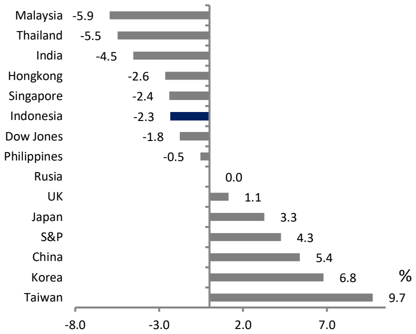
Friday,24 March 2023

Strategy

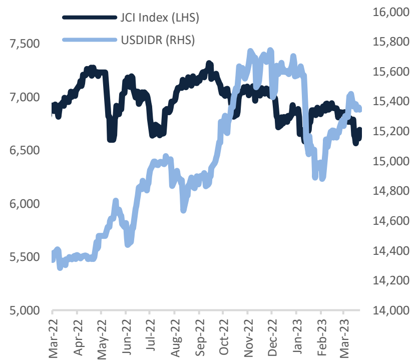
Almost Done

YTD share performance (%)



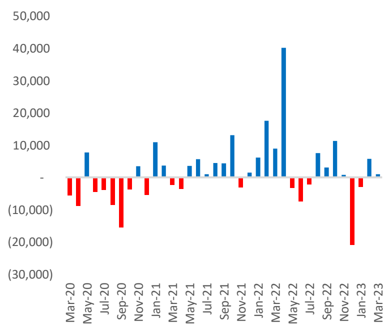
Source: Bloomberg

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.

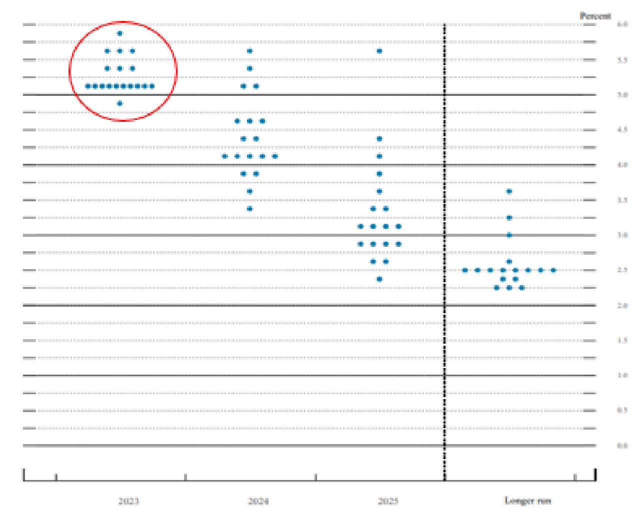
Lower growth expectations. In terms of economic growth projections, the committee reduced its 2023 GDP growth estimate to 0.4%, down from 0.5% forecast in December, or standing in contrast to the recent increase in the Atlanta Fed GDPNow estimate for 1Q23 of 3.2% from 2.0% earlier this month. Growth 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.

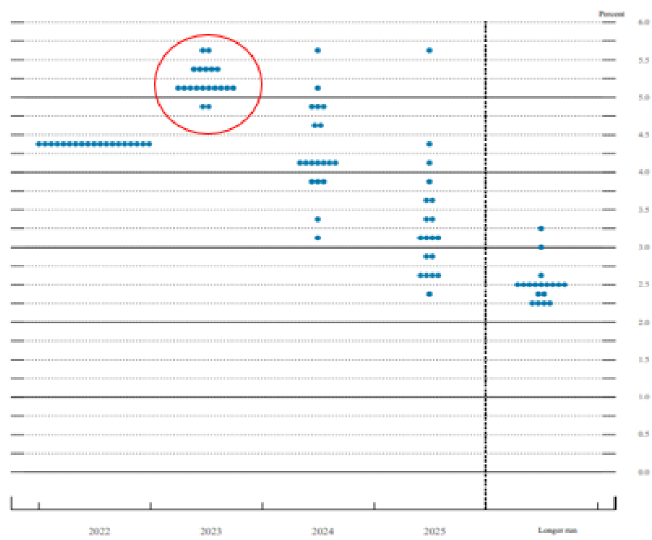
Domestic macro resilience will prevail in Indonesia. While the Fed made no change to its QT program, the newly-launched BTFP (Bank Term Funding Program) may increase overall financial system liquidity, as evidenced in the recent increase in the Fed's total assets. It appears that the Fed has prioritized 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

Mar 2023 Dot Plot



Dec 2022 Dot Plot



Source: FOMC March 2023 Summary of Economic Projections

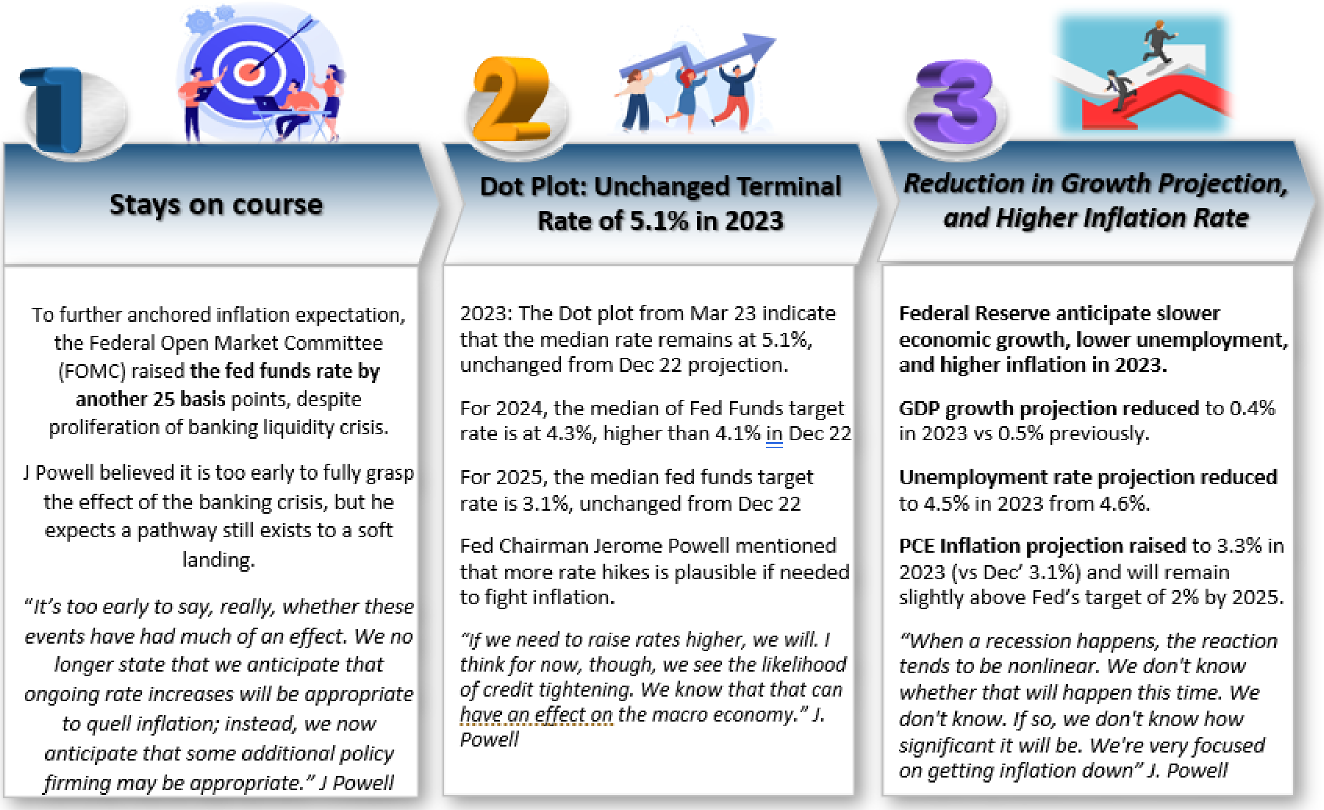
Exhibit 2. Economic projections in Mar 2023

Percent

Variable	Median[1]				Central Tendency[2]				Range[3]			
	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[4]	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

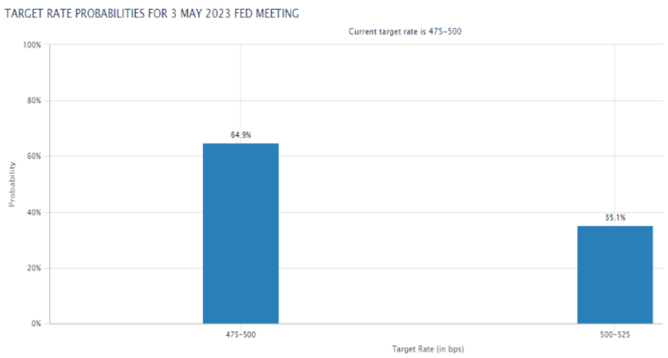
Source: FOMC March 2023 Summary of Economic Projections

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



Source: BRIDS

Exhibit 4. No More Rate Hike in May FOMC



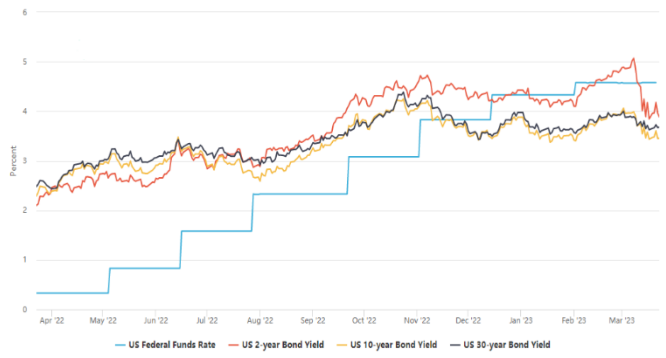
Source: CME Fedwatch

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%

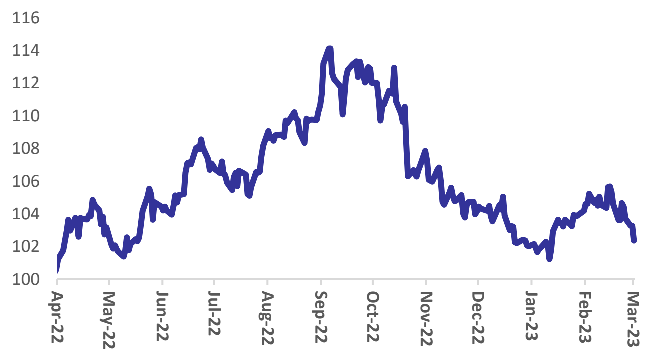
Source: CME Fedwatch

Exhibit 6. Higher volatility in 2-years yield



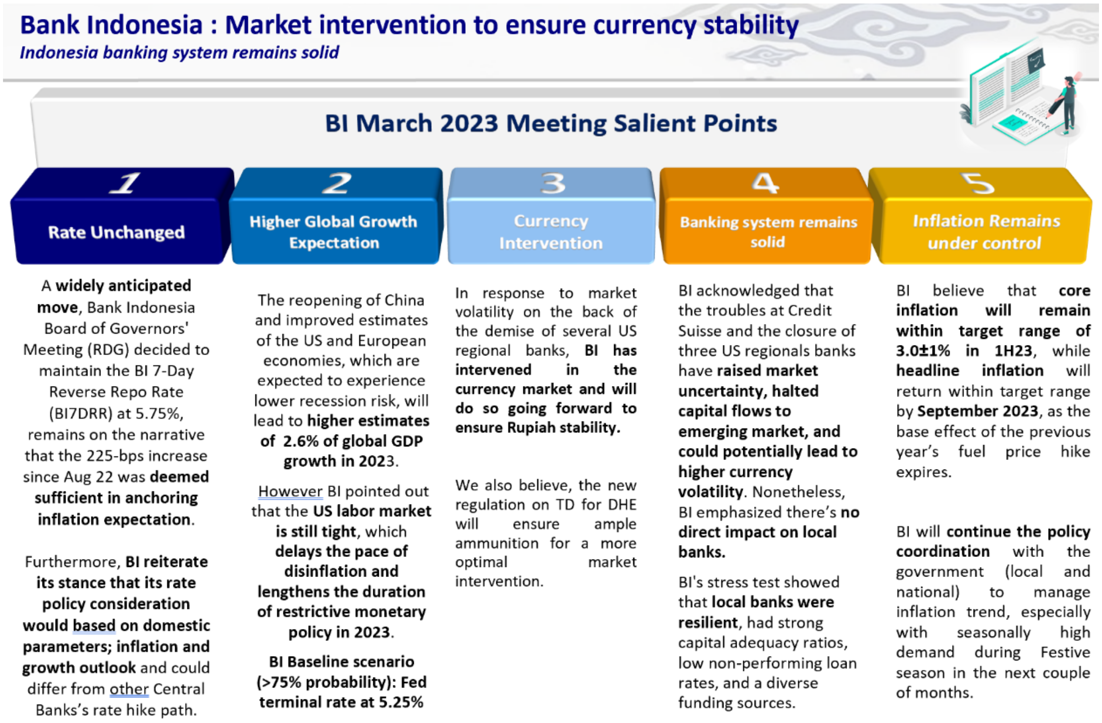
Source: Macromicro

Exhibit 7. Weak DXY on Rate Cut Expectation



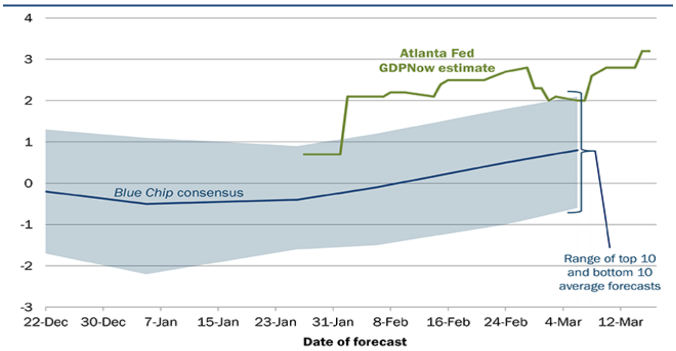
Source: TradingEconomics

Exhibit 8. Bank Indonesia: Ensuring Currency Stability



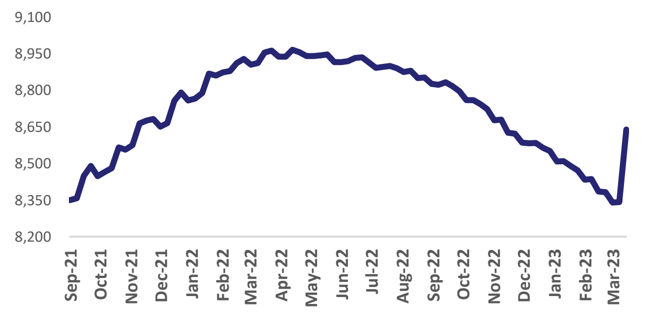
Source: BRIDS

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