LPEM FEB UI
Institute for Economic and Social Research

Macroeconomic Analysis Series

BI Board of Governor Meeting

December 2024

Highlights

- Bank Indonesia should keep the BI Rate unchanged at 6.00%.
- Headline inflation registered at 1.55% (y.o.y.), approaching the lower end of Bank Indonesia's target range, driven by high-base effect and adequate supply of food ingredients.
- Indonesia suffered a capital outflow of around USD0.75 billion and Rupiah depreciation of 1.39% (m.t.m) due to the looming threat of Trump's trade war.

Macroeconomics, Finance & Political Economy Research Group

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Inflation in November 2024 declined to 1.55% (y.o.y) and reached its lowest level since April 2021. Lower inflation figure in November 2024 was mainly driven by lower inflationary pressure of food ingredients and deflation in volatile food prices due to the high-base effect and adequate supply of food ingredients after harvest season. Capital markets across developing countries have been under selling pressure in the past two months amid worries over potential U.S. tariff hikes on regional exports under Donald Trump's administration. Consequently, Indonesia suffered a capital outflow of around USD0.75 billion since mid-November and depreciated Rupiah by 1.39% (m.t.m) from IDR15,770 per USD to IDR15,990 per USD in the last 30 days. Given the mounting pressure on Rupiah, we believe BI should keep the BI rate unchanged at 6.00% in December's Board of Governor meeting.

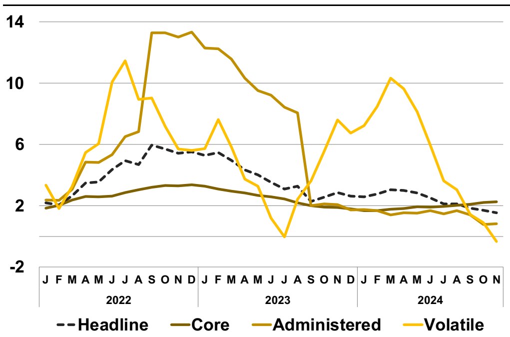
Lower End of Inflation Target

Headline inflation decreased further nearing the lower end of Bank Indonesia's inflation target range (1.5% to 3.5%), recorded at only 1.55% (y.o.y) in November 2024, down from 1.71% (y.o.y) in October 2024, the lowest inflation rate since April 2021 (Figure 1). A decline in the inflation of food ingredients, coupled with deflation in volatile food prices, were among the main factors driving the decrease of overall inflation figure. The drop in price pressure in volatile foods and food ingredients was due to the high-base effect and adequate supply of food ingredients after harvest season. The Government of Indonesia's (GoI) price-sustaining measures, such as fuel price adjustments, also contribute to lower costs across various economic activities. Inflation in the food, beverages, and tobacco group dropped from 2.35% (y.o.y) in October 2024 to 1.68% (y.o.y) in November 2024. Information, communication, and financial services group inflation remain unchanged at -0.28% (y.o.y) from September to November 2024. Year-end seasonality brought slight improvements in transportation inflation, which rose from -0.08% (y.o.y) in October 2024 to 0.03% (y.o.y) in November 2024. Restaurants followed a similar trend, with inflation ticking up from 2.36% (y.o.y) in October to 2.40% (y.o.y) in November 2024, the highest for the past six months.

Looking at monthly data, headline inflation continued to recover from the deflationary trend of preceding periods, rising from 0.08% (m.t.m) in October 2024 to 0.30% (m.t.m) in November 2024 (Figure 2). This increase was driven by higher prices in the food, beverage, and tobacco group, which climbed from 0.09% (m.t.m) in October 2024 to 0.78% (m.t.m) in November 2024, the highest level since April 2024, contributing 0.22 percentage points to the monthly inflation.

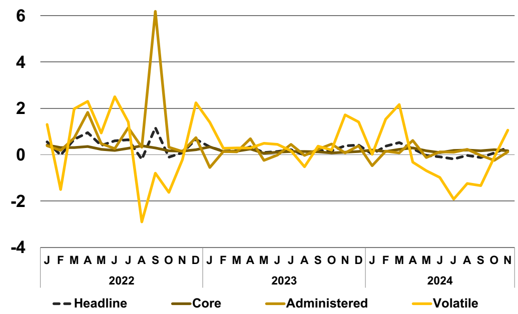
Core inflation recorded a slight increase to 2.26% (y.o.y) in November 2024, up from 2.21% (y.o.y) in October 2024 (Figure 1). On the other hand, the monthly trend indicated a slight decrease from 0.22% (m.t.m) in October 2024 to 0.17% (m.t.m) in November 2024 (Figure 2). Similar to the previous month, inflation was driven by commodity prices amidst managed inflation expectations, with key contributors including gold jewellery with increased demand as a safe-haven asset from global uncertainties, cooking oil due to higher production costs and rainy season distribution constraints, and ground coffee driven by climate-induced crop failures and high global demand.

Figure 1: Inflation Rate (%, y.o.y)



Source: CEIC

Figure 2: Inflation Rate (%, m.t.m)



Source: CEIC

While administered prices slowly recovered from their downward trend, volatile food experienced its first annual deflation since August 2023. Volatile food recorded inflation at -0.32% (y.o.y) in November 2024, a significant decline from 0.89% (y.o.y) in October 2024 (Figure 1) being the lowest since September 2020. This annual deflation is attributed to lower prices of various chili types driven by harvest season stable production levels. Meanwhile, month-to-month inflation reached 1.07% (m.t.m) in November 2024 up from -0.11% (m.t.m) in October 2024 (Figure 2), a typical pattern based on historical trends ahead of the Christmas and New Year holiday season. Administered prices experienced a modest increase in annual inflation, rising from 0.77% (y.o.y) in October 2024 to 0.82% (y.o.y) in November 2024 (Figure 1). Recovery was also observed in the monthly figure, from -0.25% (m.t.m) in October 2024 to 0.12% (m.t.m) in November 2024 (Figure 2). Inflation in the administered prices category was mainly driven by machine-rolled clove cigarettes (SKM) and air transportation fares, reflecting the continued transmission of increased tobacco excise duties and higher public mobility as the year approaches its end.

Key Figures

BI-Rate (Nov '24)
6.00%
GDP Growth (y.o.y, Q3 '24)
4.95%
Inflation (y.o.y, Nov '24)
1.55%
Core Inflation (y.o.y, Nov '24)
2.26%
Inflation (m.t.m, Nov '24)
0.30%
Core Inflation (m.t.m, Nov '24)
0.17%
FX Reserve (Nov '24)
USD150.2 billion

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Although monthly inflation is rising due to seasonal factors, annual inflation is trending downward, approaching the lower end of the inflation target range, only 0.05 percentage point short of reaching outside the target. The declining trend cannot be attributed to low optimism as Consumer Confidence Index (CCI) rose to 125.9 in November 2024 from 121.1 in October 2024, likely influenced by the upcoming end-of-year holiday season. Bank Indonesia remains confident that inflation will stay within the 1.5% to 3.5% target range in 2024 and 2025. In the upcoming months, inflation may rise, given heightened holiday demand, as well as crop failures and logistical disruptions due to high rainfall, which disrupt the supply chain. Additional inflationary pressure risk stems from the potential introduction of new tariffs under Trump administration, which could drive up cost of imports and contribute to imported inflation. However, given recent declines in inflation, even though the final months of the year typically boost demand due to heightened seasonality, the issue appears to be rooted in weak demand driven by low purchasing power, evident as most expenditure groups are experiencing annual inflation rates below Bank Indonesia's target.

Imports Drop Outpaces Exports, Bolstering the Trade Balance

Indonesia sustained its trade surplus in November 2024, accompanied by both month-to-month and year-to-year growth. A trade surplus of USD4.42 billion was achieved this month, reflecting an increase of 1.94% (m.t.m) from USD2.48 billion surplus in October 2024 and 2.01% (y.o.y) from USD2.41 billion surplus in November 2023. The trade balance surplus in November 2024 was the second largest of 2024, after March 2024 surplus, reaching USD 4.57 billion. Breaking down its component, both exports and imports indicated a decrease in November 2024; however, the sharper decline in imports contributed to a considerable increase in the trade surplus. The decline in both exports and imports was substantially contributed by the reducing global oil prices by the end of November 2024.

Exports slowed down by 1.70% (m.t.m) compared to the previous month, from USD24.42 billion in October 2024 to USD24.01 billion in November 2024. However, this figure conveyed a growth of 9.14% (y.o.y) from the same period in 2023 as its exports was valued at USD22.00 billion. Both oil and gas and non-oil and gas exports in November 2024 encountered a slight decline of 2.10% (m.t.m) and 1.67% (m.t.m), consecutively. The weakening of non-oil and gas exports was mainly affected by a 0.92% (m.t.m) decrease in manufacturing sector, as it contributed by 0.70 percentage points to the overall decrease. Furthermore, of the ten commodities with the highest non-oil and gas exports value in November 2024, several experienced a decline, with the largest decline seen in animal/vegetable fats and oils (HS15) by 10.48% (m.t.m) due to increasing cost of production as a consequence of rainy

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season, accompanied by decline in vehicles and its part (HS87, 8.38% (m.t.m) decrease) and footwear (HS64, 7.92% (m.t.m) decrease). Meanwhile, the commodity that experienced an increase was nickel and its derivatives, rising by 87.26% (m.t.m) compared to the previous month. Nickel has gained prominence due to its role in EV battery production, leading to a rise in both global demand and price.

As for imports, Indonesia experienced a 10.71% (m.t.m) decline, falling from USD21.94 billion in October 2024 to USD19.59 billion in November 2024. A similar trend to exports was observed in imports, as its annual basis has shown a slight increase of 0.01% (y.o.y). Moreover, a greater decline of imports was apparent in oil and gas commodities, amounting 29.88% (m.t.m), whereas the non-oil and gas commodities experienced a decline of 6.87% (m.t.m). The decline in oil and gas imports was attributed to a reduction in crude oil imports by 59.38% (m.t.m) and refined oil products by million 15.28% (m.t.m), as uncertainty in global economy has led to reduction in oil price. Meanwhile, machinery/electrical equipment and parts in non-oil and gas commodities experienced the largest decline of 15.49% (m.t.m) in November 2024 compared to the previous month. The weakening of Rupiah indicated a significant impact on imported goods, including the downward trend of machinery/electronic equipment demand.

Trump's Effect Started to Materialize

Capital markets across developing countries have been under selling pressure in the past two months amid worries over potential U.S. tariff hikes on regional exports next year under Donald Trump administration. The worries have been somewhat confirmed by Trump's statement inferring that his administration will impose tariffs of 25% on all imports from Canada and Mexico, and an extra 10% on Chinese goods on December 2nd. The announcement immediately boosted even further the ongoing strengthening of the US Dollar as investors shifted its portfolio towards USD-backed assets away from emerging markets', including Indonesia's stocks and bonds. As a consequence, Indonesia suffered a capital outflow of around USD0.75 billion since mid-November, which consists of USD0.35 billion outflow from government bond assets and USD0.40 billion foreign net selloffs in stock market (Figure 3). Foreign investors' withdrawal from government bonds was mostly on short-term government bonds, as indicated by the rise in its yield. 1-Year government bond's yield spiked up from 6.33% on November 19th to 6.74% on December 13th, while 10-Year government bond's yield 'only' increased from 6.93% to 7.05% during the same period (Figure 4). Despite mostly driven by concerns over upcoming US trade policy, the narrowing yield curve of Indonesia's government bond might also suggest that investors' worry over Indonesia's short-term economic prospects.

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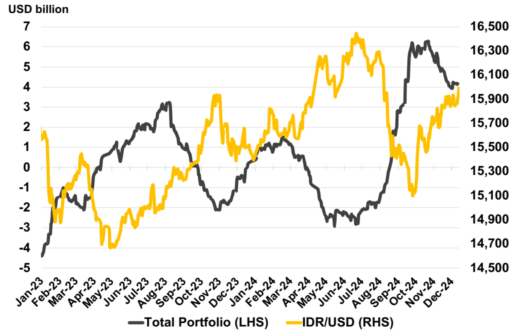
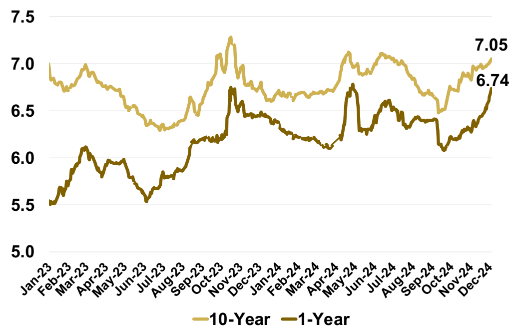
Figure 3: IDR/USD and Accumulated Portfolio Capital Inflow (since Jan-23)



Source: CEIC

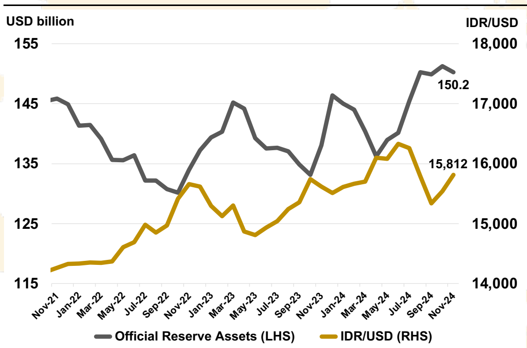
Figure 4: Government Bonds Yield (% p.a.)



Source: CEIC

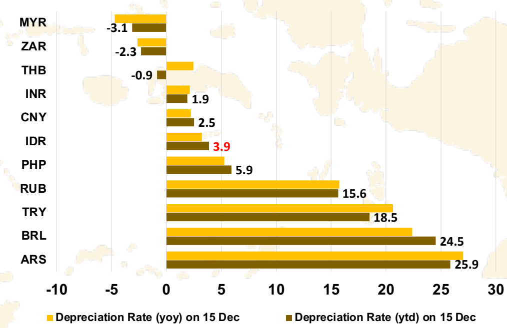
The recent episode of massive capital outflows from emerging markets has spurred depreciation trends among its currencies and led to rising US Dollar Index (DXY) from 103.42 in early November to 106.94 in mid-December. In the past 30 days, Rupiah depreciated 1.39% (m.t.m) from IDR15,770 per USD to IDR15,990 per USD. Considering its relative performance throughout 2024, Rupiah has a moderate performance compared to its peers. With a depreciation rate of 3.86% (y.t.d), Rupiah performed better than Philippine peso, Russian Ruble, Turkish Lira, Brazilian Real, and Argentine Peso which recorded a double-digit depreciation (except Philippines Peso). However, Rupiah depreciated deeper than Chinese Yuan, Indian Rupee, Thailand Baht, South African Rand, and Malaysian Ringgit. As the pressure on Rupiah has been mounting since October, Indonesia's official reserve assets decreased by around USD1 billion from USD151.2 billion in October to USD150.2 in November due to Bank Indonesia's intervention to stabilize Rupiah. Besides currency stabilization effort, the decline in official reserve assets was also influenced by the government's external debt payments. The current position of reserves assets is equivalent to 6.5 months of imports or 6.3 months of imports and servicing the government's external debt, which is well above the international reserve adequacy standard of around three months of imports.

Figure 5: IDR/USD and Official Reserve Assets



Source: CEIC

Figure 6: Depreciation Rates of Selected EMs (15 December 2024)



Source: Investing.com

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On external front, the US government's potential tariff and trade policies became the dominant factor of international capital flows in the past few weeks, pushing investors to shift away from emerging markets and weakening emerging markets' currencies. In addition, the market is currently assigning a 96% probability that the Fed will implement a quarter-point rate cut at the upcoming FOMC meeting. On the domestic side, inflation rate prolonged its downward trend for the last eight months and edged toward the lower end of BI's inflation target. Muted inflation rate is driven by a combination of structural issue of weak domestic aggregate demand, high-base effect, and seasonal factors. Given there is room for BI to cut its policy rate, current pressure on Rupiah is rather significant and any rate cut might worsen the depreciation pressure. Thus, we are of the view that BI should keep the BI rate unchanged at 6.00% in December's Board of Governor meeting.

8 DECENT WORK AND ECONOMIC GROWTH