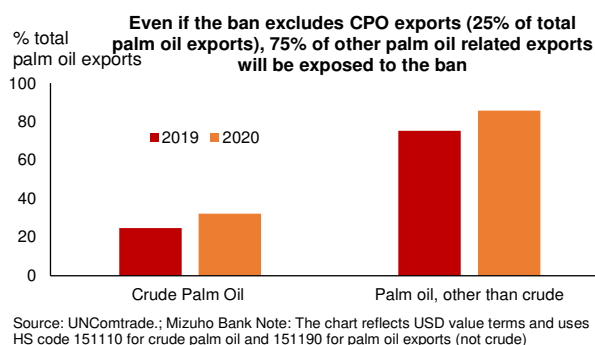
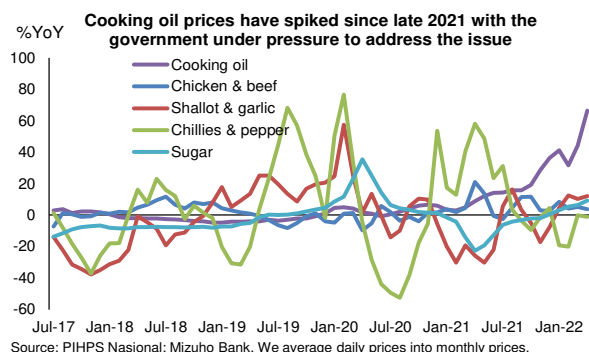


Palm Oil Pressures

In a nutshell: *The ban on exporting palm oil from 28 April will have a significant impact, even if the directive does not include Crude Palm Oil (CPO) exports. In a bid to stem the rise in domestic cooking oil prices, the government’s export ban threatens additional pressure on the external balance, bouts of IDR volatility and potentially elevated food domestic prices from a circular feedback loop of global food prices staying elevated.*

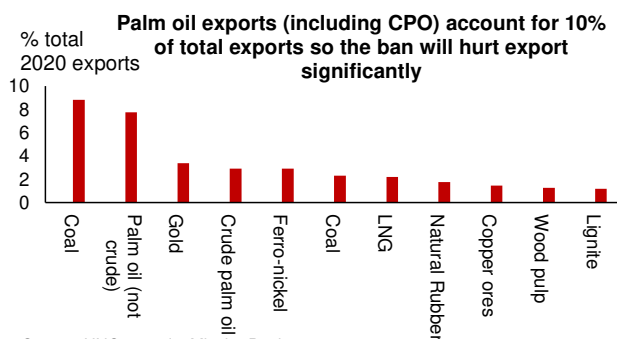
The government’s decision to ban palm oil exports, later clarified to exclude CPO exports, from 28 April aims address domestic cooking oil shortages and the subsequent price spike. Cooking oil prices have soared since November 2021 and attempts by the government to stymie the rise in prices by setting a domestic market obligation of 20% for palm oil producers and capping retail prices failed, pushing them to resort to a more drastic export ban.

The ban order itself has been marred by uncertainties. The initial announcement on 22 April suggested that Indonesia would ban palm oil exports for an indefinite period (i.e. until the government deems the domestic supply-demand situation resolved). However, a later clarification on 25 April stated that the ban excluded CPO exports, which in 2019 (pre-Covid) accounted for 25% of total palm oil exports while other palm oil exports constituted the 75%.

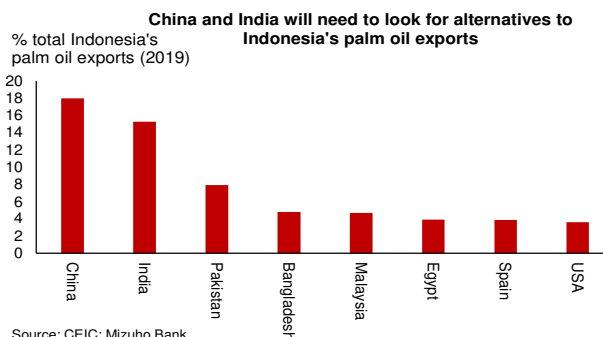


Even so, the ban will have a considerable impact on exports. Palm oil (including CPO) accounts for over 10% of exports, and along with coal, is the biggest contributor to exports. And non-CPO related palm oil exports account for ~8%. Notwithstanding resilient export volumes, the strong price effects from higher global palm oil prices boosted Indonesia’s trade (and current account) position in 2021. While these tailwinds were set to reverse into this year, this ban has expedited the process. We estimate that the ban, if imposed for a month, can worsen the current account balance for the year by 0.2% of GDP¹. This impact will compound if the ban is extended for longer periods of time.

¹ This is a rough back of the envelope calculation based on past non-CPO related revenues, adjusted for a monthly.



Source: UNComtrade; Mizuho Bank.
Note: We look at HS6 level details on exports



Source: CEIC; Mizuho Bank

The ban leaves Indonesia’s main palm oil export markets, India and China, exposed to higher price pressures and domestic shortages of their own. India and China account for a third of total palm oil exports and will be scrambling to look for alternatives to replace this supply. Malaysia, the next biggest palm oil exporter, will be benefit to some extent from this substitution demand but with a lag (as contracts are made etc.) exacerbating already fragile situations in both countries: India already dealing with rising food inflation and China with food shortages on account of Covid related lockdowns.

More worryingly, it is unclear whether the ban will have a lasting impact on domestic prices and with it inflation. The ban aims to address a more fundamental supply and demand issue for the domestic consumer, which may go unresolved. Anecdotal evidence suggests that there has been hoarding to palm oil supplies in a bid to take advantage of rising prices² and it is unclear if the ban will address this. Even so, there is a risk that lower domestic cooking oil prices may be subsumed by broader global food inflation pressures (which, ironically, the ban will have contributed to) hence, keeping domestic food prices sticky.

From a monetary policy perspective, Bank Indonesia will continue to be in wait-and-see mode. The immediate respite from higher cooking oil prices on food inflation will be welcome for BI and support its view on inflationary pressures being “manageable”. But this will not be without currency and macro stability risks: higher IDR volatility is likely to persist as abrupt protectionist policy decisions hurt credibility, even if the intention is to address domestic economy pitfalls.

² Conglomerate Salim caught up in Indonesia's cooking oil crisis, Nikkei Asia, 22 February 2022.

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