# Global Economic Outlook 2025

## A sliver of light, but dark clouds are all around

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# Summary


- **High interest rates in the US (and expensive USD) may continue to be a concern for the global economy**, as the US government is expected to boost its debt issuance. At the same time, the sustained growth momentum and returning inflationary pressures mean that the Fed may need to adjust its rate cut signal.
- **Further stimulus interventions may not be enough to turn the slowing trend in China's loan growth**, given its lingering property and debt crises. Still-muted domestic demand will continue to force Chinese manufacturers to sell cheaply to the export market, thus threatening manufacturers in other economies.
- **The uncertain outlook for global manufacturing activities translates negatively to commodity prices**, although a supply-driven price spike remains a possibility for some commodities.
- The combination of still-high global rates and sidelining commodity prices highlight the unideal external condition the Indonesian economy faces in 2025, possibly forcing the economy to seek more growth momentum within its internal market.


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# Part 1: Introduction

*A snapshot of the year's past*

***Chapter Summary***

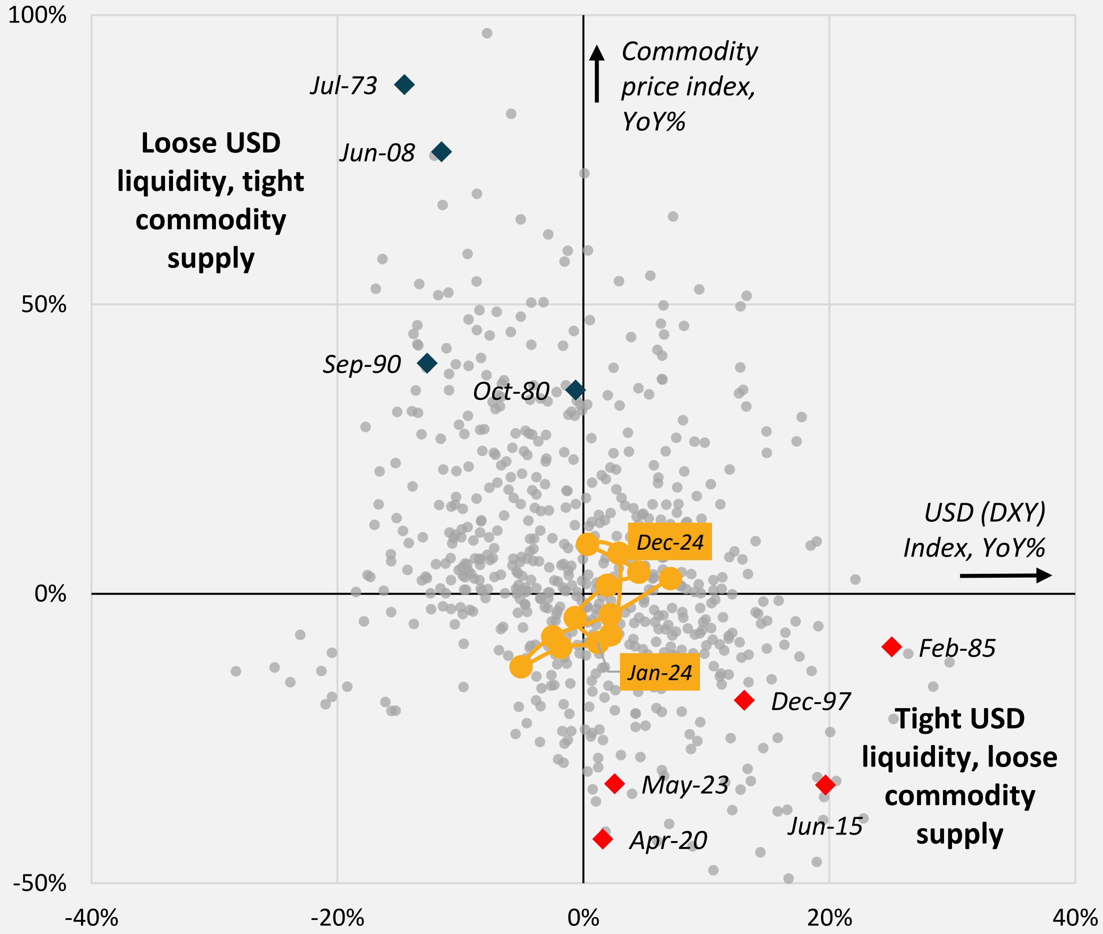
- The stalling disinflation progress delays the widely anticipated FFR cut until the end of Q3-2024. FOMC members' limited use of forward guidance, and the expected shift in US policies under President Trump, **have lessened the Fed's control over long-term US interest rates.**
- The continued expansion in China's manufacturing activities remains a contributing factor in the global disinflation. However, **competition against Chinese exporters proves to be detrimental for manufacturers elsewhere.**
- **The flatlining commodity prices and still-expensive US Dollar** highlight the global challenges that have curbed Indonesia's growth potential in 2024.

# The global economy is stuck in the middle throughout 2024

- The global economy continued to move towards relative normalcy in 2024. Weaker demand gradually lowered commodity prices to a more manageable level, while the USD is moving sideways as the Fed could only realise the long-awaited FFR cut in late Q3-2024.
- The inflationary world of tight liquidity and commodity supplies (such as in 2022-23) are gone, **replaced by a world where both commodity prices and the USD is hanging mid-air** – capable of swinging in either direction. Where the USD and commodity prices will swing in 2025, of course, will be con-sequential for the Indonesian economy.
- **A top-left swing *(see chart 1.1)*, where commodity prices rally and the USD weaken, will be the most ideal scenario for Indonesia.** This scenario rema-ins open, as the Fed Funds Rate is still some measure away from its neutral level, while fiscal stimulus may prolong manu-facturing expansions in China.
- Alas, some risk factors may drag the global economy towards a less ideal condition. For instance, returning inflationary pressures could keep the USD expensive, while the high raw material stockpile obscures the outlook for the commodity market. **"Soft landing" remains the baseline scenario, as the Fed moves to balance the risk between unemployment and inflation.**

**Chart 1.1**

The Indonesian economy tends to rally during an environment of loose liquidity and high commodity prices, and vice versa




**Source:** Bloomberg, BCA Economic Research. Monthly data from January 1971 to December 2024 (17-01-2024 data cutoff). Green dots indicate periods of above-average Indonesia GDP growth. Red dots indicate periods of below-average Indonesia GDP growth or recession. Yellow dots and line indicate recent periods.

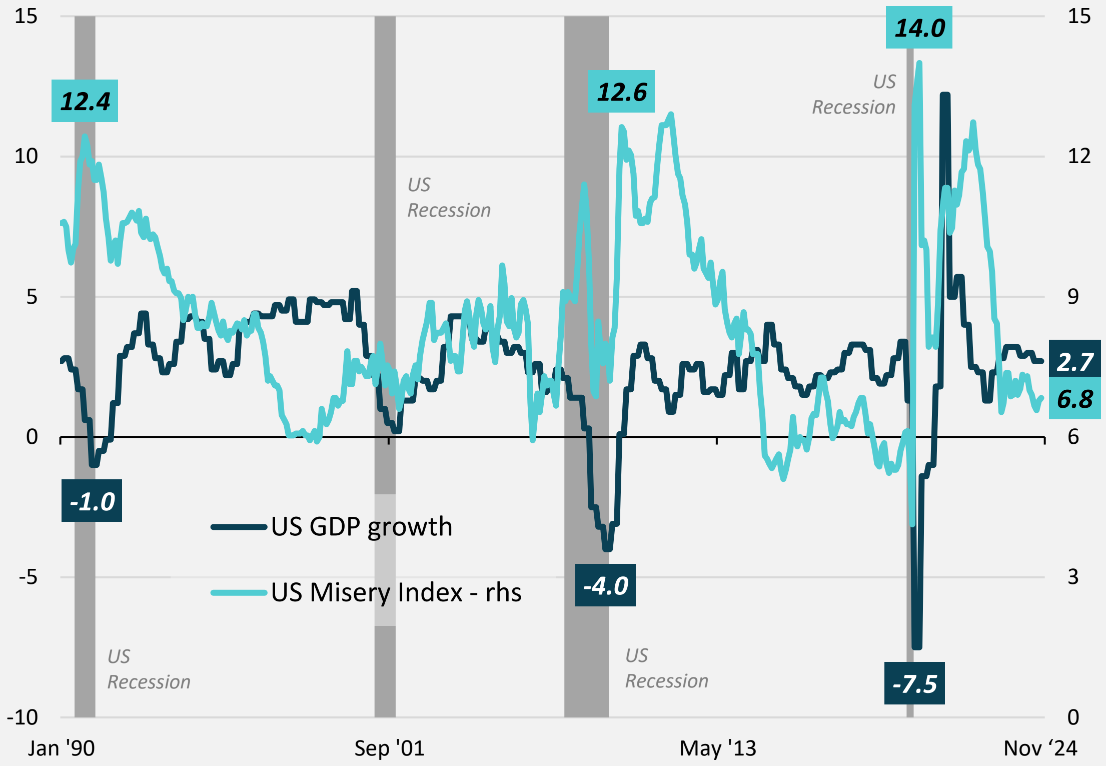
# The US economy remains strong, but economic misery lingers

- The Fed cutting its policy rate in 2024 was, in a way, is inevitable. **The market has been strong-arming the Fed to cut its policy rate**, and the loosening labour market condition (the unemployment rate increased from 3.73% early in the year to 4.20% by the time the Fed cut the FFR) justifies the Fed started its policy-loosening campaign by a 50-bps cut. **A cooling labour market, of course, is never a welcome development for the real sector**, despite the cheer in the financial market.

- Lower demand for workers, especially in consumer services and other blue-collar sectors, lowers the public's confidence in the economy, with the consumer sentiment index falling to its 2024 nadir of 66.4 by July 2024 (79.0 in January 2024**). The declining employment opportunities for lower-skilled workers, combined with the still-high price level (average petrol prices in 2024 is USD 3.2/gallon, vs. USD 2.4 2017-2021 average), explains the public's discontent**, which seems to play a part in President Trump's electoral success in the 2024 elections.

**Chart 1.2**

The US economy continues to record robust growth, but the upward trend in the unemployment rate encouraged the Fed to start its rate-cutting cycle with an initial 50-bps cuts despite the stagnating progress towards 2% inflation.

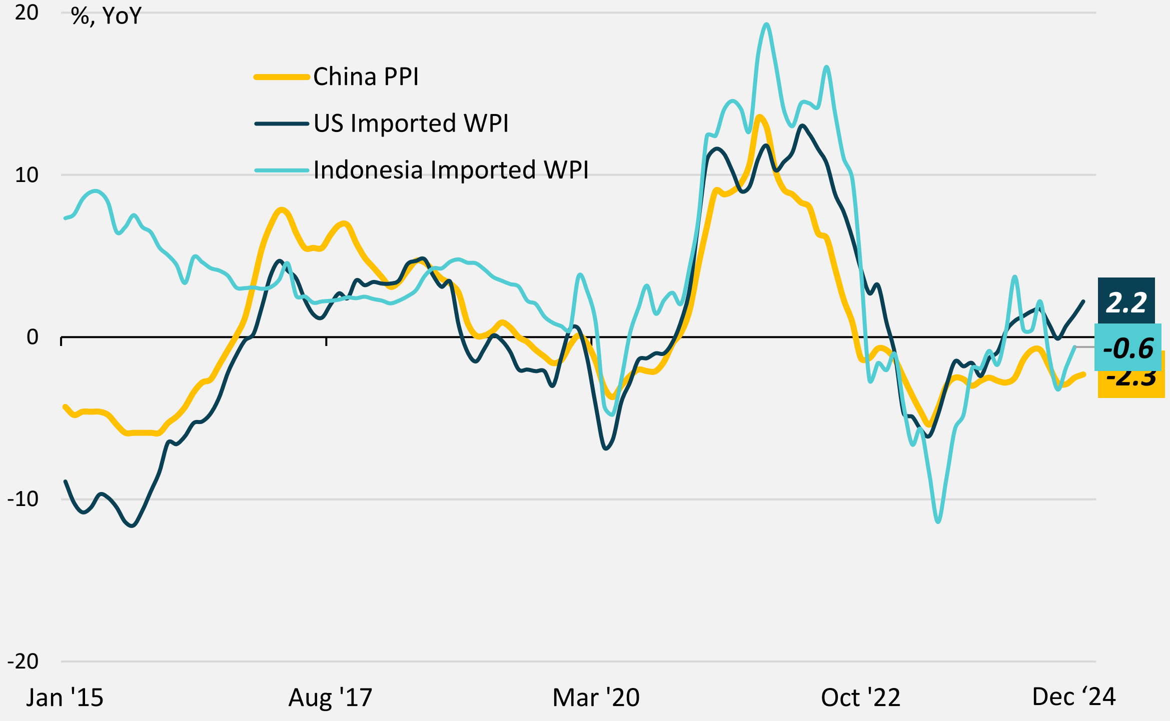



**Source:** Bloomberg, NBER, BCA Economic Research. Monthly data from January 1990 to November 2024 (GDP is quarterly). The misery index is monthly CPI inflation added to the unemployment rate. GDP is in constant prices.

# China offers recourse for consumers, but at the cost of manufacturers

**Chart 1.3**

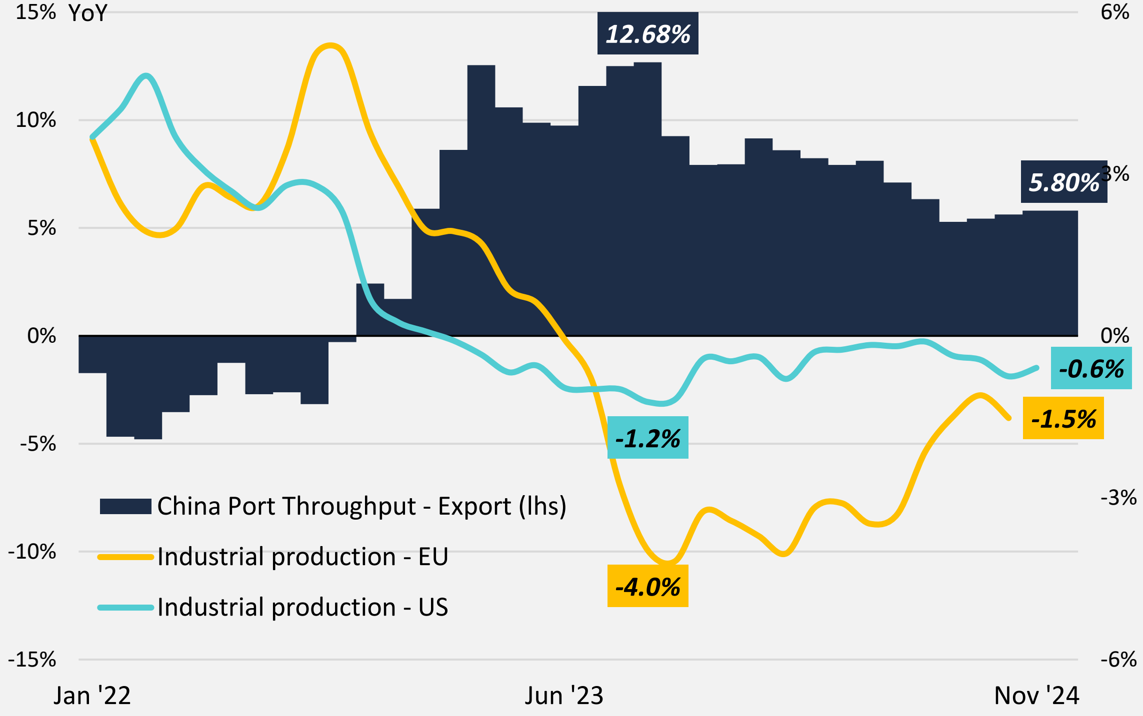
Lower factory gate prices in China reduce import prices globally, given that the weak demand in China gives no option to manufacturers but to export.




**Source:** Bloomberg, BLS, BPS, BCA Economic Research. Monthly data from January 2015 to December 2024 (last available data).

**Chart 1.4**

Accelerating exports in China coincide with periods of industrial slowdown in big consumer economies such as the US and EU




**Source:** Bloomberg, BLS, Eurostat, BCA Economic Research. Annual changes of 3CMA monthly data from January 2022 to November 2024 (last available data, October 2024 for EU data).

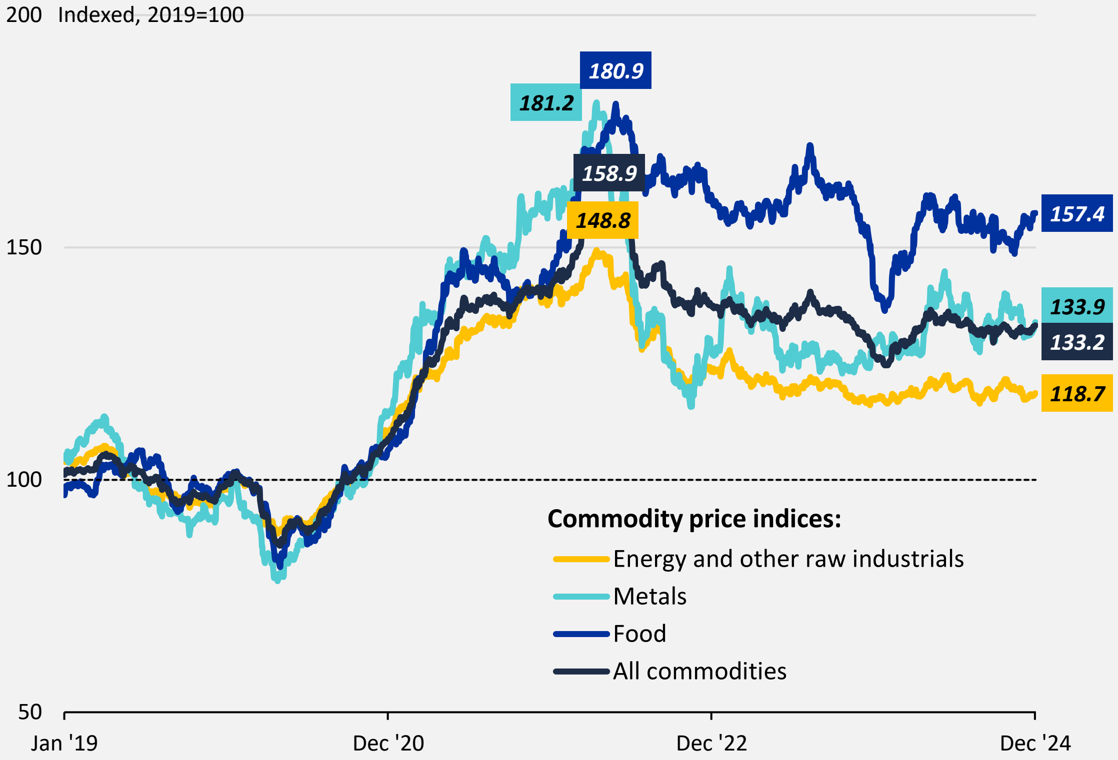
- Despite the worsening sentiment, lower goods prices have enabled American households to continue expanding their consumption basket. **The flood of imports from China plays an important role in lowering prices**, as Chinese manufacturers have no means but the export market to offload their manufacturing surplus.
- Alas, what's good for consumers does not seem beneficial for manufacturers. **Competition from Chinese exporters has pummelled local manufacturers in the rest of the world (including Indonesia),** as Chinese manufacturers could operate with lower margins thanks to their scale advantage (and the alleged unfair subsidies).

# Commodity prices flatlined, albeit not far from its record high

- Meanwhile, further normalisation in the worldwide supply chain has also pushed commodity prices lower, especially for energy and other industrial materials, given the weak momentum in global manufacturing activities.
- The flatlining global commodity prices are bad news for commodity producers, including Indonesia. **Analysts have been looking for stimulus in China to drive commodity prices higher**, leading to the expectation that the stimulus-funded recovery in China's domestic demand will put the Chinese manufacturing sector in a higher gear and, thus, drive the demand for commodities higher.
- **Unfortunately, there is still a question mark on the impact of China's recent stimulus on the real sector**, meaning that it may not be too likely for commodity prices to return to their previous high.
- However, global food prices show a relatively different picture. **The combination of lower investments and more challenging weather conditions has led to episodes of supply disruptions, especially for tropical crops.** The high food prices (in level terms) also feed into the negative sentiment shrouding the US and other economies, despite the more palpable decline in goods and energy prices.

**Chart 1.5**

Stagnating global manufacturing activities dragged energy and other industrial materials prices lower, but consumers are still reeling from high food prices.



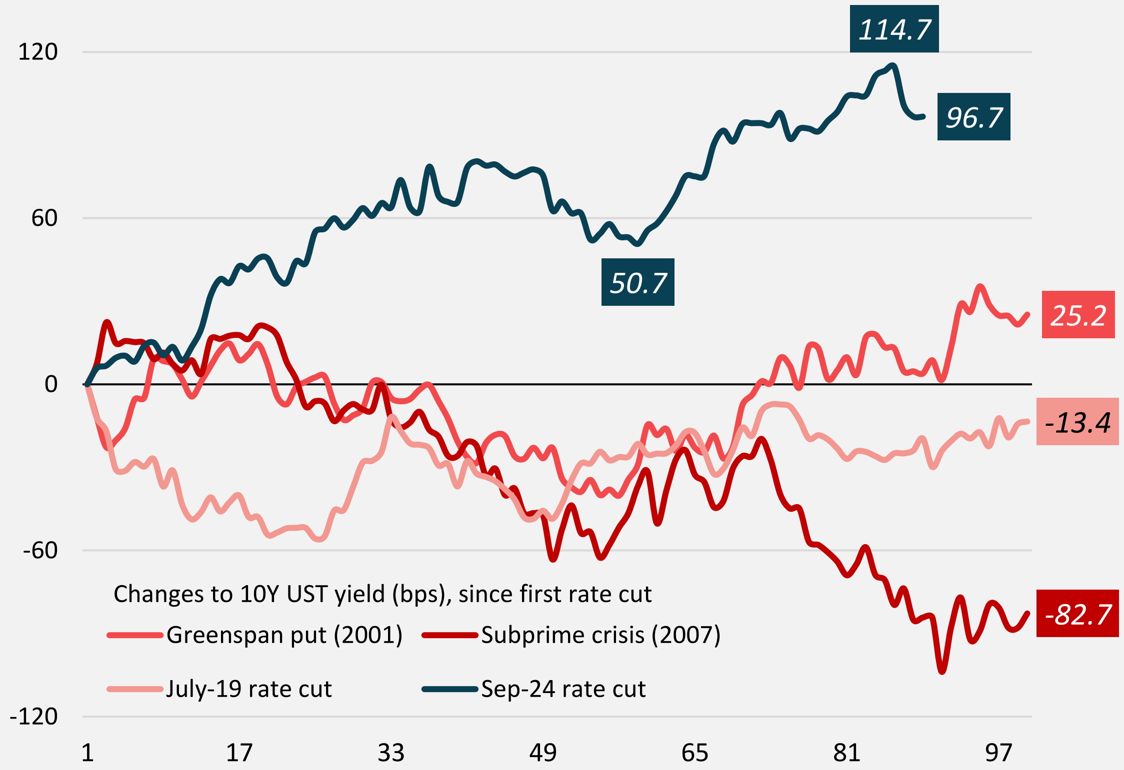

**Source:** BLS, BCA Economic Research. Daily data from 1 January 2019 to 17 January 2025 (last available data).

# US financial conditions continue to tighten despite the lower FFR

- The flatlining commodity prices, especially for energy commodities such as oil, seem to influence the Fed's decision to lower the policy rate, as indicated by the correlation between the Fedspeak index and oil prices.
- However, despite the 75 bps rate cuts already delivered by the Fed, financial conditions in the US have actually tightened. The expectations of policy shifts following the US presidential election have led to what the market called the "Trump trade", as **the expected higher deficit under the second Trump presidency turned investors bearish on the US Treasury market.**
- **The threat of a second trade war has also strengthened the USD**, as the risk of higher import tariffs put downward pressure on the CNY and other hard currencies.
- President-elect Trump's pragmatic pick for the US Treasury Secretary nominee has seemingly calmed the market. Alas, **the tariff question is for the more hawkish Commerce Secretary nominee to answer, while the next US Treasury secretary may also have the normalising UST yield curve to think about.** How far US policies will shift under the second Trump presidency, as it seems, remains the X-factor that will shape the global economy in the new year.

**Chart 1.6**

The benchmark 10Y UST yield continue to increase despite FFR cuts in 2024, driven by the projected higher deficits and returning inflation expectations under the upcoming Trump presidency.




**Source:** Bloomberg, BCA Economic Research. Daily data. X-axis represent daily changes in the 10Y UST yield (USGG10Y) for up to 100 days since the first Fed funds rate cut.

# Part 2: Of rates and policies

*Hanging in mid-air*

***Chapter Summary***

- **The expected higher debt issuance and longer duration in the UST market may keep the long-term UST yield high**, which may prompt the Fed to slow its balance sheet runoff as the occasional spike in the money market rate also highlights the not-so-ample condition in US bank reserves.
- Despite the potential end to QT, **the Fed's rate-cutting path remains obscured** by the still-robust US labour market and the risk of returning inflationary pressures amidst the upcoming shift in US government policies.
- **The USD's value may remain higher for longer as higher yields and alpha attract foreign capital inflows to the US market.** However, it is to be seen whether investors could continue to justify the increasingly higher premium in the US financial market.

***Implications to the Indonesian economy***

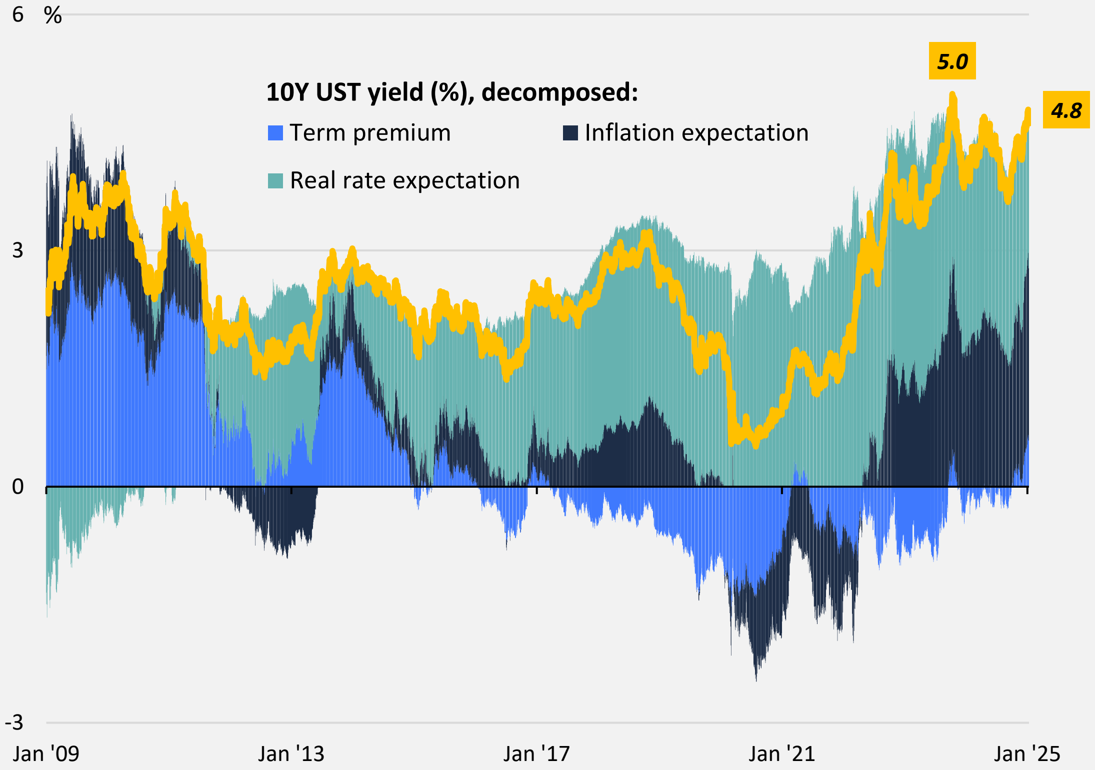
| Exchange rates | Current account | Growth potential |
|---|---|---|

# Interest rates in the US may have become structurally higher

- Economic discussion have pointed to the expected deeper fiscal deficits under the next Trump presidency as the reason behind the elevated UST yield. Indeed, making the provision under the 2017 TCJA* permanent and lowering corporate tax to 15% is expected to cost the US government USD 3.01 Tn in lost revenue over the next 10 years, leaving a USD 211.2 Bn in funding shortfall during the period after accounting for the higher tariff revenue. **A successful review of the US government's efficiency (spearheaded by DOGE) will help to narrow the gap, but much of the funding needed may still come from higher debt issuance.**
- However, speculations over US policy changes in 2025 cannot be alone in hoisting the UST yield higher. **The US economy has proven its ability to maintain growth in a high-rate environment, leading to a real appreciation in the market's real rate expectation.** The estimation of the neutral US interest rate (R-star^) has also shifted higher in recent periods (to 1.25% from 1.06% 2009-19 average), a sentiment which is also apparent in FOMC members' own forecast of long-term interest rates (3.0%, up from 2.9% in Sep-24 summary of economic projections).

*The Tax Cuts and Jobs Act was signed into law by President Trump in 2017, due to expire in 2025.
^Estimations by the NY Fed, using

**Chart 2.1**
Returning inflationary pressures, the higher neutral interest rate, and the expected increase in long-term bond issuance may keep the benchmark US interest rate high



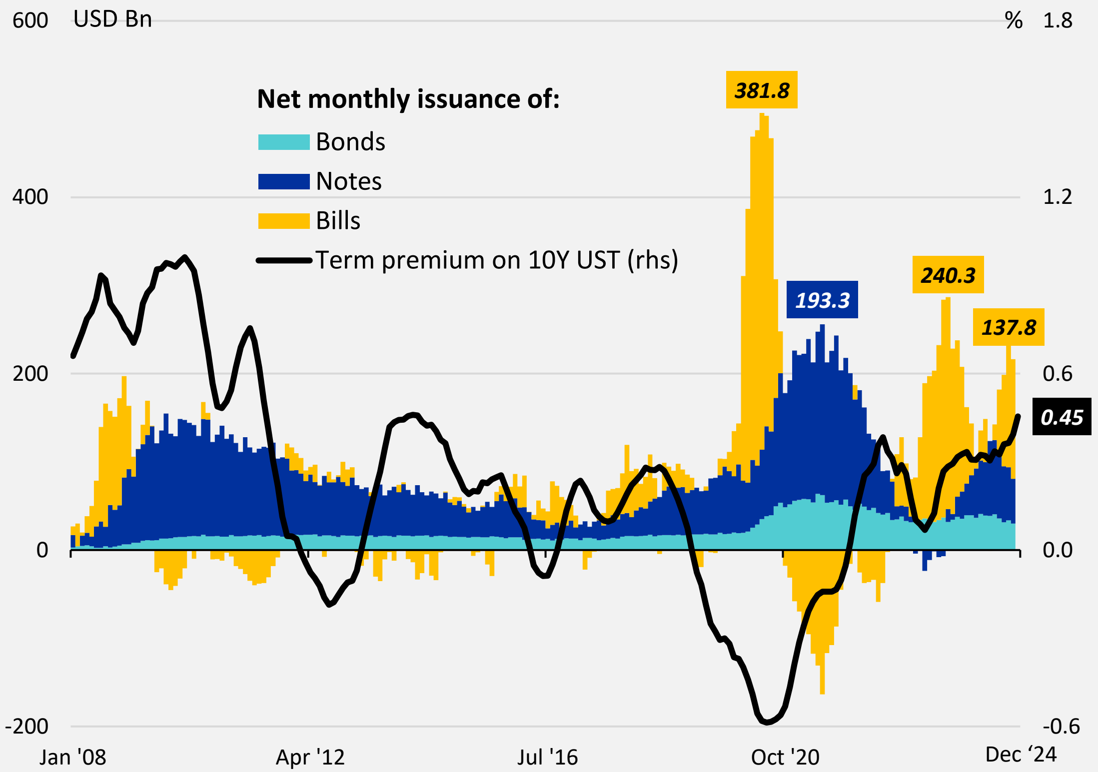

**Source:** Bloomberg, BCA Economic Research. 10Y UST term premia is estimated using a model by Adrian, Crump, and Moench (2014). Daily data from 2 January 2009 to 17 January 2025.

# Long-term rates may continue to be elevated as duration normalise

- Apart from the fiscal balance, the US Treasury Department's debt issuance strategy will also dictate how financing conditions in the US might swing in 2025.
- The Treasury's strategy to rely on T-Bills and limit long-term bond issuance has effectively eliminated term premia from the UST market, with one estimate show that the Treasury's strategy to limit long-term bond supplies has brought a loosening effect similar to a one-point cut in the FFR. **Alas, the Treasury Department may not be able to run the strategy for much longer**, given the rollover risk that may add to the US government's sky-rocketing interest burden.
- The next Treasury Secretary, then, may see such an activist treasury issuance to unwound, potentially lifting the long-term UST yields by 30-50 bps according to an estimate.
- **Investors' ability to absorb the longer-dated and higher number of USTs remains uncertain**, which could drive interest rates higher. Markets' positive reaction following fiscal hawk Scott Bessent's nomination serves as a symptom, highlighting the increasingly active bond vigilantes currently.

**Chart 2.2**

The increasing concentration risk in the T-bills market may necessitate the upcoming US Treasury secretary to issue more long-term bonds.




**Source:** SIFMA, Bloomberg, BCA Economic Research. Monthly data from January 2008 to December 2024. 7 months centered moving average.

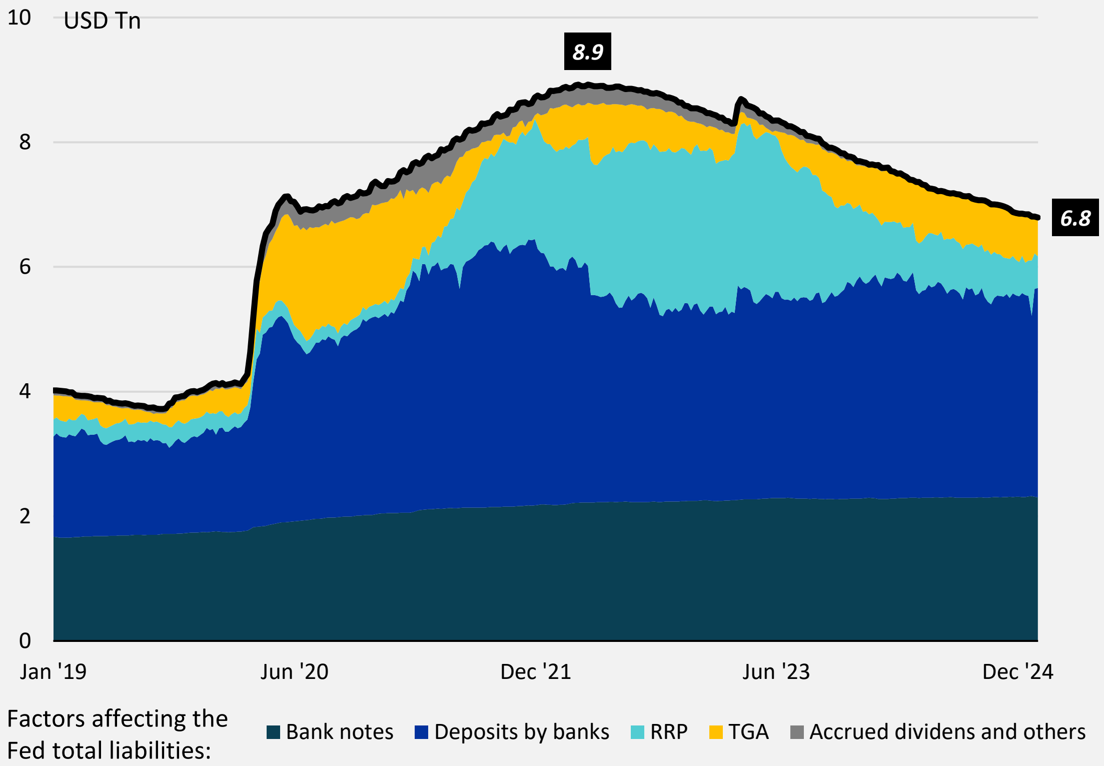
# A shock in the UST market may add the argument for the Fed to rethink its QT campaign

- The positive liquidity effect generated by the Treasury's ATI[1] experiment has also helped the Fed to execute its quantitative tightening. Despite earlier concerns, the decision to use T-bills to spearhead the TGA[2] refill operation has kept the US bank reserves intact, as T-bills' more money-like property unlocks the demand from money market funds and, thus, drawing liquidity not from bank reserves but from the Fed's RRP balance. However, **the recent spike in SOFR rate (SOFR was printed at 22bps higher than EFFR in October 2024) shows that at USD 3.2 Tn currently, the US bank reserves may not be as abundant as Fed officials' thought**[3].
- The Fed have introduced a 5bps technical adjustment to the ONRRP rate, designed to draw liquidity out of the repo facility to help stabilise money market the rate.
- **However, the RRP balance also dwindles, weakening the liquidity buffer that hitherto protected bank reserves.** The expected higher and longer issuance of UST securities could also funnel liquidity away from bank reserves, potentially adding volatility in the US money market. Such a condition may force the Fed to rethink its liquidity absorption strategy, with another slowdown (or even a full stop) to the QT campaign looking likely.

[1]Activist treasury issuance. [2]Treasury general account.
[3]Lowest comfortable level of reserves.

**Chart 2.3**

Despite the stable US bank reserves, the dwindling RRP balance and spiking long-term UST yield may put an end to the Fed's balance sheet run-off.

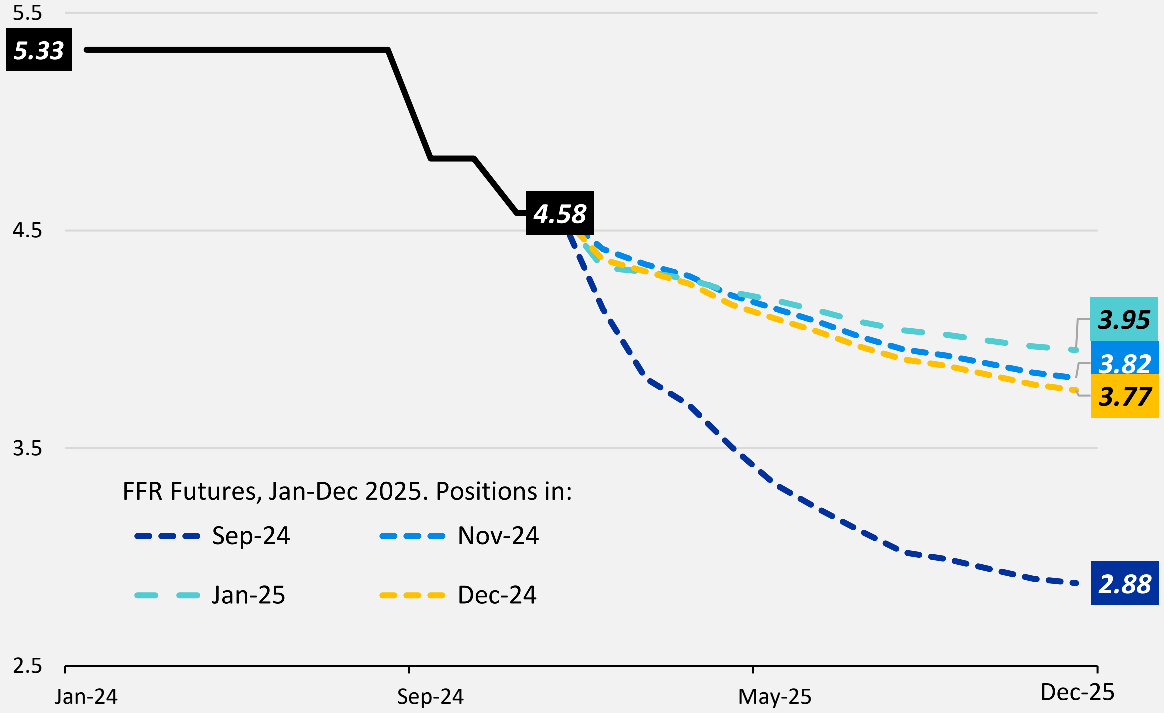



**Source:** FRED, BCA Economic Research. Weekly data from 2 January 2019 to 15 January 2024. Wednesday level

# The market does not expect Fed policies to loosen significantly in 2025

**Chart 2.4**

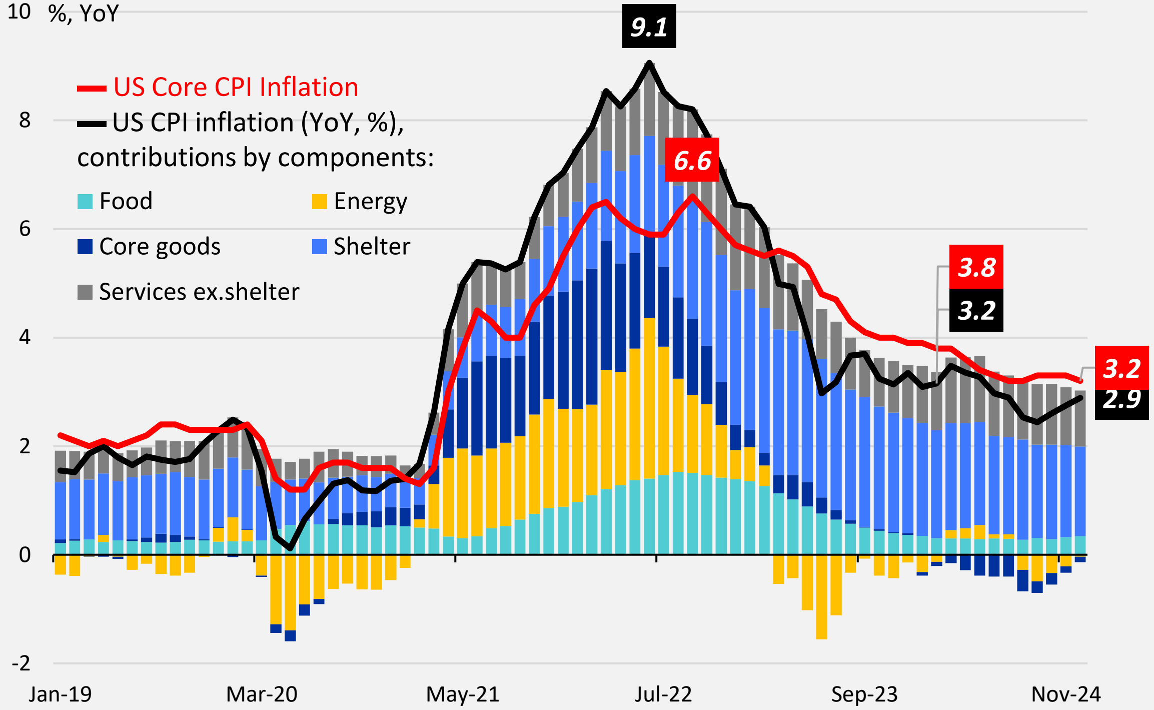
The market is expecting the Fed to neither far nor fast in its rate-cutting campaign in 2025, given the still robust economic data in the US.




**Source:** Bloomberg, BCA Economic Research. **Black** line indicates the actual effective Fed Funds Rate. Daily data from 2 September 2024 to 17 January 2025.

**Chart 2.5**

The sticky services and shelter inflation continue to stand in the way between the Fed and its 2% inflation target.




**Source:** BLS, BCA Economic Research. Monthly data from January 2019 to December 2024.

- The market, however, seems to be treating the strain in SOFR as a sideshow. The FFR outlook remains the focal point, as the market is now in general retreat following FOMC members' limited outlook for rate cuts in the next year (down to 50 bps from 100 bps).
- The argument for a hawkish Fed in 2025 is more easily seen in the current circumstances. Inflation remains hot, while the still-strong macro data lowers the concern for an impending US recession. The expected US policy changes add to the reflation concern, leading to FOMC members revising up their inflation expectation in 2025 from 2.1% to 2.5%.

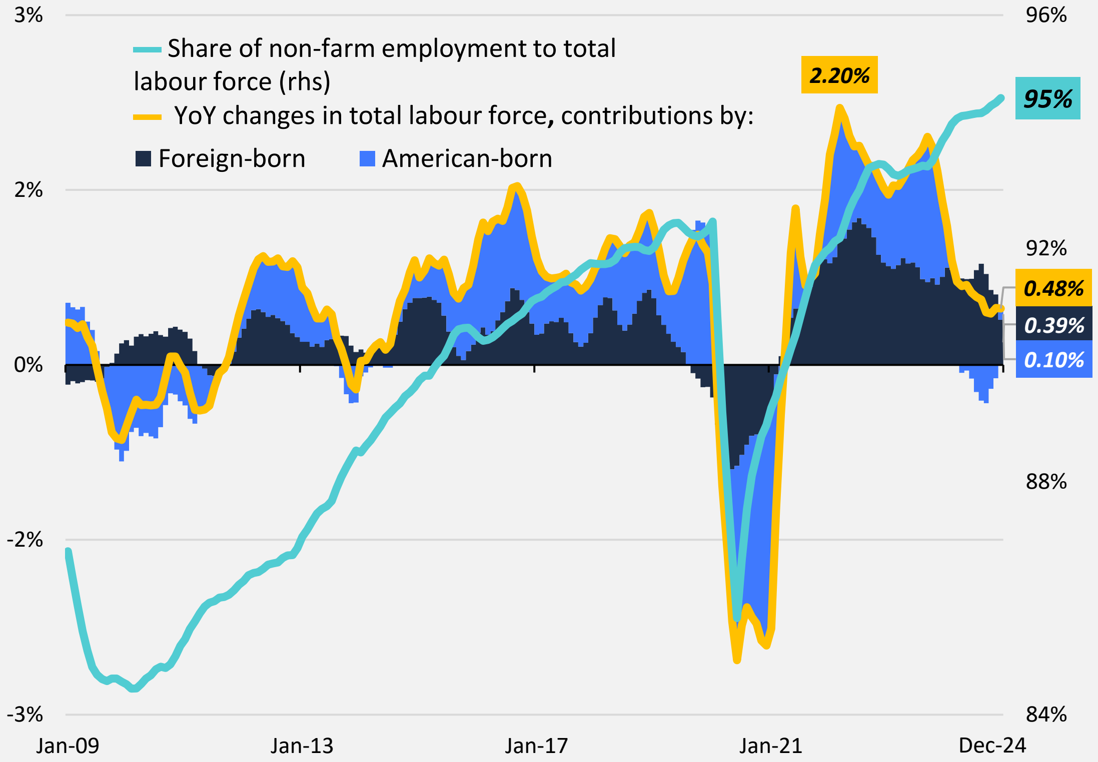
# President-elect Trump's policy agenda may have put the Fed further into quandary…

- Many analysts have fired a broad-side attack on President Trump's import tariffs agenda, pointing to the policy as the main concern that may bring inflationary pressures back to the US. However, our concern for a lingering inflationary pressure in the US stems from another Trump's trademark policy agenda – that is the tighter border control.
- Indeed, President Biden's "Build Back Better" agenda has led to a higher non-residential FAIs, which drives up the demand for workers in the construction sector. President Trump's deregulation and other pro-business policies may further expand the labour market, possibly keeping the unemployment rate close to NAIRU*
- The potential job market expansion is incongruent with the US labour market, which has now relied on a higher influx of foreign-born workers to keep its growth momentum.
- Reducing the foreign workers population may also create a structural imbalance in the US labour market, given the high representation of foreign workers in the services sector (and vice versa). Ergo, akin to the situation in 2021, a lower foreign worker population may create competition for labour in the service sector, keeping the services^ component of the price index elevated.

*Non-accelerating inflation rate of unemployment. Currently at 4.6% according to an estimate by Philadelphia Fed vs. 4.2% actual unemployment rate.
^Services other than energy services and shelter

**Chart 2.6**

A tighter immigration policy may bring back inflation to the US, given that the economy remains reliant on foreign-born workers to relieve the still-tight labour market.

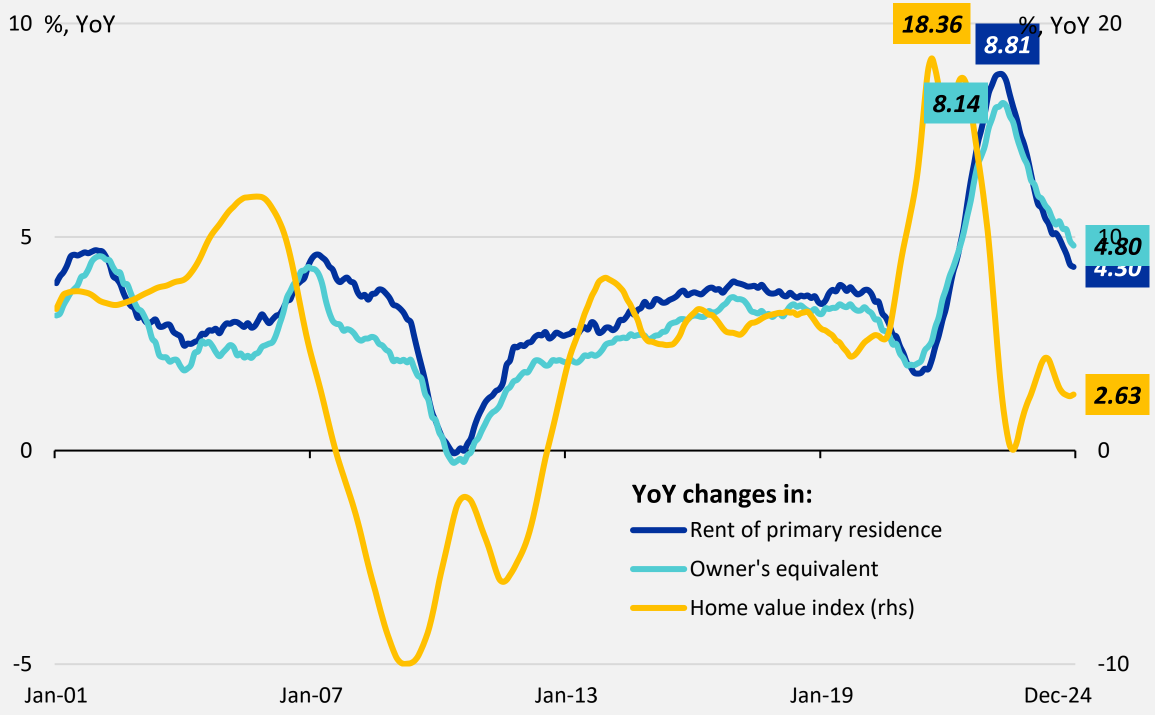



**Source:** BLS, BCA Economic Research. Monthly data from January 2009 to December 2024.

# …although the sticky rental inflation may eventually come unstuck

**Chart 2.7**

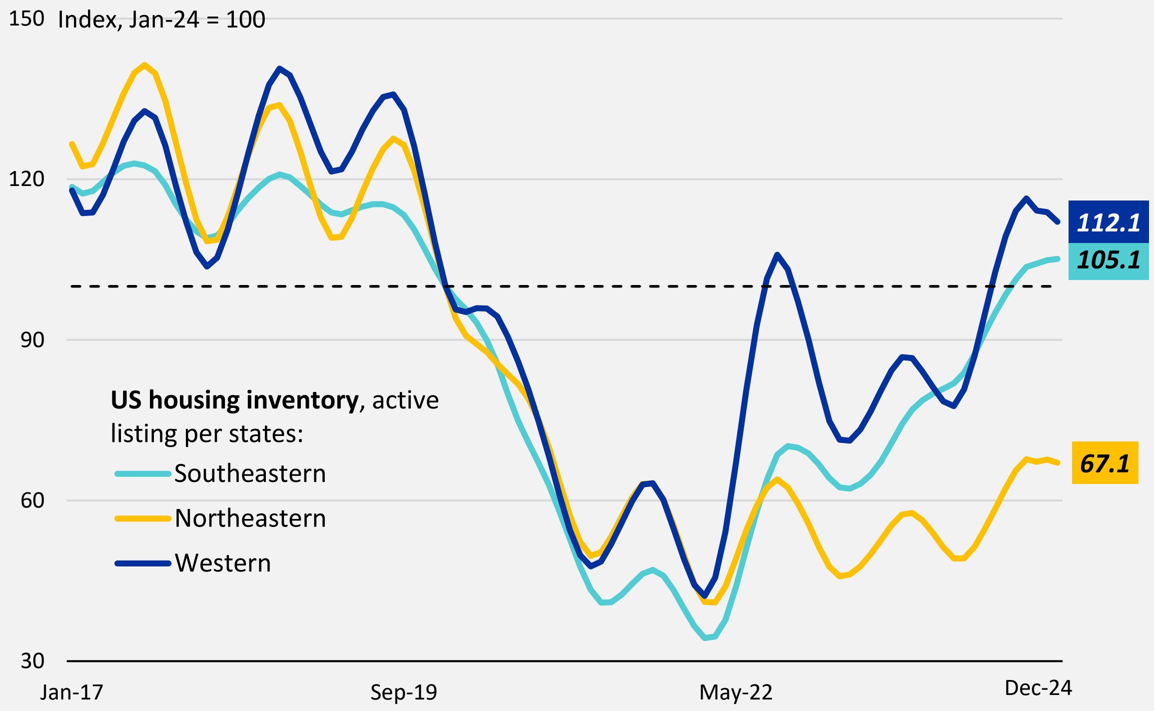
Rental inflation continue to decline, thanks to lower migration to the denser northern states and the higher rental supplies, especially in southern states.




**Source:** BLS, Zillow, BCA Economic Research. Monthly data from January 2001 to December 2024.

**Chart 2.8**

Housing inventories in the US are improving, especially in the southern and western states, which enjoy a net positive migration in the past couple of years.




**Source:** FRED, BCA Economic Research. Monthly data from January 2001 to December 2024.

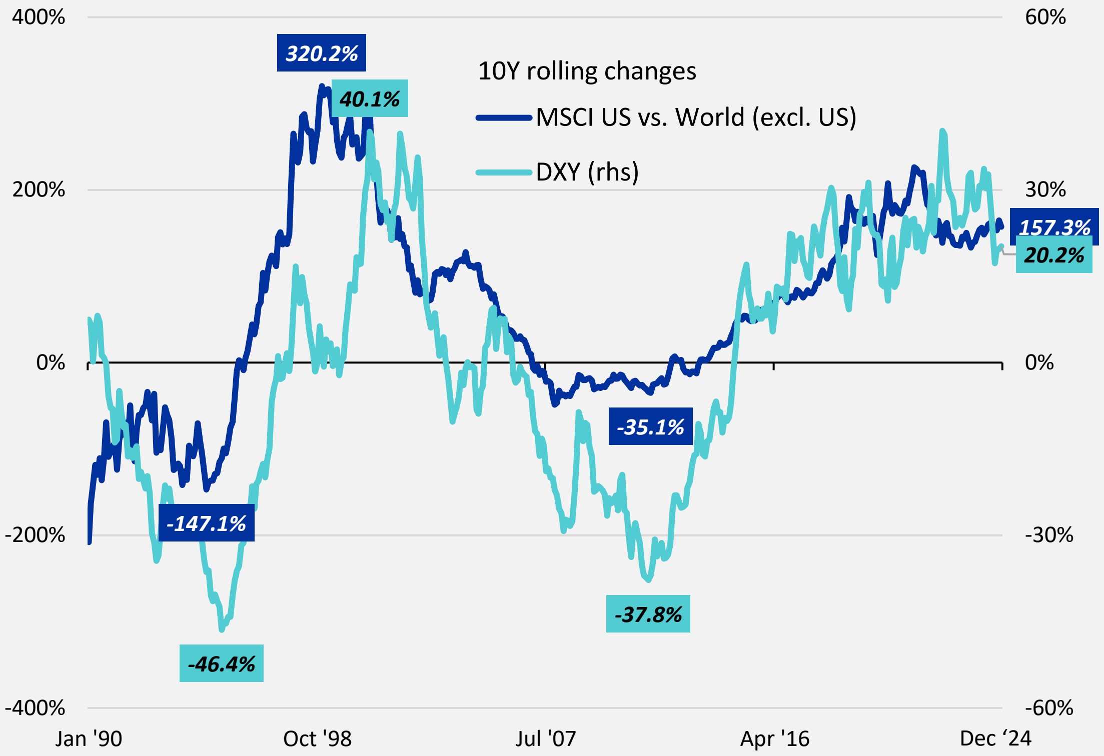
- Another factor that hitherto keeps US inflation high is the agonisingly sticky shelter inflation. Alas, the Fed's policy tool is not geared to tame rental inflation. Higher-for-longer policy rates will only lower the activity in the residential property market, worsening the market balance.
- Luckily, recent migration trends outside of the denser Northeastern states help to correct this imbalance. Lower construction costs also translated to higher housing inventory growth in Southeastern and Western states, which generally recorded a net positive migration. Maintaining this trend is crucial to lowering the shelter inflation in the US. Alas, increasing opposition to remote working means that Americans may flock again to denser states.

# A continuously strong USD is unfavourable, even for the US

- The Fed's hawkish New Year message, along with mounting uncertainties leading up to the second Trump presidency, have led to a further strengthening in the USD value. The USD's strength amidst periods of global uncertainties highlights its unique feature as the global reserve currency, as investors tend to concentrate their assets in the US financial market during such periods.
- Indeed, periods of Dollar up-trend often coincide with periods of US equity performance. This observation is particularly true in the past couple of years, as the AI mania provides the justification for the spiking premium on US equities.
- However, as indicated by the long-term historical trend, there remains a ceiling in how high the USD could continue its rally. More investors will eventually point to concentration risk as US equities charged even higher premiums, making the US financial market more vulnerable to signs of slowing growth momentum.
- Even without a considerable economic slowdown, higher premiums charged in the US financial market may also prompt investors to look for opportunities elsewhere – leading to a sell-off in the US market. The market, then, may eventually force the USD lower, especially if alternatives to the USD continue to emerge.

**Chart 2.9**

Periods of higher USD value often coincide with strong inflows to the US financial market, up to the point when the highly concentrated US market compels investors to look for opportunities elsewhere.



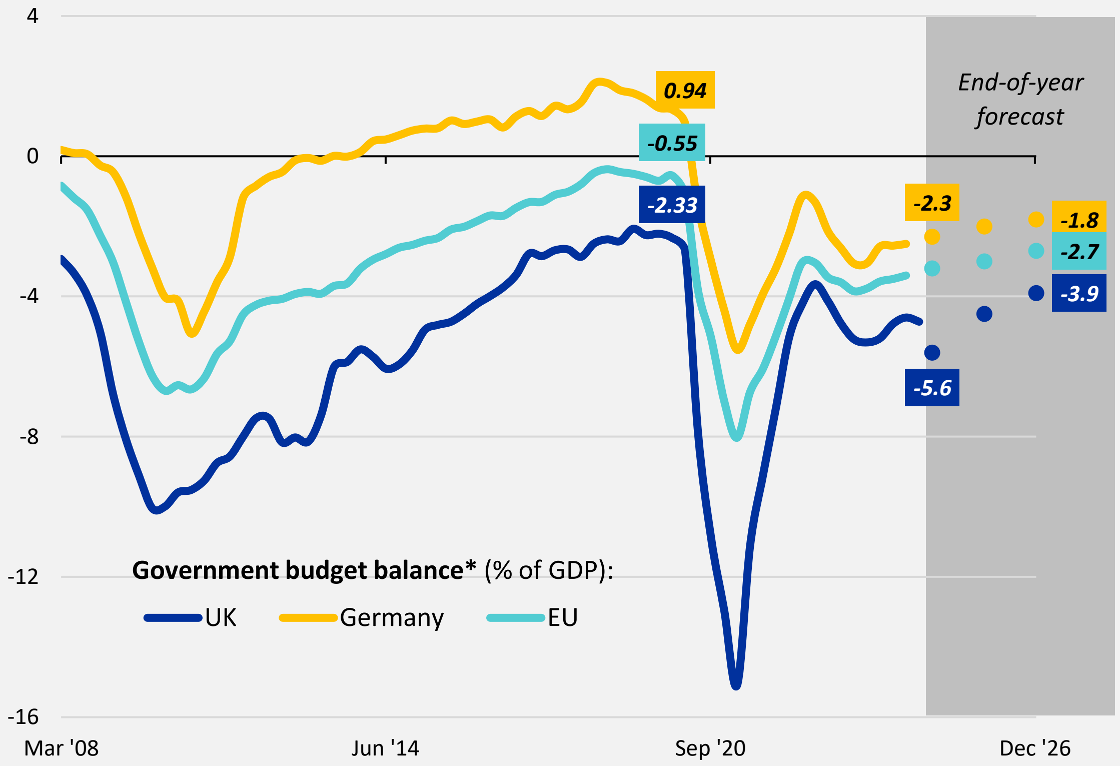

**Source:** Bloomberg, BCA Economic Research. Monthly data from January 1990 to December 2024

# The European bond market may add to the challenge for the UST market

- The generally undervalued European bond market highlights the alternative for global investors outside the US financial market. The relatively tame inflationary pressures (-0.3% MoM CPI inflation in Nov-2024) and weak growth momentum mean that central banks in Europe are on a clearer rate-cutting path, unlike the condition faced by the Fed.
- However, the gloomy growth outlook continues to trouble European policymakers. China's success in climbing up the manufacturing ladder (especially for industrial machineries and automobiles) have declawed German exporters, so does the potentially higher US import tariffs.
- At the same time, many European governments are struggling to maintain their trademark social-democratic policies amidst the narrowing fiscal space, leading to domestic political crises in France and Germany. Indeed, despite the forecasted lower fiscal deficit in most European economies, some European economic powerhouses have found it hard to balance their budgetary posture, with the UK government already announcing a GBP 19.2 Bn increase in their 2024/25 gilt issuance, while the debate in the German parliament seems to be moving in favour of loosening the debt brake (*schuldenbremse*) mandate set by the first Merkel government.

**Chart 2.10**

European economies' budget balance is expected to even more gradually return to its pre-pandemic level, portending higher debt issuance in some European economic powerhouses such as the UK and Germany.



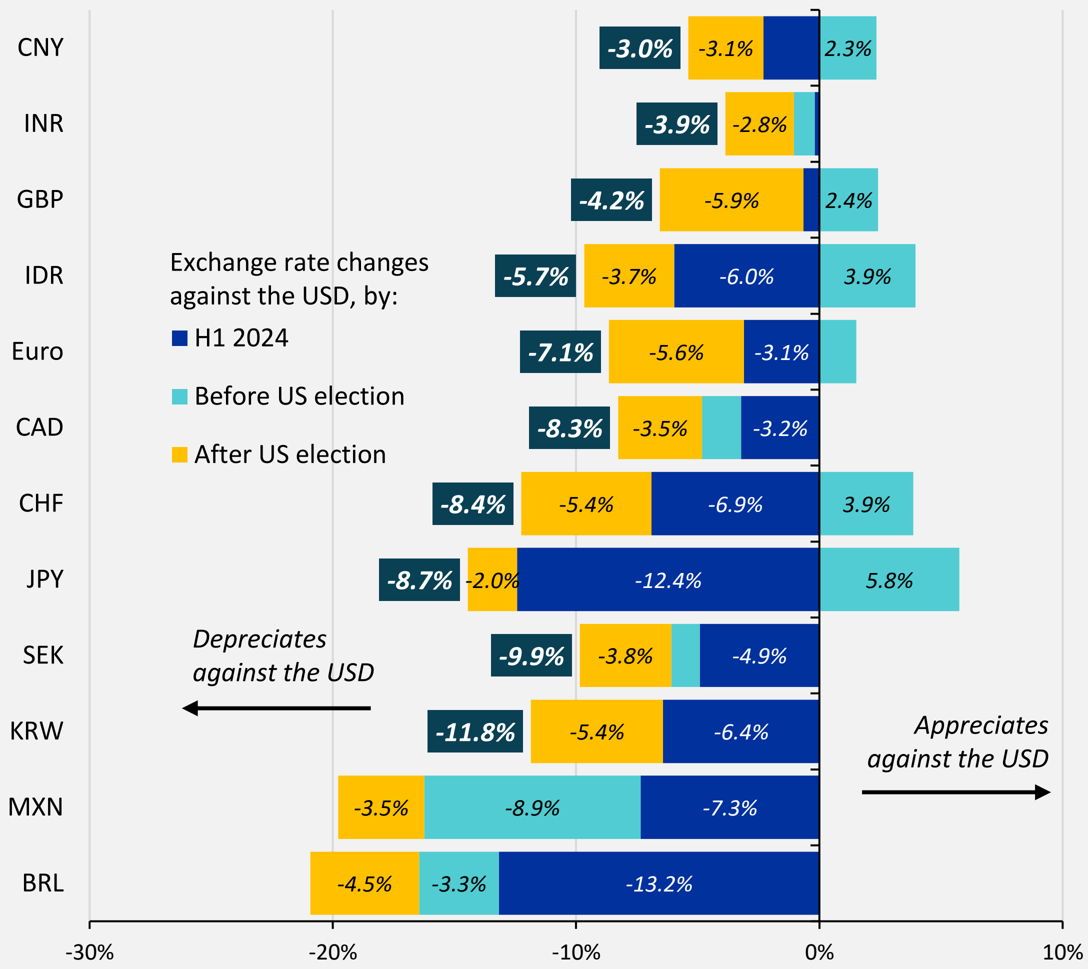

**Source:** UK Debt Management Office, Germany Finanzagentur GmbH, Eurostat, OECD. *Dot highlight forecasts. BCA Economic Research. Actual data in EUR and GBP. Quarterly data from Q1-2008 to Q3-2024.

# The recent USD strengthening is especially harmful for Asia's anchor currencies

- The threat the upcoming US policy shift poses on the global economy (and even the US economy itself) has been accepted as a consensus, but nowhere has it become a more pressing problem than in Asian economies. Some anchor Asian currencies suffer from more significant depreciation pressure following the US election, as the risk of a renewed trade war lowers the sentiment on Asian countries' export-led growth strategy. The gigantic Chinese manufacturing sector underlines the scale of the problem, as the president-elect has put the threat stemming from the economy as the focus of the rhetoric that shapes his policy agenda.
- The worsening sentiment on East Asian economies stems beyond the macroeconomics realm. President Trump's quid-pro-quo approach to foreign policies has created a pressing security problem for many regional powers, which rely on the US military presence for their security. Trump's lower commitment to foreign treaties may force East Asian policymakers to funnel more funding for defence-related expenditures, adding to the fiscal burden with marginal boost to the economic growth momentum. European economies may also face the same dilemma, although the need to increase military spending may not be too urgent as most NATO members already fulfil its 2% defence spending commitment by 2024.

**Chart 2.11**

The downward trend in the USD index ends abruptly as the outcome od the recent US election brought uncertainties back to the global economy in general and Asian economies in particular.



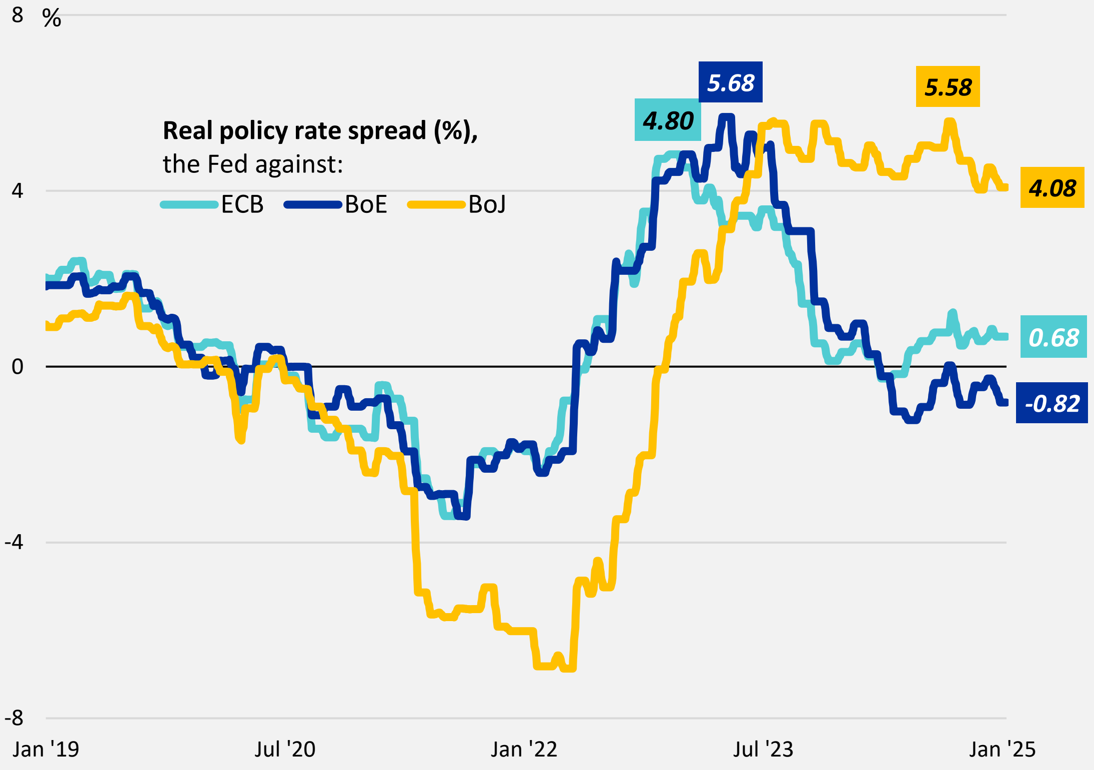

**Source:** Bloomberg, BCA Economic Research. YTD changes of cross rates. Data is valid as of 17 January 2025

# The stop-start approach for policy normalisation heighten the JPY's volatility

- While the JPY did not suffer from noticeable depreciation following the US election, the strengthening USD index ended the upward trend in the JPY/USD exchange rate in H2 2024.
- The downward pressure facing the JPY is further compounded by the BoJ's decision to halt its policy normalisation campaign, as the BoJ opted to keep its policy rate at 0.25% at the December 2024 meeting despite a rising inflation outlook (2.9% YoY in Nov-2024, up from 2.3% YoY previously). The ongoing domestic political crisis in Japan (following the ruling LDP party's abysmal election result) further obscures the BoJ's rate-hiking path.
- The looming global trade war has been noted as another reason behind the BoJ's decision to keep its policy rate lower for longer.
- However, this does not mean that the BoJ's policy normalisation agenda is already dead in the water. Governor Ueda has stated that the BoJ is nearing another rate hike, and the higher inflation figure should translate to higher wage growth in the upcoming *shunto* (wage negotiation) period. Indeed, wage growth (3.0% YoY median forecast) in Japan is expected to outpace inflation in 2025, providing support for domestic consumption that will justify the BoJ to push its policy rate to 0.50%.

**Chart 2.12**

Still-wide rate differences between the US and Japan compound the pressure on the JPY, but the gap should narrow as the BoJ is expected to continue normalising its policy rate in 2025.



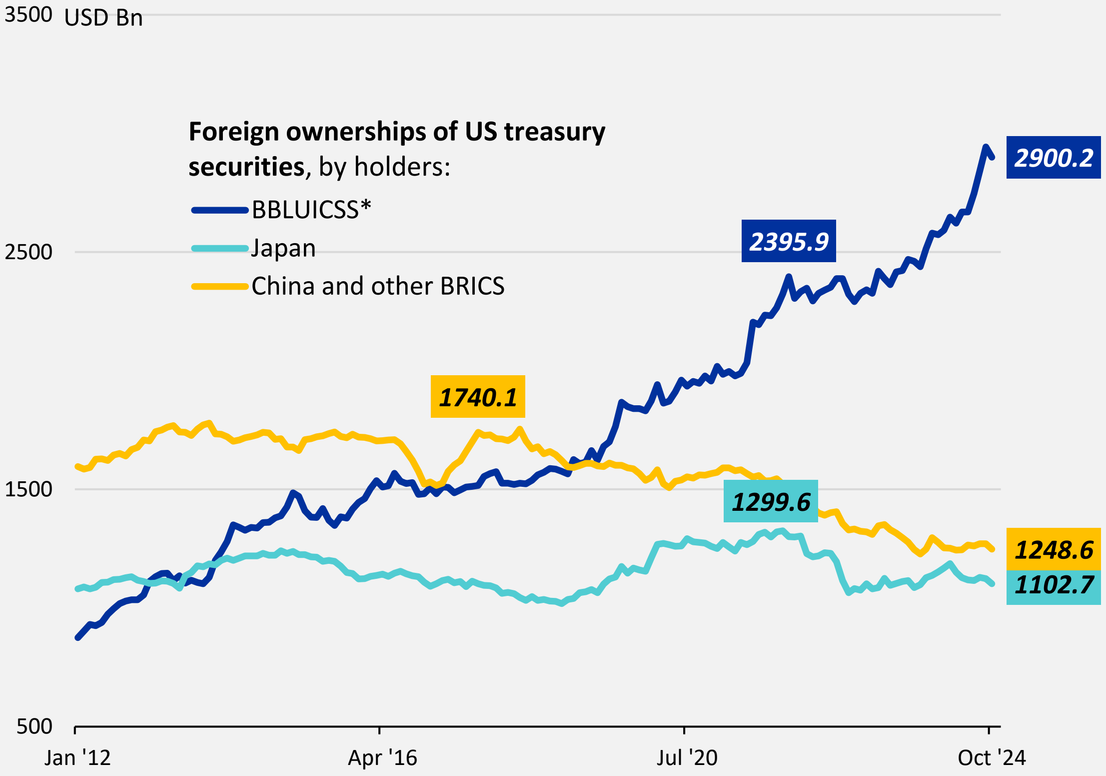

**Source:** Bloomberg, BCA Economic Research. Real rate is policy rate minus YoY CPI inflation. Daily data from 1 January 2019 to 17 January 2025.

# Returning private sector liquidity may protect the US from BoJ's policy normalisation

- **The BoJ's expected policy normalisation in 2025 presents a challenge for the UST market.** Previous BoJ rate hikes in April and July 2024 have coincided with periods of spiking UST yields, driven by the unwinding JPY carry trade. Further consolidation of BRICS (and its de-dollarisation agenda) may further reduce the global demand for UST amidst the backdrop of higher debt issuance and lower projected rate cuts in the US.
- Fortunately, **the expected decline in Japanese and BRICS demand for UST may be replaced by the higher demand from other private investors**, as indicated by the rising UST outstanding owned by investors in tax haven economies.
- The UST market may also see some pick-up in demand from corporate treasurers, as the planned effective corporate tax rate reduction to 15% (21% currently) would encourage companies to park their profits at home. **However, it remains to be seen whether the higher demand from private investors could meaningfully yank UST yields lower in 2025**, given the reasons we have described earlier (higher debt issuance and real rate expectations).

**Chart 2.13**

Japanese investors reacted to the end of NIRP by selling their UST holdings. However, the stable demand from tax haven economies helps to calm the market amid concerns over carry trade unwinding.




**Source:** Bloomberg, BCA Economic Research. Monthly data from January 2012 to September 2024 (last available data). *UST ownership by Belgium, Bermuda, Luxembourg, UK, Ireland, Cayman Island, Switzerland, and Singapore are aggregated as a proxy for UST demand from tax haven economies.

# Part 3: The China factor

*One does not simply spend massively, wisely*

***Chapter Summary***

- The looming trade war will hit the sentiment on the Chinese economy the hardest, meaning that **the RMB may continue to face significant downward pressure in 2025.**
- Further stimulus packages are to be expected in China, with the central government signalling its intention to issue more debt in 2025. However, **debt risk stabilisation may remain the focus for China's fiscal stimulus**, while the depreciation pressure on the RMB may only allow the PBoC to launch a moderate stimulus programme.
- Cheaper financing may allow Chinese manufacturers to operate at lower margins, meaning that **Chinese exports may remain competitive despite the threat of tariffs**. Hence, China may continue to export goods deflation worldwide, a threat to manufacturers globally.

***Implications to the Indonesian economy***

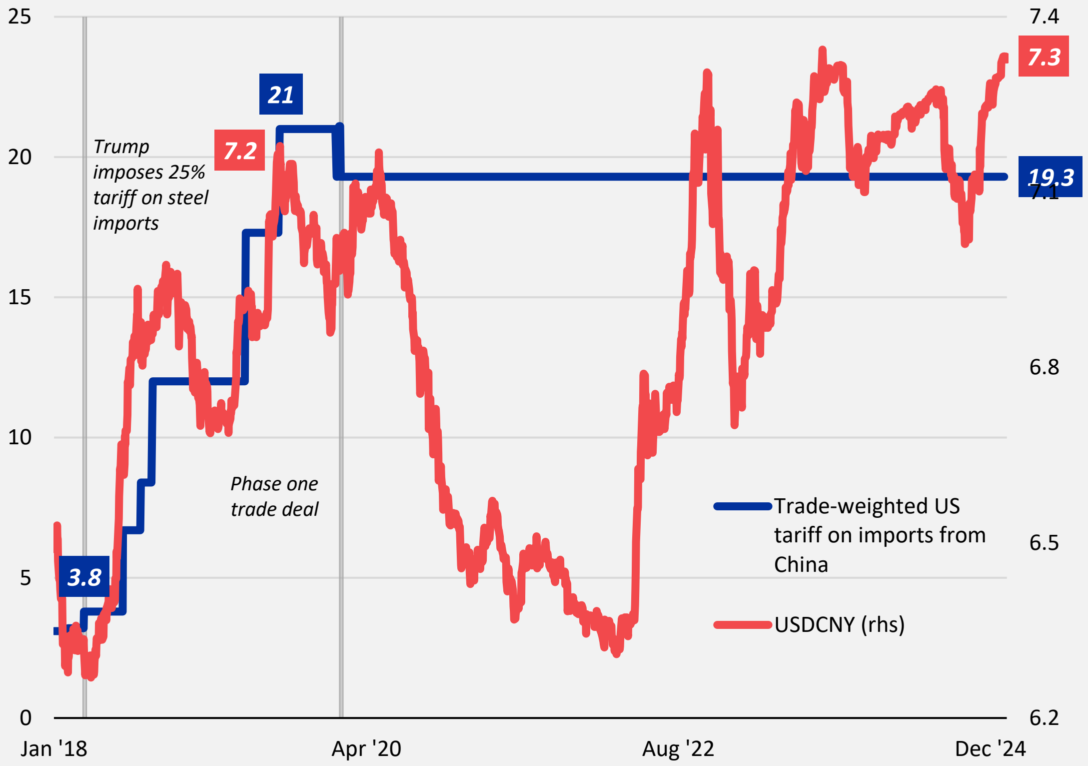
| Exchange rates | Current account | Growth potential |
|---|---|---|
| = | ↓ | ↓ |

# Anaemic domestic demand and less-friendly external conditions whipsawed China

- Another thing for Asian currencies to consider is the continued pummelling faced by the CNY. Monetary stimulus introduced by the PBoC early in Q3-2024 may have encouraged foreign investors to re-enter the Chinese market, but the condition in the real sector remains concerning. The economy may still cling to the 5% YoY GDP growth target, thanks to the strong export performance in 2024. However, The US government's combative trade policies are expected to close this external demand spigot, delivering a severe blow to China's export-led growth engine that did not help to improve the sentiment on the economy or other Asian economies.
- Domestic problems, of course, also continue to plague the Chinese economy. China watchers have anticipated that authorities will deliver a sizable stimulus package to boost the economy. However, **the CNY 10 Tn stimulus announced in October 2024 seems to be tuned to stabilise the financial sector, especially local government debts.** China's domestic demand may continue to suffer from anaemia, which, together with the less supportive external environment, may keep investors away from the Chinese market.

**Chart 3.1**

The CNY responded quickly to the announcement of higher US import tariffs, while a lull in the trade war often coincides with the period of strengthening CNY.




**Source:** PIIE, Bloomberg, BCA Economic Research. Daily data from 1 January 2019 to 17 January 2025.

# The property sector remains an urgent concern

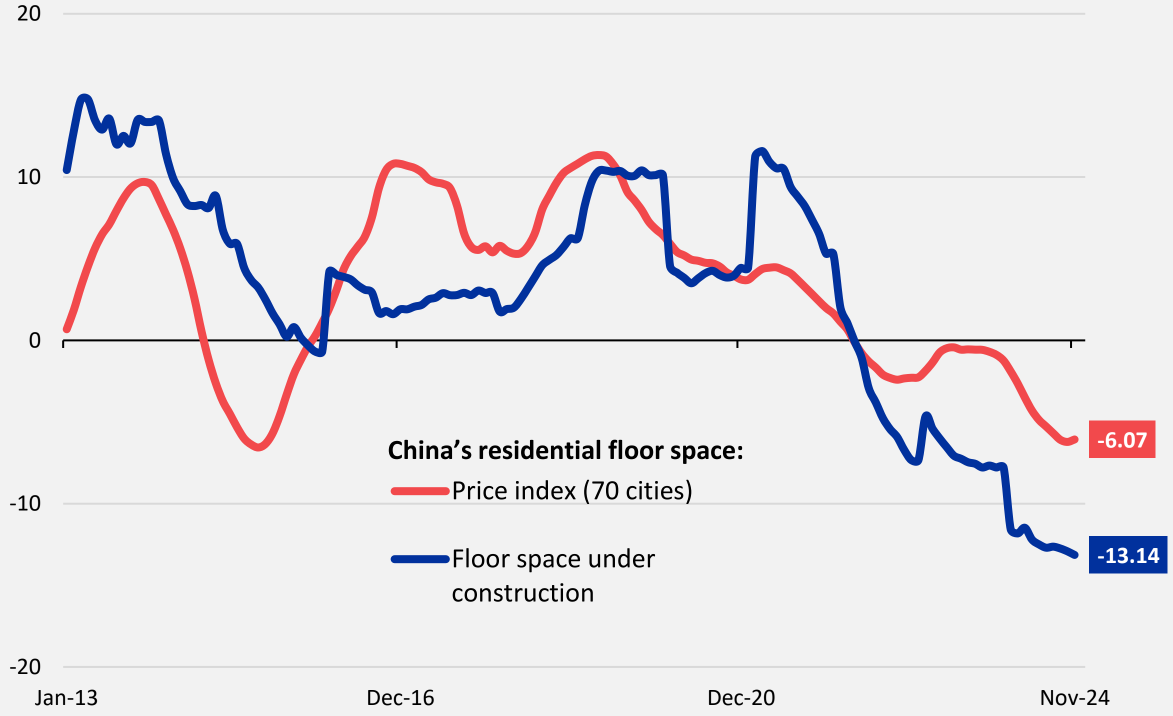
**Chart 3.2**

China's property supply overhang continue to widen in 2024 as government initiatives help developers finish stalled projects while sales remain subdued.


**Source**: Bloomberg, BCA Economic Research, monthly data from January 2013 to November 2024

**Chart 3.3**

At the same time, developers remain wary of launching new building projects as property prices continue to plummet.




**Source**: Bloomberg, BCA Economic Research, monthly data from January 2013 to November 2024

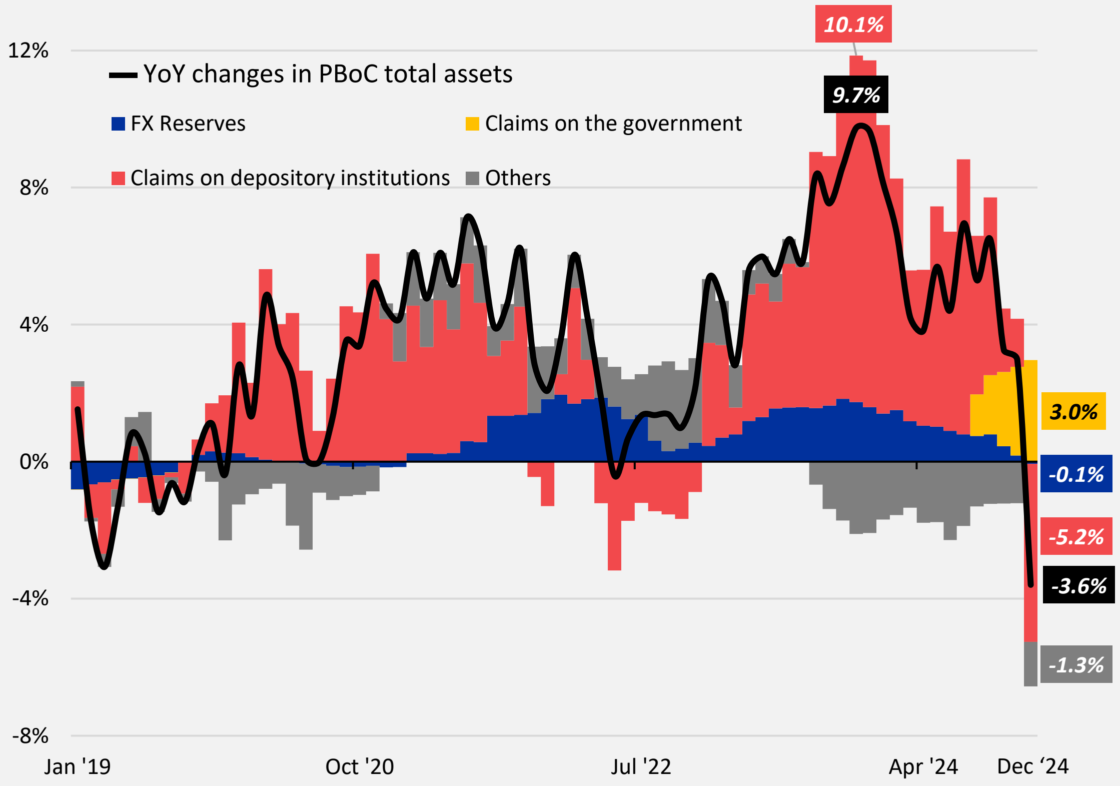
- The spiralling property sector is at the heart of China's domestic problem. Chinese authorities have implemented various measures to stabilise the sector, ranging from expanding the "whitelist" of existing real estate projects that are eligible for financial support to finish the project to reducing the 5Y LPR rate (benchmark rate for mortgage loans) to its record-low 3.60%. The intervention shows some results, with developers able to put more floor spaces for sales upon the project's completion. However, property sales are only slowly following the recovery, leading to a massive supply overhang that may still bring down prices and discourage developers from launching new projects in periods to come.

# The hitherto inefficient stimuli may compel China to double down on fiscal interventions

- External demand is expected to contribute positively to China's growth engine in 2025, as Chinese FDI may facilitate trans-shipments to the US market via third countries. Chinese invest-ments have also enlarged their exporters' market share in the Global South, while access to the European import market may remain open thanks to China's prowess with battery techno-logies.
- **The more pressing concern for China, however, is its weak do-mestic demand.** China's polit-buro has been calling for "more proactive" fiscal policies in 2025, with goals such as "vigo-rously boosting consumption" and "stabilising the property and stock market" also men-tioned.
- **The increase in the 2025 deficit target to 4% of GDP signals the readiness to adopt a more agg-ressive stance on fiscal inter-ventions.** China's plan to issue CNY 3 Tn in special treasury bonds is a welcome develop-ment, given its record-low bond yields.
- **Meanwhile, the PBoC may resort to a more modest stimulus in 2025.** The PBoC has lowered its policy rate (5Y LPR) to a record-low 3.60%, although with limited effect as loan growth continues to plummet. However, a more drastic policy loosening may exert downward pressure on the CNY, complicating the private sector's payment of their USD-denominated debts.

**Chart 3.4**

Monetary stimuli are insofar unable to re-energise money creation in China, necessitating the government to launch a sizable fiscal stimulus.

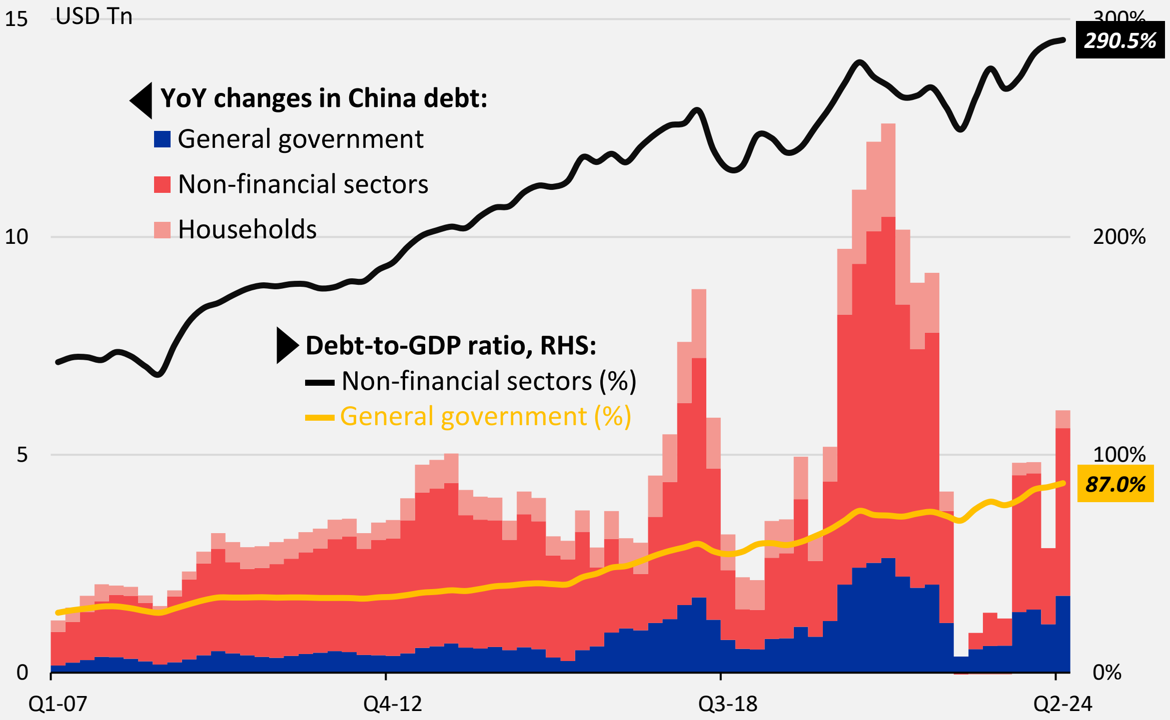



**Source:** People's Bank of China, BCA Economic Research.

# Debt concerns may remain the focus for China's fiscal stimulus

**Chart 3.5**

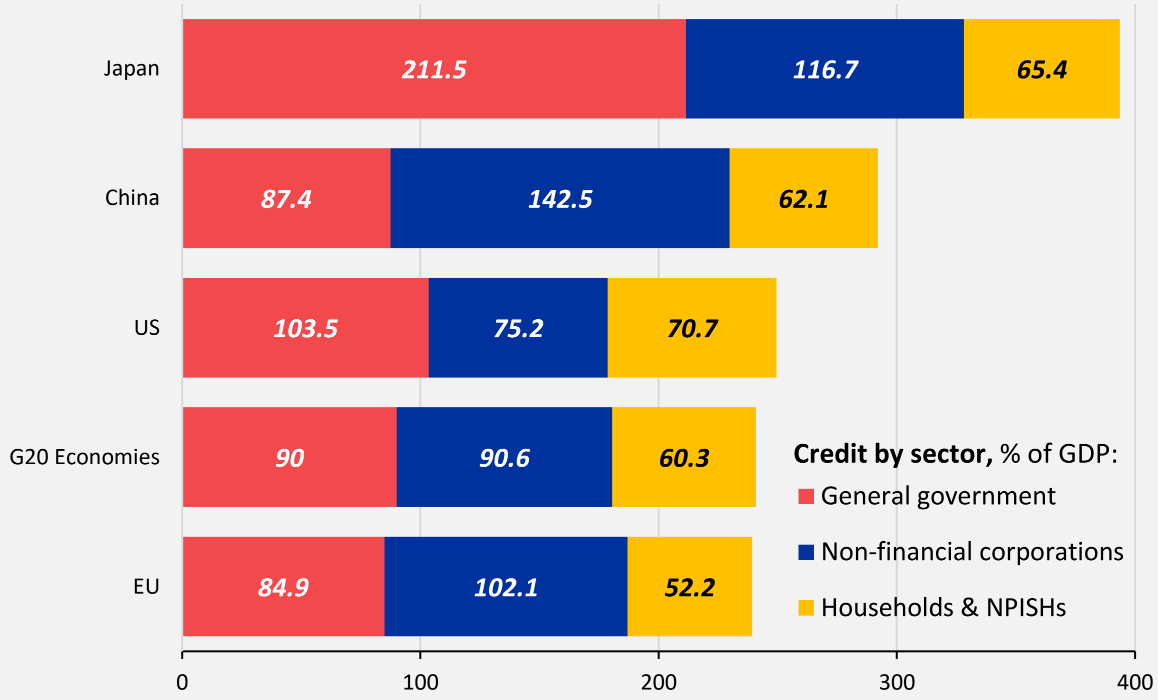
China's recent stimulus package is intended to put a guardrail around its highly-leveraged private sector, putting consumption lower in the priority list.




**Source:** Bank for International Settlements, BCA Economic Research. Annual changes of quarterly data from Q1-2006 to Q2-2024

**Chart 3.6**

China's problem with its highly-leveraged private sector is unique compared to other major economies, as the cleanup will require extraordinary expansion of fiscal debt



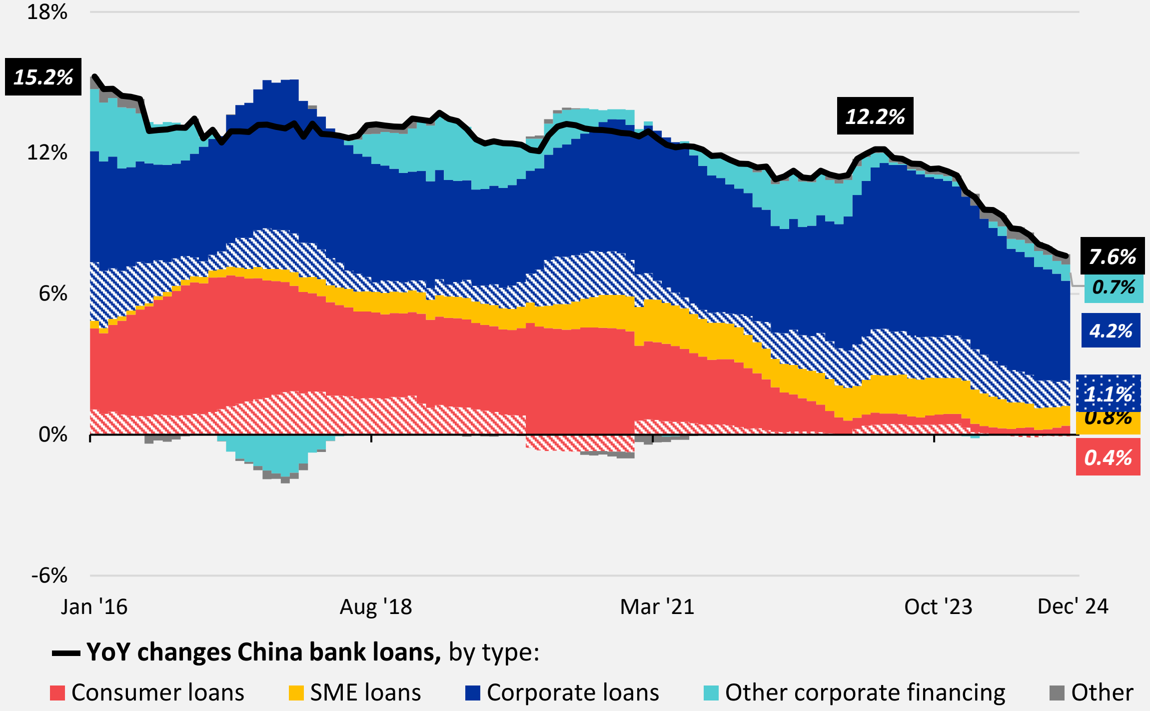

**Source:** Bank for International Settlements, BCA Economic Research. Q2-2024 data (last available data).

- Despite the commitment to launch another stimulus package, the biggest question remains whether the Chinese government will continue prioritising stability over the much-needed expansions. **Unlike other major economies, debt concentration outside of the central government complicates China's stabilisation plan, requiring policymakers to announce numerous programmes.** Indeed, Chinese authorities have announced a series of programmes amounting to RMB 14.3 Tn only to solve the problem of local government hidden debt, leaving less money in the deflation-breaker war chest for other, demand-side intervention programmes.

# China's lending remains concentrated in the manufacturing sector

**Chart 3.7**

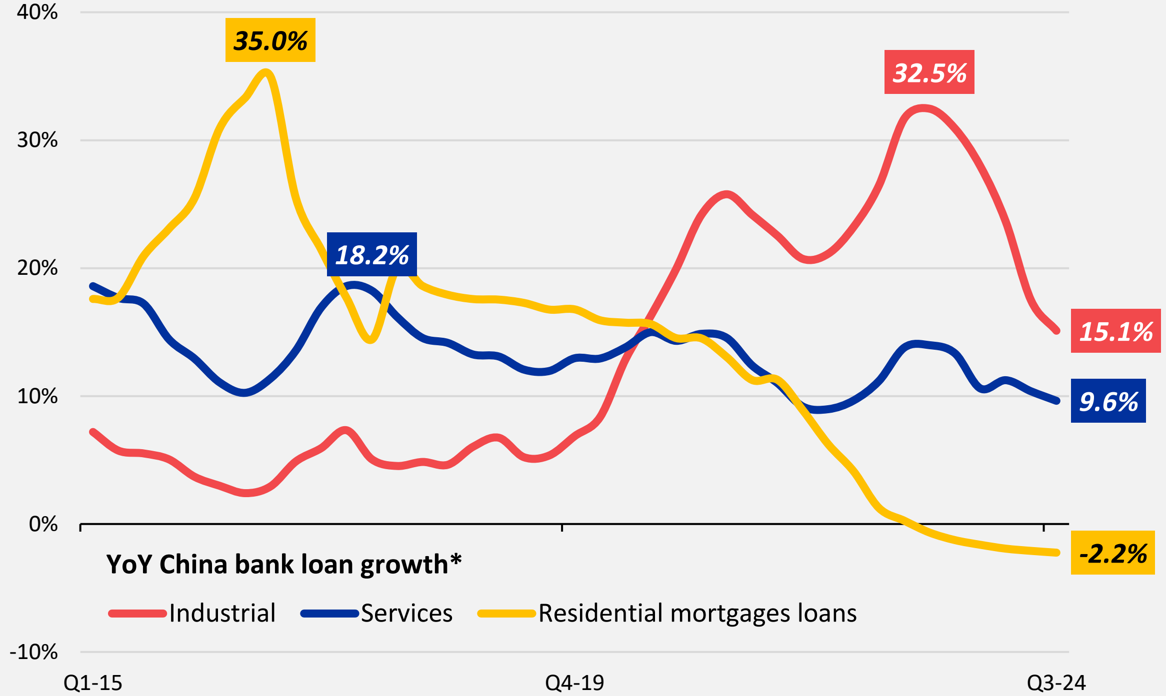
Chinese banks may not rely on the corporate sector to drive new loans, as the tariff threat haunt the Chinese industrial sector.




**Source:** People's Bank of China, BCA Economic Research. Annual changes of monthly data from January 2016 to December 2024. Patterned colour = short-term loans.

**Chart 3.8**

Chinese authorities cannot rely on other sectors but the manufacturing sector to drive the demand for bank loans as long as China's domestic demand remains muted.



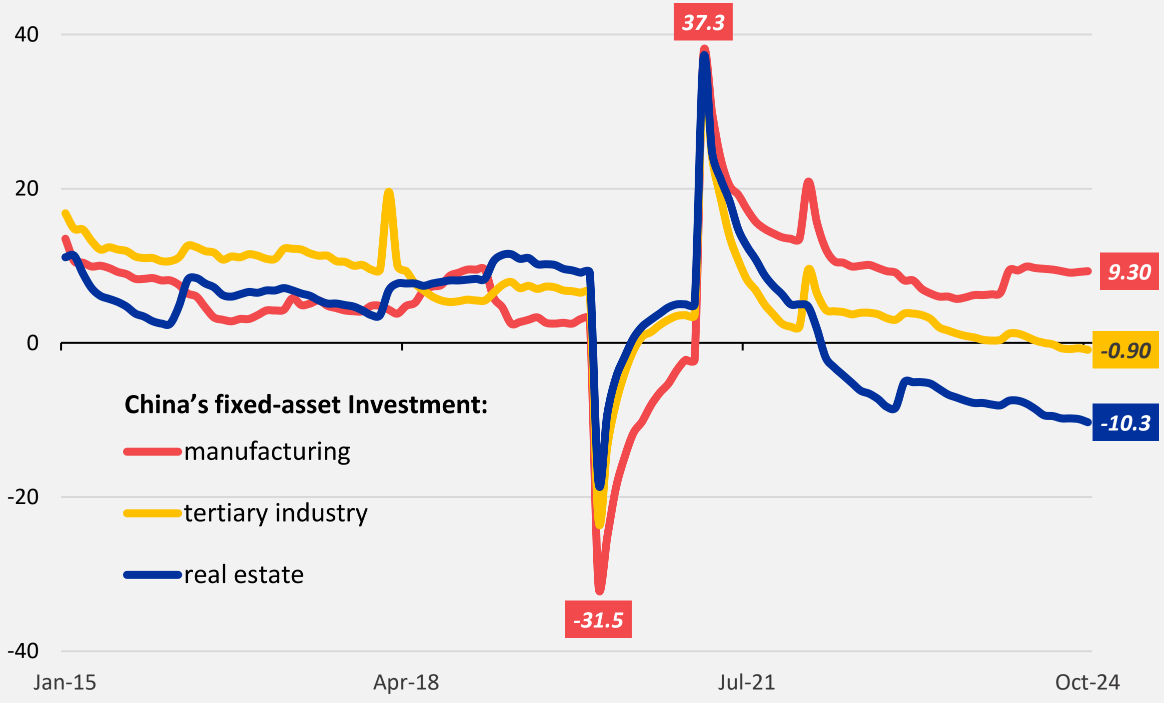

**Source:** People's Bank of China, BCA Economic Research. Annual changes of quarterly data from Q1-2015 to Q3-2024. *RMB- and FX-denominated loans, except for residential mortgages (RMB only).

- We could make the argument, of course, that a healthier balance sheet will allow businesses and other entities to soak up more loans and pursue another growth-driving venture. Alas, **opportunities to distribute the stimulus money are not clear to see.** The slowing sales growth, which hit even EV cars, indicates that the demand for consumer loans are non-existent, while the demand for loans from domestic-oriented sectors is stagnating at best. The export-looking manufacturing sector remains the cleanest shirt in China's dirty laundry. **However, given more stains on the industry amidst the looming trade war, it might be best to expect money creation in China to continue slowing in 2025.**

# China may continue to export deflation to the global economy…

**Chart 3.9**

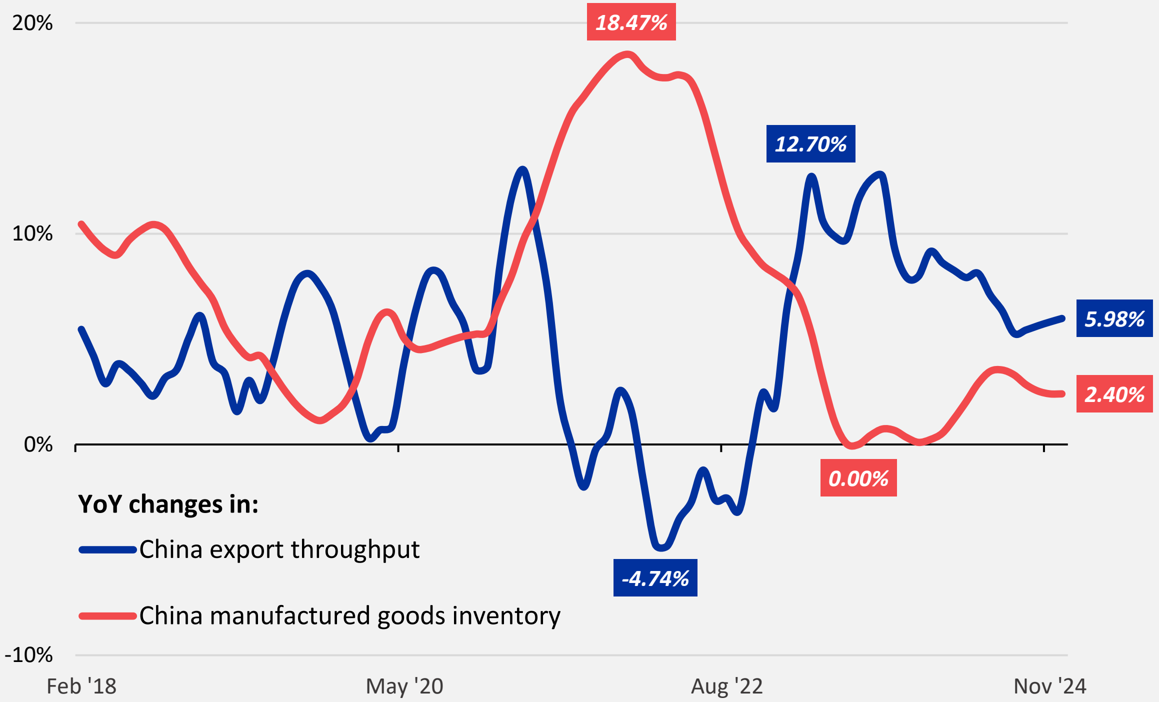
China's investments are diverging even further as weak domestic demand narrows their options, leaving manufacturing as the only viable choice.




**Source**: Bloomberg, BCA Economic Research, monthly data from January 2015 to October 2024

**Chart 3.10**

A higher export volume will be crucial to free up the space for Chinese manufacturers to expand their productive capacity while keeping their inventory level low.




**Source**: Bloomberg, BCA Economic Research, monthly data from February 2018 to November 2024

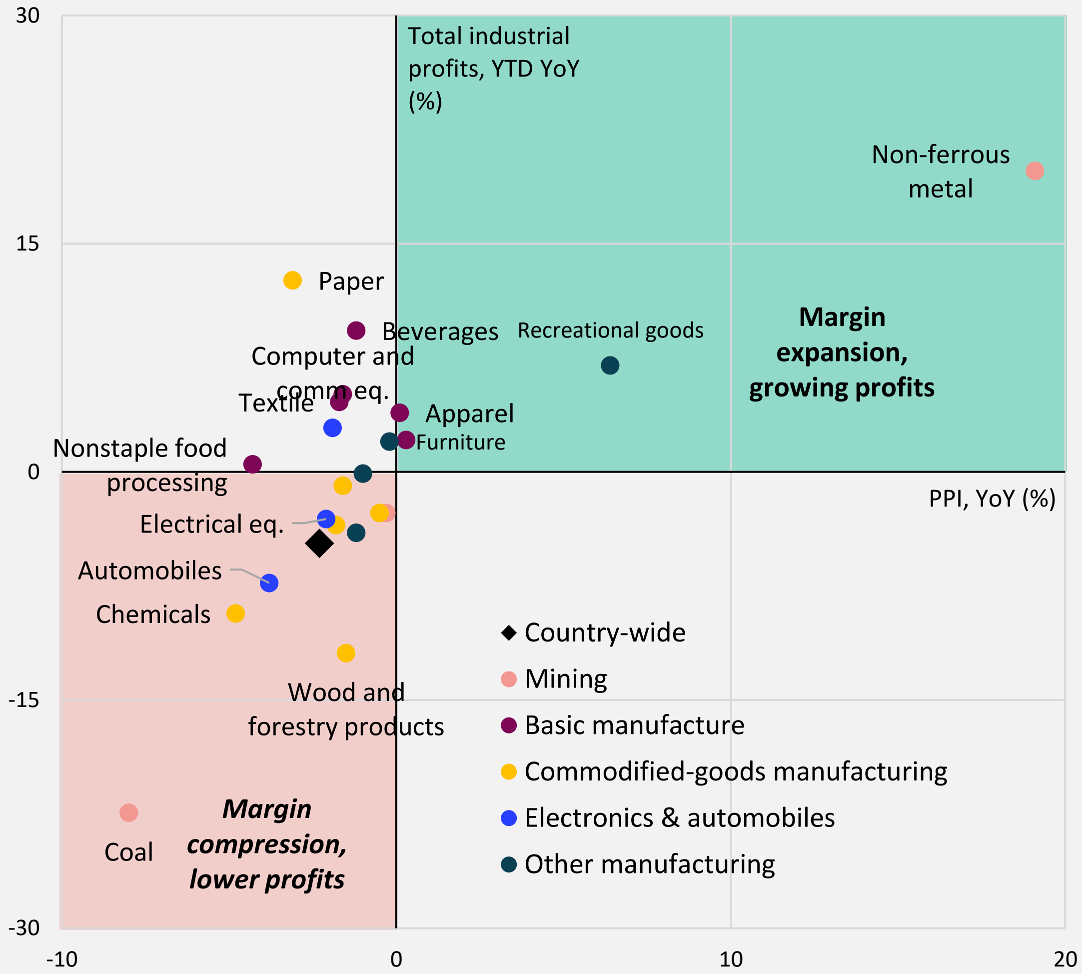
- The prospect of even cheaper financing in 2025 adds to the argument for Chinese manufacturers to continue their investment spree in 2025. This year is the final year of the "Made in China 2025" industrial policy, and the still-lagging development in crucial sectors such as semiconductor and aerospace engineering means that Chinese authorities will continue to pump liquidity into those sectors.
- However, the room for Chinese manufacturers to invest and expand may prove to be more limited. Continuing to expand despite the uncertain outlook for its export volume will only lead to swelling inventory, which may force Chinese manufacturers to firesale their products. The ongoing Chinese deflation, then, may continue to spread to the global economy, especially in tertiary markets (including Indonesia) that may not be able to put up import tariffs to guard themselves against the watershed of cheap imported goods from China

# …as margin advantage allows exporters to continue competing on prices

- Luckily, Chinese exporters may continue to benefit from a relatively healthy stream of external demand. Chinese manufacturers can tap into global export markets and maintain their expansionary trend in 2024 by lowering their margins and winning market share by effectively exporting factory price deflation to the global economy, a strategy enabled by the availability of cheap financing.
- The success of this strategy is particularly evident for manufacturers of consumer electronics (such as computers and communications equipment), which have managed to post positive profits in 2024 despite falling factory prices.
- The availability of even cheaper financing may allow Chinese manufacturers to take this this "sell cheap, sell more" strategy to the extreme in 2025, as Chinese exporters will need to further adjust their price points to attract price-sensitive customers the Global South.
- A weaker CNY will further boost demand for Chinese-made goods, which could help China's manufacturing sector remain relatively stable despite the overall poor sentiment. However, without a significant recovery in domestic demand, China's manufacturing sector will only expand by stealing growth from other manufacturers, which explains the worrying outlook for global manufacturing activity.

**Chart 3.11**

Cheap credit lines to the manufacturing sector may explain the continued manufacturing expansion in China despite the palpable margin and profit squeeze.



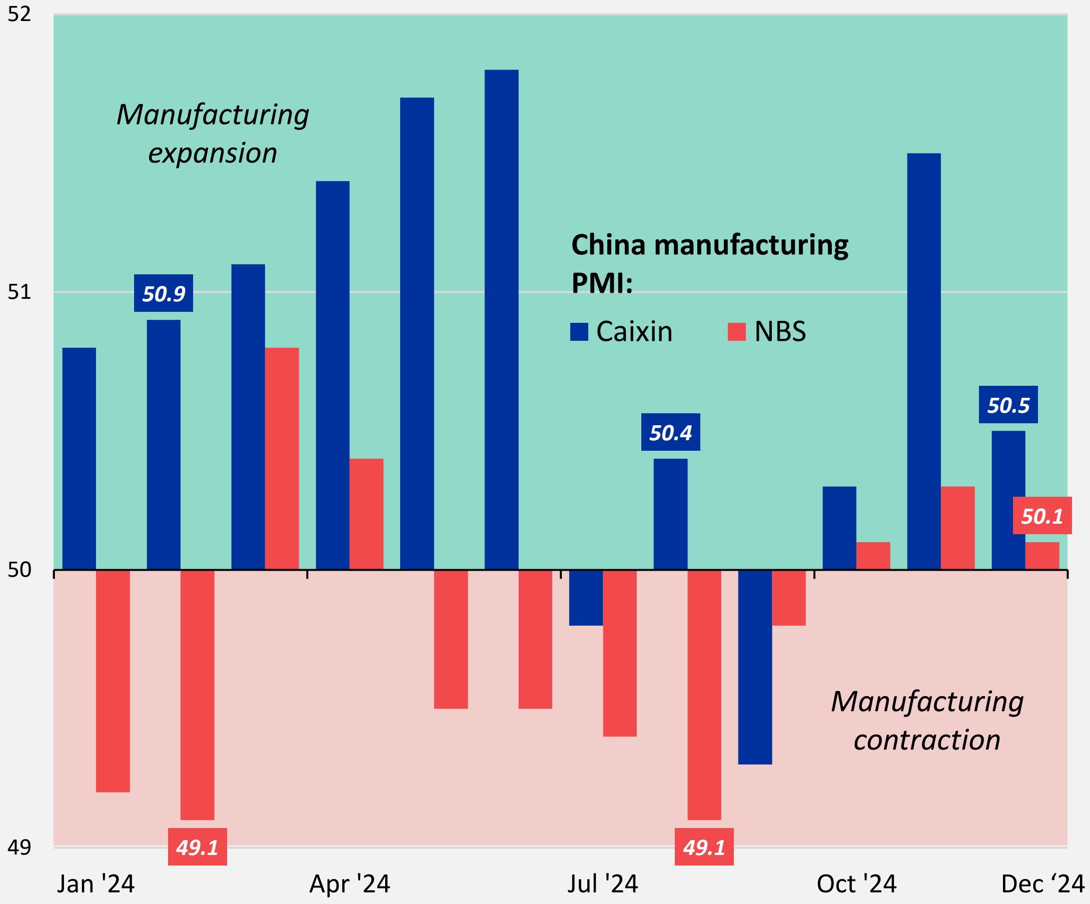

**Source:** Bloomberg, BCA Economic Research. December 2024 data

# Growth momentum in China may remain exclusive to some sectors

- It should be noted, however, that **China is not immune to the global manufacturing imbalance.** Indeed, China's two gauges for manufacturing activities (Caixin and NBS PMI) seldom move in the same direction in 2024, illustrating a sharp contrast of reality for businesses within China's highly segmented manufacturing sector.
- This bi-directional movement between export-oriented businesses (tracked by Caixin PMI) and more inward-looking industries (tracked by NBS PMI) may continue in 2025, albeit with smaller extremes (Caixin PMI once jumped to 51.8 in 2024 while NBS PMI succumbed to 49.5).
- Unfortunately, it is the export oriented Caixin PMI that may start to follow NBS PMI in 2025. Despite arguments laid earlier (*see p.25-27*), maintaining the same expansion momentum as in 2024 will be a tall task without the same degree of access to the US import market. In contrast, the NBS PMI may record a marginal improvement in 2025, depending on how far Chinese authorities will follow Politburo's messaging of using fiscal stimulus to vigorously boost consumption in 2025.

**Chart 3.12**

The PMI index that track export-oriented, mostly private companies stay in the expansionary zone for most part of 2024, unlike the index that tracks domestic-oriented companies.




**Source**: Bloomberg, BCA Economic Research, monthly data from January 2022 to December 2024, axis centered at 50; values above 50 indicate expansion, while below 50 indicate contraction

# High-tech sectors will remain as the main driver of Chinese growth

**Chart 3.13-14**

China's high-tech sectors continue to record higher outputs.

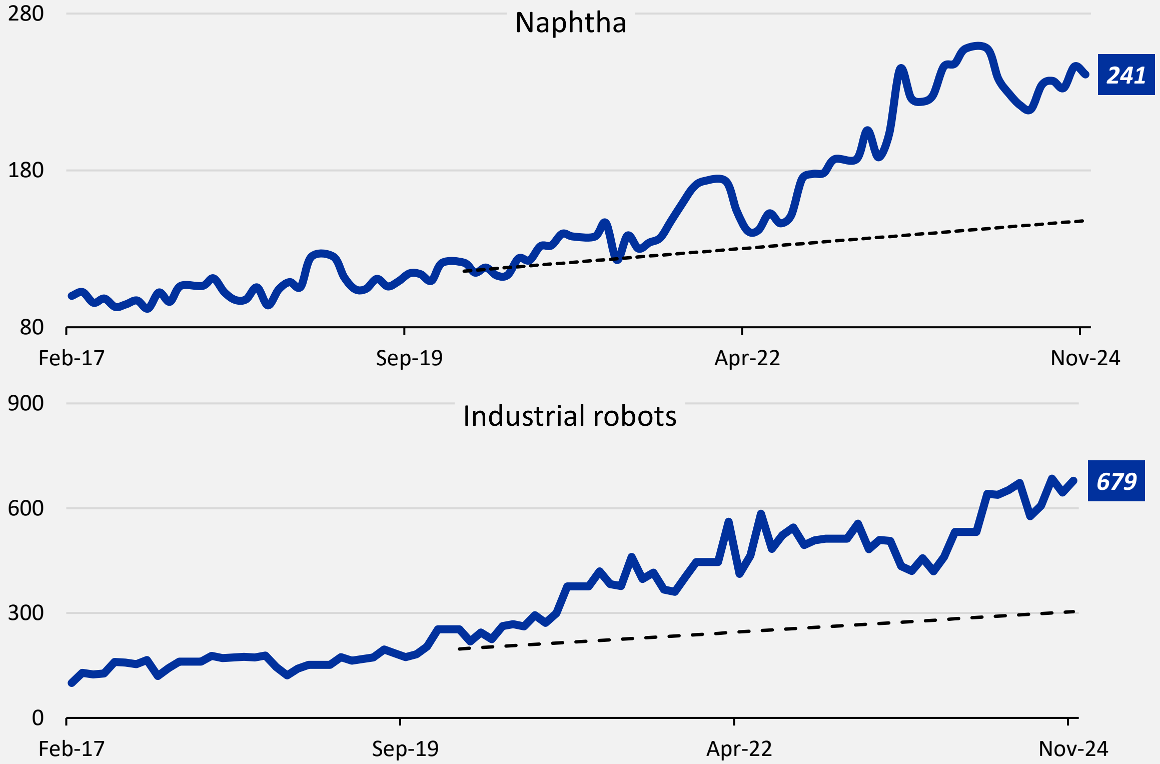
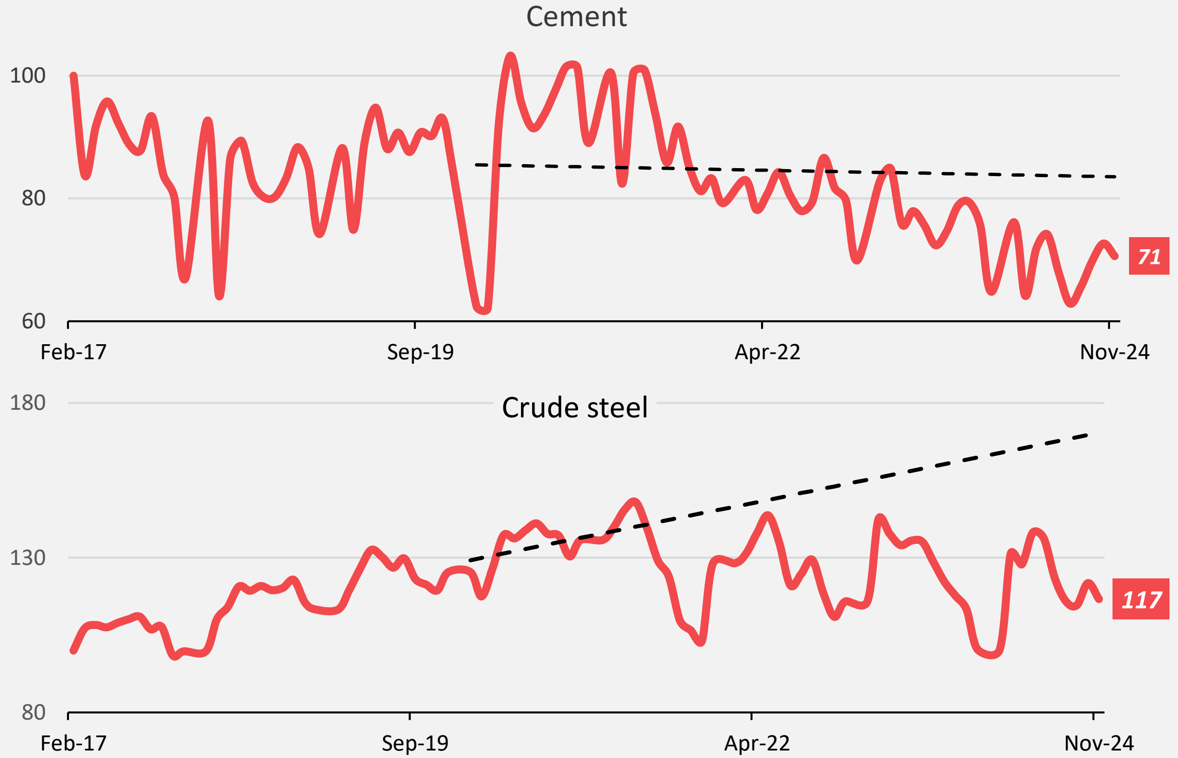



**Chart 3.15-16**

At the same time, certain energy-intensive industries are driving into the sunset.




**Source**: Bloomberg, BCA Economic Research, monthly data from February 2017 to November 2024, starting data indexed to 100

- China's industrial output remains supported by its strong production in advanced technology and petrochemicals, critical inputs for electric vehicles and solar panels. **Despite its green energy push, the country continues to rely heavily on petrochemicals and coal**, sustaining demand for oil and coal even as other industries face a slowdown.
- In contrast, **production in energy-intensive and polluting industries further plummets below its pre-pandemic trend**, which is especially evident for the production of housing materials as problems with the property sector persist. However, **the decline may also reflect China's outward FDI in these sectors**, which may continue to provide a lifeline for growth momentum in emerging economies (such as Indonesia) amidst the ongoing superpower competition that has insofar breath uncertainties to the global economy.

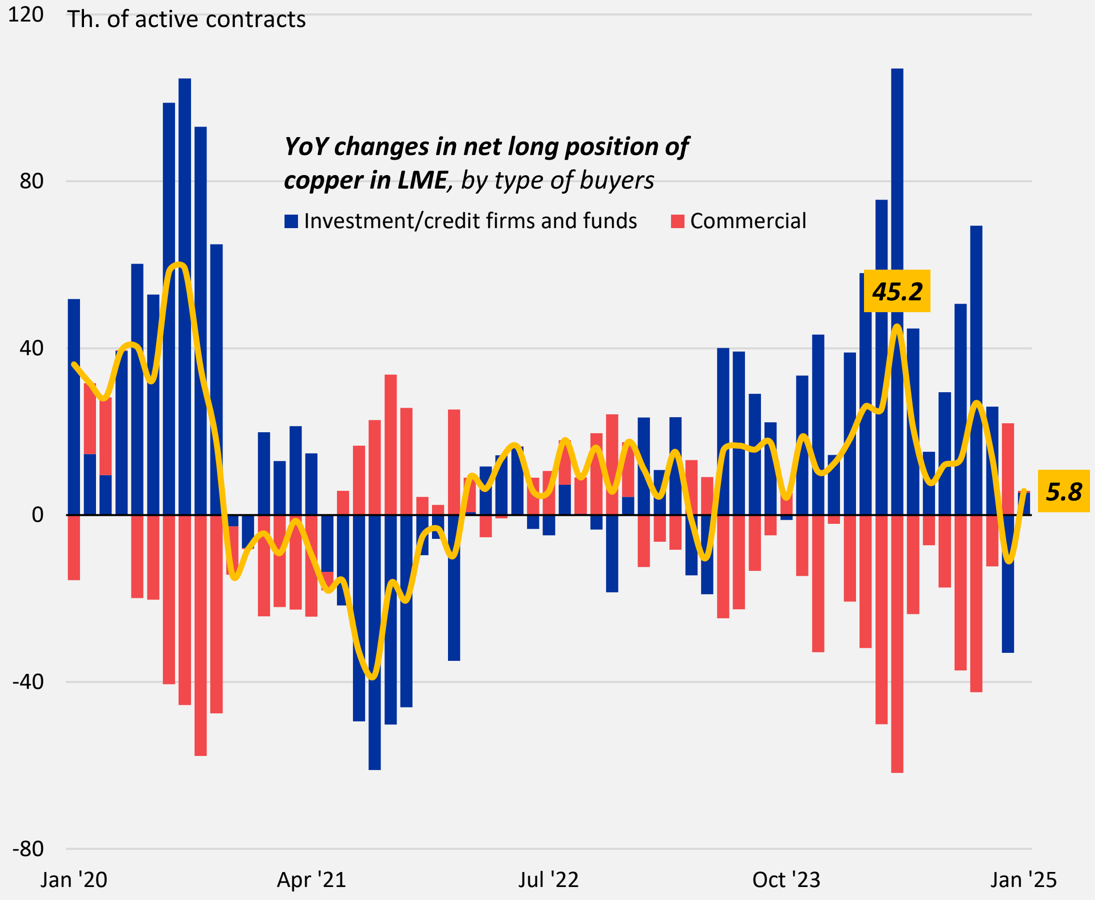
# Continued manufacturing expansion provides a floor for the global commodity demand

- Hence, while we maintain our relative optimism about China's manufacturing sector, how it translates to the demand for industry or energy commodities remains uncertain. At the present stage, it seems more likely for China to continue exporting deflation to the global economy, benefiting importers at the cost of lower manufacturing activities anywhere outside of China.
- As such, the continued global manufacturing imbalance means that the global demand for commodities in 2025 may remain largely stagnant. The slow recovery in commercial demand* for copper, the quintessential industrial raw material, reflects our less optimistic view on the global demand for commodities.
- More hawkish expectations on global liquidity following the US election also lower speculators' demand for commodities, which could send global commodity prices on a flatline trend at best. It is important, however, not to adopt a one-size-fits-all view of the global commodity market. For instance, lower yields amidst the increasingly volatile climate have sent prices of many tropical crops northward. Understanding how commodity prices may swing will be crucial in any study on how the global economic outlook will shift the Indonesian economy, given the increasing share of commodity-producing sectors in the economy's exports and GDP.

*A proxy for physical demand for commodities

**Chart 3.17**

Continued expansion in the Chinese manufacturing sector will be needed to sustain the improvement in the physical demand for industrial commodities.




**Source:** London Metal Exchange, BCA Economic Research. Annual changes of monthly data from January 2020 to January 2025. Net long position of commercial buyers indicate physical demand for commodities. Copper used as a proxy for industrial metals.

# Part 4: The commodity market

*A familiar fog*

***Chapter Summary***

- China's housing crisis continues to **weigh on industrial metal demand**, but prices remain supported by supply constraints. Meanwhile **coal demand persists** propped by the country's manufacturing in high-tech and green energy products. However, seaborne coal may face some challenges ahead.
- **Oil prices continue to weaken** amid moderating global activity, further pressured by Trump's tariffs. Geopolitical uncertainty and global slowdown continue to **push gold as a safe-haven asset** outside the US dollar, however price gains may be minimal compared to 2024.
- **Tropical crop prices are expected to slightly correct** after sharp increases in 2024. Prices remain supported by extreme weather patterns, particularly during the La Niña season.

***Implications to the Indonesian economy***

**Exchange rates**

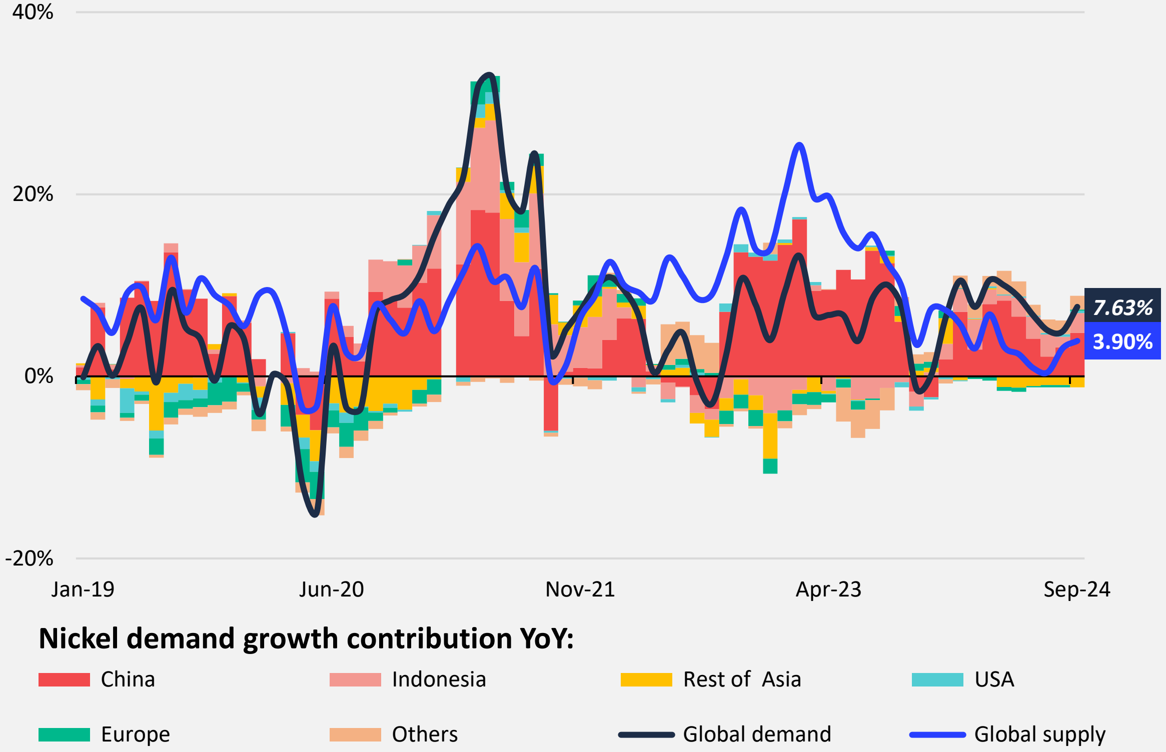
**Current account**

**Growth potential**

# Metal demand remains limited as China's slowdown continues

**Chart 4.1**

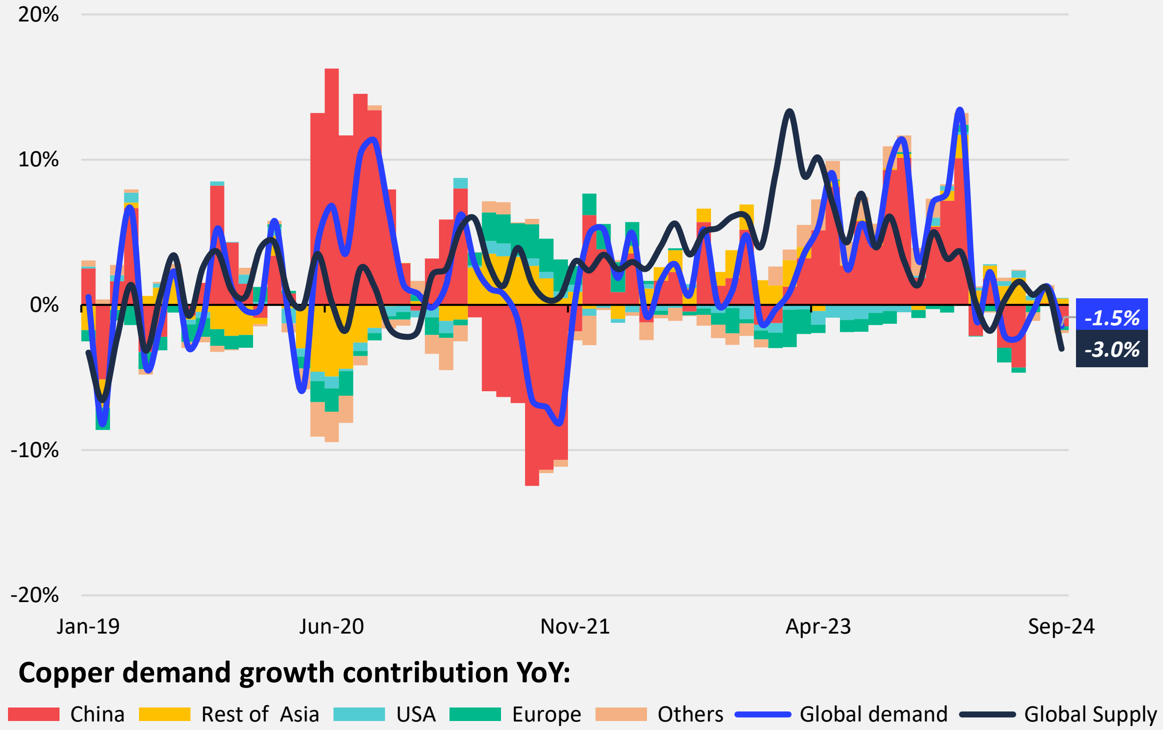
Nickel demand growth began to rebound late into the year, but prices have yet to reflect this recovery and continue to decline.




**Source**: Bloomberg, BCA Economic Research, monthly data from January 2019 to September 2024, February data removed due to abnormality

**Chart 4.2**

Copper demand continue to slump, but prices remain supported by a simultaneous drop in supply.




**Source**: Bloomberg, BCA Economic Research, monthly data from January 2019 to September 2024

- China, the world's largest consumer of metals, has long been a key driver of global metal demand. However, with its property sector in a protracted downturn, metal demand has significantly weakened, and recovery appears unlikely in the near term.
- While metal prices have stabilized, this is largely due to supply constraints rather than robust demand. Copper, in particular, continues to face weak demand as the downturn in China's property sector weighs heavily on consumption. Although nickel demand may show signs of growth, **its short-term price still depends on constraining supply**, while China's pivot to non-nickel battery technologies further burdens its long-term outlook.

# Sluggish demand puts oil prices in check

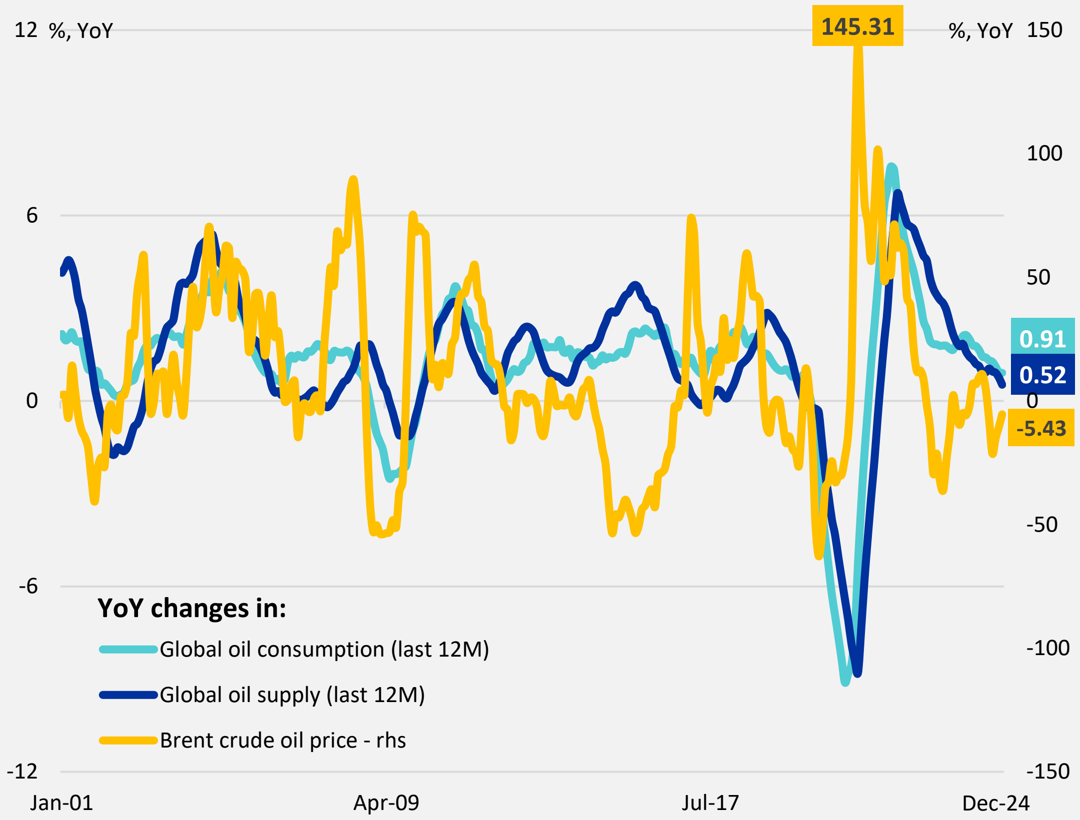
- The oil market in 2024 continues to face downward pressure, with prices declining in line with slowing global economic activity. Weak demand—particularly from China, the world's largest oil importer—remains a key factor. Slow demand has pushed OPEC+ to delay the start of its oil output increase until April 2025. Additionally, the group have extended its full production unwinding timeline to the end of 2026. This strategic move reflects OPEC's response towards persistently weak demand on a global scale and aims to prevent further downward pressure on prices.

- Despite heightened geopolitical tensions in the Middle East, oil prices have remained relatively stable throughout the year. This stability is largely due to conflicts occurring in areas that pose minimal risk to oil production infrastructure, reducing the immediate impact on global supply.

- Geopolitical shocks may, however, still trigger short-term price spikes, particularly with global oil inventories at their lowest levels since January 2017. However, **impact may be more controlled as robust production growth from non-OPEC countries**—led by the United States, which accounts for 90% of non-OPEC supply growth—has significantly added to global supply, keeping oil prices in check.

**Chart 4.3**

Oil prices have been declining, largely driven by a global economic slowdown that has dampened demand.



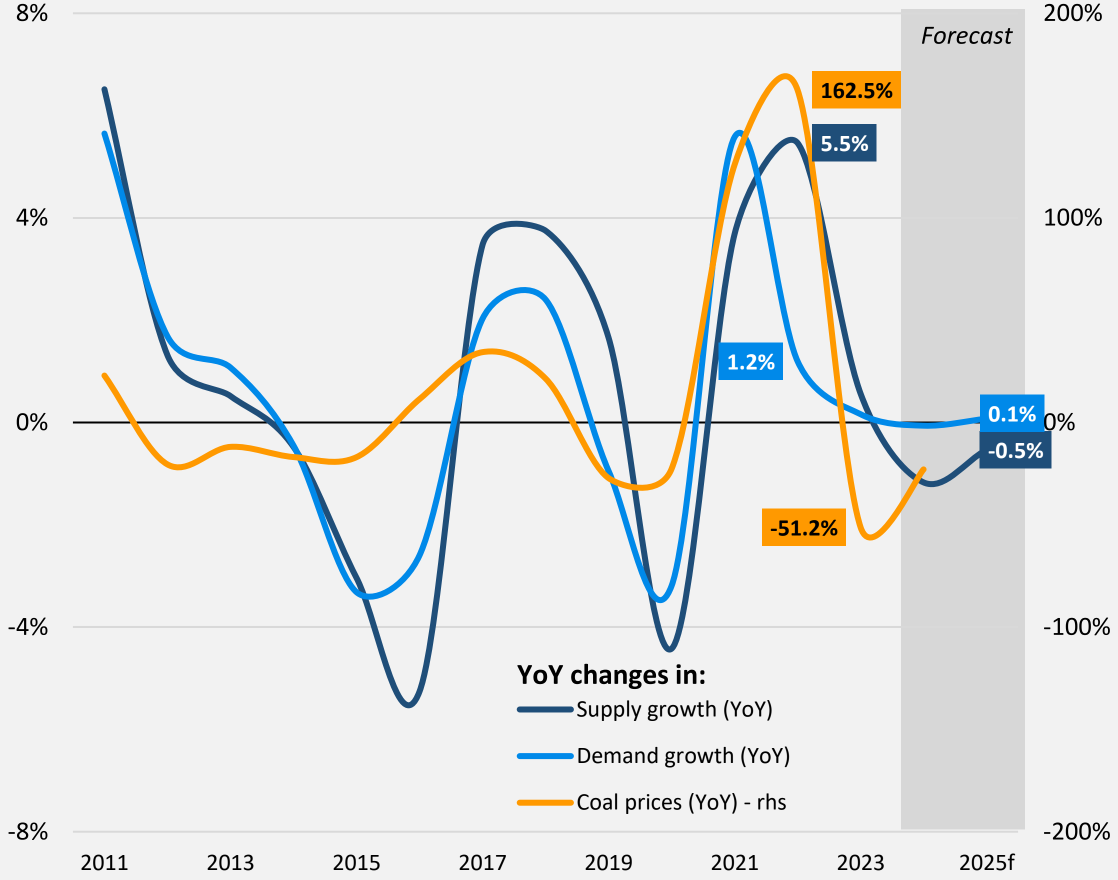

**Source**: Bloomberg, BCA Economic Research, monthly data from Jan 2001 to Dec 2024 , oil supply and consumption growth averaged from last 12 months.

# Coal demand has plateaued, but prices remain supported

- Coal demand has plateaued in 2024, as demand in advancing nation such as European Union and the United States have declined, driven by their transitions toward green energy and sluggish industrial activity throughout the year. Meanwhile, thermal coal demand from China still record a positive growth albeit at a much slower pace of 2.5%.
- Production mirrored this trend, with China, the world's largest producer accounting for roughly 50% of output, increasing production by just 2% in 2024. However, growing demand and production from developing nations, particularly India, offset these slowdown.
- Coal prices have receded from the highs of the energy crisis but remain well above pre-pandemic levels. This price movement continues to support strong earnings for coal exporters, as profitability endures despite tempered demand growth. However, another price surge akin to the energy crisis is unlikely under current market demand conditions.
- Heading into 2025, global coal demand is expected to remain steady, but with limited growth. Prices are likely to stabilize further, with both production and demand plateauing.

**Chart 4.4**

Coal demand has stabilized, followed by supply, while prices have declined but remain elevated above pre-pandemic levels.

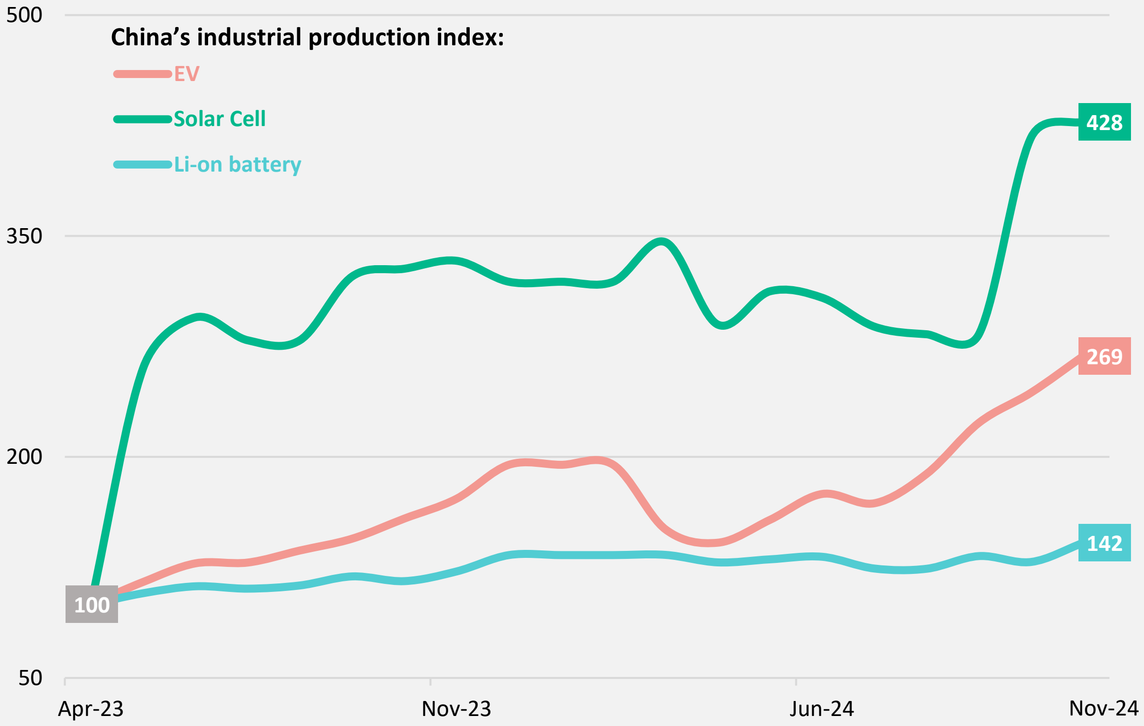



**Source**: Bloomberg, IEA, BCA Economic Research, monthly data from Jan 2011

# China’s ambition toward self-sufficiency boosted growth on clean energy sector

**Chart 4.5**

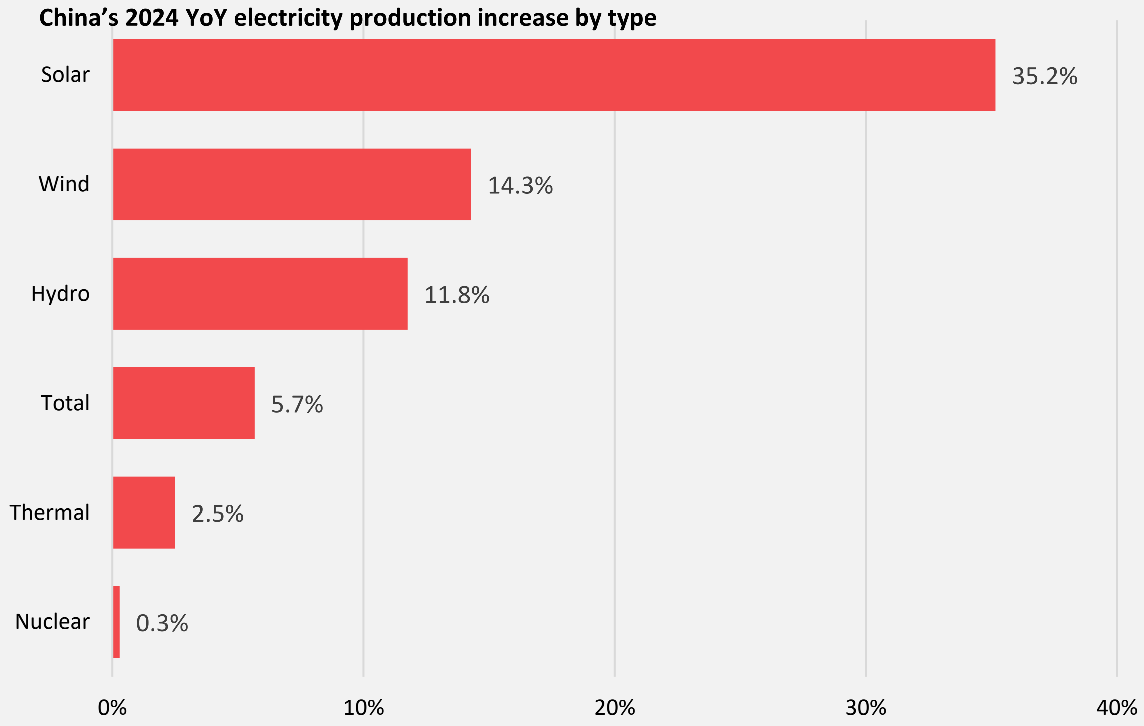
Continued government support on clean energy technology provide a strong manufacturing capacity in China’s “New Three” (Chinese: *Xin San Yang*).




**Source**: Bloomberg, BCA Economic Research, monthly data, April 2023 production indexed to 100

**Chart 4.6**

Strong growth in renewable energy output highlight China’s commitment to clean energy transition.




**Source**: Bloomberg, BCA Economic Research, monthly cumulative 2024 year on year data

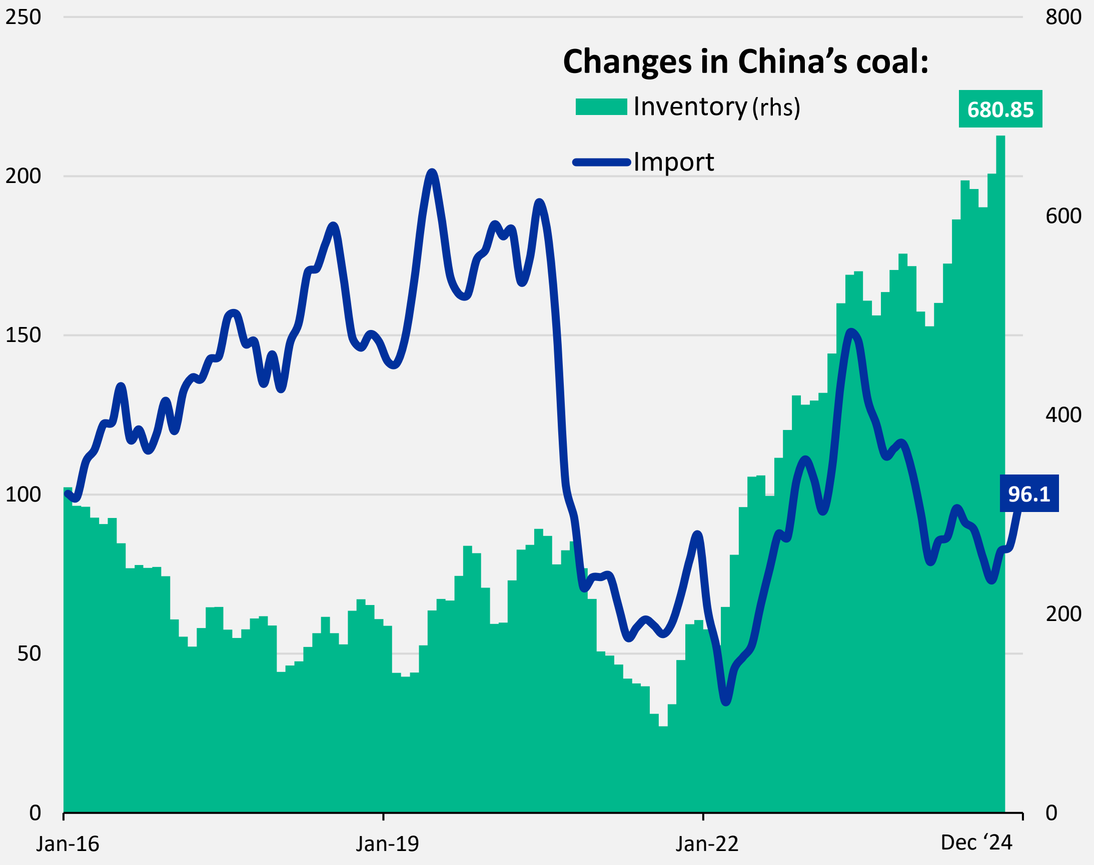
- Green energy investment has emerged as a crucial pillar supporting China’s sluggish economic growth, with manufacturing in this sector remaining strong. China accounts for 56% of the global installed solar capacity; this growth is not confined to China, as the rest of the world continues to expand rapidly, consistently exceeding analyst expectations.
- Despite this progress, thermal power generation continues to record positive growth, **indicating that coal sourced energy still plays a significant role in China's energy mix.** This dual development underscores the complexity of China's energy transition as it balances expanding renewable capacity with existing thermal power infrastructure.

# China's coal continue to stockpile

- China continues to play a pivotal role in shaping global coal prices. The country's Producer Price Index (PPI) slowdown, reflecting weak industrial demand, has been dragging coal prices lower.
- However, China's limited growth in coal output—at just 2.03% YoY (compared to 3.8% in 2023 and 11.47% in 2022)—prevents a significant price collapse. This stability is further supported by the growth in thermal electricity demand, which outpaces coal output at 2.5% YoY. Despite this, the small gap between output and demand also constrains any significant price recovery, particularly as China advances its transition toward green energy targets.
- Coal demand projections for China in 2024 might be underestimated due to stronger than expected manufacturing activity, which continue to expand by year-end. Paradoxically, as China scales up the production of green energy products, coal remains a critical, though temporary, input. Manufacturing these products still heavily relies on coal-fired power, especially given the energy intensity of production processes. **This dynamic ensures a steady demand for coal, including Indonesia's lower-quality thermal coal, into 2025.**

**Chart 4.7**

Although coal imports have slowed, much of the imported coal is being allocated to stockpiles rather than immediate use.

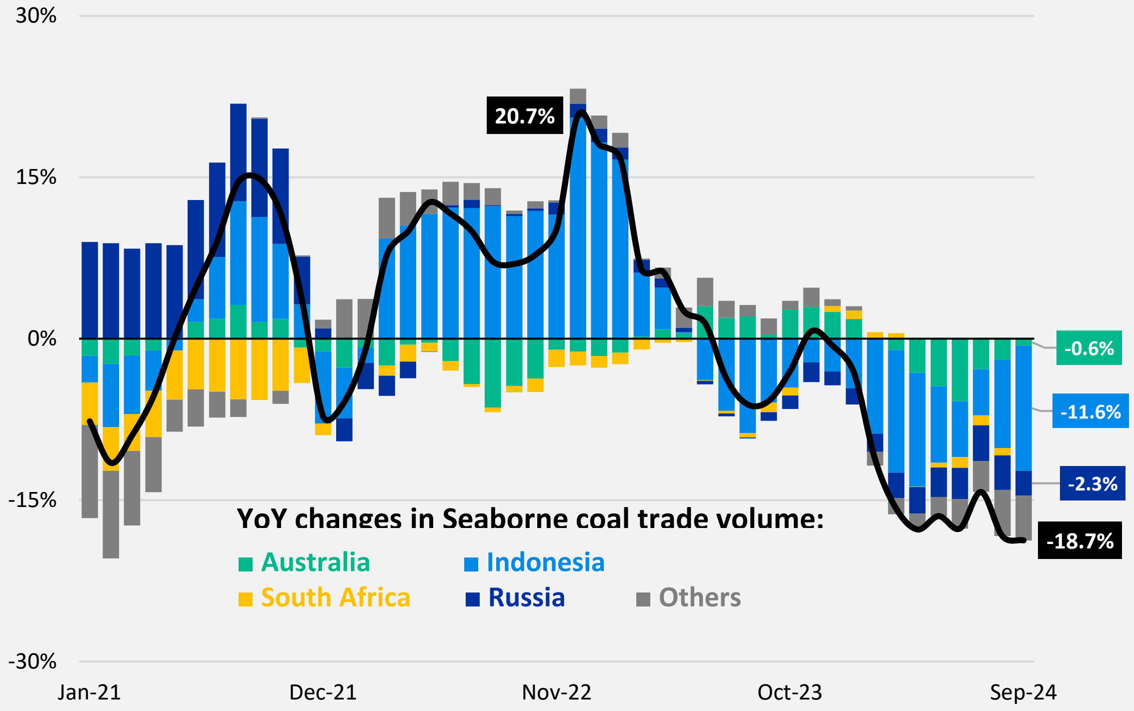



**Source**: Bloomberg, BCA Economic Research, monthly data, monthly data from January 2016 to December 2024 (latest data October 2024 for China coal inventory), monthly 12-week coal import average indexed to 100.

# Rising competition to seaboarne coal

**Chart 4.8**

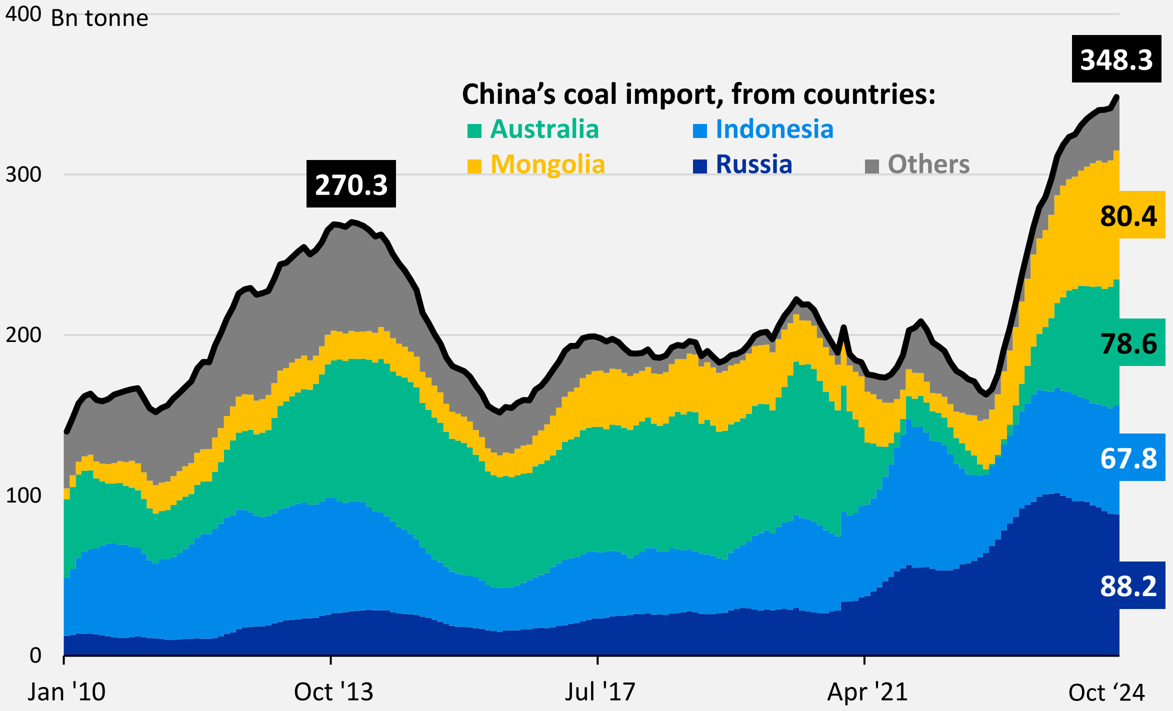
Seaborne coal trade experience a negative growth throughout 2024.




**Source:** Bloomberg, BCA Economic Research, monthly data from January 2021 to September 2024.

**Chart 4.9**

Mongolia's coal exports to China continue to increase after the construction of Shivee Kuren – Ceke rail in October 2023.




**Source:** Bloomberg, BCA Economic Research, last 12-month cumulative import data, monthly from January 2010 to November 2024.

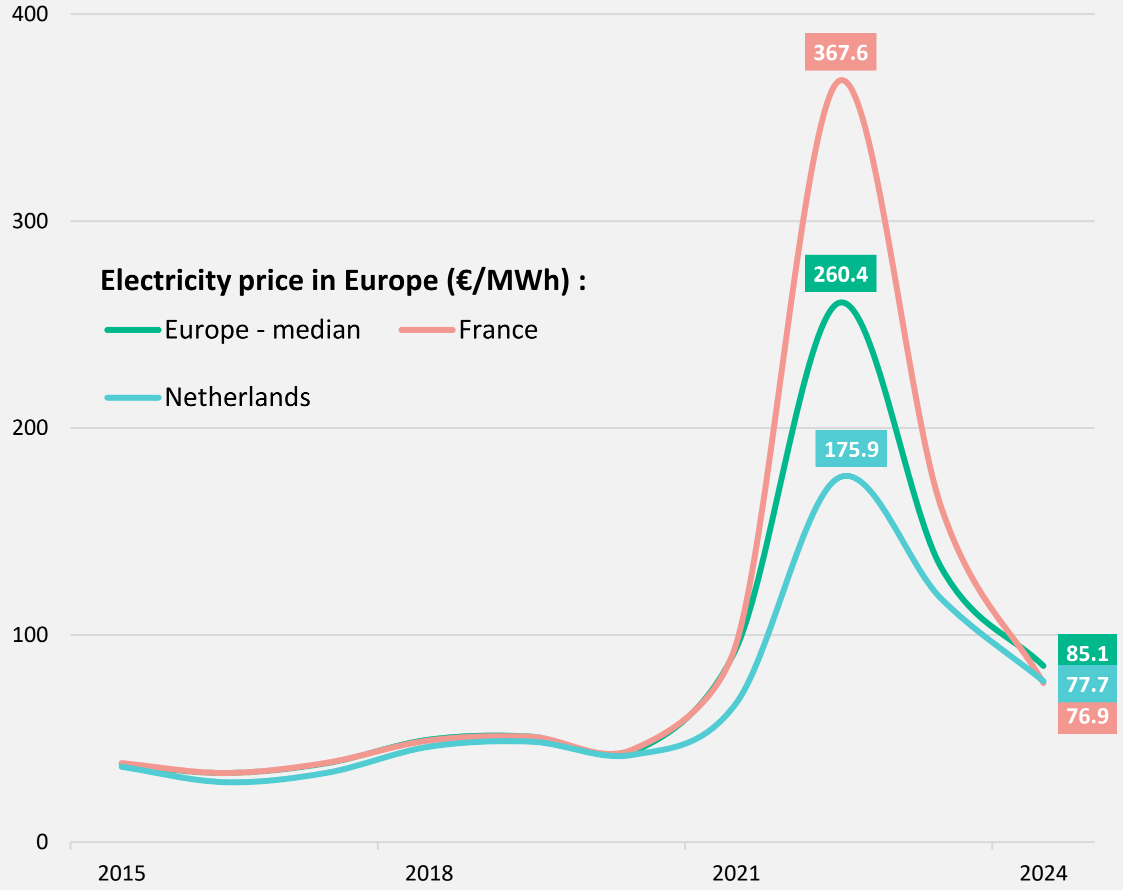
- Despite the potential for increased demand in China's imports, seaborne coal exporters face significant challenges, as seaborne exports declined in 2024. Improved railroad connectivity between China and Mongolia has bolstered coal imports from Mongolia, reducing reliance on seaborne shipments. Additionally, rising dry bulk shipping costs in late 2024 have added further pressure on seaborne exports.

# Europe's cheap electricity, another blow for seaborne coal

- Europe's extensive adoption of renewable energy has brought an unexpected challenge: electricity becoming excessively cheap. The intermittent nature of wind and solar power often results in supply surpassing demand, creating periods of abundance, even more than what their demand could absorb, where electricity prices drop to near zero—or even turn negative. This phenomenon was further amplified by a combination of strong wind, hydroelectric output, and abundant sunshine throughout the year in parts of Europe.
- The issue is further compounded by Europe's declining electricity demand. Despite the growing push for electrification, particularly in sectors like electric vehicles, electricity consumption in 2024 remains below 2020 levels. Reduced industrial activity and energy efficiency improvements, which have lowered overall power usage even amid efforts to electrify. Germany's manufacturing sector, for instance, ended 2024 on a notably weak note, with the HCOB Germany Manufacturing PMI falling to 42.5 in December

**Chart 4.10**

Electricity prices continued to drop all across Europe, although still higher than pre-pandemic level.



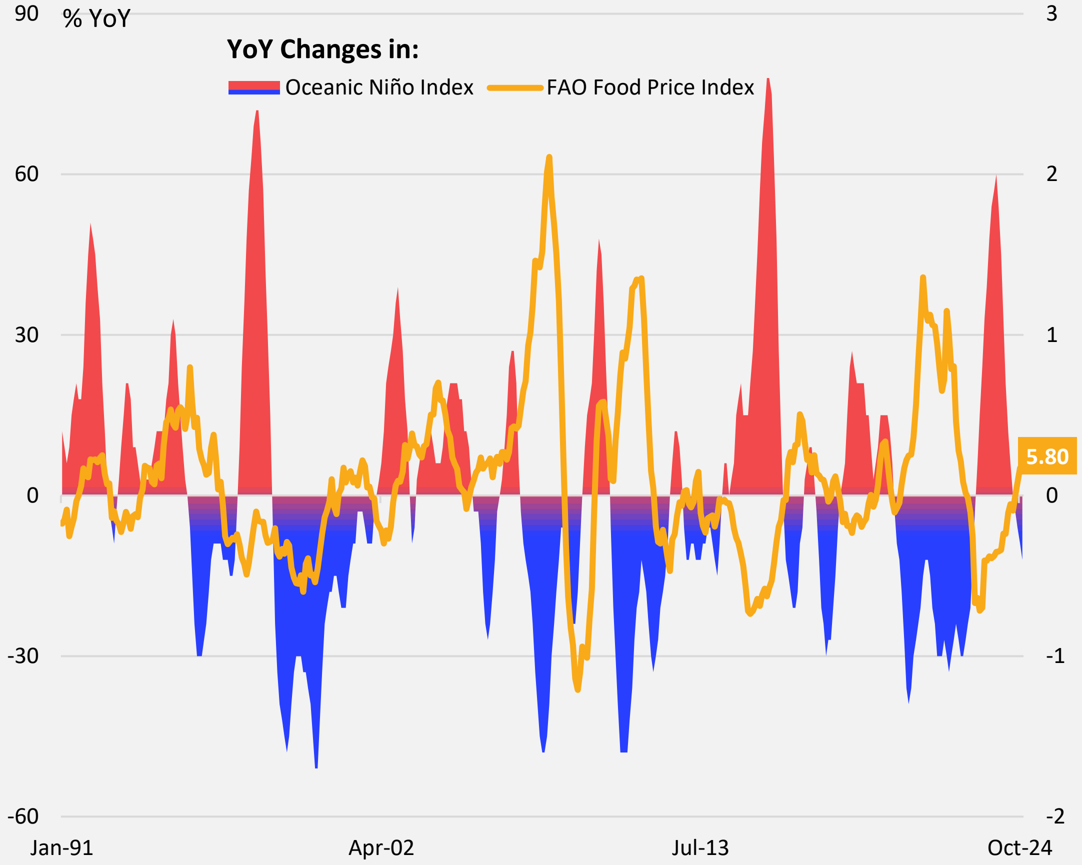

**Source:** Bloomberg, BCA Economic Research. Average yearly electricity price on selected European countries from 2015 to 2024.

# Food price to rise as global temperature entering La Niña

- Global temperatures are heading toward another La Niña season, which has historically driven food prices higher. South America is expected to face drier conditions, threatening the production of soybeans, corn, and wheat. At the same time, Southeast Asia, and parts of Africa are likely to experience heavier rainfall, disrupting key crops such as rice, palm oil, and sugar. These weather extremes are poised to tighten global agricultural supplies and fuel price volatility.
- Extreme weather conditions have influenced the prices of several tropical crops throughout 2024, driving notable increases in the prices of cocoa, coffee beans, and CPO.
- **An extreme La Niña event could sustain high prices into 2025**, particularly if it continues to disrupt crop production. However, excessive rainfall during this period could also negatively impact supply chains and harvests in affected regions. CPO's price is likely to benefit the most, as drought conditions in soybean-producing areas could lead to a slump in soybean oil production, a key edible oil alternative. This would drive further demand for CPO, allowing it to maintain its elevated price levels for a longer period.

**Chart 4.11**

Both La Niña and El Niño events frequently disrupt agricultural harvests, but La Niña tends to have a more disruptive effect on food prices.



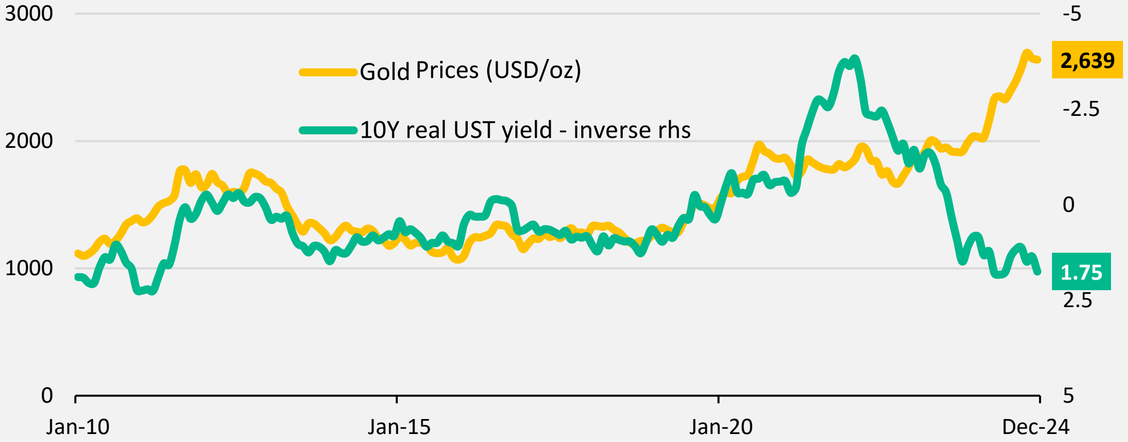

**Source**: National Oceanic and Atmospheric Administration (NOAA), food and agriculture organization (FAO), BCA Economic Research, monthly data from Jan 1991, a negative ONI index indicate temperature heading toward La Niña, a positive ONI index indicate temperature heading El Niño.

# The golden surge may continue in 2025, although at a slower pace

- Gold prices surged to record highs in 2024, defying the traditional gold-oil ratio and its inverse relationship with U.S. Treasury yields. Despite elevated yields, gold demand continued to soar, fueled by unprecedented geopolitical uncertainty. Meanwhile, oil prices remained stable as the global economy slowed, further shifting their historical ratio.
- Trump's outspoken criticisms of de-dollarization and proposed penalties have only amplified uncertainty, fueling fears of a potential crisis and driving gold purchases, which has disrupted the traditional gold-yield correlation.
- Efforts toward de-dollarization have driven BRICS+ nations to stockpile gold. While China initially appeared to slow its gold accumulation in 2024, a significant uptick in late 2024 signaled a renewed push heading into 2025.
- As we move into 2025, gold may be expected to extend its rally albeit to more limited extent, **due to China's intensified efforts to de-dollarize and persistent geopolitical tensions**. The main question mark now is about US yields: will high real yields force gold to fall, or is the high gold price pointing towards a future Fed capitulation to stagflation?

**Chart 4.12**

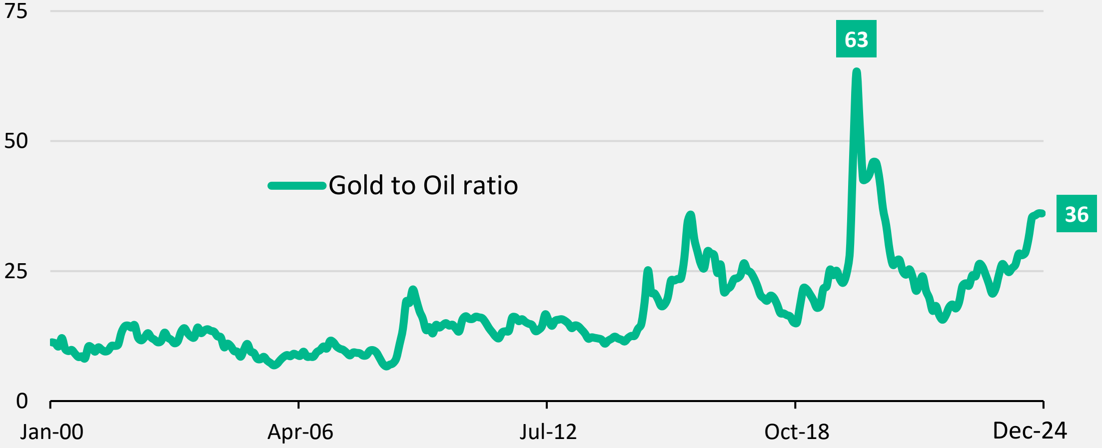
The 10-year U.S. Treasury yield remained elevated as expectations for Fed rate cuts have slowed. However, gold prices have continued to rise despite higher yields.




**Source**: Bloomberg, BCA Economic Research, monthly data from January 2010 to December 2024

**Chart 4.13**

The gold-to-oil ratio has reached its highest level outside the pandemic era, driven by low oil prices and the continued rise in gold prices.




**Source**: Bloomberg, BCA Economic Research, monthly data from January 2000 to December 2024

# 2025 commodity expectations

- **The outlook for industrial metals remains subdued** due to China's prolonged property sector downturn. However, demand for nickel and copper from the renewable energy sector, combined with controlled production limits, may prevent a supply glut and support prices.

- **Coal prices are expected to remain resilient, with limited potential for a small recovery.** Thermal coal remains crucial for energy-intensive manufacturing linked to renewable technology, which is anticipated to stay robust despite the proposed Trump tariffs.

- Gold is expected to remain as a safe haven in 2025 amid ongoing global geopolitical uncertainties. However, price increases may be more modest compared to 2024, as they face a higher base from previous gains. Even so, **further growth is possible as China continues to advance its de-dollarization efforts.**

- **Oil prices are anticipated to stabilize as global activity continue to moderate**, further dampened by Trump's tariffs. While geopolitical tensions, particularly in the Middle East, could spark temporary price spikes, these are unlikely to be sustained, echoing 2024 trends.

- **Tropical crops may experience slight price corrections in 2025** following sharp increases in 2024. Nonetheless, prices are expected to remain elevated compared to 2023 and early 2024, supported by robust demand and ongoing supply disruptions due to uncertain weather conditions.

- Corrections in tropical crop prices, though remaining elevated, could provide Indonesia with a competitive edge. At the same time, stabilizing oil prices may offer a degree of economic stability. However, limited gains in metals, especially amid persistently weak demand, are likely to present a significant challenge as Indonesia navigates 2025.

| Commodity | Unit | Spot | Futures | Bloomberg |
|---|---|---|---|---|
| Coal (Newcastle) | USD/MT | 126.75 | 137.22 (+8.26%) | 138.28 (+9.10%) |
| CPO | RM/MT | 4935 | 4155 (-15.81%) | 4667 (-5.44%) |
| Gold | USD/oz | 2632 | 2762 (+4.94%) | 2786 (+5.82%) |
| Copper | USD/MT | 8951 | 9153 (+2.26%) | 10046 (+12.24%) |
| Nickel | USD/MT | 15477 | 16104 (+4.05%) | 16971 (+9.66) |
| Oil | USD/bbl | 73.32 | 70.12 (-4.36%) | 73.60 (+0.38%) |

Source: Bloomberg, spot price, Q4 2025 futures, and analyst mean forecast as of late December.

# Part 5: Scenario analysis

*Another global storm for Indonesia?*

***Chapter Summary***

- **External conditions are unlikely to benefit Indonesia in 2025**, given the expected flat demand for commodities and still-high global interest rates thanks to the higher debt issuance and limited room for additional rate cuts in the US.
- **The US economy's inability to withstand higher interest rates may turn things for the worse for the global economy and Indonesia**, especially if inflationary pressures continue to block the Fed from re-commencing its rate-cut campaign.
- **A sizable stimulus package in China, enough to rejuvenate its domestic demand, will be crucial for Indonesia to improve its growth momentum in 2025**, given its spillover effect on the global demand for commodities that will provide Indonesia with enough liquidity to pursue its pro-growth agenda.

# 2025 scenario: Dark clouds here and there

## **Worst case** scenario*

***How things may unfold:***

- **UST yields rise even higher** due to lower foreign demand amidst uncertainties due to US policy shifts, **resulting in lower growth environment even in the US** as the slowing loan growth dragged households' consumption.
- Inflationary pressures in the US due to the higher import tariffs and tighter labour market prove to be significant, **forcing the Fed to abandon its rate cut campaign in 2025**.
- Further interventions in China helps to stabilise its debt problem, **but the domestic demand condition is still timid as liquidity fails to reach the consumer sector.**
- **Commodity prices remain muted** as weak manufacturing activities lower the demand for commodities, **apart from energy prices** (primarily oil) as geopolitical tensions continue to threaten supply while the US fails to increase production .

## **Baseline** scenario

***How things may unfold:***

- Higher debt issuance due to TCJA provisions (along with additional cuts) continue to **boost the US economy and keep long term interest rate high**. However, the demand for USTs remain stable thanks to the demand from private investors.
- **Returning inflationary pressures forced the Fed to stick with its 50 bps FFR cut signal**, as the relatively high USD value will be needed to lessen inflationary pressures due to the higher import tariff.
- Further interventions in China helps to stabilise its debt problem, **although the domestic demand condition remains timid apart from subsidised goods such as EVs.**
- **The global manufacturing imbalance subdued commodity prices**, apart from episodic supply-driven price increases for some commodities (such as tropical crops).

## **Best case** scenario*

***How things may unfold:***

- **Better fiscal efficiency and more revenue raised from the higher import tariffs** help to fund President Trump's pro-growth agenda, **lowering US long term interest rates** as foreign demand for USTs also remain stable.
- The USD's relative strength lessens inflationary pressures due to the higher import tariff, **allowing the Fed to shift its focus to alleviate the increasingly palpable liquidity concern in the financial sector.**
- Sizable interventions in China helps to stabilise its debt problem, **allowing local governments to look for investments thanks to its recovered balance sheet.**
- Global manufacturing activities start to recover as consumer demand in China recovers, leading to **a more stable demand for industrial raw materials and other commodities.**

**Implications** for Indonesia

Worst → Better → (Baseline) → Better → Best

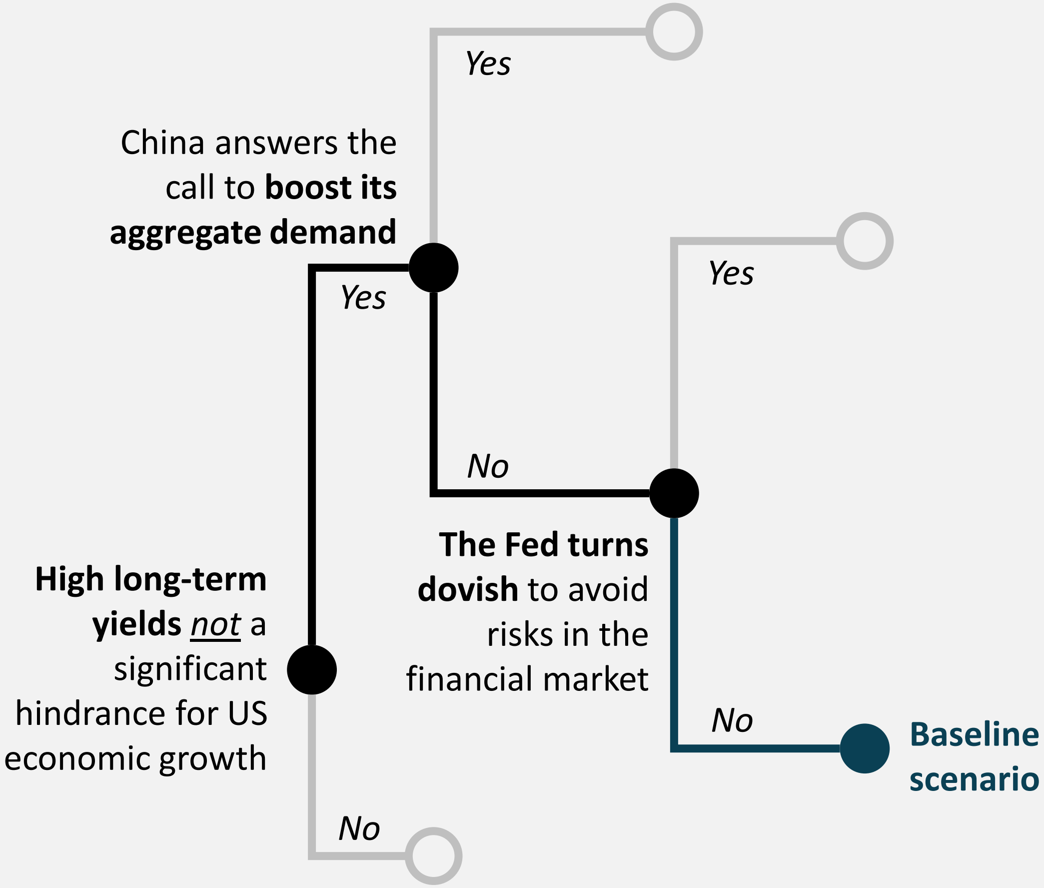
*According to Indonesia's perspective. Best case scenario explains external development that will enable higher growth in Indonesia's real sector and more stability for the Indonesian financial market.

Baseline scenario:

# External conditions are unlikely to benefit Indonesia in 2025

**Probability:**

60%




*Implications to the Indonesian economy:*

**Exchange rates** | **Current account** | **Growth potential**

- High UST yields and persisting pressures on Asia's anchor currencies (such as the RMB) means that exchange rate stability is likely to remain as the focus of Bank Indonesia's policy. **The expected high real rates in 2025 may weigh down demand for loans and overall economic activities in Indonesia**, although BI may still pull a 25-50 bps rate cuts following the Fed's signal.
- Cheap financing may allow Chinese manufacturers to dominate the export market, despite the expected lower demand from the US. **Cheap imports from China will continue to flood the Indonesian market; invited over by the IDR's strength relative to the RMB**. Meanwhile, slowing manufacturing growth in China (and globally) may lower Indonesia's terms of trade, **indicating a slimmer trade surplus in 2025**.
- Lower liquidity due to lower trade surplus (along with high real rates) may suppress investments, although the higher-yet-manageable SBN yield may allow the government to spend and keep Indonesia's real GDP growth above the 5% benchmark.

Worst case scenario:

# Bond vigilantes may start a domino that may overwhelm EMs (including Indonesia)

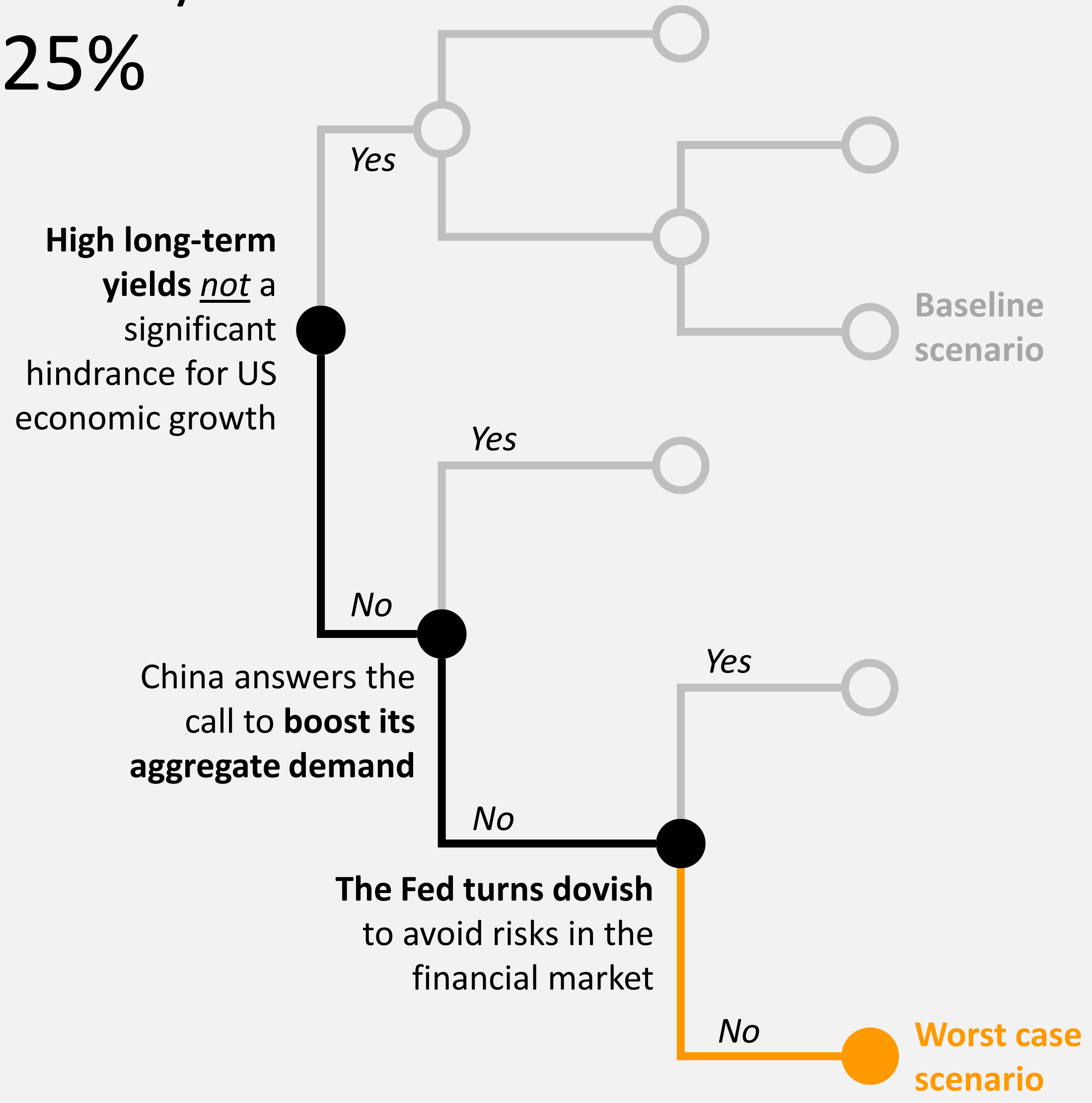
*Implications to the Indonesian economy:*

| Exchange rates | Current account | Growth potential |
|---|---|---|

- The actual size of debt issuance in 2025 may steer investors away from the UST market, sending UST yields even higher which could force the US government to forego most of its spending agenda. **The high yield and low growth environment in the US may spark a flight to safety, exacerbating outflow risks from riskier markets such as Indonesia**. It is not impossible, then, for the IDR to breach past 17,000/USD – potentially forcing Bank Indonesia to ponder the necessity of an emergency rate hike.
- **China may also opt to devalue the RMB to protect its share in the export market, possibly dragging other Asian currencies against the USD.** Chinese exports may continue to flood the Indonesian market, while the uncertain outlook for manufacturing expansion amidst the trade war will be a drag on Indonesia's commodity exports.
- The domestic liquidity condition declines further as exports plummeted, while slowing investments due to the high real rates may translate to a below 5% GDP growth.

**Probability:**

25%



Best case scenario:

# Favourable policies in China may allow the Indonesian economy to recover

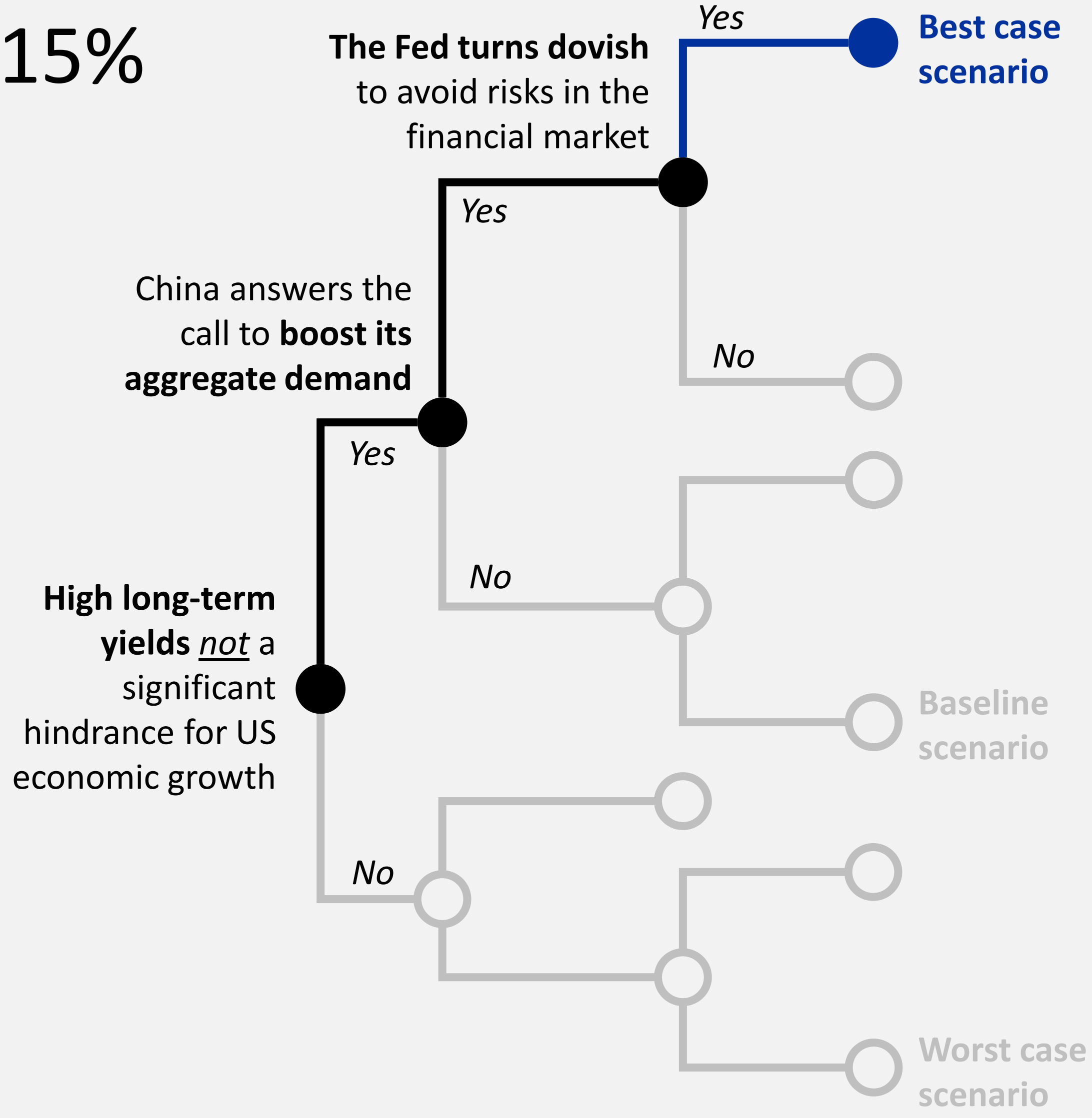
*Implications to the Indonesian economy:*

**Exchange rates** | **Current account** | **Growth potential**

- UST yields may move lower in 2025, driven by strong demand from foreign investors (repatriated corporate funds) and lower UST issuance. Inflows to the US market will lead to a stronger USD, negating the inflationary effect of the higher import tariffs that will allow the Fed to shift its policy posture. **The preferable global setting will reduce the pressure on IDR (and other currencies), allowing Bank Indonesia to follow the Fed's move and lower its policy rate.**
- Meanwhile, **mounting pressures may encourage China to launch a sizable demand-side stimulus**, turning the tide on the ongoing deflationary trend. Improving domestic demand in China will allow the global manufacturing sector to recover (as Chinese producers stop competing on price in the export market), translating to a substantial increase in the demand for commodities that will improve Indonesia's export performance, providing the additional liquidity necessary to boost Indonesia's GDP growth to 5.2% YoY

**Probability:**

15%



# Projections 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 | 6.97# | 7.47 |
| USD/IDR exchange rate (end of year) | 13,866 | 14,050 | 14,262 | 15,568 | 15,397 | 16,102# | 16,887 |
| Trade balance (USD Bn) | -3.2 | 21.7 | 35.3 | 54.5 | 37.0 | 31.0# | 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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