Beware of the regressive trait of inflation

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Summary

- A weaker Rupiah and rising food prices are increasingly contributing to higher domestic prices, which appear to be weighing on household consumption.
- Worse-off households may be more exposed to the ongoing uptrend in food prices, revealing the regressive nature of the current inflationary pressures.
- Prices also appear to be more volatile in worse-off and often more populous regions, signalling greater sensitivity to price pressures.

- The global macro focus appears to have once again turned to Japan over the past week. In a complete U-turn from the previous concerted efforts by the US Treasury Department and the Bank of Japan to stabilise the JPY, US Treasury Secretary Bessent has signalled his expectation that the BoJ will take more decisive action to support the currency, driving a dramatic appreciation in the JPY as traders gear up for another BoJ rate hike.
- While the significance of a dramatic swing in the JPY and the entailing risk of JPY carry trade unwinding have been widely discussed, it is worth noting that the UST market has remained relatively stable as of now. The Fed may explain this still-dynamic development, as recent statements by some FOMC members have pushed the market firmly towards a no-hike outlook for the upcoming FOMC meeting. This policy signal, of course, contrasts with the more hawkish signals from other major central banks (such as the BoJ and ECB), helping to explain the ongoing weakness in the DXY index (-0.93% WoW).
- Other currencies, of course, have benefited from the USD's recent weakness, including the Rupiah. The ongoing weak Dollar environment has encouraged foreign investors to commit around USD 1.23 Bn in net purchases since July 2026, with most of it recorded in the domestic sovereign bond market. These returning inflows, of course, have helped to lift the dark clouds that had shrouded the Rupiah throughout June and July 2026, helping the currency stabilise within the 17,600-17,800/USD range as of now.
- However, it might be wise not to call a win for the Rupiah hastily. The recent Rupiah appreciation has been driven largely by the weakening USD, while the IDR's cross-rate against other currencies, such as the CNY, has barely changed from the June-July 2026 low. A stronger Rupiah should remain high on BI's and the government's list of priorities, as the effect of currency weakness on inflationary pressure has become increasingly noticeable in the past months.

Hard-pressed by prices

- The recent August 2026 CPI inflation data release further strengthens our concern about how the weak Rupiah has contributed to rising inflationary pressures. Stripping out the effect of the recently spiking gold prices, the contribution of the core component to the headline inflation number has more than doubled the level in early 2026 ***(see Chart 1)***, **indicating that currency weakness is increasingly feeding through to domestic prices**. This transmission is particularly relevant for Indonesia given the domestic supply chain's high import content (imports account for as much as 25% of total inputs for the communication equipment and household electronics sectors), as higher import costs could raise both production costs and, eventually, consumer prices.

- Alas, goods prices are not the only component that may continue to contribute to headline inflation. Although still mostly contained, **foodstuffs and other volatile components have begun contributing more to headline inflation**, partly driven by stronger demand from the government's flagship programme. While the government has taken strategic steps to strengthen domestic agricultural productivity and offset this higher demand, the prolonged dry season caused by the supersized El Niño may complicate these efforts, risking a supply shock that may give birth to a prolong uptrend in food prices.

- The threat of food-induced inflation is problematic in several ways. The first stems from foodstuffs' role as necessities, meaning that higher food prices will directly raise the cost of living, as households have little choice but to face the increasing prices. This dynamic greatly differs from inflation driven by other components, where consumers may find it easier to avoid higher prices by cutting back on consumption. Indeed, the recent uptrend in food prices has seen an increasing number of households reporting weaker demand for durable goods despite a noticeable increase in their consumption rate ***(see Chart 2)***, **suggesting that households have started sacrificing less-essential items to maintain the size of the bread on their consumption basket.**

- Second, **the ongoing uptrend in food prices appears to be regressive *(see Chart 3)***. Using data across different types of markets and quality of produce, our analysis shows that food prices have risen more noticeably in traditional markets, whereas prices in modern markets appear to have remained relatively flat. **This data point suggests that worse-off households, which may shop predominantly in traditional markets, could be bearing the full brunt of the ongoing inflationary pressures**, while food price increases in modern markets may not yet have reached levels noticeable to better-off households.

"Food-induced inflation is often regressive, as food prices in traditional markets tend to be more volatile than in modern markets"

- Some factors may explain this divergent trend in food prices between modern markets, which predominantly cater to better-off households, and traditional markets. For instance, greater market concentration in the retail industry may make businesses less willing to pass on higher costs to consumers, while new entrants to this industry also often try to compete on prices. This condition, of course, is less applicable to traditional markets dominated by mom-and-pop retailers.

- Meanwhile, procurement practices under the government's flagship Free Nutritious Meals programme may also explain this price discrepancy. Local nutritional fulfilment service (SPPG) kitchen units are often reported to procure ingredients directly from local vendors and farmers, creating a captive market for local producers.

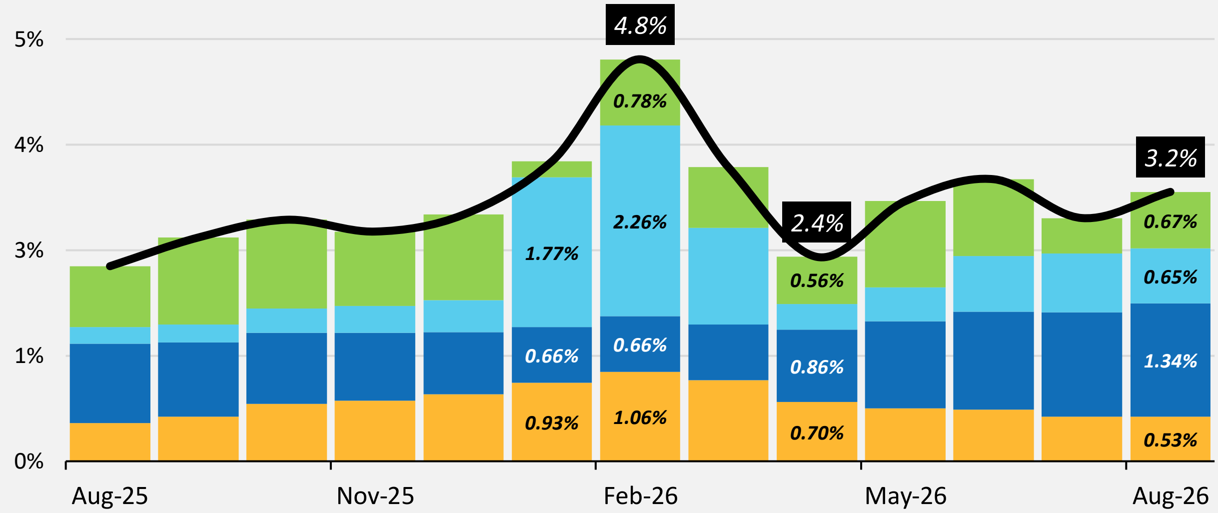
- However, without a corresponding increase in local agricultural production, this procurement system could redirect food supplies towards the programme, reducing the availability of produce in traditional markets and, in turn, risking higher prices for households. **Public intervention in the food and agricultural supply chain, then, will be needed to mitigate this regressive nature of food-induced inflation** – an operation that the government may not find too difficult to execute given reports of sufficient national food supplies currently.
- Alas, inflationary threats may not be regressive only in the case of food-induced inflation. Historically, **headline CPI inflation tends to be more volatile in regions with lower household purchasing power *(see Chart 4)***, which are often more populous than better-off regions. More volatile inflation in economically vulnerable regions highlights Indonesian households' sensitivity to changes in prices, which could detrimentally affect consumption growth (as also highlighted by Chart 2).
- This vulnerability is further compounded by weaker fiscal capacity in poorer regions. In some cases, higher logistics costs already make price stabilisation more challenging in these areas, while adjustments to regional government funds could constrain local governments' ability to improve logistical infrastructure.
- The pressure may have been further amplified as regional governments responded to reduced transfers by curbing subsidy spending and increasing tariffs on local services, meaning that some regions may also experience inflationary pressures from the administered prices component. We could argue, then, that fiscal consolidation at the regional level could have an unintended inflationary consequence, particularly in regions where households have weaker purchasing power and, therefore, are more sensitive to price increases.
- Another straw that may break the domestic price stability's back is a series of natural and environmental disasters occurring simultaneously, in which impact may translate either directly or indirectly via supply and infrastructure disruptions. The ongoing disasters also pose another test to the fiscal balance, making our previous discussions even more complex.
- Every economic agenda, of course, has its own unintended consequences. The government's plan to boost demand and increase efficiency by centralising resources has been successful in accelerating GDP growth in recent quarters, yet textbook economics explains that inflation can be a byproduct of above-trend GDP growth. **The task now is to limit these inflationary pressures and mitigate their regressive nature**, which will be key not only to achieving a higher GDP number, but also to delivering more equitable economic growth.

"High logistic costs mean inflation is often more volatile in less-dynamic regions"

Chart 1

Hard-pressed by prices

Indonesian households start noticing higher prices as unfavourable weather condition lift food prices, while weak Rupiah starts to translate to higher core inflation



Indonesia CPI prices (YoY, %), contributions by: (Yellow) Gold & Jewellery | (Dark blue) Core inflation ex.gold | (Sky blue) Administered prices, inc. energy | (Green) Foodstuffs & other volatile components.
Source: BPS, BCA Economic Research

Chart 2

Spending more on primary items

The demand for durable goods continues to weaken despite households starting to allocate more of their income to consumption, indicating a rise in living costs

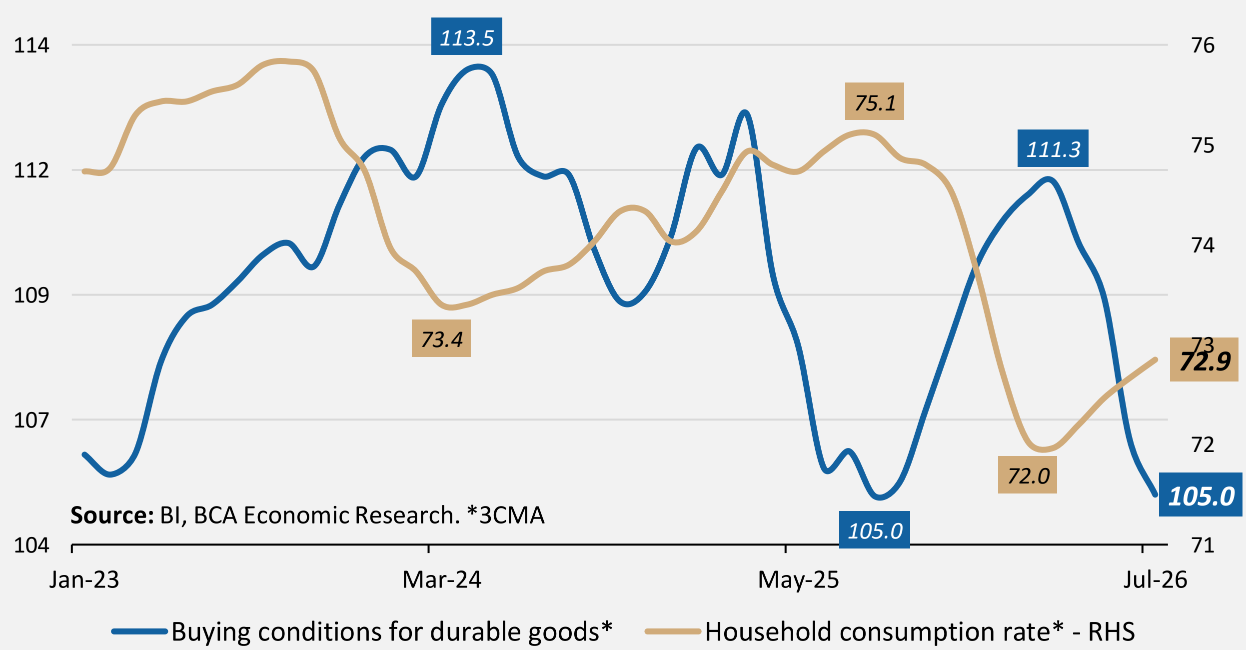
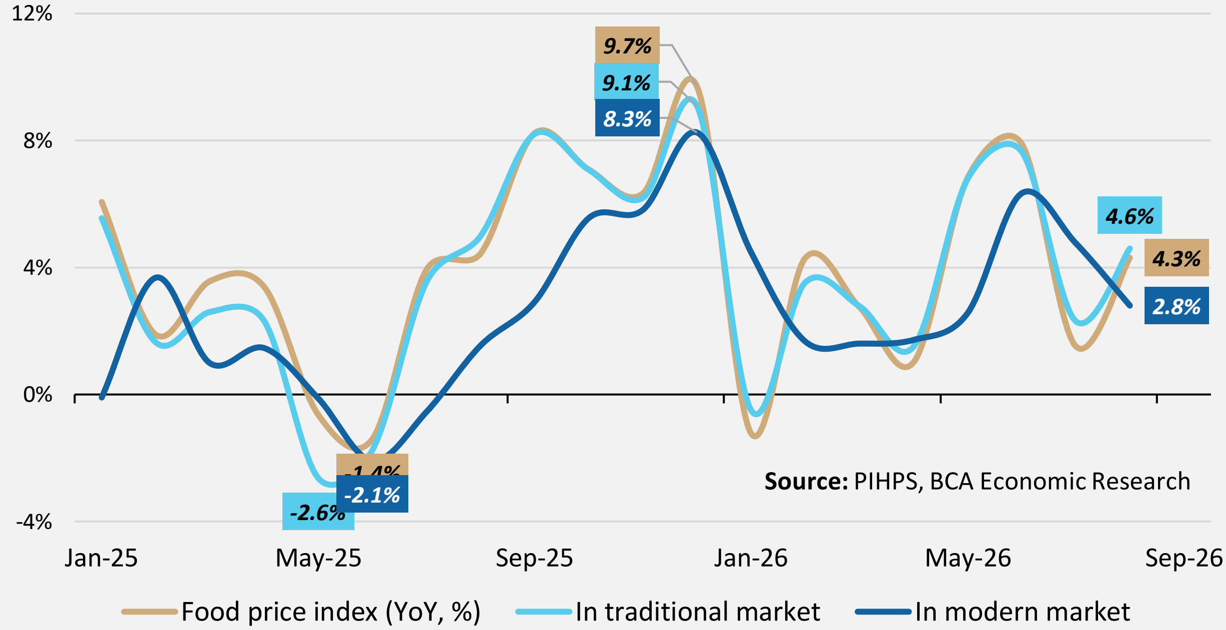


Chart 3

Wet markets cost more

Food prices in traditional markets rose higher than in modern ones, potentially exposing worse-off households to greater inflationary pressures

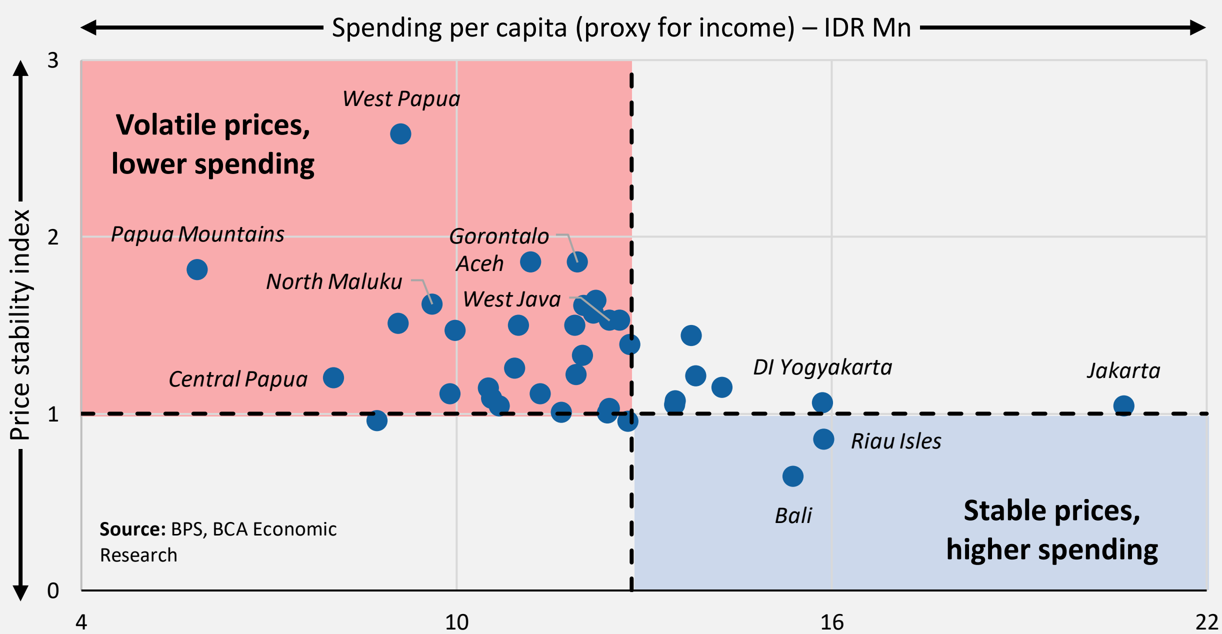


Source: PIHPS, BCA Economic Research

Chart 3

Affordability only for those who can afford it

Consumer prices tend to be more volatile in regions with weaker spending power, highlighting households' sensitivity to prices



Source: BPS, BCA Economic Research

Economic Calendar

		Actual	Previous	Forecast*
01 September 2026				
ID	S&P Global Manufacturing PMI	49.8	50.2	50.5
ID	**Trade balance (Aug-26), USD Bn**	**0.13**	**-0.45**	**-0.3**
ID	**Inflation Rate YoY, %**	**3.19**	**2.88**	**3.2**
US	S&P Global Manufacturing PMI	53.9	53.9	53.2
03 September 2026				
US	Trade balance (Jul-26), USD Bn	-88.6	-71.2	-91.2
04 September 2026				
EA	Retail Sales YoY, %	0.6	1.4	0.9
US	Non Farm Payrolls, th	162	21	42.0
07 September 2026				
ID	**Foreign Exchange Reserves, USD Bn**	**146.5**	**145.3**	**-**
08 September 2026				
CN	Trade balance, USD Bn		112.5	120.0
09 September 2026				
CN	Inflation Rate YoY, %		0.5	-
ID	Consumer Confidence		116.8	117
10 September 2026				
ID	Retail Sales YoY, %		-3	-
ID	Motorbike Sales YoY, %		8.3	-
11 September 2026				
US	Inflation Rate YoY, %		3.4	-
ID	Car Sales YoY, %		33.3	-
15 September 2026				
CN	Retail Sales YoY, %		0.6	-
16 September 2026				
US	Retail Sales YoY, %		5	-
17 September 2026				
US	**Fed Interest Rate Decision, %**		**3.75**	**4**
23 September 2026				
ID	**BI-Rate Decision, %**		**5.75**	**5.75**
ID	Loan Growth YoY, %		13.58	-
24 September 2026				
ID	M2 Money Supply YoY, %		8.3	-
30 September 2026				
US	PCE Price Index YoY, %		3.7	-

*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	3.75	Dec-25	0.35
UK	3.75	Dec-25	0.85
EU	2.40	Jun-26	-0.90
Japan	1.00	Jun-26	-0.90
China (lending)	2.00	Sep-24	3.85
Korea	3.00	Aug-26	-0.10
India	5.25	Dec-25	0.80
Indonesia	5.75	Jun-26	2.56

Money Mkt Rates	04-Sep	-1 mth	Chg (bps)
SPN (1Y)	6.79	6.82	-2.9
SUN (10Y)	7.09	7.31	-21.8
INDONIA (O/N, Rp)	5.65	6.29	-63.3
JIBOR 1M (Rp)	5.03	5.03	0.0

Bank Rates (Rp)	Jun	May	Chg (bps)
Lending (WC)	8.07	7.95	12.00
Deposit 1M	4.96	4.52	44.00
Savings	0.68	0.68	0.00

Currency/USD	04-Sep	-1 mth	Chg (%)
UK Pound	0.740	0.743	0.50
Euro	0.861	0.867	0.72
Japanese Yen	156.3	157.8	0.95
Chinese RMB	6.711	6.749	0.57
Indonesia Rupiah	17,637	18,023	2.19

Capital Mkt	04-Sep	-1 mth	Chg (%)
JCI	6,636.5	6,319.6	5.01
DJIA	53,414.3	54,085.9	-1.24
FTSE	10,831.1	10,879.4	-0.44
Nikkei 225	65,020.9	63,957.5	1.66
Hang Seng	25,650.9	25,852.9	-0.78

Foreign portfolio ownership (Rp Tn)	Aug	Jul	Chg (Rp Tn)
Stock	2,949.5	2,805.0	144.49
Govt. Bond	907.8	892.4	15.35
Corp. Bond	4.8	5.6	-0.74

Trade & Commodities	04-Sep	-1 mth	Chg (%)
Baltic Dry Index	3,628.0	2,936.0	23.6
S&P GSCI Index	735.8	652.5	12.8
Oil (Brent, $/brl)	96.3	79.4	21.3
Coal ($/MT)	153.0	134.1	14.1
Gas ($/MMBtu)	2.92	2.69	8.4
Gold ($/oz.)	4,430.0	4,078.0	8.6
Copper ($/MT)	14,490.2	14,168.9	2.3
Nickel ($/MT)	16,686.3	16,995.2	-1.8
CPO ($/MT)	1,143.7	1,102.3	3.8
Rubber ($/kg)	2.37	2.19	8.2

External Sector	Jul	Jun	Chg (%)
Export ($ bn)	26.22	25.46	2.98
Import ($ bn)	26.09	25.91	0.72
Trade bal. ($ bn)	0.12	-0.45	-127.06
Central bank reserves ($ bn)*	145.3	145.6	-0.17

Prompt Indicators	Jul	Jun	May
Consumer confidence index (CCI)	116.8	117.8	120.9
Car sales (%YoY)	33.3	33.0	14.0
Motorcycle sales (%YoY)	8.3	1.1	-5.1

Manufacturing PMI	Aug	Jul	Chg (bps)
USA	53.9	53.9	0
Eurozone	52.7	51.9	80
Japan	54.9	54.5	40
China	51.5	50.9	60
Korea	52.3	53.1	-80
Indonesia	49.8	50.2	-40

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

	2020	2021	2022	2023	2024	2025	2026E
Real GDP growth (% YoY)	-2.1	3.7	5.3	5.0	5.0	5.1	5.3
Nominal GDP growth (% YoY)	-2.5	9.9	15.4	6.7	6.0	7.6	9.1
GDP per capita (USD)	3912	4350	4784	4920	4960	5083	5126
CPI inflation (% YoY)	1.7	1.9	5.5	2.6	1.6	2.9	3.2
BI Rate (%)	3.75	3.50	5.50	6.00	6.00	4.75	6.00
SBN 10Y yield (%)	5.86	6.36	6.92	6.45	6.97	6.05	7.31
USD/IDR exchange rate (average)	14,529	14,297	14,874	15,248	15,841	16,468	17,621
USD/IDR exchange rate (end of year)	14,050	14,262	15,568	15,397	16,102	16,690	18,238
Trade balance (USD Bn)	21.7	35.3	54.5	37.0	31.0	41.1	19.2

Notes:

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

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