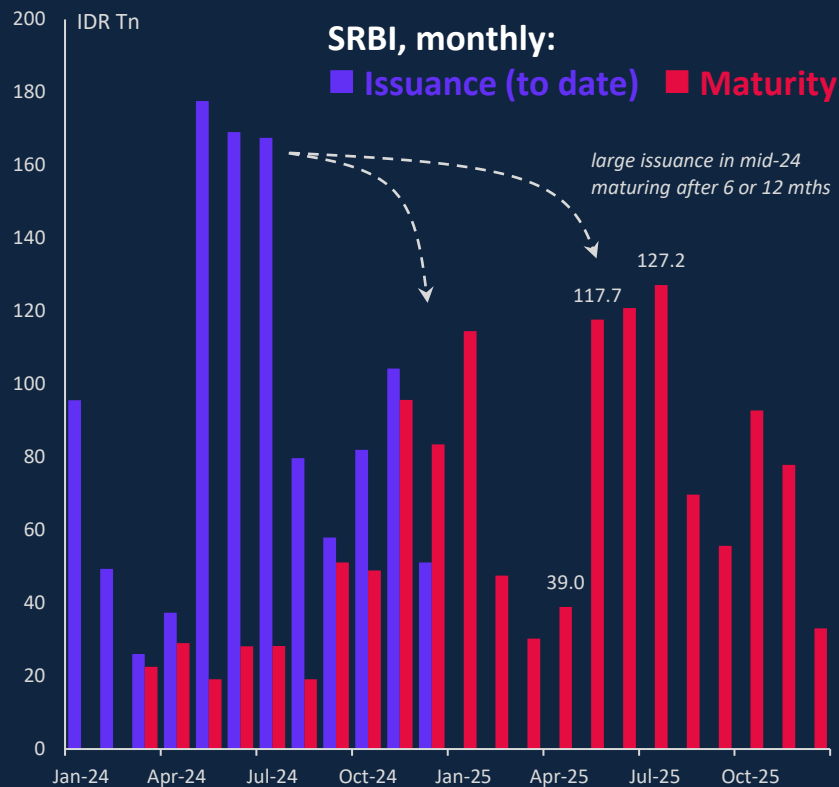
◀ **Spread, Indonesia minus DF***

▶ **Spread, SRBI 1Y minus DF***

* figures are 1-week average

Summertime blues?

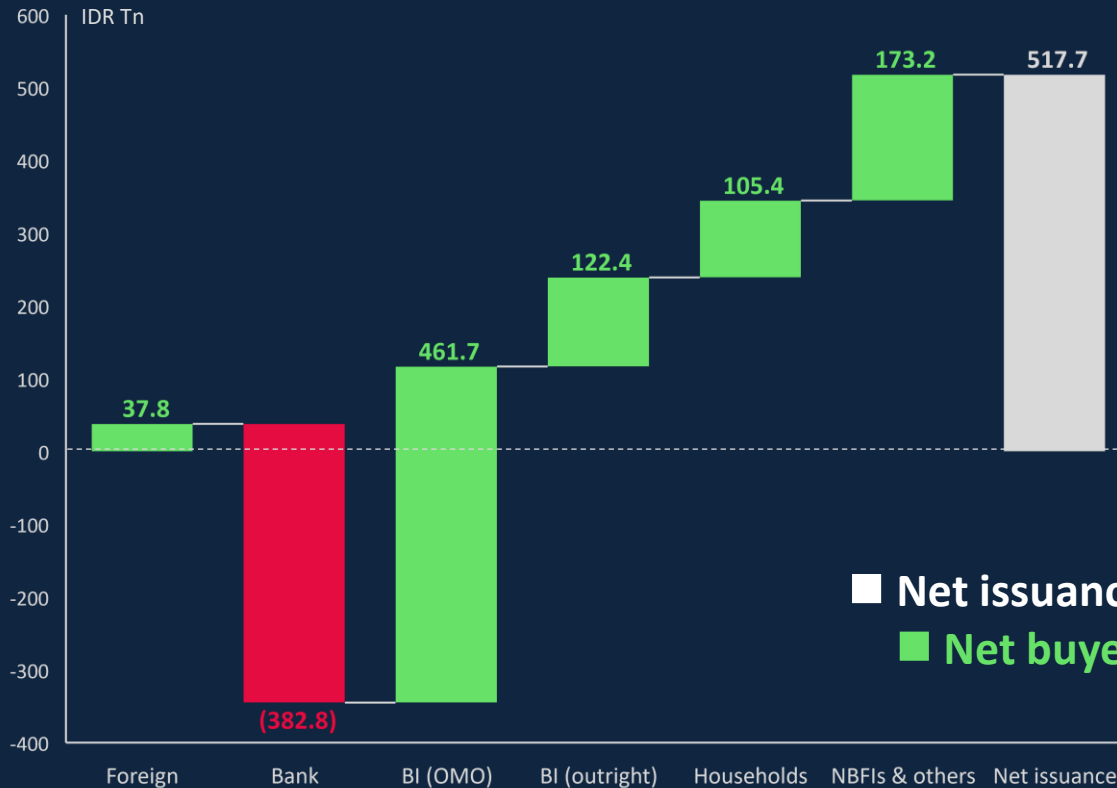
A wave of SRBI and FX bond maturity in mid-2025 calls for deft navigation by the monetary and fiscal authorities



Source: BI, MoF, calculations by BCA Economic Research

Stepping up to the plate

Amid limited inflows and a shift in banks' asset allocation, SBN has mainly been absorbed by BI, households, and NBFIs

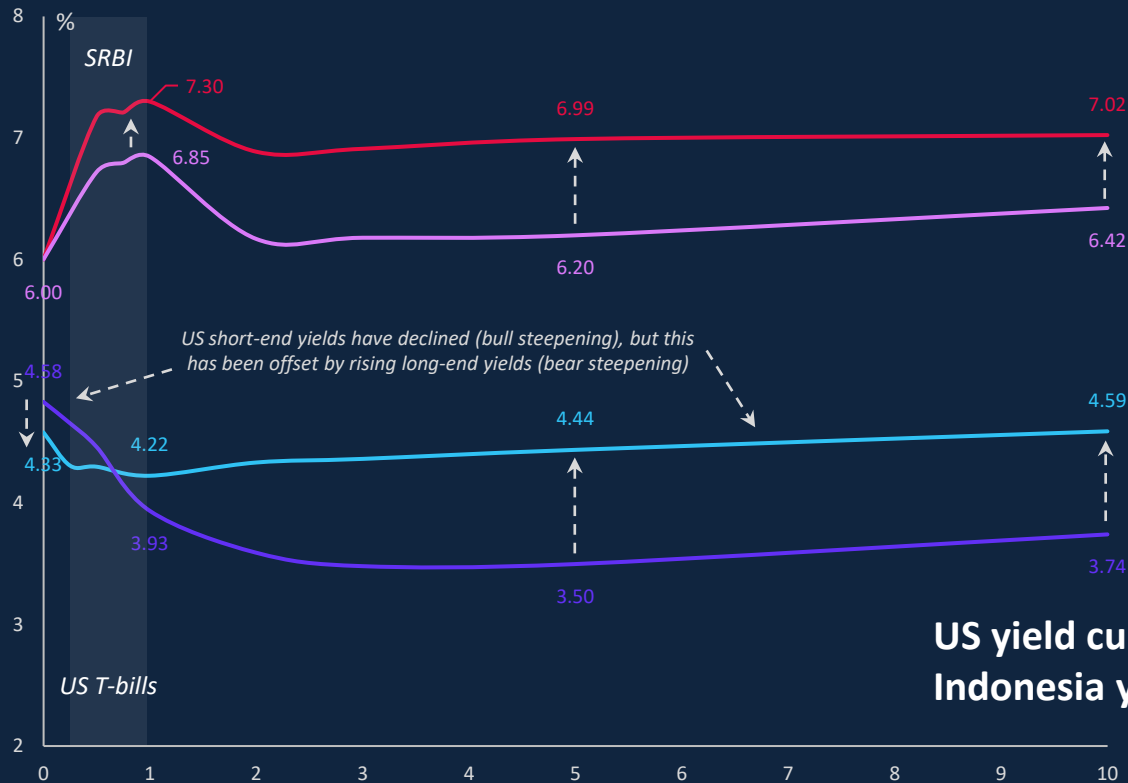


- **Net SBN selloff** by banks has been driven by strong loan growth as well as a shift to SRBI
- Outright purchase increases BI's gross ownership of SBN, whereas purchase in open market operations (OMO) merely adds to its net ownership

■ Net issuance of tradable SBN, YTD 2024:
 ■ Net buyers ■ Net sellers

Slippery slope

The use of SRBI was necessitated by the US' inverted yield curve, but bear steepening complicates BI's exit strategy



- SRBI effectively “inverted” our yield curve to mirror the US
- Given the potential re-steepening of the US yield curve under Trump—plus rising SBN issuance—the likely outcome is higher SBN yields and therefore steeper Indonesian curve
- Alternatively: Indonesian gov’t shifts issuance to the short-end (SPN)—but SPN market lacks sufficient liquidity

US yield curve: — Sep 20 — Dec 24
 Indonesia yield curve: — Sep 20 — Dec 24

Go with the flow

BI's press statements appear to take a partial cue from the market's perception of the Fed's future policy



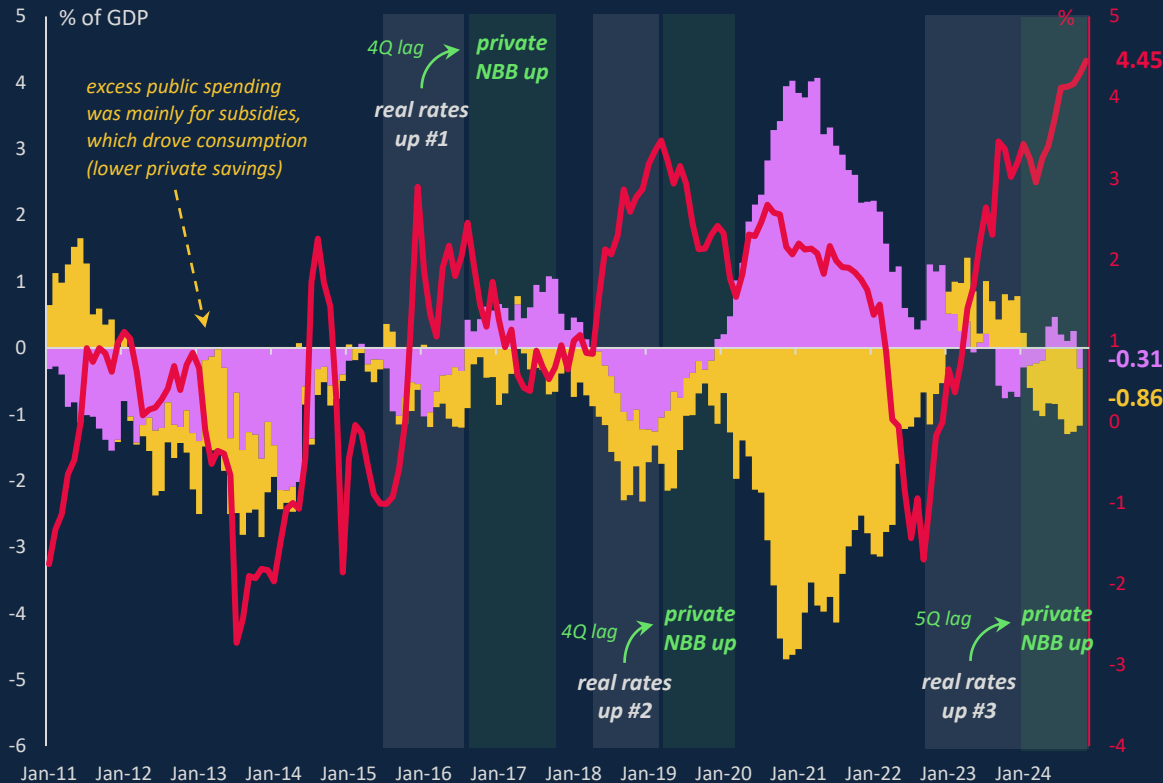
- BI's communiqués generally eschews explicit forward guidance regarding its own policies—which makes its references to external events, especially Fed policies, very valuable in gauging its thinking

◀ Fed funds rate futures, for Dec-25

▶ Keyword ratio, mention of “stability” vs. “growth” in BI’s policy meeting press release

Forced savings

As fiscal policy becomes more expansionary, BI resorts to high real rates to stabilize private liquidity and avoid Rupiah depreciation



- An increase in **real policy rate** induces the **private sector** to conserve liquidity, but only after a long lag (4-5 quarters)
- Given close correlation between NBB and IDR/USD, an **expansive fiscal policy** has to be balanced by more conservative monetary policy—unless BI is willing to tolerate some depreciation

- **Real BI policy rate (minus CPI inflation)**
- ◀ **Net bank balance (NBB), YoY change:**
 - **Private sector***
 - **Public sector#**

Source: BI, OJK, MoF, calculations by BCA Economic Research

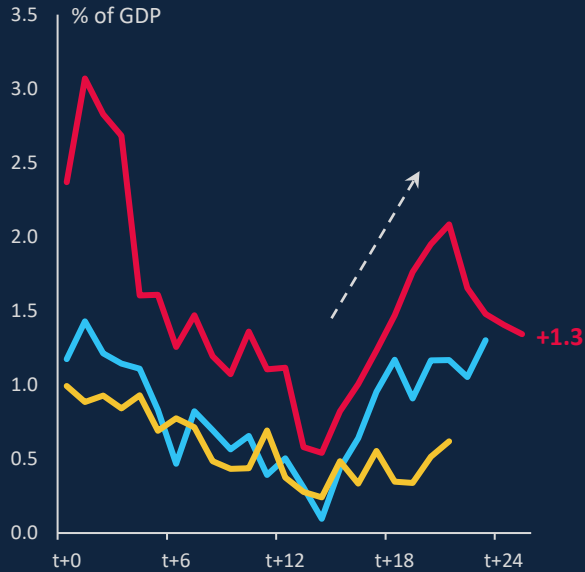
* private corporations, SMEs, and households

general government and SOEs

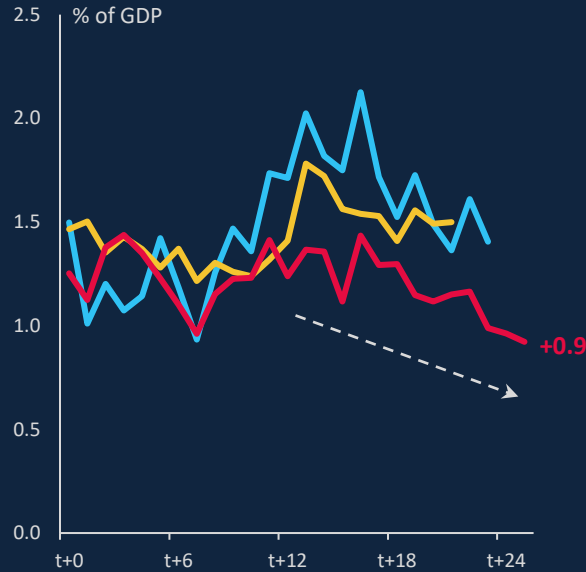
Impulse and response... or lack thereof

BI's latest rate hike cycle has bolstered corporate savings, but declining savings by households and especially SMEs remain an intractable problem

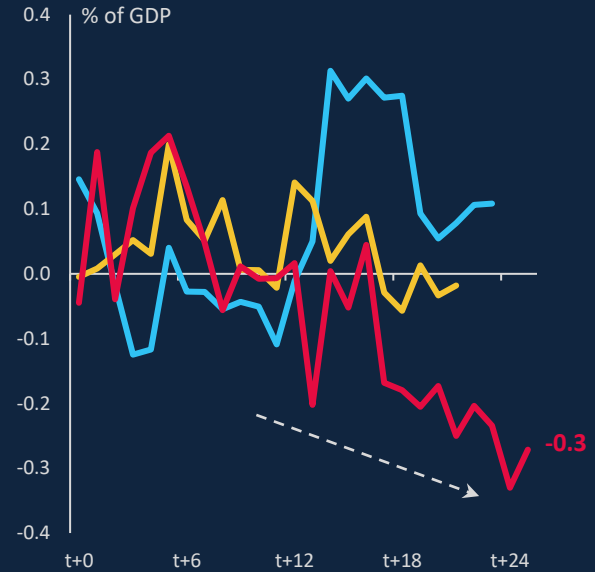
**Private corporations,
YoY change in deposits**



**Households,
YoY change in deposits***



**SMEs,
YoY change in deposits**

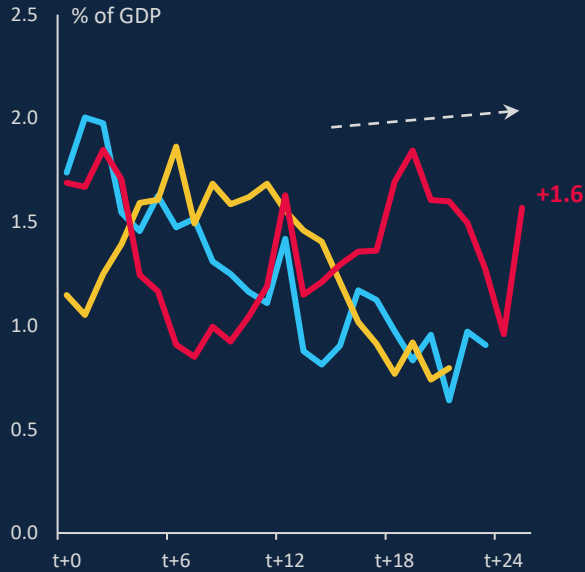


Periods of rising BI real policy rate: — Starting Jul-15 — Starting Apr-18 — Starting Sep-22

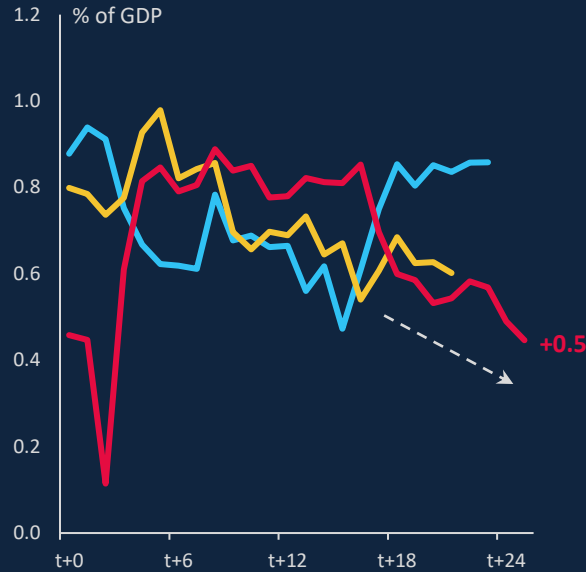
Diverging appetite

High real rates dampens household and SME loans, but corporate borrowing remains robust—a sign of strength among capital-intensive industries

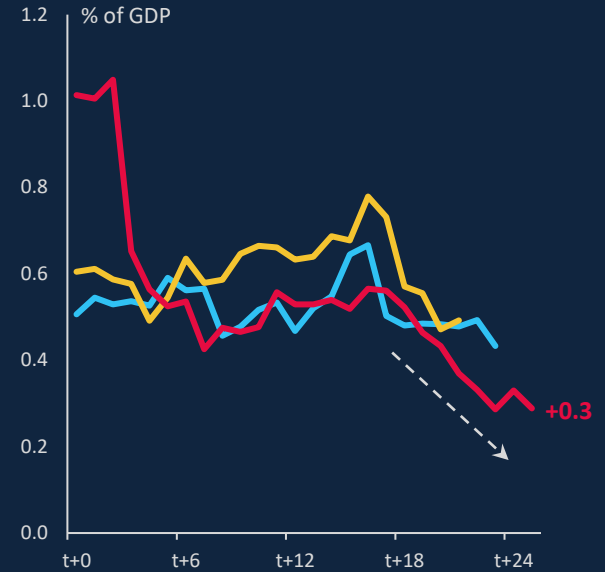
**Private corporations,
YoY change in loans & bonds**



**Households,
YoY change in loans**



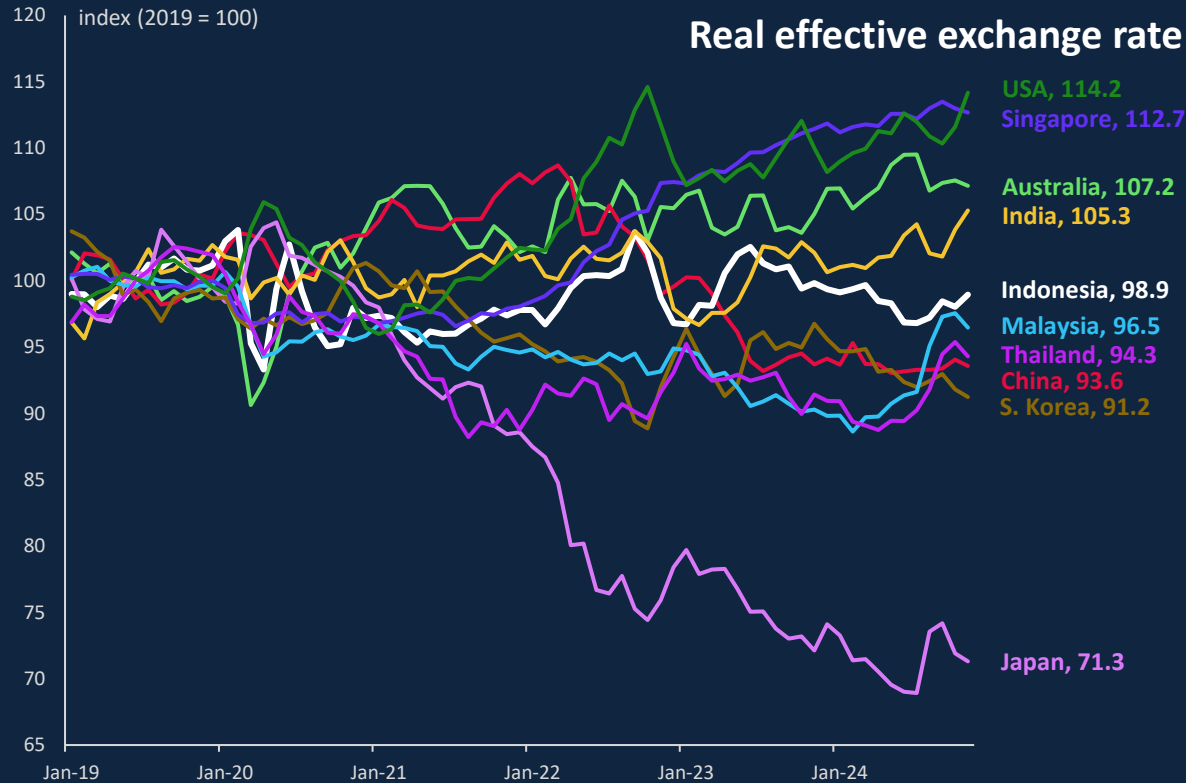
**SMEs,
YoY change in loans**



Periods of rising BI real policy rate: — Starting Jul-15 — Starting Apr-18 — Starting Sep-22

Deceptively strong

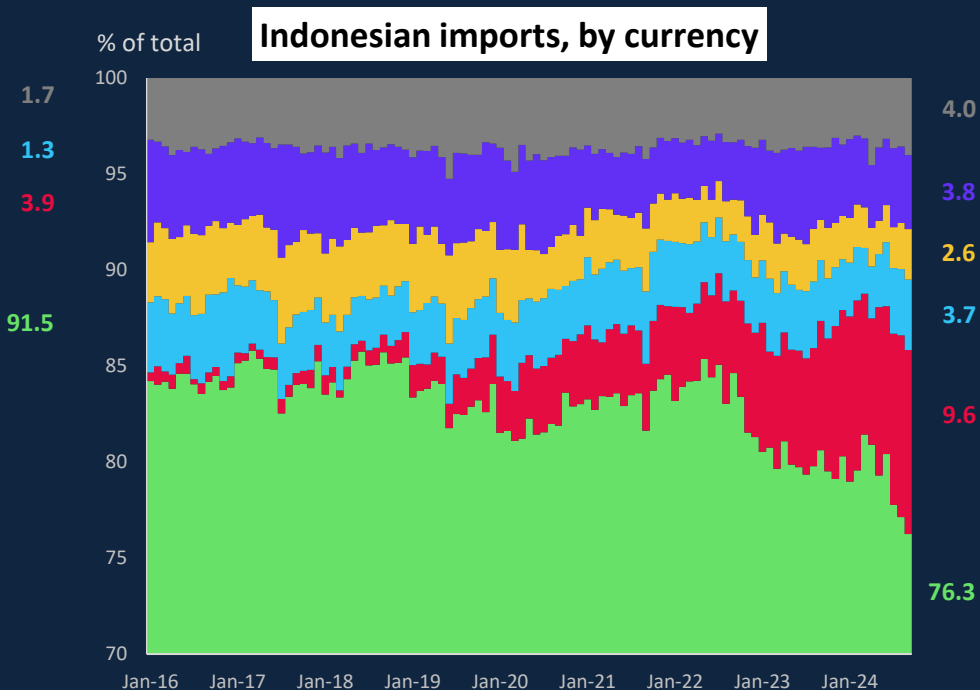
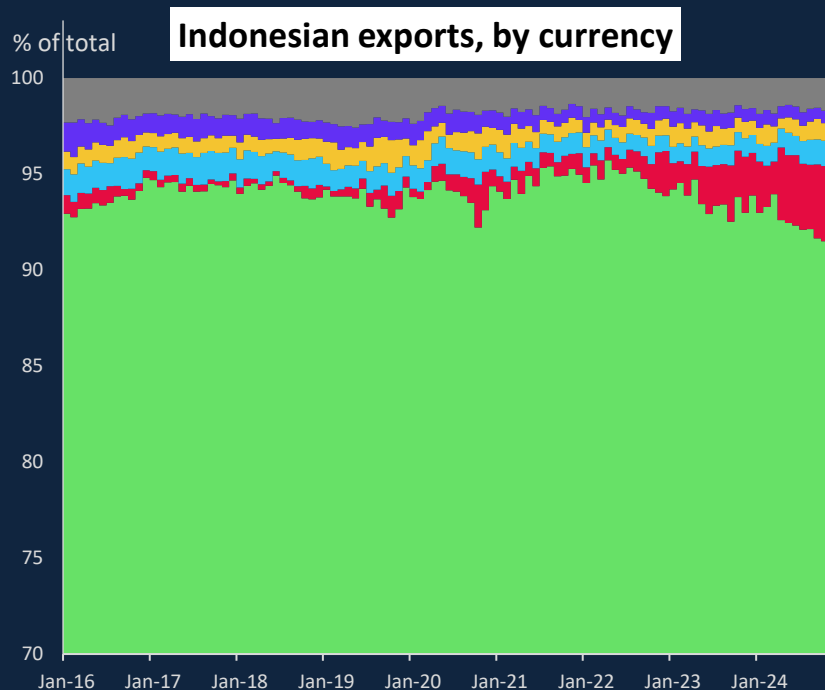
The Rupiah has lost ground against a raging USD, but it remains overvalued compared to most of its Asian peers



- The Rupiah’s REER has been kept at a relatively tight range— a sign of implicit targeting?
- Rupiah’s relative strength vs. Asian currencies, especially the Yuan, may potentially worsen Indonesian trade balance as Trump’s tariffs ratchet up

A yuan-sided match

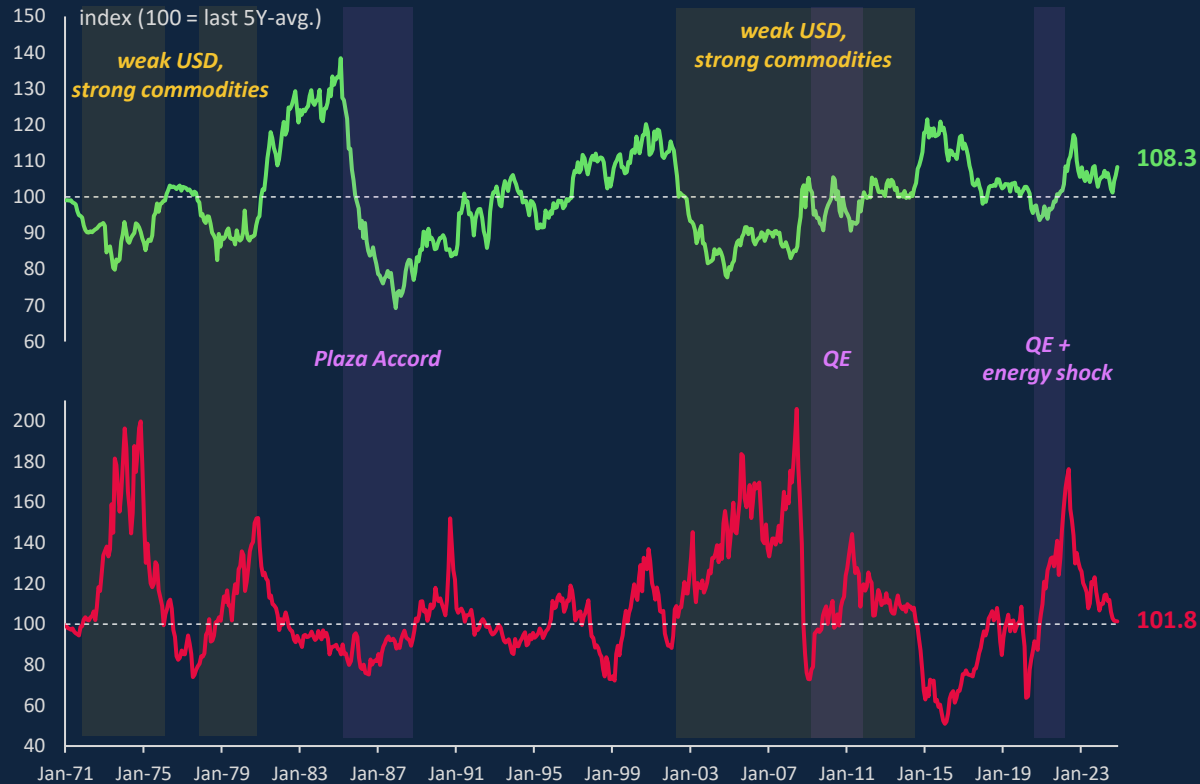
De-Dollarization has mostly been driven by imports of Chinese goods, causing a CNY shortage equivalent to nearly USD 1 Billion each month



Transaction denominated in: ■ USD ■ CNY ■ IDR ■ JPY ■ EUR ■ Others

Waiting for the wheels to turn

Despite favorable commodity prices, strong USD has prevented Indonesia from reliving the “golden years” of the 1970s and 2003-13



- The Indonesian economy is at its best when **commodities** are strong and the **US Dollar** is weak
- Commodities have been strong since 2021, but the Fed has been fighting its inflationary effect by raising rates ...
- ... ergo, we are betting for the Fed to give up the fight, perhaps due to fiscal dominance?

— Dollar index
 — S&P commodity price index (GSCI)

Recap and precap: The liquidity straitjacket

- Our discussion in [Ch. 4](#)—particularly charts [\[60\]](#) and [\[68\]](#)—clearly shows a tradeoff between government spending, private sector spending (including households), and a stable Rupiah.
- At the crux of this *trilemma* is the issue of liquidity and financing [\[76\]](#). The government can use private savings to finance its deficit, and vice versa. But when both the government *and* private sector have more financing needs than they have savings, they become reliant on foreign liquidity, at the cost of possible depreciation.
- This has been a recurring issue for Indonesia, typically resolved by a combination of monetary and fiscal adjustments, and *yes*, some weakening of the Rupiah.
- Indeed, had we relied only on domestic liquidity in order to avoid IDR depreciation, we estimate that GDP growth would have been (on average) 0.7-1.0% slower over the past ten years [\[77\]](#).
- What pulls the liquidity straitjacket tauter recently is a confluence of several factors. One is the shift from labor-intensive to capital-intensive industries, which depresses household savings while at the same time enlarging corporate financing needs.
- Government spending is also becoming more expansive, with the fiscal push in 2024 followed by the new programs of the Prabowo government. This has absorbed much of the excess savings among wealthier households and corporates, via SBN.
- All these are happening amid a backdrop of higher global interest rates which reduces global inflows, plus weak commodity prices—at least compared to 2021-23—which further crimp private sector savings.
- The attempt to hold the line on the exchange rate, long-end SBN yields, and loan growth only adds to the tension, and—unless the global situation markedly improves—some adjustments may soon become necessary.



Escaping the straitjacket

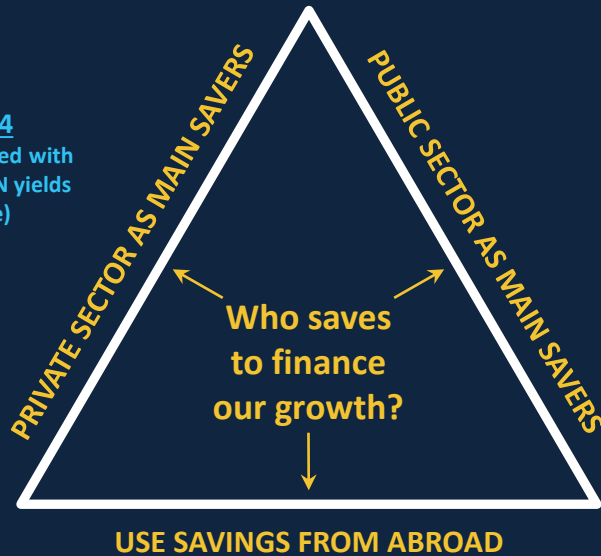
- Our caution for the short-term, however, *does not* equal pessimism for the long-term. Aside from commodity booms—which are beyond our control—the strict logic of the liquidity straitjacket could be relaxed through FDI, and by *refocusing* domestic investment towards efficient, export-oriented projects.
- In both areas, Indonesia has plenty of room to improve. FDI starts, for one, have increased rapidly in recent years, but inflows related to FDI have not [78]. This shows the need for better monitoring, to ensure that initial commitments do turn into actual investment.
- Investment efficiency is another crucial issue, as the incremental capital-output ratio (ICOR) had been trending up from about 2012 until the commodity boom in 2021-23 [79].
- At current ICOR, Indonesia would need China-level investment—and thus China-level saving rates—in order to grow at 7-8% [80]. This actually aligns with the Prabowo government’s wish for additional financing [43], but such rapid rise in savings likely requires a different political-economy setup than what we currently have.
- The inefficiency, we should add, is apparent not just for government projects as some might think, but for also for the broader economy. Case in point—sectoral ICOR, which has been rising for all but a handful of sectors [81].
- Indeed, there is a perverse logic to Indonesia’s investment cycle [82], where it is higher revenue—usually from commodity windfall—that drives CAPEX, but CAPEX itself does not seem to correlate with future revenue growth.
- A related issue is that investment tends not to generate exports—perhaps with the sole, but recent exception of the metal sector [83]. As such, we become overly dependent on commodity booms to generate that extra savings to fuel our next CAPEX cycle.
- Finally, while downstreaming (nickel, cocoa) has been that rare success story where investment bolsters exports, *it has not gone downstream enough* to the final goods stage. The case of cocoa, which remains stuck at the intermediate stage [84] after nearly 15 years, should serve as a lesson for future planners.

How to finance growth? A simple trilemma

If fiscal expansion is a *sine qua non*, policymakers would have to navigate between the risk of depreciation and weaker “animal spirit”

Strong & stable Rupiah

Example: 2023-24
high fiscal spending, coupled with high real rates but low SBN yields (inverted yield curve)



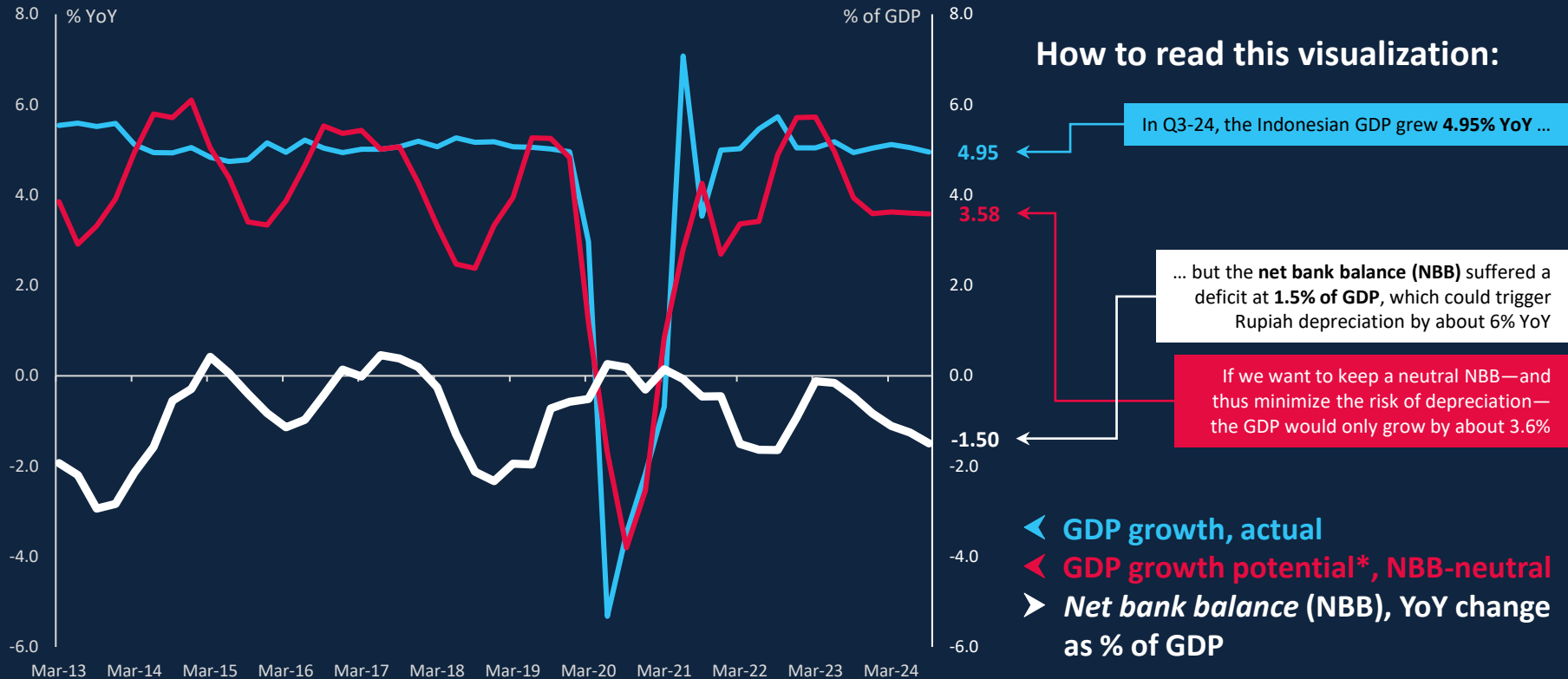
Example: 2012-13
consumption-oriented fiscal spending, e.g. energy subsidies

How to shake loose from this trilemma?

- 1 Commodity boom (luck-based)
- 2 Attracting more FDI
- 3 Focus on investments that generate exports (i.e. generate its own savings)

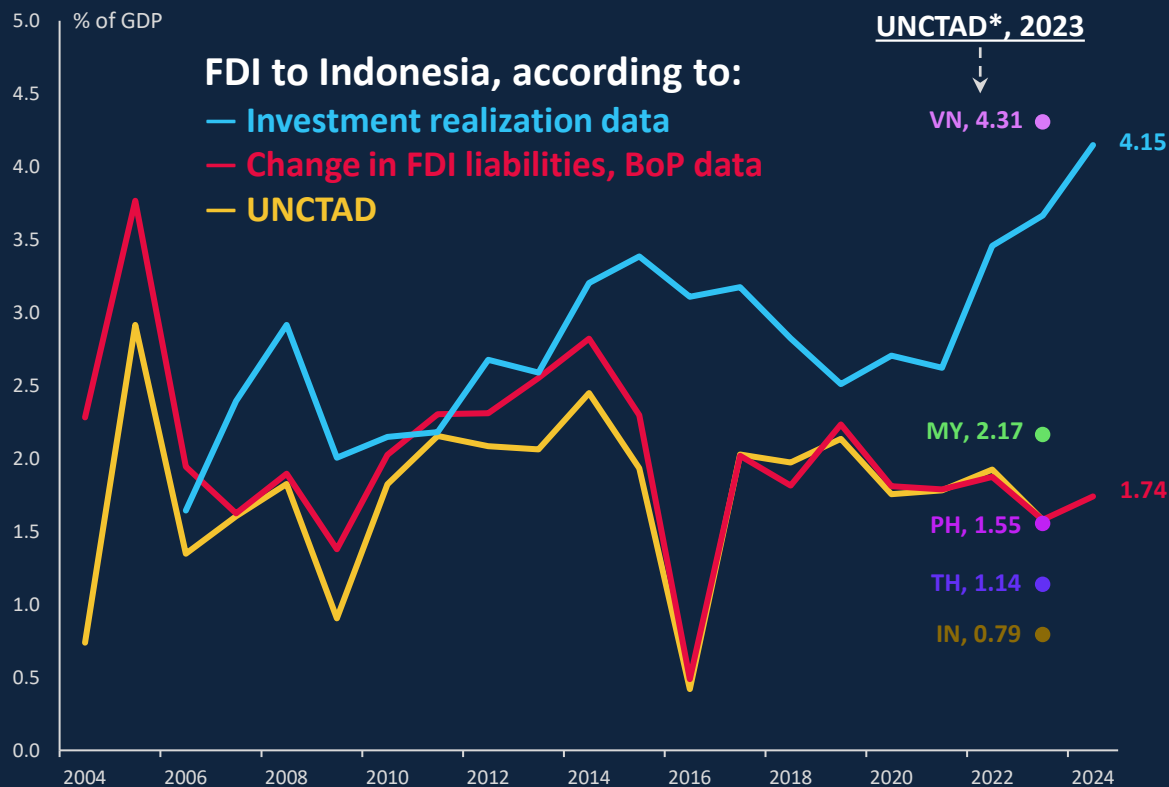
Growth vs. exchange rate: The ultimate tradeoff

Indonesia's growth potential may best be seen in terms of financing constraint—and therefore the risk of Rupiah depreciation



FDI: The beginning is not the end?

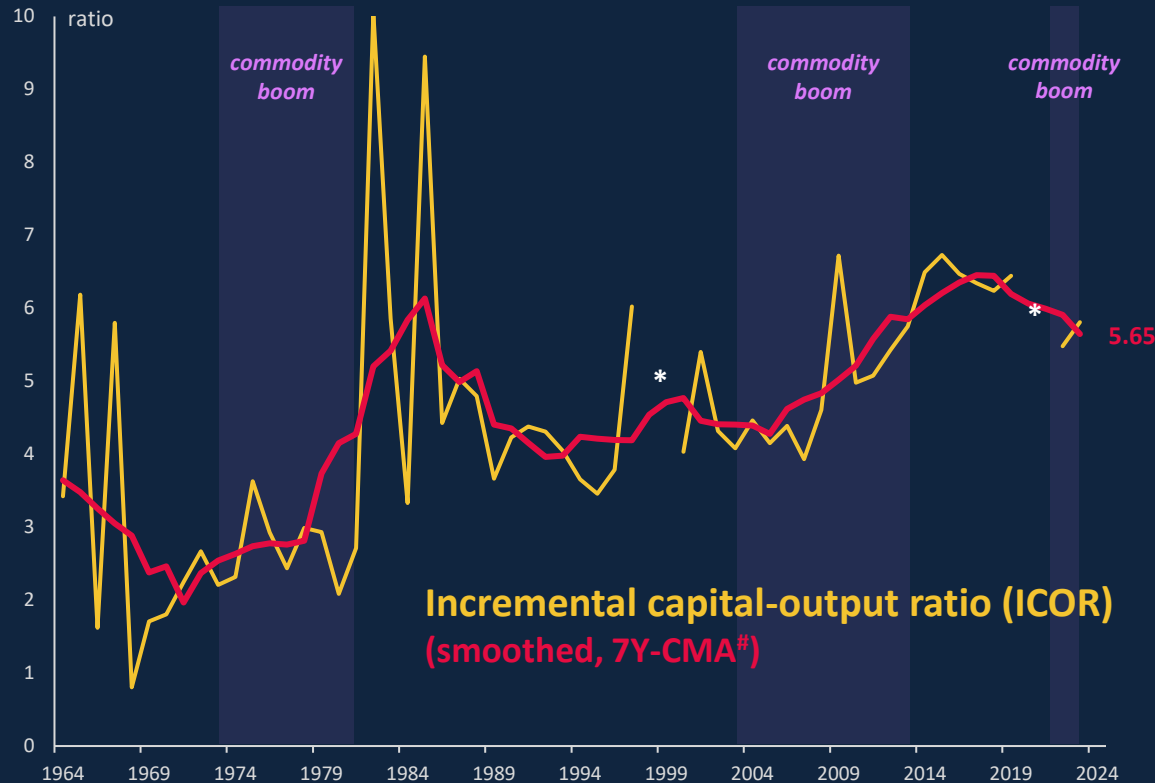
Initiation of FDI projects in Indonesia seem to approach Vietnam levels—but actual inflows are considerably smaller



- Despite its name, “investment realization” refers to the start/groundbreaking of projects, as opposed to its completion
- The gap between realization and BoP data may thus reflect project postponements ...
- ... or alternatively investors procuring fixed assets directly from abroad, with little need of liquidity injection to Indonesia

National ICOR: Still commodity-bound, after all?

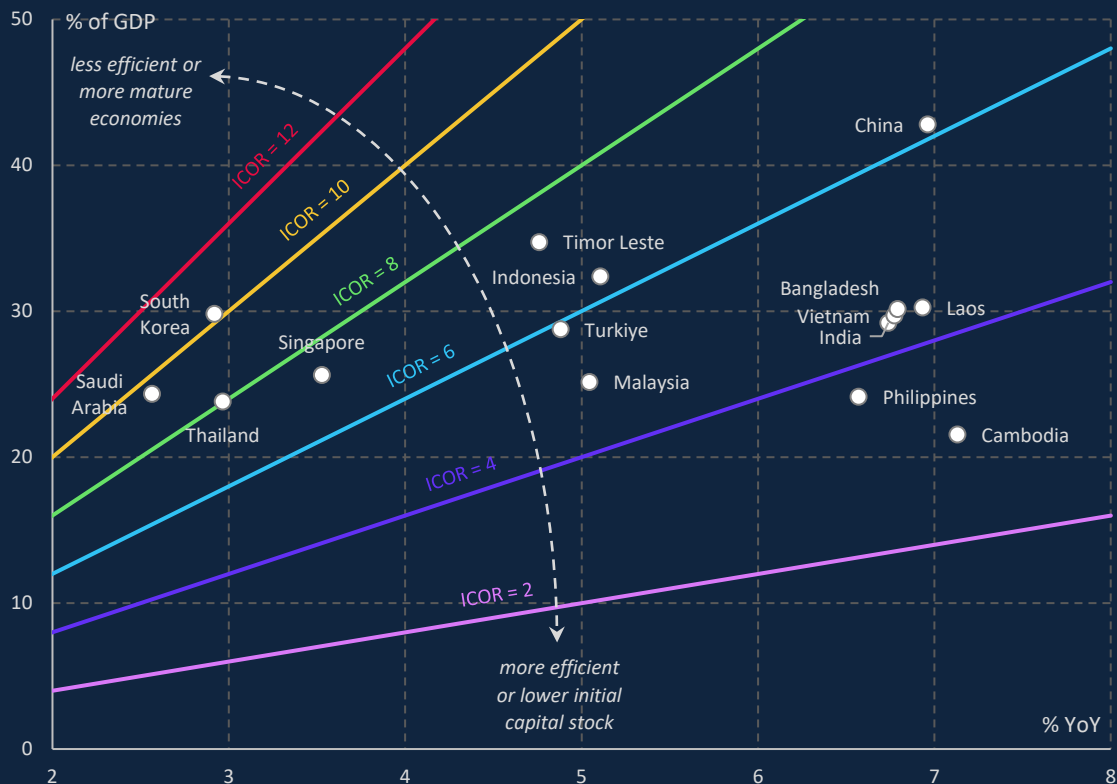
Investment has become much less efficient, and post-pandemic improvement is likely connected to downstreaming and commodity boom



- ICOR is the ratio of investment to growth—higher ICOR, therefore, implies lower efficiency
- Indonesian ICOR tends to increase sharply at the end of commodity booms—a sign that these booms might have encouraged inefficient spending
- The period of FDI-driven industrialization between 1988 and 1996 was among the rare times when ICOR stayed low without a commodity boom

How to grow faster? Go big or *git gud*

At current investment efficiencies (ICOR above 6), Indonesia would need China-level forced savings to achieve 7-8% growth rate



- To grow at 7% YoY, Indonesia needs investment to be 39-45% of the GDP —reversing the usual consumption-driven growth model
- National saving rate is only 29-33%, although it approached 37% during the 2022 commodity boom ...
- ... the gap, as such, will have to be bridged by FDI or other inflows

▲ (y-axis)

Investment as a share of GDP
(average 2013-23 excl. pandemic)

(x-axis) ►

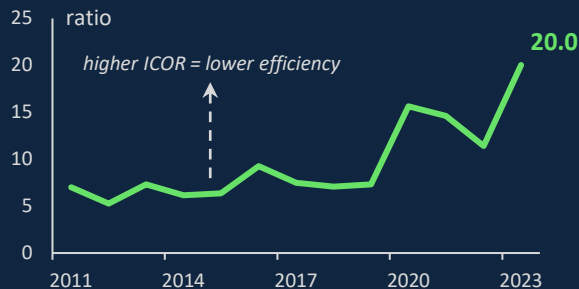
GDP growth
(average 2013-23 excl. pandemic)

Source: World Bank, calculations by BCA Economic Research

Sectoral ICOR: Are we misallocating our resources?

Rising ICOR across most industries are a sign of falling productivity—but also potentially misdirected investment (malinvestment)

ICOR: Agriculture



ICOR: Mining



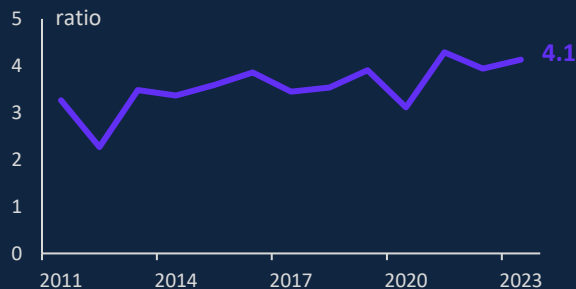
ICOR: Manufacturing



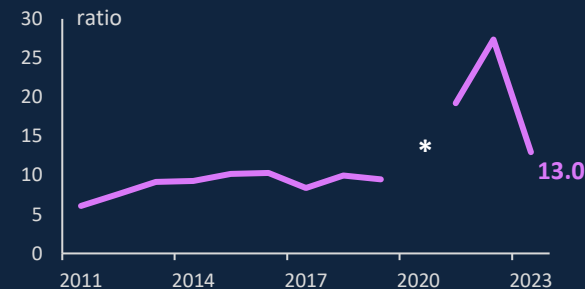
ICOR: Logistics



ICOR: IT & communication

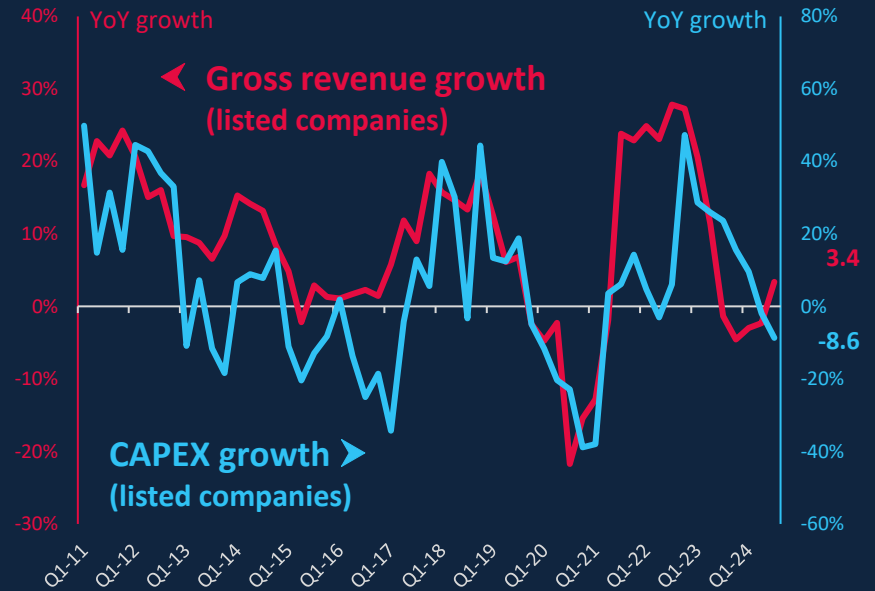
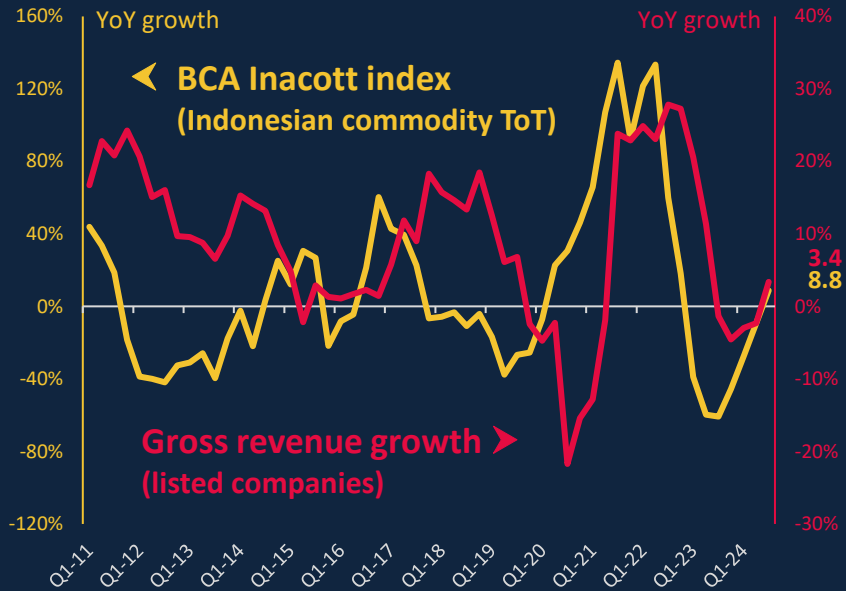


ICOR: Construction + Real estate



Corporate CAPEX: Good money after bad?

Global commodity cycle predicts the CAPEX cycle, but increased CAPEX does not seem to drive revenues higher



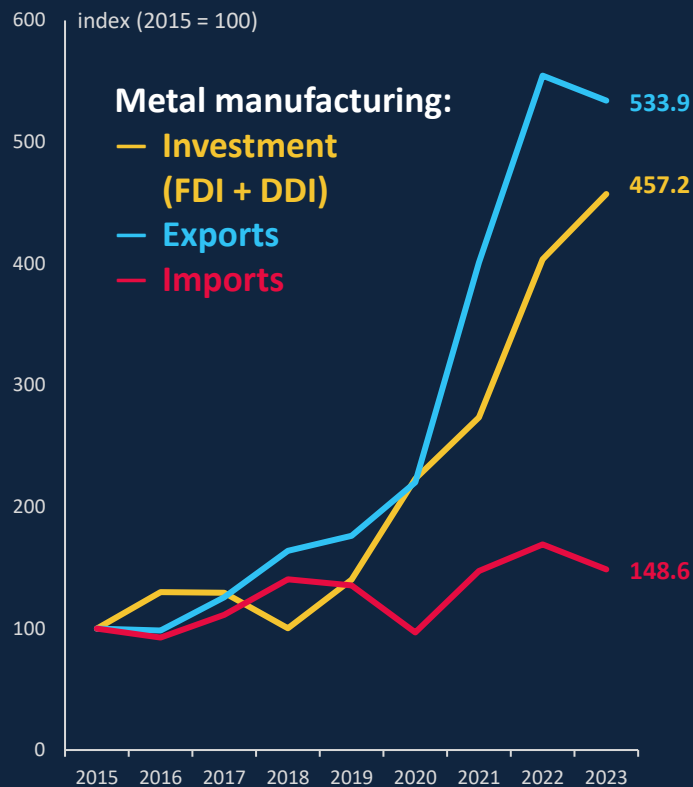
Correlation coeff.	q	q+1	q+2	q+3	q+4	q+5	q+6
Inacott > Revenue	0.134	0.369	0.524	0.574	0.546	0.449	0.287

Inacott correlates positively with gross revenue after 2-4 quarters lag

Correlation coeff.	q	q+1	q+2	q+3	q+4	q+5	q+6
Revenue > CAPEX	0.623	0.707	0.614	0.521	0.444	0.261	0.077
CAPEX > Revenue		0.453	0.204	0.005	-0.191	-0.278	-0.326

Can investment generate its own savings?

Nickel downstreaming has boosted the trade balance, but investment in other areas seems largely unable to improve the S-I gap



Manufacturing sector: Investment growth vs. trade

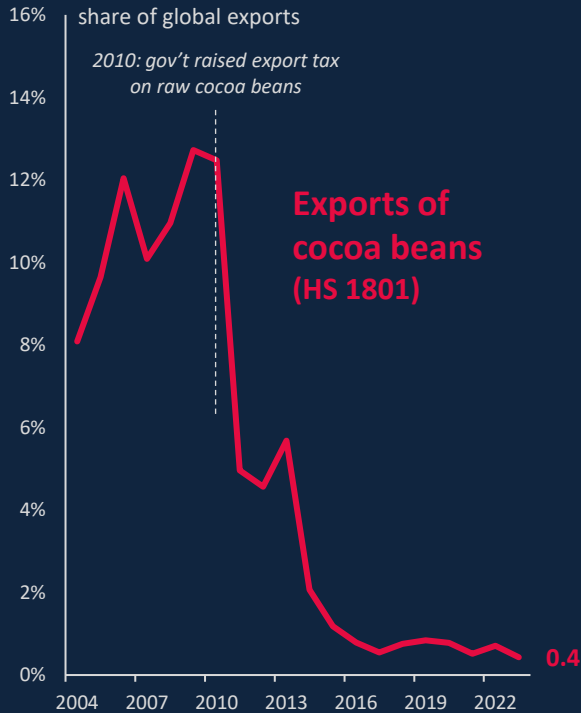
Sub-sector (HS Code)		CAGR (2015 – 23)			
		Investment	Exports	Imports	(Gap)
Metals	72-83	20.9%	23.3%	5.1%	+18.2%
Chemical & pharmaceutical	28-36, 38	9.1%	8.1%	3.3%	+4.8%
Vehicles	87	3.7%	9.4%	8.4%	+1.0%
Machinery	84-85	11.4%	5.3%	5.5%	-0.2%
Textiles	54-63	5.5%	-0.3%	2.0%	-2.3%
Plastic & rubber	39-40	2.5%	-0.4%	4.4%	-4.8%
Footwear	42, 64	23.7%	5.9%	12.5%	-6.7%

- Individual companies may obtain positive RoI, but **only exports constitute extra savings at a national level**—which is also why export-led growth (as in East Asian economies) has been the **only successful and self-sustaining development strategy**

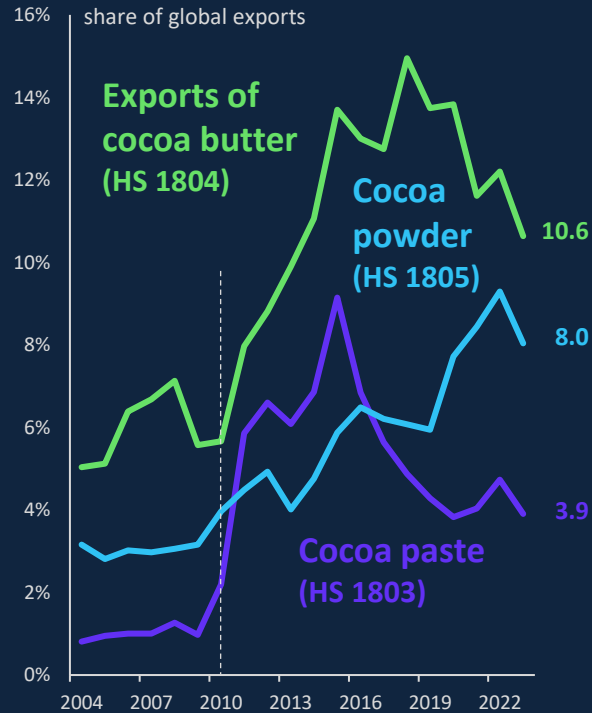
Downstreaming: Still not downstream enough

Cocoa, Indonesia's first big downstreaming success story, remains firmly stuck at the intermediate stage after more than a decade

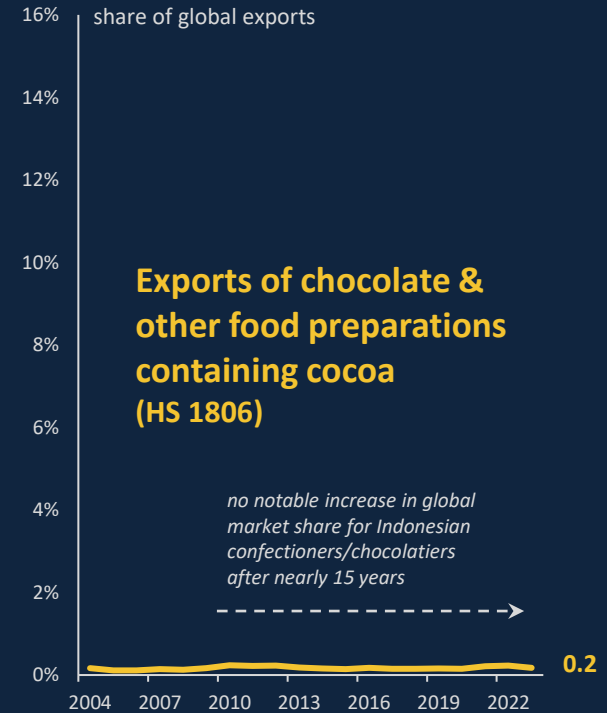
Raw material



Upstream manufacture



Downstream manufacture



Projection of Indonesian economic indicators



	2019	2020	2021	2022	2023	2024E	2025E
Real GDP growth (% YoY)	5.0	-2.1	3.7	5.3	5.0	5.0	4.9
Nominal GDP growth (% YoY)	6.7	-2.5	9.9	15.4	6.7	7.0	7.9
GDP per capita (USD)	4175	3912	4350	4784	4920	4975	5005
CPI inflation (% YoY)	2.7	1.7	1.9	5.5	2.6	1.6 [#]	2.5
BI Rate (%)	5.00	3.75	3.50	5.50	6.00	6.00 [#]	5.50
SBN 10Y yield (%)	7.04	5.86	6.36	6.92	6.45	7.04	7.47
USD/IDR exchange rate (end of year)	13,866	14,050	14,262	15,568	15,397	16,150	16,887
Trade balance (USD Bn)	-3.2	21.7	35.3	54.5	37.0	31.4	26.2
Current account balance (% of GDP)	-2.7	-0.4	0.3	1.0	-0.1	-0.6	-0.9

Notes:

- USD/IDR exchange rate projections are for fundamental values; market values may diverge significantly at any moment in time
- Numbers marked with (#) for 2024 are final; other numbers for 2024 are our projections

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A black and white photograph of a man with dark hair, wearing a light-colored shirt, leaning over a dark table. He is holding a clear glass filled with water with his right hand. His left hand is resting on the table. The background is blurred, showing some lights and a window. The text "Thank You" is overlaid in the center of the image in a large, white, sans-serif font.

Thank You