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BI's Policy Set Overcomes Trilema Monetary Theory

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In line with our expectations, the Bi7DRRR rate was maintained at 5.75% (Cons: 5.75%, KBVS: 5.75%, Prev: 5.75%). This interest rate condition also implies to maintaining the Deposit Facility rate at 5.00% and the Lending Facility rate at 6.50%. We believe this policy is aligned with BI's confidence in maintaining the inflation rate within the range of 3.0% (±1%) YoY until the end of 2023 and softer further to 2.5% (±1%) YoY in 2024. Nevertheless, we also observe that BI starts facing pressures from the domestic real sector, evident in slower loan growth in Jun '23, which only grew 7.76% (YoY), accompanied by potential wait-and-see behavior from domestic businesses regarding investment. Additionally, the possibility of declining external demand, as indicated by lower economic growth and contractionary Manufacturing PMIs in major economies, is a concern that may exert pressure on domestic economic growth.

We anticipate that these conditions will compel BI to maintain the three policies, known as the monetary policy trilemma, which involves simultaneous inflation management control (through TPIN-TPID policy coordination), stabilizing the Rupiah (via triple intervention and twist operations), and promoting domestic economic growth (through macroprudential policy stimulus). This situation contradicts conventional monetary policy theories, which typically allow monetary authorities to pursue only 2 out of 3 policy targets. We hope that these measures can be executed effectively, in line with the upcoming implementation of the DHE (Devisa Hasil Ekspor/ Foreign Exchange Export Proceeds) on 01 Ags '23, and the implementation of increased total incentives for RIM (Rasio Intermediasi Makroprudensial/Macroprudential Intermediation Ratio) up to a maximum of 4.0% (Prev: 2.8%), targeted towards downstreaming, inclusive financing, and green economy sectors, to be effective from 01 Oct '23.

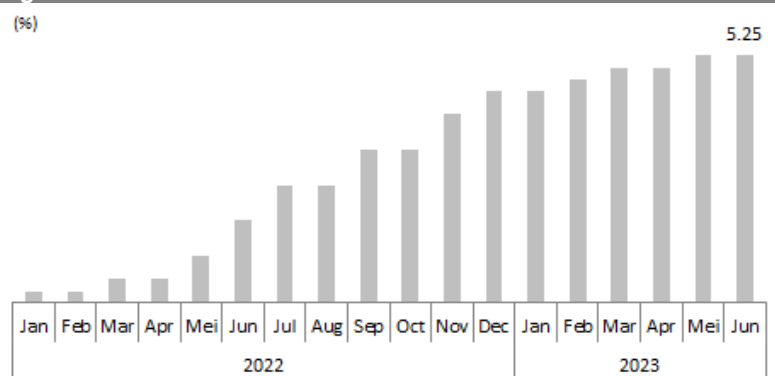
However, we also recognize that BI faces several challenges in the near future. These challenges include: a) the possibility of increasing Rupiah volatility due to the narrowing interest rate differential between Bi7DRRR and the Fed Rate, which may lead to a decline in SUN-UST yield spread; b) rising risks of domestic inflation due to the El Nino session; and imported inflation due to higher global energy and food prices; and c) the continuation of a wait-and-see approach from the business sector, influenced by the ongoing dynamic political conditions domestically. Nevertheless, if these three challenges can be managed, we anticipate that BI will be able to maintain the Bi7DRRR terminal rate at its current level (5.75%) and potentially lower it by the end of 2023.

Table 1. Interest Rate Data

Indicators	25-July-23		Monthly Changes (in bps)	Ytd Changes (in bps)
	Latest	M-1		
Policy Rate (in %)				
United States	5.25	5.25	0.0	75.0
European Union	4.00	4.00	0.0	150.0
United Kingdom	5.00	4.50	50.0	100.0
Japan	-0.10	-0.10	0.0	0.0
China	3.55	3.55	0.0	(10.0)
India	6.50	6.50	0.0	25.0
Thailand	2.00	2.00	0.0	75.0
Philippines	6.25	6.25	0.0	75.0
Indonesia	5.75	5.75	0.0	25.0
Global Monetary Policy Change (in number of countries)				
Easing	11	12		
Unchanged	55	47		
Tightening	26	37		
Average International Interest Rate (in %)				
USD LIBOR -				
Overnight	5.06	5.08	(1.4)	75.6
USD LIBOR - 1 Month	5.41	5.15	25.8	75.3
USD LIBOR - 3 Months	5.61	5.52	9.3	73.8
USD LIBOR - 6 Months	5.86	5.67	18.3	53.8
USD LIBOR - 12 Months	6.04	5.90	14.4	45.1
Domestic Interbank Money Market (in %)				
INDONIA	6.00	5.18	81.2	15.8
JIBOR - 1 Month	6.39	6.39	(0.0)	59.9
JIBOR - 3 Months	6.75	6.75	(0.2)	55.4
JIBOR - 6 Months	6.87	6.87	(0.1)	16.0
JIBOR - 12 Months	7.05	7.06	(0.4)	13.8

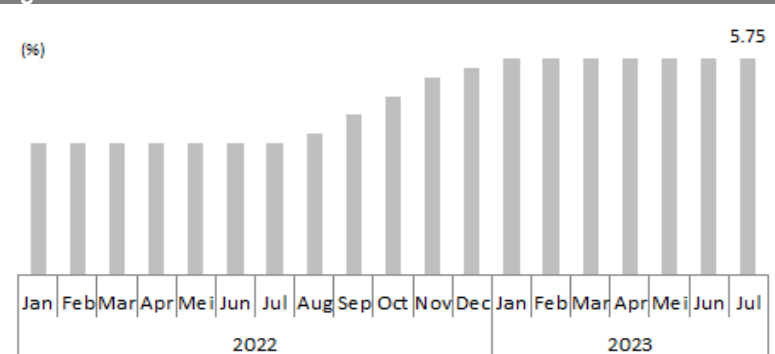
Sources : Each Central Bank and GlobalRates – treated (2023)

Fig 1. Fed Rate



Source: The Fed – treated (2023)

Fig 2. Bi7DRRR

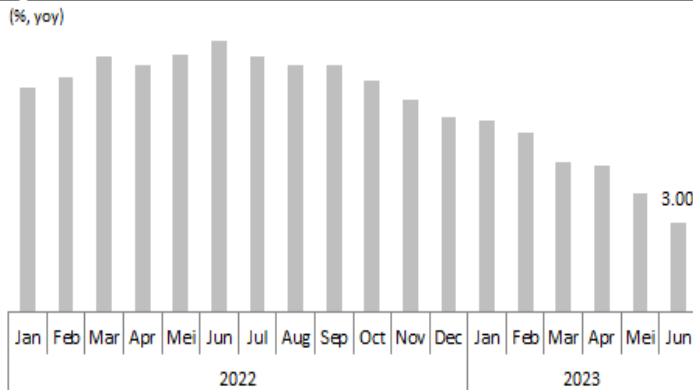


Source: Bank Indonesia – treated (2023)

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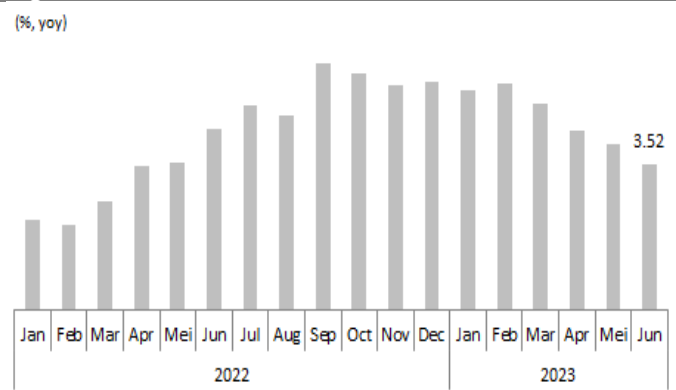
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Fig 3. US CPI Inflation



Source : BLS – treated (2023)

Fig 4. Indonesia CPI Inflation



Source : BPS – treated (2023)

Table 2. Fed Rate Probabilities, as of 18 April 2023

MEETING DATE	Target Rate (in bps)									
	350-375	375-400	400-425	425-450	450-475	475-500	500-525	525-550	550-575	575-600
26-Jul-23	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	98.9%	1.1%	0.0%
20-Sep-23	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	81.1%	18.7%	0.2%
1-Nov-23	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	67.6%	29.1%	3.3%
13-Dec-23	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	5.1%	64.7%	27.1%	3.0%
31-Jan-24	0.0%	0.0%	0.0%	0.0%	0.0%	1.7%	24.8%	52.3%	19.2%	2.0%
20-Mar-24	0.0%	0.0%	0.0%	0.0%	0.9%	13.5%	38.8%	35.4%	10.4%	1.0%
1-May-24	0.0%	0.0%	0.0%	0.8%	11.9%	35.7%	35.8%	13.5%	2.2%	0.1%
19-Jun-24	0.0%	0.0%	0.3%	5.9%	22.9%	35.7%	25.6%	8.3%	1.2%	0.1%
31-Jul-24	0.0%	0.3%	4.5%	18.5%	32.4%	28.2%	12.7%	3.0%	0.4%	0.0%
25-Sep-24	0.2%	3.7%	15.8%	29.8%	29.0%	15.7%	4.9%	0.9%	0.1%	0.0%

Source : CME Group – treated (2023)

Table 3. Meeting Calendar The Fed (FOMC) and Bank Indonesia (RDG-BI) in 2023

No	Month	FOMC Meeting	RDG-BI
1	January		18 – 19 Jan
2	February	31 Jan – 1 Feb	15 – 16 Feb
3	March	21 – 22 Mar	15 – 16 Mar
4	April		18 – 19 Apr
5	May	2 – 3 May	24 – 25 May
6	June	13 – 14 Jun	21 – 22 Jun
7	July	25 – 26 Jul	24 – 25 Jul
8	August		23 – 24 Aug
9	September	19 – 20 Sep	20 – 21 Sep
10	October		18 – 19 Oct
11	November	31 Oct – 1 Nov	22 – 23 Nov
12	December	12 – 13 Dec	20 – 21 Dec

Sources : The Fed and Bank Indonesia – treated (2023)

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