Indonesia 2024 bond market outlook

Lower fiscal risk, manageable inflation and expectation of lower interest rate in 2024 as the positive catalyst for bond market

Bond market outlook 2024

- The disinflationary process in US will takes time while the progress toward the desirable level at around 2% is on progress. The impact of accumulative high interest rate to hold the economic activity from overheating has been seen in the slower leading economic activity. This will makes the US GDP to record at below 1.3% or below 2% while the unemployment is expected to slight higher and the wage is projected to expand at slower pace. This will translated to the expectation of pivoting US monetary policy stance to relax the interest rate and its monetary policy. The expectation of lower Fed Fund Rate in 2024 as the positive catalyst for rupiah and also for Indonesia bond yield that will have a room to move lower. We expect that the 10yr yield is possibly to fluctuate at around 6.5% to 7%.

- Indonesia bond yield is remain attractive compared to the several countries due to the monetary policy mix that at the hawkish tone to maintain the inflation at the manageable level. This was as the preemptive movement from the central bank to anticipate the uncertainty in the global market that made a volatility in the market. This policy has reflected in the lower inflation and manageable rupiah volatility to avoid an excessive foreign capital outflow in the bond market.

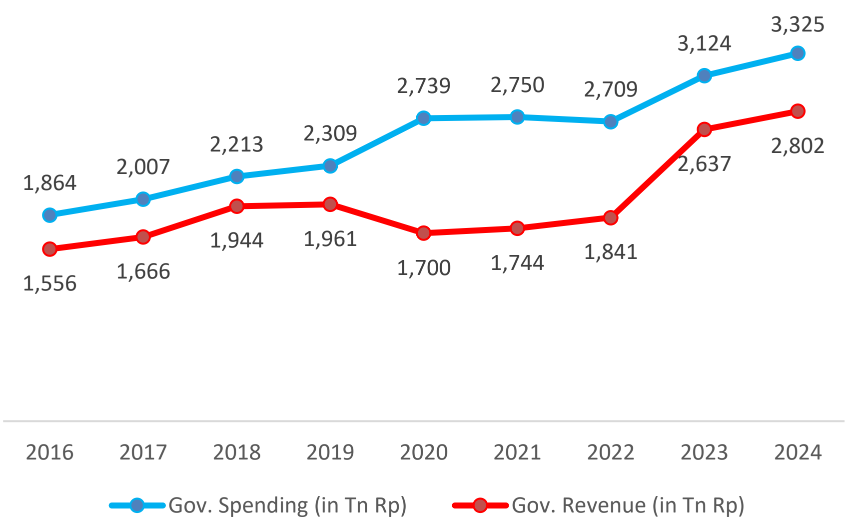
- The low inflation that at 2.86% is another factor that has supported the attractiveness of the real yield to reduce the foreign outflow amid the uncertainty regarding the trajectory of the US Fed Fund Rate.

- The bond supply to fund the fiscal deficit is believe could be absorbed by the market without creating an excessive pressure in the price since the demand for the bond market and the liquidity from external side is estimated will increase along with the outlook of the Fed Fund Rate to change its monetary stance.

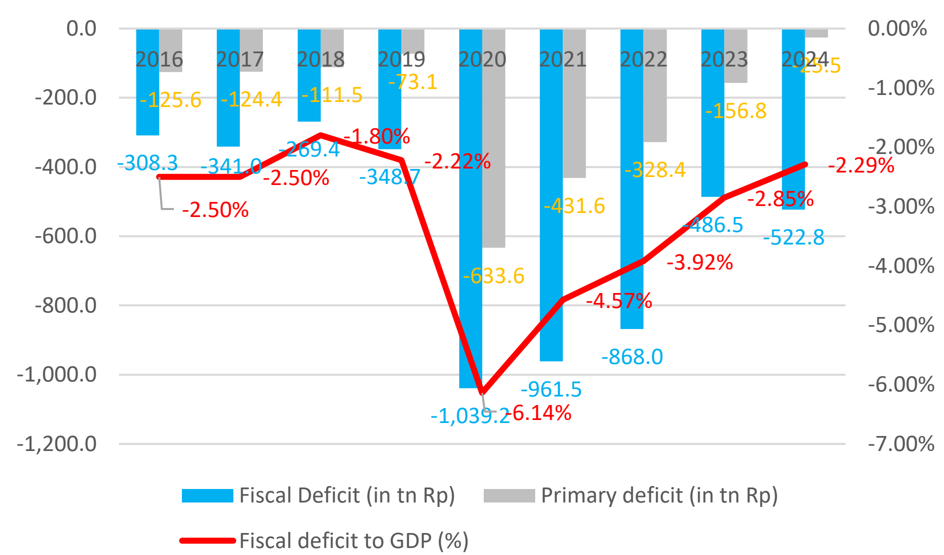
Narrowing the fiscal gap has eased the fiscal pressure amid the uncertainty

Despite the need of financing is increasing to Rp522tn in 2024 from Rp486tn, the size of deficit is going to stronger with the fiscal deficit to GDP is set to reduce to -2.29% in 2024 from -2.9% in 2023. The narrowing fiscal pressure is also reflected in the primary deficit that estimated to reduce to Rp25.5tn from Rp156tn in 2023. This means that the fiscal discipline is continue while providing the room for growth through infrastructure and social assistance to maintain the buying power. By expecting the economic growth at the range of 5% yoy and reducing fiscal deficit ratio to GDP , we expect that the market could absorb the new bond supply without deteriorating the yield. This is because of the supporting factor from external side especially from foreign investor is project to improve, couple with the improving of domestic saving and liquidity as the source of the domestic financing. **The manageable inflation and lower fiscal risk as the necessary condition for the bond price to appreciate in 2024.**

Narrowing fiscal deficit post-pandemic



Fiscal deficit is set to narrow below -3% of GDP in 2023



Source: MOF,SSI

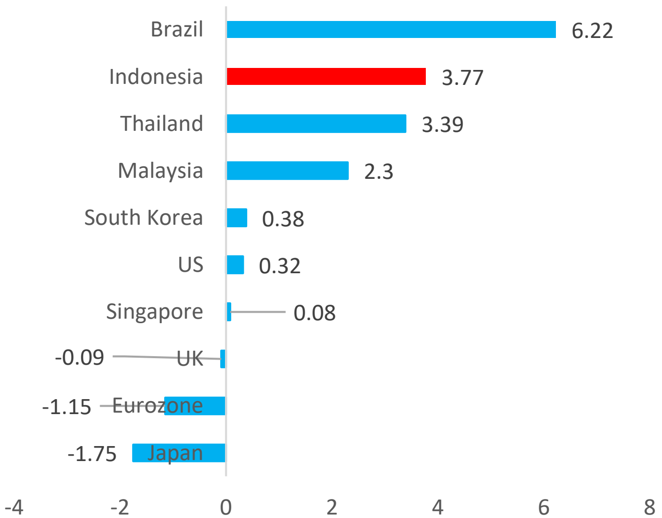
Ample real yield spread to maintain the stability in rupiah as well as in the bond market

Indonesia bond yield is remain attractive compared to the several countries due to the monetary policy mix that at the hawkish tone to maintain the inflation at the manageable level. This was as the preemptive movement from the central bank to anticipate the uncertainty in the global market that made a volatility in the market.

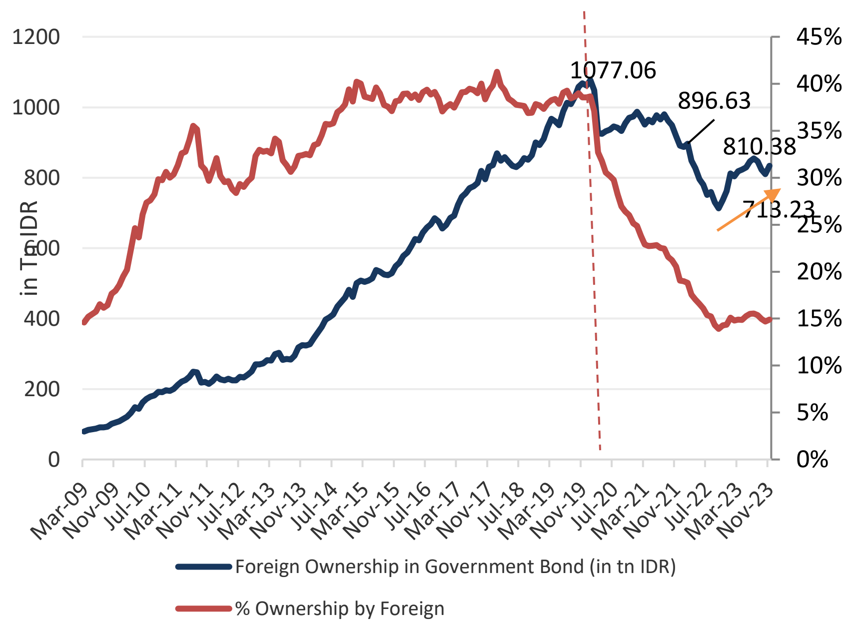
The low inflation that at 2.86% is another factor that has supported the attractiveness of the real yield to reduce the foreign outflow amid the uncertainty regarding the trajectory of the US Fed Fund Rate.

The combination of the manageable inflation and the hawkish monetary policy has also supported the rupiah exchange rate from the further pressure. The rupiah remain relatively resilient against the dollar in 2023 compared to the other country

Manageable inflation and monetary policy mix offering attractive yield



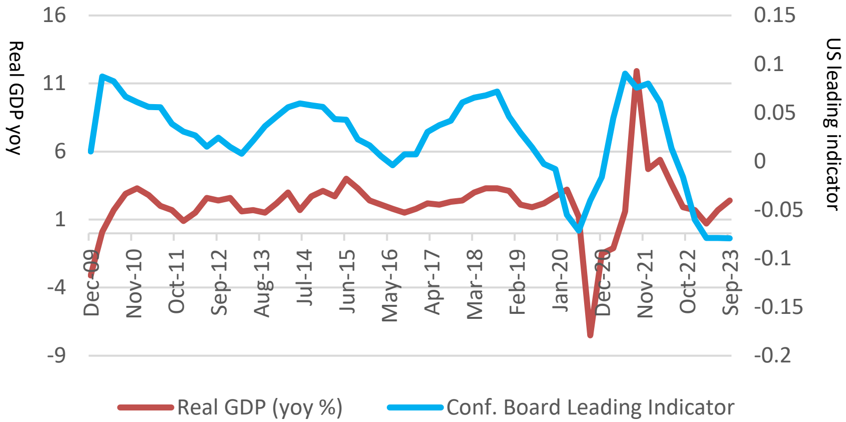
Manageable inflation and monetary policy mix



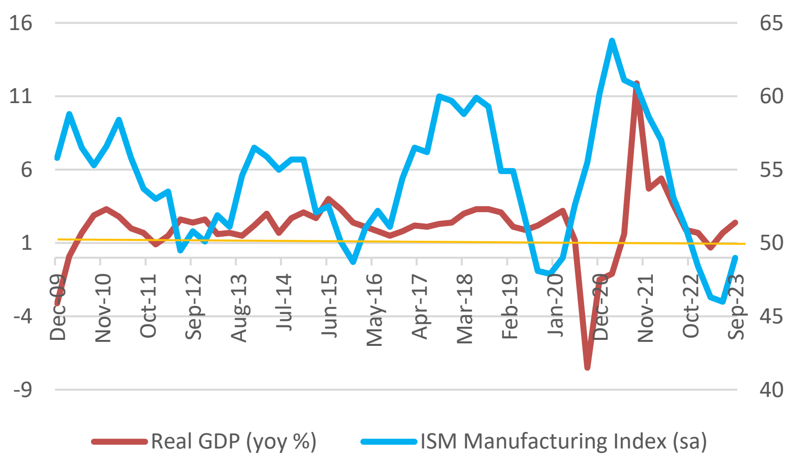
Source: Bloomberg model

US GDP is estimated to posted a lower or below 2% due to the accumulative interest rate

US Real GDP and leading indicator



US real GDP (LHS) and US ISM manufacture index(RHS)



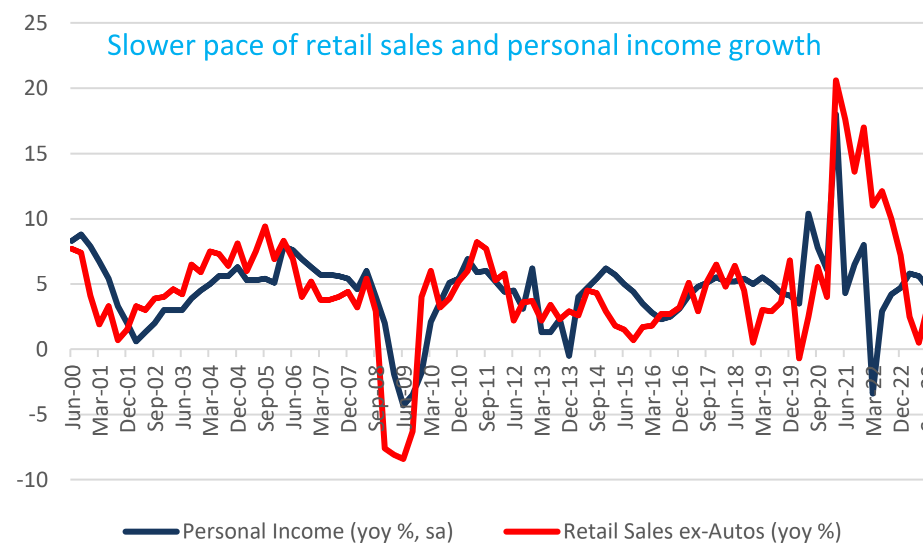
Source: Bloomberg model

The accumulative interest rate hike that has increased the cost of credit is estimated will bring the US GDP in 2024 to fluctuate at the lower growth at below 2% or somewhat at 1.3%.

The US leading economic indicator has also confirmed this expectation that remained at downward trend. This means that the economic in the next couple of quarters will be at the slower pace.

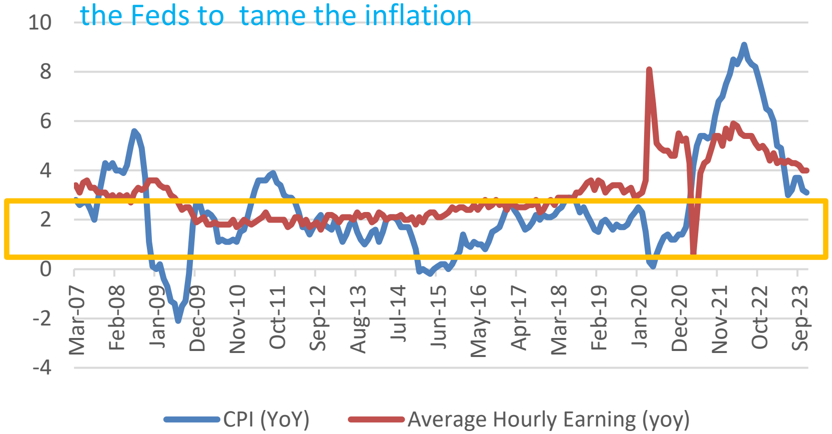
Despite the US economic was resilience however the slower pace in 2024 was likely as seen in the ISM manufacture index that slightly below 50.

The soft lending scenario is likely amid the labour market that remained tight, meaning that the spending and the consumer income remained support the economic. However the slower pace of personal income has been seen which support the sub par growth in 2024.

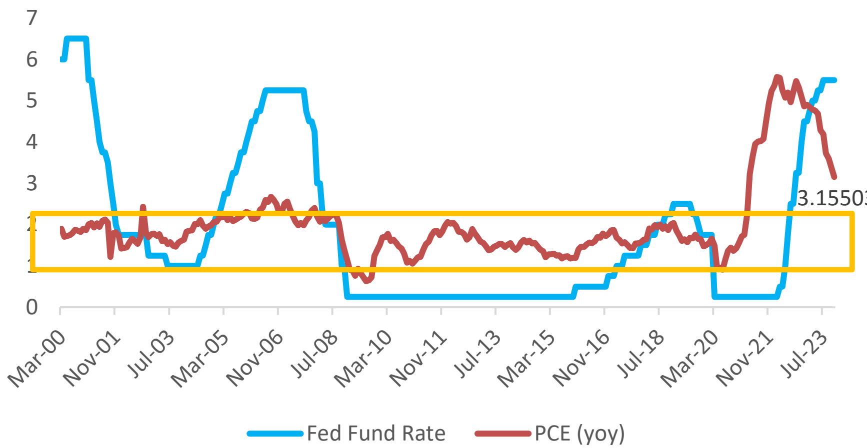


Fed Fund Rate, inflation, wages and economic growth. The pivoting in 2024 is possible

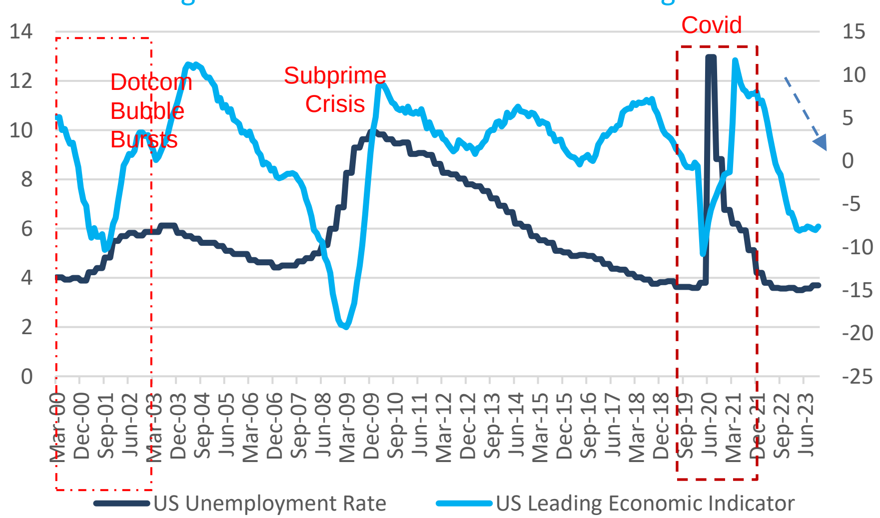
Tight labor and wage prices as the factor that burdened the Feds to tame the inflation

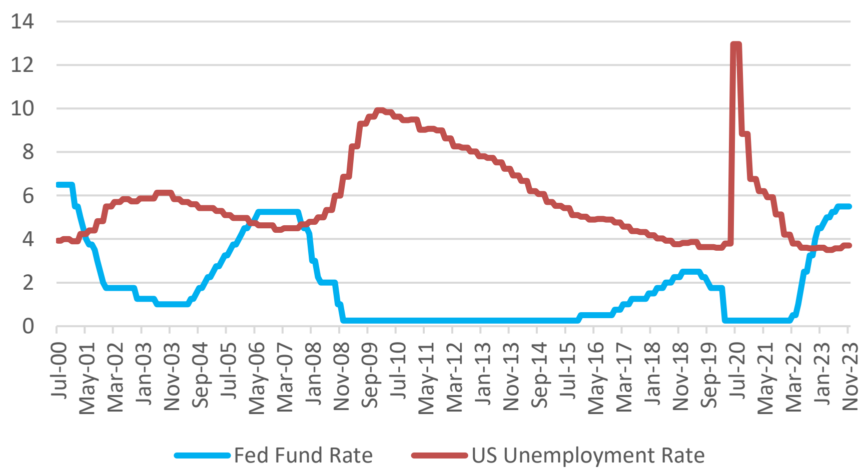


Disinflationary process is still going but need a time to tame the inflation to the desirable level



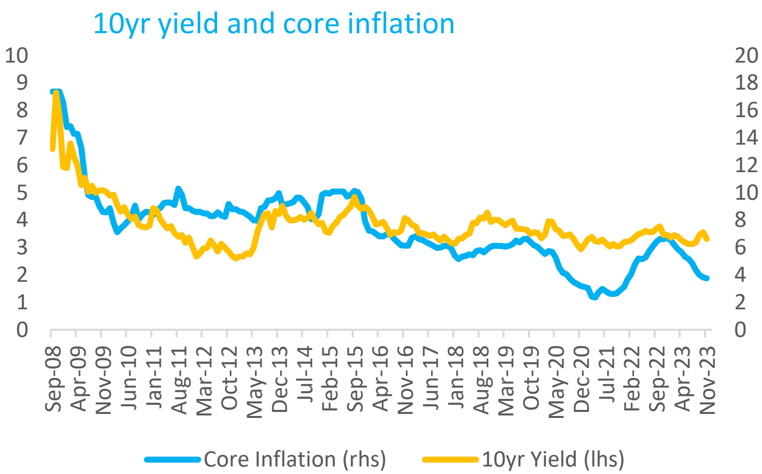
US Leading Economic indicator shows a slower growth





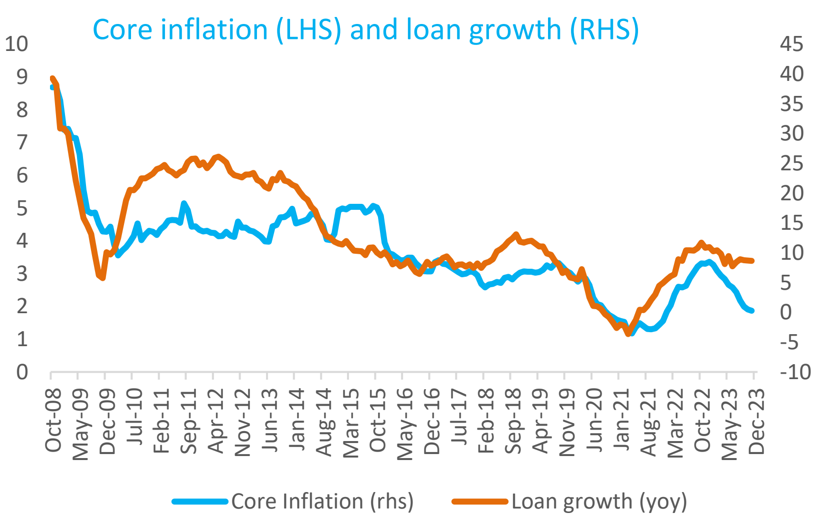
Source: Bloomberg model

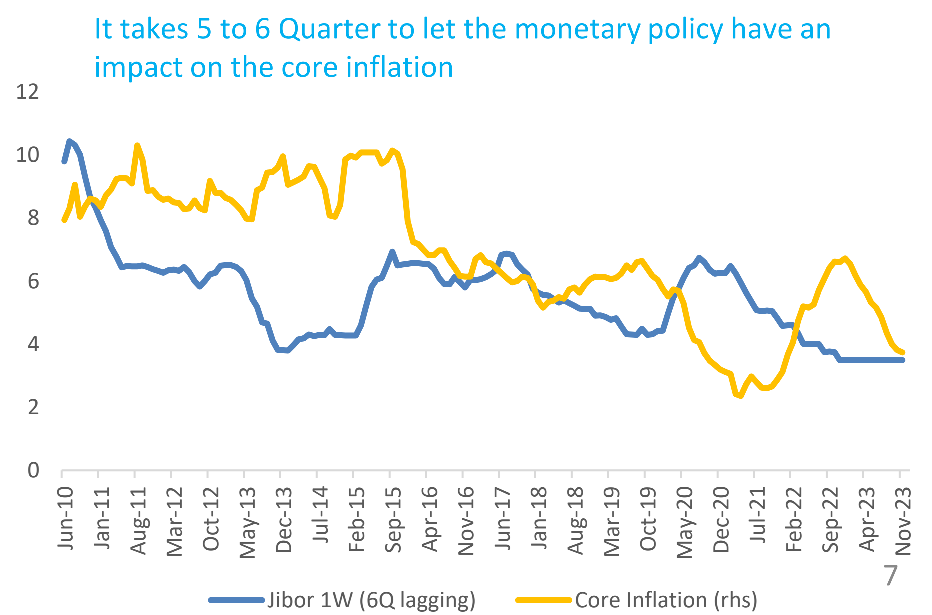
Core inflation, bond yield and monetary mechanism transmission as the factor to expect the yield trajectory



Loan growth as the early indication of the core inflation trajectory. To manage the higher core inflation rate, the Bank of Indonesia has raised the 7D Repo rate to control the peak of the core inflation at a manageable level. The aim for the higher 7D Reverse Repo rate is to anchor the expectation of the forward core inflation rate.

We think that the BI will end its hawkish tone and will consider to cut the rate at the second semester of 2024. The 7D RR rate is expected to hold at the range of 6% and expected to slightly lower to 5.25%. It takes 5 to 6 Quarters to let the monetary policy have an impact on the loan growth as well as the core inflation. We expect the 10yr yield to have room to decrease at the range of 6.5% to 7% in 2024.





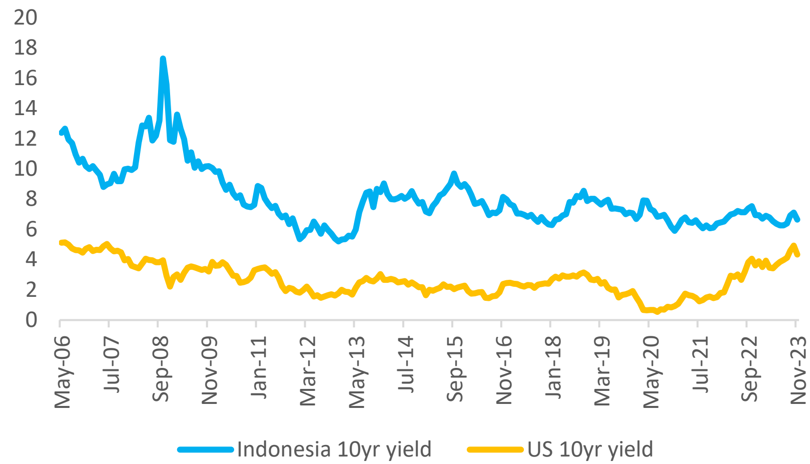
Source: Bloomberg model

Core inflation, bond yield and monetary mechanism transmision as the factor to expect the yield trajectory

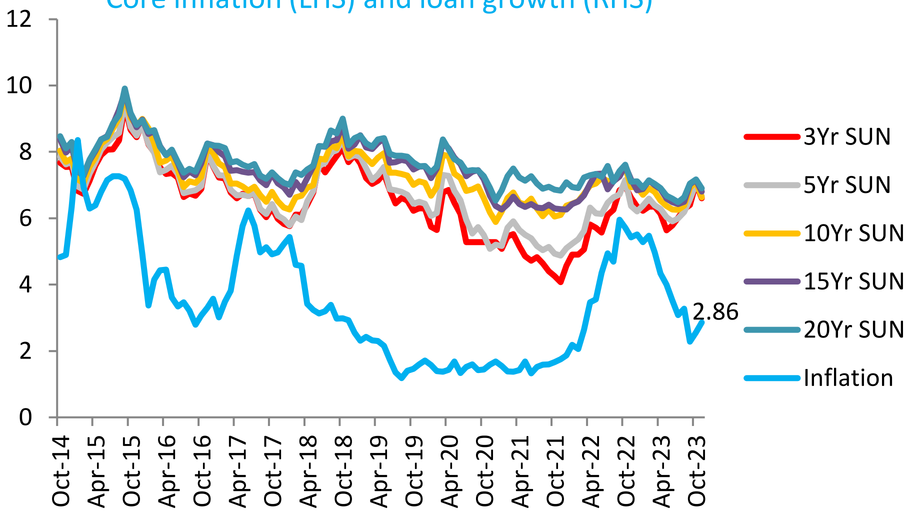
The yield curve shape was reflecting the market expectation toward the inflation, central bank reaction function and also the expectation toward the US policy trajectory toward its economy. With the considerable low inflation environment and positive real yield, we think that this provide room for the yield curve to slightly lower in 2024 on one side. At the other side we also see that the market is also anticipating the pivoting policy in US that possibly will change its monetary tone in 2024 as the result of the US inflation that expected to fluctuate at its desirable level at around 2%.

We saw a possibility for the 10yr yield to fluctuate at below 7% or at around 6.5% in 2024.

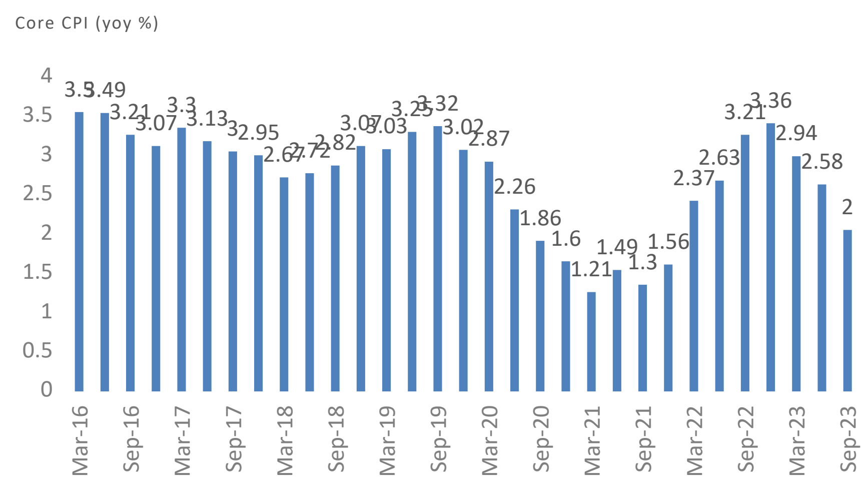
Indonesia & US 10yr yield



Core inflation (LHS) and loan growth (RHS)



US Inflation and Fed Fund Rate



Source: Bloomberg model

Economic projection – Expecting soft economic growth

The Indonesian economy is believed will grow by 4.8% to 5.2% in 2024. The slightly higher interest rate amid slower global economic growth as the challenge while the expectation of pivoting in monetary policy in 2024 as the positive factor to expect the lower volatility in the exchange rate and lower yield in 2024. The domestic aggregate demand is believed would support the growth due to the positive consumer confidence, lower unemployment rate, higher minimum wage, and the result of last year's additive expectation from last year income. Government spending has been set to be consolidative or relatively neutral to the economy this year. Thus we estimate that household consumption will grow by 4.8%, followed by investment growth that is expected to accelerate by 5%. Rupiah is estimated to steady at the range of Rp15,000/USD on the back of the prospect of limited US dollar index appreciation amid the limited upside of the US Fed Fund Rate**. This could be the positive factor to expect the bond yield to move lower in 2024 at around 6.5%.**

Indicator	2016	2017	2018	2019	2020	2021	2022	2023	2024
Economic Activity									
Real GDP (YoY%)	5	5.1	5.2	5	-2	3.7	5.3	5	5
CPI (YoY%)	3.5	3.8	3.2	2.8	2	1.6	4.2	3.7	3
Unemployment (%)	5.6	5.4	5.2	5.1	6	6.4	5.9	5.4	5.4
External Balance									
Curr. Acct. (% of GDP)	-1.8	-1.6	-2.9	-2.7	-0.4	0.3	1	-0.3	-0.8
Fiscal Balance									
Budget (% of GDP)	-2.5	-2.5	-1.8	-2.2	-6.1	-4.6	-3.6	-2.1	-2.3
Interest Rates									
Central Bank Rate (%)	4.75	4.25	6	5	3.75	3.5	5.5	6.05	5.45
3-Month Rate (%)	7.46	5.48	7.7	5.51	4.06	3.75	6.62	6.89	6.16
2-Year Note (%)	7.47	5.54	7.29	5.77	3.85	4.13	6.08	6.57	5.98
10-Year Note (%)	7.97	6.32	8.03	7.06	5.89	6.38	6.94	6.86	6.52
Exchange Rates									
USDIDR	13,473	13,555	14,390	13,866	14,050	14,263	15,573	15,500	15,000

Source: SSI calculation

Thank You

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