November 22, 2017

MONETARY WATCH: Concerns grow ahead of the December FMOC Meeting

DRI Forecast for 2017

7D Reserve R. (%)	4.25
Inflation (%)	3.2 - 3.6
GDP Growth (%)	5.2 - 5.3

- As expected, at its monetary policy meeting from 15-16 November, BI left its benchmark 7-Day RR rate unchanged at 4.25 percent. Meanwhile, the deposit and lending facility rates were kept at 3.50 and 5.00 percent, respectively. The 7-Day RR rate was left unchanged for the second straight month, after it was cut by 25 bps in both August and September. In its statement, BI said that the decision was consistent with its efforts to maintain macroeconomic and financial system stability, whilst it also seeks to facilitate domestic economic recovery in addition to taking into consideration global and domestic economic dynamics.

- Against this backdrop, the interbank interest rate as proxied by the JIBOR O/N rate has been stable in the last three weeks, which averaged 3.91 percent. Meanwhile, the JIBOR O/N rate in the first three weeks of November was slightly more volatile than it was in the first three weeks of October (0.06 bps vs 0.03 bps, respectively).

- We expect concerns to grow ahead of the FMOC meeting in December in which the Fed is expected to hike the FFR (the probability of a rate hike is put at 92.3 percent). Given this, we don't expect BI to cut its benchmark rate in the December Governors' meeting.

DAMHURI NASUTION
Head of Economic Research
damhuri@danareksa.com

PRAMAYANTI MEITISARI
Analyst
pramayanti@danareksa.com

WAHYUNI K. HANDAYANI
Junior Analyst
wahyuni.handayani@danareksa.com

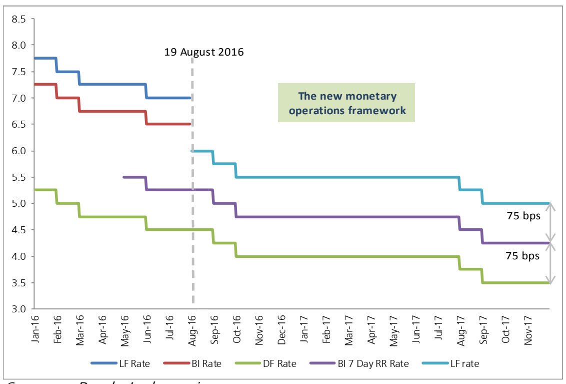
BI 7-Day RR Rate: Extending the Pause

- As expected, at its monetary policy meeting from 15-16 November, BI left its benchmark 7-Day RR rate unchanged at 4.25 percent. Meanwhile, the deposit and lending facility rates were kept at 3.50 and 5.00 percent, respectively. The 7-Day RR rate was left unchanged for the second straight month, after it was cut by 25 bps in both August and September. In its statement, BI said that the decision was consistent with its efforts to maintain macroeconomic and financial system stability, whilst it also seeks to facilitate domestic economic recovery in addition to taking into consideration global and domestic economic dynamics.

- In general, the global economy has continued to improve. US growth is increasingly solid, whilst the economies of China, Japan and Europe are also recovering. The Fed's balance-sheet reduction and the likelihood of a FFR hike in December will, nonetheless, have far-reaching ramifications and create challenges for BI to ease monetary policy further. Other considerations are the recent geopolitical conditions in several regions.

- Domestically, the latest GDP data for the third quarter reveals that the Indonesian economy grew by 5.06 percent (YoY), or more briskly than in the previous two quarters when growth reached 5.01 percent (YoY). The inflation rate in October was 0.01 percent (MoM) or 3.58 percent (YoY), lower than the October average in the past three years of 0.18 percent (MoM). On the currency front, the average rupiah rate was weaker in October (the rupiah depreciated on average by 1.63 percent to Rp13,528 per USD, reflecting the financial market's response to developments such as the change of the Fed governor, the Fed's monetary policy normalisation, growing expectations of a further FFR hike and plans for tax reform).

BI Reference Rate

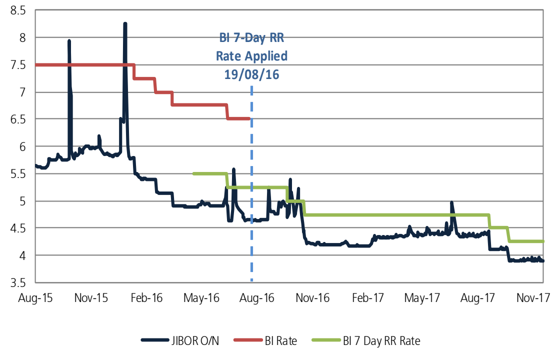


Source: Bank Indonesia

Interbank Interest Rate: Stable After the Benchmark Rate was Left Unchanged

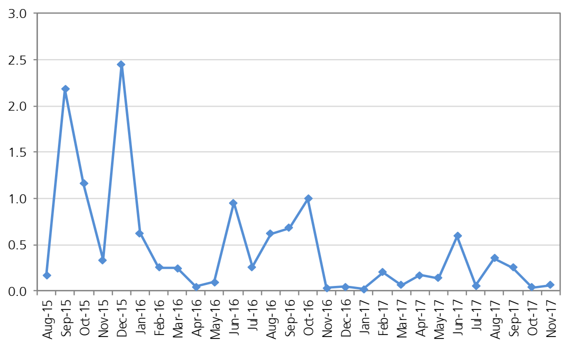
- The interbank interest rate as proxied by the JIBOR O/N rate has been stable in the last three weeks after the benchmark 7-Day RR rate was left unchanged. The average JIBOR O/N rate in the first three weeks of November was 3.91 percent, unchanged from its level in the first three weeks of October. Meanwhile, the JIBOR O/N rate in the first three weeks of November (0.06 bps) was slightly more volatile than it was in the first three weeks of October (0.03 bps). Nonetheless, it was still close to zero, meaning that volatility was very low. Looking ahead to December, the JIBOR O/N rate can be expected to increase slightly and also be more volatile due to the end-of-year festivities and the greater likelihood of a FFR hike.

JIBOR O/N Rate



Source: Bloomberg

JIBOR O/N Spread

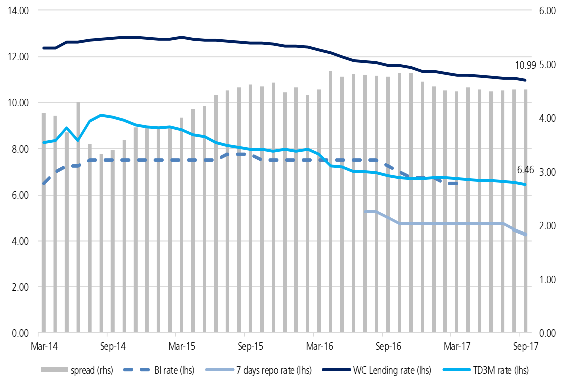


Source: Bloomberg, DRI

Deposit and Credit Rates: Benchmark Rate Cuts Have Started to be Transmitted

- After the benchmark rate was cut by 50 bps in total in August and September, and then followed by a LPS rate cut on 15th September, the deposit rate recorded a decline of 8 bps in September. As a result of the benchmark rate cuts, time deposit rates for all tenors (1 month to 24 month time deposits) were effectively pushed down. Similarly, lending rates also declined: they were down by 8 bps. By loan type, rates on working capital loans and investment loans declined to around 10 percent, while rates on more-risky consumer loans stood at around 13 percent. Looking at the credit quality, gross NPLs improved slightly to 2.93 percent in September from 3.05 percent in the previous month. In October, we expect further transmission of the benchmark rate cuts on deposit and credit rates.

The Interest Rate Spread of Banks



Source: Bank Indonesia

December BI Governors' Meeting: Will Take Place Prior to December's FMOC Meeting

- Inflation eased to 3.58 percent in October – less than our expectation of 3.67 percent (YoY). Also encouragingly, core inflation was recorded at its lowest rate for the past three years. We expect the full year inflation to be in the range of 3.2 – 3.6 percent – still in line with BI's target of 4±1 percent. In the third quarter, the economy grew by 5.06 percent – faster than the growth pace of 5.01 percent in the second quarter, yet below the consensus forecast of 5.13 percent. Nonetheless, the economy is expected to grow more briskly in the second half of the year due to better government budget realization, a wider trade surplus and stronger household consumption (our CCI has trended upward since June, increasing by 2.1 percent mom in October).

- However, heightened concerns over increasingly-likely Fed rate hikes, monetary policy normalization and US plans for tax reform have led to USD appreciation in October. Exchange rate volatility was also on the rise in October, marked by 1.6 percent rupiah depreciation (mom) against the USD. Moreover, international reserves also declined significantly by US$2,855 million from September to October on account of net foreign asset sales. We expect concerns to grow ahead of the FMOC meeting in December in which the Fed is expected to hike the FFR (the probability of a rate hike is put at 92.3 percent). Given this, we don't expect BI to cut its benchmark rate in the December Governors' meeting.

RESEARCH TEAM

Damhuri Nasution
Head of Economic Research
damhuri@danareksa.com

Kahlil Rowter
Chief Economist
kahlil.rowter@danareksa.com

Asti Suwarni
Analyst
asti@danareksa.com

Pramayanti Meitisari
Analyst
pramayanti@danareksa.com

Darwin Sitorus
Economist / Database Officer
darwin@danareksa.com

Handri Thiono
Junior Economist
handrit@danareksa.com

Natalia Daisyana
Research Assistant
natalia@danareksa.com

Martin Jenkins
Editor
martin@danareksa.com

Rika Pantjawati
Executive Secretary
rikap@danareksa.com

Wahyuni K. Handayani
Junior Analyst
wahyuni.handayani@danareksa.com