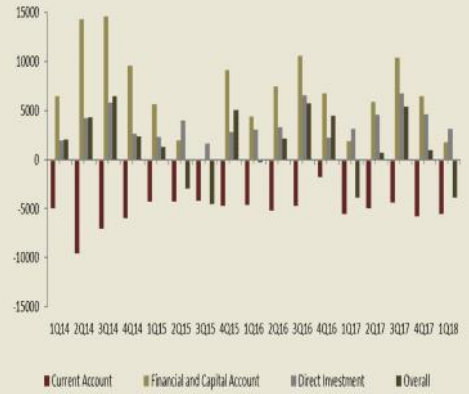
BoP Review

BoP Deficit May Push BI to Raise Rate Earlier

BoP Components

	2016	2017	1Q17	1Q18
Current Account	-19.5	17.3	-2.2	-5.5
Capital Account	0.04	0.05	0.00	0.06
Financial Account	29.3	29.8	6.9	1.8
BoP	12.1	11.6	4.5	-3.8
CAD (% of GDP)	-1.8	-1.7	-0.9	-2.1

BoP Breakdown



Source : BPS & Bank Indonesia

Rupiah and Foreign Reserve

Source : Bloomberg

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BoP fell to deficit for first time since 2015

According to Bank Indonesia (BI), 1Q18 balance of payment (BoP) entered deficit territory of USD -3.8 bn, which was the first time since 1Q16. The sign of BoP deficit has already seen since the foreign reserve position had a downtrend since January position at USD 131 bn to March position at USD 126 bn. However, it is higher than our initial estimate which see BoP deficit at below USD 1 bn.

CAD stabilize at our estimate of 2.1% of GDP

Indonesia's current account deficit (CAD) slightly eased to 2.1% of GDP from 4Q17 position at 2.3% of GDP. Lower CAD in 1Q18 was helped by seasonality in lower service trade deficit and primary income deficit than 4Q17 even though it was still higher than 1Q17 position (see exhibit 1). Goods trade saw a lower surplus at USD 2.4 bn (4Q17: USD 3.0 bn; 1Q17: 5.6 bn) due to jump of imports growth at 19.7% YoY while exports only grew 8.9% YoY. We see most the import growth went to investment segment as BPS noted capital goods import grew 27.7% YoY and investment growth in GDP was at uptrend of 7.95% YoY. On service trade side, the deficit was at USD -1.4 bn which was mainly driven by higher deficit on transportation segment at USD -1.7 bn. We see that higher goods import growth pushing higher import of transportation service at 20.2% YoY as most of imported goods still use foreign freight service. While primary income segment experienced deficit at USD 7.9 bn in 1Q18 but it will give more significant impact on CAD in 2nd quarter and 3rd quarter as the dividend payment will peak on these quarters. We believe that imports growth will not grow as significant as 1Q18 as the consumption remained weak in the beginning of this year. However, higher trade surplus will be challenged by peak of service trade deficit and primary income deficit in next 2 quarters.

Financial account: solid fundamental but volatile global

High global volatility became the main restrain of 1Q18 financial account (FA) which only posted small surplus at USD 1.8 bn or the lowest since 3Q15. If we breakdown the components, we will see that the fundamental side of FA or the direct investment remained solid as it grew 10% YoY. It showed that foreign investors still had positive views on fundamental in long term and current volatility only existed for short term. Portfolio account experienced deficit of USD -1.2 bn as the result of capital outflow. Current global volatility was caused by shifting of FFR hike expectation starting in February when it shifted from 2x hike to 3xhike and in April when it shifted to 4x FFR hike. Despite huge capital outflow in 1Q18, Rupiah performance (depreciate 3.9% YTD) was still better than its peers which had similar investment grade like Rupee (INR) and Peso (PHP) (see exhibit 6). However, deficit in financial account and especially portfolio account showed necessity of central bank to adjust the interest rate to maintain the premium of Indonesia interest rate against US.

BI may increase the rate as fast as this month

Our pessimistic prediction (assuming no effect from Moody's upgrade on Rupiah) of Rupiah approaching Rp 14,000 was happened faster than our previous estimate in year end. At first, we predicted the shifting expectation of 3x hike to 4x FFR hike will happen in 2H18 but it shifted faster than our prediction due to better US economic performance. This condition gave us 2 implications. First, we see that downside risk from FFR hike expectation almost met the end and we predicted that it will end on June when FOMC will give newest projection of FFR hike by 4x. Second, we see that BI will need to adjust the policy rate sooner than our previous forecast. We previously believe that BI will need to adjust rate if Rupiah exceed Rp14,000/USD and had better economic growth which make us believe BI will adjust rate in 1Q19. As Rupiah has exceeded the psychological level in May, we see there is an opportunity of central bank to increase the rate at 25 bps as soon as 2Q18 or even this month. An 25 bps rate hike is believed to not give significant effect to fundamentals, like the GDP growth but it will help to stabilize capital inflow/outflow and Rupiah itself. Furthermore, central bank in Friday has stated that it had huge room for policy rate adjustment.

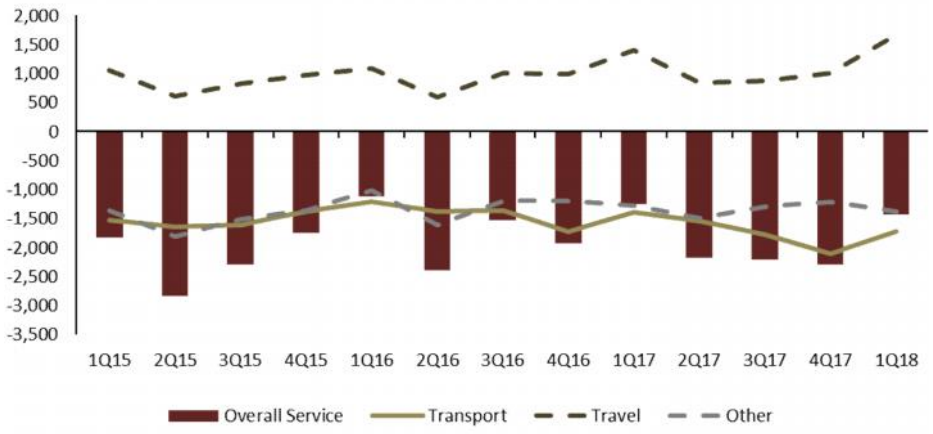
Deficit in Portfolio investment account pull BoP into deficit territory

Exhibit 1: BoP Breakdown

Components	2015	2016	2017	1Q17	4Q17	1Q18
Current Account	**-17,519**	**-16,952**	**-17,293**	**-2,178**	**-5,761**	**-5,542**
%of GDP	*-2.03*	*-1.80*	*-1.70*	*-0.90*	*-2.20*	*-2.15*
Goods	14,049	15,318	18,892	5,637	3,161	2,357
Service	-8,697	-7,084	-7,864	-1,230	-2,296	-1,425
Primary Income	-28,379	-29,647	-32,838	-7,723	-7,821	-7,887
Secondary Income	5,508	4,460	4,517	1,138	1,196	1,412
Capital Account	**17**	**41**	**46**	**0**	**22**	**58**
Financial Account	**16,843**	**29,306**	**29,834**	**6,933**	**6,523**	**1,814**
Direct Investment	10,704	16,136	20,151	2,924	4,605	3,129
Portfolio Investment	16,183	18,996	20,662	6,572	1,887	-1,174
Derivative	20	-9	-128	-72	-69	60
Other Investment	-10,064	-5,817	-10,851	-2,491	99	-200
Net error	**-439**	**-305**	**-1,002**	**-241**	**189**	**-185**
Overall Balance	**-1,098**	**12,089**	**11,586**	**4,514**	**974**	**-3,855**

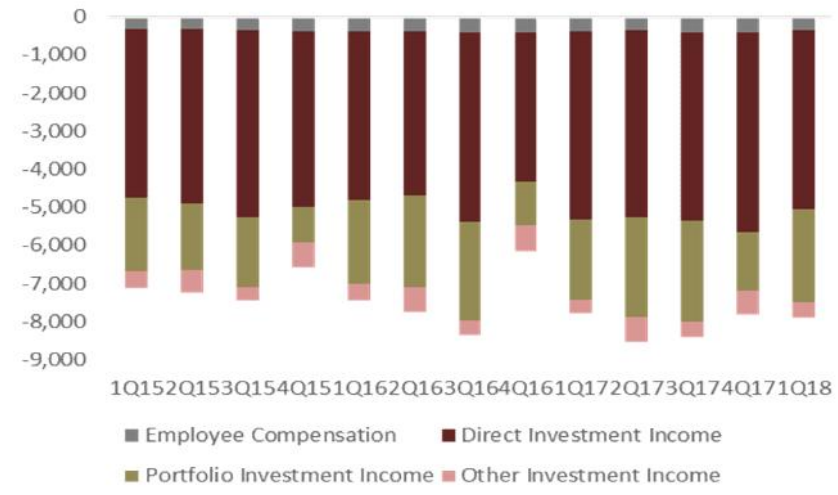
Source: BI

Exhibit 2: Service Sector Breakdown



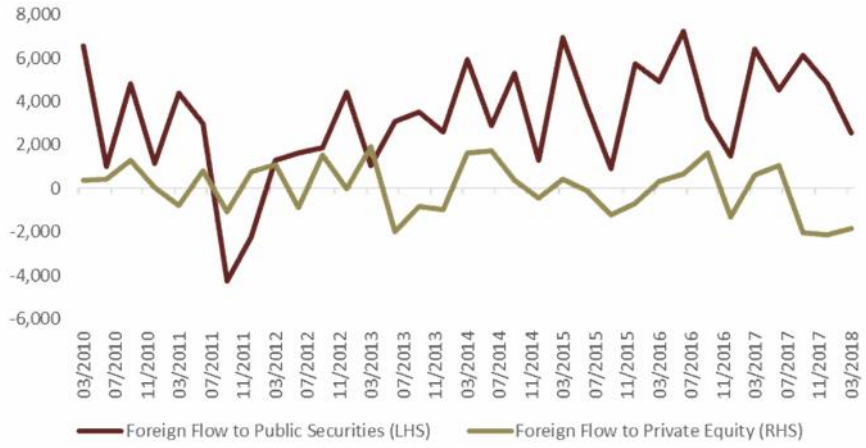
Source: BI

Exhibit 3: Primary Income Breakdown



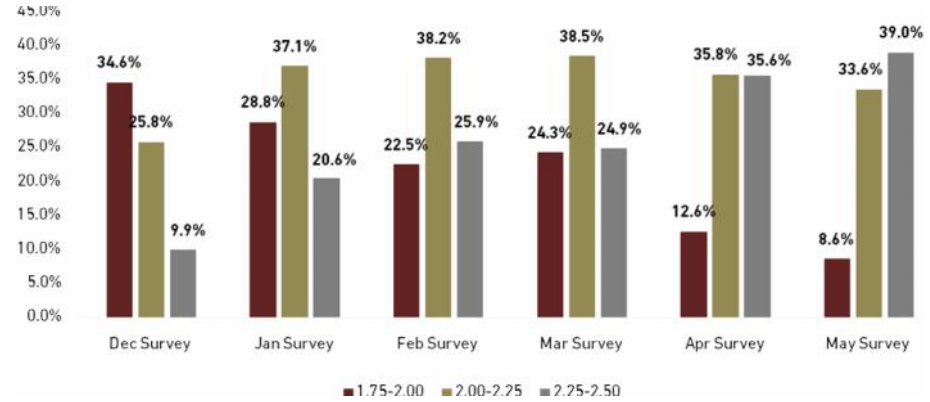
Source: BI

Exhibit 4: Foreign Net Flow to Public Securities and Private Equity



Source: BI

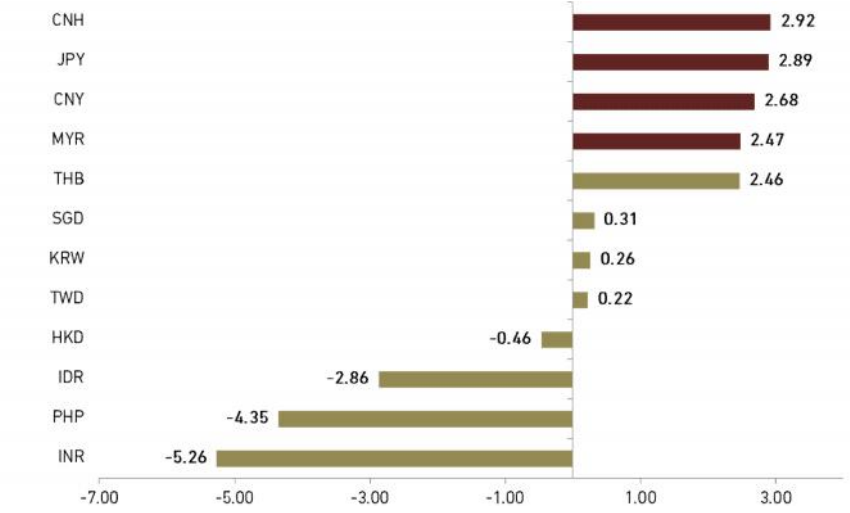
Exhibit 5: FFR Hike Projection



Source: Bloomberg

Current survey showed most economists predict 4x FFR hike in 2018

Exhibit 6: Currencies Performance YTD as of May 14 (in%)



Rupiah performance is still better than Peso (PHP) and Rupee (INR) which has similar sovereign rating

Central bank may raise policy rate as fast as this month

Exhibit 7: Macroeconomic Indicators

Year-end 31-Dec	14A	15A	16A	17A	18F
Nominal GDP (Rp tn)	10,543	11,541	12,407	13,588	14,878
Nominal GDP (USD bn)	888	861	974	1,015	1,102
GDP/capita (USD) - Nominal	3,530	3,377	3,605	3,877	4,158
Real GDP (%YoY)	5.0	4.8	5.0	5.1	5.3
Private Consumption (%YoY)	5.1	5.0	5.0	4.9	5.0
Government consumption (%YoY)	2.0	5.4	-0.1	2.1	3.5
Gross Fixed Capital Formation (%Yo	4.1	5.1	4.5	6.1	7.5
Exports (%YoY)	1.0	-2.0	-1.7	9.1	7.3
Imports (%YoY)	2.2	-5.8	-2.3	8.1	10.5
Inflation rate (%YoY) - year end	8.4	3.4	3.0	3.6	3.5
Core inflation rate (%YoY) - year end	5.5	4.0	3.1	3.0	3.3
BI Rate	7.75	7.50			
BI 7 Days Reverse Repo Rate - year end			4.75	4.25	4.50
Rupiah / US Dollar - average	11,878	13,398	13,473	13,380	13,620
Rupiah / US Dollar - year end	12,440	13,788	13,346	13,555	13,700
Current account as % of GDP	-2.9	-2.1	-1.8	-1.7	-2.1
Fiscal balance as % of GDP	-2.4	-2.8	-2.5	-2.5	-2.4

Source: BI, BPS, MoF, Ciptadana Estimates

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