

Inflation: A higher floor and a lower ceiling for growth

Executive Summary:

- **Indonesia's CPI declined by 0.16% MoM as demand wound down from its Lebaran high.**
 - **The recent surge in cases would likely present more of a speed bump rather than a deep economic plunge akin to last year.** India's economic performance in the past few months – which did decline but nowhere close to the drop last year – is instructive in this regard.
 - **In the long term however, a combination of a relatively slow pace of vaccination as well as newer, more virulent strains of Covid means that Indonesia's prospects of an American or Chinese style rebound appear to be slim.**
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- **Indonesia's CPI declined by 0.16% MoM (+1.33% YoY) last month, an overall weaker number than that expected by most analysts.** Much of this was part of an expected seasonal drop as demand winds down from its Lebaran high. Indeed, those categories recording the sharpest deflation last month – foodstuffs and transportation – are staples of the annual Lebaran spike.
 - The recent surge in Covid cases however, which has already outpaced the post-Christmas surge that peaked earlier in the year, raises fresh questions about the prospects of Indonesia's economy. Would the coming months herald a decline far deeper than what a mere post-Lebaran correction could muster?
 - The likely answer, fortunately, is relatively measured. **The economic damage of such a surge would be more akin to a speed bump rather than the apocalyptic plunge observed last year.** For starters, take the extreme case of India, which was battered by a massive surge of cases in April and May. Amidst such a storm, PMI figures – even for the services sector – were still far above the abysmal numbers recorded last year, even if they did decline measurably (**Chart 1**). Relative to India, Indonesia's more commodity-oriented manufacturing sector also has the further luxury of being buttressed by currently high commodity prices.
 - So much for scenario analyses. When we turn to current domestic indicators, a similar picture emerges: a creak, but not a wholesale collapse. **While mobility numbers are quite diminished from their Lebaran peaks, current numbers suggest that the decline this time may be more measured than what we saw last year (Chart 2).** Still, it remains to be seen exactly what the full economic effects of the recently announced emergency lockdown (to be implemented on 3-20 July) will be.
 - Additionally, historical trends suggest that a partial decoupling between business activity and mobility has emerged over the past months (**Chart 2**). The likely culprits here are the online channels that businesses have been compelled to build up as the pandemic raged on. **With a much more robust foundation for online commerce relative to the early months of the pandemic, business activity should now have a greater degree of resilience against mobility restrictions.** Some note should also be made however, that declines in business activity may be more precipitous for the lower and lower middle classes, where online channels are likely to be relatively less developed.
 - There are other caveats as well. While all this may provide some relief in the short term, it also illustrates several deeper issues in the long run. For instance, the current damage being done by the Delta strain of Covid highlights the dangers of new variants, and this still without considering the potentially higher potency of newer strains yet to emerge. **When coupled with its relatively low pace of vaccinations, Indonesia's prospects of an American or Chinese style rebound appear to be slim.** Even should the current pace of a million vaccinations a day be maintained, we would not reach the government's target for herd immunity until the end of 2021.
 - **In sum then, Indonesia's growth trajectory is likely to have a higher floor and a lower ceiling than previously expected.** We are unlikely to see an economic cratering on the scale of what we saw in 2020, even if there is another large surge of cases. The very fact however, that an under-vaccinated Indonesia may remain trapped in a precarious limbo where the threat of a renewed surge lurks in every corner for the foreseeable future, means that recovery in the long run is unlikely to swiftly return to pre-Covid levels just yet.

Chart 1. While PMI figures in India declined somewhat during the Covid surge of the past few months, they remain much higher than their lowest points last year

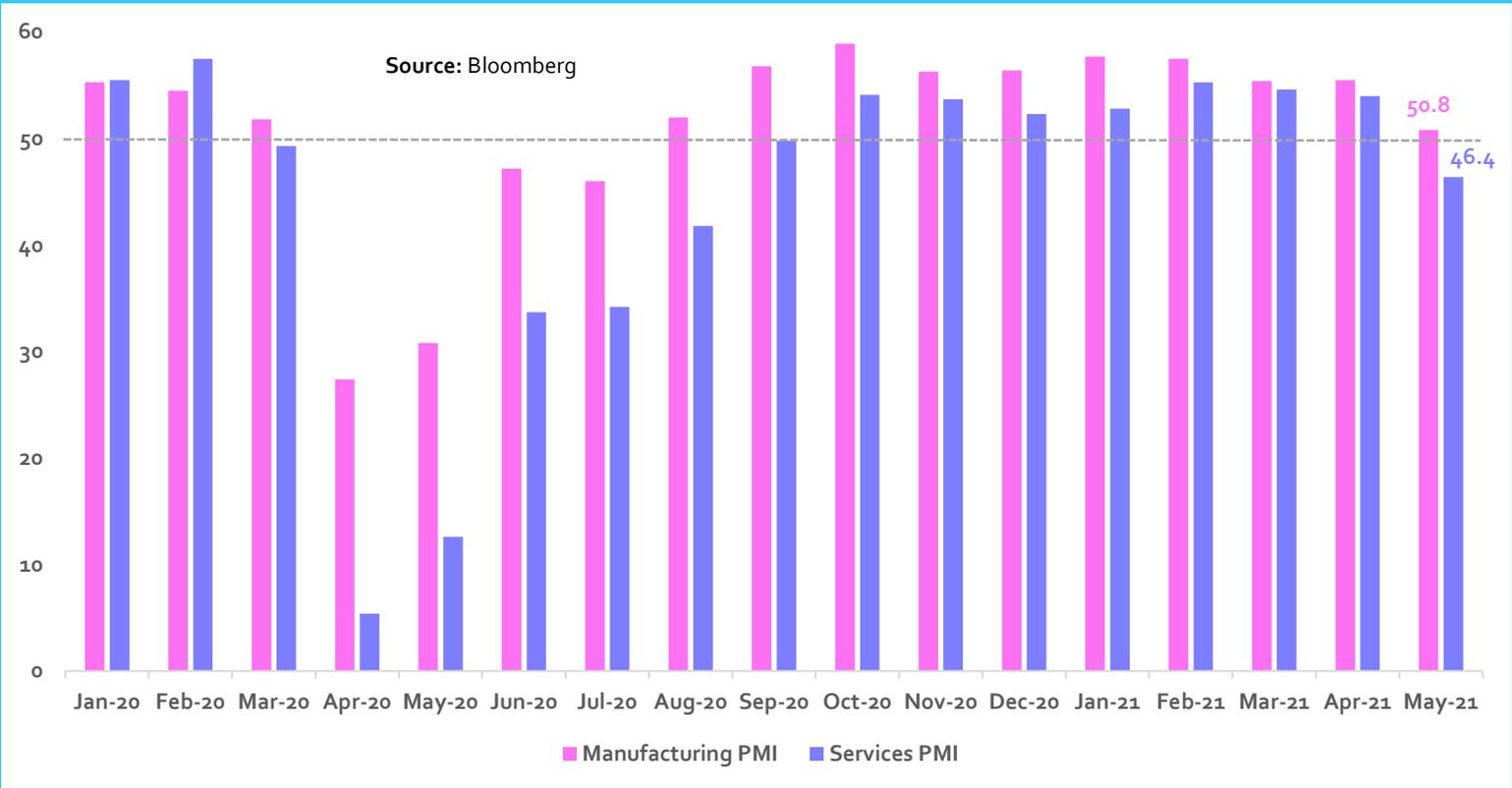
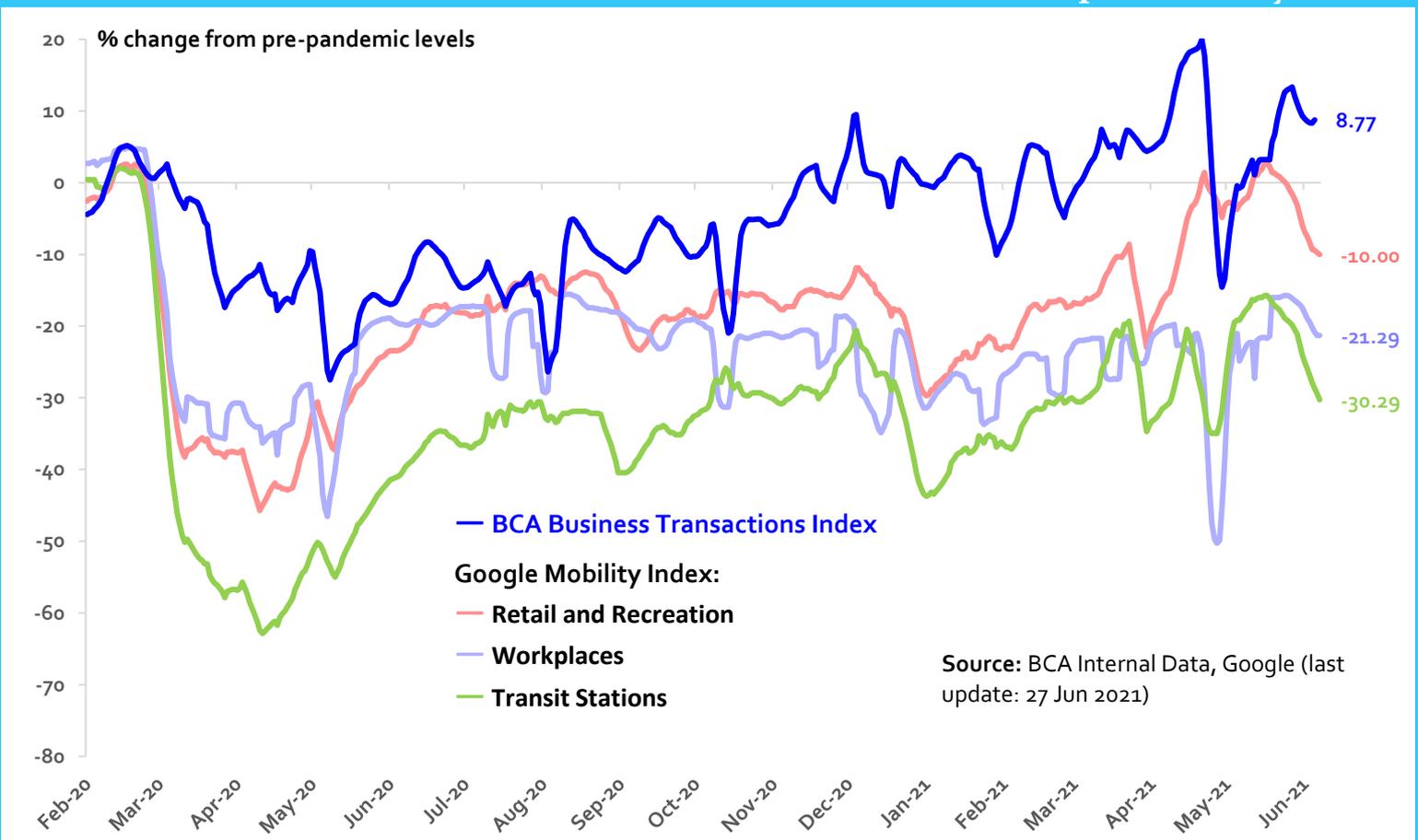


Chart 2. Business transactions continued to increase beginning late last year even as mobility indices remained stagnant or decreased. The recent decline in transactions is also much more modest relative to the drop in mobility



Selected Recent Economic Indicators

| Key Policy Rates | Rate (%) | Last Change | Real Rate (%) | Trade & Commodities | 30-Jun | -1 mth | Chg (%) |
|-------------------------------------|----------|-------------|---------------|---------------------------------|----------|----------|-----------|
| US | 0.25 | Mar-20 | -4.75 | Baltic Dry Index | 3,383.0 | 2,596.0 | 30.3 |
| UK | 0.10 | Mar-20 | -2.00 | S&P GSCI Index | 536.0 | 519.2 | 3.2 |
| EU | 0.00 | Mar-16 | -1.90 | Oil (Brent, \$/brl) | 75.1 | 69.6 | 7.9 |
| Japan | -0.10 | Jan-16 | 0.00 | Coal (\$/MT) | 128.9 | 108.9 | 18.3 |
| China (lending) | 4.35 | Oct-15 | 3.05 | Gas (\$/MMBtu) | 3.72 | 2.84 | 31.0 |
| Korea | 0.50 | May-20 | -2.10 | Gold (\$/oz.) | 1,770.1 | 1,903.8 | -7.0 |
| India | 4.00 | May-20 | -2.30 | Copper (\$/MT) | 9,351.5 | 10,248.3 | -8.8 |
| Indonesia | 3.50 | Feb-21 | 2.17 | Nickel (\$/MT) | 18,212.0 | 18,078.0 | 0.7 |
| Money Mkt Rates | 30-Jun | -1 mth | Chg (bps) | CPO (\$/MT) | 947.1 | 1,008.7 | -6.1 |
| SPN (1M) | 1.98 | 2.67 | -69.2 | Rubber (\$/kg) | 1.59 | 1.69 | -5.9 |
| SUN (10Y) | 6.57 | 6.42 | 14.3 | External Sector | May | Apr | Chg (%) |
| INDONIA (O/N, Rp) | 2.80 | 2.79 | 0.6 | Export (\$ bn) | 16.60 | 18.49 | -10.3 |
| JIBOR 1M (Rp) | 3.56 | 3.56 | -0.3 | Import (\$ bn) | 14.23 | 16.20 | -12.2 |
| Bank Rates (Rp) | Apr | Mar | Chg (bps) | Trade bal. (\$ bn) | 2.36 | 2.29 | 3.2 |
| Lending (WC) | 9.08 | 9.12 | -3.94 | Central bank reserves (\$ bn) | 136.4 | 138.8 | -1.73 |
| Deposit 1M | 3.68 | 3.74 | -6.64 | Prompt Indicators | May | Apr | Mar |
| Savings | 0.80 | 0.83 | -2.82 | Consumer confidence index (CCI) | 104.4 | 101.5 | 93.4 |
| Currency/USD | 30-Jun | -1 mth | Chg (%) | Car sales (%YoY) | 1,443.6 | 902.9 | 10.6 |
| UK Pound | 0.723 | 0.705 | -2.52 | Motorcycle sales (%YoY) | 1,065.7 | 282.0 | -7.2 |
| Euro | 0.843 | 0.820 | -2.74 | Cement sales (%YoY) | #N/A | 8.3 | 10.9 |
| Japanese Yen | 111.1 | 109.9 | -1.13 | Manufacturing PMI | Jun | May | Chg (bps) |
| Chinese RMB | 6.457 | 6.369 | -1.37 | USA | N/A | 61.2 | 0 |
| Indonesia Rupiah | 14,500 | 14,285 | -1.48 | Eurozone | 63.1 | 63.1 | 0 |
| Capital Mkt | 30-Jun | -1 mth | Chg (%) | Japan | 52.4 | 53.0 | -60 |
| JCI | 5,985.5 | 5,848.6 | 2.34 | China | 51.3 | 52.0 | -70 |
| DJIA | 34,502.5 | 34,529.5 | -0.08 | Korea | 53.9 | 53.7 | 20 |
| FTSE | 7,037.5 | 7,022.6 | 0.21 | Indonesia | 53.5 | 55.3 | -180 |
| Nikkei 225 | 28,791.5 | 29,149.4 | -1.23 | | | | |
| Hang Seng | 28,828.0 | 29,124.4 | -1.02 | | | | |
| Foreign portfolio ownership (Rp Tn) | Jun | May | Chg (Rp Tn) | | | | |
| Stock | 1,893.1 | 1,892.8 | 0.34 | | | | |
| Govt. Bond | 977.4 | 957.5 | 19.95 | | | | |
| Corp. Bond | 26.6 | 27.5 | -0.96 | | | | |

Source: Bloomberg, BI, BPS

Notes:

*Previous data

For change in currency: **Black indicates appreciation against USD, **Red** indicates depreciation

***For PMI, > 50 indicates economic expansion, < 50 indicates contraction

Indonesia – Economic Indicators Projection

| | 2016 | 2017 | 2018 | 2019 | 2020 | 2021E |
|--|--------|--------|--------|--------|--------|--------|
| Gross Domestic Product (% YoY) | 5.0 | 5.1 | 5.2 | 5.0 | -2.1 | 4.5 |
| GDP per Capita (US\$) | 3605 | 3877 | 3927 | 4175 | 3912 | 4055 |
| Consumer Price Index Inflation (% YoY) | 3.0 | 3.6 | 3.1 | 2.7 | 1.7 | 3.1 |
| BI 7 day Repo Rate (%) | 4.75 | 4.25 | 6.00 | 5.00 | 3.75 | 3.50 |
| USD/IDR Exchange Rate (end of year)** | 13,473 | 13,433 | 14,390 | 13,866 | 14,050 | 14,460 |
| Trade Balance (US\$ billion) | 8.8 | 11.8 | -8.5 | -3.2 | 21.7 | 15.0 |
| Current Account Balance (% GDP) | -1.8 | -1.6 | -3.0 | -2.7 | -0.4 | -1.3 |

** Estimation of Rupiah's fundamental exchange rate

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