

February 2008

CPI AND SBI OUTLOOK

February 2008 Inflation Outlook: To stay above 7 percent

- ❑ In January 2008, the consumer price index (CPI) rose 1.77% MoM (month-on-month), after increasing by 1.10% MoM in December 2007. As such, the YoY (year-on-year) inflation rate increased from 6.59% in December to 7.36% in January.
- ❑ Prices rose in all components of the CPI. The biggest increase was posted by the Foodstuffs component (up 2.77% MoM), followed by the clothing component (up 2.31%), the processed foods component (up by 2.02% MoM), the housing component (up 1.80% MoM), the medical care component (up 0.72% MoM), the transportation component (up 0.24% MoM), and the education component (up 0.10% MoM).
- ❑ The January inflation figure was considerably higher than expected (we had expected the January inflation figure to reach 1.06% MoM). Driving inflation higher were high prices of rice and kerosene. Note that flooding in some parts of the country has heightened concerns of poor harvests in the coming months. This created rumors of rice scarcity, which, in turn, led to sharply higher rice prices. Government intervention in the rice market had been expected to help stabilize the price of rice. But such efforts did not help as much as expected, however. As a result, rice prices rose significantly in January – in fact even more than in December. Making things worse, traders took advantage of the situation by raising the selling prices of other foodstuffs as well. And since higher foodstuff prices mean higher input costs for the prepared foods industry, the producers of prepared foods passed on the increases in production costs to consumers.
- ❑ The significant rice price increases in December-January over the last two years might alter inflation expectations, and furthermore, might slightly alter the long-term inflation trend. As such, inflation might not fall below 6 percent in 2008.
- ❑ Looking ahead, although the flooding in parts of the country shall put some additional upward pressures on prices, we still expect seasonality factors to help ease inflationary pressures in February. For a start, the harvesting season will start to kick in at the end of the month. In addition, the government announced its “price stabilization policy” in early February in a bid to bring down the prices of five main commodities (rice, cooking oil, soybeans, wheat, kerosene) to their normal levels. Hopefully, this policy shall help to minimize price fluctuations. As such, we expect monthly inflation to be lower in February than in January.
- ❑ Against this backdrop, we predict that inflation will reach 0.61% MoM in February 2008, with the YoY inflation rate falling slightly to 7.35%.

DRI Forecast for February 2008

Inflation	
MoM (%)	0.61
YoY (%)	7.35

SBI	
End of period (% p.a)	8.00

Forecast for 2008

Inflation (%)	6.13
SBI (% p.a)	7.50

PURBAYA YUDHI SADEWA, Ph.D.
 Head of Economic Research
 (62-21) 350 9777 ext 3600
 yudhi@danareksa.com

DAMHURI NASUTION
 Senior Econometrician
 (62-21) 350 9777 ext 3602
 damhuri@danareksa.com

BRAMANIAN SURENDRO
 Economist
 (62-21) 350 9777 ext 3605
 bramanian@danareksa.com

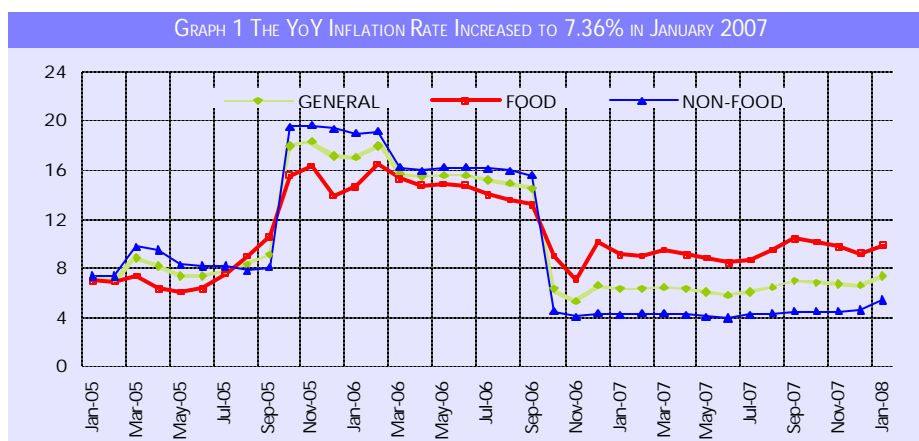
The Impact on Interest Rates

Limited Room for Further Cuts in the Benchmark Rate.

The rupiah has started to strengthen again on the back of increasing capital flows into the country. The year-on-year inflation figure, however, has been above 6.5% since August 2007. It even reached 7.36% last month, and is likely to stay at a similar level next month. As such, we do not expect the central bank to ease its monetary policy further given that the central bank has formally adopted an Inflation Targeting (IT) monetary policy framework. Under this framework, the central bank's sole goal is to keep inflation in check. It can do this either by hiking interest rates or maintaining interest rates at a relatively high level. As such, we do not expect the central bank to cut rates from their current level of 8.00%.

The benchmark rate is unlikely to be cut in the first quarter of 2008.

January's high inflation figure will prevent the Indonesian central bank from cutting interest rates in the first quarter of 2008. In April, however, the central bank might have room again to lower its benchmark rate further - provided inflation is benign.



Changes in Consumer Price Index (percent)

	M-on-M changes			Y-on-Y changes			YTD (Jan-Jan)		
	Nov-07	Dec-07	Jan-08	Nov-07	Dec-07	Jan-08	2006	2007	2008
FOODSTUFF	0.04	2.47	2.77	11.96	11.26	11.35	4.29	2.68	2.77
PREPARED FOOD	0.43	0.91	2.02	6.63	6.41	7.62	0.94	0.87	2.02
HOUSING	0.12	0.63	1.80	4.99	4.88	6.01	0.70	0.71	1.80
CLOTHING	1.66	0.99	2.31	7.50	8.42	11.21	0.73	-0.25	2.31
MEDICAL CARE	0.26	0.41	0.72	4.98	4.31	4.51	1.06	0.54	0.72
EDUCATION	0.11	0.12	0.01	8.77	8.83	8.73	0.20	0.10	0.01
TRANSPORTATION	-0.27	0.22	0.24	1.13	1.25	1.39	-0.05	0.10	0.24
GENERAL	0.18	1.10	1.77	6.71	6.59	7.36	1.36	1.04	1.77
Food and Non-Food									
FOOD	0.20	1.84	2.47	9.74	9.26	9.83	2.86	1.94	2.47
NON-FOOD	0.17	0.49	1.16	4.55	4.58	5.40	0.45	0.37	1.16

Source : BPS

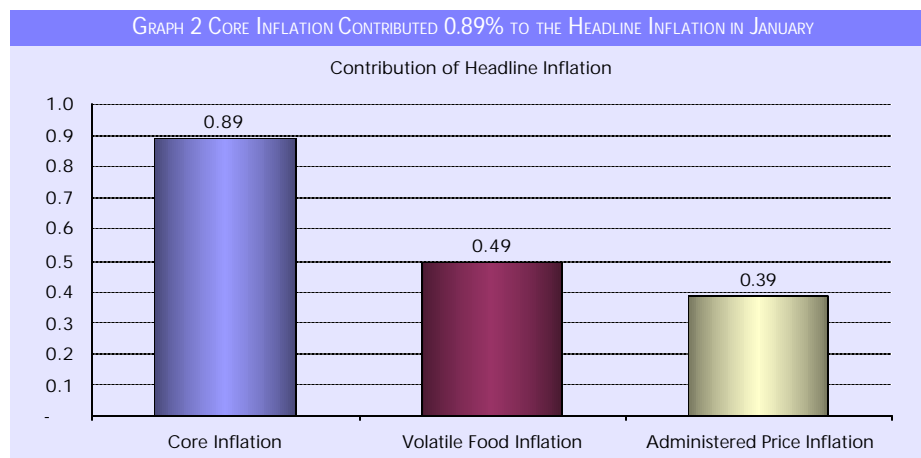


TABLE 2. DRIVERS OF PRICE CHANGES IN JANUARY

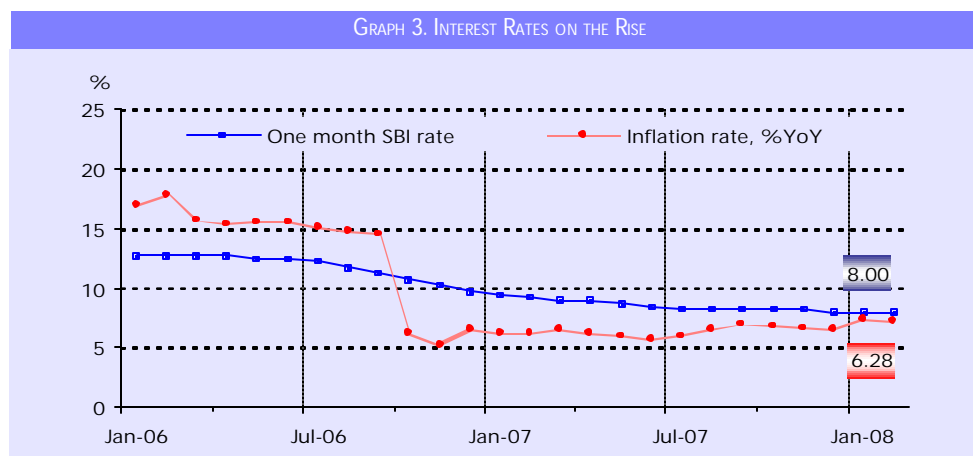
Component	Change (%)	Drivers	Contribution (%)
Foodstuffs	2.77	Rice, fresh fish, tempe, raw tofu, cooking oil, egg, chicken meat, spinach, coconut, dry noodle, dry noodles instant, wheat flour, beef, powdered milk, kangkung, green mustard greens, long eggplant, carrots, wine	0.67
Prepared foods, beverages and cigarettes	2.02	Noodles, rice with the side dish, oily biscuit, sweet bread white bread, filtered cigarette, doughnut, gado gado, wet cake, martabak, granulated sugar, clove-flavoured cigarette	0.34
Housing	1.80	Kerosene, concrete iron, house lease free, bricks, cement, house rent fee, craftman salary, lpg, servant salary	0.49
Clothing	2.31	Gold and Jewelry	0.13
Medical care	0.72	Toothpaste	0.03
Education, recreation and sports	0.01	-	-
Transportation and communications	0.24	Lubricant, atm card	0.04
General			1.77

TABLE 3. FEBRUARY 2008 INFLATION FORECAST

	Jan-07	Feb-07	Mar-07	Apr-07	May-07	Jun-07	Jul-07	Aug-07	Sep-07	Oct-07	Nov-07	Dec-07	Jan-08	Feb-08
M-on-M changes	1.04	0.62	0.24	-0.16	0.10	0.23	0.72	0.75	0.80	0.79	0.18	1.10	1.77	0.61
Y-on-Y changes	6.26	6.30	6.52	6.29	6.01	5.77	6.06	6.51	6.95	6.88	6.71	6.59	7.36	7.35
Yearly*	6.10	6.13	6.34	6.13	5.86	5.64	5.91	6.34	6.76	6.34	6.52	6.41	7.14	7.13

* 12-month cumulative

GRAPH 3. INTEREST RATES ON THE RISE



RESEARCH TEAM

Purbaya Yudhi Sadewa, Ph.D.

Head of Economic Research
yudhi@danareksa.com

David E. Sumual

Economist
davidsumual@danareksa.com

Asti Suwarni

Industry Analyst
asti@danareksa.com

Bramanian Surendro

Economist/Econometrician
bramanian@danareksa.com

Natalia Daisyana

Research Assistant
natalia@danareksa.com

Damhuri Nasution

Senior Econometrician
damhuri@danareksa.com

Darwin Sitorus

Economist / Database Officer
darwin@danareksa.com

Martin Jenkins

Editor
martin@danareksa.com

Handri Thiono

Junior Economist
handrit@danareksa.com

Rika P. Ismalestari

Secretary
rikap@danareksa.com

Danareksa Research Institute

Danareksa Building
Jl. Medan Merdeka Selatan 14
Jakarta, 10110
INDONESIA
Tel : (62-21) 350 9777 / 888 (hunting)
Fax : (62 21) 3501709

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