

## One step out from the brink

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### Summary

- The Indonesian financial market has shown little reaction to the stalled US-Indonesia trade talks, as the announcement was preceded by yet another extension of the 'reciprocal' tariff implementation deadline.
- The inelastic demand for key Indonesian exports may help cushion the decline in US demand, although exporters of more elastic goods appear to be facing increasing competition in the US market.
- The breakthrough in the IEU-CEPA negotiations provides a lifeline for the domestic manufacturing sector, given the similar demand profiles of European and American consumers.

- Last week's news on an imminent US-Indonesia trade deal proved to be a misfire, as the Trump administration maintains the 32% tariff rate on Indonesian exports. Luckily, the Indonesian financial market has not reacted much to the confirmed higher tariff. The benchmark 10Y SBN yield remains stable at a low 6.56%, thanks to the USD 300.37 Mn in foreign capital inflows to the SBN market throughout the past week. Inflows to the domestic debt market outweigh the USD 115.19 Mn flowing out of the equities market, which helps the IDR exchange rate to remain stable around the 16,200/USD range.
- There are a couple of arguments that may explain investors' limited response to President Trump's announcement of tariffs on Indonesian exports. The more widely cited explanation is that investors have grown accustomed to the so-called 'TACO' market dynamic, in which President Trump frequently

frames higher import tariffs as beneficial to his administration and the US economy, yet routinely delays implementation in pursuit of more favourable trade terms. Indeed, the US 'reciprocal' tariff is now scheduled to take effect on 1 August 2025, effectively granting importers an additional three-week extension, as the US government has only managed to formally secure two trade agreements (with the UK and Vietnam) during the previous 90-day tariff suspension.

- Another possible explanation is that investors are now less prone to overstating the potential impact of heightened US trade barriers on the Indonesian economy. While the tariff-induced price increases are widely expected to negatively impact Indonesia's manufacturing exports to the US, the resulting decline in demand may be more limited than initially thought, given the relatively inelastic demand profile of some Indonesian products and

commodities in the US import market (*see Chart 1*). While most of these inelastic goods fall in the category of raw materials, and thus are more volatile considering the bullwhip effect, Indonesian commodity producers' relative competitiveness ( $RCA > 1$ ) may help them to maintain market share in the US market.

- **Even more encouraging is the apparent inelasticity of American consumers' demand for major Indonesian exports**, such as CPO and its derivatives, chemical products, and apparel. This inelastic demand profile may help sustain demand for Indonesian products in the US market, particularly if household consumption remains resilient on the back of the OBBB-enabled fiscal expansion.
- **The Trump administration's singular focus on bilateral trade deficits as the basis for determining tariff rates on specific countries may also inadvertently benefit Indonesian commodified goods producers and manufacturers.** For instance, the 35% tariff imposed on Bangladeshi goods is an advantage for Indonesia's apparel industry, which has been facing intensifying competition from its lower-cost counterpart.
- However, it may not be wise to rely on inelastic demand conditions and other countries' tariff misfortunes to protect Indonesian exports to the US over the long term. Our calculation of the May 2025 US trade data shows a 1.9% decline in the unit cost of apparel imported from Indonesia, suggesting that Indonesian apparel exporters are still being forced to compete on price in the US market, despite the

***"Inelasticity of demand and higher tariffs on competing countries may sustain US demand for some of Indonesia's key export products"***

two advantages outlined above (inelastic US demand and still-favourable tariff rate due to the 90-day freeze). **Exports of more elastic products, such as vehicles and parts, toys, and consumer electronics, appear to have experienced a more pronounced decline in unit costs**, underscoring the margin Indonesia's manufacturing sector (particularly in higher-value segments) must sacrifice to maintain its toehold in the US market.

- Indeed, Indonesian manufacturers may not be able to rely on US import demand to sustain its export growth momentum. **While higher demand from the US largely explains the recent increase in Indonesian export growth in the past couple of months, US contributions to Indonesia's non-O&G YoY growth appear to have stalled in May 2025 (*see Chart 2*).**

Hence, while some Indonesian exporters may still expect to receive orders from their American clients, the higher tariff may make it unlikely for American importers to deliver more business for Indonesian producers.

- **The tall task to sustain the growth momentum in the manufacturing sector, then, will require the domestic manufacturing sector to secure alternative export markets.** Fortunately, the Indonesian government have recently managed to deliver some good news in this direction. Agreements with the EU on a potential IEU-CEPA are reported to have been in place, with government officials signalling that the trade deal could be formally signed as soon as September 2025.
- While details remain scant, the breakthrough that may soon lead to the signing of the IEU-

CEPA holds a couple of significances. **First, for Indonesia, access to the EU market is increasingly critical as the US raises its trade barriers, given the near-identical demand profile of European and American consumers (see Chart 3).** Greater access to the EU market is particularly relevant to Indonesia's industrial policy, which aims at upgrading its manufacturing sector on the back of a downstreamed nickel supply chain, given the higher prevalence of LNCM batteries in Europe's EV market.

- **Second, for the EU, the reported breakthrough may reveal the shift in the European parliament's priorities.** Indonesia's Trade Minister suggested that the breakthrough was made possible by the EU's more lenient stance on its deforestation regulation (EUDR), a framework whose derivative, the Renewable Energy Directive (RED) II, had previously brought the two

economies into a WTO dispute in late 2019. This softer EUDR stance seems to reflect the results of the June 2024 EU parliament election, with right-wing alliances gaining seats at the expense of centre-left and green parties.

- That being said, it is important to recognise that a realignment in trade relations rarely occurs in the short term. Indonesian businesses may require time to build their European contact networks, while the deadline for the US 'reciprocal' tariff looms large. **Any decline in US import demand is likely to disproportionately impact labour-intensive sectors**, with downstream effects on household income and employment. As such, the domestic manufacturing sector may continue to face pressure from this twin shock to both export and domestic demand, underscoring the increasingly critical role of the public sector in supporting aggregate demand.

Chart 1

### (Partially) saved by inelasticity

Despite the damage on manufactured goods exports, Indonesia's raw material exports to the US may remain stable considering its inelastic demand

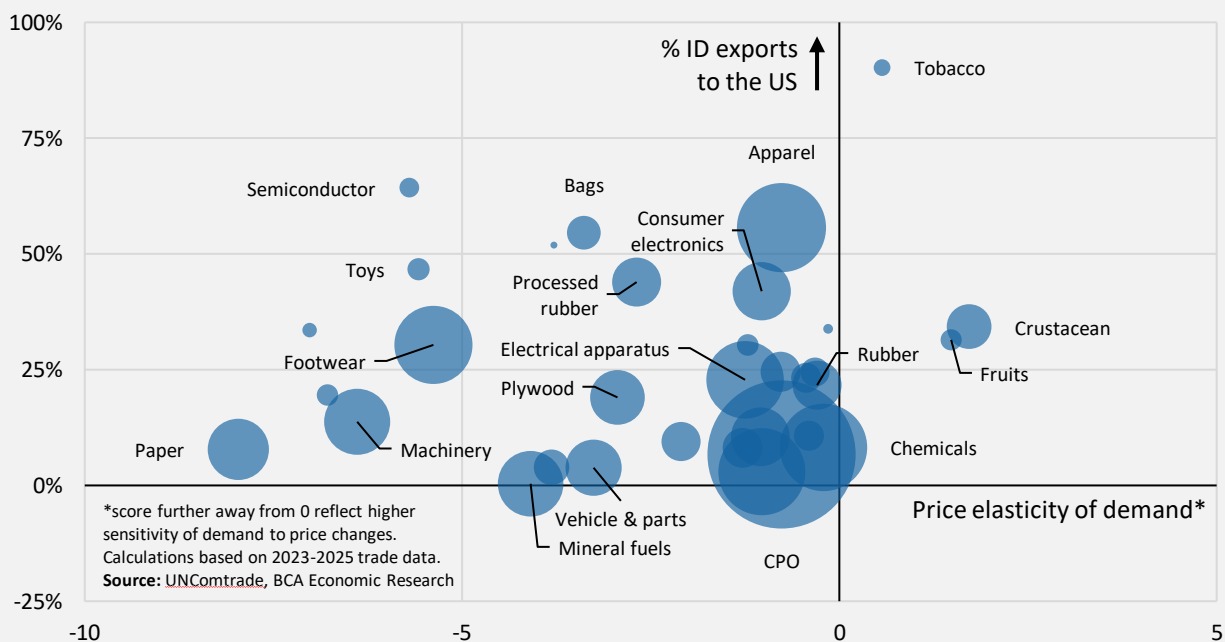


Chart 2

### Fortress Europa

EU is behind the US and China in explaining the spike in Indonesia's exports in May 2025, a trend which may continue given the recent breakthrough in IEU-CEPA negotiations

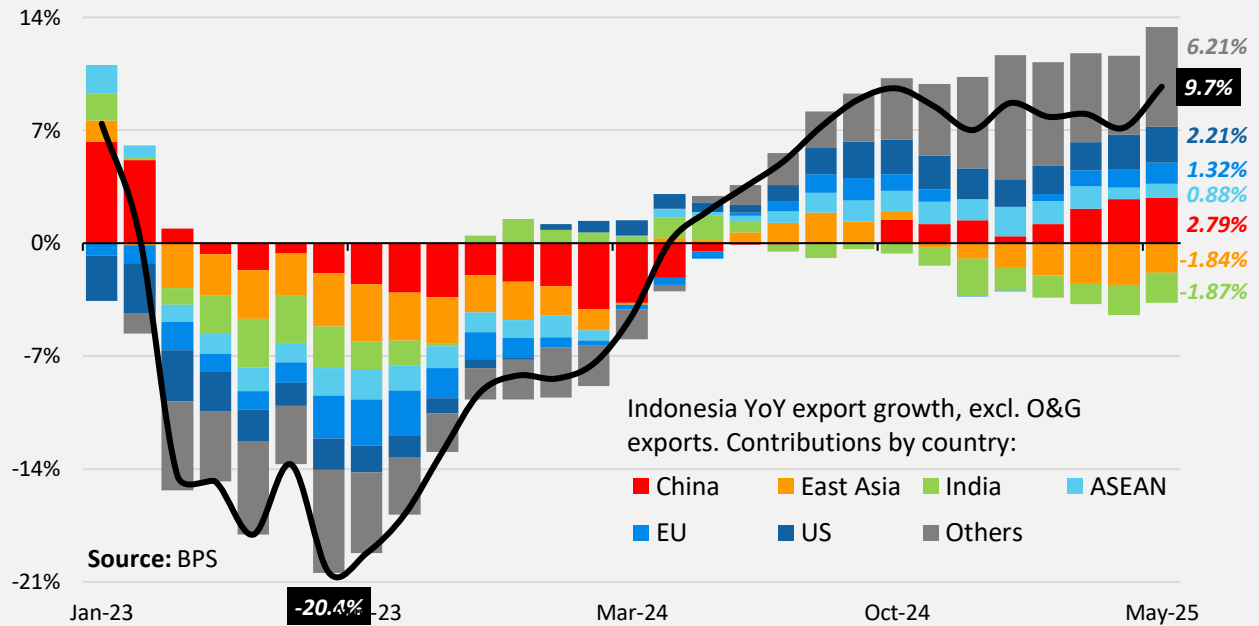


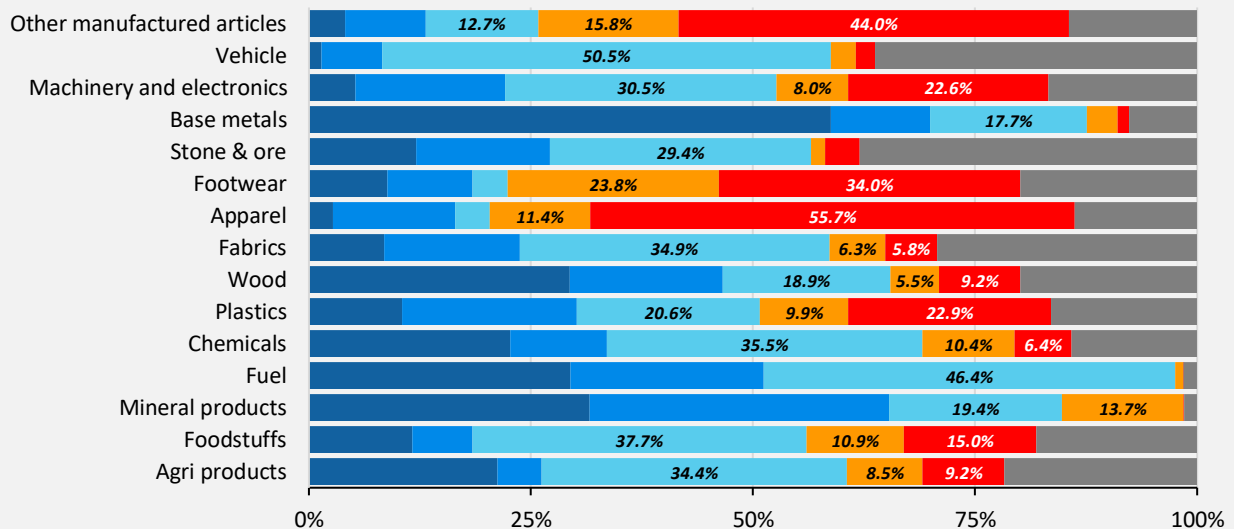
Chart 3

### Temporarily offline

EU's demand for Indonesian exports largely follows the US, meaning that the IEU-CEPA deal may provide a lifeline for Indonesian manufacturers

Indonesia exports destination (2023-2025), share of total Indonesia exports

China (Dark Blue) East Asia (Blue) SEA and South Asia (Light Blue) EU (Orange) USA (Red) Others (Grey)



| Economic Calendar |                                          |              |              |              |
|-------------------|------------------------------------------|--------------|--------------|--------------|
|                   |                                          | Actual       | Previous     | Forecast*    |
| 01 July 2025      |                                          |              |              |              |
| ID                | S&P Global Manufacturing PMI             | 46.9         | 47.4         | 48.5         |
| ID                | <b>Trade balance (May-25), USD Bn</b>    | <b>4.3</b>   | <b>0.16</b>  | <b>1.0</b>   |
| ID                | <b>Inflation Rate YoY, %</b>             | <b>1.87</b>  | <b>1.6</b>   | <b>1.7</b>   |
| US                | S&P Global Manufacturing PMI             | 52.9         | 52           | 52           |
| 03 July 2025      |                                          |              |              |              |
| US                | Trade balance, USD Bn                    | -71.5        | -60.3        | -72          |
| US                | Non Farm Payrolls, th                    | 147          | 144          | 100.0        |
| 07 July 2025      |                                          |              |              |              |
| ID                | <b>Foreign Exchange Reserves, USD Bn</b> | <b>152.6</b> | <b>152.5</b> | <b>157.0</b> |
| EA                | Retail Sales YoY, %                      | 1.8          | 2.7          | 1.7          |
| ID                | Motorbike Sales YoY, %                   | -0.3         | -0.1         | -            |
| 08 July 2025      |                                          |              |              |              |
| ID                | Consumer Confidence                      | 117.8        | 117.5        | 123          |
| 09 July 2025      |                                          |              |              |              |
| ID                | Retail Sales YoY, %                      | 1.9          | -0.3         | 0.3          |
| ID                | Car Sales YoY, %                         | 22.6         | -16.1        | -            |
| CN                | Inflation Rate YoY, %                    | 0.1          | -0.1         | 0.1          |
| 14 July 2025      |                                          |              |              |              |
| CN                | Trade balance, USD Bn                    | 114.77       | 103.22       | 100          |
| 15 July 2025      |                                          |              |              |              |
| CN                | GDP Growth Rate YoY, %                   |              | 5.4          | 4.1          |
| CN                | Retail Sales YoY, %                      |              | 6.4          | 4.6          |
| US                | Inflation Rate YoY, %                    |              | 2.4          | 2.5          |
| 16 July 2025      |                                          |              |              |              |
| ID                | <b>BI-Rate Decision, %</b>               |              | <b>5.5</b>   | -            |
| ID                | Loan Growth YoY, %                       |              | 8.43         | 8.5          |
| 17 July 2025      |                                          |              |              |              |
| US                | Retail Sales YoY, %                      |              | 3.3          | 3.6          |
| 22 July 2025      |                                          |              |              |              |
| ID                | M2 Money Supply YoY, %                   |              | 4.9          | -            |
| 29 July 2025      |                                          |              |              |              |
| ID                | <b>Foreign Direct Investment YoY, %</b>  |              | <b>12.7</b>  | -            |
| 31 July 2025      |                                          |              |              |              |
| US                | <b>Fed Interest Rate Decision, %</b>     |              | <b>4.5</b>   | <b>4.5</b>   |
| US                | PCE Price Index YoY, %                   |              | 2.2          | 2.2          |

\*Some forecasts 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 (%) | Trade & Commodities             | 11-Jul   | -1 mth   | Chg (%)   |
|-------------------------------------|----------|-------------|---------------|---------------------------------|----------|----------|-----------|
| US                                  | 4.50     | Dec-24      | 2.10          | Baltic Dry Index                | 1,663.0  | 1,680.0  | -1.0      |
| UK                                  | 4.25     | May-25      | 0.85          | S&P GSCI Index                  | 551.4    | 543.6    | 1.4       |
| EU                                  | 2.15     | Jun-25      | 0.15          | Oil (Brent, \$/bbl)             | 70.4     | 66.9     | 5.2       |
| Japan                               | 0.50     | Jan-25      | -3.00         | Coal (\$/MT)                    | 120.2    | 113.9    | 5.6       |
| China (lending)                     | 2.00     | Sep-24      | 4.25          | Gas (\$/MMBtu)                  | 3.22     | 2.78     | 15.8      |
| Korea                               | 2.50     | May-25      | 0.30          | Gold (\$/oz.)                   | 3,355.6  | 3,323.7  | 1.0       |
| India                               | 5.50     | Jun-25      | 2.68          | Copper (\$/MT)                  | 9,638.9  | 9,840.6  | -2.0      |
| Indonesia                           | 5.50     | May-25      | 3.63          | Nickel (\$/MT)                  | 14,995.8 | 15,123.8 | -0.8      |
| Money Mkt Rates                     | 11-Jul   | -1 mth      | Chg (bps)     | CPO (\$/MT)                     | 968.0    | 929.9    | 4.1       |
|                                     |          |             |               | Rubber (\$/kg)                  | 1.71     | 1.67     | 2.4       |
| SPN (1Y)                            | 5.57     | 6.00        | -42.8         | External Sector                 | May      | Apr      | Chg (%)   |
| SUN (10Y)                           | 6.56     | 6.76        | -19.8         | Export (\$ bn)                  | 24.61    | 20.74    | 18.66     |
| INDONIA (O/N, Rp)                   | 5.14     | 5.69        | -54.3         | Import (\$ bn)                  | 20.31    | 20.59    | -1.32     |
| JIBOR 1M (Rp)                       | 6.14     | 6.16        | -2.6          | Trade bal. (\$ bn)              | 4.30     | 0.16     | 2,608.75  |
| Bank Rates (Rp)                     | Mar      | Feb         | Chg (bps)     | Central bank reserves (\$ bn)*  | 152.5    | 152.5    | 0.01      |
| Lending (WC)                        | 8.66     | 8.67        | -0.75         | Prompt Indicators               | Jun      | May      | Apr       |
| Deposit 1M                          | 5.01     | 5.02        | -0.47         | Consumer confidence index (CCI) | 117.8    | 117.5    | 121.7     |
| Savings                             | 0.68     | 0.68        | 0.16          | Car sales (%YoY)                | -22.6    | -15.1    | 5.0       |
| Currency/USD                        | 11-Jul   | -1 mth      | Chg (%)       | Motorcycle sales (%YoY)         | -0.3     | -0.1     | -3.0      |
| UK Pound                            | 0.741    | 0.741       | -0.05         | Manufacturing PMI               | Jun      | May      | Chg (bps) |
| Euro                                | 0.856    | 0.875       | 2.31          | USA                             | 52.9     | 52.0     | 90        |
| Japanese Yen                        | 147.4    | 144.9       | -1.74         | Eurozone                        | 49.5     | 49.4     | 10        |
| Chinese RMB                         | 7.170    | 7.188       | 0.25          | Japan                           | 50.1     | 49.4     | 70        |
| Indonesia Rupiah                    | 16,211   | 16,273      | 0.38          | China                           | 50.4     | 48.3     | 210       |
| Capital Mkt                         | 11-Jul   | -1 mth      | Chg (%)       | Korea                           | 48.7     | 47.7     | 100       |
| JCI                                 | 7,047.4  | 7,230.7     | -2.54         | Indonesia                       | 46.9     | 47.4     | -50       |
| DJIA                                | 44,371.5 | 42,866.9    | 3.51          |                                 |          |          |           |
| FTSE                                | 8,941.1  | 8,853.1     | 0.99          |                                 |          |          |           |
| Nikkei 225                          | 39,569.7 | 38,211.5    | 3.55          |                                 |          |          |           |
| Hang Seng                           | 24,139.6 | 24,162.9    | -0.10         |                                 |          |          |           |
| Foreign portfolio ownership (Rp Tn) | Jun      | May         | Chg (Rp Tn)   |                                 |          |          |           |
| Stock                               | 3,336.8  | 3,435.7     | -98.91        |                                 |          |          |           |
| Govt. Bond                          | 918.7    | 995.6       | -76.96        |                                 |          |          |           |
| Corp. Bond                          | 4.3      | 5.2         | -0.92         |                                 |          |          |           |

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   | 2024   | 2025E  |
|-------------------------------------|--------|--------|--------|--------|--------|--------|--------|
| Real GDP growth (% YoY)             | 5.0    | -2.1   | 3.7    | 5.3    | 5.0    | 5.0    | 4.8    |
| Nominal GDP growth (% YoY)          | 6.7    | -2.5   | 9.9    | 15.4   | 6.7    | 6.0    | 5.7    |
| GDP per capita (USD)                | 4175   | 3912   | 4350   | 4784   | 4920   | 4960   | 4996   |
| CPI inflation (% YoY)               | 2.7    | 1.7    | 1.9    | 5.5    | 2.6    | 1.6    | 2.0    |
| BI Rate (%)                         | 5.00   | 3.75   | 3.50   | 5.50   | 6.00   | 6.00   | 5.00   |
| SBN 10Y yield (%)                   | 7.04   | 5.86   | 6.36   | 6.92   | 6.45   | 6.97   | 7.02   |
| USD/IDR exchange rate (average)     | 14,141 | 14,529 | 14,297 | 14,874 | 15,248 | 15,841 | 16,350 |
| USD/IDR exchange rate (end of year) | 13,866 | 14,050 | 14,262 | 15,568 | 15,397 | 16,102 | 16,625 |
| Trade balance (USD Bn)              | -3.2   | 21.7   | 35.3   | 54.5   | 37.0   | 31.0   | 26.0   |
| Current account balance (% of GDP)  | -2.7   | -0.4   | 0.3    | 1.0    | -0.1   | -0.6   | -1.0   |

**Notes:**

- USD/IDR exchange rate projections are for fundamental values; market values may diverge significantly at any moment in time

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