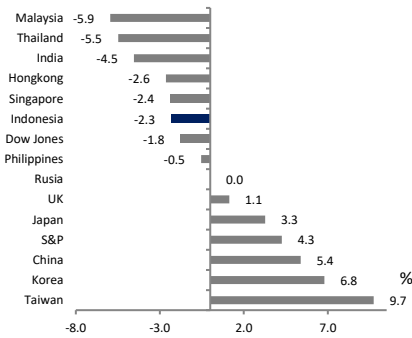


Friday, 24 March 2023

# Strategy

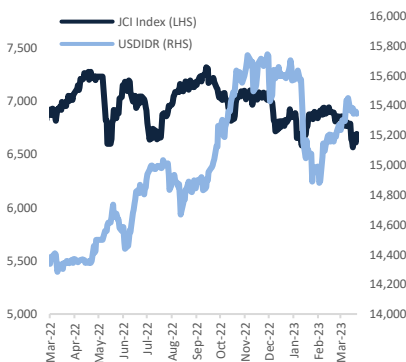
## Almost Done

### YTD share performance (%)



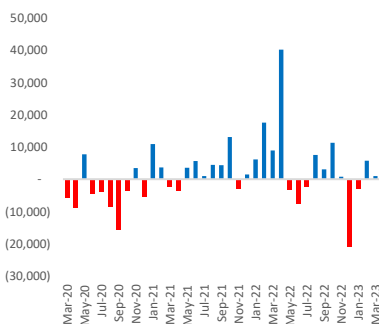
Source: Bloomberg

### JCI vs USD



Source: Bloomberg

### Net foreign flow (IDRbn)



Source: Bloomberg



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The Fed raised interest rate by 25 basis points, and while this move was widely anticipated, it also signals the Fed's confidence in the US banking system despite the escalation of the banking liquidity crisis. The March 23 dot plot shows an unchanged terminal rate of 5.1% this year, indicating that there will be no rate cuts in 2023. The Fed also reduced its growth forecast while raising its PCE inflation forecast. On the back of tighter credit conditions, they anticipate some additional policy firming might be appropriate, a progression from "ongoing rate increases" narrative previously; a signal that could indicate that a pause is on the way, which is a key positive for IDR on weaker DXY outlook.

**Still on course.** The Federal Open Market Committee (FOMC) raised the Fed Funds Rate by 25 basis points to further anchor inflation expectations. While this move was widely anticipated, it also signals the Fed's confidence in the US banking system despite the escalation of the banking liquidity crisis. Recently, the Fed has been leaning toward a hawkish stance, owing to stronger-than-expected economic data, implying that the ultimate level of interest rates is likely to be higher than previously anticipated, a condition which did not transpire in the March 23 dot plot readings.

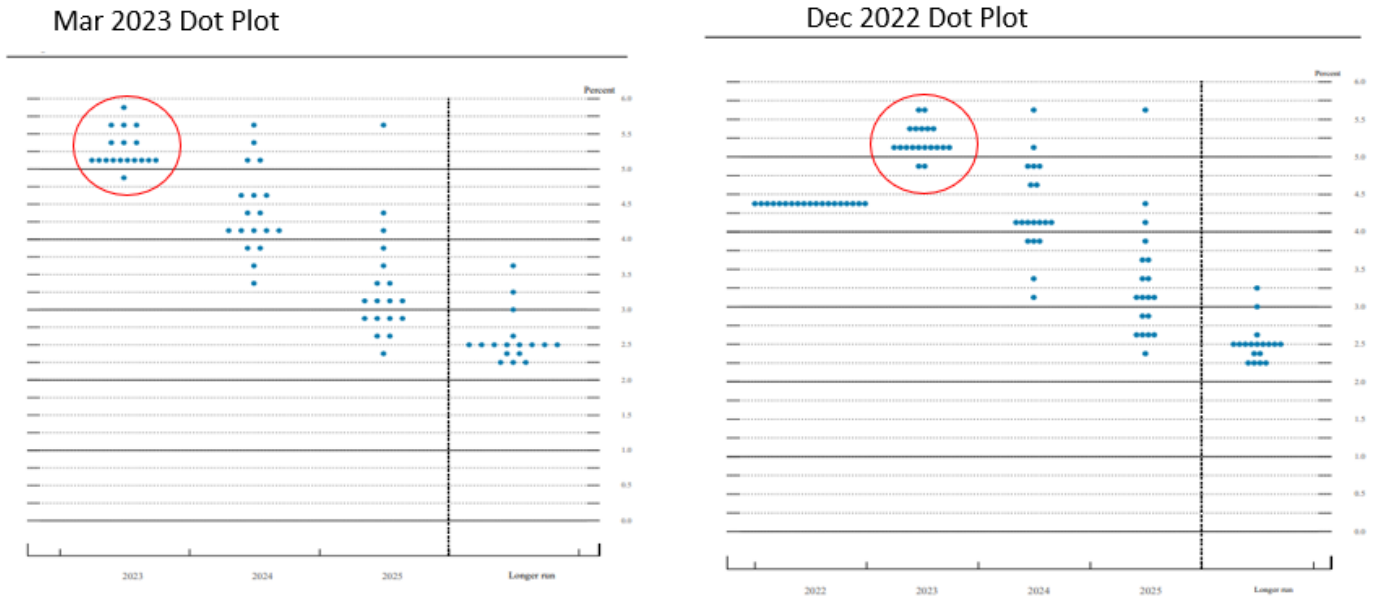
**No Rate Cuts this year.** According to the March 23 dot plot, benchmark interest rates are expected to peak at 5.1% this year, unchanged from the Fed's previous December projection, which still suggests no rate cuts this year, unlike the market's current expectation of a pivot in 2H23. We still note wide dot plot dispersion in 2024, with the median Fed Funds Rate target standing at 4.3%, higher than 4.1% in Dec 22, potentially indicating 75 bps of rate cuts next year. In 2025, the median Fed Funds target rate is 3.1%, unchanged from Dec 22, an indication of 125 bps of rate cuts in 2025.

**Lower growth expectations.** In terms of economic growth projections, the committee reduced its 2023 GDP growth estimate to 0.4%, down from 0.5% forecast in December, or standing in contrast to the recent increase in the Atlanta Fed GDPNow estimate for 1Q23 of 3.2% from 2.0% earlier this month. Growth will improve starting in 2024, with GDP growth expected to rise to 1.2%, albeit lower than Dec 22's 1.6% forecast. Furthermore, there is also a slight upward alteration in the PCE Inflation forecast, with inflation now expected to stand at 3.3% at end-2023, higher than the 3.1% forecast in Dec 22 and 2.8% in Sep 22. On the flip side, the Fed cut its unemployment projection to 4.5% in 2023 (from 4.6% previously) before it gradually rises to 4.6% in 2024-25.

**Signal for a pause?** The Fed also sees that it is too soon to determine the extent of banking crisis effects as well as the appropriate monetary policy response. As a result, they anticipate some additional policy firming might be appropriate, a progression from "ongoing rate increases" narrative previously; a signal that could indicate that a pause is on the way. Regarding the recent balance sheet expansion, the Fed acknowledges that it was a temporary lending measure to banks to meet special liquidity demands created by recent tensions, rather than a measure intended to directly alter its monetary policy stance. The Fed also believes that such a policy is helping to boost trust in the banking system.

**Domestic macro resilience will prevail in Indonesia.** While the Fed made no change to its QT program, the newly-launched BTFP (Bank Term Funding Program) may increase overall financial system liquidity, as evidenced in the recent increase in the Fed's total assets. It appears that the Fed has prioritized financial system stabilization over monetary policy operations. We continue to believe that QE will essentially reduce the effectiveness of rate hikes and result in greater uncertainty on inflation normalization, as well as economic growth and a tight labor market. With Indonesia's manageable inflation combined with a firm growth trajectory and greater IDR stability, further inflows should be enticed into the market, a key catalyst for a market re-rating.

**Exhibit 1. Dot Plot Trends – Terminal Rate Unchanged at 5.1%, no rate cut this year**



Source: FOMC March 2023 Summary of Economic Projections

**Exhibit 2. Economic projections in Mar 2023**

Variable	Median <sup>1</sup>				Central Tendency <sup>2</sup>				Range <sup>3</sup>			
	2023	2024	2025	Longer run	2023	2024	2025	Longer run	2023	2024	2025	Longer run
Change in real GDP	0.4	1.2	1.9	1.8	0.0-0.8	1.0-1.5	1.7-2.1	1.7-2.0	-0.2-1.3	0.3-2.0	1.5-2.2	1.6-2.5
December projection	0.5	1.6	1.8	1.8	0.4-1.0	1.3-2.0	1.6-2.0	1.7-2.0	-0.5-1.0	0.5-2.4	1.4-2.3	1.6-2.5
Unemployment rate	4.5	4.6	4.6	4.0	4.0-4.7	4.3-4.9	4.3-4.8	3.8-4.3	3.9-4.8	4.0-5.2	3.8-4.9	3.5-4.7
December projection	4.6	4.6	4.5	4.0	4.4-4.7	4.3-4.8	4.0-4.7	3.8-4.3	4.0-5.3	4.0-5.0	3.8-4.8	3.5-4.8
PCE inflation	3.3	2.5	2.1	2.0	3.0-3.8	2.2-2.8	2.0-2.2	2.0	2.8-4.1	2.0-3.5	2.0-3.0	2.0
December projection	3.1	2.5	2.1	2.0	2.9-3.5	2.3-2.7	2.0-2.2	2.0	2.6-4.1	2.2-3.5	2.0-3.0	2.0
Core PCE inflation <sup>4</sup>	3.6	2.6	2.1		3.5-3.9	2.3-2.8	2.0-2.2		3.5-4.1	2.1-3.1	2.0-3.0	
December projection	3.5	2.5	2.1		3.2-3.7	2.3-2.7	2.0-2.2		3.0-3.8	2.2-3.0	2.0-3.0	
Memo: Projected appropriate policy path												
Federal funds rate	5.1	4.3	3.1	2.5	5.1-5.6	3.9-5.1	2.9-3.9	2.4-2.6	4.9-5.9	3.4-5.6	2.4-5.6	2.3-3.6
December projection	5.1	4.1	3.1	2.5	5.1-5.4	3.9-4.9	2.6-3.9	2.3-2.5	4.9-5.6	3.1-5.6	2.4-5.6	2.3-3.3

Source: FOMC March 2023 Summary of Economic Projections

### Exhibit 3. FOMC Mar 2023 Salient Points: The pause is near, slower growth forecast with higher inflation

#### 1 Stays on course

To further anchored inflation expectation, the Federal Open Market Committee (FOMC) raised the fed funds rate by another 25 basis points, despite proliferation of banking liquidity crisis.

J Powell believed it is too early to fully grasp the effect of the banking crisis, but he expects a pathway still exists to a soft landing.

*"It's too early to say, really, whether these events have had much of an effect. We no longer state that we anticipate that ongoing rate increases will be appropriate to quell inflation; instead, we now anticipate that some additional policy firming may be appropriate."* J Powell

#### 2 Dot Plot: Unchanged Terminal Rate of 5.1% in 2023

2023: The Dot plot from Mar 23 indicate that the median rate remains at 5.1%, unchanged from Dec 22 projection.

For 2024, the median of Fed Funds target rate is at 4.3%, higher than 4.1% in Dec 22

For 2025, the median fed funds target rate is 3.1%, unchanged from Dec 22

Fed Chairman Jerome Powell mentioned that more rate hikes is plausible if needed to fight inflation.

*"If we need to raise rates higher, we will. I think for now, though, we see the likelihood of credit tightening. We know that that can have an effect on the macro economy."* J. Powell

#### 3 Reduction in Growth Projection, and Higher Inflation Rate

Federal Reserve anticipate slower economic growth, lower unemployment, and higher inflation in 2023.

GDP growth projection reduced to 0.4% in 2023 vs 0.5% previously.

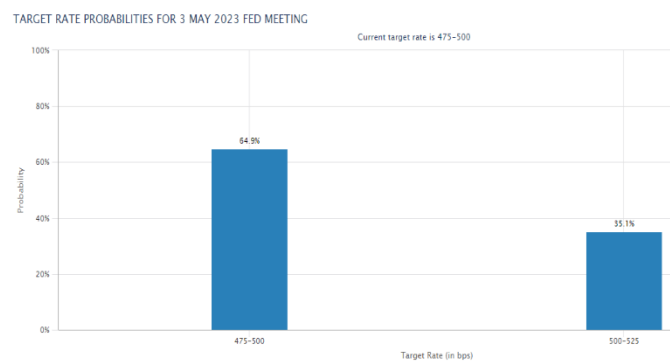
Unemployment rate projection reduced to 4.5% in 2023 from 4.6%.

PCE Inflation projection raised to 3.3% in 2023 (vs Dec' 3.1%) and will remain slightly above Fed's target of 2% by 2025.

*"When a recession happens, the reaction tends to be nonlinear. We don't know whether that will happen this time. We don't know. If so, we don't know how significant it will be. We're very focused on getting inflation down"* J. Powell

Source: BRIDS

### Exhibit 4. No More Rate Hike in May FOMC



Source: CME Fedwatch

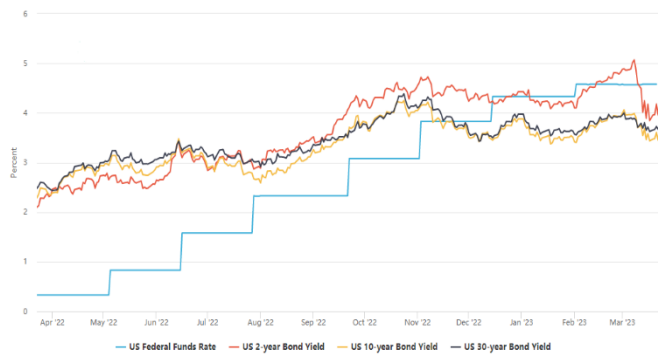
### Exhibit 5. Rate Cut Expectation in 2H23

MEETING PROBABILITIES

MEETING DATE	175-200	200-225	225-250	250-275	275-300	300-325	325-350	350-375	375-400	400-425	425-450	450-475	475-500	500-525
5/3/2023								0.0%	0.0%	0.0%	0.0%	0.0%	65.2%	34.8%
6/14/2023			0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	28.5%	51.9%	19.6%
7/26/2023	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	25.1%	49.1%	23.4%	2.3%
9/20/2023	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	15.3%	39.7%	33.4%	10.6%	0.9%
11/1/2023	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	6.7%	26.0%	37.0%	23.5%	6.4%	0.5%
12/13/2023	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	4.9%	21.0%	34.1%	27.0%	10.8%	2.0%	0.1%
1/31/2024	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	3.6%	16.5%	30.5%	29.0%	15.3%	4.5%	0.7%	0.0%
3/20/2024	0.0%	0.0%	0.0%	0.0%	0.0%	2.9%	14.1%	27.8%	29.3%	17.9%	6.5%	1.4%	0.2%	0.0%
5/1/2024	0.0%	0.0%	0.0%	0.4%	4.3%	15.8%	28.0%	27.8%	16.4%	5.9%	1.2%	0.1%	0.0%	0.0%
6/19/2024	0.0%	0.0%	0.2%	2.3%	9.9%	21.7%	27.9%	22.3%	11.3%	3.6%	0.7%	0.1%	0.0%	0.0%
7/31/2024	0.0%	0.1%	1.5%	7.1%	17.3%	25.6%	24.4%	15.4%	6.5%	1.8%	0.3%	0.0%	0.0%	0.0%
9/25/2024	1.0%	5.1%	13.7%	22.7%	24.8%	18.5%	9.6%	3.4%	0.8%	0.1%	0.0%	0.0%	0.0%	0.0%

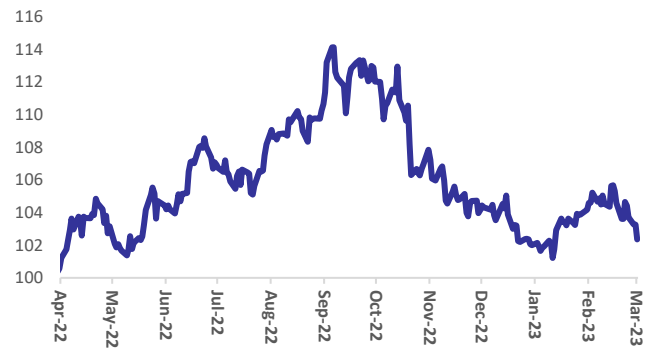
Source: CME Fedwatch

**Exhibit 6. Higher volatility in 2-years yield**



Source: Macromicro

**Exhibit 7. Weak DXY on Rate Cut Expectation**



Source: TradingEconomics

**Exhibit 8. Bank Indonesia: Ensuring Currency Stability**

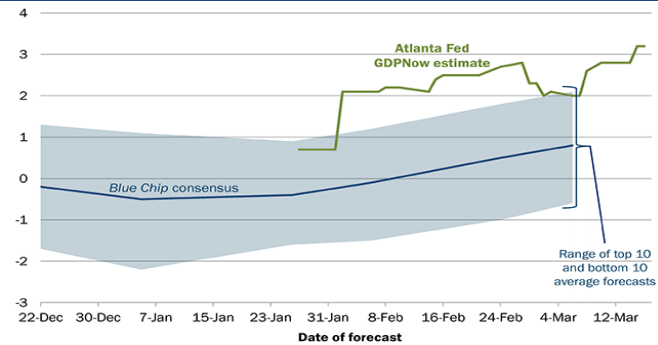
**Bank Indonesia : Market intervention to ensure currency stability**  
Indonesia banking system remains solid

### BI March 2023 Meeting Salient Points

- Rate Unchanged**  
A widely anticipated move, Bank Indonesia Board of Governors' Meeting (RDG) decided to maintain the BI 7-Day Reverse Repo Rate (BI7DRR) at 5.75%, remains on the narrative that the 225-bps increase since Aug 22 was deemed sufficient in anchoring inflation expectation.  
Furthermore, BI reiterate its stance that its rate policy consideration would based on domestic parameters; inflation and growth outlook and could differ from other Central Banks's rate hike path.
- Higher Global Growth Expectation**  
The reopening of China and improved estimates of the US and European economies, which are expected to experience lower recession risk, will lead to higher estimates of 2.6% of global GDP growth in 2023.  
However BI pointed out that the US labor market is still tight, which delays the pace of disinflation and lengthens the duration of restrictive monetary policy in 2023.  
BI Baseline scenario (>75% probability): Fed terminal rate at 5.25%
- Currency Intervention**  
In response to market volatility on the back of the demise of several US regional banks, BI has intervened in the currency market and will do so going forward to ensure Rupiah stability.  
We also believe, the new regulation on TD for DHE will ensure ample ammunition for a more optimal market intervention.
- Banking system remains solid**  
BI acknowledged that the troubles at Credit Suisse and the closure of three US regional banks have raised market uncertainty, halted capital flows to emerging market, and could potentially lead to higher currency volatility. Nonetheless, BI emphasized there's no direct impact on local banks.  
BI's stress test showed that local banks were resilient, had strong capital adequacy ratios, low non-performing loan rates, and a diverse funding sources.
- Inflation Remains under control**  
BI believe that core inflation will remain within target range of 3.0±1% in 1H23, while headline inflation will return within target range by September 2023, as the base effect of the previous year's fuel price hike expires.  
BI will continue the policy coordination with the government (local and national) to manage inflation trend, especially with seasonally high demand during Festive season in the next couple of months.

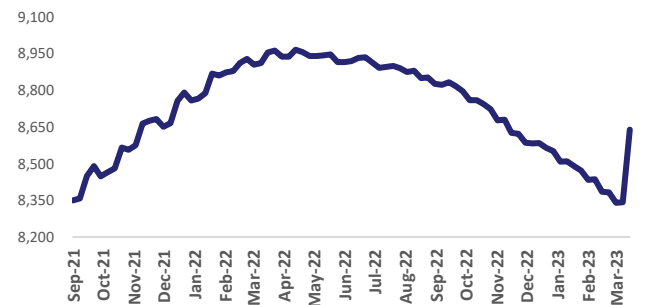
Source: BRIDS

**Exhibit 9. Evolution of 1Q23 Quarterly GDP growth**



Source: Fed Reserve Bank of Atlanta

**Exhibit 10. The Fed Balance Sheet (USDbn.)**



Source: FRED St Louis

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