Cost reduction or reallocation?

24 January 2025

Lazuardin Thariq Hamzah
lazuardin_hamzah@bca.co.id

Barra Kukuh Mamia
barra_mamia@bca.co.id

Scan for the link to our report depository

Summary

- The Indonesian government has instructed ministries, institutions, and regional governments to slash spending by around IDR 306.7 Tn (1.26% of GDP) in 2025, enough to offset the lost revenue due to the delayed VAT hike.
- Most savings are expected from reduced meeting expenses, business trips, and other activities under the management support (*DukMan*) programme, whose budget swelled since the pandemic.
- Rather than reducing overall spending, the cuts may aim to reallocate funds to the central government, creating fiscal space necessary to support its flagship programmes.

- Today marks the first of Donald Trump's second presidency, and the global financial markets are unfolding much as we expected before the inauguration. The president opted to raise the issue of immigration and border control as the focal point in his inaugural speech, which helped ease market concerns over the risk of higher import tariffs so soon in the presidency. The relatively serene conditions are reflected in the declining VIX index following the inauguration, while the USD (DXY index) has also stabilised, now sitting below its early January 2025 level (107.98 vs. 109.22 on 3 January 2025).
- The Indonesian financial market, of course, benefitted from the relative calmness in the US. The benchmark 10Y SBN yield reverted to 7.07% as the market opened today, a sizable 10.7 bps drop from its position last Monday. However, it is clear that import tariffs remain close to the thought of the sitting US president (new tariffs on China, Canada, and Mexico could come within 10 days of his second presidency), highlighting the topsy-turvy global landscape that could come back and hit the Indonesian financial market in the upcoming weeks.

More of a reallocation effort

- As we have discussed *ad nauseam*, the current global situation did not help the Indonesian government (among others) with its financing. As such, we did not expect the government will cover its revenue shortfall (including the potential IDR 71 Tn shortfall due to the delayed VAT rate hike) by adding more supplies to the SBN market, whose net issuance is expected to grow by IDR 190.7 Tn (42.2% YoY) in 2025 even at the current 2.53% of GDP fiscal deficit posture. **As widely predicted, the government will look to cover the shortfall by optimising its spending**, which is precisely the message of the first presidential instruction of the year (*Inpres* 1/2025).

- Indeed, the government has instructed a saving effort amounting to around IDR 306 Tn (1.26% of GDP), with the president instructing regional leaders to adjust its spending to reflect the potential IDR 50.5 Tn cut in transfers to regional governments. **The bulk of the saving measure, however, will be directed towards ministries and other government institutions (K/L)**, which have been instructed to trim as much as IDR 256.1 Tn (1.05% of GDP) in the current fiscal year.

- In hindsight, the 1.26% of GDP worth of the saving target is not unreachable. **K/L spending has not been particularly efficient in the post-COVID years, as evidenced by the significant portion allocated to the management support programme (program *dukungan manajemen*, or *DukMan*)**, which at one point accounted for more than a third of total K/L expenditures when it peaked in 2022 ***(see Chart 1)***. According to the definition provided to us, the *DukMan* programme encompasses activities intended to support the implementation of other strategic programmes managed by specific ministries and government institutions. The programme's budget covers various activities, including (but not limited to) meetings, group discussions or seminars, business trips or surveys, and purchases of stationery.

"The budget allocated for the 'dukungan manajemen' programme peaked in 2021, when the word 'WFB' seemed to be trending among government employees"

- As highlighted in Chart 1**, budget allocations for the non-core *DukMan* programme have been declining since 2.29% of GDP in 2021, now settling at 1.47% of GDP allocated for 2025. The optimisation process, however, has been gradual, especially when compared to the pandemic-year spike in the budget from around 1.0% of GDP in pre-pandemic years to 2.29% of GDP in 2021**. However, given President Prabowo's specific instructions to cut the budget for business trips and meetings, we may expect the budget for the *DukMan* programme to fall more significantly in 2025.

- The question, then, is how much the budget for the *DukMan* programme could realistically be reduced. The current Minister of Finance may have some experience in shepherding the *DukMan* spending lower, having successfully done so when she resumed office in mid-2016. However, the 0.04% GDP reduction in the *DukMan* programme's budget achieved in 2016 will not be sufficient to meet the current mandate of trimming 1.26% of GDP worth from the K/L spending, meaning that more drastic actions will be needed.

- Records from the fiscal years 2012 to 2014 show that ministries and other government institutions could still deliver their strategic programmes while allocating an average of only 4.89% of the total K/L budget to the *DukMan* programme (compared to 30.76% of the total K/L budget at the moment). A return to this 2012-2014 budget structure may save around IDR 180.3 Tn in total K/L spending, a significant progress toward meeting the mandate to trim IDR 256.1 Tn from the K/L budget.

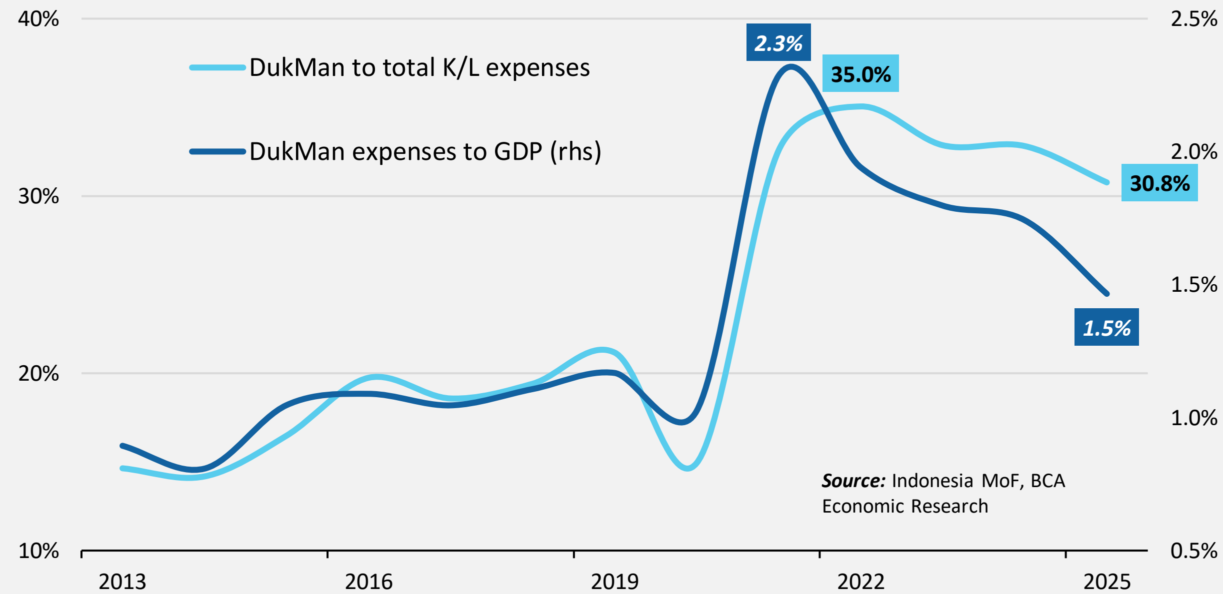
- **Aside from the political will required, such a sudden drop in the spending on *DukMan* could have some adverse effects on the real sector.** The hospitality and air transport sector comes to mind, given the very definition of the *DukMan* programme. Companies in the hospitality and passenger air transport sectors have experienced slower revenue growth amid the declining share of the *DukMan* programme budget in total K/L spending ***(see Chart 2)*** – a trend which may negatively impact regional growth and reduce the demand for labour, given the more labour-intensive and less Jakarta-centric nature of the hospitality sector.
- For a pro-growth government to adopt this budget-saving measure – despite its potential adverse impact on labour-intensive hospitality sectors – highlight the limited options currently available to the government to balance its financing. As discussed in the opening paragraph, the lost revenue from the delayed VAT rate hike necessitated the government to embark on some cost-saving measures, lest the fiscal deficit may meander past the targeted 2.53% of GDP.
- However, despite the scale of the ordered cost-saving measures seemingly exceeding what is required to offset the lost VAT revenue, we should note that the budget optimisation may not be intended solely to yank the fiscal deficit (and debt issuance) below the 2025 target. **The budget optimisation campaign instructed for ministries, institutions, and regional governments may instead be driven by the need to reallocate more funds to the (non-K/L) central government *(see Chart 3)***, which may provide the necessary fiscal breathing room for the central government to execute its flagship *Asta Cita* programmes. For some context, there is a growing concern that the earmarked IDR 71 Tn may not provide much breathing room for the central government to execute its signature free nutritious meal programme, especially with the ongoing uptrend in domestic food prices ***(chart 4)***.
- Depending on its success, the ongoing K/L's and regional governments' budget optimisation efforts may suffice to keep the fiscal deficit at the targeted 2.53% while enabling the central government to maintain (or potentially expand) its flagship programmes. A prudent fiscal management, of course, remain crucial in the current situation, given the still-uncertain global financial market.

"The budget optimisation measure may be intended to reallocate more funds for the central government, lest the fiscal deficit in 2025 may exceed the targeted 2.53% of GDP"

Chart 1

Speeding up the decline

Ministries and other public institutions have been slowly trimming their non-core expenses since the post-COVID year peak, but the first Presidential instruction of the year may speed up the process

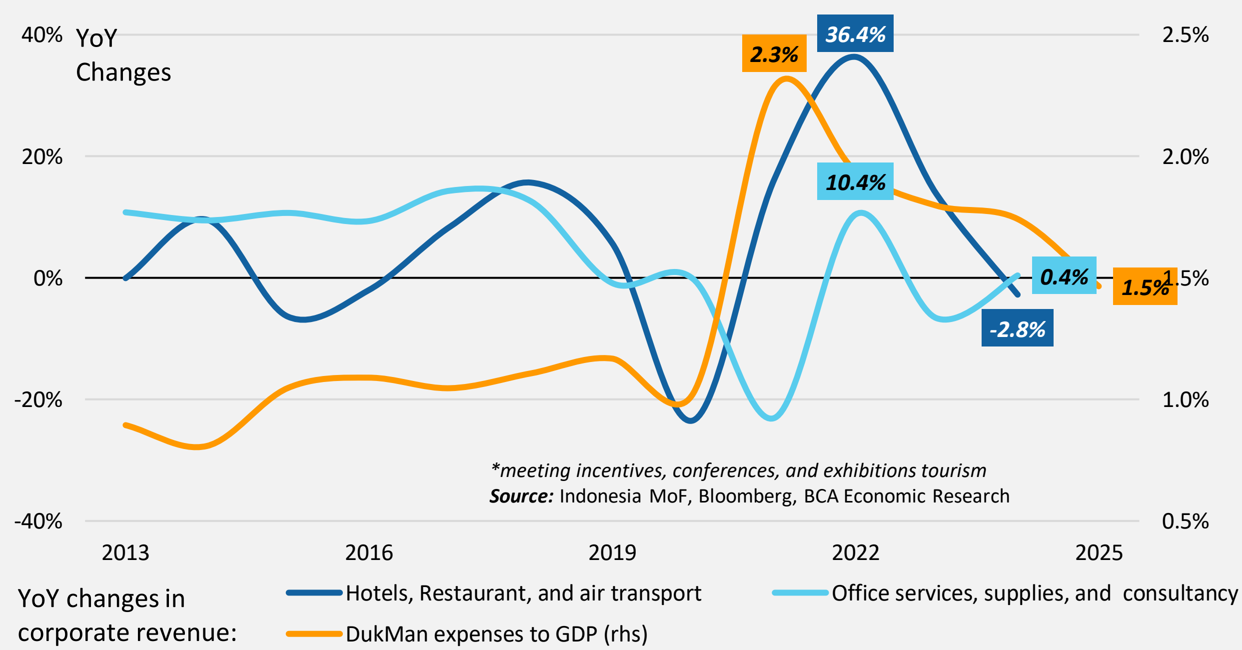


Source: Indonesia MoF, BCA Economic Research

Chart 2

Ratting the MICE*

A more efficient ministries/public institutions expenses may translate negatively to the private sector, especially the labour-intensive MICE* sector.



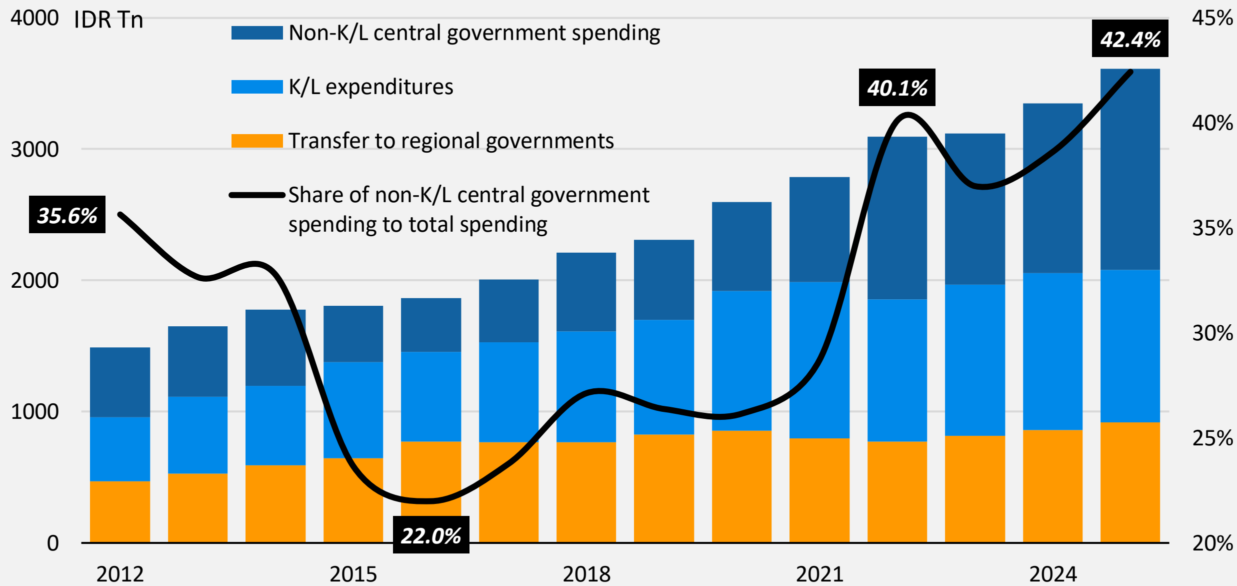
**meeting incentives, conferences, and exhibitions tourism*

Source: Indonesia MoF, Bloomberg, BCA Economic Research

Chart 3

Resources, redistributed

The lower K/L and regional government spending may be intended to funnel more money for the central government, rather than lowering the fiscal deficit below the 2.53% target.

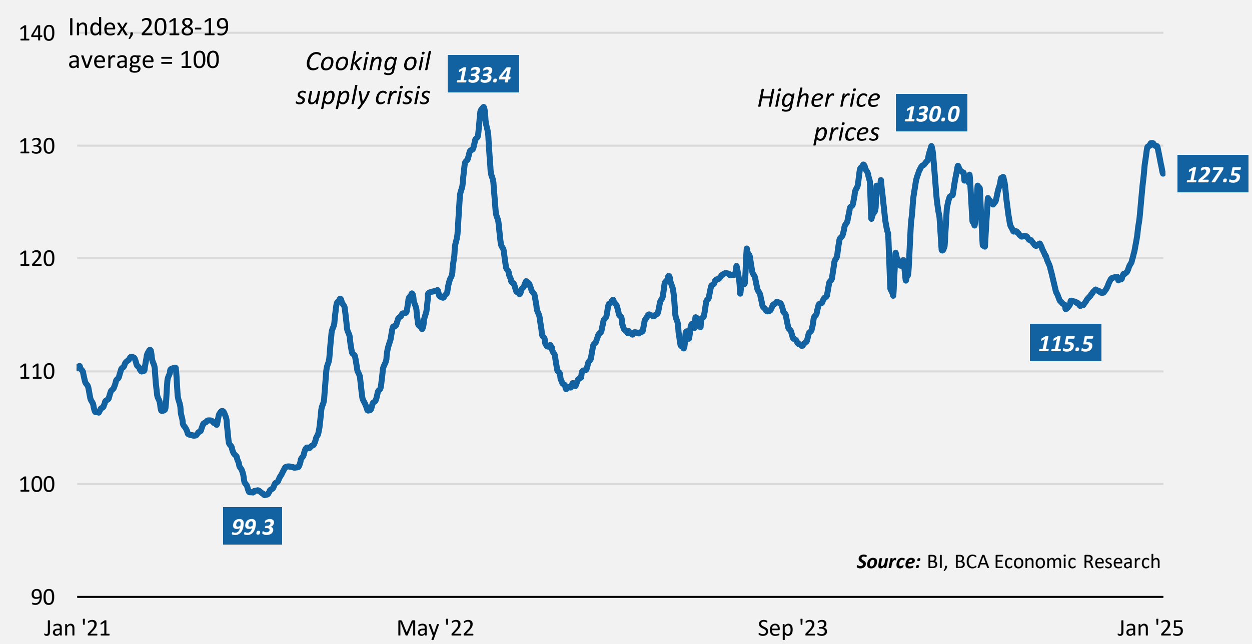


Source: Indonesia MoF, BCA Economic Research

Chart 4

When the push finally comes to shove

Domestic food prices are on the rise lately (including rice), highlighting the challenge for the government execute its programmes given the presently constricted fiscal space.



Source: BI, BCA Economic Research

Economic Calendar

		Actual	Previous	Forecast*
02 January 2025				
ID	S&P Global Manufacturing PMI	51.2	49.6	50
ID	**Inflation Rate YoY, %**	**1.57**	**1.55**	**1.7**
US	S&P Global Manufacturing PMI	49.4	49.7	48.3
07 January 2025				
US	Balance of Trade, USD Bn	-78.2	-73.8	-70
08 January 2025				
ID	**Foreign Exchange Reserves, USD Bn**	**155.7**	**150.2**	**152.0**
09 January 2025				
ID	Consumer Confidence	127.7	125.9	120
CN	Inflation Rate YoY, %	0.1	0.2	0.2
EA	Retail Sales YoY, %	1.2	2.1	1.7
10 January 2025				
ID	Car Sales YoY, %	-6.4	-11.9	-
ID	Motorbike Sales YoY, %	-5.5	-10.3	-
ID	Retail Sales YoY, %	0.9	1.5	-
US	Non-Farm Payrolls, th	256	212	200
13 January 2025				
CN	Balance of Trade, USD Bn	104.84	97.44	85
15 January 2025				
ID	**Balance of Trade, USD Bn**	**2.24**	**4.37**	**3.7**
US	Inflation Rate YoY, %	2.9	2.7	2.9
ID	Loan Growth YoY, %	10.39	10.79	10
16 January 2025				
EA	Balance of Trade, USD Bn	16.4	8.6	7.8
17 January 2025				
CN	Retail Sales YoY, %	3.7	3	3.2
CN	GDP Growth Rate YoY, %	5.4	4.6	5
23 January 2025				
ID	M2 Money Supply YoY, %	4.4	6.5	-
27 January 2025				
ID	**Foreign direct investment, % YoY**		**18.55**	**-**
30 January 2025				
US	**Fed Interest Rate Decision, %**		**4.5**	-
31 January 2025				
US	PCE Price Index YoY, %		2.4	2.4

*Forecasts of some indicators are simply based on market consensus
Bold indicates indicators covered by the BCA Monthly Economic Briefing report

Selected Macroeconomic Indicator

Key Policy Rates	Rate (%)	Last Change	Real Rate (%)
US	4.50	Dec-24	1.60
UK	4.75	Nov-24	2.25
EU	3.15	Dec-24	0.75
Japan	0.25	Jul-24	-3.70
China (lending)	2.00	Sep-24	4.25
Korea	3.00	Nov-24	1.10
India	6.50	Feb-23	1.28
Indonesia	5.75	Jan-25	4.18
Money Mkt Rates	**23-Jan**	**-1 mth**	**Chg (bps)**
SPN (1Y)	6.69	6.88	-19.1
SUN (10Y)	7.06	7.02	3.4
INDONIA (O/N, Rp)	5.73	6.09	-35.7
JIBOR 1M (Rp)	6.39	6.63	-23.9
Bank Rates (Rp)	**Oct**	**Sep**	**Chg (bps)**
Lending (WC)	8.72	8.87	-15.48
Deposit 1M	4.78	4.81	-2.76
Savings	0.66	0.67	-0.14
Currency/USD	**23-Jan**	**-1 mth**	**Chg (%)**
UK Pound	0.810	0.798	-1.46
Euro	0.960	0.961	0.10
Japanese Yen	156.1	157.2	0.72
Chinese RMB	7.286	7.296	0.13
Indonesia Rupiah	16,280	16,175	-0.64
Capital Mkt	**23-Jan**	**-1 mth**	**Chg (%)**
JCI	7,232.6	7,096.4	1.92
DJIA	44,565.1	42,907.0	3.86
FTSE	8,565.2	8,102.7	5.71
Nikkei 225	39,958.9	39,161.3	2.04
Hang Seng	19,700.6	19,883.1	-0.92
Foreign portfolio ownership (Rp Tn)	**Dec**	**Nov**	**Chg (Rp Tn)**
Stock	3,521.3	3,402.4	118.98
Govt. Bond	876.6	872.5	4.15
Corp. Bond	5.9	7.1	-1.18

Trade & Commodities	23-Jan	-1 mth	Chg (%)
Baltic Dry Index	824.0	994.0	-17.1
S&P GSCI Index	570.3	537.3	6.1
Oil (Brent, $/brl)	78.3	72.6	7.8
Coal ($/MT)	123.7	128.9	-4.0
Gas ($/MMBtu)	3.97	2.89	37.4
Gold ($/oz.)	2,754.9	2,612.6	5.4
Copper ($/MT)	9,105.5	8,801.5	3.5
Nickel ($/MT)	15,499.2	15,060.2	2.9
CPO ($/MT)	1,029.2	1,080.6	-4.8
Rubber ($/kg)	2.02	1.90	6.3
External Sector	**Dec**	**Nov**	**Chg (%)**
Export ($ bn)	23.46	24.00	-2.24
Import ($ bn)	21.22	19.63	8.10
Trade bal. ($ bn)	2.24	4.37	-48.73
Central bank reserves ($ bn)*	155.7	150.2	3.65
Prompt Indicators	**Dec**	**Nov**	**Oct**
Consumer confidence index (CCI)	127.7	125.9	121.1
Car sales (%YoY)	-6.4	-11.9	-3.9
Motorcycle sales (%YoY)	-5.5	-10.3	5.4
Manufacturing PMI	**Dec**	**Nov**	**Chg (bps)**
USA	49.4	49.7	-30
Eurozone	45.1	45.2	-10
Japan	49.6	49.0	60
China	50.5	51.5	-100
Korea	49.0	50.6	-160
Indonesia	51.2	49.6	160

Source: Bloomberg, BI, BPS
Notes:
*Data from an earlier period
For changes in currency: **Black indicates appreciation against USD, **Red** otherwise
***For PMI, **>50** indicates economic expansion, **<50** otherwise

Indonesia – Economic Indicators Projection

	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#	2.3
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*

Economic, Banking & Industry Research Team

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

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

Barra Kukuh Mamia
Head of Macroeconomic Research
barra_mamia@bca.co.id
+6221 2358 8000 Ext: 1053819

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

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

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

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

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

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

Nicholas Husni
Economist / Analyst
nicholas_husni@bca.co.id
+6221 2358 8000 Ext: 1079839

Samuel Theophilus Artha
Economist / Analyst
samuel_artha@bca.co.id
+6221 2358 8000 Ext: 1080373

PT Bank Central Asia Tbk

Economic, Banking & Industry Research of BCA Group
20th Grand Indonesia, Menara BCA
Jl. M.H Thamrin No. 1, Jakarta 10310, Indonesia
Ph : (62-21) 2358-8000 Fax : (62-21) 2358-8343