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Macroeconomic Analysis Series

# BI Board of Governor Meeting

## November 2023

### Highlights

- BI should keep the policy rate unchanged at 6.00% this month.
- Still within the target range, inflation soars mildly to 2.56% (y.o.y) due to rice production disruption.
- Trade surplus widened in October 2023 while Rupiah indicated an appreciation following BI's decision to raise the BI rate last month and The Fed's decision to hold the interest rate steady.


**Macroeconomics, Finance & Political Economy Research Group**

**Jahen F. Rezki, Ph.D.**
jahen@lpem-feui.org

**Syahda Sabrina**
syahda.sabrina@lpem-feui.org

**Teuku Riefky**
teuku.riefky@lpem-feui.org

**Amalia Cesarina**
amalia.cesarina@lpem-feui.org

**Faradina Alifia Maizar**
faradina@lpem-feui.org

**Yoshua Caesar Justinus**
yoshua@lpem-feui.org


Disruption in rice production due to El Nino phenomenon causes mild inflationary pressure in October 2023 with headline inflation recorded within the target range at 2.56% (y.o.y). Trade balance posted an increasing surplus of USD3.48 billion in October supported by less severe decline in both exports and imports compared to the previous month. On top of that, Rupiah edged higher against the greenback after BI decided to increase its interest rate during October 2023 meeting coupled with the Fed's decision to leave its policy rate unchanged. The Fed is likely to maintain the current level of its policy rate in FOMC meeting in December 2023. While pressure on Rupiah from global market uncertainty remains, these four combined suggested that BI should maintain the interest rate unchanged at 6.00% this month.

### Rice Price Soars due To El Nino Causing Inflation to Rise

Still within the central bank's target range and in line with market's expectation, headline inflation was recorded at 2.56% (y.o.y) in October 2023, a modest rise from September 2023 figure at 2.28% (y.o.y). Headline inflation has been within the target range for seventh straight months or since May 2023 when inflation hit the upper bound of the target range. Similar to previous month, the main contributor to October's inflation was higher food prices as indicated by an annual inflation of 5.41% (y.o.y) in food, beverage, and tobacco expenditure group contributing 1.39% to October's inflation. On a monthly basis, headline inflation slowed to 0.17% (m.t.m) in October 2023 from 0.19% (m.t.m) a month earlier caused by increase in rice prices and non-subsidized fuel prices. At the beginning of October 2023, Pertamina raised its non-subsidized fuel prices, including Pertamax, Pertamax Green, Pertamax Turbo, Dexlite, and Pertamina Dex. However, the impact of fuel prices increases was moderate as Pertamina only raised non-subsidized fuel prices, which are not used by the majority of consumers, and the price increase was relatively mild averaging 5.55%. This was in contrast compared to September last year when the GoI increased not only Pertamax price but also Pertalite and Solar, subsidized fuel, with an average price increase of 26.25%.

Breaking down its component, administered prices recorded an inflation of 2.12% (y.o.y) in October 2023, edging up from 1.99% (y.o.y) in September 2023. On a monthly basis, administered prices increased by 0.46% (m.t.m) in October 2023, doubled the September 2023 figure of 0.23% (m.t.m). Apart from higher fuel prices, increase in airfares due to rise in aviation fuel also led to higher administered prices inflation. Volatile food prices indicated an increase of 5.54% (y.o.y) in October 2023 and has been on an increasing trend since August 2023, which was mainly driven by

## Key Figures

BI Repo Rate (7-day, October '23)
**6.00%**
GDP Growth (y.o.y, Q4 '23)
**4.94%**
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**2.56%**
Core Inflation (y.o.y, October '23)
**1.91%**
Inflation (m.t.m, September '23)
**0.17%**
Core Inflation (m.t.m, October '23)
**0.08%**
FX Reserve (October '23)
**USD133.1 billion**

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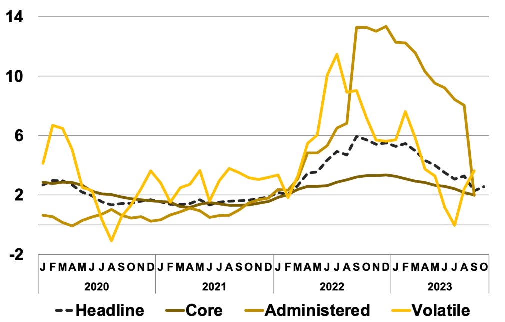
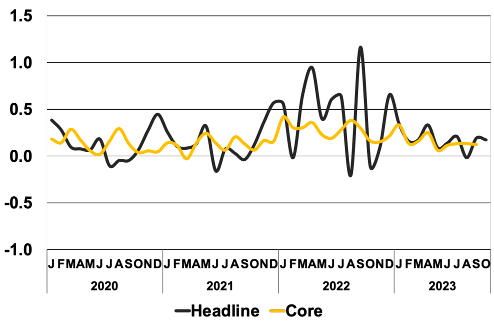
rising rice price. Increase in rice price was resulted from El Nino phenomenon, which caused disruption in both domestic and global rice production. Considering rice consumption hardly fall when price increases as it is an inelastic commodity, the GoI through State Logistics Agency (Bulog) will import an additional of 1.5 million tonnes of rice on top of previously agreed two million tonnes of rice, which totalled to 3.5 million tonnes of rice imports in 2023. The additional 1.5 million tonnes of rice should arrive by mid-January 2024. On a monthly basis, volatile food prices experienced a lower inflation of 0.21% (m.t.m) in October 2023 from 0.37% (m.t.m) in September 2023. Although rice price increased, it was offset by lower price of purebred chicken eggs and cooking oil on the back of adequate supply.

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




Source: CEIC

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




Source: CEIC

Core inflation remained low at 1.91% (y.o.y) in October 2023, resuming its decreasing trend since January 2023. On a month-to-month basis, core inflation was reported at 0.08% (m.t.m) in October 2023, down from 0.12% (m.t.m) in September 2023. The main contributors to lower core inflation were gold jewellery and house rentals. For the remaining of 2023, inflation is expected to remain low in November 2023 considering decrease in prices of nonsubsidized fuel at the beginning of the month and will increase in December 2023 due to seasonal effect of Christmas and New Year holiday. Overall, inflation in 2023 is predicted to be below 3%, within BI's target range.

### Economic Growth Falls Short of Expectation

Below the previous quarter's growth of 5.17% (y.o.y), Indonesian economy grew by 4.94% (y.o.y) in July – September quarter of 2023, falling short of 5% for the first time since the last quarter of 2021. The latest level of growth is in line with the long-standing pattern of lower economic growth in the quarter after Ramadan season, except during the Covid-19 pandemic. In addition, growth in Q3-2023 was affected by the high-base effect as the growth rate was reported at 5.73% (y.o.y) in Q3-2022 due to the low base in Q3-2021. By expenditure, slowing growth is attributable to softer household consumption and shrinking exports. Household consumption

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posted a growth of 5.06% (y.o.y) in Q3-2023, lower than 5.22% (y.o.y) in Q2-2023. Slower household consumption can be explained by seasonal effect of religious holidays in Q2-2023, such as Eid Al-Fitr and Eid Al-Adha, and school holiday, which did not happen in Q3-2023. Released alongside with the economic growth data, the Consumer Confidence Index (CCI) demonstrated a lift to 124.3 in October 2023 after dipping to 121.7 in the previous month. On the other hand, Purchasing Managers Index (PMI) fell to 51.5 in October 2023 from 52.3 in September 2023, marking the 26th straight month of being in the expansionary territory but the lowest level since June 2023. Lower new order growth and a decline in export sales contributed to a lower PMI.

In the middle of falling commodity prices, Indonesia booked another positive trade balance of USD3.48 billion in October 2023, marking a record 42nd consecutive month of trade surplus. This figure was a slight increase of 2.08% (m.t.m) from USD3.41 billion in September 2023. Trade surplus can be attributed increase in exports, which edged up by 6.76% (m.t.m) to USD22.15 billion, while imports increased to USD18.67 billion or 7.68% (m.t.m). Increase in exports was driven by non-oil and gas exports increase to USD1.44 billion (7.42% (m.t.m) with the highest increase was evident in precious metals and jewellery/ gems that increase by 43.10% (m.t.m) to USD691.3 million. Imports of non-oil and gas also increased by 10.37% (m.t.m), driving the overall monthly increase in imports. The highest increase was apparent also in in precious metals and jewellery/ gems, which expanded by 47.12% (m.t.m) to USD299.5 million. Increase of both exports and imports of precious metals and jewellery/ gems suggested that the precious metals industry in Indonesia has become more competitive in the global level over the past months.

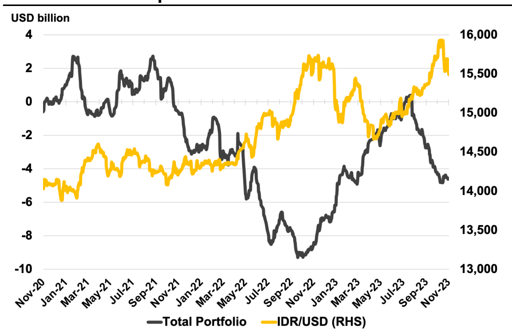
On a yearly basis, exports fell by 10.43% (y.o.y) in October 2023, an improvement from 16.17% (y.o.y) drop observed in September 2023. This was driven by global price fluctuations especially in primary commodities of Indonesia, such as coal, nickel, and palm oil. Imports also fell, though to a lesser extent, by 2.42% (y.o.y) in October 2023 compared to a double-digit drop of 12.45% (y.o.y) in September 2023. Although raw material imports decreased by 6.08% (y.o.y) in October 2023, total decline in imports was offset by increases in capital and consumer goods purchases made abroad, which increased by 11.08% (y.o.y) and 3.83% (y.o.y), respectively.

### Moderating Pressure on Rupiah

Although the US inflation still stands well above the target of 2%, the Fed held rates steady at 5.25% – 5.50% during its November's meeting against a backdrop of growing economy and resilient labor market indicated by steady job and growing wage. This was the second consecutive meeting that the FOMC decided to hold the interest rate, which have remained in that range since an increase in July 2023. To date, the Fed has raised interest rates almost a dozen time since early 2022 to battle spiking inflation, which peaked at above 9% in June 2022. The US inflation rate eased to 3.24% (y.o.y) in October, down from 3.70% (y.o.y) in September 2023. Lower US annual inflation in October 2023 was due to drop in price of petrol that offset increase in housing costs. After the Fed announced its decision on 1 November, the yield on the 2-year US Treasury and the 10-year US Treasury went down by 12bps to 4.95% and 11bps to 4.77%, respectively. Since mid-October, both yield on the 2-year and 10-year Treasury have fallen precipitously, partly due to safe-haven purchases driven by concerns over intensifying Israel's aggression against Palestine.

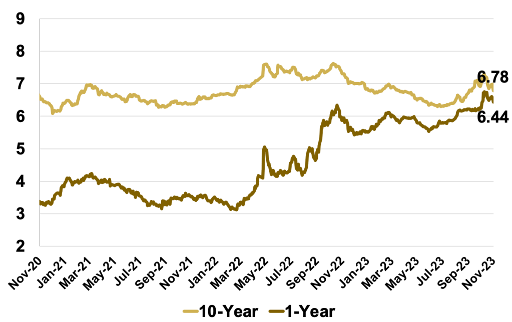
Driven by the Fed's hawkish stance, coupled with global economic slowdown and uncertainty from Israeli aggression and Russia-Ukraine ongoing war, investors move their assets from emerging market, including Indonesia, resulting in capital outflows from bonds and stock market of USD300 million between mid-October 2023 and mid-November 2023. This was translated into increasing yield of 1-year Indonesian government bond from 6.27% mid-October 2023 to 6.44% mid-November 2023. In contrast, yield of 10-year Indonesian government bond fell from 6.94% in mid-October 2023 to 6.78% in mid-November 2023, suggesting a shift in investors' preference towards longer-term assets.

Figure 3: IDR/USD and Accumulated Portfolio Capital Inflow (Last 36 Months)




Source: CEIC

Figure 4: Government Bonds Yield (% pa)




Source: CEIC

During October's meeting, Bank Indonesia surprisingly decided to hike its benchmark rate by 25bps to 6.00% due to rapid weakening of Rupiah that almost reached IDR16,000 per USD in October 2023, the weakest level since April 2020. Rupiah was under pressure as risk-averse investors prefer safe-haven assets during market turbulence due to global monetary tightening and Palestine-Israel war. Bank Indonesia's decision combined with the Fed's decision resulted in Rupiah appreciation by 1.15% to IDR15,530 per USD as of 15 November 2023 compared with the level recorded on 16 October 2023. The currently appreciating Rupiah was also partly contributed by the new policy instrument tool introduced in August 2023 by BI, Bank Indonesia Rupiah Securities (*Sekuritas Rupiah Bank Indonesia* (SRBI)), which is used to strengthen money market deepening efforts, attract portfolio

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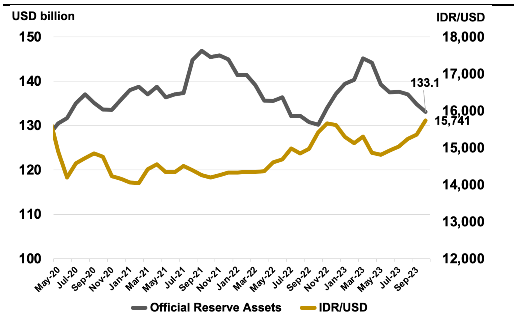
or go to [http://bit.ly/LPEMCommentarySubscription](http://bit.ly/LPEMCommentarySubscription) inflows, and optimise the SBN assets held by Bank Indonesia as underlying. During the second week of November 2023, non-residents booked a net inflows of IDR1.17 trillion into SRBI on top of IDR1.73 trillion net inflows into government bond (SBN) market, compensating IDR1.34 trillion outflows from the stock market.

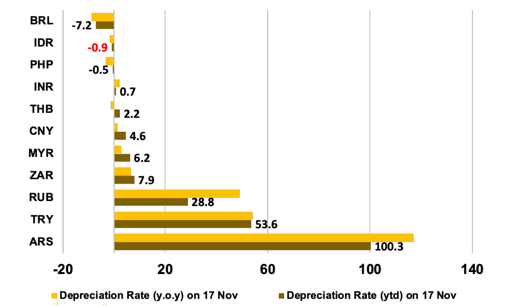
Despite being pressured by rally in the US dollar, Rupiah appreciated by 0.9% (ytd), performing better than most emerging economies currencies and only performing worse than Brazilian Real that experienced a year-to-date appreciation 7.2%. Other currencies, such as Thailand Baht, Malaysian Ringgit, and Türkiye Lira indicated a year-to-date depreciation, ranging from 0.7% (Indian Rupee) to 100.3% (Argentine Peso). To keep Rupiah stable and to facilitate government's foreign debt payments, Indonesia foreign exchange reserved declined by UDR1.8 billion from UDR134.9 billion at the end of September 2023 to USD133.1 billion at the end of October 2023. Although decreasing, the current position of foreign exchange reserve is equivalent to finance 6.1 months of imports or 5.9 months of imports and servicing government's external debt, well above the international adequacy standards of three months imports.

Figure 5: IDR/USD and Official Reserve Assets




Source: CEIC

Figure 6: Depreciation Rates of Selected EMs (17 November 2023)




Source: Investing.com

The unexpected rate hike by Bank Indonesia last month appeared to be working to relieve renewed pressure on Rupiah. Although capital outflows are still expected caused by heightened uncertainty in the global market, slowing global demand, and the Fed's 'higher-for-longer' stance, the currency is now relatively manageable and indicating an appreciating pattern over the last month. Additionally, The Fed is expected to keep its benchmark rate unchanged, providing room for BI to leave the interest rate unchanged. Therefore, BI should hold its policy rate at the current level of 6.00% during its November meeting. The below 3% level of inflation and trade balance surplus also serve as justification for BI to maintain the interest rate at the current level. The sub-5% growth also gives BI another supporting factor for holding the current level of interest rate.

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