

Indonesia's central bank cuts policy rate to bolster economy

Indonesia's central bank finally trimmed the policy rate as pressure on the economy mounts leaving the door wide open for more rate cuts



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4.25%

As expected

7-day reverse repurchase

BI policy rate

Central bank's new projections don't look too great

Emerging from the partial lockdown in June, Indonesia's economy has already shown signs of stress with both trade and PMI data pointing to a probable contraction in GDP by 2Q.

Bank Indonesia's Governor Warjiyo announced a downward revision to GDP growth for 2020 with the central bank now expecting growth to expand by just 0.9-1.9% as it predicts a weak 2Q GDP performance.

The central bank's latest forecast for the external position with the current account deficit expected to settle at 1.5% of GDP is likely due to import compression. What is clear is that the

economic outlook remains dim as Indonesia continues to report more than a thousand new daily Covid-19 infections.

The rupiah steadies

With economic growth faltering, the central bank opted to finally cut policy rates to shore up the sagging growth momentum.

Governor Warjiyo had made it clear that currency stability was a key decision variable for any sort of easing and with IDR steadying of late and the economy on a downturn, the Bank lowered its policy rate by 25 bps to 4.25%.

Despite recent resilience, Warjiyo still believes the rupiah remains “undervalued”, expecting the currency to enjoy another bout of strengthening in the near term in line with Indonesia’s fundamentals.

Warjiyo’s pledge: Support growth

Governor Warjiyo carried out a dovish cut, trimming the 7-day reverse repurchase rate by 25 basis points while leaving the door wide open for more monetary easing.

With well-behaved inflation and the currency enjoying some stability, we expect governor Warjiyo to cut policy rates further in 3Q with the economy sorely in need of additional stimulus from both fiscal and monetary authorities.

Despite the rate cut, IDR may enjoy slight appreciation pressure driven by Warjiyo’s comments on the IDR being “undervalued” but we expect another bout of depreciation in the coming months as economic indicators will likely point to contracting growth in 2Q and possibly in the third-quarter too.

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