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Credit growth is limited, BI Rate needs accommodative fiscal support

Bank Indonesia (BI) decided to keep its benchmark interest rate unchanged at 5.50% (Cons: 5.50%, KBVS: 5.50%, Prev: 5.50%), reflecting a cautious stance amid heightened global uncertainty. Key concerns include rising geopolitical tensions, particularly the conflict between Iran and Israel, which has the potential to push global oil prices higher and prompt investors to shift portfolios toward safer assets. Meanwhile, the trade tensions between China and the U.S. have shown signs of easing following several bilateral meetings aimed at tariff negotiations. While this has helped ease inflationary pressures in the U.S., prices of certain imported goods remain elevated due to lingering tariff policies, indicating that the possibility of stagflation still exist and thus strengthening expectations on the direction of future Fed Funds Rate cuts.

The domestic macroeconomic backdrop continued to show signs of moderation and still within Bank Indonesia's target. Inflation remained well-contained at 1.60% YoY in May 2025—comfortably within BI's 2.5% ±1% target range. At the same time, GDP growth remained stable, supported by increased household spending during the long holidays for Vesak and Ascension Day. Looking ahead, economic activity is expected to strengthen in 2H25, driven by the social assistance disbursement and wage subsidy that will be held in June and July 2025. Overall, BI forecasts economic growth in FY25 to be in the range of 4.6-5.4%.

Within the banking sector, liquidity pressures persisted as the growth of third-party funds (DPK) further moderated to 4.29% YoY in May '25 (Prev: 4.55% YoY in April), heightening competition for funding. In response to this softening liquidity, Bank Indonesia encouraged banks to reduce their deposit rates following last month's policy rate cut. However, the adjustment has been minimal—average deposit rates only declined by 2.00 bps to 4.81% in May '25 (Prev: 4.83%).

Credit growth currently stands at 8.43% YoY (Prev: 8.88% YoY), and although Bank Indonesia maintains its projection of 8-11% YoY growth for FY25, the figure has been declining for seven consecutive months, indicating persistent weakness in lending activity despite supportive policy measures. However, similar to deposit rates, lending rates have been slow to adjust—bank lending rates declined only slightly by 1.00 bps to 9.18% (Prev: 9.19%). BI continues to urge banks to lower lending rates in order to improve credit transmission and stimulate broader access to financing. Despite these challenges, Indonesia's banking sector remains fundamentally strong, supported by a high Capital Adequacy Ratio (CAR) of 25.41% and a manageable Non-Performing Loan (NPL) ratio of 2.24%.

The slowdown in credit growth is closely linked to ongoing structural changes in Indonesia's economy. On the demand side, stagnation in labor-intensive sectors has limited job creation and wage growth, resulting in weaker consumer purchasing power. This has led to more cautious household spending, contributing to subdued domestic demand. **Under these circumstances, monetary policy easing, such as reducing the BI Rate, has had limited impact on boosting consumption and credit growth**. To strengthen demand, fiscal stimulus should be directed toward programs with high multiplier effects, such as social protection, and support for MSMEs, which can generate jobs, raise incomes, and stimulate broader economic activity.

On the supply side, producers are also under strain, as reflected in Indonesia's Manufacturing PMI, which remains in contraction territory. Possibly because of these conditions, improving the investment climate must be a key priority to address supply-side constraints. This includes clarifying regulations, simplifying business procedures, and removing hidden costs that discourage both foreign and domestic investors.

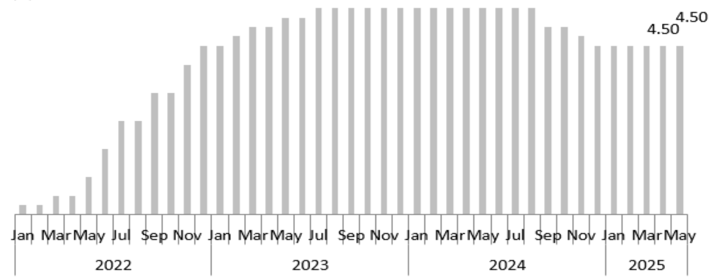
Bank Indonesia's forward policy remains focused on maintaining rupiah stability, enhancing liquidity, and supporting sustainable growth. Interventions in the spot, NDF, and DNDF markets, along with SBN purchases, will continue to stabilize the exchange rate—strengthened by rising foreign exchange supply from exporters following stricter the Natural Resource Export Proceed (DHE SDA) implementation and ongoing capital inflows. The rupiah is expected to remain stable, underpinned by BI's firm policy commitment, attractive yields on domestic financial instruments, and the maintenance of a favorable interest rate differential between the BI Rate and the Fed rate. To reinforce these goals, BI will optimize monetary operations through SRBI, SVBI, and SUVBI instruments, with rate adjustments to maintain market interest.

Table 1. Interest Rate Data

Indicators	18-Jun-25		Monthly Changes (in bps)	Ytd Changes (in bps)
	Latest	M-1		
Policy Rate (in %)				
United States	4.50	4.50	0.0	(100.0)
European Union	2.15	2.40	(25.0)	(235.0)
United Kingdom	4.25	4.50	(25.0)	(100.0)
Japan	0.50	0.50	0.0	60.0
China	3.00	3.10	(10.0)	(45.0)
India	5.50	6.00	(50.0)	(100.0)
Thailand	1.75	1.75	0.0	(75.0)
Philippines	5.50	5.50	0.0	(100.0)
Indonesia	5.50	5.50	0.0	(50.0)
Global Monetary Policy Change (in number of countries)				
Easing	1	3		
Unchanged	22	19		
Tightening	13	10		
Average International Interest Rate (in %)				
USD LIBOR -1 Month	4.96	4.96	0.0	(45.0)
USD LIBOR -3 Months	4.85	4.85	0.0	(75.6)
USD LIBOR -6 Months	4.68	4.68	0.0	(117.8)
Domestic Interbank Money Market (in %)				
INDONIA	5.83	5.71	11.7	(16.8)
JIBOR - 1 Month	6.31	6.01	29.9	(7.6)
JIBOR - 3 Months	6.61	6.38	23.1	(13.7)
JIBOR - 6 Months	6.71	6.69	2.7	(15.6)
JIBOR - 12 Months	6.91	6.97	(6.7)	(14.4)

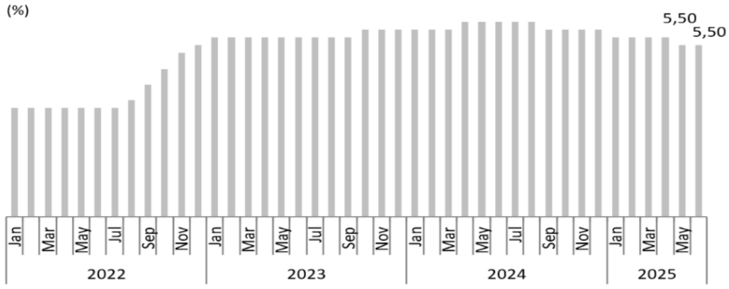
Sources: Each Central Bank and GlobalRates – treated (2025)

Fig 1. Fed Rate



Source: The Fed – treated (2025)

Fig 2. BI Rate

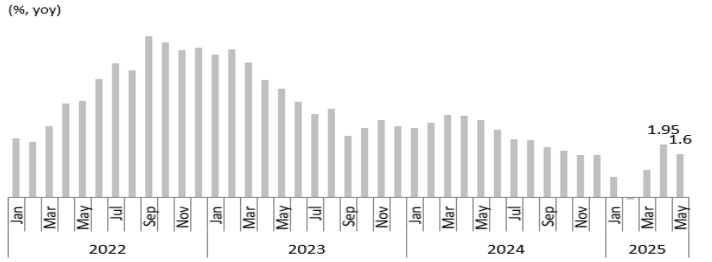


Source: Bank Indonesia – treated (2025)

Fig 3. US CPI Inflation

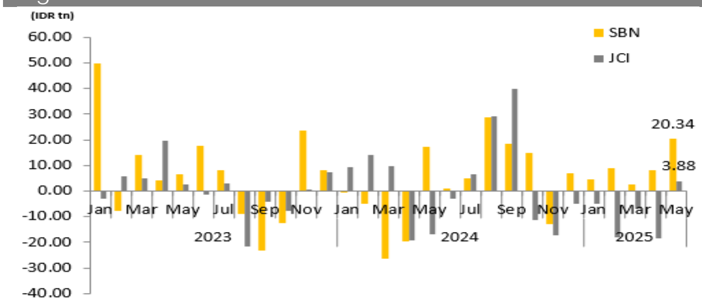
Source: US BLS– treated (2025)

Fig 4. Indonesia CPI Inflation



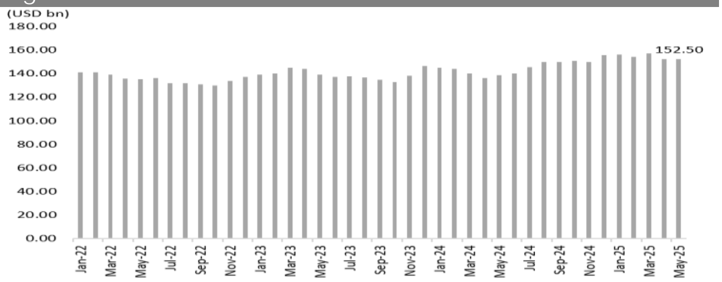
Source: BPS – treated (2025)

Fig 5. Indonesia Portofolio Flow



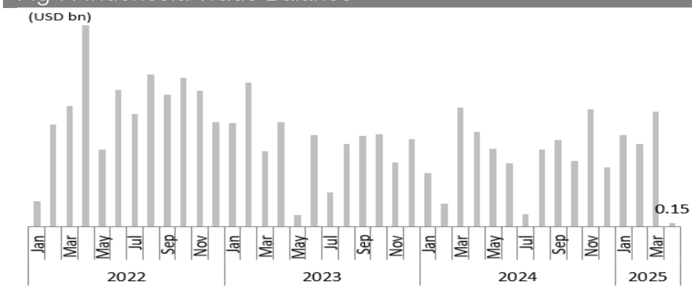
Source: Bloomberg – treated (2025)

Fig 6. Indonesia FX Reserves



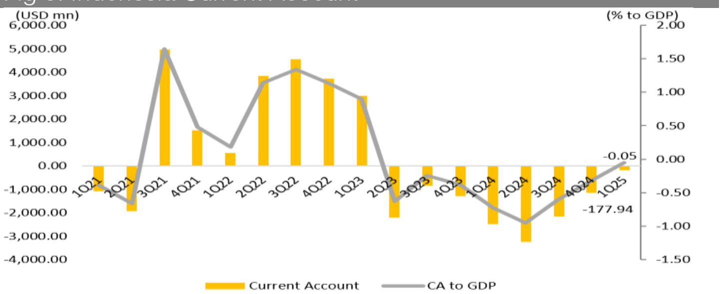
Source: BI – treated (2025)

Fig 7. Indonesia Trade Balance



Source: BI – treated (2025)

Fig 8. Indonesia Current Account



Source: BI – treated (2025)

Table 2. Fed Rate Probabilities, as of 18 Jun '25

MEETING DATE	MEETING PROBABILITIES				
	325-350	350-375	375-400	400-425	425-450
18-Jun-25	0.0%	0.0%	0.0%	0.1%	99.9%
30-Jul-25	0.0%	0.0%	0.0%	14.5%	85.5%
17-Sep-25	0.0%	0.0%	8.3%	54.9%	36.8%
29-Oct-25	0.0%	3.9%	30.2%	46.4%	19.5%
10-Dec-25	2.4%	20.2%	40.2%	29.8%	7.4%

Source: CME Group – treated (2025)

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