economic

WEEKLY REVIEW SERIES

Heading to Higher Inflation

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Exhibit 1 Indonesia Macro Data Forecast

Macro Indicators	2020	2021F
Real GDP (%YoY)	-2.07	3.76
Average Inflation (%YoY)	2.04	1.87
BI-7 DRR (%)	3.75	3.5
Budget Deficit (%GDP)	6.09	5.73
USD/IDR	14,500	14,325
Current Account (%GDP)	-0.40	-1.03
10 Year Indo GB (%)	5.89	6.15
JCI	5,979	6,800

Source : BI, MoF, BPS, MNCS Estimate

Exhibit 2 Global & Domestic Key Rates

Rates (%)	Dec-20	Nov-21*
BI-7 DRR	3.75	3.50
Lending Facility	4.50	4.25
Deposit Facility	3.00	2.75
10 Year Indo GB	5.89	6.04
FFR	0.25	0.25
ECB Rate	0.00	0.00
BoE Rate	0.10	0.10
BoJ Rate	-0.10	-0.10

Source : Bloomberg, BI as of Nov 25, 2021

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Tracking Global Inflation & its Causes

- Rising inflation is a phenomenon triggered by Covid-19 shock as supply and demand imbalance widen.
- Both emerging market economies and developed countries experience the same trend. The average inflation of several G20 countries gave us an evidence of rising inflationary pressure.
- The average inflation of EU in 2021 hit the 75th percentile of 5 years historical figures. This case is also found in France and Germany.
- U.S. average inflation this year reached 4.3% YoY and significantly higher than inflation level since Oct-16.
- The similar phenomenon was also observed in emerging economies. On average, Russia's CPI rose by 6.34% YoY in 2021. That is higher than its upper quartile of inflation level during 2016-21.
- Brazil gives us another example where inflation started to nerve consumers. Last month, Brazil CPI increased 10.67% YoY.
- Soaring commodity price is one of inflation contributing factors. Combination of weather, labor shortage and other geopolitical related tension have caused production can not cope up with the demand side.
- Energy and food prices reached a multiyear highs and this trend is expected to stay in 2022.

Monetary Policy Normalization in Check

- U.S. rising inflation and improving job market is expected to drive the Fed more aggressive tightening agenda by speeding up tapering and increasing FFR by early on Jun-22.
- Elsewhere, a hawkish move has been taken by BoK and Norges Bank in Aug-21 and Sep-21 respectively. Korean and Norway central bank became the first developed economies to increase their interest rate by 25 bps.
- In Nov-21 meeting, BoK even set the base rate at 1% or implying a 25 bps increase well aligned with market consensus.
- Some other emerging market country's central banks set a more hawkish tone such as Russia, Brazil and Turkey as inflation and massive currency depreciation are haunting.
- Turkey's Lira saw a massive depreciation against USD by more than 50% on an annual basis and becoming the worst performing emerging countries local currency due to central banks lack of independence and credibility.
- Even with the high inflation, BRCA kept the benchmark policy rate unchanged causing Argentina Peso to drop by 20% in value against USD.
- We already witnessed that rising inflation could have more damaging impact for emerging countries that structurally experience high inflation.

Indonesia : Are We Heading to a Higher Inflation?

- Indonesia's inflation started to pick up in 3Q21. However, the inflationary pressures remain low and benign even below the lower target of central bank ITF.
- Throughout 2021, we observed that CPI across sectors to record a positive growth.
- We expect Indonesia FY21 inflation figure to remain below 2% as the lower band of Bank Indonesia (BI).
- Looking ahead, we see several factors that could drive higher inflation in 2022 including : 1) rising commodity prices and its ripple down effect; 2) higher VAT rate and possible 3) higher tobacco excise rate.
- We assume that inflation to stay manageable given the inflation expectation remain anchored within central bank's target range of 2-4%.
- However with the increase in hawkish tone from global central bank and in order to maintain IDR stability we see that Bank Indonesia has room to increase benchmark policy rate by 50 bps next year.

Tracking Global Inflation and its Causes

Lockdown easing and gradual economic recovery leave another consequence. The severe damage that hit both aggregate demand and supply is then followed by rising inflation. Now we see inflation is everywhere from emerging market economies to developed countries to a level not seen in the last 5 years. The G20 countries gave us clear evidence that even in some economies which inflationary pressure is decelerating now it turns to pick up.

The average inflation of EU in 2021 hit the 75th percentile of 5 years historical figures. This case is also found in France and Germany. U.S. average inflation this year reached 4.3% YoY and significantly higher than inflation level since Oct-16. U.S. became one of the developed nation to experience the highest inflation among peers.

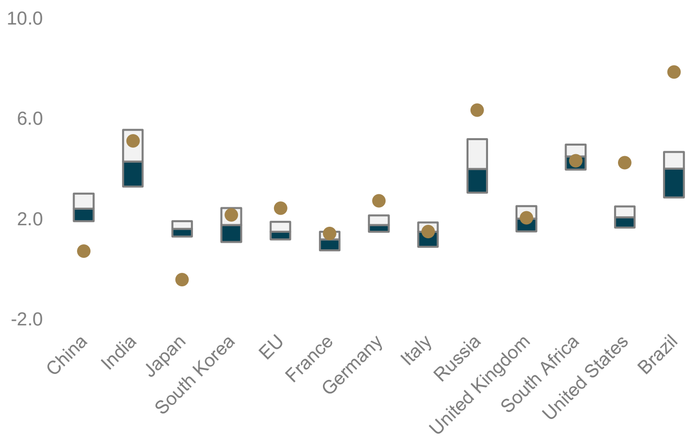
The similar phenomenon was also observed in emerging economies. Russia for instance, in Oct-21 its CPI level rose by 8.13% YoY to the highest level since Oct-16. On average, Russia's CPI rose by 6.34% YoY in 2021. That is higher than its upper quartile of inflation level during 2016-21.

Brazil gives us another example where inflation started to nerve consumers. Last month, Brazil CPI increased 10.67% YoY. Inflation in Brazil started to pick up since 2H20. It means that higher and more persistent inflation lasted for more than a year.

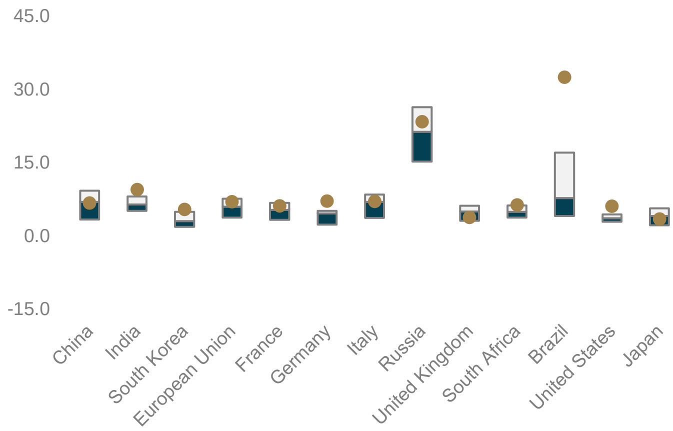
It is worth noted that indeed producers also felt the same way when it comes to inflation. Brazil PPI jumped more than 30% YoY on average this year. Besides the pandemic driven low based effect to persist, we still can not overlook that continued soaring prices in which it can cause a self-fulfilling prophecy to materialize for inflation to have a damaging impact on economies.

Exhibit 3 PPI and CPI Rose to a Multiyear Highs Globally

Average annual CPI growth in 2021 to hit its upper percentile of 5-year historical figures



Average annual PPI growth in 2021 to hit its upper percentile of 5-year historical figures

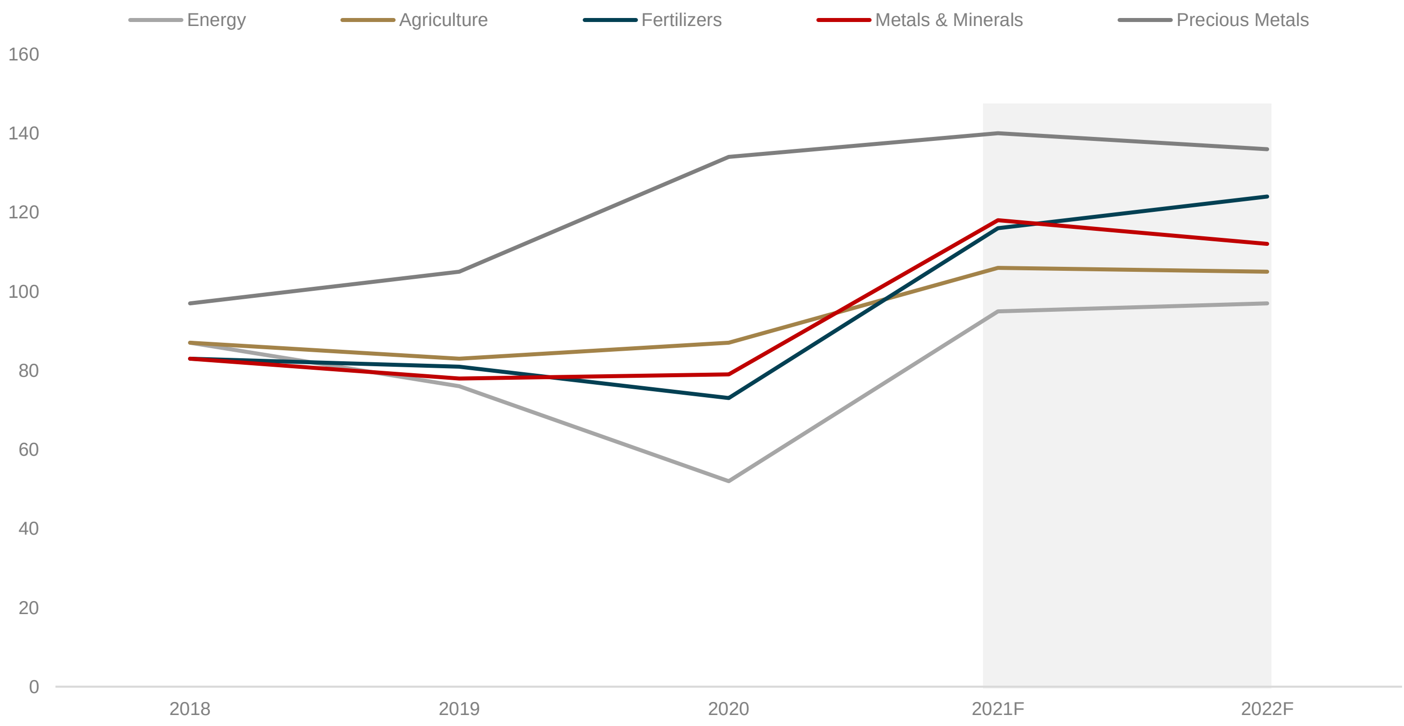


Notes : the dot plot represents avg inflation of 2021 among countries
Source : Bloomberg, CEIC, Trading Economics, MNCS

The supply and demand imbalance is behind it all. Production function was disrupted during lockdown. However, with the unprecedented expansionary macro policy, demand started to gradually recover. Unfortunately, due to several factors such as weather, labor shortage and other geopolitical related tension have caused production can not cope up with the demand side. Therefore, the high rise of inflation began.

Commodity prices from energy, food to agricultural product such as fertilizers and lumber are surging. Besides the benefits it gave to commodity exporting countries, soaring commodity price also driving up inflation. According to World Bank, commodity prices tend to normalize next year as production is being adjusted, yet commodity prices will likely to stay above pre-pandemic level.

Exhibit 4 Historical & Forecast of Commodity Prices



Source : World Bank, MNCS

International Energy Agency (IEA) projected oil demand is set to bounce back with an increase of 5.5 mbpd to 96.3 mbpd in 2021 and 3.3 mbpd to 99.6 mbpd next year. The rise in oil price with spot Brent to record USD84/bbl in Oct-21 was driven by OPEC+ to stick with production increase of 400 kbpd.

The combination of higher coal, gas and European carbon prices have resulted the electricity prices to follow the suit. Low level of stocks and outage driven by maintenance works keeping the price to stubbornly high.

High energy prices cause a ripple down effect that influence household and business sectors bills. It is worth noted that the jump in natural gas price forced utilities company to switch to coal rather than to renewables. The implication is clear, as coal and gas is used in fertilizer, cement and steel production. A sharp rise in those manufactured goods if also combined with logistic disruption on the back of mobility restriction will be translated into a broader price increase.

Monetary Policy Normalization in Check

Besides the complex interaction between supply and demand that spur inflation, we can not set aside that during Covid-19 economic shock central banks play a major role as economic stimulator agent. An unconventional approach partly through liquidity injection (QE) is enacted by global central banks both in emerging and developed economies

The U.S. core PCE inflation recorded an increase of 4.1% YoY hitting the highest level that was not seen since Jan-91. Combined with improving jobs market, the Fed is pressured to adjust its pace on asset purchase program. In Nov-21 policy meeting The Fed finally decided to reduce QE by USD15bn per month or simply recognized as tapering.

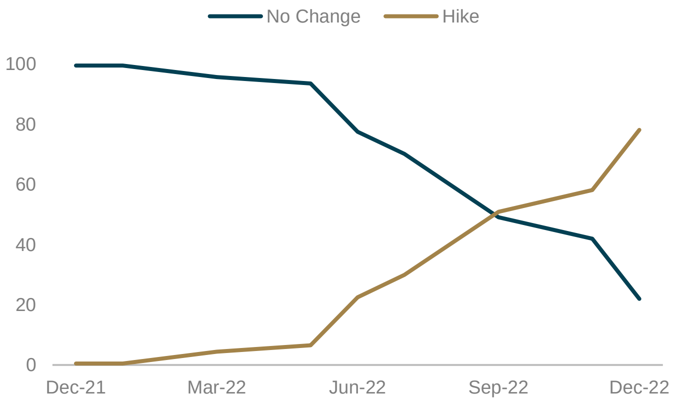
Given that no surprise in policy measures taken and well anticipated move by the Fed, global financial markets did not show a negative reaction that we saw back in 2013. However, continued rise in inflation may trigger the Fed to step in with more aggressive move by speeding up tapering process and followed by hiking benchmark policy rates next year.

Markets have started to anticipate a more hawkish tone of monetary policy as the idea of temporary inflation is waning. In 1H21 both majority of FOMC participants and markets expect that rising benchmark policy rate is expected to happen in 2023. However, in Sep-21 meeting 9/18 FOMC participants foresaw that room for increasing FFR by 25 bps is widely open in 2022.

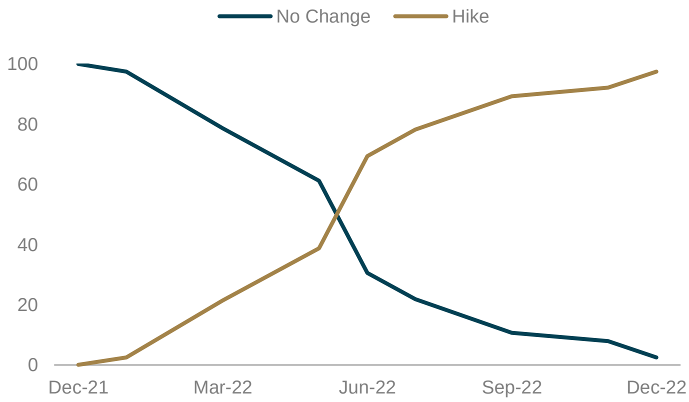
Going forward, with the high rise of inflation to stay markets see that interest rate increase can be taken in Jun-22. Even consensus now skew towards 3x interest rate hike in 2022 as we can see on CME FedWatch contracts recently. By the end of 2022, FFR target is likely to be at 50-75 bps.

Exhibit 5 The probability of the Fed to tighten monetary policy in Sep-21 vs Nov-21

Sep-21 : The Fed is expected to increase FFR by 25 bps in Dec-22



Nov-21 : The Fed is expected to increase FFR by 25 bps in Jun-22 and followed by another 50 bps hikes for the rest of 2022



Source : CME FedWatch, MNCS

Elsewhere, a hawkish move has been taken by BoK and Norges Bank in Aug-21 and Sep-21 respectively. Korean and Norway central bank became the first developed economies to increase their interest rate by 25 bps. In Nov-21 meeting, BoK even set the base rate at 1% or implying a 25 bps increase well aligned with market consensus.

In emerging economies that already experience high inflation before Covid-19 shock such as Turkey, Russia and Brazil, rising consumer prices is followed by monetary tightening. The interest rates in those 3 countries have been raised cumulatively by more than 100 bps since early 2020.

Turkey’s Lira saw a massive depreciation against USD by more than 50% on an annual basis and becoming the worst performing emerging countries local currency. This was attributable to worsening central banks independence and credibility besides the high inflation problems. To put in the context, the 2021-average inflation of Turkey has reached 17.6% YoY or significantly higher than central bank’s target of 5%.

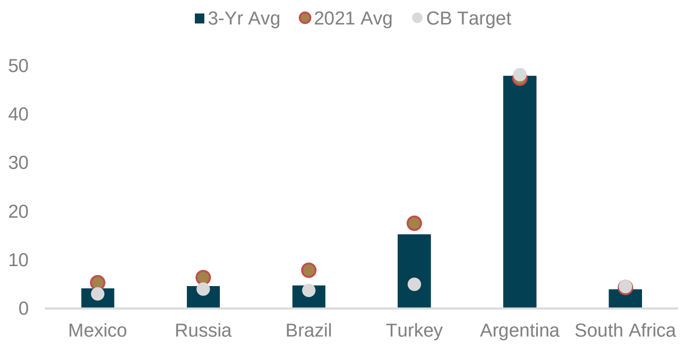
Argentina's inflation is even more dramatic. However, BRCA seems to resist to tighten their monetary policy. The interest rate in Argentina remained 200 bps lower since 2020. As the result, Argentina Peso value has lost more than 20% of its value against USD.

We already witnessed that rising inflation could have more damaging impact for emerging countries that structurally experience high inflation. Therefore, the room for central banks to stimulate economic performance is far more limited.

Given the current condition of high inflation, global investor is set to trim bond holding from their portfolio. A recent survey by Reuters showed that in Oct-21, bond holding is expected to be reduced to below 40% from global balanced funds portfolio. Now investors globally overweight on equities as bond price is expected to decline further.

Exhibit 6 Inflation & Rates across Fragile Emerging Economies

Overshoot inflation was observed in emerging market economies (%)



Source : Trading Economics, MNCS

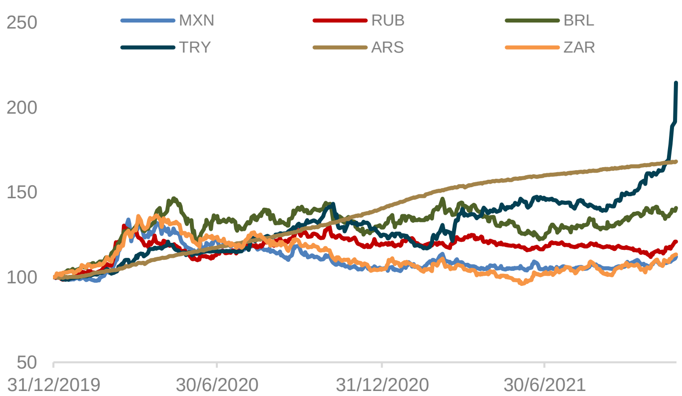
Russia, Brazil and Turkey have tighten their interest rates

Countries	Pandemic Cut	Rate Hikes	Overall Change	MP Status
Mexico	-300	100	-200	Loose
Russia	-175	325	150	Tightening
Brazil	-225	575	350	Tightening
Turkey	-250	-200	425	Tightening
Argentina	-200	0	-200	Loose
South Africa	-275	25	-250	Loose

Notes : size of pandemic driven rate cut since early 2020 to the lowest level (bps); cumulative rate hikes throughout 2021 (bps); overall changes indicated benchmark rates hikes/declines since 2020.

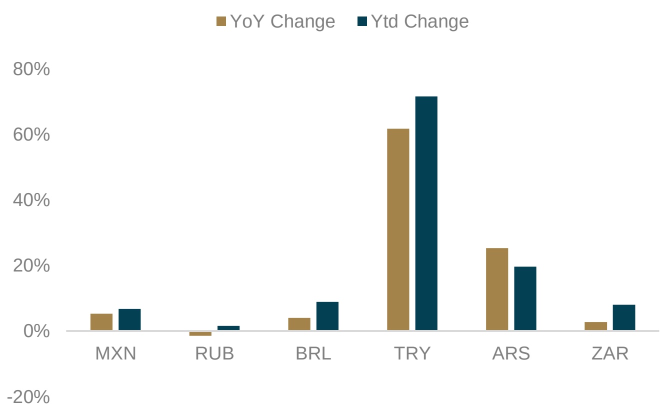
Exhibit 7 Currency Performance across Fragile Emerging Economies

The movement of USD against fragile emerging economies since 2019



Source : Bloomberg, MNCS

The annual and year to date degree of depreciation against USD



Indonesia : Are We Heading to a Higher Inflation?

After a deflationary impact of Covid-19 shock, consumer prices started to accelerate in 3Q21. Despite the rise in consumer price, inflationary pressure remained low and benign below central bank's target of 2-4%. Of a note Indonesia CPI rose by 1.66% YoY in Oct-21.

Despite the increasing in inflation, the broad money (M2) supply is still increasing with the double digit pace during the same period. We believe that ample liquidity in the economy to have a stimulatory impact for the output given that inflationary pressure to remain low.

Throughout 2021, we observed that CPI across sectors to record a positive growth. Based on the expense, a year to date CPI in Food, Beverage and Tobacco tend to decelerate with the pace of 0.6% (vs 2.0% in 2020). The key driver remain on a stable food staple price and adequate supply.

We see that higher public mobility after easing of PPKM Darurat to have a positive impact on transportation, recreations and clothing CPI as discretionary spending increase. However as work from home policy is being implemented, the inflation that came from household equipment particularly on eating equipment and housing & gardening device significantly increased.

Meanwhile the impact of soaring energy commodity price started to materialize this year. The energy price inflation rose by 0.3% year to date (vs -0.3% in 2020). The cost of electricity, gas and other fuels for household tend to follow the suit.

Inflation from healthcare sectors remained positive yet the pace is slowing. As of Oct-21, the healthcare sector CPI rose 2% YoY or equal to 1.5% year to date (vs 2.4% in 2020). This was attributable to government policy to control PCR and other Covid-19 related diagnostic prices.

We expect Indonesia FY21 inflation figure to remain below 2% as the lower band of Bank Indonesia (BI). Looking ahead, we see several factors that could drive higher inflation in 2022. We believe that higher commodity price will have an inflationary impact in Indonesia too.

Rising oil price if followed by higher mobility should be translated to higher oil imports values and volume. In the previous weekly report[1], our model has showed that for an increase of oil price by USD1/bbl would be translated into 0.12 percentage point higher in CPI. For 1STD shock in oil price would be positively responded by inflation for at least 5-6 months.

Another factor that we see to have an inflationary effect is government tax reform by hiking VAT rate by 1pp to 11% that due on Apr-22. Increasing 1pp of VAT would add 0.27 percentage point to CPI, our model showed[2].

We also closely watched MoF fiscal policy on tobacco excise rate for 2022 that is scheduled by the end of this month. Historically speaking, government has increased tobacco excise rate by more than 10% annually in order to increase revenue collection and controlling smokers population among youngster and women in Indonesia.

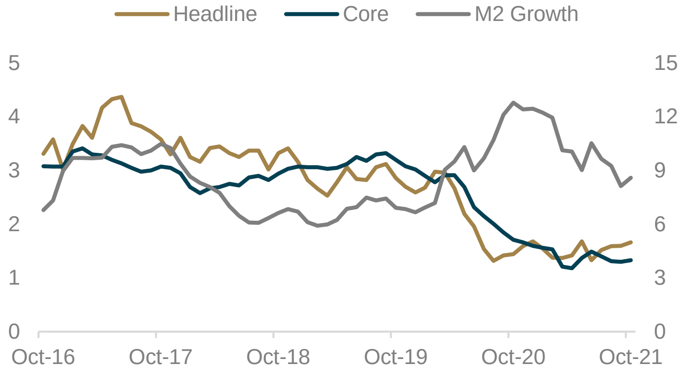
Rising tobacco excise rate will have an inflationary impact too, yet we believe that this will be insignificant given the trend that showed excise rate hikes is not always followed by the same degree of increasing cigarette retail price. Indeed, we see higher inflation is coming next year.

We assume that inflation to stay manageable given the inflation expectation remain anchored within central bank's target range of 2-4%. However with the increase in hawkish tone from global central bank and in order to maintain IDR stability we see that Bank Indonesia has room to increase benchmark policy rate by 50 bps next year.

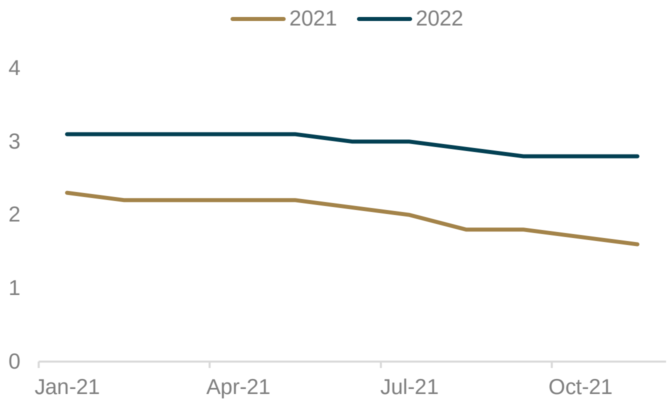
Foot note :
1 Economic Weekly Review Series : Our Notes on Crisis Supply Disruption, Commodity Boom and Inflation (November 2, 2021)
2 Economic Weekly Review Series : Tax Reforms Challenges Fine Tuning Between Timing & Fiscal Sustainability (October 18, 2021)

Exhibit 8 Indonesia Inflation and Inflation Expectation

Inflation started to pick up in 3Q21yet remained below CB target despite ample liquidity in the economy



Inflation expectation well anchored to CB target of 2-4%



Source : Bank Indonesia, Statistics Indonesia, MNCS

Exhibit 9 Indonesia Inflation by Expense

Indonesia CPI	FY20	Oct-21 MoM	Oct-21 YoY	Oct-21 YTD
Based on Components				
Core	1.4%	0.1%	1.3%	1.2%
Headline	0.5%	0.3%	1.5%	1.0%
Volatile	1.7%	0.1%	3.2%	-0.3%
Based on Specific Components				
Energy	-0.3%	0.1%	0.2%	0.3%
Food Ingredients	1.7%	0.0%	3.2%	-0.1%
Based on Expense				
Food, Beverage & Tobacco	2.0%	0.1%	3.0%	0.6%
Food	1.7%	0.0%	3.0%	0.1%
Non -Alcoholic Beverages	1.1%	0.2%	1.6%	1.4%
Alcoholic Beverages	-0.3%	0.0%	0.7%	0.5%
Tobacco	4.9%	0.5%	4.4%	3.9%
Clothing & Footwear	0.9%	0.2%	1.4%	1.2%
Clothing	0.9%	0.2%	1.5%	1.4%
Footwear	0.8%	0.1%	0.8%	0.7%
Housing, Water, Electricity & other Fuels	0.2%	0.1%	0.5%	0.5%
Housing Rent	0.1%	0.0%	0.5%	0.5%
Housing Maintenance & Repair	0.9%	0.2%	1.7%	1.6%
Water Supply & Housing Services	0.1%	0.2%	0.2%	0.2%
Electricity, Gas & other Fuels	0.0%	0.0%	0.0%	0.2%
Household Equipment, Equipment & Routine Maintenance	0.9%	0.1%	2.2%	2.1%
Furniture, Household Equipment, and Carpet	0.1%	0.0%	1.7%	1.5%
Household Textile	1.9%	0.0%	2.4%	2.0%
Household Device	1.5%	0.4%	1.4%	1.3%
Glassware, Eating and Drinking Device, and Equipment	0.7%	0.9%	5.9%	5.1%
Housing and Gardening Device and Equipment	2.1%	0.6%	4.6%	4.2%
Goods and Services for Routine Household Maintenance	0.9%	0.0%	2.0%	1.9%
Health	2.4%	0.1%	2.0%	1.5%
Medicines and Health Product	4.6%	0.1%	3.3%	2.3%
Outpatient Care	1.4%	0.1%	1.5%	1.2%
Inpatient Care	0.3%	0.0%	0.5%	0.5%
Other Health Services	1.6%	0.0%	3.0%	2.6%
Transportation	0.0%	0.3%	1.2%	0.4%
Vehicles Purchasing	1.2%	0.0%	-0.3%	-0.4%
Personal Transportation Equipment Operations	-0.1%	0.1%	1.3%	1.3%
Passenger Transportation Service	-0.7%	1.2%	2.6%	-0.7%
Package Courier Service	0.8%	0.1%	0.3%	0.3%
Information, Communication, and Financial Service	-0.4%	0.0%	0.0%	0.0%
Information and Communication Device	-0.4%	0.2%	0.0%	0.0%
Information and Communication Service	-0.4%	0.0%	0.0%	0.0%
Insurance	0.0%	0.0%	0.2%	0.2%
Financial Service	0.0%	0.0%	0.1%	0.1%
Recreation, Sports, and Culture	0.6%	0.0%	0.9%	0.8%
Durable Recreation Goods	-0.3%	0.0%	1.1%	1.1%
Other Recreation Goods	1.3%	0.0%	0.5%	0.5%
Recreation Service	0.5%	0.0%	0.4%	0.4%
Cultural Equipment	1.5%	-0.3%	1.7%	0.1%
Cultural Service	-0.7%	0.1%	-0.5%	-0.4%
Newspaper, Books, and School Supplies	0.7%	0.1%	1.8%	1.7%
Education	1.5%	0.0%	1.7%	1.6%
Basic and Early Age Education	1.4%	0.0%	1.5%	1.5%
Intermediate Education	1.0%	0.0%	2.2%	2.2%
Higher Education	2.1%	0.0%	1.3%	1.3%
Education That is not Determined by Levels	1.3%	0.0%	2.6%	1.4%
Food and Beverage Provision/Restaurant	2.1%	0.1%	2.6%	2.2%
Food and Beverage Provision Service	2.1%	0.1%	2.6%	2.2%
Personal Care and Other Services	5.3%	0.0%	0.5%	1.1%
Personal Care	2.1%	0.2%	2.8%	2.3%
Other Personal Care	12.0%	-0.3%	-3.5%	-1.2%
Social Protection	0.7%	0.0%	0.6%	0.6%
Other Services	3.2%	0.0%	1.7%	1.1%

Source : Statistics Indonesia, MNCS

MNC Research Industry Ratings Guidance

OVERWEIGHT: Stock's total return is estimated to be above the average total return of our industry coverage universe over next 6-12 months

NEUTRAL: Stock's total return is estimated to be in line with the average total return of our industry coverage universe over next 6-12 months

UNDERWEIGHT: Stock's total return is estimated to be below the average total return of our industry coverage universe over next 6-12 months

MNC Research Investment Ratings Guidance

BUY : Share price may exceed 10% over the next 12 months

HOLD : Share price may fall within the range of +/- 10% of the next 12 months

SELL : Share price may fall by more than 10% over the next 12 months

Not Rated : Stock is not within regular research coverage

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