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Indonesia update - 19 January 2018

Growth prospects are favorable this year and the stronger IDR recently and in the near term could help moderate import-related inflation pressures, allowing Bank Indonesia (BI) to keep the policy unchanged in 2018

In this bundle

Indonesia: BI is likely to keep policy rates steady

Bank Indonesia (BI), Indonesia's central bank, is likely to keep monetary policy settings steady at tomorrow's meeting

Source: istock

There are no compelling reasons to tweak policy settings

Recent factors that BI considers in deciding on monetary policy settings are quite favorable. Inflation is expected to remain within the 2018 target range of 2.5% to 4.5%%. Growth is expected to moderately accelerate. The IDR has recently appreciated and is likely to achieve the target rate of Indonesia's fiscal program.

Inflation in 2018 is likely to remain within target.

We expect inflation to average 3.7% in 2018, a shade below the Bloomberg consensus forecast of 3.8% and near the government's 2018 point-target of 3.5% inflation. Nevertheless, the inflation forecasts are within the central bank's inflation target range of 2.5% to 4.5%. Preliminary January inflation forecast by BI is 0.6% MoM which translates to a 3.2% YoY inflation. The government continues to take steps to address some inflation pressures that led to the upside inflation surprise of 3.6% in December. Food inflation accelerated to 1.3% in December from November's YoY contraction of 0.5%. The government is allowing rice imports to augment local supplies from next month. This year's energy subsidies will likely keep administered energy prices stable at least in the short-term. Fiscal leeway could allow this stability to continue in 2H as the country heads to regional elections by mid-year and national elections in 2019.

3.7%

2018 inflation forecast

Within BI's target range of 2.5% to 4.5%

Growth is likely to improve in 2018

Growth prospects are favorable this year. Bloomberg's consensus forecast shows a mild acceleration of growth to 5.3% in 2018 from the estimated 2017 GDP growth of 5.1%. We believe that there are reasons why GDP growth should achieve the government's target rate of 5.4%. Sustained infrastructure spending together with improvements in business spending will underpin overall economic activity. Household spending, a concern in 2017, is likely to also improve as inflation has moderated and is expected to stabilize. In addition, a mild push from election spending would contribute to a higher overall economic growth.

5.4%

GDP growth in 2018

Improvements in business and household spending

IDR strength would moderate inflation pressures

The IDR has appreciated by 1.8% in the past two weeks. Indonesia's local currency bond yields are one of the highest in the region. This has attracted investors to increase their local currency bond exposure. We estimate that investors have poured an additional $1.9bn into local currency government bonds recently. We are in line with Bloomberg consensus of a year-end currency exchange rate of IDR13500. This is also in line with this year's government budget assumption of IDR13500. Trading of the IDR will likely range from the prevailing IDR13300 to IDR13500 this year. The stronger IDR recently and in the near term could help moderate import-related inflation pressures.

Snap | 15 January 2018 Indonesia

Indonesia: Current Account stress from weak December exports

Any downside growth surprise from exports in December would lead to a less favorable current account deficit expectation

Source: istock

6.9%

December export growth

disappointing export performance

Worse than expected

Downside growth surprise from exports

Any downside growth surprise from exports in December would lead to a less favorable current account deficit expectation. Decmber import growth of 17.8% was roughly in line with the market forecast of 18.1%. Weak exports and relaitvely strong imports resuled to the second monthly deficit in 2017, at -$271m in December, a reversal of the $1.1bn surplus in December 2016. December exports were up 6.9% YoY, only half the market forecast. Non-oil exports were a major disappointment, posting only a 5.6% YoY increase, a third of the 11M average growth of 18% and below our forecast of 15%. Possibly slower demand and negative base effects resulted to the weakness. Import growth on the other hand resulted from 50% YoY growth in oil and gas imports and a 13% YoY increase in non-oil imports. Non-oil import growth was slower than then 11M average growth of 15.6%.

Current account deficit for 4Q forecast likely to be larger than 4Q16

The 4Q17 current account deficit could reach $4bn with a significantly lower trade surplus of just $945m -30% of the trade suplus of $3.1bn in 4Q16. We had earlier expected a current account deficit of only $3bn on a trade surplus of $2.2bn. The rvised current account deficit forecast of $4bn is equivalent to 1.7% of GDP. The full year 2017 current acocunt deficit would likely amount to $15.5bn or 1.5% of GDP. Bank Indoensia, Indonesia's central bank, expects the 2017 current acocunt deficit o be below 2% of GDP. We expect export growth in 2018 to slightly outpace import growth, reuslting to a trade suplus of $14.5bn and a current account deficit of $18bn or 1.6% of GDP.