

MONETARY POLICY REPORT

JANUARY 2007

The Monetary Policy Report is published quarterly by Bank Indonesia after the Board of Governors' Meetings in April, July, October, and December. In addition to fulfilling the mandate of article 58 of Act Number 23 of 1999 concerning Bank Indonesia, amended by Act No. 3 of 2004, the report has two main purposes: (i) to function as a tangible product of a forward-looking working framework in which formulation of monetary policy is based on economic and inflation forecasts; and (ii) as a medium for the Board of Governors of Bank Indonesia to present to the public the various policy considerations underlying its monetary policy decisions.

The Board of Governors

Burhanuddin Abdullah	<i>Governor</i>
Miranda S. Goeltom	<i>Senior Deputy Governor</i>
Bun Bunan E.J. Hutapea	<i>Deputy Governor</i>
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Muliaman D. Hadad	<i>Deputy Governor</i>

New and Enhanced Monetary Policy Measures Under Inflation Targeting Framework

In July 2005, Bank Indonesia implemented a new and enhanced monetary policy measures within the Inflation Targeting Framework (ITF) which encompasses four main areas: the use of the BI rate as an operational target, enhanced decision making process, more transparent communications strategy, and strengthened policy coordination with the Government. The more is intended to strengthen the effectiveness and to provide good governance to its monetary policy making to achieve the price stability needed to support sustainable economic growth and attain social welfare.

Monetary Policy Strategy

Basic Principles

- With the ITF, inflation target is the overriding objective and nominal anchor of monetary policy. In this regard, Bank Indonesia will apply a forward-looking strategy to steer present monetary policy towards achievement of the medium-term inflation target.

Inflation

- Application of the ITF does not mean that monetary policy will not take account of economic growth. This policy will retain the fundamental paradigm of monetary policy in striking an optimal balance between inflation and economic growth in both the establishment of the inflation target and in monetary policy response, which will be targeted towards low, stable inflation in the medium and long-term.

The Inflation Target

- The Government, after consultation with Bank Indonesia, has established and announced targets for CPI inflation targets at $8\% \pm 1\%$, $6\% \pm 1\%$, and $5\% \pm 1\%$ for 2006, 2007, and 2008 (Based on press release on 17 March 2006 from the Office of Coordinator Ministry of Economics). These inflation targets are consistent with the process of gradual disinflation towards a medium to long-term inflation target of about 3%, competitive with other nations.

Instruments and Monetary Operations

- The BI Rate is used to convey the monetary policy stance and operational targets. The BI Rate is a one-month interest rate regularly announced by Bank Indonesia for a specific time frame.
- The BI Rate is implemented through open market operations (OMO) using 1-month SBIs. To strengthen the effectiveness of liquidity control on the market, Fine Tune Operations (FTO) will be carried out on a daily basis using SBIs and Government Securities as underlying instruments.

Policymaking Process

- The BI Rate is determined by the Board of Governors in the quarterly Board of Governors' Meeting held each January, April, July, and October. Under certain conditions, if necessary, the BI Rate may be adjusted in the Board of Governors' Meeting convened in other months. Changes in the BI Rate are indicative of Bank Indonesia's assessment of the inflation forecast in relation to the established inflation target.

Transparency

- From time to time, monetary policy will be communicated through customary media communications, such as statements to the press and market players, the website, and the publication of the Monetary Policy Report (MPR). This transparency is intended to strengthen understanding and build public expectations of the economic outlook and future inflation as well as the monetary policy response pursued by Bank Indonesia.

Coordination with the Government

- To provide coordination in inflation targeting, monitoring, and control, the Government and Bank Indonesia have set up a team made up of officials from various relevant agencies. In the course of its work, the Team deliberates and issues recommendations concerning the necessary policies for both the Government and Bank Indonesia in curbing inflationary pressure to achieve the established inflation target.

Foreword



The Governor of Bank Indonesia

Indonesia's economic gains in Q4/2006 alongside stable macroeconomic conditions give us much cause for thanks. It is no exaggeration to say now that Indonesia's economic machinery is on the right track. Economic growth in Q4/2006 is estimated the highest for any quarter in 2006. In other important areas, the balance of payments posted a surplus, the exchange rate maintained an appreciating trend and inflation recorded steady decline. These achievements were supported by a generally stable financial sector as demonstrated in the performance of the stock market, capital market and money market. All of this has combined to create a window of opportunity. If Indonesians from all walks of life are able to join forces, work shoulder-to-shoulder and devote even greater effort to the needed tasks, there is hope for realising the needed improvements in all areas of life.

The achievement of macroeconomic stability has paved the way for the economy to chart more broad-based growth. In Q3/2006, the economy visibly entered an expansion phase, despite lack of equilibrium due to the various impediments in the investment climate and the high costs of doing business. Investment growth was slower compared to the previous year, while exports and private consumer demand continued to provide the primary driving force for economic growth throughout 2006. In Q4/2006, we began to witness a rise in credit expansion followed by a fiscal stimulus from accelerated government expenditures, bringing estimated 2006 growth to 5.5% (y-o-y).

The balance of payments recorded a hefty surplus in Q4/2006, which bolstered the stability of the rupiah throughout the quarter. International reserves thus mounted to USD42.4 billion, equivalent to about 4.6 months of imports and official debt payments. At this level, reserves were well up from the previous year. With relative stability in the rupiah, inflation remained subdued and on a downward trend to the end of December 2006. Measured annually, CPI inflation at end-2006 reached 6.60% (y-o-y), down sharply from 17.11% (y-o-y) in 2005. Inflation thus came in below the prescribed target of 8.0% \pm 1%.

With macroeconomic aggregates well under control, Bank Indonesia saw that there was sufficient leeway to proceed with gradual reductions in the BI Rate. During the quarter, the BI Rate was lowered 3 times, representing a total rate cut of 150 bps to 9.75%. The sustained reductions in the interest rate were welcomed by business and met with positive response from market actors. Reflecting this were steadily rising share prices with the stock index closing at 1,805, decline in long-term bond yield and renewed


growth in consumer confidence. Despite this, the reductions in the BI Rate have only seen limited transmission to lending rates.

For the future, Bank Indonesia is optimistic that Indonesia will be able to achieve higher economic growth in 2007 alongside sustained macroeconomic stability. Growth in 2007 is predicted to reach 5.7%-6.3%, up from the 5.5% growth rate estimated for 2006. On 4 January 2007, the Bank Indonesia Board of Governors decided to lower the BI Rate by 25 bps to 9.50%. This decision took into account the objective information presented in the 2007 economic forecast, the various risks that lie ahead and the likelihood of achieving the future inflation targets of $6\% \pm 1\%$ and $5\% \pm 1\%$ for 2007 and 2008.

With Indonesia entering 2007, it is Bank Indonesia's view that co-ordination and co-operation with other agencies possessing the relevant powers, functions, expertise and policy instruments will do much to resolve the various problems confronting our economy. In the monetary sector, policy will remain focused on achievement of macroeconomic stability in support of sustainable economic growth. In the banking system, Bank Indonesia will keep working to strengthen the banking intermediary function to ensure effectiveness in availability of financing to meet business needs.

Jakarta, January 2007

The Governor of Bank Indonesia

A handwritten signature in black ink, appearing to read 'Burhanuddin Abdullah', written in a cursive style.

Burhanuddin Abdullah



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1. Overview

Overall, Indonesia's economic performance in Q4/2006 showed steady improvement accompanied by stable macroeconomic conditions. Economic growth during this quarter is estimated to be the highest recorded in 2006. Positive trends were also visible in a range of macro indicators, such as the balance of payments surplus, appreciating exchange rate and falling inflation. These achievements were supported by a generally stable financial sector as demonstrated in the performance of the stock market, capital market and money market. On 4 January 2007, the Bank Indonesia Board of Governors decided to lower the BI Rate by 25 bps to 9.5%. This decision took into account the economic and monetary outlook, the various risks that lie ahead and the likelihood of achieving the future inflation targets of $6\% \pm 1\%$ and $5\% \pm 1\%$ for 2007 and 2008.

In Q4/2006, economic growth reached an estimated 6.5% (y-o-y), ahead of the preceding three quarters. This brought economic growth for 2006 overall to about 5.5%. Key factors driving the growth were the sustained strong performance in exports and rising consumption. Also contributing to growth was a rise in investment, although only on a modest scale. Growth was recorded across almost all economic sectors. Nevertheless, the most important contributions to growth came from the trade, hotels and restaurants sector and the manufacturing sector.

Stronger export performance did much to bolster Indonesia's balance of payments surplus. In Q4/2006, Indonesia recorded a hefty balance of payments surplus, mainly due to the surplus in the current account. Key to the current account surplus was robust non-oil and gas export growth, with export performance buoyed by persistent strong world demand and high international commodity prices. At the same time, import growth was largely flat, due to continued weak domestic demand. The capital and financial account, however, recorded a deficit, partly from capital outflows with residents shifting more financial placements to offshore banks. At the same time, portfolio investment flows remained strong, reflected in increased foreign holdings of securities such as Bank Indonesia Certificates (SBIs) and stocks. With the sizeable current account surplus, international reserves climbed to USD42.4 billion, equivalent to about 4.6 months of imports and payments of official debt. At this level, reserves were well up from the previous year.

The improved balance of payments, steady yields on rupiah placements and improvement in risks all contributed to greater stability in the rupiah during the period under review. Point-to-point, the rupiah appreciated to Rp 8,995 in Q4/2006, up from Rp 9,225 in the preceding quarter. This appreciation was also accompanied by improved exchange rate stability, with volatility down at 0.46% compared to 0.85% one quarter earlier.

With relative stability in the rupiah, inflation remained subdued to the end of December 2006 while maintaining a declining trend. Measured annually, CPI inflation

at end-2006 reached 6.60% (y-o-y), down sharply from 17.11% (y-o-y) in 2005. Inflation thus came in below the prescribed target of 8.0% \pm 1%. Core inflation and administered prices inflation were also down. Annualised core inflation eased from the previous quarter to 6.03% (y-o-y), consistent with the subdued movement in fundamentals.

Having achieved macro stability and kept inflation within the inflation targeting range, Bank Indonesia launched a series of cuts in the BI Rate. During Q4/2006, the BI Rate was lowered 3 times, representing a total rate cut of 150 bps to 9.75%. The sustained reductions in the interest rate were welcomed by business and met with positive response from market actors. Reflecting this were steadily rising share prices with the stock index closing the year at 1,805, decline in long-term bond yield and renewed growth in consumer confidence. Despite this, the reductions in the BI Rate have only seen limited transmission to lending rates.

For the future, Bank Indonesia is optimistic that Indonesia will be able to achieve higher economic growth in 2007 alongside sustained macroeconomic stability. Growth in 2007 is predicted to reach 5.7%-6.3%, up from the 5.5% growth rate estimated for 2006. During the first half of 2007, economic growth will be driven mainly by consumption, while private investment is not expected to see significant expansion. Economic growth is predicted to gather momentum in the second half of the year, with significant expansion in private investment and hefty increases in government capital expenditures. In fiscal management, prompt and properly targeted government expenditures are expected to deliver an effective growth stimulus. On the external front, the robust expansion in exports is predicted to continue, despite a slowing trend as a result of less vigorous world economic growth compared to 2006. At the same time, imports of goods and services are expected to mount higher as domestic demand gathers momentum. These conditions are expected to influence the balance of payments in 2007, which is again predicted to record a surplus and thus support stability in the rupiah.

The renewed economic momentum is not expected to generate excessive upward pressure on overall prices. CPI inflation in 2007 is predicted to come within the government-set target range of 6 \pm 1%. Increased demand in line with rising economic growth will still be adequately offset by supply side improvements, thus alleviating pressure on core inflation. The CPI inflation forecast for 2007 is also supported by low pressure in administered prices components in the absence of government plans for increases in strategic administered prices. Added to this, inflationary pressure from volatile foods is also expected to remain low, with the government committed to ensure smooth distribution of foods and especially of staple goods.

Nevertheless, Bank Indonesia is also aware of various external and internal risks that could impact the economy in 2007. Externally, Bank Indonesia is constantly vigilant against the likelihood of slow global economic growth and changes in global investment preferences. Within Indonesia, structural issues such as delays in

implementing the investment climate, infrastructure and financial policy packages are risks that call for close monitoring, in addition to other issues such as the possibilities of disruptions to domestic distribution of goods and of a capital market bubble. If these risks can be addressed properly, economic growth in 2007 may climb beyond the forecasted level.

Having considered the objective information presented in the 2007 economic forecast, Bank Indonesia sees the need for intensified efforts and closer co-ordination from relevant agencies at the policymaking level and in policy implementation in the field. Likewise, the active role of all economic participants will be crucial to achieving higher levels of quality economic growth. In the monetary sector, policy will remain focused on achievement of macroeconomic stability in support of sustainable economic growth. In the banking system, Bank Indonesia will keep working to strengthen the banking intermediary function to ensure effectiveness in availability of financing to meet business needs.

2. Macroeconomic Performance

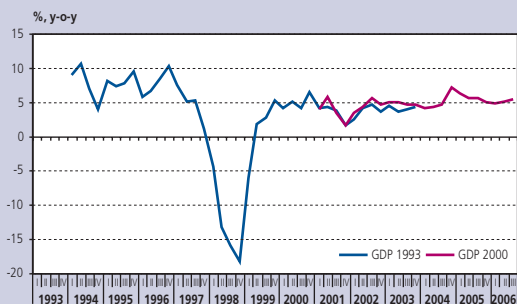
Overall, Indonesia's economic performance in Q4/2006 points to an improving trend. Economic growth mounted higher, outperforming the previous quarter while macroeconomic conditions remained stable. **In Q4/2006, the economy grew by an estimated 6.5% (y-o-y), bringing growth for 2006 overall to about 5.5% (y-o-y).** On the demand side, growth was spurred by rising consumption and sustained high levels of exports. Investment also began to show improvement. On the supply side, all sectors are estimated to have charted increased growth, with the most important contributions coming from the manufacturing and agriculture sectors. With exports and capital inflows running high, the balance of payments again posted a surplus. International reserves thus widened to USD42.4 billion, equivalent to about 4.6 months of imports and official debt payments.

ECONOMIC GROWTH

Estimates for Q4/2006 point to a rise in economic growth to 6.5% (y-o-y) (Graph 2.1). Economic activity, which showed some weakening in early 2006 as a result of falling public purchasing power in the wake of the October 2005 fuel price hike, has gradually regained momentum. Domestic demand in the twin areas of consumption and investment, which had climbed only slightly during Q3/2006, underwent robust expansion. Alongside this, estimates indicate that export growth remained strong.

Aggregate Demand

Estimated growth in household consumption in Q4/2006 reached 3.6% (y-o-y), up from the previous several quarters. This upswing is explained by stronger public purchasing power and the downward trend in inflation. Accordingly, growth in household consumption for 2006 is estimated at 3.1% (y-o-y).



Graph 2.1
GDP Growth

Various indicators and surveys also confirm the rise in household consumption during Q4/2006. In the real sector, sales of motorcycles, cars (Graph 2.2) and household electronics goods were all on the rise. In the monetary sector, the real money supply (real M1) and real consumption credit began to show signs of recovery. Mounting household consumption was reflected in the rising trend in the Consumer Confidence Index, even though the index remained at a pessimistic level. In November 2006, the Consumer Confidence Index reached its highest ever level since October 2005. Contributing to this was the upward trend in the Current Economic Conditions Index and the Consumer

% (y-o-y)

	2005	2006				2006*
		I	II	III	IV*	
Total Consumption	4.4	3.8	5.6	2.8	4.9	4.3
Private	3.9	2.9	3.0	3.0	3.6	3.1
Government	8.1	11.5	28.8	1.7	12.1	12.9
Total Investment	9.9	1.5	1.2	-0.3	9.5	3.0
Export of Goods and Services	8.6	11.2	11.6	12.1	8.3	10.8
Import of Goods and Services	12.4	3.9	8.4	9.7	9.9	8.0
GDP	5.6	4.8	5.1	5.5	6.5	5.5

* Projection figures

Expectations Index Six Months Forward. The Consumer Tendency Index organised by the Central Statistics Agency (BPS) and the Danareksa Consumer Survey (Graph 2.3) reinforce the estimates of rising household consumption. Reflecting this was the improvement in forecasted household incomes in the BPS survey and the upward trend in the Danareksa Consumer Confidence Index. The Bank Indonesia Retailer Survey (SPE-BI) also

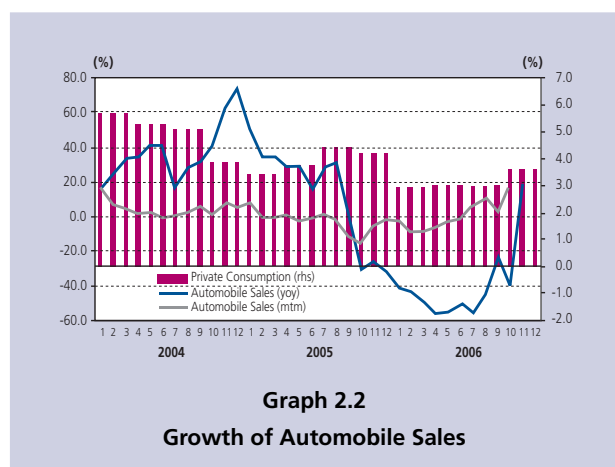
pointed to stronger public consumption, reflected in the improved growth trend in the real retail sales index.

Growth in investment (gross fixed capital formation) during Q4/2006 reached an estimated 9.5% (y-o-y). This figure is supported by investment prompt indicators, such as real investment credit and capital goods imports. Leading indicators for

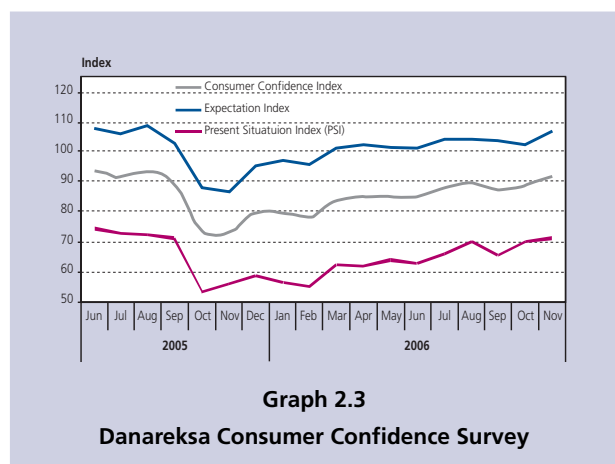
investment also point to an upward trend in investment growth during Q4/2006. Investment growth for 2006 overall is therefore estimated at 3.9% (y-o-y), lower than the growth recorded in 2005. The low rate of investment is explained by such factors as weakened public purchasing power, which has eroded the incentive for investment on the domestic market, as well as lack of a conducive investment climate.

The renewed investment growth in Q4/2006 is understood to be driven by construction and non-construction investment. Growth in construction investment is estimated to be on par with quarterly growth, recorded in the 6.0%-8.0% range. However, non-construction investment, which showed a declining growth trend early in the year, is believed to have gained fresh momentum. The rise in government investment is also explained by realisation of capital and procurement expenditures that took place largely in Q4/2006.

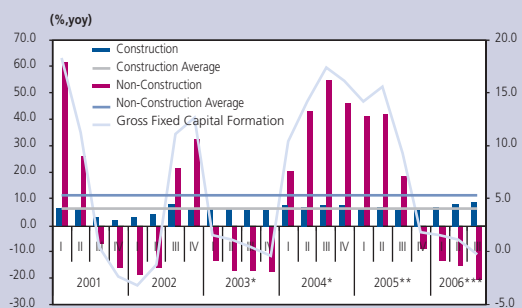
Exports of goods and services in Q4/2006 climbed by an estimated 8.3% (y-o-y), ahead of growth in the preceding year and outperforming the historical trend even though slightly less than in the previous quarter (Graph 2.8). Estimated export growth for 2006 thus reached 10.8% (y-o-y), the highest annual rate of export growth since 2001. Driving export growth was sustained heavy world demand for some of Indonesia's leading export commodities despite a dip at the beginning of the year, while rising export volume also played a role.



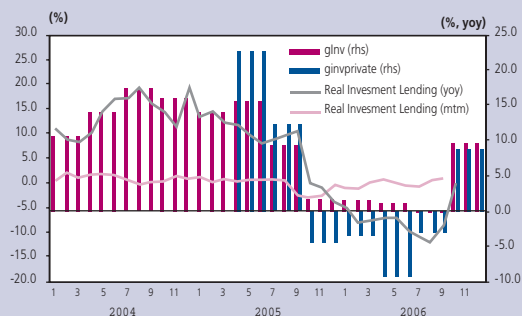
Graph 2.2
Growth of Automobile Sales



Graph 2.3
Danareksa Consumer Confidence Survey



Graph 2.4
Investment by Category
(Gross Fixed Capital Formation)



Graph 2.5
Growth in Real Investment Lending
and Gross Fixed Capital Formation

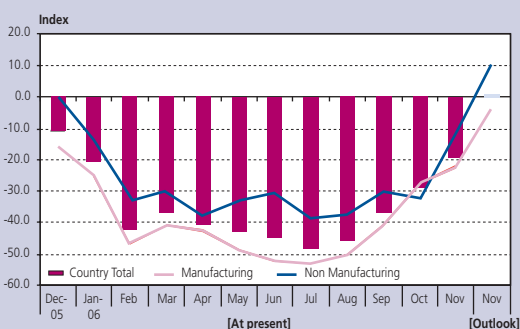
Export growth in 2006 is estimated to have surpassed the levels reached in previous years. Over the year, exports of goods and services forged ahead by more than 10%, with a rising trend in quarterly growth that peaked at 12.1% in Q3/2006. Disaggregated by components, export growth was strong for both goods and services, with the most important contribution coming from exports of goods. The principal factor driving exports was strong world demand since the beginning of the year for key Indonesian export products, which produced steady improvement in volume and value of Indonesian exports to the end of the year. Analysis by category of goods shows that export growth was especially high for mining products. Agricultural and manufactured exports also showed a rising trend, bolstered by strong performance in estate crops such as palm oil in keeping with the expansion under way in this industry.

Imports of goods and services climbed by an estimated 9.9% during Q4/2006. The key factor thought to have spurred import growth during the quarter was rising demand for capital goods and raw materials to support production. Import growth for consumer goods, on the other hand, remained low.

Import growth for 2006 overall is estimated at 8.0%, down from the previous year. This is explained by the low rate of import growth during the first half of 2006, a result of weak domestic demand. During the second half, however, import growth began to mount, especially for consumer goods and capital goods. Consumer imports were up on the strength of improved public

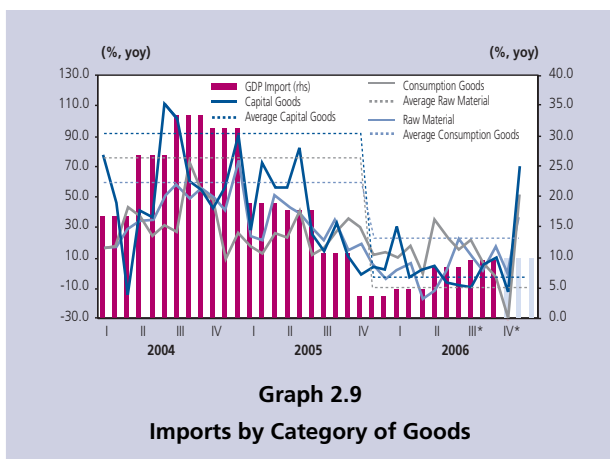
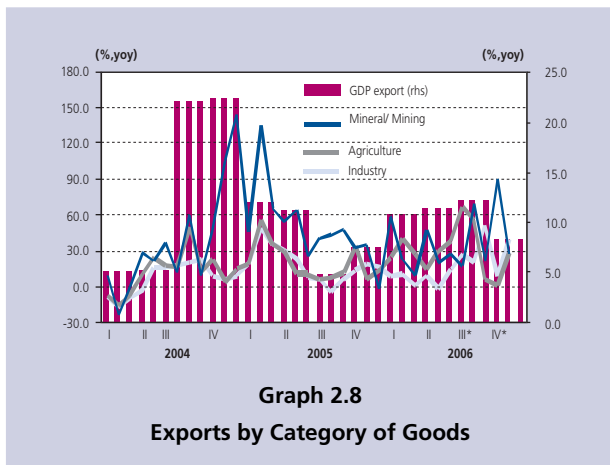
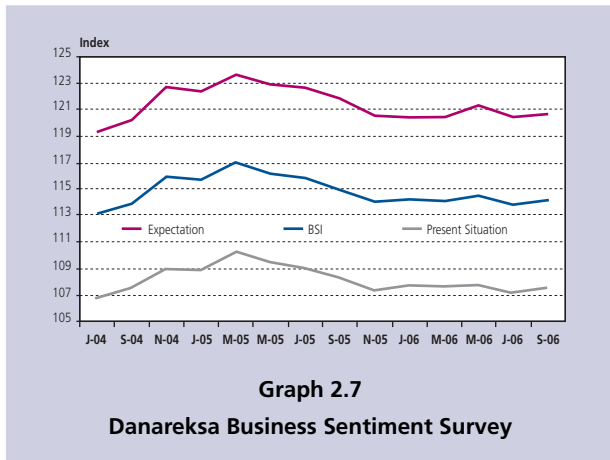
purchasing power, while the renewed surge in capital goods imports was buoyed by rising investment activity.

In Q4/2006, the government significantly boosted consumption and investment expenditures over the preceding quarter. Increased government consumption was recorded mainly in central government expenditures, with higher volume of realisation for Goods Procurement and Other Expenditures. The government similarly boosted investment mainly in central government investment, with brisk realisation of Capital Expenditures and Other Expenditures. Overall, fiscal policy in 2006 delivered a positive contribution to economic growth. Findings of a study on the fiscal impulse¹ indicate an expansive fiscal policy during 2006.



Graph 2.6
JETRO Survey

¹ The fiscal impulse is calculated by comparing the actual deficit value of government finances with the potential deficit (structural balance) that conceptually should be formed. If the actual deficit exceeds the potential deficit, the fiscal impulse can be described as having an expansionary impact on the economy. This fiscal deficit only takes account of domestic budget components and excludes external components, such as oil and natural gas revenues and servicing of foreign debt.



Even so, the fiscal expansion involved mainly consumption and transfer payments, bringing only limited multiplier effects.

Government contributions to the real sector through transfer payments also mounted higher in Q4/2006. The increase in transfers was related mainly to payments of remaining budget funds for various subsidies and Social Aid. In November, average subsidy payments still averaged only half of the budget allocations. Actual spending on the fuel subsidy stood at only 75% of the budgeted Rp 64.2 trillion. The electricity subsidy was at only 48% of the budgeted Rp 31.25 trillion and spending on other subsidies (foodstuffs, seeds, fertilisers, subsidised interest and Public Services Obligations (PSOs)) had reached only 51% of the Rp 12 trillion budget allocation. The underspending on the fuel subsidy is also thought to be related to the recent downward movement in world oil prices. At the same time, spending on Social Aid as of November had similarly reached only 74% of the allocation in the Revised State Budget. In 2005, Social Aid reached 80.9% of the budgeted level due to adjustments under new budget management procedures. In 2006, a higher rate of realised spending on Social Aid is expected in comparison to 2005.

Aggregate Supply

On the supply side, Q4/2006 GDP growth reached an estimated 6.47% (y-o-y), up from the growth recorded in the previous three quarters (Table 2.2). Growth was recorded across all economic sectors, with transport and communications in the lead. Measured by contribution, GDP formation was again dominated by tradable sectors, i.e. manufacturing (28.15%) and agriculture (12.22%).

Manufacturing recorded an estimated 5.5% growth (y-o-y) during Q4/2006. Factors driving manufacturing growth included rising domestic market demand in line with the onset of recovery in purchasing power, downward movement in interest rates and sustained heavy demand from foreign markets. Stronger manufacturing growth was confirmed by the JETRO Survey and Business Tendencies Index Survey by BPS. The JETRO survey of Japanese manufacturers operating in Indonesia indicates improvement in the business sentiment index during Q4/2006.

The BPS Business Tendencies survey also points to improvement in business conditions for manufacturing in Q4/2006 compared to earlier quarters. Survey findings were reinforced by real increases in orders for input goods and real increases in orders from domestic and international buyers.

		Table 2.1 Economic Growth - Supply Side				% (y-o-y)
	2005	2006				2006*
		I	II	III	IV*	
Agriculture	2.5	4.3	3.8	2.3	2.2	3.2
Mining and Quarrying	1.6	2.2	3.7	1.0	1.5	2.1
Manufacturing	4.6	3.3	3.7	5.3	5.5	4.5
Electricity, Gas, and Water Supply	6.5	5.8	5.2	6.5	7.1	6.1
Construction	7.3	7.1	8.1	8.4	7.9	7.9
Trade, Hotels and Restaurants	8.6	4.9	4.5	7.2	9.8	6.6
Transportation and Communication	13.0	11.5	13.2	13.5	15.1	13.4
Financial, Rental and Business Services	7.1	5.5	5.2	4.6	6.7	5.5
Services	5.2	6.0	6.4	7.0	7.1	6.6
GDP	5.6	4.8	5.1	5.5	6.5	5.5

* Projection figures

Growth in the trade, hotels and restaurants sector reached an estimated 9.8% (y-o-y) during Q4/2006. Higher turnover of freight was reported for all four major seaports (Belawan, Tanjung Priok, Tanjung Perak and Ujung Pandang) alongside a corresponding rise in the retail sales index in the BI Retail Sales Survey. The brisk growth in the trade sector in Q4/2006 is also explained by an upswing in domestic demand buoyed by improved purchasing power. Also important was

sustained world demand for Indonesian products, reflected in high export turnover.

The agricultural sector grew by an estimated 2.2% (y-o-y) in Q4/2006, down slightly from the previous quarter. Factors contributing to more modest growth in agriculture include declining production in key subsectors, among others food crops and estates, due to the effects of the prolonged dry season. Also confirming the downward growth trend was falling production for major food crops and a tapering off in export volume for estate commodities such as rubber and palm oil.

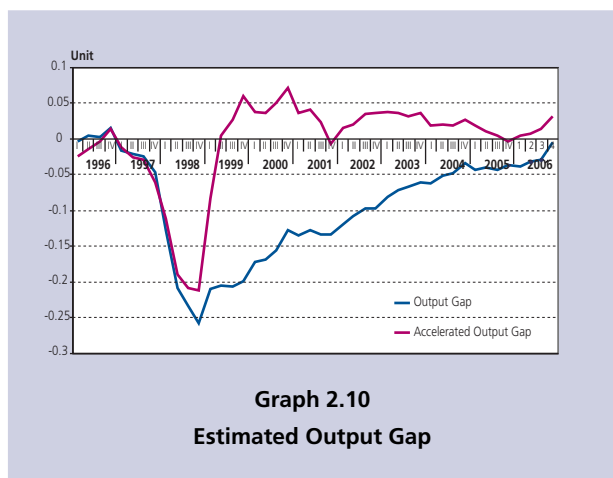
Estimated Q4/2006 growth in the mining and quarrying sector was 1.5% (y-o-y), up slightly from the previous quarter. Confirming the growth in this sector was brisk production of major mining and quarrying commodities, reflected among others in rising exports of coal and aluminium.

The transport and communications sector forged ahead by about 15.1% (y-o-y) in Q4/2006, up from the previous quarter. The more robust growth in transport and communications during Q4/2006 was also confirmed by indicators such as increasing numbers of train and airline passengers and the continued rapid expansion in cellular telephone users that has led to high rates of telephone usage.

Growth in the construction sector during Q4/2006 reached an estimated 7.94% (y-o-y). This was reflected in such indicators as rapid expansion in commercial properties, including shopping centres, apartments and condominiums. During the full year of 2006, construction moved ahead at a slightly faster rate (7.88%) compared to 2005 (7.34%). Factors spurring growth in construction included optimism among developers of the outlook for commercial property, the onset of renewed growth in public purchasing power and downward movement in interest rates.

Output Gap

Because of the continued slack pace of investment activity in 2006, there was no meaningful increase in economic capacity. At the same time, **demand continued to rise, producing a further narrowing in the output gap,** i.e. the difference between



potential and actual GDP. This was worsened by the persistent lack of efficiency in the national economy, as reflected in the relative absence of change in the Incremental Capital Output Ratio (ICOR) compared to 2005. The narrowing of the output gap calls for careful monitoring. If not offset by increased investment activity, the output gap could put pressure on macroeconomic stability, mainly through inflation.

BALANCE OF PAYMENTS

In Q4/2006, the balance of payments again recorded a surplus.

The increased surplus came mainly from the current account, bolstered by robust export performance that contrasted with relatively flat import growth. Also contributing to the current account surplus was a rise in overseas worker remittances. On the other hand, the capital and financial account recorded a slight deficit due to slowed disbursements of bank credit lines and increased placements of resident-held assets in offshore banks. Nevertheless, sustained high capital inflows, particularly for portfolio investment, kept the deficit at a manageable level. Taken together, the balance of payments generated an added contribution to international reserves, which reached an estimated USD42.4 billion at end-2006.

The Current Account

In Q4/2006, the current account again recorded an estimated surplus. Key to this surplus was rising export growth amid relatively unchanged growth in imports. Export growth was boosted by stronger performance in non-oil and gas exports, buoyed by continued high prices for non-oil and gas commodities. During Q4/2006, non-oil and gas export growth reached an estimated 15.4% (y-o-y). At the same time, little change was observed in import growth and especially growth of non-oil and gas imports, due to persistently low domestic demand. Estimated growth in non-oil and gas imports came to 8.3% (y-o-y). During this period, there was also a sharp rise in current transfers from increased overseas worker remittances.

The Capital and Financial Account

Capital and financial flows in Q4/2006 were still characterised by high inflows of foreign capital, particularly for portfolio investment. The brisk rate of portfolio investment flows was supported by relatively high yields offered in Indonesia compared to the region. Other factors also bolstering capital inflows were expectations of future improvement in the economy, reflected in the stable exchange rate, and the increasingly liquid secondary market for SBIs. In addition to portfolio investment, foreign direct investment (FDI) transactions in Q4/2006 also recorded an estimated surplus in keeping with the more carefully nurtured macroeconomic

stability. The other investment account, however, recorded an estimated deficit. This deficit is explained largely by increased offshore asset placements by residents, with much of these funds held savings deposits and call money. In addition, residents also held overseas asset placements in trade credit, a development consistent with the ongoing rise in exports.

International Reserves

In response to these various developments, the balance of payments in Q4/2006 recorded an estimated surplus. The balance of payments surplus thus boosted international reserves to USD42.4 billion at end-2006, equivalent to about 4.6 months of imports and official debt payments. International reserves were therefore up 22.1% from the end-2005 position recorded at USD34.7 billion. The more robust international reserves will also make a positive contribution to future macroeconomic stability.

MACROECONOMIC POLICY

During Q4/2006, the government introduced few significant policy changes in comparison to policies issued in previous quarters. Concerning improvements to the investment climate, only 35 of the planned 49 action items were completed as of November 2006. These items covered the following areas: general reforms (14 items), taxation (4 items), customs (7 items), labour (6 items) and MSMEs (4 items). In the area of infrastructure policy, as of October 2006 the government had completed 55 out of a total of 120 action items.

Progress was slow in the area of structural policies and actions, especially for improvement of the investment climate and infrastructure. The principal reasons for slow progress on action on the investment climate include poor co-ordination and the legislative process at Parliament that has delayed the completion of legislative products crucial to progress on other action items, such as the Investment Law and Taxation Law. Work is also stalled on the Labour Law. Concerning infrastructure, progress has been held up by lack of co-ordination and uncertainties over risk sharing and returns on projects to be financed.

With only limited progress in completion of action items, the reforms so far have had little impact on structural policies. Some members of the business community believe that the policy packages have still had only minimal impact. Problems cited by business include: public inadequately informed of the actions taken by the government; policies not fully implemented by officials in the field, giving rise to impressions of inconsistency; rampant practices that drive up costs for business, especially at ports; and the excessively slow pace of government actions. On its part, the government recognises that one of the difficulties responsible for slow action in completion of action items and application of policies for improvement of the investment climate is problems

with co-ordination. At the regional level – according to survey findings and sampling of a number of regency level administrations – the investment climate in any particular region is determined to a great extent by the head of the regional government. Areas in which local government leaders have a pro-business vision tend to have a better investment climate and succeed in attracting more investors.

On a sectoral level, the policies pursued by the government have sought mainly to remove hurdles to boosting efficiency and productivity. **In the industry and trade sector**, new policies/incentives issued by the government include process of VAT refunds within 1 month; tariff harmonisation to reduce trading scheme distortions; removal of multipurpose electricity billing rates; the Customs Law; delegation of power from the Minister of Law and Human Rights to Regional Offices for Law and Human Rights for validation of the incorporation of limited liability companies; amendments to 8 laws and regulations concerning trade licensing; various regulations to expedite the movement of goods (Director General of Customs and Excise and the Minister of Finance); 30 minute target release time in the green lane, and 3 day release time for the red lane; reduction in use of red lane to 10% by end-2006; use of priority lane to be expanded to 130 importers by end-2006. In addition to these policies, the government also issued specific policies for certain industries, such as Regulation of the Minister of Finance No. 79/PMK.010/2006 concerning Import Duty Exemption for Automotive Parts and Components Used in Production of Exported Vehicles.

Progress in policy reforms for agriculture has also been limited. The (macro) policy for revitalisation of agriculture, fisheries and forestry, launched in July 2005, has been beset by delays. Some observers claim that these delays can be partly attributed to the excessively broad goal of the policy, which is to raise living standards and competitiveness through revitalisation of agriculture. During 2006, the government took other measures including a 10%-15% rise in official retail prices for subsidised fertilisers (May 2006).

In the mining sector, policies launched thus far have failed to stimulate investment. Mining sector policies issued by the government have so far been only piecemeal. One example is Regulation of the Minister of Finance No. 97/PMK.010/2006 concerning import duty exemptions for equipment used in upstream oil and gas production. Overall, there have been only limited policy reforms in the mining sector, offering little incentive for investors. Investment in mining has also been held up by conflicting provisions in other ministerial regulations, such as Regulation of the Minister of Forestry No. P.14/Menhut-II/2006 concerning lease and use of forest areas, regulations on regional autonomy and the delays in promulgation of the Law on Mining of Minerals and Coal.

In the area of labour reforms, no structural changes took place during 2006. The planned passage of the new Draft Labour Law designed to replace Act No. 13 of 2003 has met with fierce opposition from trade unions and workers, and it is

impossible to predict when the law will reach completion. In 2006, work was completed on the following action items on labour issues:

(1) On the domestic front, new policies were issued on skills development for the unemployed in the regions through revitalisation of Vocational Training Centres (BLK); launching of a nationwide movement on combating unemployment at the village, subdistrict and regency level; and operation of job centres in each province.

(2) Regarding overseas workers, new policies were issued on reform of the systems for recruitment and protection of overseas workers, including reduction in bureaucratic processing for overseas workers from 40 desks to 11 desks; improved treatment of overseas workers through provision of special departure and arrival areas; decentralisation of licensing and services for overseas workers to the regions, especially through the development of one-roof services; reductions in the costs borne by overseas workers by elimination of charges on worker ID cards, removal of the exit tax requirement and 60% reduction in cost structures; registration of overseas worker recruitment companies and revocation of licences for 104 companies; signature of MoUs with destination countries; campaign for the right of children of overseas workers in Malaysia to attend school; and unloading of 80 thousand tons of overseas worker belongings held up at Cengkareng since 2001.

Besides policies issued by the government, new policies issued by trading partners during 2006 offer opportunities for boosting exports of some Indonesian products.

These policies include incentives offered by the European Union, which has revoked Anti Dumping Charges on Indonesian polyester staple fibre. In addition, China has removed its import tariff on Indonesian cocoa, formerly set at 10%-25%.

3. Monetary Indicators and Policy QIV-2006

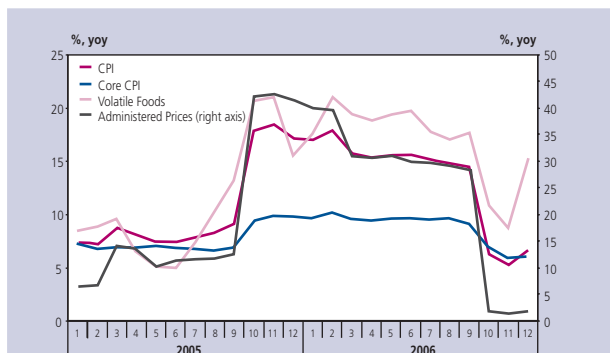
During Q4/2006, monetary conditions maintained an improving trend. Reflecting this was falling inflation, an appreciating trend in the rupiah accompanied by reduced volatility and adequate liquidity to support economic activities. The improvement in monetary conditions alongside optimism over the economic outlook and rising confidence in future inflation control offered room for further reductions in the BI Rate. During Q4/2006, the BI Rate was lowered three times in a total rate cut of 150 bps to 9.75% at end-2006, bringing the overall reduction in the BI Rate from the beginning to the end of 2006 to 300 bps. The rate cuts began in May 2006 in a move that also signified a change in the monetary policy stance from tight biased to cautious easing.

The sustained reductions in the interest rate were welcomed by business and met with positive response from market actors. Reflecting this were steadily rising share prices with the stock index closing at 1,805, decline in long-term bond yield and renewed growth in consumer confidence. In the banking sector, the Indonesian banking system showed overall improvement in the operation of the intermediary function. As of November 2006, credit expansion reached Rp 78.2 billion (10.7%), bringing total bank lending to Rp 806.3 trillion. Funding this credit expansion was a Rp 123 trillion (10.9%) rise in depositor funds to a cumulative Rp 1,251 trillion.

INFLATION

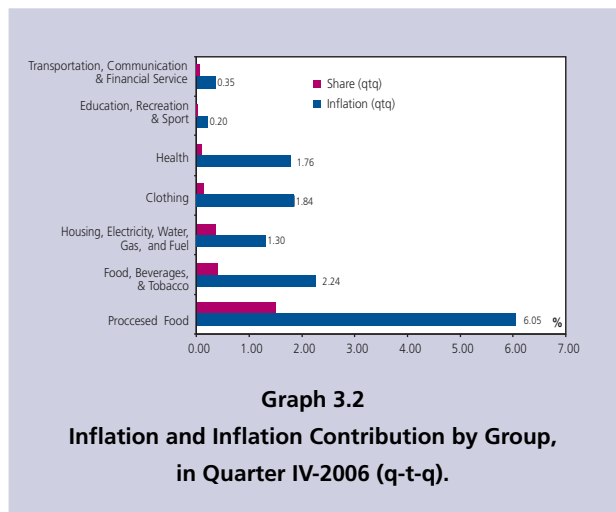
CPI inflation maintained a downward trend during Q4/2006. The reduction in CPI inflation was largely attributable to the minimum impact from administered prices and control of inflationary pressure from fundamentals. Inflation in administered prices was minimal due to the absence of government decisions to raise prices for strategic commodities. In regard to fundamentals, the appreciation in the rupiah

and management of inflation expectations contributed to lower core inflation. CPI inflation in Q4/2006 thus came to 6.60% (y-o-y), down from 14.55% (y-o-y) in Q3/2006 (Graph 3.1). The overall 6.60% (y-o-y) CPI inflation for 2006 represents a sharp decline from 17.11% (y-o-y) in 2005. This drop resulted from a combination of fundamentals and non-fundamental factors. In regard to fundamentals, the appreciation in the rupiah, controlled expectations of inflation and lack of full recovery in domestic demand all contributed to lower core inflation. From the non-fundamentals side, the postponement of the rise in electricity billing rates in 2006 and the absences of hikes in other strategic administered prices produced a major reduction in administered prices inflation.



Graph 3.1

CPI, Administered, Core, and Volatile Foods Inflation



Only modest inflationary pressure from administered prices was observed during Q4/2006.

The low inflation in administered prices was linked to the minimum increases in strategic administered prices and the passing of the impact from the fuel price hike on 1 October 2005. During the quarter under review, inflationary pressure in administered prices came from hikes in retail kerosene prices linked to shortages caused by distribution bottlenecks in some regions, as well as escalating prices for clove filter cigarettes. At the same time, administered prices were also affected by lower prices for non-subsidised fuels in Q4/2006 due to the effect of the mixing of non-subsidised fuels in petrol and the resultant inclusion of these lower prices in administered prices inflation. Accordingly, administered prices inflation at end-Q4/2006 reached 0.57% (q-t-q), down from 26.99% (q-t-q) in Q4/2005 but up slightly from the 0.22% (q-t-q) recorded in the preceding quarter.

Overall, administered prices inflation fell sharply during 2006 to 1.84% (y-o-y) from 41.71% (y-o-y) in 2005.

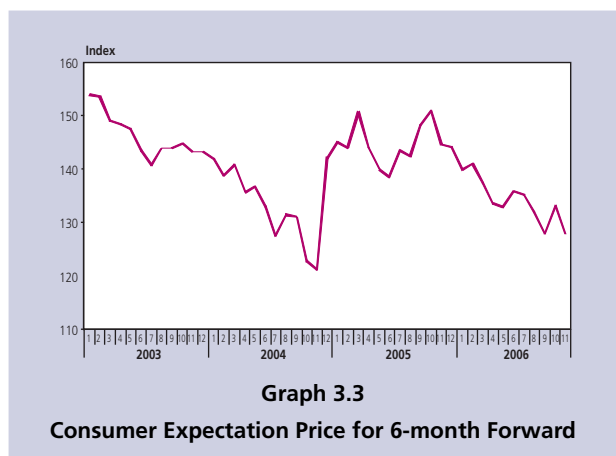
Volatile foods inflation eased to 15.57% (y-o-y) in the quarter under review, down from 17.57% (y-o-y) in the preceding quarter.

Measured quarterly, volatile foods inflation was recorded at 7.00% (q-t-q), up from 1.31% (q-t-q) in Q3/2006. The higher quarterly inflation is explained not only by seasonal trends in volatile foods, but also by a significant rise in rice prices. Prices for rice mounted in part because of limited market supply associated with the delay in the planting season. Also contributing to higher rice prices was increased demand due to the discontinuing of rice aid for the poor in October 2006 and the celebration of the religious festivities and the new year. Another factor thought to have driven up rice prices was speculation by traders in anticipation of the prolonged dry season and the increase in the government rice procurement price planned for early 2007. Throughout 2006, the government took action on various fronts to ensure adequate market supply and free-flowing distribution of volatile foods commodities to mitigate

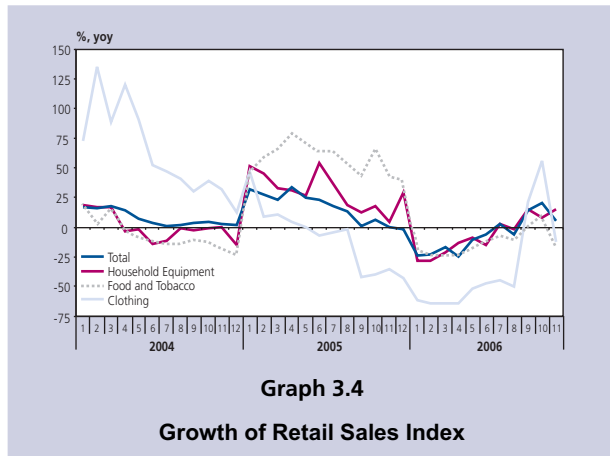
upward pressure on prices from the fuel price hike on 1 October 2005. These efforts proved largely successful in stabilising volatile food prices, but failed to have an impact during the peak of the dry season. This was reflected in the dramatic surge in volatile foods inflation at the beginning and end of 2006.

Core inflation reached 6.03% (y-o-y) in Q4/2006, down from the previous quarter's level of 9.12% (y-o-y).

Even so, the quarterly measure of CPI inflation in Q4/2006 came to 1.76% (q-t-q), up slightly from 1.50% (q-t-q) in Q3/2006. Core inflationary pressure in Q4/2006 was generated mainly by rising public expectations of inflation (Graph 3.3). In contrast, external factors and the output gap produced little upward pressure on core inflation. Externally, a modest rise in international commodity



Graph 3.3
Consumer Expectation Price for 6-month Forward



Graph 3.4

Growth of Retail Sales Index

prices – mainly gold and sugar – during the quarter under review did not produce inflationary pressure because of the appreciating trend in the rupiah. At the same time, pressure from the output gap was again minimal because of lack of recovery in public purchasing power that kept a lid on aggregate demand amid adequate levels of supply.

Bank Indonesia’s efforts in 2006 to maintain overall macroeconomic stability proved effective in curbing core inflationary pressure, particularly that generated by fundamentals.

The appreciation in the rupiah and subdued expectations of inflation contributed to lower core inflation. Furthermore, the lack of recovery in aggregate demand due to persistently weak purchasing power kept inflationary pressure from the output gap

to a minimum. On the other hand, a general improvement in the supply and distribution of goods and services also minimised inflationary pressure from the output gap. These developments in fundamentals brought core inflation for 2006 down to 6.03% (y-o-y), down from 9.75% (y-o-y) in 2005.

RUPIAH EXCHANGE RATE

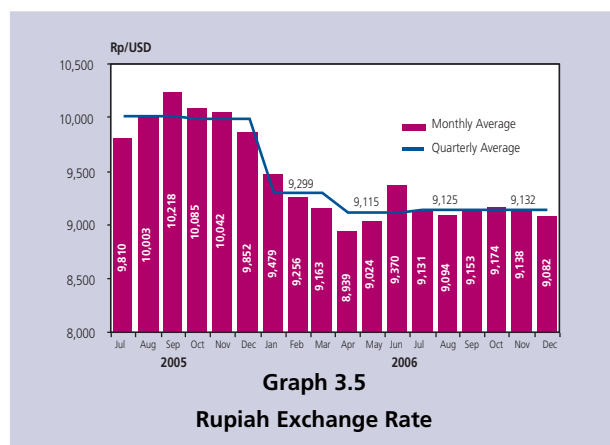
In Q4/2006 the rupiah demonstrated more stable movement compared to the preceding quarter, accompanied by an appreciating trend.

Improved stability in the rupiah was also reflected in a reduction in volatility from 0.85% to 0.46% (Graph 3.6). Point-to-point, the rupiah strengthened from Rp 9,225/USD at end-Q3/2006 to Rp 8,995 at end-Q4/2006. Measured as an average for the quarter, the rupiah weakened slightly to Rp 9,132/USD from the previous quarter’s level of Rp 9,125/USD (Graph 3.5). Rupiah stability was bolstered by improved domestic macroeconomic conditions and reduced external pressures. Improvement was recorded in several macroeconomic indicators during Q4/2006, especially in inflation. Furthermore, the rupiah maintained its attractiveness for investors due to the

improvement in risk indicators amid the downward trend in rupiah investment yields. Externally, the US Federal Reserve kept its rate on hold and the downward trend in oil prices eased pressure on the rupiah. At the same time, Thailand’s move to impose tighter restrictions on capital inflows had little effect on the rupiah.

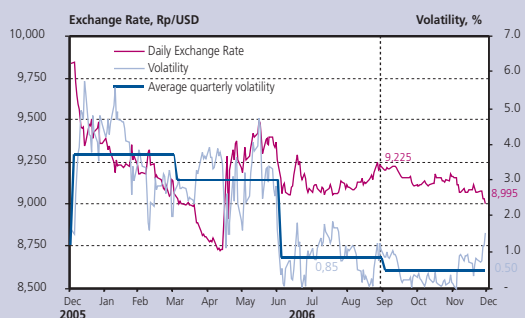
Rupiah stability in Q4/2006 was supported by the improving condition of economic fundamentals.

Improvement was recorded across a range of economic indicators - such as exports, GDP growth and the inflation rate. Buoyed by the continued rise in global demand and export commodity prices, exports kept climbing during the January-October 2006 period, with non-oil and gas export growth reaching 19.4%. During the same period,

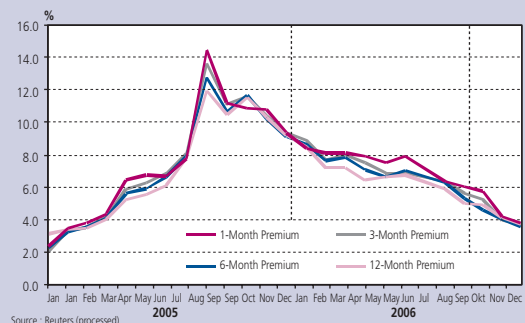


Graph 3.5

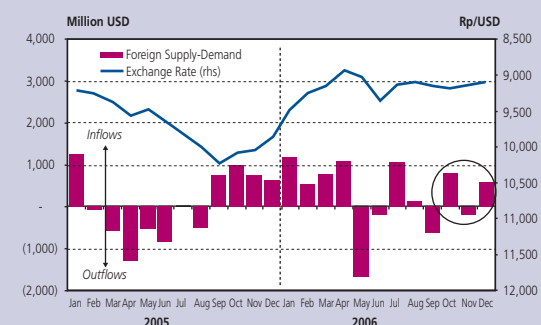
Rupiah Exchange Rate



Graph 3.6
Exchange Rate Volatility



Graph 3.7
Swap Premium for Various Tenors



Graph 3.8
Forex Supply and Demand based on Spot Transactions

growth of non-oil and gas imports reached only 0.5%, leaving a considerable surplus in the current account. The steady rise in export commodity prices that outpaced growth in import prices also strengthened Indonesia's terms of trade. The combined effect of these developments resulted in a heftier balance of payments surplus, which provided key fundamental support for the rupiah.

Concerning risks, improvement was observed in domestic risks during Q4/2006, reflected in the narrowing of the yield spread and swap premium. The yield spread between government foreign currency bonds and US T-Notes eased from 1.8% to about 1.3%. Similarly, the swap premium steadily declined across all tenors (Graph 3.7). The improvement in these risk indicators reinforced stability in the rupiah at a time of downward movement in the BI Rate, helping to keep rupiah yields at levels sufficient to attract foreign capital inflows.

Alongside this, external developments during Q4/2006 had minimal downward impact on the rupiah. The decision by the Fed to keep its rate on hold at 5.25% and falling oil prices both eased downward pressure on the rupiah. However, in another external development, the imposition of restrictions on capital inflows by the Bank of Thailand (unremunerated reserve requirement or URR) also had little impact on the rupiah exchange rate. The rupiah came under pressure only on the day of the announcement of the restriction on 18 December 2006, and quickly resumed its appreciating trend. This owes much to an immediate official announcement by BI, stating that Indonesia

would not be following Thailand's example. BI's statement, alongside similar statements in Malaysia and the Philippines, succeeded in calming the jitters of global investors, who had reacted by pulling funds out of the region.

Overall, the rupiah performed better throughout 2006 compared to 2005, maintaining a strengthening trend against the USD accompanied by more stable movement. During 2006, the rupiah gained 8.4% point-to-point, rising from Rp 9,831/USD at end-2005 to Rp 8,995 at end-2006. Measured as an average, the rupiah also strengthened from Rp 9,713 in 2005 to Rp 9,116/USD in 2006. Not only did the rupiah gain value, but it also maintained more stable movement compared to the previous year. This was reflected in reduced volatility, down from 4.04% in 2005 to 3.79% in 2006.

Inflows of foreign investment capital in Q4/2006 brought added supply to the interbank forex market (Graph 3.8). On the other hand, excess domestic demand for foreign currencies was also

up slightly from the previous quarter. The rising excess domestic demand for foreign currencies came largely from more robust forex demand in the corporate sector. As a result, the domestic forex market continued to sustain an overall condition of excess demand. Nevertheless, measured cumulatively, excess demand was down considerably from the previous quarter. Throughout 2006, the forex market was marked by excess foreign currency demand, but at far lower levels than in 2005. This is an indication of reduced pressure on the rupiah, which allowed the rupiah to appreciate against the US dollar.

MONETARY POLICY

Strategy

Following an overall assessment of the economy that took into consideration various risks to future economic performance, the Board of Governors' Meetings at Bank Indonesia decided on further reductions in the BI Rate. In Q4/2006, the Board of Governors' Meetings convened on 5 October 2006, 7 November 2006 and 7 December 2006 lowered the BI Rate by 50 bps in each meeting to the year-end level of 9.75%. Thus by the end of 2006, the BI Rate had come down 300 bps from the beginning of the year. The rate cuts began in May 2006 in a move that also signified a change in the monetary policy stance from tight biased to cautious easing. This policy stance was taken to guide public expectations of inflation towards the CPI inflation target, set at $8 \pm 1\%$ and $6 \pm 1\%$ (y-o-y) for 2006 and 2007. On the operational level, the rate cuts were supported by new regulations on the fixed rate tender for the 1-month SBI auction, longer intervals between the 3-month SBI auctions, and discretion (closure) in provision of the 7-day FASBI window. Overall, monetary policy operations in 2006 met with positive response from market actors and were welcomed by business. This was reflected in such developments as soaring share prices, which broke a new record, as well as the downward trend in bond yield.

Concerning the exchange rate, Bank Indonesia steadily pursued a series of measures to bolster the stability of the rupiah. These measures were carried out partly with the use of interest rate instruments and through needed improvements to existing monetary instruments. Bank Indonesia also took active steps to maintain an adequate level of international reserves for use as a buffer in case of sudden capital reversal, especially following the US\$3.8 billion early repayment of IMF debt on June 30, 2006. Bank Indonesia also monitored the operation of various regulations relevant to the exchange rate, primarily to curb downward pressure on the rupiah from short-term capital flows (mainly buying swaps) and/or non-underlying transactions. The regulatory basis for this action is set out in Bank Indonesia Regulation 7/14/2005 concerning Restrictions on Rupiah Transactions and Foreign Currency Lending by Banks, issued on 14 June 2005.

Policy was also co-ordinated with the government to safeguard macroeconomic stability. Bank Indonesia has worked tirelessly on building synergy with the

government to maximise the benefits of the fiscal stimulus and for improvement in the investment climate, which is key to promoting economic growth. This synergy involves practical steps to achieve these objectives, including accelerated government capital expenditures, accelerated disbursement of budget funds, mainly for regional governments, and more rapid progress in improvements to the investment climate and infrastructure.

Interest Rates

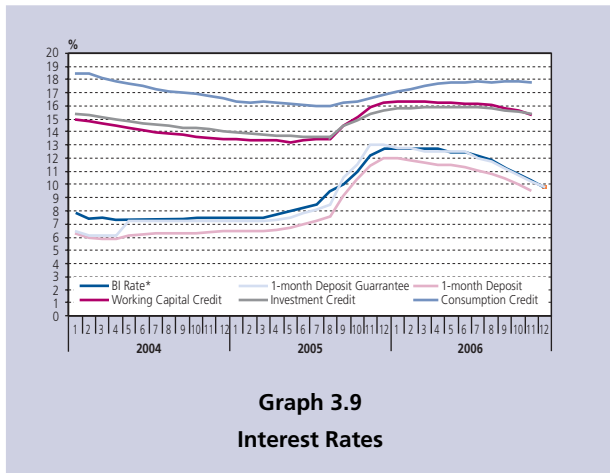
The cuts in the BI Rate were followed by across the board reductions in monetary instrument rates. The overnight FASBI rate eased to 4.75% and the SBI Repo rate to 12.75%. On an operational level, the lowering in the BI Rate was immediately reflected in the 1-month SBI auction, consistent with the nature of the Fixed Rate Tender (FRT) auction system. Under this new system, the aim of monetary operations is to ensure that the general monetary policy direction transmitted through the BI Rate is consistently aligned to current conditions on the interbank money market in regard to both levels and interest rates formed.

The reductions in the BI Rate have been followed by downward movement in deposit guarantee rates and bank deposit rates. During Q4/2006, the 1-month deposit guarantee rate eased 150 bps from 11.25% at end-Q3/2006 to 9.75% (Table 3.1). One-month deposit counter rates followed suit, dropping to 8.6% from 9.8% at the end of the previous quarter. The weighted average 1-month rupiah deposit rate in November 2006 came to 9.5%, similarly down from the end-Q3/2006 level of 10.5%. This movement in deposit rates represents a continuation of the downward trend in time deposit rates since February 2006 (Graph 3.9).

Loan interest rates also eased, as indicated by the fall in the base lending rate. At the end of Q4/2006, the base lending rate stood at 15.0%, down from 15.5% at the end of the previous quarter (Table 3.1). This was followed by across-the-board

Interest Rate	Quarter I-2006			Quarter II-2006			Quarter III-2006			Quarter IV-2006		
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
BI Rate	12.75	12.75	12.75	12.75	12.50	12.50	12.25	11.75	11.25	10.75	10.25	9.75
1-month Dep. Guarantee	12.75	12.75	12.50	12.50	13.00	12.50	12.00	11.75	11.25	10.75	10.25	9.75
1-month Dep. (Weight Avg)	12.0	11.9	11.6	11.5	11.5	11.3	11.1	10.8	10.5	10.0	9.5	
1-month Dep. (Counter Rate)	10.4	10.5	10.4	10.5	10.3	10.4	10.2	10.0	9.8	9.3	9.0	8.6
Base Lending Rate	16.1	16.1	16.0	16.0	16.0	15.8	15.8	15.7	15.5	15.1	15.1	15.0
Working Capital Credit	16.3	16.3	16.4	16.3	16.3	16.2	16.1	16.1	15.8	15.6	15.4	
Investment Credit	15.8	15.9	15.9	15.9	15.9	15.9	15.9	15.9	15.7	15.5	15.4	
Consumption Credit	17.1	17.3	17.5	17.7	17.8	17.8	17.9	17.8	17.9	17.9	17.8	

reductions in lending rates to the end of November 2006. Rates for working capital credit, investment credit and consumption credit fell to 15.4%, 15.4% and 17.8% from the Q3/2006 levels of 15.8%, 15.7% and 17.9%.



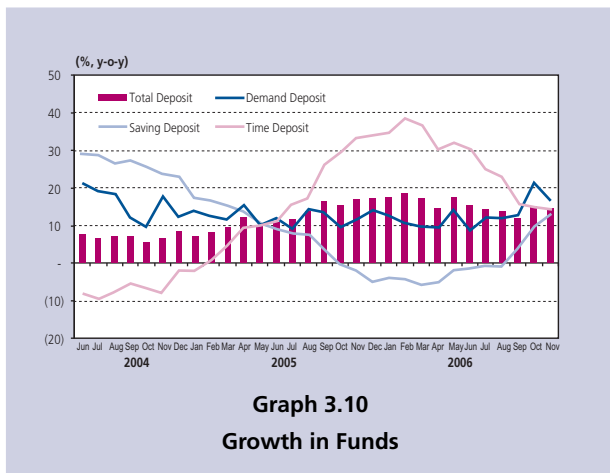
Graph 3.9
Interest Rates

Funds, Credit and the Money Supply

The reductions in the BI Rate were followed by more vigorous funds mobilisation. Despite the easing in time deposit and deposit guarantee rates, depositor funds held at banks continued to rise. At end-November 2006, depositor funds were up 14.7% (y-o-y), bringing the cumulative total to Rp 1,251 trillion. The continued rise in depositor funds reflects strong public confidence in the domestic banking system, even at a time of downward movement in interest rates.

In regard to lending, the lowering of the BI Rate was followed by improvement in the bank intermediary function. Credit expansion mounted higher. As of November 2006, lending was up Rp 78.2 trillion, bringing total bank credit to Rp 806.3 trillion. Funding this credit expansion was a Rp 123 trillion rise in depositor funds, which mounted to a cumulative Rp 1,251 trillion. The higher rate of loan disbursements reflects bank performance in the operation of the intermediary function, which is expected to provide financing for the economy and the real sector.

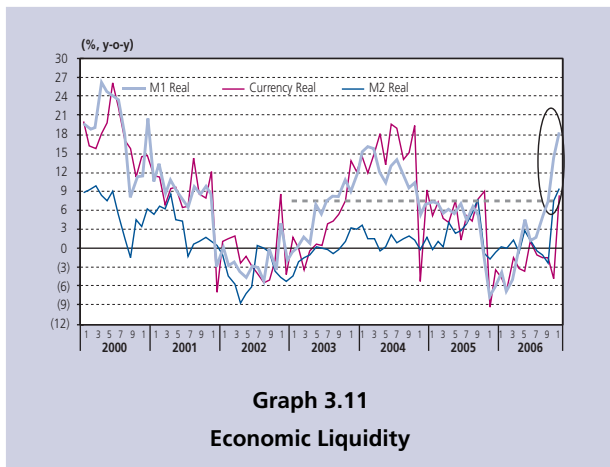
In the area of the money supply, M1 and M2 continued to rise with more robust growth at end-November 2006 compared to earlier periods. Measured in nominal, annual growth in M1 and M2 reached 23.8% and 14.6%, up from 20.8% and 13.7% in the preceding month. Similarly, real M1 recorded accelerated growth, far surpassing the average over the past two years (Graph 3.11). Since October, real M2 has also resumed positive growth. Analysis of M2 components also shows that the increased M2 growth was supported by faster growth in savings deposits.



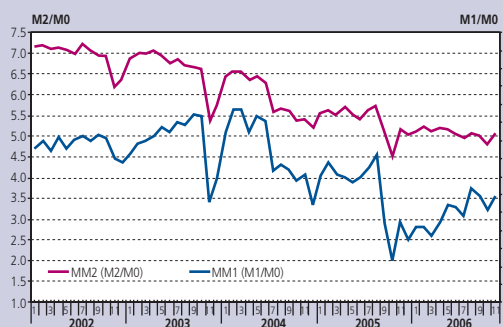
Graph 3.10
Growth in Funds

Financial Markets

The 300 bps reduction in the BI Rate during 2006 spurred even more vigorous trading on the capital market. Added to this, the steady improvement in various macroeconomic indicators and recovery in foreign investor confidence in Indonesia's economic stability also met with positive response from market players on the Jakarta Stock Exchange (JSX). Share trading continued to mount, pushing the Jakarta Composite Index upwards to close at 1,806 at end-2006, or 55.3% higher than the end of 2005. The index gains earned the JSX the distinction of one of the best performing exchanges in 2006. As the year progressed in 2006, the improvement in economic fundamentals and the micro position of stock issuers combined with strong prospects became a robust driving force for the JSX, taking the index to new highs.



Graph 3.11
Economic Liquidity



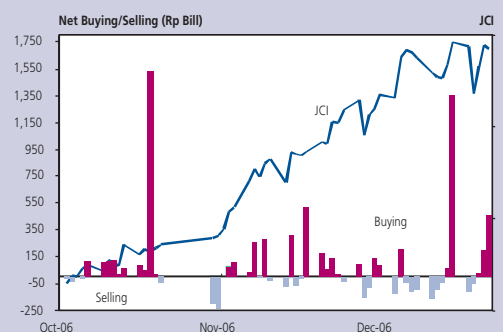
Graph 3.12
Development of Money Multiplier

Domestically, the subdued inflation that remained on a downward trend to come below the projected range, higher GDP growth and robust international reserves were interpreted by investors as signs that economic recovery was on track. The stable rupiah, which has maintained an appreciating trend, also contributed to positive sentiment over investment yields on the stock market. Externally, the ongoing bullish mood on world and regional stock markets in response to the decision by the US Fed to keep its rate on hold, combined with the downward trend in world oil prices, worked indirectly as a positive contribution to the JSX.

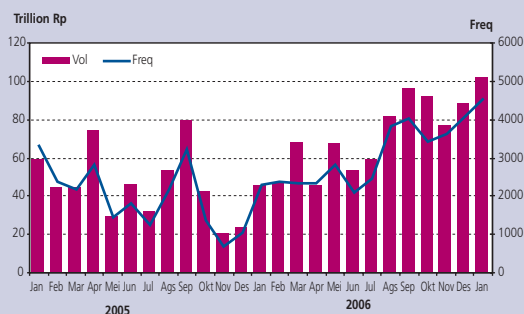
Concerning investors themselves, foreign investor trading again influenced domestic investor behaviour. Global conditions

marked by the absence of change in US interest rates kept stock markets in a bullish mood. This prompted foreign investors to expand their stock portfolios in Indonesia, as indicated by the enlarged net purchase by foreigners during Q4/2006 compared to the preceding quarter.

Heavy buying by non-resident investors encouraged local investors to follow suit, producing renewed gains in the JSX index. During Q4/2006, the net foreign purchase reached Rp 4.6 trillion against Rp 3.5 trillion in Q3/2006 (Graph 3.13). Measured as a daily average, the net foreign purchase widened from Rp 58 billion/day in the previous quarter to Rp 92 billion/day. Throughout 2006, foreign investors similarly recorded a net purchase. One of the implications of being a small open economy is that sentiment from external changes will inevitably affect domestic investor behaviour. Changes in global conditions, marked by relatively stable US inflation, high world market commodity prices and the absence of change (for the time being) in US interest rates have prompted international investors to seek venues for their investments. With these developments, the net foreign purchase in 2006 reached Rp 17.3 trillion.



Graph 3.13
JCI and Net Foreign Purchase Q IV-2006



Graph 3.14
Government Bond Trading Activities

The lowering of the BI Rate also met with positive response on the market for Government Securities (GS), as reflected in increased volume and frequency of GS trading. GS trading activity mounted steadily throughout 2006, both in volume and frequency. Volume and frequency of GS trading were up 35.6% and 36.7% over the previous year (Graph 3.14). The downward trend in the BI Rate since May 2006, the steady improvement in macroeconomic conditions and the bullish capital market all helped boost GS prices across all tenors. Reflecting this was the sustained decline in yield. The steepest drop in yield was recorded for GS with remaining maturity of less than 2 years. However,

average GS yield for medium and long-term GS (less than 7 years) also dropped to below or on par with the current BI Rate of 9.75%. Broken down by category of buyer, GS buying remains dominated by non-residents, followed by mutual funds and insurance companies. Accordingly, throughout 2006, foreign investors recorded a net purchase of Rp 27.3 trillion.

GS auctions were marked by overwhelming volume of incoming bids, with awarded bids exceeding target. To cover the fiscal deficit, the government again assigned priority to domestic financing through bond issues. During 2006, the government held primary offerings and reopenings covering a total of 16 series of government bonds, raising a total of Rp 37.3 trillion. To encourage more of the general public to invest in bonds, the government also issued the Retail GS (ORI Series 1) in early August 2006 to the value of Rp 3.2 trillion. As a rule, each auction has been consistently oversubscribed at highly competitive yield. Accordingly, the number of awarded bids has constantly exceeded target (except for the auction on 16 May 2006, when awarded bids were below target because of the overpriced offering). Total awarded bids, excluding ORI, have therefore surpassed the budget financing needs of Rp 35.8 trillion.

4. Economic Outlook for 2007

*In view of the overall condition and dynamics of the economy in 2006 and future trends, macroeconomic conditions in 2007 are predicted to remain stable. **Economic growth is projected at 5.7%-6.3%, up from the growth achieved in 2005 and 2006.** During the first half of 2007, economic growth will be driven mainly by consumption, while private investment is not expected to see significant expansion. Growth is predicted to gain added momentum in the second half of 2007 as the private sector boosts investment. In fiscal management, prompt and properly targeted government expenditures are expected to deliver an effective growth stimulus. On the external front, the robust expansion in exports is predicted to continue, despite a slowing trend as a result of less vigorous world economic growth compared to 2006. At the same time, imports of goods and services are expected to mount higher as domestic demand gathers momentum. These conditions are expected to influence the balance of payments in 2007, which is again predicted to record a surplus and thus support stability in the rupiah.*

CPI inflation in 2007 is predicted to come within the government-set inflation targeting range of 6±1%. Improvements on the supply side will still be adequate to offset rising demand driven by higher economic growth and thus keep inflationary pressure low. This CPI inflation forecast is based on modest pressure from administered prices and volatile foods in keeping with the government commitment to ensure adequate supplies of food and especially staple goods and to keep hikes in strategic administered prices to a minimum.

ASSUMPTIONS AND SCENARIOS

International Economic Conditions

In 2007, the world economy is predicted to see slower growth compared to the preceding year, although growth will still be on the high side at 4.9% (Table 4.1). While there are concerns over the impact of the housing slowdown in the US, for the time being this can be offset by stronger economic growth in other regions. World economic growth has becoming more evenly distributed alongside improvement in the growth structure. The slowdown in world growth also means that world trade volume is expected to decline. In keeping with this trend, prices of some commodities are also predicted to ease, although not to the extent earlier predicted. These commodity prices are still expected to have a positive bearing on Indonesia's exports.

Inflationary pressure is also expected to fall with global monetary policy switching to a neutral bias marked by the possibility of interest rate cuts in the US. Despite a modest decline in capital flows, FDI is expected to remain strong in emerging markets and the Asia-Pacific region. Taken together, overall conditions in the world economy will continue to benefit Indonesia's external sector performance. Nevertheless, to

(Annual Percentage Changes)

Table 4.1
Key Indicators for the World Economy

	Actual		Projection	
	2004	2005	2006	2007
World output	5.3	4.9	5.1	4.9
Advanced economies	3.2	2.6	3.1	2.7
United States	3.9	3.2	3.4	2.9
Euro Area	2.1	1.3	2.4	2.0
Japan	2.3	2.6	2.7	2.1
Other emerging market and developing countries	7.7	7.4	7.3	7.2
Africa	5.5	5.4	5.4	5.9
Sub-Sahara	5.6	5.8	5.2	6.3
Developing Asia	8.8	9.0	8.7	8.6
Cina	10.1	10.2	10.0	10.0
India	8.0	8.5	8.3	7.3
Middle East	5.5	5.7	5.8	5.4
Western Hemisphere	5.7	4.3	4.8	4.2
World trade volume (goods and services)	10.6	7.4	8.9	7.6

Source: IMF, *World Economic Outlook*, September 2006

support prospects for further improvement in balance of payments performance underpinned by a more robust structure, the possibility of falling international commodity prices needs to be anticipated by measures to boost production of export-based products and stronger measures to attract more FDI to Indonesia.

Fiscal Policy Scenario

Fiscal policy in 2007 will again aim for equilibrium between fiscal sustainability and the fiscal stimulus, to be achieved through consolidation and reduction in debt burdens and risks. The government is optimistic of having made

improvements in the management of state finances at the central government level and in the regions, and thus compared to 2006, the rate of budget realisation is expected to improve both on a quarterly basis and for the year as a whole. Nevertheless, given the risk that oil prices could sink below the budget assumption, the 2007 fiscal deficit could be lower than the 2007 Budget target of 1.1% of GDP and also less than the deficit recorded in 2006 (possibly 1% of GDP). With the added factor of the expected reduction in the official debt stock ratio, fiscal sustainability is set to remain on track in 2007.

Real Sector Policy Scenario

Alongside Bank Indonesia's efforts to maintain macroeconomic stability, the government is pursuing a series of initiatives in support of economic recovery. A range of government policies already in force and other policies currently under development are focused on the creation of a conducive investment climate. These policies are essentially related to government efforts to implement the infrastructure policy package and the investment policy package issued in the past.

The various policies supporting the implementation of the investment and infrastructure policy packages include the following:

- **Government equity participation in non-SOE companies operating in infrastructure.** This policy is related to the government plan for urgent implementation of Act No. 1 of 2004 concerning the State Treasury, which permits the government to invest state funds in entities other than SOEs. Government equity in non-SOE entities will be invested under almost the same mechanism as the Investment Funds Account policy. State funds invested in non-SOE entities have not so far been included in the 2007 State Budget, but the instruments and supporting policies are targeted for completion in 2007 to enable this form of investment to proceed. The Law on the State Treasury allows the government a free hand to engage in long-term investments other than government equity in SOEs.
- Concerning the institutional framework, the government has **established two new agencies, the Directorate of Investment Funds Management and the Risk Management Unit**, which also manages investment risk. This policy has been pursued to strengthen the public-private partnership. Thus if the government wishes to invest capital in a venture or project, there is an agency that makes the necessary calculations to prevent and overcome risk of project failure. The investment funds will be allocated to various designated vehicles, such as the infrastructure fund and green fund. The Public Services Agency in charge of land expropriation funds serves as one legal umbrella. Once all instruments are in place, the government will invest on the capital market or in other forms of capital investment.
- **Enforcement of Presidential Decree No. 80 of 2003 concerning Guidelines for Government Procurement of Goods and Services**, which requires investors to use local components in all government projects. Commencing in early 2007, all government agencies will be required to comply with rules prioritising the use of local components, following the issuance of Decree of the Minister of Industry No. 11/M-IND/PER/3/2006 concerning Technical Guidelines for Use of Domestic Products, which comprises instructions for implementation of the Presidential Decree. The use of local components will ensure that average national manufacturing growth of 8.5% in the 2005-2009 period will be achieved.
- **A Government Regulation has been issued stipulating that government units not holding certificates are permitted to draw on budget funds.** With this ruling, the project tender process in 2007 is expected to be free of delays.
- **Establishment of business clusters** for improvement of product quality and access to the local and export markets.
- The government is encouraging the **reutilisation of dormant footwear plants** in order to expedite the investment realisation process.
- **Establishment of the Taiwanese Investment Desk** and provision of an investment tax allowance or investment rebate of 30% to be refunded over six years, or alternatively a 5% reduction on tax each year as an incentive for investment from Taiwan.

On the sectoral level, various government policies in 2007 will remain focused on enhancing efficiency and productivity. **In the industry and trade sectors**, government is expected to launch more policies/incentives aimed at boosting industry performance in 2007, including VAT exemptions for primary commodities and an amendment to Government Regulation No. 148/2000. **In the agricultural sector**, the government will support efforts to improve rice cultivation through provision of seeds at prices discounted up to 75% of normal, seedling subsidies for 8.2 million hectares of arable land, improvements in irrigation channels and other support. These actions are expected to raise productivity from the current average of 4.5 tons per hectare. **In the mining sector**, Act No. 13 of 1967 concerning Mining will be amended in early 2007 by the Draft Law on Mining of Minerals and Coal. The government and Parliament have reached agreement on the difficult areas of the draft, such as contracts with investors to be made by legal entities yet to be established.

In labour relations, the government will move ahead with efforts to amend the Labour Law. The amendment will be made through the harmonisation of three legal products: the Laws on Worker Social Security (Jamsostek), National Social Security System and Labour. The harmonisation will begin in January 2007 with the amendment to Act No. 3 of 1993 concerning Worker Social Security and Act No. 40 of 2004 concerning the National Social Security System and will be followed by amendment to Act No. 13 of 2003 concerning Labour. In the case of the Labour Law, the amendment will be agreed in a tripartite forum, particularly in regard to severance pay and pensions. Harmonisation of the three laws is targeted for completion in 2007, and this is expected to encourage more labour-intensive investments.

OUTLOOK FOR ECONOMIC GROWTH

Economic activity is expected to gather fresh momentum in 2007, following a year of weak public purchasing power in 2006. In the first half of 2007, the primary engine of economic activity will be private consumption. Investment, on the other hand, is predicted to remain low. Improvement in purchasing power from increases in civil servant salaries and Provincial Minimum Wages is expected to boost private consumption. Even stronger economic activity is forecasted for the second half of 2007, buoyed by significant widening of investment. In addition to improved realisation of government capital expenditures, strong growth is predicted in private investment. Private investors are expected to acquire stronger expectations of the outlook for future growth in economic activity. These expectations alongside the downward trend in bank interest rates will provide more room for private investors to realise their investments in 2007. Externally, slowing world demand is predicted to lead to reduced growth in exports of goods and services, while imports of goods and services will in fact mount in response to increased economic activity. Analysed by sector, the improvement in domestic economic activity will be buoyed by high

growth in manufacturing and the trade, hotels and restaurants sectors. According to this forecast, the **economy is predicted to achieve 6.0% growth in 2007, with possible variation within the 5.7%-6.3% range depending on scenarios that could influence future economic performance.**

Outlook for Aggregate Demand

Household consumption is predicted to climb 4.3% in 2007 compared to 3.1% in 2006, due to increases in real disposable income. The rise in household consumption, which began in the last quarter of 2006, is expected to carry forward into 2007 with 3.8% growth (y-o-y) in Q1/2007, as well as improvement for 2007 overall. In the first half of 2007, higher public incomes will come mainly from the pay hike for civil servants and increases in Provincial Minimum Wage levels. In the second half, economic conditions are predicted to improve further alongside continued subdued inflation, and thus will support a further rise in real public incomes. Overseas worker remittances are also expected to rise in 2007, due to the increased number of Indonesians taking up employment in other countries.

Further increases in government consumption are predicted for 2007, although at a slower rate than in 2006. All components of government consumption are set to rise in terms of nominal value. Nevertheless, the more modest increase in General Allocation Funds (DAU) and Profit Sharing Funds (DBH) compared to 2006 will bring about some slowing in government consumption growth in 2007. Government policy for boosting incomes is reflected in increased Personnel Expenditures for such items as the civil servant pay rise, basic pensions for retired civil servants and increases in functional and structural work allowances. In view of these changes, government consumption is estimated to widen by 11.6% in 2007. In Q1/2007, government consumption is predicted to rise by about 15.1% (y-o-y). This rise will be driven mainly by the hike in basic salary levels in January 2007 and the increased procurement budget.

Investment is predicted to see significant expansion in 2007, with growth reaching about 13.0%. Little investment growth is expected in the first half of 2007, mainly because of the traditional pattern of limited government capital expenditures at

% (y-o-y)

the beginning of the year. Following the brisk 9.5% (y-o-y) growth in Q4/2006, investment growth in Q1/2007 is expected to come in at 8.8% (y-o-y). A significant upturn in investment growth is envisaged for the second half of 2007, fuelled by more active investment by the government and private sector. Expected sources of investment financing in 2007 are government funding, bank lending, the capital market, non-bank financial

Table 4.2
Economic Growth Projections – Demand Side

	2005	2006				2006*	2007*
		I	II	III	IV*		
Total Consumption	4.4	3.8	5.6	2.8	4.9	4.3	4.8 - 5.7
Private	3.9	2.9	3.0	3.0	3.6	3.1	4.2 - 4.7
Government	8.1	11.5	28.8	1.7	12.1	12.9	9.4 - 13.3
Total Investment	9.9	1.5	1.2	-0.3	9.5	3.0	11.6 - 14.6
Exports of Goods and Services	8.6	11.2	11.6	12.1	8.3	10.8	8.0 - 8.6
Imports of Goods and Services	12.4	3.9	8.4	9.7	9.9	8.0	10.2 - 11.4
GDP	5.6	4.8	5.1	5.5	6.5	5.5	5.7 - 6.3

* Projection figures

institutions, external sources and other financing sources such as equity and reserves. Bank credit expansion in 2007 is predicted to reach 18%. Financing from capital market sources is also predicted to rise in light of the continued macroeconomic stability and downward movement in interest rates.

In 2007, exports of goods and services will show slightly less growth at about 8.3%. This is related to the predicted slowdown in expansion of world trade. Despite this, increased production capacity and improved competitiveness in response to the government's deregulatory measures for the real sector are expected to mitigate the impact of softening world demand. Export growth is predicted to slow during Q1/2007, with growth at 7.7% (y-o-y) compared to 11.2% (y-o-y) recorded in Q1/2006.

Further expansion in imports of goods and services is expected in 2007, with growth estimated at about 10.5% (y-o-y) in line with strengthening economic activity. Capital goods imports, which until October 2006 recorded 0.7% growth, are predicted to climb significantly in response to brisk growth in non-construction investment. Imports are set to rise not only because of increased economic activity, but also the stable level of the rupiah. In Q1/2007, import growth is predicted to reach 8.6%, buoyed by stronger domestic demand.

Outlook for Aggregate Supply

Economic growth on the production side is forecasted higher in 2007 compared to 2006, consistent with expectations of more robust domestic demand. All sectors are predicted to chart higher growth against 2006. Especially strong growth is expected in the manufacturing and the trade, hotels and restaurants sectors (Table 4.3).

Manufacturing growth in 2007 is forecasted at 5.6%, strengthened by the expected rise in domestic demand. High growth is predicted to come from the transportation manufacturing, food processing, beverages and tobacco, chemical manufacturing

and the basic metals, iron and steel subsectors. A robust surge is expected in the automotive market, with GAIKINDO predicting car production to reach as many as 380,000 units in 2007 – up almost 20% from 2006 – on the strength of rising purchasing power. In the food and beverages subsector, optimism for stronger performance is reflected in planned startups by at least 36 new companies in 2007, while existing companies are reportedly upgrading their production capacity.

	2005	2006				2006*	2007*
		I	II	III	IV*		
Agriculture	2.5	4.3	3.8	2.3	2.2	3.2	3.2
Mining & Quarrying	1.6	2.2	3.7	1.0	1.5	2.1	2.6
Manufacturing	4.6	3.3	3.7	5.3	5.5	4.5	5.6
Electricity, Gas & Water Utilities	6.5	5.8	5.2	6.5	7.1	6.1	6.4
Construction	7.3	7.1	8.1	8.4	7.9	7.9	7.9
Commerce, Hotels & Restaurants	8.6	4.9	4.5	7.2	9.8	6.6	7.1
Transport & Communications	13.0	11.5	13.2	13.5	15.1	13.4	13.5
Finance, Leasing & Services	7.1	5.5	5.2	4.6	6.7	5.5	5.8
Other Services	5.2	6.0	6.4	7.0	7.1	6.6	6.6
GDP	5.6	4.8	5.1	5.5	6.5	5.5	6.0

* Projection figures

Stronger domestic demand is also expected to spur growth in the chemicals and steel industries. Key to the higher growth are plans for substantial expansion in production capacity in 2007. Higher steel production will also be driven by world demand, with demand in India and China predicted to rise by 5%. In the textiles and textile products subsector, more robust growth will be supported by the government-sponsored machinery restructuring programme in which companies purchasing new machines will benefit from an interest subsidy. The allocation for this subsidy in the 2007 State Budget is Rp 285 billion, an amount slated for regular increases in future years. Stronger performance in the manufacturing sector will be supported by the government amendment of Government Regulation No. 148 of 2000, which offers tax incentives for 15 business sectors. These tax incentives are expected to promote stronger growth in the industrial sector.

Growth in the trade, hotels and restaurants sector is forecasted to surpass the 7.1% recorded in the past year. While retail business will benefit from stronger demand, prospects in 2007 are also brighter because of lower interest rates. The hotels and restaurants subsector is also expected to perform better due to the improved image of tourism in Indonesia and various government-sponsored promotions. In 2007, Indonesia will host the PATA (Pacific Asia Travel Association) Mart, which will support efforts to rebuild the number of international tourists visiting Indonesia. In 2007, the government has set a target of 6 million foreign tourist arrivals, up about 20% from 2006. Domestic tourism is also targeted at 190 million journeys, ahead of the estimated 180 million in 2006.

The agricultural sector is predicted to grow by about 3.2%. Key to higher agricultural production will be the foodstuffs subsector, and particularly the rice crop. The Ministry of Agriculture targets national rice production at 56.47 million tons in 2007 on a total planted area estimated at 12.7 million hectares. This rice production target is also higher than the 2006 rice output recorded at 54.66 million tons (ARAM III). To boost production, the government will support rice cultivation through provision of such items as low-rice seeds, seedling subsidies for 8.2 million hectares and repairs to irrigation channels. High growth is also predicted for the estates subsector, which will benefit from the government commitment to a Rp 1 trillion interest subsidy for smallholder farmers applying to banks for loans for biofuel development and revitalisation of estates.

The transport and communications sector in 2007 will again chart high growth at 13.5%. Mounting activity in manufacturing and trade will in turn boost activity in cargo and freight. At the same time, the communications subsector will see another year of vigorous growth spurred by the rapid pace of technological developments and various innovations in communications. PT Telkom – Indonesia's largest communications operator – will invest Rp 17 trillion in capital expenditures during 2007. This investment will be used to expand investment in the cellular business, wireless fixed-line phones and other telecommunications infrastructure.

The mining sector will see an estimated 2.6% growth, up from the previous year.

Higher growth in this sector will be supported by increased production in the non-oil and gas mining subsector, including coal. The Indonesian Coal Society predicts continued high demand in the coming year. Increased demand within Indonesia will come from the accelerated completion of the 10,000 MW coal-fired power plant. On the export market, demand will be spurred by the Central Electricity Authority of India construction of a 42,000-47,000 MW coal-fired power plant in 2007-2012. Also boosting growth in the mining sector will be the government programme for accelerated development of 11 mining projects currently held up by forestry regulations (oil and gas drilling). The overall investment value of these projects is estimated at US\$9 billion.

The construction sector is predicted to grow by a robust 7.9% in 2007.

The downward trend in interest rates since the middle of the year is also seen likely to boost activity in construction. Further impetus for growth in construction during 2007 will come from the government incentives offered through the Indonesia Infrastructure Fund. At this time, the Ministry of Public Works has set aside Rp 2 trillion in incentive funds for infrastructure projects that include the development of roads, water utilities and housing through to 2009.

Financial sector growth in 2007 is predicted at 5.8%, up from 5.5% in 2006.

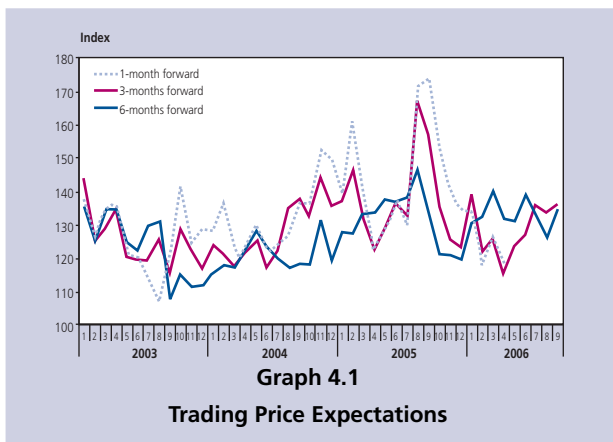
An increased net interest margin is expected in the bank subsector, boosted by the steeper downward trend in deposit rates compared to lending rates. Banks are also expected to see stronger credit expansion fuelled by a new upturn in economic activity. In addition, falling interest rates and mounting economic activity will also boost performance in the non-bank financial institutions subsector, consisting mainly of consumer finance and leasing companies.

INFLATION FORECAST**CPI inflation in 2007 is predicted to come within the government-set inflation targeting range of 6±1%.**

Improvements on the supply side will still be adequate to offset rising demand driven by higher economic growth and thus keep inflationary pressure low. This CPI inflation forecast for 2007 is based on modest pressure from administered prices and volatile foods in keeping with the government commitment to ensure adequate supplies of food and especially staple goods and to keep hikes in strategic administered prices to a minimum.

Public expectations of inflation are likely to rise, consistent with the improving economic outlook

(Graph 4.1). Driving higher expectations of inflation will be greater expectations of depreciation in the rupiah and gains in public purchasing power. Improvement in public incomes will come from such actions as the average 15% increase in the provincial minimum wage and civil servant salaries and the forecasted investment growth that is expected to create more jobs. This in turn will encourage more to plan on increased consumption in the future and ultimately lead to rising



Graph 4.1

Trading Price Expectations

public expectations of inflation. Nevertheless, the relative stability in the exchange rate and the government decision to hold back from price increases for strategic goods and especially from any increases in fuel prices and electricity billing rates will help mitigate upward pressure on inflation expectations during 2007.

Demand-side inflationary pressure is predicted to remain low.

The relatively modest demand pressure in 2007 – reflected in the negative level and limited acceleration in the output gap – is a delayed effect from demand conditions in the past year that can still be covered by the supply side.

Like before, external factors will bring only limited upward pressure on CPI inflation.

This is because of the relative stability in the exchange rate and diminished outlook for inflation in trading partner countries, which is predicted to reach 1.7% in 2007.

Inflationary pressure in the volatile foods category is expected to ease in 2007 compared to the preceding year.

In regard to production, the climate, the availability of production inputs at affordable prices and the assumed absence of natural disasters will help minimise crop failures in 2007. Concerning distribution, better infrastructure following the launching of the infrastructure development programme, particularly in the regions, will help reduce price distortions caused by distribution problems and shortages. In addition, the management of food supplies is expected to proceed smoothly, especially during the fasting month and the 2007 Eid-ul-Fitr festivities, and this is expected to mitigate any excessive price movements during the religious festive season.

RISKS

Looking ahead, the outlook for the economy and inflation may be affected by a number of risks arising from both external and internal factors. These factors represent mainly downside risks affecting the prospects for the Indonesian economy. **Externally**, Bank Indonesia is constantly vigilant against the likelihood of slow global economic growth and changes in global investment preferences. At the same time, **within Indonesia**, structural issues such as delays in implementing the investment climate, infrastructure and financial policy packages are risks that call for close monitoring, in addition to other issues such as the possibilities of disruptions to domestic distribution of goods and of a bubble on the capital market. If these risks can be addressed properly, economic growth in 2007 may climb beyond the forecasted level.

5. Monetary Policy Response Q I-2007

After an evaluation of Indonesia's macroeconomic conditions in 2006, the economic and monetary outlook, the various risks ahead and progress towards the inflation target, set at $6\% \pm 1\%$ and $5\% \pm 1\%$ for 2007 and 2008, **Bank Indonesia decided to lower the BI Rate to 9.50%, down 25 bps** from the previous level.

Bank Indonesia regards the year 2007 as a crucial year offering promise for rebound in the national economy. Consistency in macroeconomic policy, sharper focus in structural policies and rapid implementation of these policies will be essential to achieving better quality economic growth. For this reason, the commitment, hard work and coordination of the entire nation will be vital to achieving higher quality economic growth in 2007.

To create this momentum, Bank Indonesia's monetary policy will remain focused on building macroeconomic stability in support of sustainable economic growth through consistent application of the Inflation Targeting Framework (ITF). On the operational level, Bank Indonesia will also introduce various improvements to the operational framework for monetary policy.

Statistics

Table 1
Interest Rate of Money Market, Deposits, and Credit
(Percentage per Annum)

Period	Interbank Money Market	SBI Discount Rate	SBPU Discount Rate	Time Deposit Interest Rate*					Credit Interest Rate*	
				1 month	3 months	6 months	12 months	24 months	Working Capital	Investment
2000										
Qtr. I	9.42	11.03	-	10.80	12.40	12.86	20.12	14.01	18.93	16.46
Qtr. II	11.12	11.74	-	10.37	11.69	12.40	13.44	13.25	18.14	16.21
Qtr. III	10.62	13.62	-	11.42	12.84	12.66	12.42	14.38	17.99	16.62
Qtr. IV	11.41	14.53	-	11.96	13.24	13.31	12.17	14.32	17.65	16.86
2001										
Qtr. I	12.73	15.82	-	13.82	14.86	14.52	13.01	16.41	17.90	16.86
Qtr. II	13.95	16.65	-	14.01	15.00	15.01	13.97	16.37	18.45	17.04
Qtr. III	15.47	17.57	-	15.49	16.16	15.44	14.46	17.51	19.06	17.22
Qtr. IV	15.66	17.62	-	16.07	17.24	16.18	15.48	18.05	19.19	17.90
2002										
Qtr. I	15.41	16.76	-	15.64	17.02	16.26	16.13	18.21	19.35	18.03
Qtr. II	14.72	15.11	-	14.76	15.85	15.73	16.28	18.10	19.08	18.11
Qtr. III	10.89	13.22	-	13.50	14.36	14.81	15.99	18.06	18.74	18.11
Qtr. IV	8.89	12.99	-	12.81	13.63	13.79	15.28	18.04	18.25	17.82
2003										
Qtr. I	12.70	11.40	-	11.90	12.90	13.22	14.16	17.98	18.08	17.85
Qtr. II	8.95	9.53	-	10.31	11.55	12.21	12.93	17.95	17.41	17.43
Qtr. III	4.89	8.66	-	7.67	8.58	10.47	11.90	17.27	16.07	16.53
Qtr. IV	4.65	8.31	-	6.62	7.14	8.25	10.39	16.13	15.07	15.44
2004										
Qtr. I	5.87	7.42	-	5.86	6.11	6.79	8.93	14.49	14.61	15.12
Qtr. II	4.24	7.34	-	6.23	6.31	6.36	7.68	9.31	14.10	14.64
Qtr. III	4.13	7.39	-	6.31	6.61	6.89	7.27	8.94	13.80	14.33
Qtr. IV	3.76	7.43	-	6.43	6.71	7.12	7.07	8.12	13.41	14.05
2005										
Qtr. I	5.95	7.44	-	6.50	6.93	7.35	8.04	9.42	13.31	13.78
Qtr. II	6.95	8.25	-	6.98	7.19	7.11	7.11	8.05	13.36	13.65
Qtr. III	6.92	10.00	-	9.16	8.51	8.01	8.65	8.82	14.51	14.47
Qtr. IV	9.44	12.75	-	11.98	11.75	10.17	10.95	12.39	16.23	15.66
2006										
Qtr. I	10.28	12.73	-	11.61	12.19	12.10	12.02	12.64	16.35	15.90
Qtr. II	10.23	12.50	-	11.34	11.70	12.09	12.28	12.61	16.15	15.94
Qtr. III	8.90	11.25	-	10.47	11.05	11.52	12.36	12.47	15.82	15.66
Qtr. IV	5.97	9.75	-	9.50	10.25	10.98	12.18	12.20	15.35	15.38

* November 2006

Table 2
Money Market Transactions
(Billion of Rupiah)

Period	Interbank Transaction ³⁾	Bank Indonesia Certificate (SBI) ¹⁾			Money Market Securities (SBPU) ²⁾		
		Issuance	Repayment	Outstanding	Issuance	Repayment	Outstanding
1999							
Qtr. I	173,045	128,441	122,292	48,914	1,018	1,018	1,018
Qtr. II	160,470	182,926	167,962	63,879	0	0	1,018
Qtr. III	127,906	205,593	196,269	73,202	0	0	1,018
Qtr. IV	133,941	194,657	204,810	63,049	644	1,662	0
2000							
Qtr. I	65,815	238,829	213,479	88,399	0	0	0
Qtr. II	56,761	241,221	250,100	79,520	0	0	0
Qtr. III	76,237	237,610	238,846	78,284	0	0	0
Qtr. IV	80,450	201,730	219,942	60,072	0	0	0
2001							
Qtr. I	110,199	271,876	263,243	68,924	0	0	0
Qtr. II	106,700	237,688	228,902	77,711	0	0	0
Qtr. III	124,296	242,354	248,896	71,167	0	0	0
Qtr. IV	119,856	209,336	224,761	55,742	0	0	0
2002							
Qtr. I	97,490	294,468	250,020	100,190	0	0	0
Qtr. II	72,907	245,643	243,251	102,582	0	0	0
Qtr. III	110,041	252,899	257,717	97,781	0	0	0
Qtr. IV	122,416	211,468	230,222	79,027	0	0	0
2003							
Qtr. I	104,122	284,429	242,858	119,947	0	0	0
Qtr. II	136,517	289,558	286,009	123,496	0	0	0
Qtr. III	118,181	350,575	340,837	133,234	0	0	0
Qtr. IV	125,166	321,710	347,918	107,026	0	0	0
2004							
Qtr. I	142,003	354,841	321,477	140,390	0	0	0
Qtr. II	87,082	283,275	304,891	118,776	0	0	0
Qtr. III	165,064	252,542	339,339	31,979	0	0	0
Qtr. IV	204,336	293,933	252,929	103,825	0	0	0
2005							
Qtr. I	216,381	369,495	415,785	57,536	0	0	0
Qtr. II	237,571	362,522	318,997	101,060	0	0	0
Qtr. III	250,610	230,028	289,659	41,429	0	0	0
Qtr. IV	264,348	183,665	150,537	74,634	0	0	0
2006							
Qtr. I	310,175	415,638	356,472	133,801	0	0	0
Qtr. II	280,836	517,854	483,966	167,687	0	0	0
Qtr. III	286,958	599,495	586,716	180,466	0	0	0
Qtr. IV*	208,430	452,545	424,063	208,948	0	0	0

* November 2006

1) Morning Transaction

2) Transaction between Bank Indonesia and Commercial Banks only. Since March 1994 includes Repo SBPU

3) Including special SBI : since October 1994 includes Repo SBI

Table 3
Banks Outstanding Credits in Rupiah and Foreign Exchange by Banking Group and Economic Sector ¹⁾
(Billion of Rupiah)

	2004		2005				2006			
	III	IV	I	II	III	IV	I	II	III	IV*
1 State Bank	200,753	217,066	223,025	235,274	243,678	250,319	247,331	256,267	264,735	271,140
- Agriculture	19,204	20,224	20,340	20,411	20,797	21,908	21,649	22,110	23,012	24,338
- Mining	3,481	4,383	4,292	4,338	3,932	3,249	3,007	3,428	3,485	4,206
- Industry	55,930	59,185	60,466	60,985	63,507	65,781	63,402	64,567	64,265	67,995
- Trade	42,400	44,928	44,881	47,275	48,095	49,809	52,729	57,548	61,031	59,990
- Services	30,170	31,755	31,966	35,446	37,647	37,448	36,148	37,094	39,269	39,730
- Others	49,568	56,591	61,080	66,819	69,700	72,124	70,396	71,520	73,673	74,881
2 Private National Foreign Bank	207,157	224,560	235,224	257,749	284,411	295,013	291,817	302,693	313,651	321,638
- Agriculture	8,722	8,697	8,915	9,015	9,625	9,541	9,693	10,248	10,316	11,055
- Mining	2,181	2,268	2,376	2,694	3,409	3,267	2,935	3,414	3,775	4,369
- Industry	41,686	45,195	45,627	48,206	53,904	55,185	53,304	57,119	58,125	59,258
- Trade	50,734	55,702	57,560	63,736	67,300	71,098	70,729	74,997	78,679	80,610
- Services	50,710	53,632	56,553	61,358	65,925	68,660	69,006	71,371	74,729	76,144
- Others	53,124	59,066	64,193	72,740	84,248	87,262	86,150	85,544	88,027	90,202
3 Regional Government Bank	35,954	37,246	38,976	42,024	44,510	44,909	47,235	51,141	55,009	56,520
- Agriculture	1,255	1,320	1,406	1,514	1,557	1,640	1,729	1,860	1,922	1,999
- Mining	30	33	36	41	52	54	57	56	54	54
- Industry	386	400	439	504	451	421	430	471	476	476
- Trade	5,991	6,292	6,683	7,269	7,546	7,532	7,668	8,058	8,312	8,342
- Services	5,709	5,322	5,108	5,260	6,058	5,633	5,851	6,561	7,531	7,861
- Others	22,583	23,879	25,304	27,436	28,846	29,629	31,500	34,135	36,714	37,788
4 Foreign and Joint Bank	69,359	74,676	79,155	87,555	100,643	99,428	95,730	100,003	107,692	112,265
- Agriculture	1,619	2,135	2,390	2,531	3,093	3,589	3,409	4,124	4,727	5,458
- Mining	851	1,046	2,205	2,028	2,036	1,303	1,548	2,173	2,369	2,218
- Industry	37,182	38,823	39,569	43,867	50,268	48,291	45,954	46,847	49,682	50,849
- Trade	3,886	4,113	4,671	5,061	6,337	5,669	5,357	5,865	6,663	6,851
- Services	15,131	17,149	17,920	20,044	22,881	23,202	21,258	21,721	24,726	26,944
- Others	10,690	11,410	12,400	14,024	16,028	17,374	18,204	19,273	19,525	19,945
5 Sub total (1 until 4)	513,223	553,548	576,380	622,602	673,242	689,669	682,113	710,104	741,087	761,563
- Agriculture	30,800	32,376	33,051	33,471	35,072	36,678	36,480	38,342	39,977	42,850
- Mining	6,543	7,730	8,909	9,101	9,429	7,873	7,547	9,071	9,683	10,847
- Industry	135,184	143,603	146,101	153,562	168,130	169,678	163,090	169,004	172,548	178,578
- Trade	103,011	111,035	113,795	123,341	129,278	134,108	136,483	146,468	154,685	155,793
- Services	101,720	107,858	111,547	122,108	132,511	134,943	132,263	136,747	146,255	150,679
- Others	135,965	150,946	162,977	181,019	198,822	206,389	206,250	210,472	217,939	222,816

* November 2006

1) Excluded central government, non-resident, foreign counter part value, and managable credit

Table 4
Money Supply and Its Affecting Factors
(Billion of Rupiah)

End of Period	M2					Affecting Factors				
	Total ¹⁾	M1			Quasy Money	Net Foreign Asset	Net Claims On Central Govt. ³⁾	Net Claims On Official Entities	Net Claims On Private Enterprise and individual	Net Others
		Total ²⁾	Currency	Demand Deposit						
2001										
Qtr. I	766,812	148,375	60,114	88,261	618,437	248,254	521,187	14,056	295,244	-311,929
Qtr. II	796,440	160,142	66,201	93,941	636,298	293,223	502,508	14,998	315,643	-329,932
Qtr. III	783,104	164,237	69,047	95,190	618,867	203,671	503,471	14,245	313,385	-251,668
Qtr. IV	844,054	177,731	76,342	101,389	666,323	233,975	529,706	18,337	310,816	-248,780
2002										
Qtr. I	831,410	166,173	69,716	96,457	665,237	221,235	544,656	16,655	306,884	-258,020
Qtr. II	838,635	174,017	71,975	102,042	664,618	206,360	539,702	20,127	312,978	-240,533
Qtr. III	859,706	181,791	72,757	109,034	677,915	238,860	529,650	22,072	341,581	-272,457
Qtr. IV	883,908	191,939	80,686	111,253	691,969	250,696	510,351	22,889	366,407	-266,435
2003										
Qtr. I	877,776	181,239	72,323	108,916	696,537	249,736	510,307	22,364	377,989	-282,620
Qtr. II	894,213	194,537	77,091	117,787	699,335	236,660	506,218	24,436	393,439	-266,540
Qtr. III	911,224	207,234	81,118	126,469	703,637	240,781	481,552	24,248	416,534	-251,891
Qtr. IV	955,692	223,799	94,542	129,257	731,893	271,785	479,013	24,087	442,741	-261,969
2004										
Qtr. I	935,247	219,086	86,881	132,205	716,161	275,819	443,440	22,803	454,663	-261,518
Qtr. II	975,166	233,726	97,574	136,152	741,440	280,070	468,907	27,806	522,161	-323,778
Qtr. III	986,806	240,911	99,505	141,406	745,895	258,684	476,451	25,261	551,562	-325,152
Qtr. IV	1,033,528	253,818	109,265	144,553	779,710	263,647	498,019	26,919	588,885	-343,940
2005										
Qtr. I	1,020,693	250,492	98,584	151,908	770,201	268,482	456,274	28,257	612,463	-344,783
Qtr. II	1,073,746	267,635	106,125	161,510	806,111	256,058	468,004	28,237	659,129	-337,682
Qtr. III	1,150,451	273,954	114,998	158,956	876,497	280,369	488,483	29,805	708,018	-356,224
Qtr. IV	1,203,215	281,905	124,316	157,589	921,310	313,082	498,901	28,059	710,783	-347,610
2005										
Qtr. I	1,195,067	277,293	112,625	164,668	917,774	347,970	470,048	25,557	705,321	-353,829
Qtr. II	1,253,757	313,153	123,761	189,392	940,604	345,457	481,654	29,746	729,609	-332,709
Qtr. III	1,291,396	333,905	129,969	203,936	957,491	401,065	481,641	31,858	758,261	-381,429
Qtr. IV*	1,338,555	342,645	129,702	212,943	995,910	417,531	481,199	33,560	778,228	-371,963

* November 2006

1) M1 plus Quasy Money

2) Currencies plus Demand Deposits

3) Including the Government's Special Account

Table 5
Base Money and Its Affecting Factors
(Billion of Rupiah)

	2004	2005				2006			
	IV	I	II	III	IV	I	II	III	IV
I. Base Money	199,446	184,878	198,427	224,414	239,781	233,878	247,742	257,843	297,080
a. Statutory Reserve Shortfall	0	0	0	0	0	0	0	0	0
b. Currency	126,895	116,376	124,427	134,871	144,869	135,005	145,666	153,569	178,572
- Currency outside bank	109,265	98,584	106,125	114,998	124,316	112,625	123,761	129,969	152,154
- Cash in vaults	17,630	17,792	18,302	19,873	20,553	22,380	21,905	23,600	26,418
c. Commercial Banks Positive Balance	72,053	67,798	73,446	89,079	94,531	98,544	101,751	104,061	118,417
d. Private Sector Demand Deposits	498	704	554	464	381	329	325	213	91
II. Factor Affecting Base Money									
a. Net International Reserve ¹⁾	170,846	173,283	163,760	141,548	173,806	213,530	213,143	255,182	274,694
b. Net Domestic Assets	28,600	11,595	34,667	82,866	65,975	20,348	34,599	2,661	22,386
- Net Claims on Central Government	226,620	187,988	197,653	210,909	239,148	209,557	218,033	219,538	265,919
- Liquidity Support	27,314	27,310	27,310	27,310	13,545	13,545	13,545	13,545	13,545
- Liquidity Credits	12,349	12,222	11,987	11,800	11,593	11,372	11,165	11,035	10,832
- Others Claims	4,586	3,673	10,141	10,166	10,101	10,156	10,172	10,175	10,003
- Open Market	-144,548	-130,783	-122,194	-59,106	-131,844	-150,413	-181,926	-197,211	-250,331
- SBI (net)	-103,825	-57,611	-101,134	-41,503	-74,632	-133,798	-167,685	-180,382	-208,763
- Rupiah Intervention	-40,723	-73,172	-21,060	-17,603	-57,212	-16,615	-14,241	-16,829	-41,568
- SBPU Repo	0	0	0	0	0	0	0	0	0
- Net Other Items	-97,721	-88,815	-97,281	-115,402	-87,087	-81,645	-44,058	-62,501	-35,912

1) Before June 1997 : NFA, after June 1997 : NIR using constant rate Rp7,000/\$
 Since 1998 up to March 1999 using constant rate Rp10,000/\$
 Since April 1999 using constant rate Rp7,500/\$
 Since 21 November 1999 using constant rate Rp7,000/\$

Table 6
Indonesia's Balance of Payment ¹⁾
(Million of \$)

November 2006

	2005*					2006**		
	I	II	III	IV	Total	I	II	III
I. Current Account	259	423	-1,196	821	307	1,573	603	4,029
A. Goods, net (Trade Balance)	3,227	4,043	3,471	6,823	17,563	6,675	6,964	10,015
Export f.o.b	20,158	21,602	21,938	23,135	86,833	23,201	25,381	28,512
Import f.o.b	-16,931	-17,559	-18,468	-16,313	-69,270	-16,526	-18,417	-18,497
B. Services (net)	-1,911	-1,176	-2,305	-3,730	-9,122	-3,403	-3,390	-3,510
C. Income (net)	-2,168	-3,464	-3,568	-3,726	-12,927	-2,836	-4,068	-3,725
D. Current Transfers (net)	1,111	1,020	1,207	1,455	4,793	1,137	1,097	1,248
II. Capital and Financial Account	-564	525	-3,319	3,645	287	2,214	-129	-688
A. Capital Account	-	33	100	200	333	60	28	83
B. Financial Account	-564	492	-3,419	3,444	-47	2,154	-157	-771
1. Direct Investment	415	3,246	857	695	5,213	463	1,224	1,085
Abroad (net)	-651	-615	-879	-920	-3,065	-655	-517	-1,089
Domestic (FDI), (net)	1,066	3,861	1,736	1,615	8,278	1,118	1,741	2,174
2. Portfolio Investment	395	-805	1,738	2,862	4,190	3,730	-1,152	691
Asset (net)	-339	-63	-462	-216	-1,080	-392	-446	-266
Liability (net)	734	-742	2,200	3,078	5,270	4,122	-706	956
3. Other Investment	-1,374	-1,949	-6,014	-112	-9,449	-2,038	-228	-2,547
Asset (net)	-631	-1,816	-4,648	-1,551	-8,646	-1,417	801	-1,555
Liability (net) ²⁾	-743	-134	-1,366	1,439	-803	-621	-1,030	-991
III. Total (I + II)	-305	948	-4,515	4,466	594	3,787	474	3,341
IV. Errors and Omissions	657	-2,429	1,346	276	-150	1,999	2,905	-704
V. Overall Balance (III + IV)	352	-1,480	-3,169	4,742	444	5,786	3,379	2,637
VI. Monetary Movements ³⁾	-352	1,480	3,169	-4,742	-444	-5,786	-3,379	-2,637
Changes in Reserves Assets ³⁾	-49	1,729	3,483	-4,500	663	-5,359	354	-2,189
a.I. Transaction	-303	-249	-313	-241	-1,107	-427	-3,733	-448
IMF:	0	0	0	0	0	0	0	0
Purchases	-303	-249	-313	-241	-1,107	-427	-3,733	-448
Repurchases								
Memorandum:								
Reserve Assets Position ⁴⁾	36,030	33,865	30,318	34,724	34,724	40,082	40,107	42,353
Current Account (% GDP)					0.1			
Debt Service Ratio (%) ⁵⁾	16.9	21.6	17.4	13.6	17.3	17.4	30.5	18.7
a.1. Government Related & Monetary Authorities ⁶⁾	8.7	5.8	6.7	5.7	6.7	9.9	21.0	6.9

* Temporary figures.

** Very Temporary figures.

1) New format since January 2004 publication.

2) Not included IMF package

3) Negative represents surplus and positive represents deficit

4) Since 1988, reserve assets position is based on Gross Foreign Asset Replacing Official Reserve. Since 2000 reserve assets position is based on International Reserve and Foreign Currency Liquidity (IRFCL).

5) Ratio of external debt service payments to export of goods and services.

6) Consists of Government, State Owned Enterprises Except Banks, and Bank Indonesia.

Table 7
Inflation Rate by Group of Goods and Services
(Percentage)¹⁾

Sub Group	2004		2005				2006			
	III	IV	I	II	III	IV	I	II	III	IV
I. Food	-3.05	6.08	1.72	0.65	2.63	8.41	4.60	0.54	1.27	6.05
A. Cereal and Product	-0.17	2.73	11.77	-1.25	4.91	8.87	16.54	-0.58	2.60	8.63
B. Meat and Meat Product	-4.18	9.45	-1.59	3.17	-2.37	6.17	-0.03	3.50	5.62	-0.25
C. Fresh Fish	2.27	3.20	-0.76	-0.73	3.90	8.85	1.54	0.29	3.66	1.46
D. Dried Fish	0.99	1.77	1.66	-1.41	2.59	6.33	0.16	2.22	2.72	1.64
E. Egg and Milk	-4.22	5.95	-2.48	4.82	0.99	3.03	-2.18	2.48	1.96	2.55
F. Vegetables	-5.45	17.69	-2.14	-2.11	-0.23	12.15	3.77	-2.28	1.00	11.87
G. Beans and Nuts	1.79	2.80	2.08	0.67	1.88	7.73	0.95	0.11	1.73	1.72
H. Fruits	2.34	2.13	-0.38	0.82	1.63	6.19	3.21	0.16	0.50	4.46
I. Species	-23.02	19.81	-3.50	4.24	8.14	18.84	3.23	-1.21	-13.98	24.41
J. Fat and Oil	-1.54	0.11	-0.43	0.80	1.24	2.08	-0.65	0.38	1.41	3.65
K. Others	2.44	0.91	1.25	0.58	2.18	6.06	-0.63	0.85	4.36	3.13
II. Prepared Food, Beverage, Cigarettes and Cloves	0.75	1.88	2.99	1.98	2.12	6.01	2.19	1.00	0.80	2.24
A. Prepared Food	1.00	1.45	2.33	1.32	1.54	9.15	2.13	0.91	0.96	2.25
B. Non-alcoholic-Beverage	0.57	5.19	5.43	0.32	4.70	2.85	3.01	0.87	0.31	1.95
C. Cigarettes, Cloves, and Alcoholic Beverage	0.32	0.39	2.51	5.18	1.48	1.17	1.93	1.23	0.86	2.59
III. Housing	1.62	1.44	2.44	1.22	1.30	8.47	1.62	1.05	0.78	1.30
A. Home Owner Cost	2.37	1.61	2.37	1.56	1.12	3.45	2.19	1.40	0.98	1.73
B. Fuel, Electricity, and Water	0.58	1.54	3.35	0.30	2.09	22.38	0.73	0.58	0.34	0.56
C. Household Equipment	0.65	0.43	1.16	0.98	1.20	3.24	0.64	0.72	0.67	0.78
D. Household Operation	0.82	0.99	1.67	1.75	0.97	3.02	1.87	0.92	0.99	0.99
IV. Clothing	0.75	2.47	0.71	0.89	2.17	2.99	1.61	2.66	0.57	1.84
A. Clothing for Men	0.60	2.04	0.58	0.66	0.56	1.90	1.25	0.77	0.80	1.81
B. Clothing for Women	0.29	1.17	0.51	0.82	0.60	2.13	0.86	0.69	0.69	1.41
C. Clothing for Children	0.77	1.43	0.40	0.55	1.27	1.65	1.18	0.56	1.00	1.35
D. Personal Effect and Other Clothing	1.77	5.91	1.28	1.65	7.28	6.52	3.13	8.78	-0.22	2.47
V. Health	0.56	1.06	0.99	1.22	1.64	2.15	1.86	1.42	0.70	1.76
A. Medical Care and Medicine	0.78	1.74	1.37	2.10	2.28	0.98	2.08	1.61	0.94	3.70
B. Medicine	0.54	0.65	0.91	0.90	1.09	1.96	1.03	0.93	-0.19	0.18
C. Personal Care	0.68	1.02	2.85	2.51	1.63	5.42	1.94	1.03	0.84	0.80
D. Personal Care and Cosmetics	0.43	0.56	0.47	0.55	1.22	2.47	2.11	1.43	0.77	0.72
VI. Education, Culture, Sport, and Entertainment	8.30	1.35	0.34	0.32	5.76	1.67	0.03	0.41	7.44	0.20
A. Education	14.61	2.21	0.12	0.13	8.45	2.03	-0.76	0.02	11.41	0.12
B. Courses and Training	0.83	1.05	0.38	1.13	1.78	0.79	2.40	0.19	2.31	0.23
C. Education Equipment	1.94	0.11	0.47	0.65	2.91	1.52	0.45	1.79	3.61	0.27
D. Recreation	0.41	-0.16	0.83	0.53	0.82	2.90	1.70	0.82	0.06	0.28
E. Sport	0.63	0.45	0.50	0.42	0.67	0.70	0.83	0.54	1.19	0.88
VII. Transportation and Communication	0.46	0.56	10.56	0.72	0.53	29.29	0.24	0.35	0.08	0.35
A. Transportation	0.08	0.70	16.17	0.98	0.61	42.53	0.07	0.37	0.02	0.33
B. Communication and Delivery	-0.02	0.00	0.00	-0.11	0.07	0.04	-0.02	0.02	-0.01	-0.01
C. Transport Facility	0.69	1.46	1.94	1.40	1.59	7.46	1.89	1.09	1.26	1.56
D. Financial Service	16.92	0.52	0.00	0.16	0.00	1.41	5.36	0.45	0.05	0.01
GENERAL	0.49	2.51	3.19	1.05	2.03	10.08	1.98	0.87	1.16	2.44

Notes :

1. Calculated based on 2002 cost of living survey from 44 cities (2002=100)

Sources: BPS-Statistic Indonesia (processed)

Table 8
Inflation Rate Contribution in 44 Cities
(Percentage)¹⁾

Cities	2004			2005				2006			
	II	III	IV	I	II	III	IV	I	II	III	IV
1. Lhokseumawe	0.90	1.85	2.64	4.89	0.79	0.50	10.66	4.02	1.49	1.09	4.45
2. Banda Aceh	1.77	2.24	2.75	9.84	3.53	4.44	18.81	1.24	2.54	2.64	2.81
3. Padang Sidempuan	4.69	-0.21	1.58	1.62	1.00	3.23	11.81	1.34	0.71	2.74	4.93
4. Sibolga	2.30	-0.03	2.52	3.35	0.57	5.14	11.99	-2.17	0.83	1.90	1.07
5. Pematang Siantar	3.46	0.20	2.62	3.63	0.54	2.71	11.82	-0.10	0.40	1.68	4.01
6. Medan	2.31	0.67	2.67	2.97	2.10	2.81	13.72	1.41	0.29	0.85	3.31
7. Padang	2.53	-0.28	3.09	6.80	-1.32	2.75	11.25	1.17	0.71	0.93	5.07
8. Pekanbaru	3.45	1.30	2.71	2.75	0.14	2.91	10.59	0.73	0.89	1.21	3.36
9. Batam	1.10	0.70	1.89	2.65	0.39	1.52	9.72	0.66	-0.40	2.30	1.97
10. Jambi	3.16	0.60	2.99	2.59	0.35	1.40	11.60	1.38	1.20	1.61	6.14
11. Palembang	4.25	1.01	3.15	4.35	-0.03	1.91	12.81	2.43	0.57	0.96	4.27
12. Bengkulu	3.10	-0.85	2.39	5.98	0.64	2.94	14.06	0.10	1.32	1.23	3.76
13. Bandar Lampung	2.10	-0.60	3.06	4.06	1.04	1.25	13.83	2.49	0.43	0.69	2.31
14. Pangkal Pinang	4.04	2.14	1.46	3.35	1.48	2.58	9.16	3.39	-0.16	2.16	0.93
15. Jakarta	2.79	0.43	1.92	3.00	1.54	1.76	9.05	2.30	0.33	1.21	2.07
16. Tasikmalaya	1.91	0.70	3.11	5.70	1.56	1.96	10.39	1.45	0.99	2.23	3.53
17. Serang/Cilegon	1.47	-0.76	2.56	4.19	1.49	1.68	7.99	2.28	0.86	1.79	2.53
18. Bandung	1.89	0.67	2.22	3.12	1.25	1.73	12.56	1.53	0.57	1.26	1.87
19. Cirebon	1.91	-0.87	1.90	2.99	1.02	1.75	10.35	1.48	-0.12	0.63	4.23
20. Purwokerto	2.99	-0.62	2.38	3.01	0.60	2.39	7.94	2.14	1.36	2.21	2.48
21. Surakarta	2.36	0.14	1.78	2.21	0.84	2.06	8.26	2.43	0.85	0.36	2.41
22. Semarang	1.46	0.78	2.59	3.25	0.93	2.69	8.83	2.03	0.87	1.48	1.57
23. Tegal	2.87	-0.20	2.44	3.69	1.08	2.21	10.52	2.15	0.71	1.48	3.19
24. Yogyakarta	1.93	1.36	2.66	2.30	1.43	3.05	7.53	2.54	2.54	2.52	2.42
25. Jember	2.24	0.25	2.88	2.96	1.11	3.26	8.71	1.78	1.52	0.70	2.68
26. Kediri	1.34	0.21	3.43	3.06	0.65	1.71	10.74	2.48	1.19	0.80	3.11
27. Malang	2.34	0.59	2.43	2.35	1.26	2.47	8.98	2.17	1.27	0.60	1.76
28. Surabaya	1.80	0.37	2.90	2.63	0.88	1.92	8.15	2.15	0.99	0.81	2.61
29. Denpasar	1.87	-0.67	3.00	2.94	-0.17	1.84	6.35	2.44	0.56	-0.12	1.37
30. Mataram	1.46	-0.90	3.79	3.21	0.94	1.39	11.44	1.63	0.61	-0.05	1.93
31. Kupang	2.05	0.63	2.41	4.69	-1.16	0.94	10.27	4.81	0.46	0.86	3.32
32. Pontianak	1.60	1.52	1.54	2.44	1.37	1.32	8.76	2.19	0.98	1.72	1.29
33. Sampit	1.94	0.41	3.09	1.71	-1.01	2.48	8.45	1.59	3.94	0.30	1.74
34. Palangkaraya	3.37	-0.18	3.01	1.52	-0.91	1.58	9.73	0.49	3.68	-0.52	3.94
35. Banjarmasin	3.33	3.00	2.96	0.88	0.19	2.65	8.86	1.31	6.15	0.10	3.14
36. Balikpapan	1.95	0.98	3.39	3.88	1.60	1.80	9.15	2.53	1.90	-0.06	1.05
37. Samarinda	2.45	1.10	1.83	3.28	1.91	1.12	9.59	1.43	1.87	2.44	0.61
38. Manado	0.79	0.41	2.60	3.84	0.14	2.88	10.98	1.52	0.05	2.15	1.29
39. Palu	2.15	1.11	4.99	2.39	1.03	3.36	8.80	2.54	2.92	1.23	1.74
40. Ujung Pandang	1.39	0.61	3.52	2.76	0.60	1.87	9.39	2.79	2.01	1.58	0.66
41. Kendari	2.56	-1.54	5.26	5.42	2.47	-0.03	12.46	1.93	3.12	2.29	2.97
42. Gorontalo	1.36	-0.10	3.12	3.24	0.02	0.54	14.20	2.56	-0.99	2.34	3.48
43. Ambon	2.76	-0.16	2.42	1.70	1.07	1.93	11.36	0.96	3.00	-0.47	1.25
44. Ternate	1.17	-0.53	4.28	6.09	-2.65	4.30	10.87	2.54	-0.04	0.82	1.72
45. Jayapura	3.84	0.30	2.82	1.67	2.32	1.13	8.50	2.85	2.47	1.57	2.31
NASIONAL	2.35	0.49	2.51	3.19	1.05	2.03	10.08	1.98	0.87	1.16	2.44

Notes :

1. Calculated based on 2002 cost of living survey from 44 cities (2002=100)

Sources: BPS-Statistic Indonesia (processed)

Table 9
Percentage Changes of Wholesale Price Index
 (Percentage) ¹⁾

End of Period	Agriculture	Mining	Industry	Import	Export			General
					Total	Non oil/gas	Oil/gas	
2003								
Qtr.I	-1.27	0.68	1.62	3.34	2.92	0.23	10.75	1.75
Qtr.II	-0.34	0.59	0.02	-6.04	-8.54	-4.12	-20.17	-3.12
Qtr.III	0.62	-3.34	0.12	2.31	3.66	2.57	7.08	1.28
Qtr.IV	2.54	0.77	1.10	3.01	2.57	0.86	7.72	1.97
2004								
Qtr.I	1.26	9.77	1.18	3.10	3.91	2.90	6.75	2.35
Qtr.II	3.20	1.55	2.34	6.67	7.32	2.26	21.16	4.37
Qtr.III	-1.29	0.35	0.60	3.41	4.68	0.89	13.39	1.80
Qtr.IV	1.84	1.02	0.52	0.34	-1.48	2.42	-9.47	0.18
2005								
Qtr.I	3.80	3.00	8.04	9.11	10.73	4.61	24.20	8.02
Qtr.II	0.00	0.70	1.34	0.69	1.43	0.00	5.13	1.38
Qtr.III	2.76	0.70	1.32	6.85	9.15	3.28	20.49	4.08
Qtr.IV	4.03	13.19	22.22	0.64	-3.87	2.38	-13.77	9.15
2005								
Qtr.I	3.87	0.61	1.60	-0.64	-1.34	-4.65	3.29	-1.20
Qtr.II	4.97	1.83	2.11	5.13	8.84	6.50	13.64	4.85
Qtr.III	5.33	2.40	2.58	0.61	0.00	2.29	-3.60	2.31
Qtr.IV*	3.93	2.34	0.50	0.00	-5.63	0.00	-16.60	-1.13

Notes :

1. Calculated based on 2002 cost of living survey from 44 cities (2002=100)

*) November 2006

Sources : BPS-Statistic (processed)