

## BoP: The financial account proves to be the weaker link

### Executive Summary:

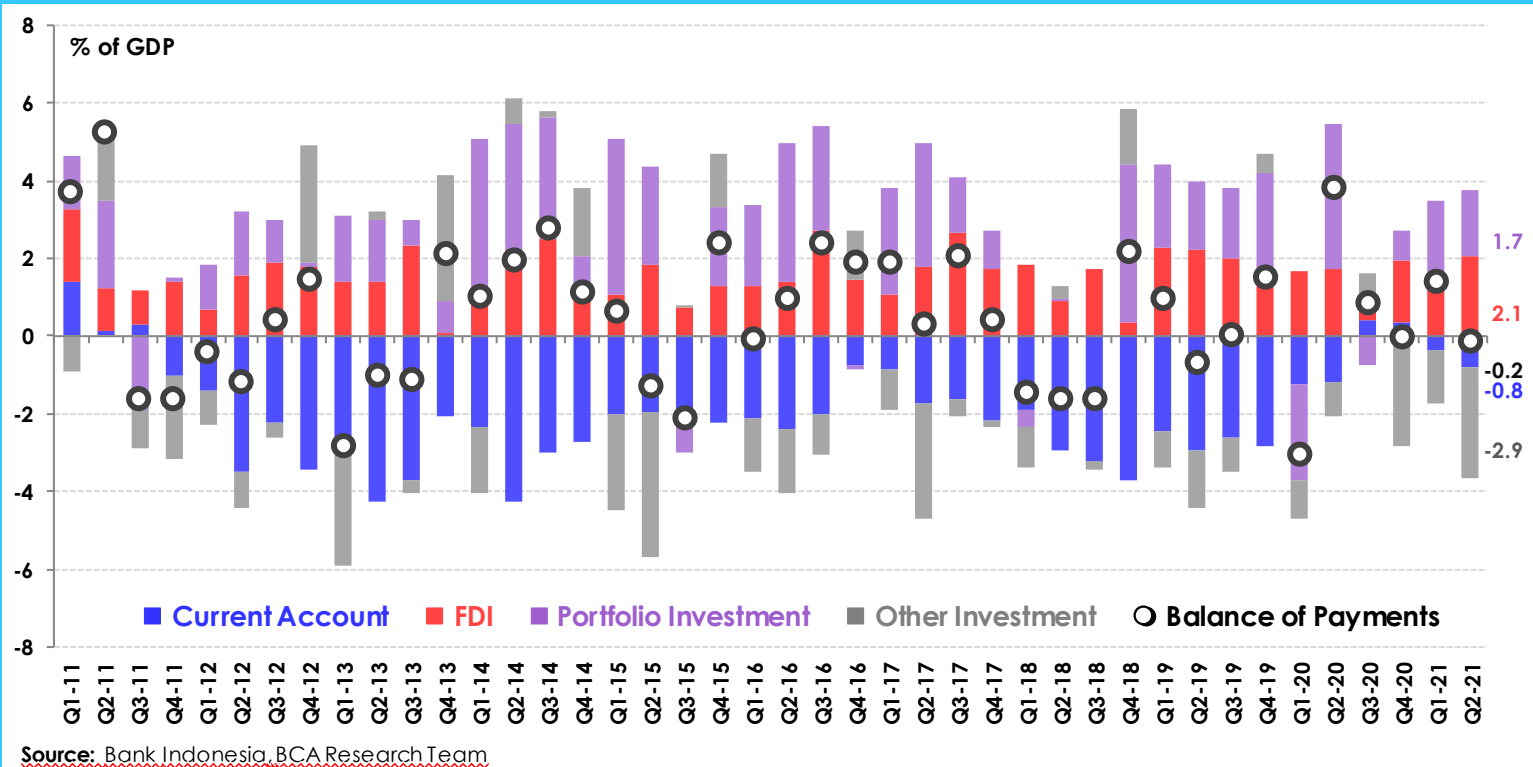
- **Indonesia's balance of payments (BoP) registered a slight deficit of USD 0.5 Bn in Q2-2021.**
- Although the seasonal repatriation of dividends was a slight drag on the current account, **the trade balance itself remained remarkably robust, despite expectations of a Lebaran-driven decline.**
- **The largest decline however, was observed in the financial account, with outflows largely driven by SOE and government debt repayments.**
- **In general, the financial account is likely to be a bigger vulnerability than the current account in the coming months.** Aside from looming SOE and government debt repayments, concerns of tapering and risk-off sentiments triggered by Delta are likely to weigh down on capital inflows.

- **Indonesia's balance of payments (BoP) registered a slight deficit of USD 0.5 Bn in Q2-2021** as both the current and financial accounts declined from their Q1 figures (**Chart 1**).
- At first glance, the doubling of the current account deficit from Q1 may appear alarming. A closer glance however, reveals that much of this was merely driven by the seasonal repatriation of dividends overseas. **The trade balance on the other hand – the beating heart of the current account – remained surprisingly robust and even increased its surplus,** despite expectations of a diminished surplus in the second quarter due to continued recovery and the onset of Lebaran. While imports did increase in line with these trends, they were more than matched by a commensurate increase in exports as well.
- **A point of concern that may be noted however, is the continuing decline in the services balance, which is emerging as a glaring weak link in the current account.** On the one hand, continued travel restrictions have dealt a severe blow to Indonesia's main services export earner. At the same time, rising global shipping costs and increased domestic demand have driven shipping-related imports. Digital trends spurred on by Covid have also driven IT service-related imports, such as subscription fees for foreign video conferencing platforms like Zoom (**Chart 2**).
- The much larger deterioration however, was observed in the financial account. **It is important to note that both direct and portfolio inflows were actually quite robust in Q2-2021 (Chart 1).** Foreign direct investment, perhaps driven by some combination of increased confidence in structural reforms and the need to shore up bottlenecks in global supply chains, had been consistently growing at a rapid pace in the past few quarters. Q2 also saw the return of substantial portfolio inflows as fears of increasing treasury yields in Q1 began to subside, and expectations of a vaccine-driven recovery reached a fever pitch (at least before the onset of Delta).
- The precipitous decline in the financial account then, was largely driven by increased outflows in other investments (**Chart 1**). Much of these outflows were likely related to debt repayments by the government and SOEs. It is tempting to write this off as a one-off event. **Unfortunately, a quick glance at SOE and government bond maturities indicate that a substantial amount of debt will be coming due in the next few years,** with the total amount of government and SOE bonds maturing this year already double the average for the past few years (**Chart 3**).
- The looming mountain of maturing public debt illustrates an emerging point: **that the financial account is likely to be a bigger vulnerability than the current account in the coming months.** The key pillar of the current account, the trade balance, has consistently registered large surpluses in the past few months. Recent trade figures from BPS also suggest that the current Delta-driven surge in cases is not likely to alter this trend too much, at least for the near future. A more lasting calm on the current account front then, seems plausible.
- The financial account, in contrast, is likely to face a great deal of headwinds. **Aside from SOE and government debt repayments, the market's current risk-off sentiment due to the spread of Delta, as well as fears concerning the looming beginning of the Fed's tapering cycle, are factors likely to weigh down on capital inflows.** There are a few buffers in place, such as BI's large FX reserves, the continuous decline in Indonesia's Covid caseloads, as well as other events likely

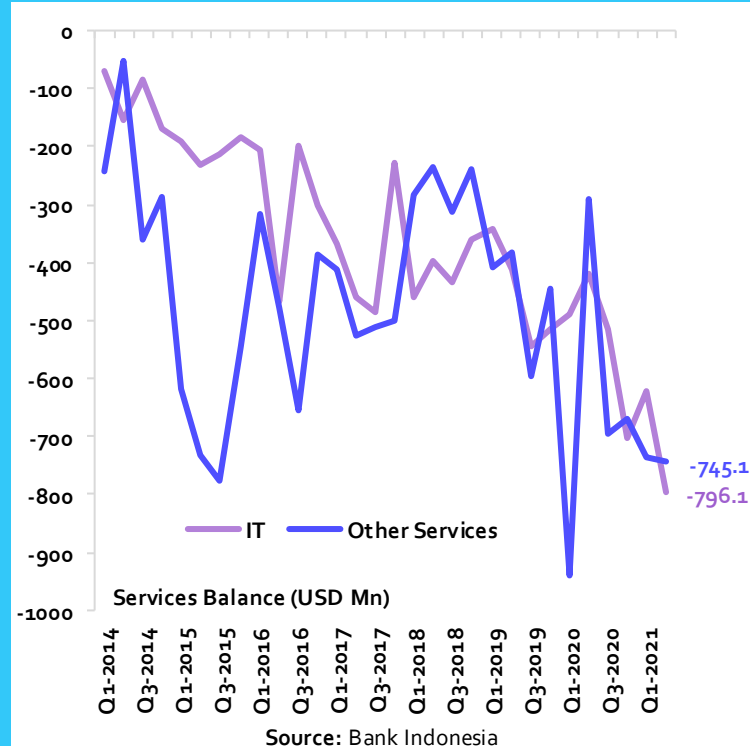
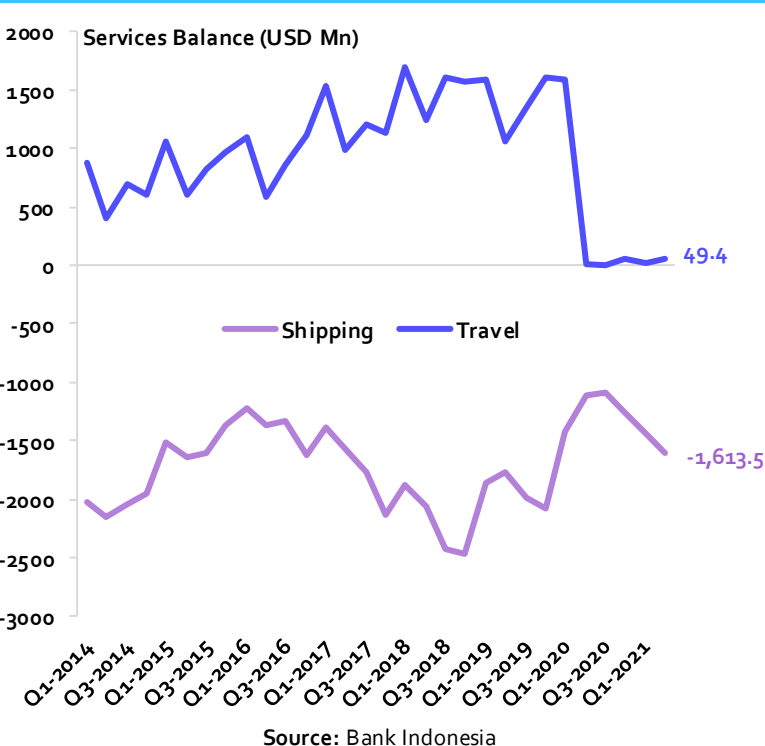
to boost inflows such as the upcoming listing of a few Indonesian big tech companies, as well as the recently

enacted Omnibus Law. Nonetheless, the aforementioned risks mean that extra caution remains necessary.

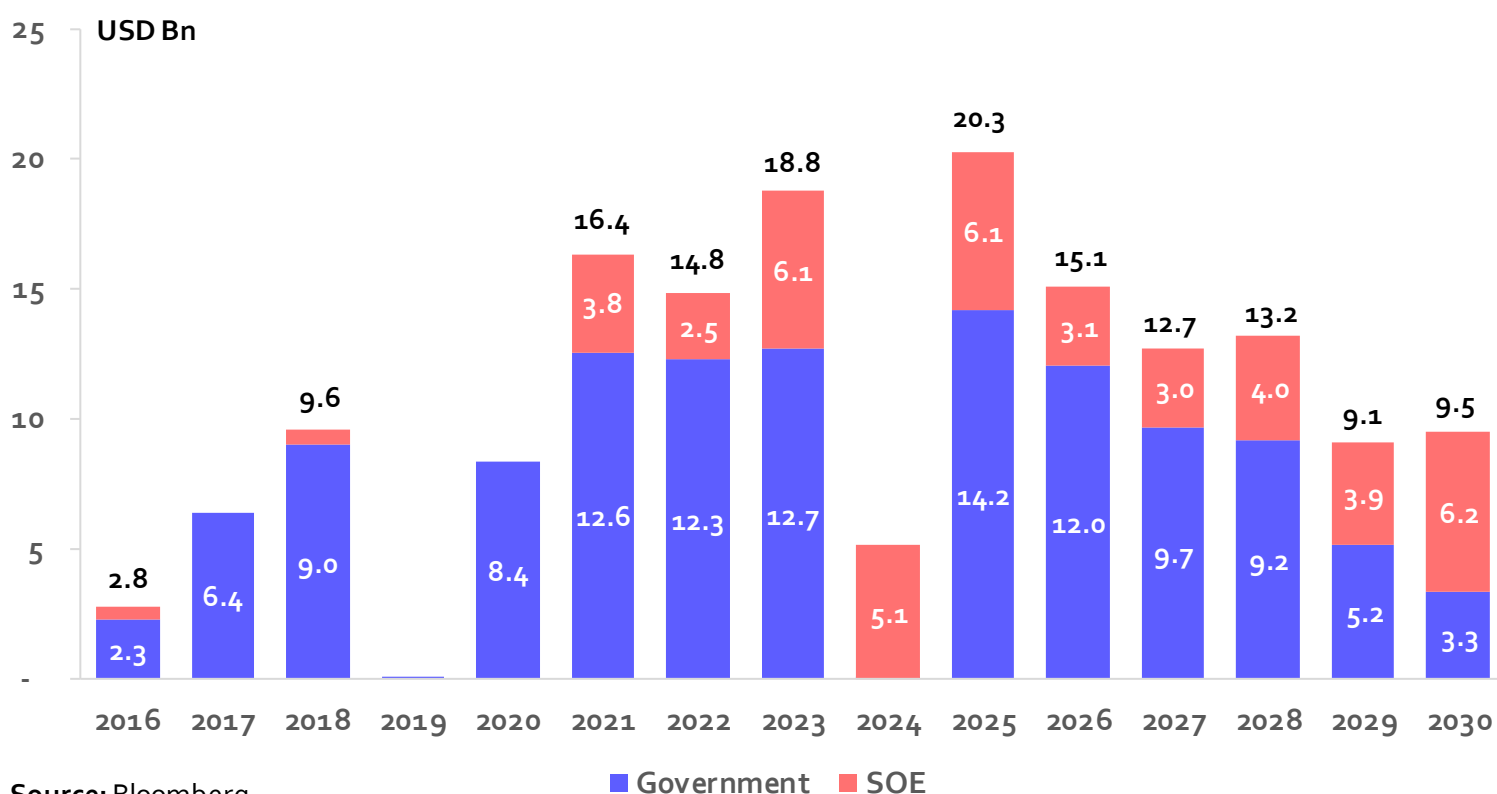
**Chart 1. Despite robust portfolio and direct investment inflows, SOE and government related debt repayments fueled significant investment outflows**



**Chart 2. The decline in tourism has deprived Indonesia of its largest services export earner. At the same time however shipping and IT services-related imports continue to increase.**



**Chart 3. Maturing SOE and government bonds are expected to increase sharply over the next few years, in part due to the large raft of SOE debt beginning to come due from this year**



**Table 1. Balance of Payment (current USD Million)**

	Q2-20	Q3-20	Q4-20	Q1-21	Q2-21	2018	2019	2020
<b>CURRENT ACCOUNT</b>	<b>-2,895</b>	<b>1,022</b>	<b>862</b>	<b>-1,057</b>	<b>-2,231</b>	<b>-30,633</b>	<b>-30,279</b>	<b>-4,452</b>
(as % of GDP)	-1.18	0.39	0.32	-0.38	-0.77	-2.94	-2.71	-0.42
A. Goods	3,952	9,791	9,964	7,628	8,098	-228	3,508	28,214
- Non-Oil/Gas	3,289	9,441	11,328	9,976	11,581	11,186	11,965	29,867
- Oil/Gas	-821	-715	-1,233	-2,269	-3,383	-11,405	-10,319	-5,386
B. Services	-2,129	-2,741	-3,088	-3,371	-3,653	-6,485	-7,641	-9,687
C. Income	-6,158	-7,399	-7,442	-6,746	-8,141	-30,815	-33,775	-28,911
D. Current Transfers	1,440	1,371	1,428	1,432	1,465	6,895	7,629	5,932
<b>CAPITAL TRANSACTIONS</b>	<b>5.60</b>	<b>6.72</b>	<b>23.79</b>	<b>2.20</b>	<b>5.00</b>	<b>97.16</b>	<b>39.06</b>	<b>36.91</b>
<b>FINANCIAL TRANSACTIONS</b>	<b>11,044</b>	<b>867</b>	<b>-1,049</b>	<b>5,548</b>	<b>1,913</b>	<b>25,122</b>	<b>36,564</b>	<b>7,816</b>
A. Direct Investment	4,433	939	4,217	4,173	5,348	12,511	20,531	13,858
B. Portfolio Investment	9,744	-1,984	1,952	4,904	4,378	9,312	21,990	3,369
C. Derivative Instruments	124.70	18.02	201.46	110.06	23.75	33.61	186.40	17.73
D. Other Investment	-3,257	1,894	-7,420	-3,639	-7,837	3,266	-6,144	-9,428
<b>NET ERRORS AND OMISSIONS</b>	<b>1,090.12</b>	<b>156.34</b>	<b>6.75</b>	<b>-428.12</b>	<b>-136.97</b>	<b>-1,717.35</b>	<b>-1,647.91</b>	<b>-804.94</b>
<b>BALANCE OF PAYMENT</b> (= change in BI international reserves)	<b>9,245</b>	<b>2,053</b>	<b>-156</b>	<b>4,065</b>	<b>-450</b>	<b>-7,131</b>	<b>4,676</b>	<b>2,597</b>

## Indonesia – Economic Indicators Projection

	2016	2017	2018	2019	2020	2021E
Gross Domestic Product (% YoY)	5.0	5.1	5.2	5.0	-2.1	3.6
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	2.3
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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