Bank Indonesia holds rate against backdrop of slowing growth

Indonesia's central bank held rates steady to support the economy as the outlook dims

Bank Indonesia trimmed the country's GDP growth forecast to 4.5-5.3%

3.5%

7-day reverse repurchase rate

policy rate

As expected

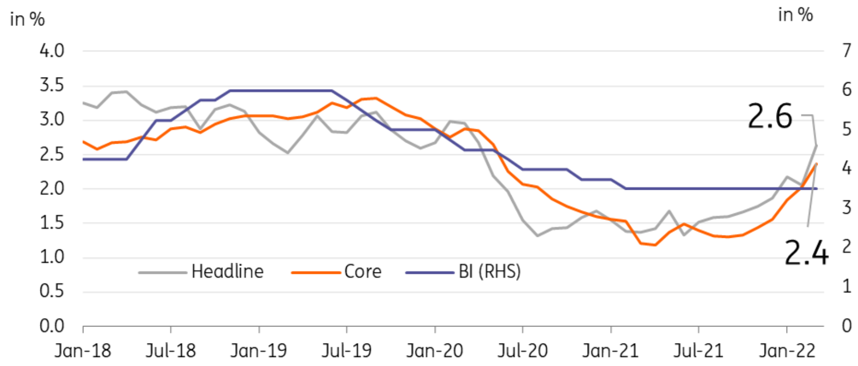
Bank Indonesia keeps policy rate at 3.5%

Against a backdrop of slowing global growth, Bank Indonesia (BI) held its 7-day reverse repurchase rate at 3.5%, as expected. The central bank also lowered its growth projection for Indonesia, trimming its GDP growth forecast to 4.5-5.3% (compared to 4.7-5.5% previously). Meanwhile, BI still expects inflation to be "manageable" this year with headline inflation to settle within target of 2-4%. Slowing growth, alongside still manageable inflation, gave BI licence to keep rates untouched even as global central banks tighten policy.

A shift in tone we were not expecting

We had previously expected a potential shift in tone at today's BI policy meeting, one that would set the stage for potential rate hikes in the near term. What we got instead was a shift in tone that suggested BI is now more inclined to retain accommodation as concerns about growth have surfaced. One development that could have helped convince monetary authorities to stay dovish was the revised projection for the current account balance, now expected to see a slight improvement as exports benefit from surging commodity prices. An improved external outlook helps provide support for the Indonesian rupiah (IDR) in the near term, which could in turn help mitigate imported inflation pressure.

BI to monitor inflation trajectory



Source: Badan Pusat Statistik and Bank Indonesia

Still watching out for likely core inflation spike

Despite today's somewhat dovish pause, we expect BI Governor Perry Warjiyo to remain watchful for any buildup in inflationary pressure. Warjiyo had previously indicated that any decision to tighten policy would be based on core inflation trends. With core inflation heating up last March (2.4% from 2.0% previously) and with signs pointing to a sustained acceleration of this indicator, BI may still need to consider a shift in tone at the May or June meetings. We expect core inflation to crest 3% in the coming months, a development that could still push BI to tighten policy rates amid the backdrop of slowing growth should inflation threaten the upper end of BI's inflation target.

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