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BANK INDONESIA

VISION

To be a credible institution and the best central bank in the region by strengthening the strategic values held as well as through the achievement of low inflation along with a stable exchange rate.

MISSION

To achieve rupiah exchange rate stability and maintain the efficacy of monetary policy transmission in order to drive quality economic growth.

To nurture an effective and efficient national financial system that can withstand internal and external shocks in order to support the allocation of funding/ financing that contributes to national economic stability and growth.

To ensure a secure, efficient and smooth payment system that contributes to the domestic economy and helps maintain monetary as well as financial system stability whilst broadening access in the national interest.

To build and maintain the organisation and human resources of Bank Indonesia, who are performance based and honour integrity, as well as to enforce good corporate governance in the implementation of tasks as mandated in prevailing laws.

STRATEGIC VALUES

The values that form the basis of Bank Indonesia, the management and employees to act and or behave, consisting of **Trust and Integrity – Professionalism – Excellence – Public Interest – Coordination and Teamwork**.

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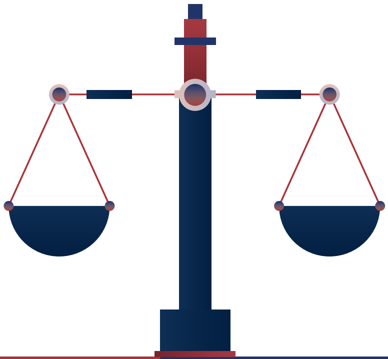

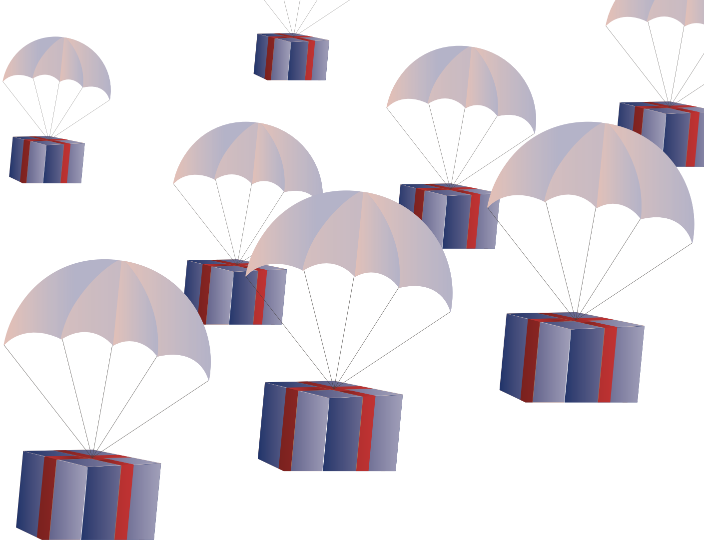

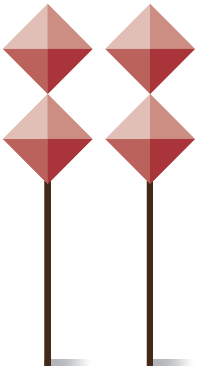

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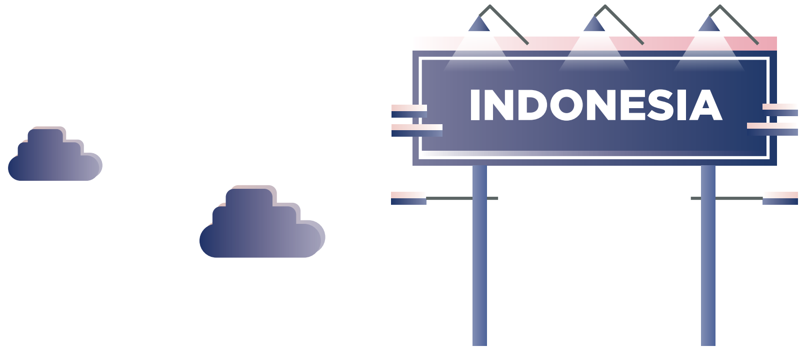
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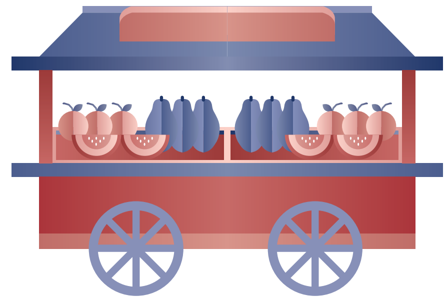

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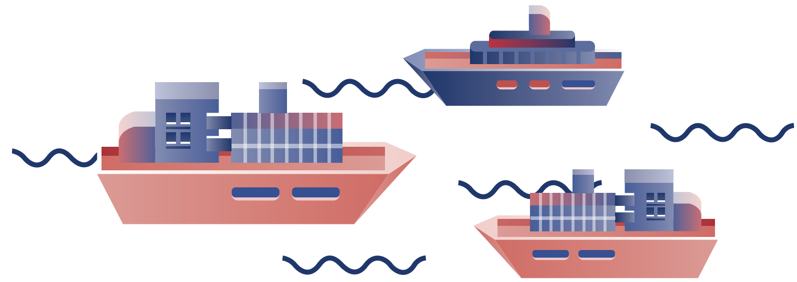

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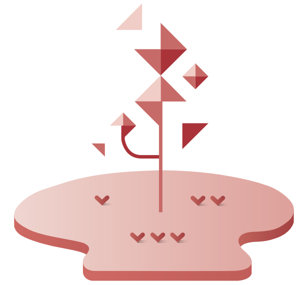

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"With a policy mix implemented on a disciplined, consistent, and measured basis within a synergetic framework for coordination, the Indonesian economy is set to chart more robust, balanced, and sustainable growth for the future"

Agus D. W. Martowardojo
Governor

FOREWORD

The changes in the global economic constellation since the 2008 crisis, with its far-reaching, deeply felt impact, have given birth to new and more complex challenges in managing macroeconomic stability. In 2015, while strenuous efforts continued on many fronts to resolve the various domestic structural problems, Indonesia also had to cope with a series of external shocks in the global economy that impacted the nation through the financial and trade channels. Recovery in the global economy has since disappointed expectations, as it has progressed slowly on a multispeed track and remains fraught with uncertainty. Advanced economies, led by the United States, have mounted a more solid recovery. However, the economies of emerging market countries, led by China, underwent a structural slowdown that sent commodity prices into decline and in turn put sustained pressure on Indonesia's exports. These imbalances in global economic recovery have produced a monetary policy divergence among countries. The monetary policy in the United States has embarked on a period of normalization after six years when interest rates were held at near zero percent. At the same time, Europe, Japan, and emerging markets pursued further relaxation of monetary policy to prevent even greater slowing of economic growth. Deterioration in commodity prices has weighed more heavily on the economic performance of emerging market economies in tandem with uncertainty over the size and speed of interest rate increases in the United States. These two factors were key forces at work in the series of shocks on global financial markets in 2015 that in turn depressed capital flows to emerging markets, including Indonesia.

Indonesia sustained considerable impact from these global economic and financial market dynamics due to an inadequately diversified export structure and heavy dependence on external sources of financing. The structure of Indonesia's exports is more resource-based, and therefore the deterioration in commodity prices had significant impact on exports that in turn has affected performance in various sectors of the economy. Besides this, the substantial import content in export commodities meant that export-oriented industry was poorly positioned to take advantage of rupiah depreciation to boost export performance. On the other hand, lack of development in sources of financing on the domestic financial market has resulted in a high level of dependence on external sources of financing. These sources consist mainly of portfolio capital inflows, which are strongly influenced by global dynamics, and private external debts, which are susceptible to exchange rate fluctuation. If not properly managed, this combination of external and domestic challenges could have disrupted macroeconomic and financial system stability and led to further economic growth slowdown.

In responding to these external and domestic challenges, Bank Indonesia and the Government have strengthened policy synergy with the aim of safeguarding macroeconomic stability and generating momentum for economic growth. Efforts to preserve macroeconomic stability included the steering of inflation to within the 2015 target range of 4±1%, reduction of the current account deficit to a more prudent level, and maintenance of exchange rate stability in keeping with fundamentals. To this end, Bank Indonesia acted consistently and with caution in staying the course with the tight bias monetary policy introduced in mid-2013 until October 2015. This policy was also bolstered by measures to stabilise the exchange rate and thus curb excessive pressure on the rupiah that could have otherwise disrupted the stability of the economy. The implementation of prudent principles in non-bank corporate external debt management has been reinforced to improve business capability in managing risks, in particular those arising from exchange rate fluctuations. At the same time, Bank Indonesia pursued selective relaxation of macroprudential policies while lowering the primary statutory reserve requirement in rupiah to generate momentum for economic recovery. These policies were managed in synergy with the increase in the government economic stimulus commensurate with the opening of fiscal space as a positive effect of the energy subsidy reforms. In the real sector, a sustained drive to accelerate the implementation of structural reforms involved the launching of a series of government policy packages supported by a number of Bank Indonesia policy actions for financial market deepening.

With excellent coordination and synergy in place for monetary, fiscal, and real sector policies, pressure on macroeconomic stability eased and economic growth gained momentum. The achievement of macroeconomic stability was reflected in the subdued inflation of 2015, on track with target, reduction in the current account deficit to a prudent level, the return of capital inflows to the domestic financial market, and more stable movement in the rupiah. Inflation was curbed to within the targeted range of 4±1%. These achievements were supported by the managed domestic demand, well-anchored inflation expectations, and adequate supply of food staples. The current account deficit also came down to about 2.1% of GDP in response to well managed domestic demand. Meanwhile, the capital and financial account saw improvement in the fourth quarter of 2015, bolstered by the easing of turmoil on global financial markets and improving perceptions among market participants of the outlook for the Indonesian economy. Consistent with these developments, the rupiah exchange rate also steadied and even underwent appreciation in the fourth quarter of 2015. As concerns economic growth, the fiscal stimulus launched by the Government and onset of renewed market confidence also created momentum for higher economic growth during the second half of 2015. In 2015, Indonesia stood out as an emerging market that maintained a stable economy with relatively high economic growth compared to other emerging market countries.

The dynamics of the economy in 2015 taught some valuable lessons for reinforcing the principles of policy application in the future management of the Indonesian economy. *First*, macroeconomic policies, both fiscal and monetary, applied in a disciplined, consistent, and timely manner are key to maintaining macroeconomic stability and promoting sustainable economic growth. *Second*, this macroeconomic discipline also needs to be supported by strong policy synergy among policy stakeholders, including Bank Indonesia, the central and regional governments, and other relevant authorities. Appropriate policies combined with strong synergy will not only help the Indonesian economy through the difficult times of shocks, but will also put the economy on the proper footing to gain momentum for growth. *Third*, during recent years, the cycles in the domestic economy have dealt lessons on the importance of implementing structural reforms and diversifying sources of growth in ways that could reinforce the foundations of the economy for greater resilience and sustainable growth. These lessons have become an important resource for dealing with the future dynamics of the world economy, which is predicted to be fraught with even more challenging risks and uncertainties.

Looking forward, the various challenges and risks require proactive measures and well-coordinated policy responses. Regarding the external side, the possibility that the global economy recovery will remain sluggish and imbalance, the continued slowdown in China's economy and the its policy implications for global financial markets, and the deterioration of commodity prices represent the three major risks that need to be mitigated for proper management of their negative impact on macroeconomic stability and economic growth momentum. On the domestic side, the structural reform policies need to be consistently implemented and directed towards raising potential output and improving the productivity and competitiveness of the economy. For this purpose, coordination will be maintained between Bank Indonesia and the Government in implementing synergetic, mutually reinforcing monetary, fiscal, and structural reform policies. Bank Indonesia will implement a policy mix that is consistently directed at safeguarding macroeconomic and financial system stability while taking prudent advantage of room for measured relaxation of monetary and macroprudential policy should various parameters in the economy permit.

With a policy mix of fiscal, monetary, and structural reforms implemented on a disciplined, consistent, and measured basis within a synergetic framework for coordination, the Indonesian economy is set to chart more robust, balanced, and sustainable growth for the future. In 2016, the Indonesian economy is forecasted to grow by 5.2-5.6% with an upward trend over the medium term, commensurate with the expanding capacity of the economy. With greater capacity in the economy, inflation is projected within the target range of 4±1% for 2016-2016 and 3.5±1% for the medium term. In view of the improved structure of the economy and more diversified sources of economic growth, current account deficit is forecasted be maintained at a safe level with more sound structure.

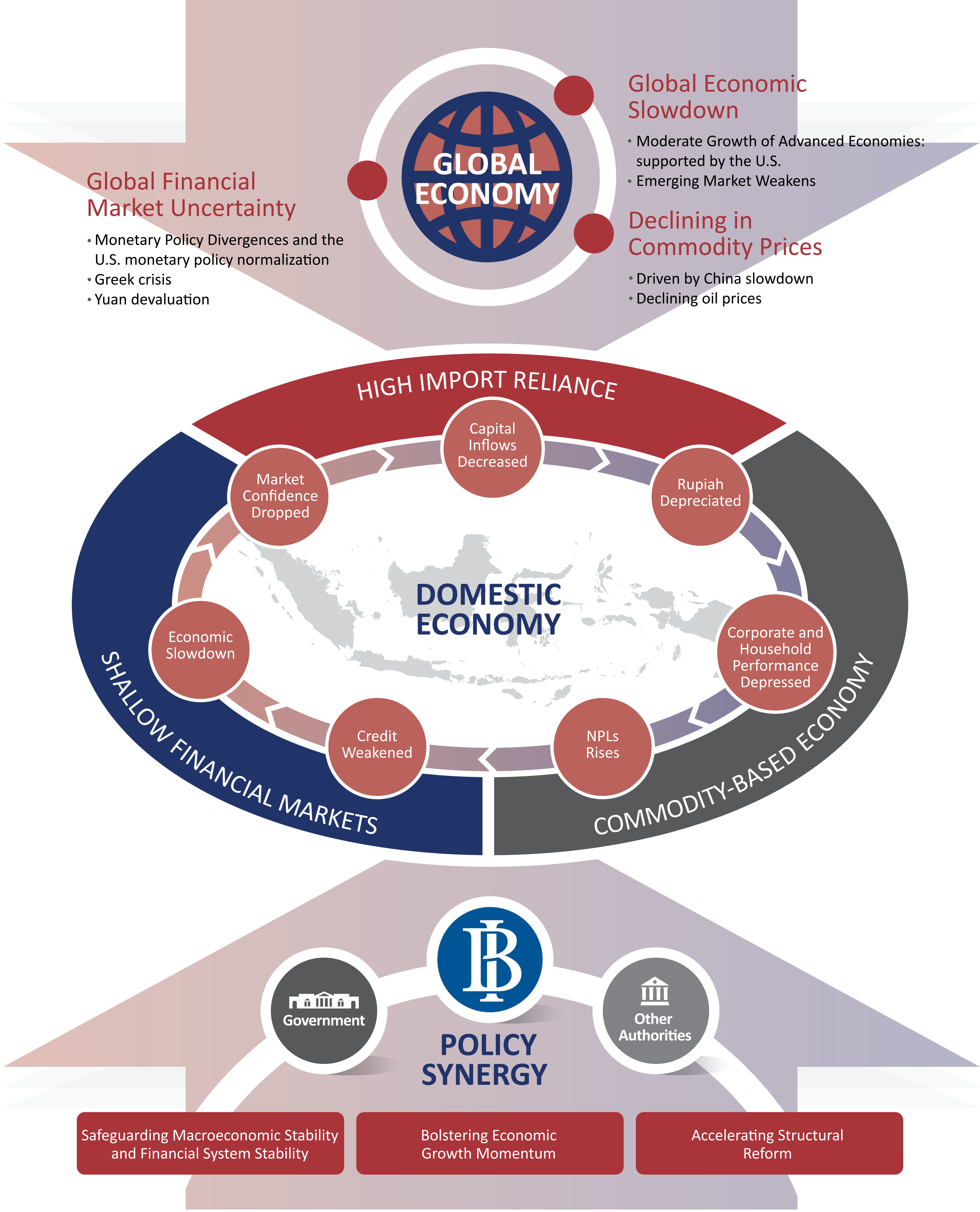
A more in-depth discussion and description of the dynamics of the economy in 2015, the various policy responses put in place, the thrust of policy, and the economic outlook is presented in this book, the Economic Report on Indonesia 2015. This book presents the linkages between global economic dynamics and the Indonesian economy and the underlying thinking of the various policies undertaken by Bank Indonesia and the Government during 2015. In reading this book, the reader is also expected to gain a comprehensive view of the roles of Bank Indonesia, the Government, and other relevant authorities in steering the Indonesian economy through the turbulence from the shocks during 2015. It is also hoped that readers will derive valuable lessons from the journey of the economy in 2015, which we are convinced are of great relevance to the future work for improving the economy. Our belief is that nothing in the journey of a nation's economy happens by accident. Our ability to learn lessons from the past will determine the future that we will be able to shape in the economy.

Finally, on behalf of the Board of Governors of Bank Indonesia, I would like to present the Economic Report on Indonesia 2015 to the public of Indonesia. Our hope is that this book will carry forward the LPI tradition of serving as a leading quality and trusted reference for developing the steps that we will take forward for building a better economy.

May God the Almighty never fail to bestow His blessing in every step of our endeavours in presenting the best work for our beloved nation, Indonesia.

Jakarta, March 2016
Governor of Bank Indonesia

Agus D. W. Martowardojo


GLOBAL ECONOMY
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NPLs Rises
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Economic Slowdown
Market Confidence Dropped
Government
Other Authorities
POLICY SYNERGY
Safeguarding Macroeconomic Stability and Financial System Stability
Bolstering Economic Growth Momentum
Accelerating Structural Reform

GENERAL REVIEW

Synergy in Safeguarding Stability, Realizing Structural Reforms

The Indonesian economy marked a year of positive performance in 2015. Macroeconomic stability improved while economic growth began to gather momentum. Greater macroeconomic stability was reflected in achievement of the 4±1% inflation target for 2015, amelioration in the current account deficit to a more prudent level, subdued pressure on the rupiah from the fourth quarter of 2015, and continued financial system stability. The onset of renewed economic growth momentum was marked by economic growth that began improving in the second half of 2015.

These positive developments represented no easy achievement. A considerable array of external and domestic challenges daunted the Indonesian economy during 2015. World economic growth fell short of earlier projections. At the same time, there was mounting uncertainty in global financial markets from the growing possibility of increases in U.S. interest rates and concerns over the fiscal negotiations with Greece, all of which was worsened by a surprise devaluation of the yuan. These adverse global developments negatively impacted the domestic economy through the trading and financial channels. This pressure bearing down on the domestic economy was compounded by long-standing domestic structural problems. These challenges exacerbated a number of risks such as the heightened pressure on the rupiah, diminishing confidence of economic agents, and escalating risks in the corporate sector. In the absence of proper management, these conditions could have led to mounting macroeconomic instability and further weakening of economic growth.

In response to these multifaceted challenges, Bank Indonesia and the Government reinforced policy synergy to safeguard macroeconomic stability, stimulate economic growth and accelerate structural reforms. Macroeconomic stability was successfully managed with the aid of the tight bias monetary policy in place until October 2015 and the exchange rate stabilization package. At the same time, Bank Indonesia pursued selective relaxation of macroprudential policies in a drive to create momentum for economic recovery while lowering the rupiah reserve requirement (RR). In the area of fiscal policy, the enlarged fiscal space created by reform of energy subsidies was harnessed to increase the economic stimulus while maintaining fiscal sustainability. In the real sector, efforts were continued to speed up the implementation of structural reforms with the launching of a series of government policy packages. This coordination of monetary, fiscal, and real sector policies proved successful in managing the economy. Pressure on macroeconomic stability eased and momentum for economic growth was created.

Looking forward, the Indonesian economy is predicted to chart steady improvement accompanied by stronger fundamentals. The forecast is for higher economic growth alongside prudently managed macroeconomic stability. The progressive easing of global financial markets uncertainties in response to the narrowing monetary policy divergence among advanced countries is expected to reduce pressures on macroeconomic stability, and in particular on exchange rate stability. Meanwhile, the forecast is for higher economic growth driven by government action to accelerate the fiscal stimulus and implementation of structural reforms. It is expected that the sustained momentum for strengthening the economy will bolster optimism for the economic outlook and encourage foreign capital inflows that in turn will ease pressure on macroeconomic stability.

A close watch will need to be kept on looming challenges that include the downturn in the global economy, uncertainty in China's financial markets and further decline in prices of commodities including oil. Besides this, work is still needed to tackle a number of unresolved domestic structural problems. To this end, there will be further strengthening of the already solid coordination between Bank Indonesia and the Government. On Bank Indonesia's part, the policy mix will continue to aim at safeguarding macroeconomic and financial system stability as well as making prudent use of room for monetary and macroprudential policies relaxation. From the Government side, policy will be directed at further strengthening of economic growth momentum while accelerating the pace of structural reforms. With this strong synergy, it will be possible to safeguard macroeconomic and financial system stability and thus enable sustainable economic growth to be achieved in the medium and long-term.

Challenges to the Indonesian Economy and Performance in 2015

While facing a broad array of challenges, the Indonesian economy marked a year of positive performance in 2015. Attesting to this was steady improvement in macroeconomic stability and the onset of renewed momentum for economic growth. Improvement in macroeconomic stability was reflected in achievement of the 4±1% inflation target for 2015, reduction in the current account deficit to a more prudent level, subdued pressure on the rupiah commencing from the fourth quarter of 2015, and continued financial system stability. After having undergone a slowing trend, economic growth began to edge upwards during the second half of 2015. This positive achievement owes much to the policy synergy of Bank Indonesia and the Government for safeguarding macroeconomic and financial system stability and promoting economic growth.

Efforts to maintain macroeconomic stability and to generate momentum for economic growth faced a range of daunting challenges. From the global perspective, challenges were posed by flagging world economic growth, the widening divergence over monetary policy among advanced countries and rising uncertainty on global financial markets. The lingering weakness of global economic growth has led to a prolonged decline in world oil prices and non-oil and gas commodity prices. At the same time, differences among developing nations in the phases of economic recovery fuelled expectations of widening divergence over monetary policy. Economic growth in the United States, which is expected to keep rising, fuelled expectations of interest rate increases. However, other countries such as Japan, the EU nations, and emerging markets with flagging growth are expected to stay the course with loose monetary policy. The divergence in monetary policy was exacerbated by the considerable uncertainty over when and to what extent the U.S. will raise interest rates, concerns over the fiscal negotiations with Greece, and uncertainty on China's financial markets, including the yuan devaluation. Despite this, uncertainty on global financial markets began to ease in the fourth quarter of 2015 in line with positive sentiment in October 2015, kindled by the likelihood that increases in the Federal Funds Rate (FFR) would be deferred and the normalisation process would take place gradually.

On the domestic front, challenges were closely linked to the various structural issues that have yet to be resolved. The leading structural issue in the real sector has arisen from an economic structure still built on commodities. Due to lack of diversification of sources of domestic economic growth, falling global commodity prices not only adversely affect the commodities sector, but also have repercussions on non-commodity sectors. Second, the high import content of Indonesia's export leaves little flexibility for exports to adjust to movements in the rupiah exchange rate, diminishing the positive effect of rupiah depreciation in bolstering Indonesia's exports. In the financial sector, the main source of structural problems lies in the shallow domestic financial market. Shocks on global financial markets that adversely impacted foreign capital inflows in Indonesia could not be properly absorbed by the still shallow domestic financial market, resulting in comparatively high market volatility. In addition, the shallowness of Indonesia's financial market has created quite high levels of corporate dependence on external financing. Due to this dependence, corporate performance is susceptible to changes in the global environment.

Uncertainty in global financial markets led to depreciation in the rupiah exchange rate during 2015. Pressure bore down on the rupiah from the first quarter and reached a peak in the third quarter of 2015. Fuelling this pressure were heightened uncertainties on global financial markets related to uncertainty over increases in the FFR, fears over fiscal negotiations with Greece, and the devaluation of the yuan. On the domestic front, pressure bore down on the rupiah from concerns over the weakening outlook for the domestic economy. In other areas, the shallow domestic foreign exchange market and corporate dependence on external financing amplified the impact of external pressure on the rupiah. Despite this, pressure for depreciation began to ease and the rupiah even appreciated during the fourth quarter of 2015. Key to this was the increase in foreign capital inflows in line with the easing of uncertainty in global financial markets. On the domestic side, amelioration of pressure on the rupiah was supported mainly by the policy actions pursued by Bank Indonesia for stabilising the exchange rate and positive investor perceptions for the outlook of the domestic economy. For the year of 2015, the rupiah recorded depreciation of 10.2% (yoy), less than that of currencies of some peer countries.

In 2015, Indonesia's balance of payments recorded a deficit despite the significant improvement that took place in the current account deficit, which came down from 3.1% of GDP in 2014 to 2.1% of GDP. This easing of the current account deficit is explained by several factors. First, falling oil prices brought improvement in the oil and gas balance. Second, non-oil and gas imports declined in keeping with weakening demand in the domestic economy and for non-oil and gas exports. Third, the declining imports due to depreciation in the rupiah exchange rate. Meanwhile, in the capital and financial account,reduced capital inflows in response to global uncertainties led to a deficit in the Indonesia balance of payments for the year of 2015. Nevertheless, the easing of uncertainties on global financial markets and improving confidence in the outlook for the domestic economy from the fourth quarter of 2015 prompted a significant rise in capital inflows bolstered mainly by higher portfolio investment inflows in government bonds and foreign direct investment (FDI). In line with the increased surplus in the capital and financial account, Indonesia's balance of payments posted a respectable surplus in the fourth quarter of 2015.

Inflation in 2015 reached 3.35% (yoy), within the 2015 inflation target range of 4±1%. The subdued inflation in 2015 is attributed to global and domestic factors. On the global side, plunging world oil prices created opportunity for the Government to lower domestic prices for fuel and 12 kg bottled LPG gas as well as reduce electricity billing rates. Second, the decline in global commodity prices, including prices of food staples, also kept volatile foods inflation in check. On the domestic front, despite the weakening of the rupiah, there was only limited exchange rate pass-through to inflation. Key to this was domestic demand that was kept within manageable levels alongside low imported inflation. Second, volatile foods inflation was quite subdued in 2015 albeit in the midst of the El Nino phenomenon. The subdued volatile foods inflation was in line with the intensified coordination between the Government and Bank Indonesia in increasing production, improving distribution, and minimising various price distortions for staple foods. As a result, core inflation in 2015 reached only 3.95% (yoy) and administered prices inflation recorded only 0.39% (yoy), while volatile foods inflation came to 4.84% (yoy).

In the real sector, Indonesia regained momentum for recovery during the second half of 2015. After continuing the trend of the economic slowdown that began in 2012 in tandem with the flagging global economy, the Indonesian economy managed a turnaround in the second half of 2015, bolstered by improvement in domestic demand. Government consumption mounted significantly in line with high absorption of budget expenditures. Improvement was also visible in investment, driven mainly by increased government capital expenditures and stronger investment growth in some high-growth sectors, including the automotive industry and construction. At the household level, buoyant consumer confidence helped household consumption to maintain relatively stable, resilient growth. Overall, economic growth in 2015 slowed from 5.02% in 2014 to 4.79%. However, it should be noted that this still represents fairly strong performance compared to other nations with commodity-based economies. This attests to the considerable flexibility of the domestic economy in coping with the global economic slowdown, such as in 2009 at the time of the global financial crisis. The geographical diversification of Indonesia's economic growth has now begun. Java, which has a manufacturing-based economy generating high value added, maintained buoyant growth. In so doing, it was able to compensate for flagging performance outside Java, where growth has suffered from the impact of weakening commodity prices.

In the financial sector, financial system stability remained sound amid escalating risks arising from uncertainties in global financial markets. The banking industry remains resilient as reflected in prudent levels of credit risk and liquidity risk, high profitability, and robust capital adequacy. Credit risk is at the low end of the scale despite an upward trend due to deterioration in corporates' ability to repay debt following the decline in corporate revenues. This was reflected in a rise in non-performing loans (NPLs), albeit within safe limits. Decline in corporate revenues and household incomes also contributed to weaker growth in bank deposits, causing liquidity risk to climb. Liquidity risk, while rising, stayed within safe levels with the ratio of liquid instruments to bank deposits well below the prudent threshold. As regards bank intermediation, credit growth maintained a downward trend at only 10.4% due to weaker performance in both supply and demand as banks tightened lending standards in response to rising NPLs. To address this concern, Bank Indonesia relaxed macroprudential policy to create room for improvement on the supply side for credit. Lack of recovery in the intermediation function and mounting credit risk caused bank profitability levels to fall. Nevertheless, reduced bank profitability had no significant impact on bank resilience given that profitability remained high compared to other countries in the region, while capital adequacy also remained strong. This was confirmed by results of stress testing of credit risk and market risk which indicate that the Indonesian banking system has high levels of capital resilience for coping with worst-case scenarios.

Performance improved further in the payment system during 2015. On the part of Bank Indonesia, the improving performance was reflected in system reliability and availability and the implementation of effective contingency plans. In the meantime, no significant disruptions took place among operators in the industry-operated payment system. Measured by transaction volume, growth climbed from 18% to 19% in 2015. The increase took place mainly in the payment system operated by the industry, involving card-based payment instruments and electronic money. This was consistent with the payment instrument electronification program carried out with the (GNNT) and Government policy for using electronic money for disbursing social assistance with the aid of electronic money. The success of this payment instrument electronification program was reflected in the increased ratio of card-based payment instruments to GDP, indicating an improvement in public preferences for use of non-cash payments. In the cash payment system front, more reliable performance was achieved in rupiah cash management with the support of rupiah cash management policy. This policy for rupiah cash management was implemented with development of a cash distribution network and cash services provided by cash custodian, an adequate cash position at Bank Indonesia, and improvement in the quality of cash in circulation through the clean money policy.

Policy Response in 2015

During 2015, the economy was daunted by three major challenges that required astute handling. The first challenge was to safeguard macroeconomic and financial system stability amid the heightened uncertainty on global financial markets. These uncertainties arose primarily from uncertainty over normalisation of the interest rate policy of the United States, fears over the fiscal negotiations with Greece and the unexpected devaluation of the yuan. These uncertainties led to a strong downward pressure on the rupiah that had to be managed carefully to avoid repercussions for macroeconomic stability. The second challenge was to bolster slow growth in a domestic economy due to the effects of flagging growth in the global economy. There was a need to mitigate the potential for prolonged slowdown in domestic economic growth in order to maintain positive sentiment for the outlook for the domestic economy. In view of the prolonged slowdown in global economic growth, efforts to bolster economic growth by stimulating domestic demand would be the key to the economic recovery process in the short-term. The third challenge was to accelerate the implementation of structural reforms. The various structural problems in the domestic economy have escalated the negative impact of external shocks on both Indonesia's macroeconomic stability and economic growth. It was therefore vital to accelerate the implementation of structural reforms in order to reinforce the foundations of the Indonesian economy as a basis for creating sustainable economic growth.

To address these challenges to the economy, policy synergy was continuously strengthened in macroeconomic management. Bank Indonesia's policy mix focused on measures to safeguard macroeconomic and financial system stability. This policy mix was also enhanced by close coordination between Bank Indonesia, the central and regional governments, and other stakeholders. Bank Indonesia also sought to generate momentum for stronger economic growth by introducing a number of accommodative macroprudential policies. These policies were implemented in synergy with an increased fiscal stimulus by the Government to accelerate the process for recovery of economic growth. In addition, the Government and Bank Indonesia worked tirelessly to strengthen coordination in accelerating the pace of structural reforms. Within this context, the Government launched the economic policy packages I-VIII, a series of policies aimed at increasing the pace of improvements to infrastructure and building greater domestic economy's competitiveness. The Government's efforts to accelerate structural reforms were also supported by Bank Indonesia policies aimed at increasing resilience and efficiency in the domestic economy.

On the part of Bank Indonesia, the measures for safeguarding macroeconomic stability focused on bringing inflation back to within the target range, curbing the current account deficit to a more prudent level, and managing the stability of the rupiah exchange rate. Against this background, Bank Indonesia worked throughout 2015 to strengthen the monetary policy mix through policy actions involving interest rates, the exchange rate, monetary operations, foreign exchange flows, and strengthening of the buffer of international reserves. At the same time, Bank Indonesia undertook a selective relaxation of macroprudential policies and lowered the primary reserve requirement aimed at bolstering the momentum for economic growth. This relaxation sought to expand capacity for bank financing by providing additional liquidity to boost lending. The relaxation on macroprudential and monetary policies involved measured actions that took into account their impacts on financial system stability. In a drive to support structural reform, Bank Indonesia took further measures for deepening of the financial market, upscaling of financial inclusion, and strengthening of the payment system. Financial market deepening was directed at creating a resilient and efficient financial market. Alongside this, policy for financial inclusion sought to improve access to economic financing. Meanwhile, payment system policy focused on strengthening the payment system infrastructure in order to be a secure, reliable, and efficient payment system with the requisite capacity to support an efficient economy.

The continued thrust of interest rate policy was on achievement of the inflation target, reduction of the current account deficit, and safeguarding exchange rate stability. Regarding inflation, the tight bias interest rate policy sought to manage inflation expectations and domestic demand in order to bring down inflation quickly to the target range of 4±1%. With inflation expectations still running high in early 2015, Bank Indonesia kept the BI Rate unchanged at 7.75% in January 2015. In February 2015, BI normalized BI Rate back to the level before the increase of BI Rate in November 2014. This normalization took place by lowering the BI Rate by 25 bps after assessing that projected inflation at the end of 2015 would return to the target. Bank Indonesia subsequently held the BI Rate steady at 7.50% until the end of 2015. In the BI assessment on one hand, the interest rate at the prescribed level was still commensurate with efforts to curb domestic demand and imports in order to bring down the current account deficit to a more prudent level. The reduction in the current account deficit in turn reduced domestic demand for foreign currencies. On the other hand, BI also regarded the prescribed interest rate as sufficiently competitive to attract a greater supply of foreign currency, mainly through foreign capital inflows. This combination was expected to relieve excessive downward pressure on the rupiah fuelled by mounting uncertainties on global financial markets. The interest rate policy proved effective in safeguarding macroeconomic stability as reflected in inflation held to within the 2015 inflation target range of 4±1%, a reduction in the current account deficit to about 2% of GDP, and the strengthening of the rupiah during the fourth quarter of 2015.

Exchange rate policy is focused on maintaining the stability of rupiah exchange rate consistent with the fundamentals. The escalation of external and domestic risks followed by deterioration in market sentiment triggered significant downward pressure on the rupiah, particularly in the second and third quarters of 2015. The steeper depreciation in the rupiah stoked expectations of exchange rate loss that subsequently led to excessive depreciation with the rupiah even falling to a low of Rp14,700 per U.S. dollar. In response to this, Bank Indonesia took action to stabilize the exchange rate and thus mitigating fallout from further weakening in the rupiah. On 9 September 2015, Bank Indonesia launched a short-term exchange rate stabilization package built on three strategic pillars. First, safeguarding the rupiah exchange rate stability; second, strengthening the management of rupiah liquidity, including the term structure of monetary operation instruments; and third, reinforcing the management of foreign exchange supply and demand. To bolster the effectiveness of the exchange rate stabilization policy in coping with the pessimistic expectations of depreciation, Bank Indonesia announced another exchange rate stabilization package on 30 September 2015. This policy package includes strengthening of the forward market by implementing forward interventions and relaxing the threshold on forward selling transactions, as well as the launching of new instruments for monetary operations in order to optimize rupiah liquidity management. The exchange rate stabilization package launched by Bank Indonesia and supported by the policy for mandatory use of the rupiah and a series of Government economic policy packages succeeded in curbing excessive fluctuation in the rupiah, as demonstrated by the appreciation recorded in the fourth quarter of 2015.

The policy for strengthening monetary operations sought to improve the effectiveness of these operations in support of stabilising the rupiah exchange rate. As part of the exchange rate stabilization package, Bank Indonesia launched a series of actions to bolster rupiah and foreign exchange monetary operations. A strategy for strengthening rupiah monetary operations (MOs) was implemented by means of adjustments in auction pricing in open market operations (OMOs) and extension of the tenors of MO instruments. The adjustment in OMO auction pricing was introduced through a change in the OMO auction mechanism from variable rate tender to fixed rate tender. Meanwhile, MO instrument tenors were extended by issuing new longer-tenor MO instruments: the Indonesian Government Bond Reverse Repo (RR SBN) in the 2-week tenor, SDBIs in 3 to 6-month tenors, and renewed issuance of SBIs in 9 to 12-month tenors. Regarding the strengthening of foreign exchange MOs, Bank Indonesia introduced changes in pricing, extension of the tenor of foreign exchange MO instruments up to 3 months, optimization of FX swaps, issuance of a regulation on forward auctions by Bank Indonesia, and issuance of foreign currency Bank Indonesia Securities. The success of consistency of measures taken by Bank Indonesia to strengthen monetary operations in 2015 was reflected in the improved duration of monetary operations and the stability of the rupiah.

Efforts to stabilize the rupiah were also supported by a policy for management of foreign exchange flows aimed at reinforcing the management of domestic foreign exchange supply and demand. Exacerbating the tendency for net demand on the domestic foreign exchange market was the diminishing foreign exchange supply during 2015 caused by lack of recovery in exports and reduced conversion of export proceeds. This also rendered the rupiah more vulnerable to external shocks. Within this context, Bank Indonesia introduced several policies aimed mainly at bolstering foreign exchange supply and information on foreign exchange flows. On the supply side, Bank Indonesia reduced the minimum holding period (MHP) for 1-month SBIs to 1 week in order to increase the supply of foreign currency from non-residents. The shortening of the MHP improved flexibility for investors in SBIs and was expected to boost interest among non-residents in investing capital in Indonesia. Concerning export proceeds, the Government introduced an incentive in coordination with Bank Indonesia for progressive reduction in the tax on deposit interest for exporters holding export proceeds in Indonesian banks or converting these funds into rupiah. This policy enabled fixed term deposits in Indonesia to generate competitive returns, with the expectation that this would attract higher inflows of non-resident capital that had previously been parked abroad. Regarding information on foreign exchange flows, Bank Indonesia introduced more stringent reporting requirements. Among others, parties conducting foreign exchange flows were required to enclose certain documents with their reports if transactions exceeded a specified threshold.

In addition, Bank Indonesia took further measures to strengthen the resilience of the domestic economy by bolstering the second line of defense for international reserves through collaboration with other central banks. Various episodes of exchange rate turbulence pointed to the necessity of continuing efforts to reinforce international reserves, even though reserves remained above the safe limit throughout 2015. To this end, Bank Indonesia and the governors of other ASEAN central banks extended the 2 billion U.S. dollar ASEAN Swap Arrangement (ASA) in 2015. The ASA can be used to help meet the short-term liquidity needs of member countries experiencing pressure in the balance of payments. In addition, Bank Indonesia entered into a 10 billion Australian dollar BCSA arrangement with the Reserve Bank of Australia to promote bilateral trade and underwrite the settlement of trade transactions in the local currencies of the two nations. The implementation of bilateral currency cooperation will ease the dependence on the U.S. dollar currency and thus support rupiah stability.

The greater stability in macroeconomic conditions since the fourth quarter of 2015 opened the possibility for monetary policy easing by lowering the primary reserve requirement in rupiah. On one hand, the measured monetary policy easing was consistent with the steady decline in inflation that was on track with the target range. On the other hand, the monetary policy relaxation would prevent further loss of domestic economic growth that would potentially escalate risks and macroeconomic instability for Indonesia. Despite the available headroom for monetary policy easing, the high exchange rate risk related to the possibility of an increase in the FFR compelled Bank Indonesia to exercise caution in selecting instruments for monetary policy easing. Bank Indonesia viewed that policy instruments other than interest rates could be deployed to benefit from the room for monetary policy relaxation. For this reason, Bank Indonesia lowered the Rupiah Reserve Requirement in November 2015 by 0.5% to 7.50%, effective from 1 December 2015. The relaxing of the reserve requirement was envisaged as a move that would expand bank financing capacity in support of economic activity, which began to improve in the third quarter of 2015.

Bank Indonesia managed the macroeconomic stabilization policy in synergy with the relaxation of macroprudential policies in order to create positive momentum for economic growth and to maintain financial system stability. At the end of 2014, as an anticipatory measure to cope with the outlook for slowing economic growth, Bank Indonesia designed more accommodative macroprudential policies for 2015. This accommodative macroprudential policy design was implemented by easing the Loan/Financing to Value Ratio (LTV/FTV) for property credit or financing and the down payment requirement for motor vehicle credit or financing. Bank Indonesia also encouraged banks to issue securities that would be included in the calculation of the Loan to Funding Ratio to replace the Loan to Deposit Ratio. This macroprudential policy relaxation sought to bolster bank capacity to provide financing in support of economic growth. In addition, Bank Indonesia launched an incentive mechanism for Micro, Small, and Medium Enterprises (MSMEs) to promote lending to MSMEs while continuing to uphold prudential principles. Additional support for Bank Indonesia's measures to bolster the MSMEs sector came from the strategy of Bank Indonesia to promote MSMEs development by expanding and deepening the financial infrastructure and through capacity building for MSMEs. Regarding the financial system stability, Bank Indonesia in coordination with the Financial Services Authority conducted examinations of some banks and performing stress tests to assess the resilience of bank capital and liquidity under conditions of rupiah depreciation.

For the payment system, the thrust of Bank Indonesia policy is to strengthen the payment system infrastructure and expand the use of non-cash instruments for the purpose of ensuring the smooth operation of the payment system. In response to the growing demand for transactions conducted through the payment system and to advancements in technology, Bank Indonesia has worked consistently to strengthen the payment system infrastructure for both large value and retail transactions. These improvements to the infrastructure are designed to ensure a secure, reliable, and efficient payment system. In the large value payment system, Bank Indonesia launched the second generation of the BI-RTGS, the BI-SSSS, and the BI-ETP, which provides more rapid and secure settlement of transactions. In the retail payment system, Bank Indonesia implemented the second generation of the Bank Indonesia National Clearing System with capability for more rapid transaction processing and providing more robust consumer protection. Regarding the development of non-cash instruments, Bank Indonesia continued the initial work on development of the National Payment Gateway (NPG) that will become the point of linkage for the various electronic retail providers in Indonesia, and thus improve efficiency. These policies have also been supported by measures to improve financial literacy under the Digital Financial Services program and preparation of the electronification roadmap to support the success of the GNNT. As part of the policy mix for maintaining stability of the rupiah, Bank Indonesia introduced mandatory use of the rupiah in the territory of the Republic of Indonesia in order to curb domestic demand for foreign currency.

In the area of rupiah cash management, Bank Indonesia reformed cash distribution and cash services to meet rupiah cash needs in support of the smooth operation of cash transactions in all areas of Indonesia. In this regard, Bank Indonesia launched five policies for rupiah cash management to provide assurance of the timely availability of rupiah cash in adequate quantity, proper quality, and appropriate denominations. The first policy was to maintain sufficient cash at all Bank Indonesia offices by holding a National Iron Stock (ISN) at 20% of total currency in circulation and ensuring availability of cash to cover 1.5 months of bank outflows. The second policy was to improve the quality of rupiah cash under the clean money policy by raising the standards for worn currency while increasing the destruction of unfit notes for circulation. The third policy was to reform the cash distribution and cash services network by opening new Bank Indonesia offices to perform the function of rupiah cash management and increase the number of cash custodian banks throughout Indonesia. The fourth policy was to bolster communication on the marks of rupiah authenticity features on a sustained basis, using both direct communication with different groups of society and communication through the electronic media. The fifth policy was to improve prevention and eradication of counterfeiting by enhancing a closer collaboration with the Indonesia National Police and the Attorney General's Office. This collaboration was supported by a laboratory for testing suspected counterfeit money and provision of a reliable information system at the Bank Indonesia Counterfeit Analysis Center (BI-CAC).

To improve policy mix effectiveness, Bank Indonesia worked steadily to strengthen coordination with the Government and other policy stakeholders involved with various aspects of the economy. Coordination was strengthened as part of the framework for managing macroeconomic stability, generating economic growth momentum, and accelerating the implementation of structural reforms. Regarding the safeguarding economic stability, coordination between Bank Indonesia and the Government was intensified to improve the effectiveness of inflation control by bolstering the role of the Inflation Monitoring and Control Team (TPI) and Regional Inflation Monitoring and Control Teams (TPIDs). Bank Indonesia and the Government also embarked on more structural management of inflation with the preparation of an Inflation Control Roadmap for 2015-2018. This roadmap encompasses mapping of inflation issues, recommendations for medium and long-term inflation control, and more specific delineation of the roles of Bank Indonesia, the Central Government, and Local Governments. Reinforcing the Inflation Control Roadmap are redoubled commitments from the regions in maintaining local price stability, accelerated construction of infrastructure and achievement of food sovereignty in the regions. Close coordination was also maintained with the Government in dealing with the excessive downward pressure on the rupiah fuelled by mounting uncertainty on global financial markets. The products of this coordination are the economic policy packages I and II, which include measures to improve management of foreign exchange supply and demand and provision of incentives for domestic retention of export proceeds. In addition, Bank Indonesia collaborated with the Government, the Financial Services Authority and the Indonesian Deposit Insurance Corporation in preparing the Draft Law concerning the Financial Safety Net, which will become the overarching legal umbrella for crisis prevention and resolution. Regarding the payment system, Bank Indonesia worked steadily to strengthen coordination with relevant ministries and other agencies in the provision and expansion of the payment system and smoothly operating, secure, and reliable rupiah cash management.

Closer coordination was also forged between Bank Indonesia and the Government to boost the momentum for economic growth. At the national level, Bank Indonesia pursued action in synergy with the Government's fiscal stimulus by relaxing macroprudential policy. In the meantime, Bank Indonesia also played an active role in as a counterpart of the People's Business Credit Program (KUR) Policy Committee, which included tabling recommendations for development of implementation guidelines and achieving targets for KUR disbursement in planning for 2015. In addition, Bank Indonesia and the Government also cooperated in optimizing business development in the marine and fisheries sectors. This included improvement in access to and outreach of financing for MSMEs. In cooperation at the regional level, efforts were made to harmonize leading sectors that had been mapped into the government planning for development of priority sectors. Within this context, Bank Indonesia made recommendations to local governments about particular sectors with potential and high value added that can be developed to promote regional economic growth, based on assessments of a growth diagnostic exercise.

Coordination between the Government and Bank Indonesia in promoting structural reforms was targeted to strengthen Indonesia's economic fundamentals. The structural reform policies put in place focused on measures to address the root causes of fundamental problems in the Indonesian economy by improving infrastructure, building competitiveness, achieving food, energy, and water security, promoting sustainable development financing, and strengthening the economic inclusion. On the Government part, a series of economic policy packages I-VIII was put in place during 2015 in a move to improve the business climate and accelerate the pace of infrastructure development. To work towards food security, the Government engaged in development and repair of agricultural infrastructure, strengthening of production and post-harvest processes, and restructuring of markets. To support energy security, the Government revamped energy policy in the areas of new energy, renewables and energy conservation, management of oil and natural gas, and provision of electricity supply, while continuing efforts to increase value added from mining products. In the area of water security, the Government promoted equitable and sustainable provision of water for the public. Under a series of policy packages described above, the Government also continued to work towards a more inclusive economy with measures that includes entrepreneurship promotion for beneficiaries of KUR, financing for small and medium enterprises, and improved worker welfare. To accelerate implementation of these structural reforms, Bank Indonesia had developed a common vision with the Central Government and local governments for development of leading sectors in various national coordination forums. During 2015, national coordination forums focused on development in four areas designated as leading priorities: the maritime sector, food, energy infrastructure, as well as industry and tourism.

Bank Indonesia consistently supported the implementation of structural reforms by the Government through the steadfast promotion of financial market deepening and financial inclusiveness. Besides creating a financial market capable of absorbing shocks to the economy, other objectives of financial market deepening were to support for monetary policy effectiveness, financial system stability, and easy access to financing. Bank Indonesia pursued measures for financial market deepening by expanding the scope of market participants, adding to the variety of financial market instruments and promoting efficient price formation. In this context, Bank Indonesia issued the financial market deepening blueprint that outlines five strategies: development of instruments and the investor base, more robust regulation and standards, development of infrastructure, institution building, along with effective education and dissemination. The financial market blueprint, equipped with these strategies, will serve as guidance for development of the rupiah and foreign exchange money markets, the sharia-compliant financial market, and the bond market. Meanwhile, for the public and particularly low-income people to gain improved access to financial services, Bank Indonesia continued to play an active role in promoting initiatives for financial inclusion. The Bank Indonesia policy for financial inclusion initiatives focuses on development of digital technology-based innovations to minimise impediments to the public in accessing and making use of financial services while also providing protection to members of the public.

The policy mix consistently applied by Bank Indonesia proved capable of sustaining the performance of Indonesia's economy amid adverse global developments. Reflecting this was prudently managed macroeconomic and financial system stability combined with renewed momentum for economic growth. Improved macroeconomic stability was demonstrated by achievement of the 2015 inflation target of 4±1%, decline in the current account deficit to about 2% of GDP, and stability brought to the rupiah from the fourth quarter of 2015. Regarding financial system stability, the various policies put in place enabled the financial system to maintain resilience in the face of external and internal shocks. In addition, the economy gained renewed momentum for more vibrant growth beginning in mid-2015.

Challenges and Future Policy Direction

The dynamics of the Indonesian economy in 2015 taught some valuable lessons for efforts to create sustainable economic growth for the future. The first lesson that came to light is about the importance of discipline macroeconomic policies, both fiscal and monetary, in ensuring macroeconomic stability and promoting sustainable economic growth. The outcomes for the economy in 2015 showed that a policy mix of tight bias monetary policy and accommodative macroprudential policies combined with a cautious fiscal stimulus was able to keep macroeconomic stability on track without unduly sacrificing economic growth. Second, efforts to boost the momentum for domestic economic growth are crucial in a time of weakening in the global economy and rising uncertainty on global financial markets. Prolonged slowdown in economic growth will lead to build-up of various risks to the economy, including exchange rate risk, corporate risk, and banking risk, that in turn can jeopardize macroeconomic stability. It was therefore necessary for macroeconomic management to be formulated carefully to generate momentum for economic growth without sacrificing macroeconomic stability. Third, a timely implementation of a policy mix is necessary to maximize its effectiveness for the domestic economy. Timing of policy implementation that is consistent with planning is therefore a key to sustaining the performance of the economy in the face of global challenges. Fourth, the complexity of problems daunting the economy points to the need for strong policy synergy among the different policy stakeholders. This includes Bank Indonesia, the central and local governments, and other related authorities. The final lesson is that the dynamics of the global economy, being fraught with uncertainty, reiterates the importance of accelerating structural reforms for strengthening economic foundations and pursuing diversification in order to build a more resilient economy capable of sustainable growth.

Challenges Ahead for the Economy

Looking ahead, the Indonesian economy will continue to face daunting and increasingly complex challenges from developments in the global as well as domestic economy. The main challenge from the global economy stems from the lingering weak growth in the global economy. In the short term, the forecast for advanced economies is continued tepid growth. At the same time, China's economic growth is predicted to slow further, with repercussions for the outlook for recovery in Indonesia. On one hand, the lack of recovery in the global economy will lead to further weakening in global commodity prices, which in turn will put pressure on the current account. On the other hand, the slack pace of economic growth, particularly in advanced nations, will bring about a narrowing in the monetary policy divergence among advanced economies. This will reduce the level of uncertainty on global financial markets and have a positive effect on the capital and financial account. However, prolonged weakness of the economy in China may potentially become a new source of uncertainty on global financial markets. The lingering fragility in Indonesia's external performance calls for further vigilance as this could lead to significant downward pressure on the rupiah and disrupt macroeconomic stability as well as the current momentum for economic growth.

The inauguration of the ASEAN Economic Community (AEC) has potential to raise formidable challenges if proper preparations are not made for this change. The growing integration of the region in the areas of trade, finance, and investment is turning Asia into one of the most important investment venues in the global production system. However, the reduction of barriers to regional trade will pave the way for the domestic economy to be flooded by foreign products with potential to overwhelm domestic products, particularly ones that are less competitive. A similar fate may await the services sector, which portends to become extremely competitive with the launching of the AEC. Domestic economic players therefore need to build their readiness in order to gain benefits from the AEC. Against this backdrop, Indonesia's relatively low position in global value chains compared to its regional neighbours must be corrected so that Indonesia does not merely become a market for the products and services of other countries in the region.

On the domestic side, the Indonesian economy also faces multifaceted domestic structural problems that have not been fully resolved. The structural challenges that must be addressed as priorities are found in four pillars of the fundamentals of the economy: i) food, energy, and water security; ii) competitiveness in the industry, maritime, and tourism sectors; iii) sustainable development financing; and iv) an inclusive economy. Food security is still an urgent issue, particularly when viewed in terms of the limited agricultural productivity and food diversification. Energy security remains vulnerable to shocks, even though Indonesia has vast energy resources potential. Water security is also not sufficiently viable to cope properly with needs in consumption, food crop production, and energy sources. At the same time, despite substantial potential in the maritime sector, challenges persist in territorial integrity, optimising of resource management, and in connectivity. Unlike the maritime sector, competitiveness in industry remains weak due to limited use of technology and the dependence of domestic industry on natural resources. The tourism sector faces impediments with lack of adequate connectivity infrastructure to support access to tourist attractions. Problems in financing are related to the limited long-term financing support from the formal financial sector and insufficient support from FDI. In building an inclusive economy, Indonesia still faces serious disparities in development and inequalities in society in access and benefiting from the results of economic growth. These four structural challenges are closely linked to challenges in building the basic capital for development, most importantly infrastructure, human resources, the business climate, and science and technology. The growth diagnostic approach shows that the main impediments to the Indonesian economy lie in limited availability of electricity infrastructure, problems with connectivity, and the low quality of human resources.

The combination of global and the existing domestic structural problems have created complex challenges for macroeconomic management. Any slowdown in the global economy particularly China that sends commodity prices tumbling further has potential to bear down on Indonesia's exports. The commodity-dependent structure of the Indonesian economy and high import content of Indonesia's exports will exacerbate the slowdown in global economy pressure on Indonesia's future economic growth. The risk of a future downturn in economic growth also arises from mounting liquidity risk in keeping with the renewed improvement in credit growth. Added to this, a careful watch needs to be kept on the risk of more limited fiscal space for raising government expenditures, given the vital role of this in the economic recovery process. For this reason, the risk of further slowdown in economic growth must be properly managed in order not to kindle other risks that could put even more pressure on economic growth and disrupt macroeconomic and financial system stability. Efforts are also needed to diversify the economy so that Indonesia can become stronger with the capacity for sustainable growth.

Future Policy Direction

In reflecting on the experiences of 2015 and taking account of the present risks and issues in the economy, the macroeconomic policy mix for 2016 needs to focus on safeguarding macroeconomic and financial system stability and sustaining the current momentum for economic growth. From Bank Indonesia's side, the policy mix will be aimed at keeping macroeconomic and financial system stability and making prudent use of room for relaxation of monetary and macroprudential policies. On the Government side, the policy will focus on providing a further boost to the present momentum of economic growth. For this, measures to promote domestic demand commensurate with the capacity of the economy will play a vital role, given the still flagging condition of the global economy. Measures to bolster domestic demand within the capacity of the economy will also be the key for maintaining macroeconomic stability reflected in achievement of the inflation target, control over the current account deficit and maintenance of financial system stability. In addition, the Government and Bank Indonesia will continue work to accelerate structural reforms for the creation of robust foundations for the economy in support of sustainable economic growth.

Bank Indonesia will continue to strengthen the policy mix of monetary policy, macroprudential policy, and payment system and rupiah cash management policy to ensure macroeconomic and financial system stability and to utilize the available room for cautious relaxation of monetary and macroprudential policies. In the monetary sector, Bank Indonesia will prudently steer interest rate policy, the reserve requirement, and the exchange rate to keep inflation on track with the target, manage the current account deficit at a prudent level, and nurture the momentum that has been created in economic growth. Within this framework, the interest rate policy stance will aim to manage inflation expectations and domestic demand while supporting exchange rate stability aligned with fundamentals. The reserves requirement policy will be directed to support adequate levels of liquidity commensurate with the needs of the economy while paying close attention to macroeconomic and financial system stability. Like before, exchange rate policy will focus on maintaining stability in the rupiah in line with the value of fundamentals. To bolster the effectiveness of monetary policy, Bank Indonesia will strengthen both rupiah and foreign exchange monetary operations. These policies will be supported by prudent management of foreign exchange flows and strengthening of the international financial safety net to bolster the resilience of the domestic economy. Regarding macroprudential policies, Bank Indonesia will stay the course with accommodative and prudent measures to promote the bank intermediation function and support financial system stability. In the payment system, Bank Indonesia policy will continue to target more secure, smooth, and efficient operation. The effort to strengthen the payment system will be supported by Bank Indonesia policy in rupiah cash management with focus on meeting needs for timely provision of cash in appropriate quality and denominations throughout Indonesia.

In 2016, the Bank Indonesia policy mix will also implement in synergy with fiscal policy to improve the overall effectiveness of macroeconomic management. Coordination with the Government will focus on measures to safeguard macroeconomic stability through inflation control, particularly for volatile foods, and maintenance of a sound current account deficit, robust financial system stability, and a reliable, secure and smoothly operating payment system and rupiah cash management. To bolster momentum for economic growth, the relaxation of monetary policy and accommodative macroprudential policies will be brought into prudent synergy with the fiscal stimulus pursued by the Government. Bank Indonesia will also strengthen the role of the Coordination of Regional Economic and Financial Policy, a coordinating forum for promoting economic growth at the regional level. Regarding fiscal policy, the Government is expected to continue providing a fiscal stimulus to boost economic growth momentum while keeping the budget deficit at a safe and sustainable level. The policy mix at these different levels is expected to provide answers to short-term economic issues, namely by strengthening the current momentum for economic growth while maintaining macroeconomic stability.

An assessment of a series of policy packages launched by the Government and a mapping of domestic structural issues indicates the need for strengthening of policy, particularly in the drive to achieve food, energy, and water security, improving competitiveness in the industry, maritime, and tourism sectors, sustainable long-term financing, building an inclusive economy, strengthening of human resources, and mastery of science and technology. Regarding food, policy needs to be directed towards responding to the challenge of relatively low productivity by such measures as enhancement and construction of agricultural infrastructure, restoration of soil fertility, and development of agricultural banks and MSME. In the energy sector, policies need to target efforts to raise production and efficiency with focus on the four priorities of energy policy. These four policy priorities include increased production and reserves of extractive energy, improvement in the energy mix, improved accessibility and greater efficiency in use of energy and electricity, and more transparent and targeted management of fuel subsidies. In water management, government policies are necessary for meeting water needs for consumption, food crop cultivation and energy sources be integrated together with conservation of water resources. This will require the construction of reservoirs, improved access to drinking water and sanitation, construction of water conservation infrastructure, protection of natural water sources, and expansion and rehabilitation of irrigation networks. For industry, policymaking is directed at efforts to improve competitiveness, productivity, and technology content. Policy will concentrate on efforts to develop industrial areas outside Java, promote growth in the industry population, reinforce integration in world supply chains, and foster improvements in competitiveness and productivity. In the maritime sector, the policy direction has the objectives of strengthening territorial integrity, management of natural resources, connectivity, and advancement of the maritime and marine economy. In tourism, policy is targeted at improvements in infrastructure and tourism facilities, as well as building of human resources capacity. The need for support from sustainable financing calls for a policy response aimed at increasing the long-term funding sources from both domestic and foreign sources. In this regard, Bank Indonesia is pressing forward with financial market deepening, with measures that include promoting the use of the General Master Repurchase Agreement and is continuing the development of rupiah and foreign exchange money market instruments. For an inclusive economy, policy must aim for equitable development and financial access. Within this context, Bank Indonesia is promoting financial inclusion by expanding the range and coverage of non-cash transactions with the support of payment infrastructure integrated into the NPG.

The reinforcement of the four pillars of structural policies has been supported by various policies for strengthening key enablers for development in the areas of infrastructure, the business climate, human resources, and science and technology. The Government has designated 2016 as the year of accelerated construction of infrastructure to lay down the foundations for sustainable economic growth. The Government has prepared a list of 225 National Strategic Projects and 30 Priority Projects as a focus for infrastructure construction, based on The National Medium-Term Development Plan 2014-2019. The Government will also improve national connectivity and digital connectivity by establishing 24 locations for strategic ports, construction of toll roads and building a national fibre optic backbone in several regions. Regarding the business climate, the Government will work relentlessly on streamlining and simplifying licensing, improvements in service provision by increasing the number and quality of One-Stop Services, better law enforcement and greater business certainty through harmonization of central and local government regulations, tax incentives, and facilitation for industrial estates. The Government will also promote the use of science and technology to strengthen competitiveness in manufacturing and services, management of natural resources, social capital, human resources, infrastructure, institution building, networks, and development of science and techno parks. In regards to human resource development, Bank Indonesia sees the necessity for raising the quality of human resources to improve Indonesia's attractiveness as a venue for export-oriented investment in order to benefit from integration into global value chains and to diversify the Indonesian economy. It is also Bank Indonesia's view that these government policies for strengthening the key enablers for development will be crucial to improving the efficiency of the economy. To contribute to greater efficiency in the economy, Bank Indonesia will accelerate development of the infrastructure for a more efficient national payment system by expanding the payment system electronification and improving the reliability of the infrastructure for the electronic retail payment system.

Short and Medium-Term Economic Outlook

In view of prudently managed economic stability, continuation of the fiscal stimulus policy, and consistent implementation of structural reform policies, the Indonesian economy is expected to mark steady improvement. In 2016, economic growth is predicted to reach 5.2-5.6%. This short-term economic growth will be driven as before by domestic demand, led mainly by government infrastructure projects. Meanwhile, private investment is expected to grow in tandem with the impact of the policy packages launched by the government and the use of the room for prudent relaxation of monetary and macroprudential policies while safeguarding macroeconomic and financial system stability. This improvement in domestic demand will also be bolstered by renewed gains in household consumption. However, the external sector contribution will remain limited due to the fragile nature of global economic growth, particularly in China. Inflation will stay subdued in 2016, within the 4±1% target range. Key to this will be the management of inflation expectations, close coordination between Bank Indonesia and the Government, and decline in prices for international commodities, including oil. Improvement in domestic economic growth bolstered by infrastructure projects in tandem with still limited gains in export performance will lead to a modest rise in the current account deficit. Nevertheless, in 2016 the current account deficit will remain in safe territory, below 3% of GDP, and have a more robust structure. Against this background, the forecast is for higher credit growth compared to the previous year, reaching 12-14% in 2016, while growth in bank deposits will reach 13-15%.

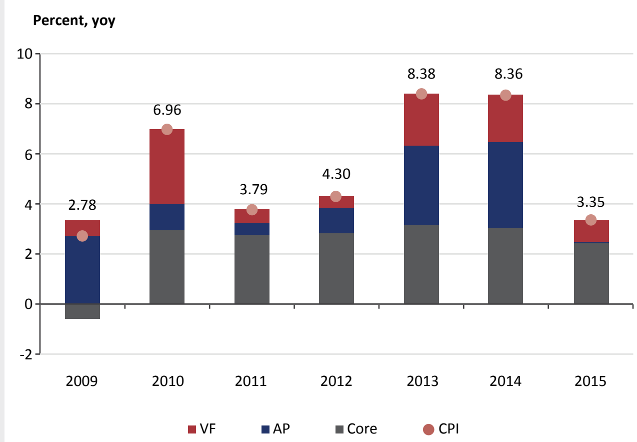
In the medium term, economic growth in Indonesia is predicted to climb in keeping with the commitment to accelerate implementation of structural reforms with consistency and synergy maintained across sectors and a suitable policy mix involving Bank Indonesia, the Government, and other policymakers. The improvement in economic growth is supported by the outlook for more solid global economy recovery in the future and impact from the structural reform policies consistently pursued by the Government, Bank Indonesia and other related authorities. Under these conditions, the Indonesian economy will be able to achieve vibrant growth of 6.3-6.8% by 2020. This growth will not only be higher, but also more inclusive and underpinned by a more robust structure. Household consumption will maintain stable growth in tandem with the expanding proportion of the middle class and more extensive provision of social security protection. The private sector will have an expanding role in investment, supported by the continuing infrastructure projects development, an improving business climate, and reforms to create a more efficient bureaucracy. This will be accompanied by progressive improvement in the quality of government spending reflected in the increasing proportion of capital expenditure as the government cuts back spending on subsidies. In the external sector, the balance of payments will improve in the medium term with the current account deficit maintained at a prudent level. Supporting this will be improvement in global economic growth, recovery in commodity prices, and more robust competitiveness of Indonesia's export products. Regarding inflation, the increased capacity of the domestic economy achieved through consistency in structural reforms and Bank Indonesia's consistency in safeguarding macroeconomic stability will enable inflation to remain within the target range of 3.5±1% over the medium term.

Consistent implementation of structural reforms will be the key for achieving this medium-term outlook for the Indonesian economy. The upward projection for the medium term accompanied by higher quality of economic growth will only be possible if structural reforms move forward at an optimum pace. This is because two vital factors in medium-term economic growth, namely infrastructure development and greater involvement from the private sector, will depend to a great extent on consistent implementation of structural reforms. However, the complexity of structural problems in the domestic economy points to the existence of various impediments with potential to hamper the implementation of these reforms. Should this happen, the setback in structural reforms will have repercussions on the progress of infrastructure projects envisaged as the backbone for resolving various supply side issues. This may impede efforts to build productivity and the capacity of the economy, which will not only result in lower economic growth but also higher inflationary pressure on the demand side and a swelling current account deficit.
To avoid this, measures to safeguard the implementation of structural reforms in a comprehensive synergy of macroeconomic management must be strengthened further for the Indonesian economy to achieve rapid and sustainable gains with greater inclusiveness and support maintenance of economic stability as a whole.

Box — Accountability for Achievement of the 2015 Inflation Target

In 2015, CPI inflation was kept under firm control within the target range of 4±1%. Inflation in 2015 was recorded at 3.35% (yoy), well below the level reached in the previous year (8.36%, yoy) (Chart 1). Low inflation was recorded in all its components: the core category, volatile foods (VF) and administered prices (AP) (Chart 2). The subdued level of core inflation owes much to the role of Bank Indonesia policies in maintaining exchange rate stability, guiding inflation expectations, and managing domestic demand. The ability to contain VF inflation at below 5% despite a strong El Nino phenomenon owes to serious Government efforts in increasing production, improving distribution, and minimizing various price distortions affecting food staples. Alongside this, low AP inflation resulted mainly from the fall in global oil and gas prices and Government action in reforming energy subsidies. Following the energy reform, pricing of fuels, gas, and electricity has moved in tandem with developments in oil and gas prices and the exchange rate (Diagram 1).

Chart 2. Decomposition of Inflation 2008 - 2015



Source: BPS - Statistics Indonesia

Core inflation stayed remarkably low throughout 2015, consistent with soft domestic demand, minimum cost-push pressure, and subdued inflation expectations. Core inflation was recorded at 3.95% (yoy), down from 4.93% (yoy) in 2014. At the start of the year, core inflation was still fairly high at about 5% (yoy), driven by the second round effects of the fuel price hike of the preceding year. Subdued inflation expectations amid the upward pressure on prices fuelled by depreciation in the rupiah, which reached a peak in September, helped keep a lid on the dynamics of core inflation during 2015. At the end of the year, renewed stability in the exchange rate helped bring core inflation down. The easing of core inflation at the end of the year is a reflection of weak pressure from demand

Chart 1. Inflation Target

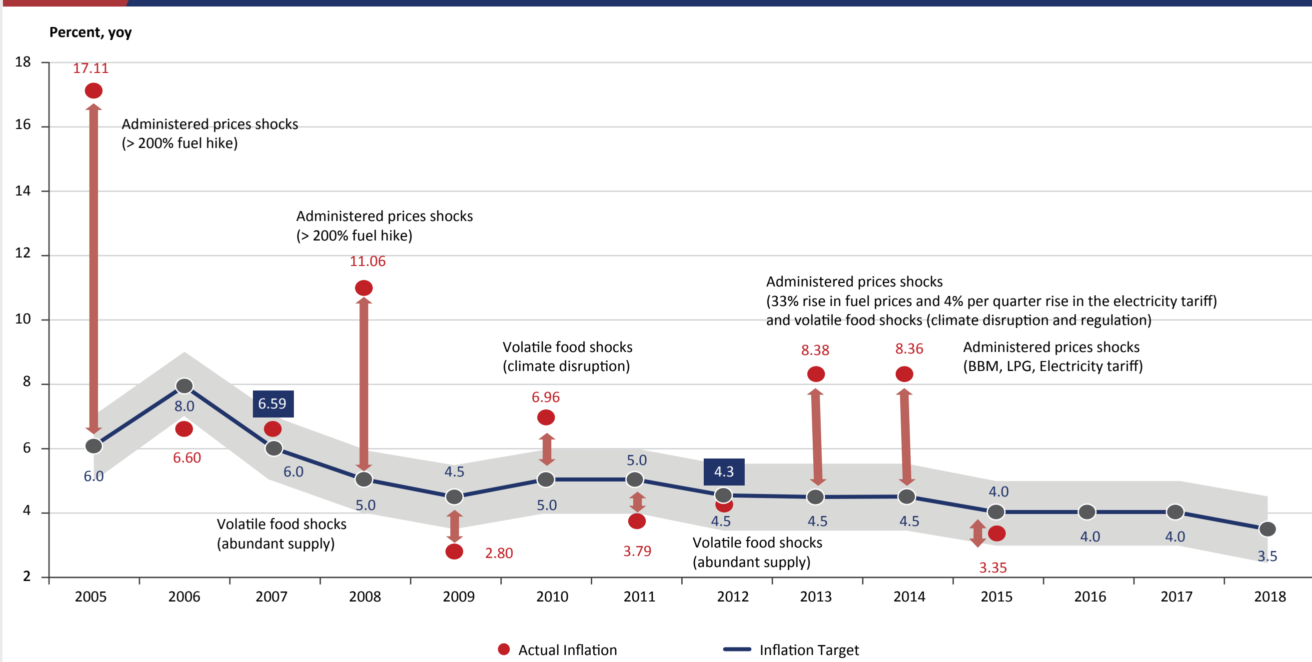
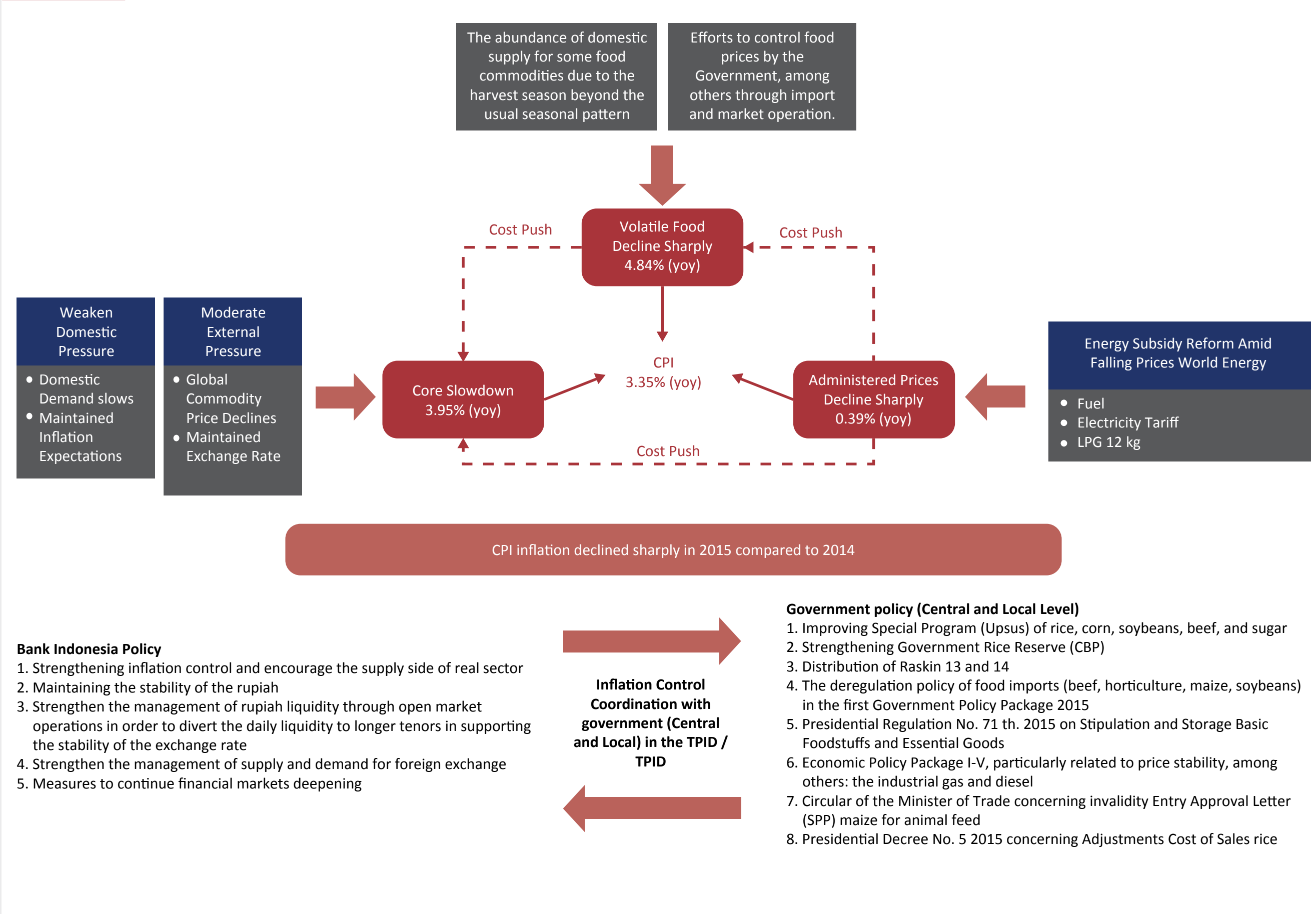


Diagram 1. Inflation in 2015 and Affecting Factors



and limited cost-push pressure demonstrated in part by low inflation in the AP and VF categories.

To support inflation control, Bank Indonesia maintained a tight bias monetary policy reflected in the steady level of the BI Rate at 7.5% since the end of the first quarter of 2015. In addition, Bank Indonesia pursued a range of policy for stabilising the exchange rate in order to anchor inflation expectations. Through this, business inflation expectations were kept well in check, thus avoiding excessive fluctuation. Inflation expectations remained subdued despite greater depreciation in the rupiah compared to that of the previous year. Mild inflation expectations were reflected in the limited exchange rate pass-through on inflation, indicating that business perceived the downturn in the exchange rate as only temporary. In addition, the limited exchange rate pass-through also caused by the effect of weakening domestic demand. In this situation, business players preferred not to pass on the full effect of exchange rate depreciation, but instead cut their margins to avoid further decline in demand.

The minimal pressure in AP inflation was explained by the implementation of pricing for fuels and electricity at their economically viable value during a time of a downward trend in world energy prices.[1] AP inflation was recorded at 0.39% (yoy), having fallen dramatically from the previous year (17.57%, yoy) and also below the historical average for the previous five years (9.01%, yoy). Plunging

1 The Government launched a policy for energy subsidy reform at the end of 2014, with fuel prices and electricity tariffs to be adjusted in line with the underlying energy prices. Under Regulation of the Minister of Energy and Mineral Resources No. 4 of 2015, amended by Regulation No. 39 of 2015, fuel prices are based in part on movements in world prices for refined petroleum products, the rupiah exchange rate and distribution costs. The government does not subsidise the Premium RON 88 gasoline, but automotive diesel continues to benefit from a fixed subsidy of Rp1,000 per litre. Under Regulation of the Minister of Energy and Mineral Resources No. 31 of 2014, electricity tariffs are based on movement in the ICP crude price, the rupiah exchange rate and the monthly inflation rate.

world oil prices prompted the Government to announce substantial cuts in fuel prices in early 2015, which kept pressure low in the AP category.[2] Despite a surge in fuel prices in March, the Government policy for control of transport fares managed to curb the second round effects of increased fuel prices.[3] Adjustment of electricity billing rates to economically viable prices helped bring down inflation in electricity rates during 2015 in keeping with the low ICP crude price and subdued monthly inflation.[4] The continuation of energy subsidy reforms at a time of low and declining world energy prices became a vital element in curbing inflationary pressure in the AP category to a minimum.

Contributing to low VF inflation were adequate levels of supply and decline in global food prices. In the VF category, inflation came to 4.84% (yoy), substantially below the previous year (10.88%, yoy) and the historical average for the past five years (9.90%, yoy). The fall in VF inflation came mainly in response to the sizeable deflation in miscellaneous chilli peppers and shallots during the year, in addition to decline in global commodity prices and particularly for CPO that impacted cooking oil prices. The low inflation in milled rice amid strongly unsettled weather conditions brought on by El Nino also kept a lid on VF inflation. Low VF inflation was also driven by Government policies for strategic foodstuffs. The Government has devoted considerable attention to supporting adequate domestic supply of food staples while also pursuing other policies. These measures involved first, Special Efforts for Improvement Program (Upsus) for paddy rice, corn, soy beans, beef, and refined sugar. Second was the strengthening of the Government Rice Buffer Stock (CBP) with assurance of 1.5 million tons of imports by March 2016. Third, measures to control prices were implemented for shallots and miscellaneous chilli peppers in: (i) the Dry Season Chilli Pepper Planting Campaign involving assistance with farming equipment and water-saving irrigation, (ii) regulation of crop growing schemes in centres of agricultural production, (iii) development of shallot and chilli pepper cultivation areas in centres of agricultural production and outside these centres, as well as development of integrated chilli pepper clusters in collaboration with Bank Indonesia in eight provinces (Bangka Belitung, West Java, East Java, West Kalimantan, South Sulawesi, West Nusa Tenggara, East Nusa Tenggara, and North Maluku), and (iv) deregulation of food import policies.[5] The Government also launched the Gerai Maritim (maritime outlets) pilot program and the nautical highway system in 2015 to overcome impediments to distribution.[6]

The achievement of the inflation target in 2015 also supported by the closer coordination forged by Bank Indonesia and the Government through the TPI and TPIDs. In 2015, the work of the TPI and the TPID National Working Group focused on strengthening the operational of secretariat and the coordination through implementation of National Coordination Meetings and Central and Regional Government Coordination Meetings, as well as building the role of the TPI and TPIDs in price stabilization. In addition, the TPI and the TPID National Working Group also submitted various recommendations to the Government, which included design and submission of an Inflation Control Roadmap for 2015-2018 and more complete and reliable information and data on food prices. The Inflation Control Roadmap is intended as a reference for the work performed by the TPI and TPIDs. This roadmap was deliberated in December 2015 by senior ministry and agency officials serving as members of the TPI and TPID National Working Group and distributed to all heads of local government. Afterward, the program in the road map is expected to be incorporated into the Government Work Plan both at the central and regional

2 On 1 January 2015, the Government reduced prices for Premium RON 88 and automotive diesel by Rp900 per litre and Rp250 per litre. Following this on 14 January 2015, the Government announced further price cuts for Premium RON 88 and automotive diesel of Rp1,000 per litre and Rp850 per litre.

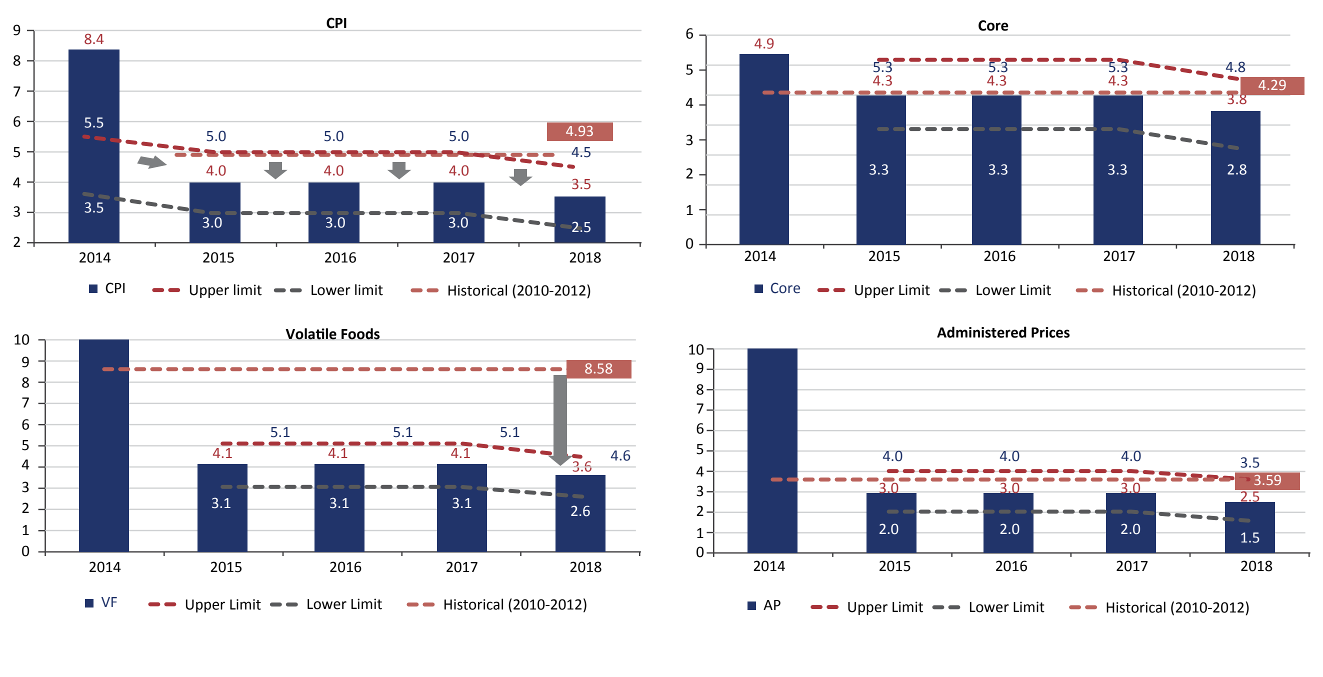
3 On 1 March 2015, the Government raised the price of Premium RON 88 gasoline by Rp500 per litre, and followed with a further increase of Rp500 per litre for both types of fuel on 28 March 2015. To curb the second round effects of these increases in fuel prices on transport fares, on 10 February 2015 the Government enacted Regulation of the Minister of Transportation No. 31 of 2015, stipulating among others that fare increases will be permitted if increases in energy prices result in a 20% change in the cost of providing transportation.

4 Under Regulation of the Minister of Energy and Mineral Resources No. 31 of 2014, electricity tariffs are adjusted to movements in the Indonesia Crude Price (ICP) the exchange rate and the monthly level of CPI inflation. The categories of electricity customers included in this formula are households (1,300VA, 2,200VA 3,500VA-6,600VA), businesses (6,600VA-200kVA, >200kVA), industry (>200kVA and >30,000 kVA), government offices (6,600VA-200kVA, >200kVA), street lighting and special services. For the 1,300VA and 2,200VA categories, implementation of the tariff adjustment was postponed from April 2015 under the original plan to December 2015.

5 The import deregulation policy has been implemented for beef, horticultural products, corn and soy beans.

6 Gerai Maritim is a collaborative program between the Ministry of Trade, the Ministry of Transportation, the Pelni national shipping line, and the Indonesian Association of Retail Businesses (Aprindo) to reduce price disparities between Western and Eastern part of Indonesia for staple goods. This program operates with the provision of transport for delivery of staple goods and subsidized freight costs to Eastern Indonesia, where the goods will be sold by local government/ designated companies at producer prices.

Chart 3. Inflation Path



levels and thus provide a reference for the work of the TPI and TPIDs.

Looking forward, the Inflation Control Roadmap will be necessary as a guide for a structured and integrated control of inflation to ensure achievement of the medium-term inflation target, set at 3.5±1% for 2018.[7] Amid the many structural issues surfacing with regard to inflation, extra effort is needed from all parties for future inflation targets to be achieved on a sustainable basis. Historical average figures (outside the periods of fuel price hikes) are 4.9% for CPI inflation, 4.3% for core inflation, 8.6% for VF inflation, and 3.6% for AP inflation. For the medium-term inflation target to be achieved, each of the components contributing to inflation must be maintained on a disinflation path (Chart 3). This means that core inflation in 2018 must be kept around the 3.8%, with VF inflation at about 3.6%, and AP inflation at 2.5%. In view of the short time remaining, Bank Indonesia and the Central Government and Local Governments will have to work harder and intensify their coordination.

The Inflation Control Roadmap is prepared for both the national level and regional level, where the design is based on regionality (islands) according to the local characteristics of inflation. Each roadmap, both national and regional, identifies issues and presents solutions for the short term (2015-2016) and medium term (2017-2018). The national Inflation Roadmap details the ministries or government agencies in charge of each inflation control activity or program that has been adopted and the regional role that is necessary for the success of the inflation control program. For the regions, the Inflation Control Roadmap also specifies the necessities of central government support for achievement of inflation control in the regions, given that some policies represent the competency of the central government.

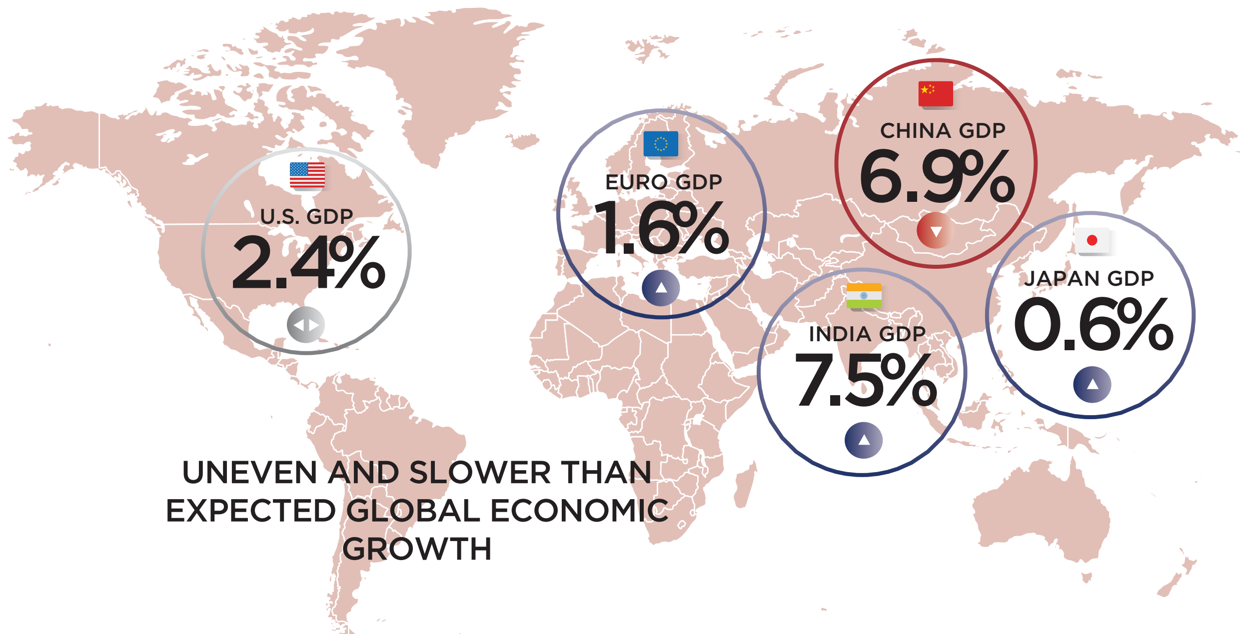
The roadmap for core inflation control covers management of domestic demand, expanding the capacity of the economy, management of exchange rate stability, and management of inflation expectations. The roadmap for VF inflation control covers measures to increase food production and buffer stocks and to improve market structures and pricing mechanisms. Meanwhile, the roadmap for AP inflation control addresses consistent implementation of the energy subsidy reform, diversification of energy consumption, and demand management. Following this, it is envisaged that the work program in the road map will be incorporated into the Government Work Plan at the central and regional levels in order to provide a reference for the work of the TPI and TPIDs.

7 In Regulation of the Minister of Finance of the Republic of Indonesia number 93/PMK.011/2014 concerning the Inflation Target for 2016, 2017, and 2018, the inflation target is set at 4±1% (2016 and 2017) and 3.5±1% (2018).

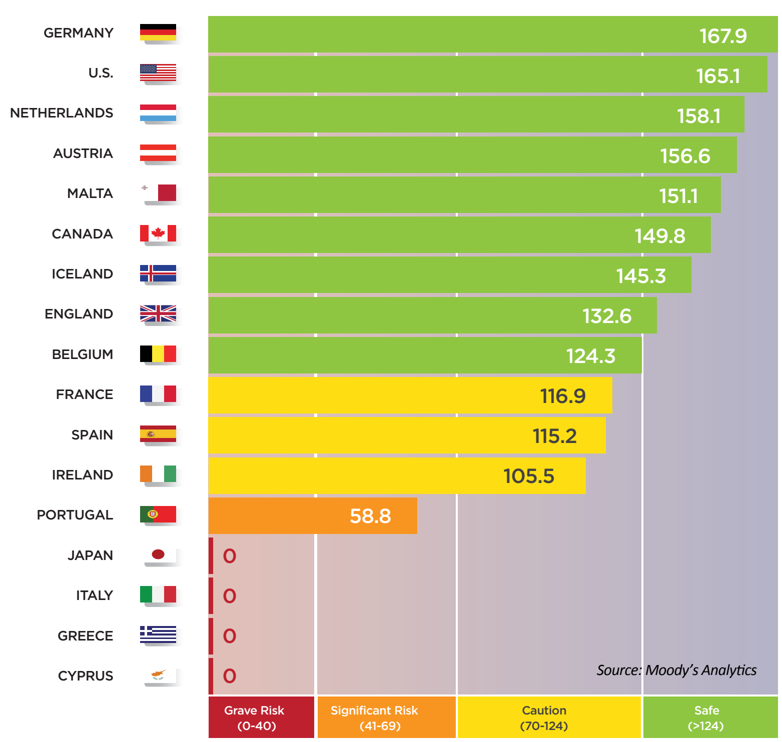
Like two Barongs, the global economy in 2015 was marred by a change in the landscape through sluggish economies in developing countries coupled with limited recoveries in advanced countries. On the other hand, global financial markets were blighted by escalating volatility in 2015, reflecting ubiquitous uncertainty.

PART I

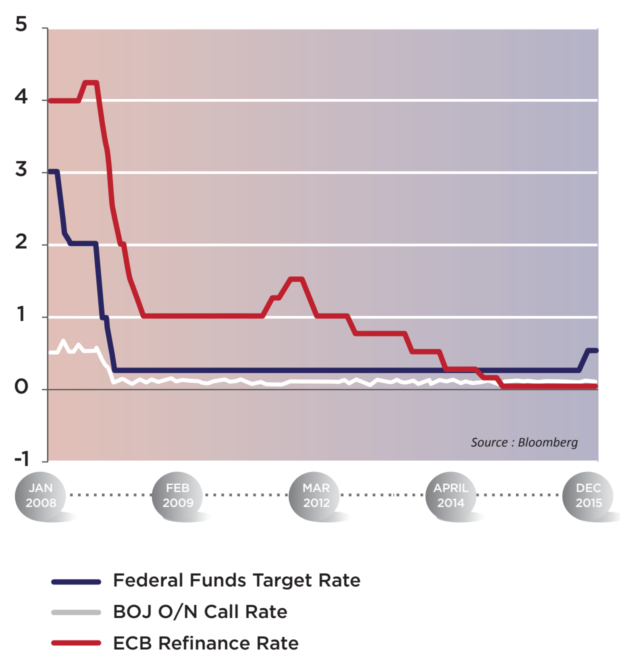
GLOBAL ECONOMY



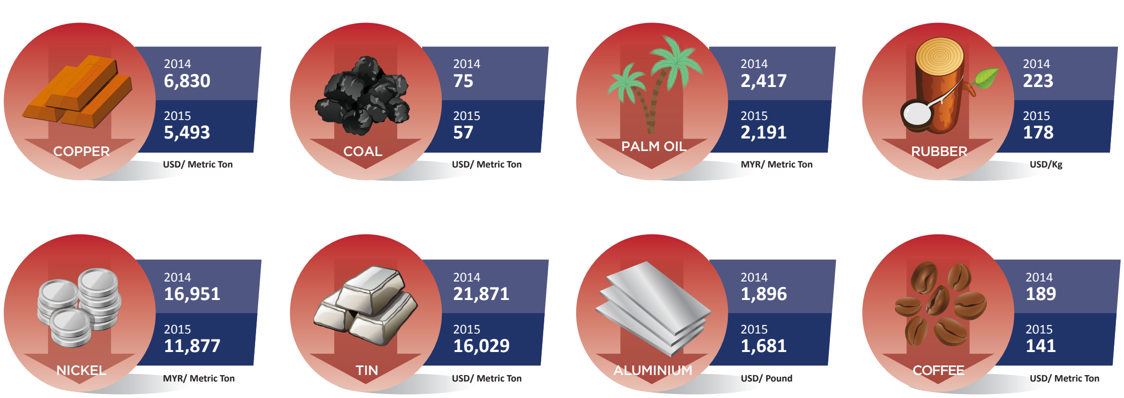
Limited Fiscal Space in Advanced Economies



Monetary Policy Divergence in Advanced Economies



INTERNATIONAL COMMODITY PRICE TRENDS STILL IN DOWNHILL



PART I
GLOBAL ECONOMY

In 2015, the recovery in the global economy progressed more slowly than expected. The world economy grew by only 3.1%, below the forecast of 3.5% at the start of the year and the 2014 growth rate of 3.4%. The economic growth in advanced economies that fell short of earlier forecasts was insufficient to serve as the engine of global economic recovery. Measures for promoting economic growth, particularly in advanced economies, had only limited success because quantitative easing policies were not fully supported by fiscal stimulus and implementation of structural reforms. Furthermore, the multispeed recovery in economic growth led to divergence in monetary policy among the advanced economies. The U.S. Federal Reserve embarked on a monetary policy normalization, while on the other hand, the European Central Bank and the Bank of Japan continued to implement accommodative monetary policies.

Global economic recovery in 2015 was also marked by changes in the landscape of economic growth. Growth slowed in emerging markets while the economies of advanced countries charted a gradual recovery trend. Although lower than predicted, economic growth in advanced economies edged upwards from 1.8% in 2014 to 1.9% in 2015. Conversely, economic growth in emerging markets slipped from 4.6% in 2014 to 4.0% in 2015. Despite experiencing a significant slowdown, the emerging market retained a dominant position in the contribution to global economic growth by 58%. Advanced economies, on the other hand, only accounted for 42%.

The global economic slowdown in 2015 was driven by both cyclical and structural factors. The cyclical factors were mainly related to the economic slowdown in China, the continued downturn in commodity prices, and uncertainty over U.S. monetary policy normalization. The structural factors, on the other hand, were visible mainly in advanced countries, and arose from declining potential output caused by the demographic factor of the ageing population and falling levels of investment in the aftermath of the global financial crisis. The decline in potential output and the policy responses pursued by advanced economies had significant spillover effects on emerging markets, transmitted through both the trade and financial channels.

The economy in China slowed further, as a result of the economic rebalancing policy that has so far not succeeded in raising consumption. In 2015, China's economy grew by only 6.9%, having slowed from the 2014 growth of 7.3%. This slowdown was prompted by the economic rebalancing policy from an investment-driven towards a consumption-driven economy in order to achieve higher quality and more sustainable economic growth. However, the improvement in consumption growth was only limited and insufficient to offset the considerably greater slowdown in investment. This resulted in a weakening of Chinese demand for imports that brought repercussions for emerging markets through the trade channel.

The downturn in global growth, particularly in China, led to a sustained fall in world commodity prices during 2015. Commodity exporting countries, including Indonesia, suffered from the twin impacts of diminishing volume of demand and falling commodity prices that hit export performance. In 2015, the Indonesia Export Commodity Price Index plunged 14.9%, a markedly greater loss than the index contraction in 2014 that reached 4.2%. The fall in commodity prices in response to the economic slowdown in China was exacerbated by tumbling world oil prices, which are closely linked to the prices of certain commodities. The weakening in world oil prices represents the effect of oversupply from both OPEC members and non-OPEC countries amid shrinking demand brought about by the global economic slowdown. Contributing to the glut in the world oil supply were the policies of oil-producing countries who have maintained production levels despite falling oil prices in order to maintain their market share on the world oil market.

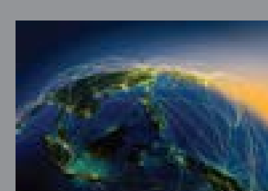
The economic slowdown and fall in commodity prices contributed to a decline in global inflation. In 2015, global inflation was recorded at 3.3%, down from 3.5% in the previous year. Inflationary pressure eased mainly in advanced economies. In 2015, inflation in advanced economies came to only 0.4%, well below the 2014 inflation of 1.4%. In some advanced economies, notably the U.S., Europe, and Japan, inflation came well below the prescribed targets. On the other hand, inflation in emerging market economies mounted to 5.6% in 2015 from 5.1% one year previously. This increase is explained mainly by the pass-through effect of depreciation in exchange rates.

In the financial sector, global financial markets were marked by rising volatility in 2015, reflecting high levels of uncertainty. The mounting volatility on world financial markets in 2015 is explained by three factors: (i) sentiment over monetary policy normalization in the U.S. that influenced global financial markets from early 2015; (ii) sentiment fuelled by concerns over resolution of the crisis in Greece during the first quarter of 2015; and (iii) devaluation of the yuan by the People's Bank of China in August 2015. The uncertainty over increases in the U.S. Federal Funds Rate (FFR) prompted risk-off behavior among global investors accompanied by diminished capital inflows into the financial markets of developing economies that in turn put pressure on exchange rates.

In response to the dynamics of the global economy and financial system, some emerging market economies pursued a policy mix to integrate monetary and fiscal policy and structural reform. Learning from the experience of some advanced economies that relied too much on monetary policy to stimulate economic growth, a number of emerging economy countries opted for a policy mix approach to bolster the otherwise flagging economic growth. The policy mix consists of a combination of monetary relaxation with macroprudential policy, fiscal policy, and structural reforms. China, India, and Indonesia are examples of emerging market economies that have consistently implemented a sound policy mix for macroeconomic management accompanied by an agenda for structural reforms. In emerging markets, there is a pressing need for structural reforms in order to improve efficiency and competitiveness and thus pave the way for the economy to achieve sustainable growth.

Efforts were also pursued to strengthen international cooperation in anticipation of global economic challenges that lasted throughout 2015. The G20 Forum emphasised the need for action to bring about strong, inclusive economic growth. At the same time, the IMF also encouraged its member countries to bolster the demand side with the use of a macroeconomic policy mix and to accelerate the implementation of structural reforms. In a similar vein to the IMF, the Islamic Development Bank (IDB) expanded its role in funding assistance for the infrastructure projects of its member countries, including support through establishment of the World Islamic Investment Bank (WIIB). International cooperation was also focused on maintaining financial system stability for resilience in the face of shocks, including establishing an agenda for reform of international financial standards. To safeguard resilience in the region, the ASEAN+3 countries strengthened their Regional Financial Arrangement (RFA) collaboration by implementing the Chiang Mai Initiative Multilateralization (CMIM) while also expanding the role of the ASEAN+3 Macroeconomic Research Office (AMRO).

Looking ahead, the outlook for global economic conditions is more favourable with higher growth rate. The onset of normalization of U.S. monetary policy will ease uncertainties on global financial markets. On the other hand, the still fragile economic recovery in the U.S. indicates that increases in the FFR will be gradual. This will lead to less divergent global monetary policies, thereby easing pressures on the financial markets of emerging market economies. The ongoing improvement in the advanced economies and the early signs of results from implementing a policy mix and particularly structural reforms in emerging markets will boost global economic growth to 3.4% in 2016. Even so, the rise in global economic growth is not expected to bring improvement in commodity prices, which will instead undergo mild correction. This condition poses a challenge for commodity-exporting countries, including Indonesia, to work consistently in implementing structural reforms in order to create new sources of economic growth in diversification away from commodities so that growth can become more sustainable and resilient to global shocks.



The global economy grew slower in 2015 than previously projected. Furthermore, the multispeed recovery triggered monetary policy divergence: the U.S. raised its policy rate, contrasting Europe and Japan that expanded quantitative easing.

Chapter 1

Global Economic Dynamics

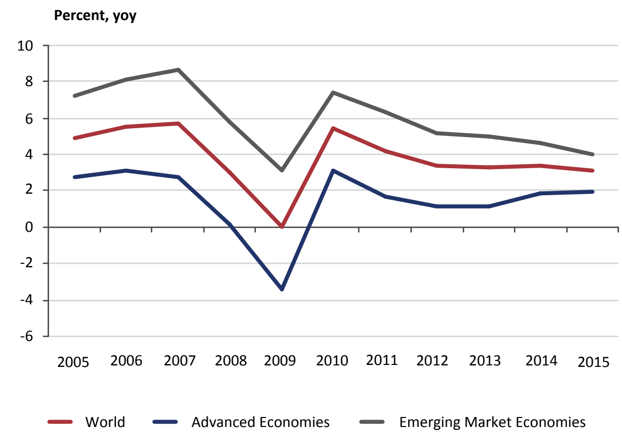
The global economy recovery in 2015 was weaker than previously projected, tainted by moderation and imbalances coupled with ubiquitous uncertainty blighting global financial markets. The global economy was underpinned by growth in advanced countries, primarily the United States, despite sluggish growth in Europe and Japan. Meanwhile, economic growth in developing countries also tended to decelerate, driven predominantly by the economic slump experienced in China. Congruous with the global economic downshift, international commodity prices, including oil prices, continued to slide.

A weaker-than-expected global recovery lingered in 2015. The rebalancing process in the wake of the global financial crisis (GFC) continued in advanced countries, which also began to spillover to emerging market (EM) countries. Post-crisis, a negative output gap, globally and individually, triggered low inflation in numerous countries, particularly advanced countries, which provided adequate space to loosen monetary policy in order to kick-start economic growth. Unfortunately, the expected pace of growth remained unachievable due to the languid implementation of much needed structural reforms combined with limited fiscal policy support in a number of advanced countries.

Disparity between the phases of economic recovery in several advanced countries prompted monetary policy divergence globally.[1] On the one hand, the U.S. began to normalize its monetary policy stance in December 2015, for which the proposed implementation was communicated at the end of 2014. Conversely, however, Europe and Japan extended loose monetary policy. Uncertainty regarding the timing and magnitude of the policy rate hike in the U.S. along with global monetary policy divergence intensified volatility on global financial markets, which triggered risk-off behavior amongst investors. Such conditions, coupled with deleveraging in advanced countries, eroded inflows to emerging market countries and eventually led to negative outflows. Furthermore, lower international commodity prices on the back of weak demand from China also exacerbated external pressures in emerging market countries, especially net exporters.

Against such an inauspicious backdrop, the global economy grew at 3.1% in 2015, down from 3.4% the preceding year (Chart 1.1). Actual growth in 2015 was below the Bank Indonesia projection at the beginning of the year as well as the International Monetary Fund (IMF) forecast of 3.5%, building on the momentum achieved in 2014. Global economic moderation was the result of both cyclical and structural factors. Cyclically, the main factor was the economic downswing observed in China that ultimately perpetuated the international commodity price slide. Additionally, policy spillover from advanced countries further undermined global growth. Structurally, however, lower potential output due to the ageing populations of advanced countries, together with sluggish investment after the global financial crisis, slowed global growth. In terms of inflation, the global slowdown, soft oil prices and sliding commodity prices coalesced into lower global

Chart 1.1. Global Economic Landscape: Economic Growth

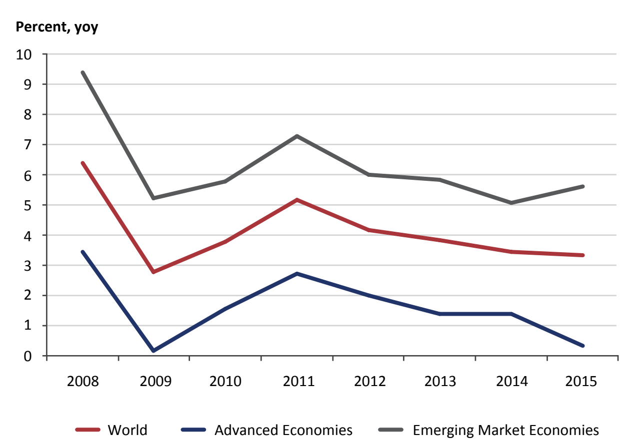


Source: WEO IMF, processed

inflation (Chart 1.2). Global inflation stood at 3.3% in 2015, down from 3.5% in 2014.

Weaker global growth in 2015 compared to the preceding year was considered the most binding challenge faced by countries worldwide, including Indonesia. In addition, the world trade structure experienced a number of increasingly significant changes over time that adversely affected the domestic economy of Indonesia. Consequently, trade elasticity to the economy was seen to decline due to mature global supply chains.[2,3] Such

Chart 1.2. Global Economic Landscape: Inflation



Source: WEO IMF, processed

1 Disclosed by the International Monetary Fund (IMF) and European Central Bank (ECB).

2 Global supply chains: the trade of raw materials or intermediate goods between countries in order to produce finished articles.

3 A range of studies conducted by various institutions, including the International Monetary Fund (IMF), World Bank, European Central Bank (ECB) and OECD produced similar findings.

conditions amplified the impact of sliding commodity prices on external sector performance in Indonesia. In addition, challenges also stemmed from a decline in capital inflows into Indonesia throughout 2015 in line with the shift in the composition of global liquidity and deleveraging in advanced countries.

1.1. ECONOMIC GROWTH AND INFLATION IN ADVANCED ECONOMIES

Economic performance in advanced countries was marked by moderate growth and very low inflation. Growth in such countries was recorded at just 1.9% in 2015, accelerating slightly from 1.8% in 2014. Meanwhile, inflation stood at just 0.4% in 2015, well below the 1.4% posted in 2014 due primarily to cheap international oil and commodity prices. In general, inflation in major advanced countries, including the U.S., Europe, and Japan, fell below target. Additionally, prices in Europe and Japan even experienced deflation, contrasting the intense inflationary pressures felt in emerging market countries such as Russia, Brazil,and other Latin American countries, where exchange rate depreciation exacerbated inflation.

In response to low inflation and lacklustre recoveries, advanced countries opted to extend loose monetary policy in order to stimulate demand. Consequently, the recoveries in such countries gained momentum, predominantly on the back of U.S. growth, albeit at a slower pace than previously expected. A gradual recover endured in Europe, while torpid gains in Japan also contributed to global growth. Notwithstanding, the dependence on loose monetary policy was not accompanied by adequate fiscal stimuli nor the accelerated implementation of structural reforms. Therefore, the efficacy of loose monetary policy was tempered in terms of catalysing economic growth. Despite improvements on the previous year, the economic contribution of advanced countries (42%) to global growth was less than that contributed by emerging market countries (58%) (Table 1.1).

U.S. economic growth was lower than expected in 2015. The U.S. economy achieved growth of 2.4% in comparison to the 3.6% projected previously due to the North American cold wave that struck in 2015 combined with strike action at ports on the West Coast in the first quarter of 2015. Such conditions reduced private spending during the same period that led to a build-up of inventory in the subsequent quarters and ultimately lowered production output (Chart 1.3). In addition, sluggish growth in the U.S. also placed pressures on U.S. manufacturing industry performance due to a contraction of external demand for exports congruous with the global economic slowdown and broad U.S. dollar appreciation (Chart 1.4).

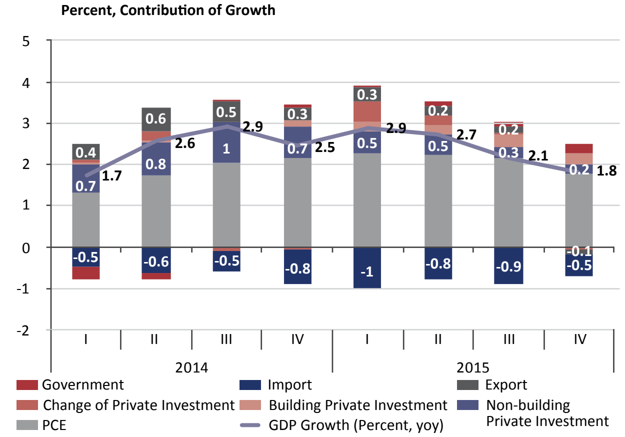
Despite relatively sound performance, the impact of U.S. economic momentum globally was minimal because U.S. growth stemmed primarily from non-tradeable sectors. Based on 2013-2015 data, around 76% of U.S. economic growth came from non-tradeable sectors, in particular the Processional and Business Services Sector as well as the Real Estate Sector. Consequently, U.S. growth was not expected to contribute tangibly to growth in other countries.

Table 1.1. Realization of Global Economic Growth

GDP (%yoy)	2014	2015*	
	Growth (%)	Growth (%)	Growth (%)
World	3.4	3.1	100
Advanced Economies	1.8	1.9	42
Japan	-0.03	0.6	4
U.S.	2.4	2.4	16
Euro Zone	0.9	1.6	11
France	0.2	1.4	2
Germany	1.6	1.3	3
Italy	-0.4	1.0	2
Spain	1.4	3.5	1
Emerging Markets	4.6	4.0	58
China	7.3	6.9	17
India	7.3	7.5	7

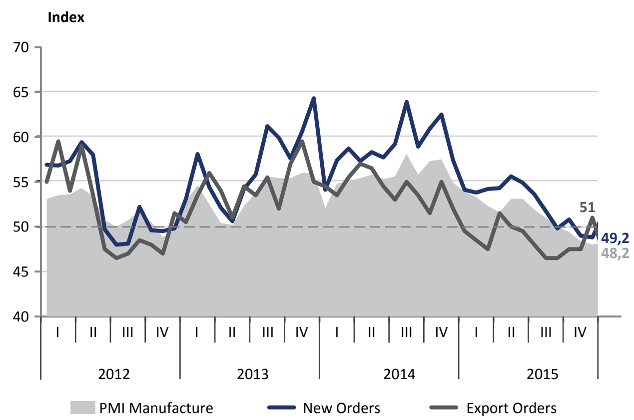
Source: update WEO IMF Jan-16, Bloomberg
*provisional figures

Chart 1.3. Decomposition of U.S. GDP Growth



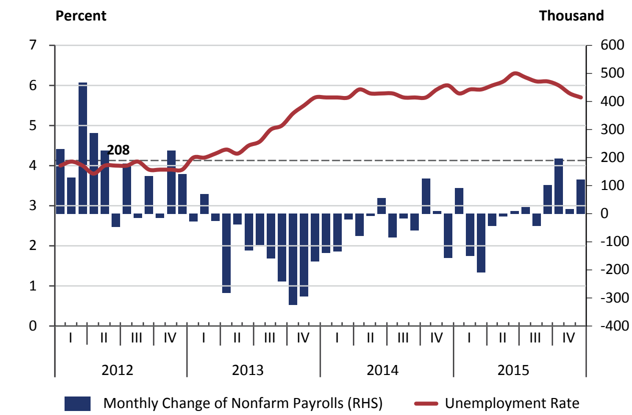
Source : BEA, processed

Chart 1.4. U.S. Manufacturing Sector



Source: Bloomberg, processed

Chart 1.5. U.S. Employment Sector



Source: Bloomberg, processed

U.S. economic momentum was predominantly supported by consumption. Private spending followed an upward trend despite slowing in the first quarter of 2015. The solid increase in private consumption was consistent with lower fuel prices in the U.S. that occasioned greater purchasing power. Furthermore, the labor sector continued to improve throughout 2015, which boosted consumption. Low fuel prices and increasingly conducive labor market conditions also bolstered consumer confidence, which ultimately served to increase private consumption further.

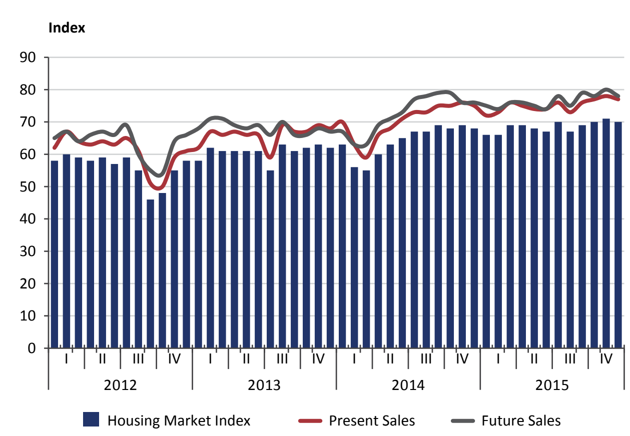
The U.S. labor market improved in 2015 in line with relatively robust economic gains, marking a drop in unemployment (Chart 1.5). The ratio of the unemployment and job openings, which is a reflection of demand in the labor sector, tended to increase to pre-crisis levels. Improvements were noted to affect all sectors, as observed cyclically and from the corresponding long-term trends. In addition, non-farm payrolls and earnings growth also improved, particularly in the services sector. The number of part-time employees for economic reasons declined, reflecting a persistently lower supply of labor.

The U.S. housing sector also contributed to U.S. economic gains in 2015. Home sales continued to grow in line with low mortgage rates. Congruously, the U.S. housing sector index rallied (Chart 1.6). Moreover, the prevalence of front loaded property purchases prior to the Federal Funds Rate (FFR) hike by the Federal Reserve also drove house sales. Future performance of the housing sector is also set to improve, evidenced by increases in Building Permits and Housing Starts as an early indicator of the U.S. housing sector.

The economy of Europe achieved growth of 1.6% in 2015 improving from 0.9% in 2014 (Chart 1.7), supported by a surge in domestic demand. Consumption in Europe, which accounted for 75% of GDP, tended to increase, indicated by strong retail sales data and new car registrations. In addition, consumption was also bolstered by gains in the labor sector as the level of unemployment noted gradual declines throughout Europe.

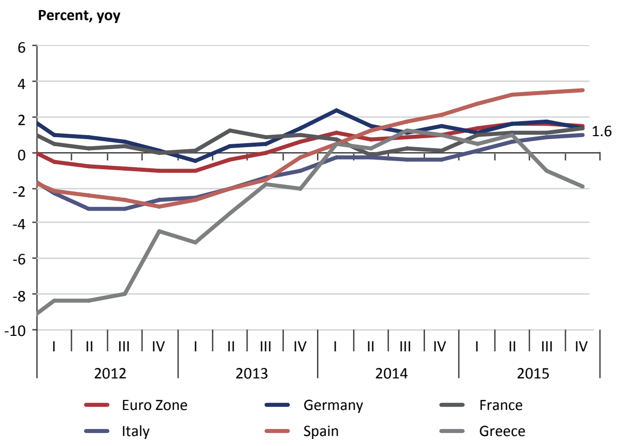
Manufacturing activity in Europe remained expansive and was balanced throughout the core countries (Chart 1.8). Manufacturing expansion in Europe was supported by strong domestic demand despite slower export growth. Solid domestic demand managed to improve manufacturing sector performance, which boosted manufacturing output. Such conditions ultimately raised the GDP outlook, considering the historically positive

Chart 1.6. U.S. Housing Sector



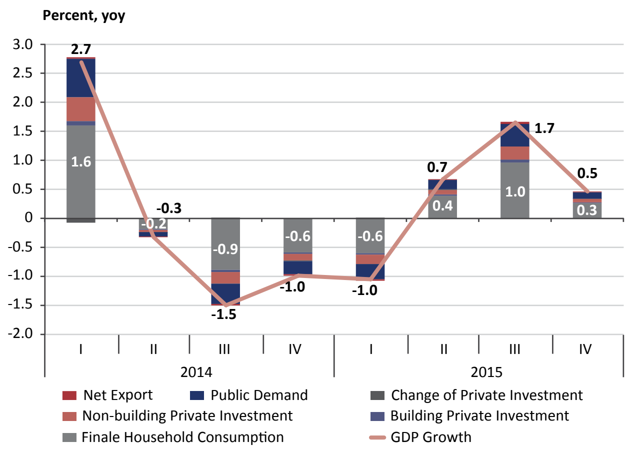
Source: Bloomberg, processed

Chart 1.7. **Euro Economic Growth**



Source: Bloomberg, processed

Chart 1.9. **Japan Economic Growth**



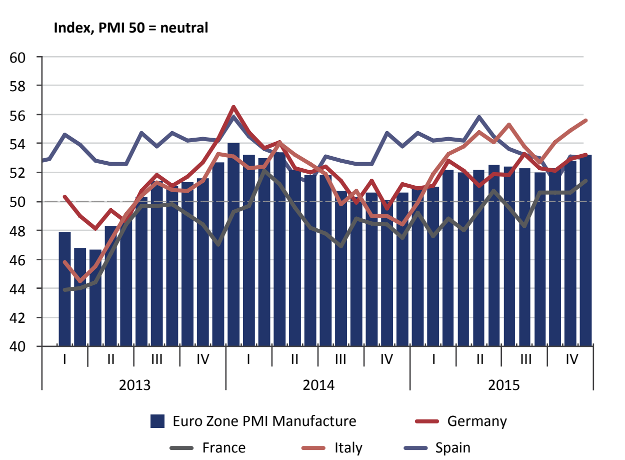
Source: Bloomberg, processed

correlation between Purchasing Managers' Index (PMI) and GDP in Europe. Nonetheless, export growth continued to decrease in line with the sluggish global economy, primarily in the form of less demand from China and other emerging market countries.

The economy of Japan also improved in 2015, growing by 0.6% and reversing the 0.03% contraction posted in 2014. Nevertheless, the economic recovery in Japan was slow and relatively weak, reflecting limited gains in the consumption sector throughout 2015 (Chart 1.9). Weak consumption was driven by limited gains on the labor market, an ageing population, the government's austerity policy, and compounded by policy to raise the sales tax in April 2014. Support for the labor sector to improve consumption was also inadequate, with an unstable level of unemployment reported along with limited salary growth. Insufficient support for the labor sector manifested when corporate profits were not passed on to the employees. Consequently, consumers lost confidence and put off consumption.

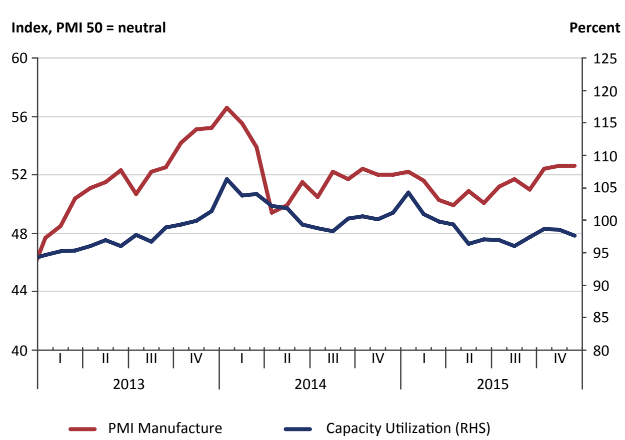
Manufacturing sector gains did, however, help to drive economic growth in Japan, with the corresponding manufacturing indicators following an expansionary phase in the second half of the year (Chart 1.10). Despite spillover from the economic moderation happening in China, demand for exports from Japan was bolstered by advanced countries that had enjoyed recent economic improvement. In addition, domestic demand also increased due to seasonal factors during the approach to yearend holidays, which boosted manufacturing sector performance at the end of 2015.

Chart 1.8. **Euro Manufacturing Sector**



Source: Bloomberg, processed

Chart 1.10. **Japan Manufacturing Sector**



Source: Bloomberg, processed

1.2. ECONOMIC GROWTH AND INFLATION IN EMERGING MARKETS

In contrast to advanced countries, the economies of emerging market countries continued to slow, while inflationary pressures continued to accelerate. The slowdown was led by economic moderation in China and the inherent spillovers therein through lower commodity prices, the trade channel as well as the confidence channel considering China's significant role in the economies of other emerging market countries. On the other hand, capital flows to emerging market countries ebbed in line with global monetary policy divergence, which heightened volatility on financial markets, along with deleveraging in advanced countries. Such conditions weakened domestic exchange rates and intensified financial risks. Moreover, structural problems and domestic policies were also responsible for economic disparity amongst the different countries.

The economies of emerging market countries grew slower in 2015 at 4.0% on average compared to 4.6% the preceding year earlier. Despite decelerating, emerging market countries maintained their dominant contribution to global economic growth in 2015, consistent with the 58% contribution of emerging market countries to the global economy and higher level of growth (4.0%) compared to advanced countries (1.9%). Meanwhile, inflation in emerging markets stood at 5.6% in 2015 compared to 5.1% in 2014 as a result of significant depreciation in countries such as Russia, Brazil, and other Latin American countries. In contrast, countries such as China and Indonesia achieved lower inflation in 2015 due to the ongoing international commodity price slide, including oil prices.

Economic moderation in China, as a primary determinant of global economic performance, was a consequence of economic rebalancing policy instituted by the authorities in China. Rebalancing was sought to transform the domestic economy from investment driven to consumption driven. In that context, economic transformation was pursued in China in order to achieve higher quality, sustainable economic growth in the long-term.[4] In its implementation, investment growth slowed throughout 2015, while the acceleration of consumption was inadequate to sustain overall growth.

In line with that, credit growth followed a downward trend in China during the second half of the year. In addition, the manufacturing sector experienced a prolonged contraction in line with deteriorating external sector performance in the form of dwindling demand for exports as the global economy moderated against a backdrop of sluggish domestic demand. The Chinese economy was also replete with external pressures linked to deluge of foreign capital outflows stemming from global monetary policy divergence. In response, the China's authorities introduced a series of policies to maintain macroeconomic stability and stave off further economic declines. Consequently, China's economy grew 6.9% in 2015, down from 7.3% the year earlier.

The various policies instituted by the Chinese authorities began to bear fruit at the end of 2015. Retail sales rebounded in 2015 to 11.1% (yoy) or 17.2% (qtq), the highest level in the past four years. Meanwhile, household disposable income grew 8.1%, surpassing GDP growth, despite prevailing stock market shocks. On the other hand, property construction began to rebound at the end of 2015 despite growth remaining in negative territory.

Economic moderation in China, combined with industrial policy that supressed domestic value added, undermined trade performance in other emerging market countries as trading partners of China. Also, this strategy was reflected in a decrease in the role of China in the global value chain. The current account deficit in China expanded, while external sector performance tended to decline. ASEAN member countries and South Korea are solid examples of emerging market countries affected by spillover from China's flagging economy through the trade channel.

Growth slowed in various emerging markets, as net producers of commodities, in line with the protracted international commodity price slide throughout 2015. The commodity price contraction reduced revenues in EM net-exporters through wider current account deficits. Additionally, domestic structural and political issues in each respective country exacerbated domestic economic declines. Brazil, México, Nigeria, Russia, and Saudi Arabia are examples of emerging market countries that experienced economic moderation due to soft commodity prices coupled with structural and political issues.

The economy of India, as an emerging market country, maintained robust growth. The country recorded growth of 7.5% in 2015, accelerating on the previous year. Nonetheless, the high level of growth recorded in India was also partially due to an upward revision as a result of changing the method to calculate GDP growth at the

4 China's Third Plenum, 2013.

beginning of 2015.[5] Domestic demand, however, remained strong, supported by government-led infrastructure projects. Although India was affected by weaker demand for exports from China, the domestic manufacturing sector remained expansive on the back of domestic demand, reflecting restored economic sentiment, robust car sales, production output gains and an improved infrastructure index.

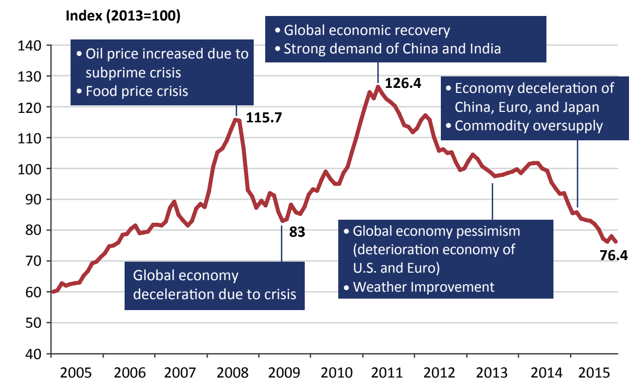
1.3. GLOBAL COMMODITY PRICES

International commodity prices faced numerous corrections throughout 2015. On an annualised basis, the Indonesia Export Price Index contracted -15%, deteriorating from -4.2% in 2014 (Chart 1.11).[6] The deeper Indonesia Export Price Index contraction was a result of the global economic slowdown, specifically China as the leading consumer of products exported from Indonesia. The close relationship between commodity prices and economic performance in China is reflected in the strong correlation between the international non-fuel commodity price index and economic growth in China at 0.7 (Chart 1.12).

Sliding export commodity prices in Indonesia during 2015 mainly affected coal, crude palm oil (CPO), and rubber. Accordingly, the coal price fell 24.5% in 2015 due to fewer shipments to China in line with China's policy to protect domestic industry as well as policy to reduce carbon emissions from power stations. Meanwhile, the price of CPO dropped 8.2%, triggered by oversupply in Malaysia. Furthermore, low international soybean and crude oil prices, as substitute products, also lowered the price of CPO. The price of rubber sank 18.6% in 2015 due to a slump in demand from China for natural rubber. A decrease in the rubber price in line with a shift in demand from natural to synthetic rubber, which also fell in price consistent with cheaper oil. Moreover, a declining automotive industry further exacerbated downward pressures on rubber prices.

In terms of crude, the world oil prices followed a downward trend in 2015. This situation was due to oversupply from OPEC and non-OPEC countries

Chart 1.11. Development of Export Commodity Prices

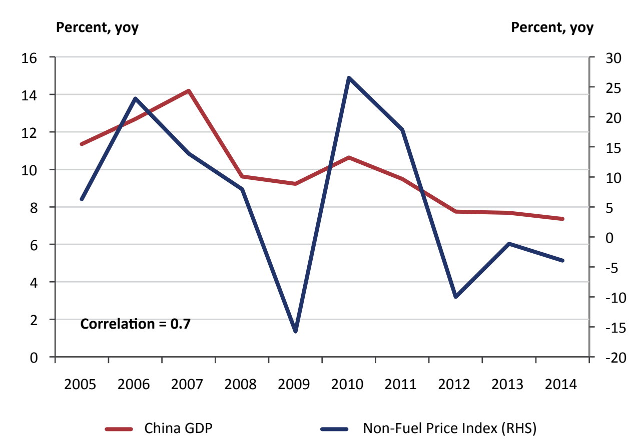


Source: Bloomberg, processed

despite dwindling demand because of global economic moderation. In addition, broad U.S. dollar appreciation throughout 2015 made oil prices relatively more expensive for the majority of countries not using the U.S. currency. It also contributed to lower demand for oil. At the end of 2015, the oil price faced yet another correction, despite declines in terms of oil production and rig counts in the U.S. This correction was caused by the large U.S. oil inventory which prompted negative sentiment and additional downward pressures on oil prices.

Although oil prices fell to nearly price in 2008, production continued to increase in 2015 sourced either from OPEC or non-OPEC countries. Higher production from OPEC members during 2015 was part of a strategy amongst oil producers to maintain market share. The strategy was

Chart 1.12. China GDP and Non-fuel Commodity Price



Source: CEIC, processed

5 Under the old method, GDP growth in India in 2013 and 2014 stood at 4.7% and 5.6% respectively. The change to calculating GDP in India involved a change to the base year and a change from factor cost to market price in accordance with the System of National Accounts (2008).

6 A composite index of major export commodity prices from Indonesia, including coal, crude palm oil (CPO), rubber, copper, nickel, tin, aluminum, and coffee.

spearheaded by Saudi Arabia, where oil production costs are remarkably low at just USD5 per barrel. On the other hand, non-OPEC oil producers, primarily the U.S., enjoyed improved production efficiency. Therefore, the lower rig count did not translate into significantly less production.

Moving forward, the risk of lower oil prices is high. The risk of further oil price declines could stem from policy to ease export restrictions in the U.S., additional oil supply from Iran after reaching a nuclear deal as well as limited potential declines to production in OPEC members due to narrower fiscal space coupled with geopolitical instability.[7] Nonetheless, there also remains the risk of incrementally rising oil prices in line with less supply from the U.S. due to less investment in the oil sector. This is possible albeit still net total world oil supply.

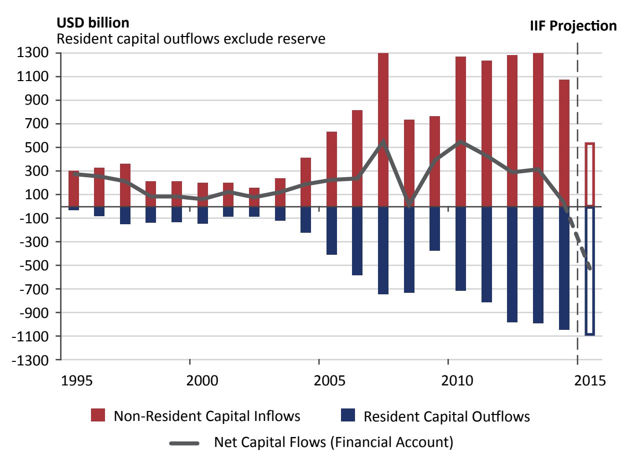
1.4. GLOBAL FINANCIAL MARKETS

Global financial markets in 2015 were blighted by heightened volatility, reflecting increased uncertainty. Heightened volatility was primarily triggered by uncertainty beginning at the end of 2014 surrounding the magnitude and timing of the proposed FFR hike in the U.S., followed by the debt crisis unfolding in Greece in March 2015, yuan devaluation in August 2015 and deep corrections on China's stock markets in the same month.[8] Initially, the proposed FFR hike was expected to take place in the middle of 2015 but expectations were shifted backwards after the release September FOMC meeting on 8th October 2015, which eased volatility stemming from uncertainty. Thereafter, however, strong U.S. economic data along with the official statement relayed at the FOMC in October 2015 brought expectations forward until the end of 2015, which again triggered uncertainty on financial markets. Ultimately, the Federal Reserve raised its policy rate by 25bps at the FOMC in December 2015. Nonetheless, considering that the increase had already been widely anticipated by the markets, excessive shocks on global markets due to the 25bps bump did not materialise. On the other hand, the European Central Bank (ECB) and Bank of Japan (BoJ) extended quantitative easing policy throughout 2015, which led to global monetary policy divergence. Such conditions, accompanied by deleveraging in advanced countries and a shift in the composition of global liquidity following the normalization of U.S. monetary policy, eroded capital inflows to emerging market countries, leading to negative net flows (Chart 1.13).

In addition to the developments transpiring on global financial markets, the global composite stock price index slumped to 142.3 at the end of 2015 from 146.3 at the end of 2014. Similar conditions were reported in terms of composite stock price indexes in Asian emerging market countries, Asia-Pacific countries and G-7 countries. On average, however, composite stock price indexes in Asian emerging market countries, Asia-Pacific countries and G-7 countries were relatively stable. The yields of government bonds, specifically in net-exporting emerging market countries such as Brazil and other Latin American countries, were observed to increase as the economic outlook deteriorated in line with sliding commodity prices (Chart 1.14 and 1.15).

Market sentiment regarding uncertainty surrounding the magnitude and timing of the proposed FFR hike along with economic developments in China influenced global stock market performance throughout 2015. In 2015, global stock prices rallied on the back of economic gains in advanced countries. Nonetheless, global stock market performance plummeted in the second semester 2015 due to uncertainty over the timing of the FFR hike and stock market shocks in China that spilled over to affect other global bourses. In the middle of 2015, China's stock

Chart 1.13. **EM Capital Flows Development**

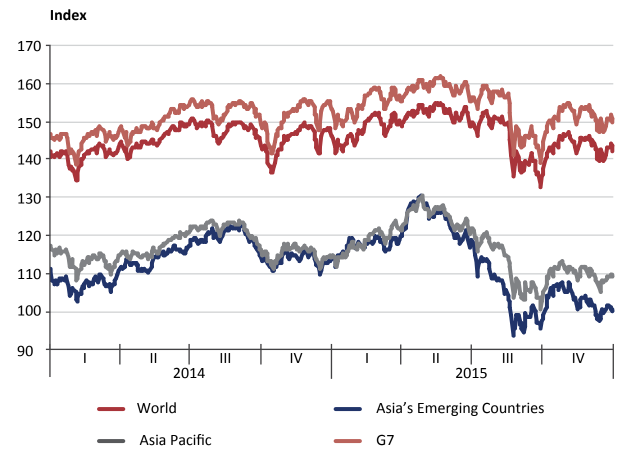


Source: Capital Flows for Emerging Markets – IIF, January 2016

7 According to prevailing policy, oil exports from the U.S. account for just 5% of total production and oil producers require a license from the U.S. Government to export crude oil, with the exception of exports to Canada and exports of condensed oil. With such export restrictions in place, the U.S. oil market suffers from abundant oversupply, leaving U.S. oil prices lower than international prices. If U.S. export restrictions were lifted, the price disparity would narrow.

8 The Greek debt crisis surfaced in March 2015 when the Greek government extended the repayment of its external debt by four months. At the end of June 2015, however, crisis conditions peaked when the Greek Government had spent all of its cash on public necessities. Uncertainty concerning whether Greece would be able to service its debt spurred widespread shocks on global financial markets.

Chart 1.14. **Global Stock Market Development**



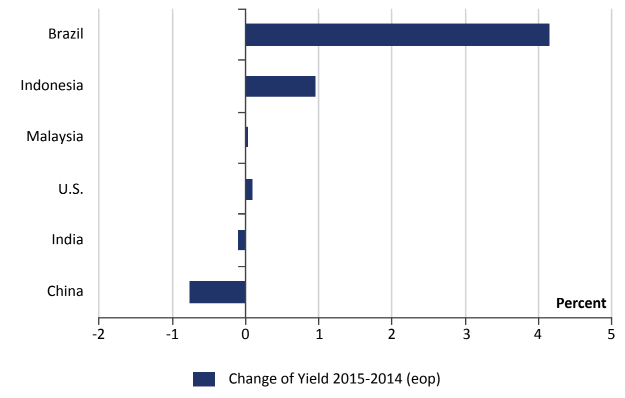
Source : Bloomberg, processed

Chart 1.16. **Shanghai Stock Exchange Composite Index**

Source: Bloomberg, processed

markets slumped dramatically, triggered by concerns of an economic slowdown. Consequently, the Shanghai Stock Exchange Composite Index plunged drastically by 75% in July and August 2015 (Chart 1.16). Furthermore, the unexpected decision to devaluate the yuan in August 2015 exacerbated already intense pressures on financial markets in China and other emerging market countries.[9] Built-up uncertainty on China's financial markets due to yuan devaluation was reflected by an increase in credit default swaps (CDS) and the magnitude of decline in the position of reserve assets, equivalent to USD512 billion in 2015.

Chart 1.15. **Government Bond Yield Development**



Source : Bloomberg, processed

9 Yuan devaluation on 11th August 2015 was the highest recorded in the past five years and was prompted by a more market-driven exchange rate regime change after the CNY was included in the SDR basket. Consequently, the exchange rate was determined based on the following criteria: (i) the USD/CNY level of the previous day; (ii) demand/supply factors; and (iii) the market movements of other currencies.

Therefore, corporate external debt risks also surfaced in China. Accordingly, yuan depreciation more than doubled the position of corporate external debt. The build-up of risks and uncertainty ultimately spilled over to global stock markets due to fears of a deeper economic downturn in China.

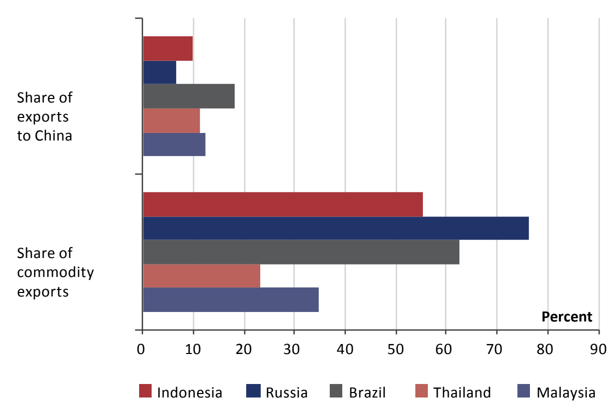
Box 1.1 Emerging Market Performance in the Face of China's Economic Moderation and Sliding International Commodity Prices

Economic moderation in China, as the second largest global economy, has directly and indirectly influenced the export performance of emerging market trading partners. Furthermore, the economic downshift in China has also undermined demand for commodities in line with China's role as one of the largest global consumers. Such conditions have depressed international commodity prices and undermined export performance in net exporting emerging markets.[1] This Box aims to compare performance and policy responses across a number of emerging market countries, namely Malaysia, Thailand, Brazil, Russia, and Indonesia itself in the face of such arduous conditions.

The impact of economic moderation in China and sliding international commodity prices on emerging market countries was influenced by the respective trade structure of each country. Higher dependence on primary sectors or industrial commodities exacerbated the impact of lower commodity prices on external sector performance, which ultimately affected overall economic performance. Of the five emerging market countries in the observation sample, Russia accounts the largest share of export commodities (76.4%), followed by Brazil (62.4%), Indonesia (55.4%), Malaysia (34.8%), and Thailand (23.3%) (Chart 1). In addition to confronting lower commodity prices, the five sample countries were also subjected to capital outflow pressures to varying degrees. The full panoply of policy responses has been formulated and instituted in response to the external pressures faced, paying due consideration to economic, social and political conditions in each respective jurisdiction.

When formulating the appropriate policy mix, limited fiscal and monetary space can impede optimal policymaking to alleviate the external pressures faced. Table 1 shows that in line with its high dependence on export commodities, Russia experienced the deepest contraction in 2015 compared to the other emerging market countries. The decline was not only precipitated by lower oil and commodity prices but also economic sanctions imposed due to the Ukraine crisis. A persistently weaker economic outlook, combined with a shift in the composition of global liquidity, subsequently triggered capital outflows from Russia. The state responded by releasing peg the Russian ruble against the U.S. dollar and euro. Thereafter, exchange rate depreciation heightened inflationary pressures,

Chart 1. Export Structure of Several EM Economies



Note: based on SITC 3 category 0-4, WITS-World Bank, 2014

thereby constricting room to further ease monetary policy.[2] From a fiscal perspective, the Government of Russia strived to maintain a low deficit despite a dramatic decline in export receipts from oil and gas, accounting for just 52% of the previous year. To maintain a low deficit, the Government of Russia decided against providing the fiscal stimuli required to avert a deeper economic contraction.

Similar circumstances prevailed in Brazil, with the second largest share of export commodities in the sample and the

Table 1. Economic Indicators in Several EM Economies

Economic Indicator	Year	Malaysia	Thailand	Brazil	Russia	Indonesia
GDP Growth (%)	2014	6.0	0.9	0.1	0.6	5.0
	2015	5.0	2.8	-3.0	-3.7	4.8
Inflation (%)	2014	3.1	1.9	6.4	7.8	6.4
	2015	2.7	-0.9	11.3	12.9	3.3
Policy Rate (%)*	2015	3.25	1.5	14.25	11	7.25
Exchange Rate depreciation	2015	19.3	5.5	41.6	17.8	10.2
Fiscal deficit (%GDP)	2015	6.5	2.5	10.3	2.6	2.5

Note:
*At the end of 2015
Source: CEIC, processed

1 According to IMF data, commodity and energy prices in 2015 contracted 35.3%, while non-fuel prices contracted 17.5%.

2 Nonetheless, the Central Bank of Russia still lowered its policy rate by 600bps from the beginning of the year until August 2015.

largest export share to China. The external sector of Brazil also sustained intense pressures during 2015. However, fiscal space was limited due to a wide government deficit stemming from various economic problems in recent years coupled with political instability. On the monetary side, monetary policy space was also narrow as a result of high inflation and a deluge of capital outflows that led to severe Brazilian real depreciation (Table 2). Consequently, Brazil's economy suffered from a deep contraction in 2015.

Meanwhile, the economies of Indonesia and Malaysia posted positive growth despite slowing on the previous year. Both countries have a number of differences, however, in terms of the trade structure and policy response. Indonesia has a relatively large share of export commodities to total exports, thus the potential decline in external performance was more pronounced than in Malaysia. Bracing for the impact of external pressures, Indonesia instituted prudent monetary policy mixed with an accommodative macroprudential policy and fiscal stimuli. To spur domestic demand and long-term growth, the Government of Indonesia also increased capital spending on strategic infrastructure projects. The fiscal space created by the Government was attributed to fiscal reforms, involving significant reductions to energy subsidies. The Government did face fiscal challenges, however, in the form of smaller revenue from the oil and gas sector, which accounted for 20% of total government revenue in 2014.

On the other hand, Malaysia enjoyed broader export product diversification in comparison to Indonesia so the impact of lower commodity prices was less pronounced. Notwithstanding, the global economic slowdown still triggered pressures on exports from Malaysia due, amongst others, to the large export share to China. Global pressures coupled with simultaneous political turmoil in Malaysia drove foreign capital out of the country, leading to significant ringgit depreciation. In addition, the Government of Malaysia experienced a decline in receipts from the oil and gas sector, the impact of which was notable because 30% of government revenues stemmed from oil and gas in 2014. Consequently, the government reduced subsidies and streamlined operational spending while introducing tax reforms to manage the fiscal deficit.3 The various policies helped to maintain relatively robust economic growth in Malaysia despite a 1% drop on the previous year.

Furthermore, Thailand, with the smallest share of export commodities, succeeded in boosting domestic economic growth. This condition was influenced by broad export product diversification, including high-tech manufacturing products, as well as the monetary and fiscal policy mix applied. Controlled inflation provided adequate space to ease monetary policy. Also, the Government of Thailand implemented fiscal expansion by accelerating government spending disbursements for transport and irrigation as well as introduced stimulus packages to the tune of USD11 billion aimed, amongst other, at helping micro, small, and medium enterprises (MSMEs) repay loans and settle taxes. Government fiscal stimuli were also disbursed to rural areas through the "Village Fund" scheme in the form of concessional loans and government investment projects in rural areas. The prevailing fiscal response sparked additional domestic demand and restored public confidence in the Thailand economic outlook.

Table 2. **Policy Response Indicators in Several EM Economies**

Policy Response Indicator	Malaysia	Thailand	Brazil	Russia	Indonesia
Change of policy rate*	0 bps	-50 bps	200 bps	-600 bps	-25 bps
Additional Fiscal Deficit*	0.0	0.3	3.6	2.0	0.2

Note:
*Compare to the end 2014
Source: CEIC, processed

3 Commencing on 1st April 2015, the Government of Malaysia introduced the Goods and Services Tax for businesses as a replacement for the Government Sales and Services Tax.

As a form of international cooperation, the Finance Ministers and Central Bank Governors of the G20 convene regular meetings. On 4-5th September 2015, such a meeting was held in Ankara, Turkey, where members agreed the pressing need to stimulate economic growth and boost investment.

Chapter 2

Global Economic Policy Response

Accommodative monetary policies were the crux in the mix of policy responses that advanced economies (AE) had carried out to revive growth amidst the global economic slowdown. The lack of supporting fiscal policies and sufficient structural reforms, however, resulted in different recovery phases and divergent monetary policies among the AE. Meanwhile, emerging markets (EM) had taken up relatively more comprehensive mix of policy responses. International cooperation was also strengthened to drive more quality growth and maintain stability in the financial system. Nevertheless, all these policy responses have yet to significantly spur global economic growth.

In 2015, monetary policies were the primary measure for the world's economies, particularly for the AE, which had applied their monetary policies by way of interest rate instruments and quantitative easing (QE) policies. The United States (U.S.) Federal Reserve System (The Fed) had normalized its monetary policies and raised its benchmark rate. Meanwhile, the European Central Bank (ECB) and the Bank of Japan (BoJ) still kept their benchmark rates down and continued with their QE policies. This difference in monetary policies reflects the different recovery phases within the AE. The Fed's policies were in line with the U.S. economy's improving fundamentals, particularly in the labor market. On the other hand, the policies of the ECB and the BoJ were in response to the ongoing risk of deflation and continued slowdown.

Meanwhile, the policy responses of the EM had relatively been more comprehensive than those of the AE, due to the complexity of the problems that the EM had to address. The monetary policies of the EM were in general complemented with fiscal policies and structural reforms. Most emerging market economies had taken up loose monetary policies followed by fiscal stimulus in the form of increased government spending. Developing countries had also carried out structural reforms to address each of their relevant structural problems. These structural reforms were mainly focused on providing proper infrastructure, improving the investment climate, and addressing population issues. The EM's policy responses were also aimed to mitigate the financial market turmoil as the impact of the global economic slowdown and the normalization of monetary policy of the U.S.

The outcome of the global economic policy responses remained limited, as worldwide economic growth continued its downturn from 2014 and fell short of its estimates. This was mainly due to the policy responses having relied too much on monetary policies. With limited support from fiscal policies and structural problems remaining unaddressed, recovery within the AE was only moderate. Meanwhile, the monetary policies of the EM alone were also unable to prop up global growth. This was partly related to the fact that the implementation of accompanying fiscal stimulus and structural reforms that still need time before having any actual effect towards the economy.

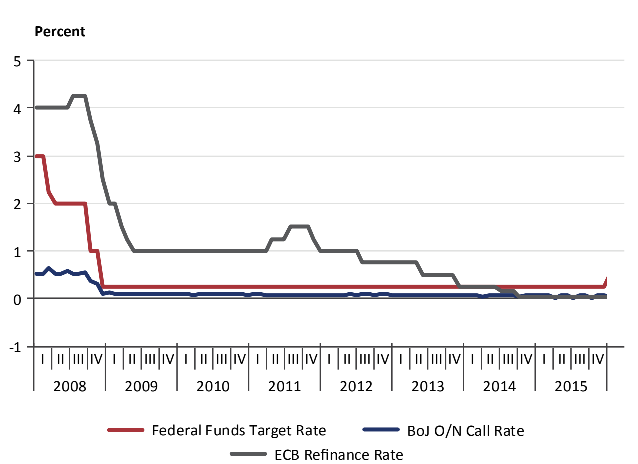
The global economic slowdown and risks of financial market turmoil has thus been a major concern for international cooperation forum. Efforts on reviving growth and maintaining financial market stability have become the main discussion in the forums. With stronger economic cooperation, it is expected that a solution can be found for achieving higher and more sustainable quality growth, while maintaining stability in the financial system, and build up regional economic resilience.

2.1. POLICY RESPONSE OF ADVANCED ECONOMIES

The policies of the U.S. were in response to the country's improving economy, particularly in the labor market. This improvement in the economy led the U.S. monetary authority to believe that the inflation rate will reach 2% in the medium-term. As an anticipatory measure, The Fed then normalized its monetary policies by raising its reference rate during the Federal Open Market Committee (FOMC) meeting in December 2015 (Chart 2.1).

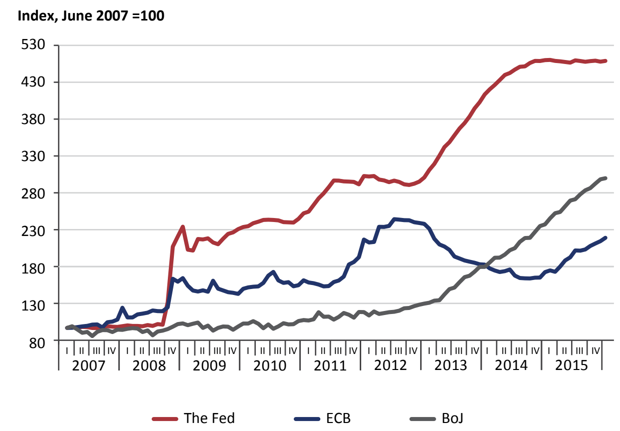
The Fed had carried out several preparatory measures as well before normalizing its monetary policies, by way of three main policies. First, rolling over its holdings of maturing U.S. Treasury securities to maintain its balance sheet in line with accommodative monetary policies (Chart 2.2). Second, setting up relevant liquidity management instruments to guide market interest rates towards their intended levels. The instruments in this case were interest rates on bank reserves and large-scale reverse repo transactions. The third and last policy was carrying out an effective communication strategy to provide a forward guidance for the market on the direction of its monetary policies. The Fed had indicated that it will keep its benchmark rate low throughout 2015. It then clearly hinted of a rate increase during the FOMC meeting in October 2015, and actually raised the rate by the end of the year.

Chart 2.1. The Fed, ECB, and BoJ Reference Rate



Source: Bloomberg, processed

Chart 2.2. **The Fed, ECB, and BoJ Total Assets**



Source: Bloomberg, processed

The Fed's decision during the December 2015 FOMC meeting to raise its Federal Funds Rate (FFR) target to between 0.25% and 0.5% was not considered as a tightening of its monetary policy. The Fed stated its stance of remaining accommodative, and explained that the rate hike was part of normalizing its monetary policy to maintain stable market prices. The Fed believed that the improving U.S. labor market will lead to inflation reaching 2% in the medium-term. Looking further ahead, The Fed has hinted that the FFR will be raised gradually, in line with its strategy to keep the momentum for recovery while anticipating risks from the global economic slowdown.

In the Euro area, policies were carried out to respond to the threat of deflation and sluggish economic growth in Europe. The ECB therefore decided in January 2015 to carry out more aggressive QE measures through the Expanded Asset Purchase Programme (EAPP). The EAPP was intended to spur the region's domestic demand through the financial sector and the credit market, and was implemented through the purchasing of EUR60 billion in assets, including Eurozone government bonds. The EAPP was carried out between March 2015 and September 2016, and continued ECB's loose but more passive monetary policy during 2008-2014.[1]

In terms of conventional monetary policy, the ECB kept its reference rate at a very low level of 0.05%. The ECB also cut its deposit facility rate by 10 basis points (bps) to -0.3% in December 2015. This negative interest rate policy was intended to encourage credit growth in the Euro area. It is taken given that credit growth as the main financing source of European economic activities was still quite low.

With inflation in the Euro area still far below its intended level the ECB expected to perform additional policies. The ECB is expected to resort to further non-conventional monetary policies. These include carrying out open-ended QE measures and increasing its asset purchases. Further rate cuts will possibly be off the desk for the meantime, for fear of risking negative effects on the banking sector.

Similar to Europe, Japan's policy response was carried out to revive growth and address deflationary risks, relying on a combination of monetary policies and fiscal policies. The BoJ maintained its accommodative monetary policies by keeping its benchmark rate at a very low level of 0.1% throughout 2015. The BoJ also continued with its QE measure by purchasing up to JPY80 billion in assets each year. In terms of fiscal policies, the Japanese government allocated up to JPY3.5 billion as a fiscal stimulus, and in February 2015 announced tax incentives for companies raising their workers' pay. In April 2015, the fiscal authorities also postponed the implementation of the second phase of the sales tax from 8% in October 2015 to 10% in October 2017.

All of Japan's efforts have, however, yet to significantly revive its economy. Growth remained sluggish. Growth in domestic consumption was off target. This was due to Japan's rigid labor law holding up the tax incentives for companies raising their workers' pay. Postponing the sales tax hike also failed to spur more consumption. The fiscal policies even caused credit rating agencies Fitch and Moody's to downgrade Japan's credit rating by a notch to A, as the policies were seen as increasing risks on the economy.

This limited impact on the economy is expected to compel Japan to carry out more stimulus policies. The BoJ is expected to top up its QE asset purchases. Application of negative interest rates policy is also a policy option that may be taken by BoJ. From the fiscal side, the Japanese government's limited fiscal space has left it with few options other than carrying on with its previous policies.

One of the most urgent structural problems that Japan and other developed countries needs to address is their ageing population. As the number of older-aged people increases within a population, the level of savings also increases to the point of slowing down consumption. The population's high dependency ratio also affects its

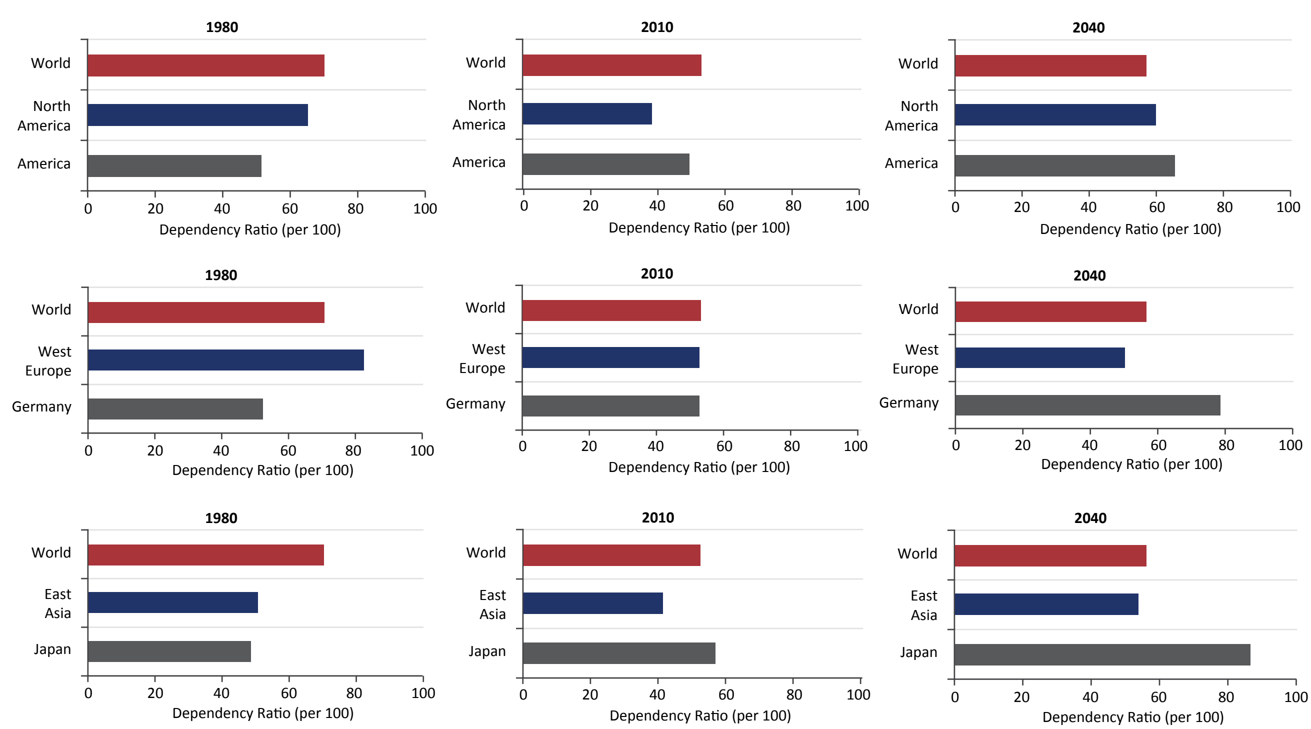
1 LTRO (Long-Term Refinancing Operation), CBPP (Covered Bond Purchase Programme), and ABSPP (Asset-Backed Securities Purchase Programme).

productivity level due to the increasing number of non-working people. Older-aged populations are also prone to fiscal drag, in which tax revenues decline while spendings for health care and pensions increase. The median age of Japan's population in 2014 was 46 years, with a life expectancy of 84 years, the highest in the world. By age, Japan's population is composed of 13% of young people (0-14 years), 61% of people in the productive age (15-64 years), and 26% of elder people (> 65 years). Japan's dependency ratio is therefore 63%, higher than both the world average and other developed countries (Chart 2.3).

This demographic condition has made it difficult for Japan to carry out reforms to increase consumption levels. The Japanese government has since 1985 encouraged people nearing retirement and those already retired to continue working, and had increased the retirement age from 55 years to 60 years. Yet with a fertility rate among the lowest in the world (only 1.4 children per female population), while its health care service is among the world's best, Japan's demographic condition is unlikely to change for the better.[2] Policy measures to address structural problems due to demographic conditions are not trivial and require time to be effective. Experience from several developed countries in increasing their fertility rates to improve their demographic structure has proven to be difficult. Such condition relates to the individual preferences and lifestyles of each country. Meanwhile, short-term measures such as immigration are also difficult to implement, due to political opposition and potential risks of social unrest.

Another structural problem that needs to be addressed by developed countries, particularly in Europe and Japan, is their limited fiscal space.[3] This condition is caused by the level of public debt has been high. A study by credit rating agency Moody's reveals that while the U.S. and a few European countries still have sufficient fiscal space, most other European countries such as Portugal, Ireland, Spain, France, and Belgium have only limited fiscal space. Japan, Italy, Greece, and Cyprus similarly have only limited fiscal space, such that increasing public debt would be risky towards macroeconomic stability (Chart 2.4).

Chart 2.3. Advanced Countries Dependency Ratio

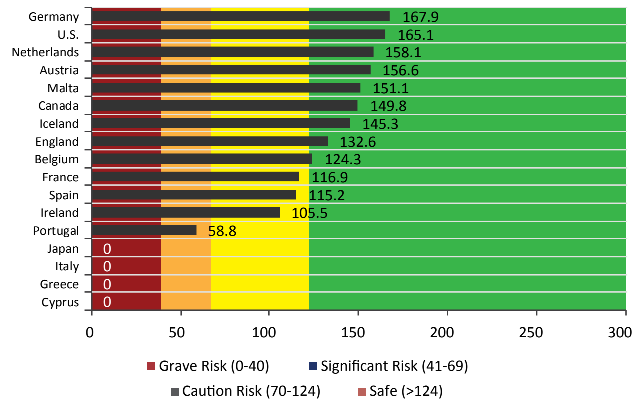


Source: BBC Capital, UN World Population Projection

2 According to the World Bank's 2015 data on Japan's population.

3 The International Monetary Fund (IMF) defines fiscal space as room in a country's state budget that can still be utilized without exceeding the budget's debt allocation or creating risks on the country's macroeconomic stability.

Chart 2.4. Advanced Countries Fiscal Space



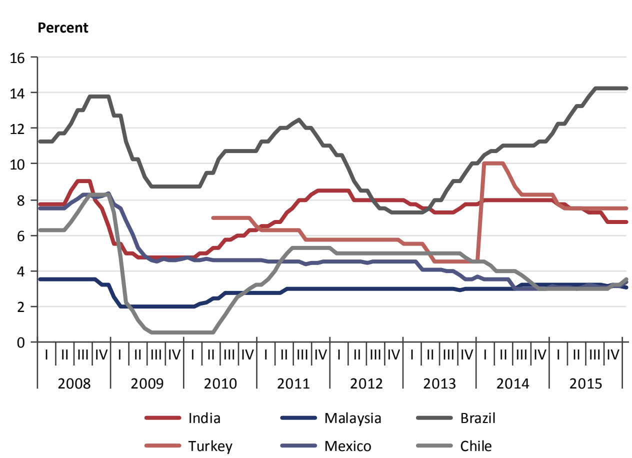
Source: Moody's Analytics, 2015

2.2. POLICY RESPONSE OF EMERGING MARKETS

The monetary policies of most EM throughout 2015 were accommodative, in response to the downturns in their respective economies. However, not all EM conduct an accommodative monetary policy. Several EM in Latin America such as Brazil, Mexico, and Chile, however, had resorted to tighter monetary policies, to manage inflationary pressures due to depreciations in their respective currencies (Chart 2.5).

Apart from accommodative monetary policies, most of the EM also carried out structural reforms. Those reforms included reforming their financial markets, increasing the capacities of their economies, and developing infrastructure. Deregulations were also carried out to improve the investment and business climate. Other structural reforms were aimed at reducing reliance on the external sector and increasing the consumption of local products.

Chart 2.5. Policy Rate in Emerging Markets



Souce: Bloomberg

China was among the EM that actively put out policies with wide spectrums throughout the year. The policies were a mix of monetary policies, macroprudential measures, and structural reforms for the finance, fiscal, manufacturing and trade sectors, as well as for addressing relevant population issues. The policies were varied in their time-frames, intended to address short-term, medium-term and long-term issues altogether, despite this different timing of the policies' targets had itself created a complexity in their implementations.

The slowdown of China's economy had compelled the country's authority to ease up on its monetary and macroprudential policies. The People's Bank of China (PBoC) cut its benchmark interest rate five times during 2015, by as much as 125 bps down to 4.35%. The PBoC also carried out macroprudential policies that included lowering both the targeted and overall minimum reserve requirement, easing the loan-to-value requirement, and injecting liquidity to several banks to increase lending. Other macroprudential policies included mitigating the risks from shadow banking activities, which was implemented by converting the debts of local government financing vehicles to banks, into municipal bonds. These municipal bonds could then be used as collateral for monetary operations.

Regarding the financial markets, China modified its currency regime and pursued market liberalization. The Chinese renminbi (or yuan)'s daily exchange rate band was widened from 1% to 2% in March 2015. The yuan's fixed exchange rate had since August 2015 also been made more flexible and market-driven.[4] Liberalization of the financial market, meanwhile, was carried out by opening up more access for foreign investors to China's onshore markets. China also promoted the yuan's international standing, by developing offshore transactions at other global financial centers, such as Singapore and London, apart from previously only at Hong Kong. This financial market liberalization and promoting the yuan's international standing is part of China's commitment to get the yuan included in the International Monetary Fund's (IMF) Special Drawing Rights (SDR) basket of currencies,

4 The yuan exchange rate now refers to the U.S. dollar exchange rate during the previous trading day, the demand and supply of foreign currencies, and the movement of other money markets.

which the IMF approved in November 2015.[5] Besides its economic advantages, the yuan's inclusion into the IMF's SDR basket is strategically important in boosting China's geopolitical role.

China also embarked on several structural reforms to meet the target of doubling its gross domestic product (GDP) and income per capita by 2020. The structural reforms included increasing domestic consumption, as well as stabilizing investments and exports. For that, China launched several long-term strategies, such as "Made in China 2025" and "One Belt One Road". The "Made in China 2025" program aims at upgrading the quality of the country's manufactured goods. Meanwhile, the "One Belt One Road" program is an initiative to bolster investments abroad and expand export markets. Other long-term structural reforms included replacing the 1-child policy, which had been enforced since 1978, with the two-child policy since October 2015. This policy is intended to anticipate potential ageing population issues, which are expected to affect China in the middle of the 21st century. The policy is also expected to maintain China's dependency ratio in line with efforts to rebalance its economy.

China's simultaneous efforts, however, had created complications of its own. Policies to rebalance its domestic economy, amidst the global economy slowdown, caused growth to decelerate below estimates. This in turn caused rapid deleveraging of China's economy and disrupted its financial markets, particularly the stock market. These shocks to the financial markets resulted in capital outflows, a weakening of China's currency, and a sharp decline to its foreign exchange reserves. The yuan's recent inclusion into the IMF's SDR basket, which required China to liberalize its financial markets, made it even more difficult to stabilize the markets.

This financial market turmoil jeopardized China's long-term economic goals. The government of China responded with tighter policies to stabilize the situation. China's monetary authority tightened its control over the currency exchange rate fixing, and consistently intervened in both the onshore and offshore forex markets. In September 2015, China's monetary authority set a minimum reserve requirement, without remuneration, of 20% for outstanding forward transactions. In December 2015, it introduced the Renminbi Trade Weighted Index (TWI) as a market guidance, so as not to refer only to the exchange rate against the U.S. dollar.

5 The Chinese yuan will effectively be included in the IMF's SDR basket on October 1, 2016.

Policies to stabilize the stock market were also carried out. Since July 2015, China's stock market authority has forbidden shareholders of over 5% in stock to sell any shares within 6 months of purchase. Authorities also encouraged state-owned enterprises (SOEs) and public companies to purchase shares and forbade any kind of short selling in the stock markets. Stock holdings were also allowed to be collateral for bank loans.

Among the EM, India was one of the countries that responded to the economic situation in 2015 with a consistent and focused policy mix. India's recent policies were consistent in maintaining macroeconomic stability and fostering growth. Its monetary authority had eased its monetary and macroprudential policies without creating significant inflationary pressures. From the government's side, policies were focused on increasing the capacity of India's economy by developing infrastructure and improving the business climate. Fuel subsidies were gradually reduced as well, to provide more fiscal space.

The Reserve Bank of India (RBI) had opted for a loose monetary policy. RBI cut its benchmark interest rate four times throughout the year, by as much as 125 bps down to 6,75%. Easing inflationary pressures due to weakening global commodity prices had enabled the RBI to make the aggressive rate cuts. The RBI macroprudential policies were also accommodative towards credit growth, to support the financing of priority sectors in India's regions. This was implemented by raising in December 2015 the minimum amount of loans that rural regional banks must disburse to priority sectors (such as agriculture, micro-businesses and SMEs, education, infrastructure and renewable energy), from 60% to 75% of total lending).

Meanwhile, the Indian government carried out policies to deregulate the country's investment sector and expedite infrastructure development. The policies included lifting restrictions on foreign direct investments (FDI) in infrastructure construction projects. Foreign investors were also allowed to own up to 50% of insurance and defense industry companies, and to wholly own coal mining companies. The Indian government also embarked on reforming the country's Agrarian Law to facilitate land acquisition for industry and infrastructure development. One-stop permit services were also developed, aimed at issuing permits within a maximum of 10 days. Lastly, minimum market prices on agricultural products were also lifted, to attract more investments in the agriculture and plantation sectors.

To provide more fiscal space, the Indian government carried out several tax and subsidy reforms. The Tax Law was revised to simplify the structures of national and regional taxes, so as to increase the tax rate. Tax incentives were in the form of eliminating any kind of double taxation. Apart from tax reforms, the Indian government also began cutting kerosene subsidies, and continued its cuts on diesel subsidies.

All these consistent and focused policies had in the end managed to bolster India's economy throughout 2015. Growth was sustained and inflation well managed. Business confidence in India had even increased (Chart 2.6). This positive sentiment further supported the resilience of India's economy against otherwise discouraging external factors.

Chart 2.6. India Business Situation Index

Source: Bloomberg, processed

2.3. INTERNATIONAL COOPERATION

The global economy's slow and imbalanced recovery, coupled with divergent monetary policies among the AE, became the year's highlight in international cooperation forums. Also in the spotlight, these were a strengthening U.S. dollar, the U.S. normalizing its monetary policy, the slowdown in China, and declining global commodity prices. As a response, countries around the world strengthened their cooperation to achieve sustainable and quality growth, while also maintaining financial system stability and bolstering regional economic resilience.

International Cooperation to Boost Growth and Trade

The G20 forum of the world's 20 largest economies stressed the importance of working together to achieve inclusive growth, which was then formulated in the "3 Is" of Implementation, Investments and Inclusiveness. This "3 Is" formula then became the tenet for the G20 in implementing its commitments, boosting investments as an engine for growth, ensuring inclusive growth, and strengthening dialogs between G20 and low-income developing countries.

Furthermore, the G20 set three priority agendas to achieve this robust and inclusive growth. First, strengthening the recovery of the global economy and further stimulating potentials for growth. This was carried out through the coordination of macroeconomic policies, formulating country-specific investment and infrastructure strategies, improving the labor market to be more inclusive, and boosting trade and investments. Regarding trade in particular, the G20 will support the policies of countries encouraging business, especially small and medium-sized enterprises (SMEs), to become part of the global value chains (GVCs).

Second on the agenda, is improving the resilience of the global economy. This will be achieved with the support of regulations in the financial sector, by reforming the international financial architecture, improving the international tax system, and promoting a culture of anti-corruption. Regarding reforms on the international financial architecture, a particular priority is on the composition of the IMF's SDR basket, to better reflect the significant currencies used in global trade and in the world's financial system. Meanwhile, regarding the international tax system, the G20 will support the G20's and the Organization for Economic Cooperation and Development (OECD)'s Base Erosion and Profit Shifting Action Plan to address problems with tax evasion.

The third and last agenda, is ensuring sustainable development. This will be achieved by carrying out: (i) inclusive and sustainable development, with the implementation of the 2030 Sustainable Development Goals (SDGs) and the Addis Ababa Action Agenda, (ii) inclusive financing, with the implementation of national remittance plans to cut global remittance fees to a maximum of 5% from the total amount transferred, and with the implementation of other initiatives in the Global Partnership for Financial Inclusion (GPFI), and (iii) ensuring energy sustainability, with commitments to the G20 Energy Access Action Plan of improving access to electricity, starting with Sub-Saharan Africa. The G20 will also improve on energy efficiency, invest in clean energy technologies, and support research and developments programs to address climate change. The G20 had also agreed upon the Toolkit of Voluntary Options for

Renewable Energy Deployment, which outlines measures to develop renewable energy resources, and reiterated its commitment to reduce fossil fuels.

The G20 member countries continued to strengthen as well their commitment in implementing the 2014 Brisbane Growth Strategy. Growth strategy outlines measures to increase the member countries' GDP by at least 2% above the baseline GDP estimate in IMF's 2013 World Economic Outlook. This is expected to be achieved by 2018, which will increase the total world GDP by 2.1% (around USD 2 trillion), as well as create millions of new jobs.

Regarding the importance of public and private investments for infrastructure projects in stimulating further growth, the G20 had agreed to set up the Global Infrastructure Hub (GIH).[6] The G20 will continue strengthening the capacity building of its member countries, implement more projects based on public-private partnerships (PPP), and encourage more participation from multinational agencies and national development banks in financing projects. Stock markets will also be tapped as the main financing source for needed investments.

In overall, the Brisbane Growth Strategy has shown progress, with the G20 member countries having implemented more than a third of their commitments. Although this progress is of varying degree, all member countries have continued to fulfill all of their commitments. Each Country-Specific Growth Strategy has been reassessed and peer-reviewed, to ensure their implementations are consistent in achieving the collective growth target. Each member country is allowed to customize their implementations of the strategy through the Adjusted Growth Strategy, to accommodate such variables as external factors, changes in the ruling government, policy changes, and shifts in economic trends from previous estimates.

Besides the G20, the IMF had also encouraged better international cooperation to stimulate a robust and balanced growth for the global economy, and to create more jobs. The IMF encouraged its member countries to continue improving business confidence and domestic demand through a mix of macroeconomic policies and structural reforms. In particular regards to stimulating growth and improving resilience, the IMF had initiated the Global Policy Agenda (GPA), which mainly outlined (i) the implementation of fiscal policies supporting growth, with investments for infrastructure as a priority, and (ii) the implementation of monetary policies that are conducive and properly communicated by advanced economies.

Meanwhile, the Islamic Development Bank forum had committed to more active participation in the infrastructure projects of its member countries. One of its participation is to set up the World Islamic Investment Bank (WIIB). The WIIB is expected to provide another means of financing for infrastructure projects, to facilitate growth for the sharia-based economy, and become a catalyst for the development of sharia-based financial instruments.

Indonesia itself had embarked on expanding its financial, trade and investment agreements with other countries to boost growth. Bank Indonesia expanded its Bilateral Currency Swap Agreements (BCSA) with Indonesia's trade partners, to facilitate transactions for more bilateral trade while reducing risks from an overly dependence on the U.S. dollar. Bank Indonesia on December 15, 2015 signed a AUD10 billion BCSA with the Reserve Bank of Australia (RBA), following the KRW10.7 trillion BCSA with the Bank of Korea (BOK) and the CNY100 billion BCSA with the People's Bank of China (PBoC). Besides facilitating trade, the BCSA can also be used to facilitate more investments, to strengthen financial cooperation, or for other purposes as agreed.

Regarding international cooperation in the trade sector to boost growth, Indonesia actively participated in the Association of South-East Asian Nations' (ASEAN) Regional Comprehensive Economic Partnership (RCEP). ASEAN's RCEP forum had in principal agreed on initiating cooperation in the trade of goods, services and investments between ASEAN's ten member countries and six trade partners.[7] Tresholds on import duty cuts, commitments in the services and investment sectors, as well as initial offers on market liberalization have all been agreed.

International Cooperation to Maintain Financial Stability

The G20 had within its agendas formulated an international standard for financial reform, which sets a total-loss-absorbing-capacity (TLAC) for global systematically-important banks (GSIBs), so as to prevent a too-big-to-fail situation. The standard is complemented

6 GIH will develop a knowledge-sharing platform and strengthen collaboration between governments, the private sector, development banks, and other international agencies to improve financing for infrastructure.

7 China, Japan, South Korea, Australia, New Zealand, and India.

in its implementation with relevant recovery plans and cross-border crisis management procedures. The TLAC itself is meant to provide sufficient liquidity that can be used for global financial institutions with systemic risks during a crisis. Also, it can avoid the use of public funds for bail-outs.

The G20 also carried out structural reforms for over-the-counter transactions in the derivative market. The reforms were aimed at strengthening the infrastructure of the derivative market, particularly its transparency and risk management, and limiting risks of negative spillovers. The G20 agreed that all derivative contracts must adhere to standards of being cleared through central clearing counter-parties and reported to trade repositories. The G20 forum also highlighted efforts in reducing risks to the stability of the global financial system from imprudent and non-transparent practices of shadow banking, formulating a Shadow Banking Roadmap in response. The roadmap outlines more strict regulations and stronger surveillance on shadow banking practices.

The IMF had on November 30, 2015 included the Chinese yuan into its SDR basket, which will become effective on October 1, 2016. The IMF concluded that the Chinese yuan had fulfilled the criteria of being freely usable for high volumes of trade. With the Chinese yuan included in the IMF's SDR basket, member countries will be able to further diversify their foreign exchange reserves and reduce their dependency on the U.S. dollar. This in turn will help maintain stability in the financial systems of emerging markets, most of whom have significant trade relations with China.

In the Southeast Asian region, the ASEAN+3 forum continued strengthening the region's economic resilience through its Regional Financial Arrangement (RFA). Implementations of The Chiang Mai Initiative Multilateralization (CMIM) were formulated and carried out, and the ASEAN+3 Macroeconomic Research Office (AMRO) was set for a more active role as well. An Operational Guideline for the CMIM activities were completed, and an Economic Review and Policy Dialogue (ERPD) Matrix was developed. The CMIM activities themselves have been focused on strengthening coordination with the IMF's Global Financial Safety Net facilities, and improving operational technicalities for implementing other relevant international standards. Meanwhile, the AMRO has been prepared to take on a more significant role, on par with such international financial institutions as the IMF and the Asian Development Bank (ADB).

Box 2.1 Implementation of AEC 2015 and ASEAN Community Vision 2025

The ASEAN regional cooperation forum concluded 2015 by entering a new historic era, with the ASEAN Economic Community (AEC) coming into effect on December 31. The AEC envisions a single market and single production base for the ASEAN region, a region with high competitiveness, with equal development, and that is tightly integrated with the global economy. In order to realize this single market and single production base for ASEAN, economic liberalization of its member countries is needed, in order to establish the free-flow of goods, services, skilled labor, capital and investments in the region. All this presents both huge opportunities as well as challenges for Indonesia, both of which of needs to be managed properly so as to reap the best of benefits from the AEC.

The ASEAN single market itself is not the final goal of the AEC, but is a stepping stone for the region's further aim, which is the ASEAN Community Vision 2025. It is therefore important to assess how far ASEAN had by 2015 followed through with its integration process for the AEC itself. This can be assessed by comparing the commitments for integration of each ASEAN member country with the accomplishments of those commitments. In overall, most of the commitments had been fulfilled and implemented.

Regarding the free-flow of goods, the integration process through market liberalizations can be said to be nearly complete. The most significant measure of this is the lifting of import duties among ASEAN member countries to nearly 0%. Several facilities to boost intra-regional trade had also been implemented, including the setting up of the ASEAN Single Window, to simplify export-import procedures and the standardization of products.

In the services sector, the integration process can be seen in more service providers from ASEAN member countries expanding their operations within the region. Workers are freely to be employed within the region as well, to support the commercial presence of those expanding businesses. In further regard to this liberalization of ASEAN's labor market, Mutual Recognition Agreements (MRAs) for cross-border employment of certain skilled workers had been reached. Integration in the financial services sector, which entitles market liberalizations for the free-flow of capital, had also shown progress, with agreements allowing Qualified ASEAN Banks (QABs) to operate throughout the region. Meanwhile, liberalizations regarding investments were pursued by cooperating together to promote both intra-regional and outside investments to ASEAN, as well as improve the region's business climate and infrastructure. It can thus be concluded that the integration process for the AEC had sufficiently progressed on schedule before its end of 2015 deadline.

Indonesia had been among the most progressive in pursuing market liberalizations for the AEC. Indonesia had significantly reduced import duties, and likewise gained export facilities through the ASEAN Trade in Goods Agreement (ATIGA). Indonesia has also been integrating its trade system with ASEAN through its National Trade Repository and National Single Window. In liberalizing the services sector, Indonesia had ratified Package 9 of the ASEAN Framework Agreement on Services (AFAS), with commitments to open up 97 sub-sectors of services.

Regarding liberalizations of the financial services, Indonesia had ratified the related Package 6 of the AFAS, as well as the ASEAN Banking Integration Framework (ABIF). Meanwhile, liberalizations on investments saw Indonesia addressing long-standing issues in several sub-sectors, as well as collectively facilitating and promoting more investments through the sharing of data and information on potential investments. Liberalization of the labor market, particularly for skilled workers, saw Indonesia improving the qualifications and competitiveness of its domestic workforce, by harmonizing relevant labor regulations and encouraging the proper certification of skills.

As previously mentioned, the ASEAN economic integration is a dynamic and ongoing process, and does not end with the AEC coming into effect. During its 27th Leader Summit on November 22, 2015 in Malaysia, ASEAN already moved further again by adopting the AEC Blueprint 2025, outlining the region's economic integration for 2016-2025. The AEC Blueprint 2025 was adopted along with the ASEAN Community Vision 2025, the ASEAN Political-Security Community (APSC) Blueprint 2025, and the ASEAN Socio-Cultural Community (ASCC) Blueprint 2025, all of which became the Kuala Lumpur Declaration under the theme "ASEAN 2025: Forging Ahead Together". The AEC Blueprint 2025's main priority is completing any pending implementations of the AEC 2015 commitments by the end of 2016. Certain commitments from Cambodia, Lao PDR, Myanmar, and Vietnam must also be completed by 2018 at the latest.

The AEC Blueprint 2025 envisions five intertwined and reinforcing features for ASEAN: (i) a Highly Integrated and Cohesive Economy, (ii) a Competitive, Innovative, and Dynamic ASEAN, (iii) Enhancing Economic Connectivity and Sectoral Integration, (iv) a Resilient, Inclusive, People-Oriented, People-Centered ASEAN, and (v) a Global ASEAN. For the financial sector in particular, the ASEAN Financial Integration 2025 Vision comprises the three main aspects of Financial Integration, Financial Inclusion, and Financial Stability, reflecting a holistic approach in balancing between initiatives of financial liberalization with financial stability and financial inclusiveness. This is in contrast to previous approaches of carrying out liberalizations of several financial sub-sectors individually.

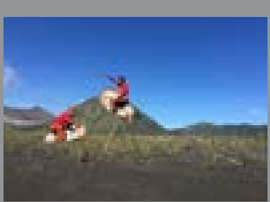
Financial Integration is crucial in facilitating intra-regional trade and investments, and can be achieved by leveraging the participation and encouraging tighter cooperation between ASEAN indigenous banks, insurance companies, and capital markets. Financial Integration must also be supported by a robust, secure, efficient, and interconnected financial market infrastructure. Regulations concerning financial market liberalizations must therefore be deliberated with ASEAN's interest of achieving more cohesive, efficient and prudent financial markets taken into account. ASEAN had agreed on providing wider market access and operational flexibility for the region's indigenous banks that pass as QABs under the ABIF.

Meanwhile, Financial Inclusion means that benefit of the Financial Integration must be cater to a wider society, particularly those previously without financial access. It is also expected to encourage the development of low-cost digital financial services and financial services for low-revenue SMEs. ASEAN has also been educating the public on financial literacy and raising public awareness on consumer protection, which includes protection against digital financial crimes.

While Financial Integration has its benefits of driving trade and investments, it also creates potential risks. Financial Stability is thus as crucial for ASEAN, and efforts to maintain financial stability has been carried out, including: (i) improving surveillance of the region's macroeconomic and financial situation, by identifying potential risks and vulnerabilities in the region's financial systems, and improving information sharing among the region's monetary and fiscal authorities, (ii) forging further cooperation between ASEAN member countries in implementing the ABIF, and (iii) formulating standards and regulations on prudential financial that are more cohesive within ASEAN and that complies to international best practices.

The ASEAN Financial Integration 2025 Vision also underlines the fact that an integrated, inclusive, and stable financial sector requires proper Capital Account Liberalizations, Payment and Settlement Systems, and Capacity Building. Liberalization of the capital markets will enable capital to flow more freely, facilitating intra-regional investments, trade, and credit. However, due to different levels of preparedness among ASEAN member countries, the capital market liberalization will be pursued with the interests of each member country taken into account, and allowing each member country to apply certain safeguard measures for their capital markets. Meanwhile, ASEAN will also improve the standards and infrastructure of the payment and settlement systems in the region that will in turn further facilitate cross-border trade and remittances, as well as facilitate the development of retail payment systems and improve existing capital markets. A secure, efficient, and competitive payment and settlements system is in the end expected to be realized. Lastly, existing gaps between the financial systems of the ASEAN member countries will be addressed through capacity building.

In achieving the goals of the AEC Blueprint 2025, particularly in the financial sector, the finance ministries and central bank governors of ASEAN member countries have authorized several Working Committees to formulate a Strategic Action Plan (SAP) for ASEAN Financial Integration Post-2015. The SAP will also ensure that the 2025 ASEAN economic integration be achieved. In regards to all this, Bank Indonesia has took the lead by participating more actively in formulating the Strategic Direction for the Working Committees in their deliberation of the Strategic Action Plan. The Strategic Direction had been formulated by taking into account the six key features of ASEAN's financial integration, that are: (i) Ensuring the financial services and capital mobilization meet the need of the real sector, (ii) Balancing financial integration with financial stability to ensure that the benefit of integration will be sustainable, (iii) Lowering transaction costs, (iv) Having greater consumer choices and protection, (v) Improving financial inclusion, and (vi) Increasing risk diversification. These key features are meant to ensure benefits for the real sector from ASEAN's financial integration, which is facilitating the flow of capital and investments for the region's real sector, and achieving the AEC 2025 Vision of “A Cohesive, Integrated, Competitive, Global and People-Centerd ASEAN's Economy”.



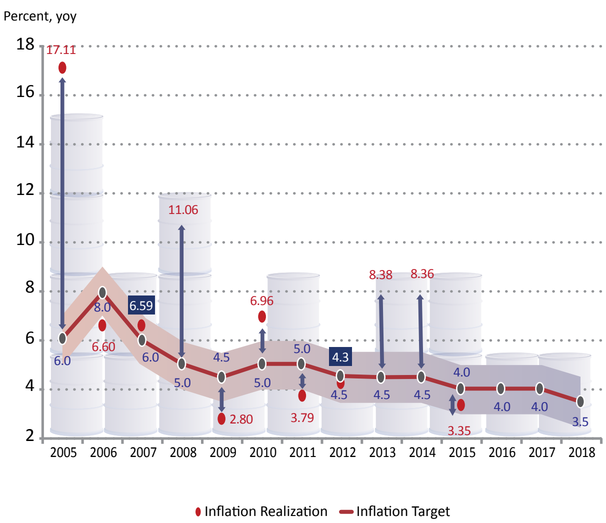
Against a backdrop of inauspicious external conditions, government spending on infrastructure was a key source of economic growth in Indonesia during 2015. Furthermore, labor absorption in the construction sector also increased.

PART II

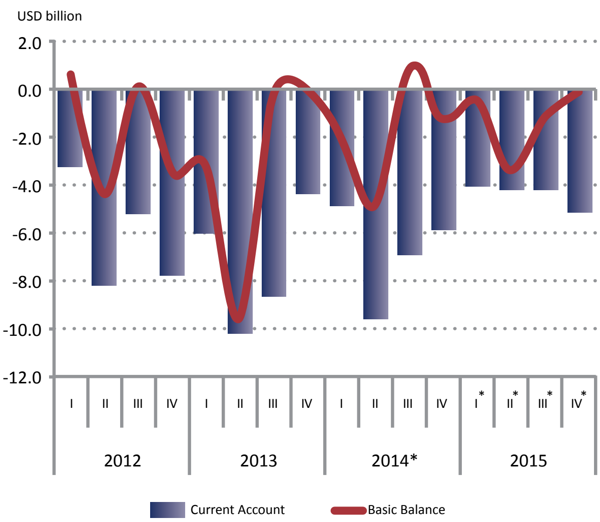
DOMESTIC ECONOMY

MAINTAINED MACROECONOMIC STABILITY AND FINANCIAL SYSTEM

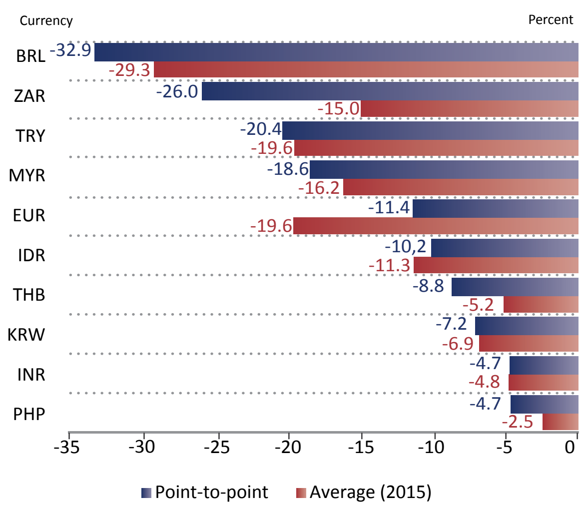
INFLATION WITHIN TARGET



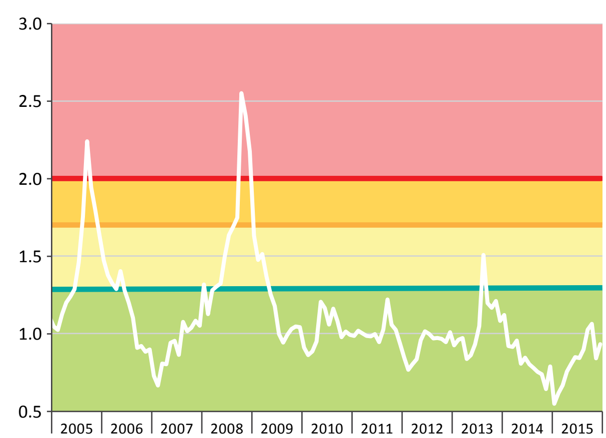
HEALTHIER LEVEL OF CAD



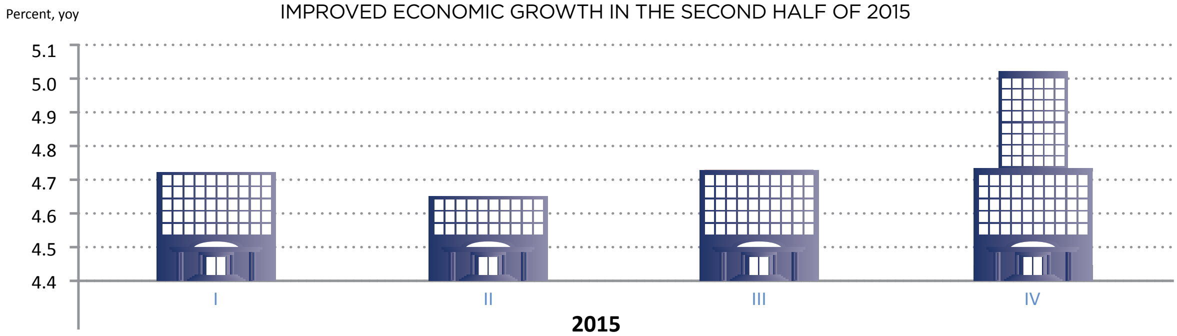
LIMITED DEPRECIATION



MAINTAINED FINANCIAL SYSTEM STABILITY



IMPROVED ECONOMIC GROWTH IN THE SECOND HALF OF 2015



PART II
DOMESTIC ECONOMY

In the midst of external and domestic challenges, the Indonesian economy charted positive achievements in 2015. Macroeconomic and financial system stability remained solid while economic growth began to gather momentum. Macroeconomic stability was reflected in inflation that returned to the targeting range of 4±1%, a reduction in the current account deficit to about 2% of GDP, subdued movement in the rupiah exchange rate, particularly from the last quarter of 2015, and a resilient financial system underpinned by high levels of capital adequacy. Meanwhile, economic growth pulled out of its previous downward trend as it gathered momentum for recovery in the second half of 2015. This achievement owes much to the policy synergy put in place by Bank Indonesia and the Government to safeguard macroeconomic and financial system stability and set in motion a process for economic recovery.

Uncertainty on global financial markets led to increased downward pressure on the rupiah during 2015. Quarterly dynamics in the rupiah exchange rate were affected most importantly by external factors, in this case uncertainty over increases in the Federal Funds Rate (FFR), concerns over fiscal negotiations with Greece, and the devaluation of the yuan. Pressure bearing down on the rupiah was exacerbated by domestic conditions, notably the deteriorating outlook for domestic economic growth, lack of deepening in the financial market and heavy corporate reliance on external financing. Despite this, downward pressure on the rupiah began to ease and the currency even charted an appreciating trend in the fourth quarter of 2015. Key to this was the increase in foreign capital inflows in keeping with the easing of uncertainty on global financial markets over expectations of delay in increases in the FFR. On the domestic side, the easing of pressure on the rupiah was assisted mainly by the policy actions by Bank Indonesia for stabilising the exchange rate, positive investor perceptions of the outlook for the domestic economy in the wake of a series of policy packages launched by the Government, and high returns on domestic assets. These positive factors contributed to appreciation in the rupiah that outweighed the currency gains in other countries. Throughout 2015, the rupiah experienced 10.2% (yoy) depreciation to Rp13,875 to the U.S. dollar, less than the depreciation sustained by the currencies of some peer countries.

In 2015, Indonesia's balance of payments recorded a deficit despite significant improvement that took place in the current account deficit, which came down from 3.1% of GDP in 2014 to 2.1% of GDP. The amelioration in the current account deficit was achieved mainly in the oil and gas trade balance and the non-oil and gas trade balance. In the oil and gas sector, the fall in world oil and gas prices and shrinking domestic consumption of fuels led to a significant reduction in oil and gas imports. The steeper drop in imports of oil and gas compared to oil and gas exports resulted from the combination of falling oil and gas prices and higher export volume from increased lifting of domestic oil. In the non-oil and gas sector, the trade balance recorded an enlarged surplus resulting mainly from contraction in non-oil and gas imports in line with weakening domestic demand and depreciation of the rupiah. This reduction in non-oil and gas imports outweighed the decline in non-oil and gas exports triggered by flagging global economic growth and commodity prices. Regarding the capital and financial account, the uncertainty on global financial markets led to significant decline in capital flows until the third quarter of 2015. Nevertheless, the easing of uncertainties on global financial markets and improving confidence in the outlook for the domestic economy from the fourth quarter of 2015 prompted a significant rise in capital inflows, particularly for portfolio investment in government bonds and direct investment. In line with the increased surplus in the capital and financial account, Indonesia's balance of payments posted a substantial surplus in the fourth quarter of 2015. For 2015 overall, the balance of payments recorded a deficit of about USD1.1 billion.

Despite the depreciation in the rupiah, inflation in 2015 reached 3.35% (yoy), within the 2015 inflation target range of 4±1%. The subdued inflation in 2015 is attributed to global and domestic factors. At the global level, plunging world oil prices created opportunity for the Government to lower domestic prices for fuel and 12kg bottled LPG gas and make adjustments to electricity billing rates. These price reductions were made possible by energy reforms that provides for pricing of energy on the basis of economic viability. This helped to keep administered prices inflation at a low level during 2015. Second, the drop in global commodity prices, including prices of food staples, helped keep volatile foods inflation in relatively subdued territory. On the domestic side, while the rupiah suffered depreciation, the pass-through from the weakening exchange rate on inflation was comparatively limited. Key to this was the managed level of domestic demand and low inflation in prices for imported goods. Second, the adequate supply of strategic food commodities also contributed to subdued volatile foods inflation amid severe disruption from El Nino. The mild level of volatile foods inflation also owes much to the stronger coordination between the Government and Bank Indonesia in stimulating increased production, improving distribution and minimising various price distortions for staple foods. As a result, core inflation in 2015 reached only 3.95% (yoy) and administered prices inflation 0.39% (yoy), while volatile foods inflation came to 4.84% (yoy).

The Indonesian economy began to regain momentum in the second half of 2015. Throughout the first half of 2015, domestic economic growth steadily declined in tandem with the flagging performance of the global economy, downward movement in commodity prices and delays in government spending due to problems with nomenclature. Despite this, economic growth began to bounce back in the second half of 2015, bolstered by improvement in domestic demand. Government spending mounted significantly, buoyed by increases in government capital expenditure related mainly to infrastructure development. The government's fiscal stimulus also met with response from the private sector, reflected in stronger investment growth in some sectors such as construction. At the household level, buoyant consumer confidence helped household consumption to maintain relatively stable, resilient growth. During 2015 overall, economic growth slowed from 5.02% in 2014 to 4.79%. Despite this decline, Indonesia has managed relatively strong growth compared to other commodity-based economies. Spatially, the structure of Indonesia's economic growth is beginning to diversify, which also helped to keep the economic growth from further decline. In Java, the manufacturing-based economy generating high added value maintained vibrant growth that compensated for weak performance outside Java, where growth has suffered from the impact of weakening commodity prices.

In the financial sector, financial system stability remained sound despite escalating risks from adverse global economic developments. This was reflected in the Financial System Stability Index (FSSI) for 2015, which at 0.89 came within safe limits. The resilience of the banking industry remains strong as reflected in prudent levels of credit risk and liquidity risk, high profitability and robust capital adequacy. Credit risk remained at the low end of the scale despite an upward trend due to deterioration in corporates' ability to pay debt following decline in corporate revenues and household incomes. Reflecting this was an increase in non-performing loans (NPLs) to 2.5%, albeit still below the 5% threshold of safety. Decline in corporate revenues and household incomes also contributed to weaker growth in bank deposit at only 7.3%. The reduced growth in bank deposit in turn led to increased liquidity risk, although safe limits were not exceeded. The ratio of liquid instruments to bank deposit fell to 19.4%, but stayed well above the safe threshold of 8.5%. As regards banking intermediation, credit growth maintained a downward trend with growth reaching only 10.4%. This was explained by falling demand, a result of flagging growth in the domestic economy, and reduced supply, due to tightening of lending standards as banks responded to increases in NPLs. Lack of recovery in the intermediation function and mounting credit risk caused bank profitability levels to fall. Despite slipping to 2.27% in 2015, at this level profitability was still ahead of other nations in the region.

The decline in profitability levels had no significant impact on the resilience of the Indonesian banking system due to the high level of bank capital adequacy. At the end of 2015, the capital adequacy ratio of the Indonesian banking system was recorded at 21.2%, up from the 2014 level of 19.4%. Further confirmation of the resilience of Indonesia's banking system came from the results of stress testing of credit risk and market risk, which indicate that Indonesia's banks have high levels of capital resilience for coping with worst-case scenarios. In the non-bank sector, the role of non-bank financing has expanded in line with the corporate response to the tightening of bank lending standards. Corporations appear to be seeking alternative funding sources on the bonds, stock and corporate Islamic bonds (sukuk) markets, and through medium term notes (MTNs) and negotiable certificates of deposit (NCDs).

Performance improved in the payment system during 2015. From the side of payment system operated by Bank Indonesia, this improvement was reflected in the reliability and availability of the payment system and effective contingency plan implementation. The industry-operated side of the payment system experienced no significant system failures. Growth in the value of payment system transactions processed by Bank Indonesia and the industry fell to 9.4% in line with more moderate economic growth. However, when measured by volume, growth improved from 18% to 19% in 2015. The increase took place mainly in the payment system operated by the industry, involving card-based payment instruments (CBPIs) and electronic money (E Money). This development is as envisaged in the payment instrument electronification program implemented through the National Non-Cash Movement (GNNT) and Government policy for using E Money for disbursing social assistance. The success of this drive for use of electronic payment instruments was also visible in the increased CBPI to GDP ratio, indicating an improvement in public preferences for use of non-cash payments. Regarding the cash payments system, rupiah cash management has become more reliable, as reflected in the expanding coverage of Bank Indonesia cash services and improving quality of cash in circulation. This reliable performance has been supported by a rupiah cash management policy that includes the development of a cash distribution network and cash services provided by cash pre-placements (Kas Titipan), an adequate cash position at Bank Indonesia, and improvement in the quality of cash in circulation under the clean money policy.

Against a backdrop of inauspicious external conditions, government spending on infrastructure was a key source of economic growth in Indonesia during 2015. Furthermore, labor absorption in the construction sector also increased.

Chapter 3

Economic Growth

Global economic dynamics marked by continued weakness in the world economy and a drop in capital flows to emerging market countries in 2015 put pressures on domestic economic growth. Congruously, the subsequent domestic economic moderation had an adverse effect on unemployment and welfare. In response to such conditions, Bank Indonesia and the Government instituted a range of policies to maintain macroeconomic stability and boost economic growth. Consistent with the policy response, risks in the economy were mitigated and confidence was restored, leading to gains in economic momentum during the second half of the year.

Weaker global growth than the year earlier undermined the domestic economy in 2015. Constrained growth in advanced economies were reported. Meanwhile, economic growth in emerging market countries, as the main drivers of global growth, tended to decelerate. China as the foremost growth engine of the global economy and a leading trade partner of Indonesia, suffered from persistent moderation. Furthermore, the global economic downswing perpetuated the international commodity price slide. Inauspicious global economic conditions spilled over to the domestic economy, reflecting an export contraction. With an economy reliant on natural resources, lower commodity prices undermined the terms of trade and overall domestic economic activities.

Against a backdrop of ubiquitous uncertainty blighting global financial markets, domestic economic moderation spurred economic risks and eroded confidence in the economy. Currency risk surfaced accompanied with decreasing confidence in the domestic economy. This resulted in lower capital inflows and increased pressure of the exchange rate. Domestic economic moderation and rupiah depreciation further sparked corporate risks in the form of weaker financial performance, which ultimately reduced investment and corporate repayment capacity. Simultaneously, banking risks escalated as non-performing loans (NPLs) increased but remained below the threshold. Addressing such circumstances, banks tightened lending standards, leading to a decline in disbursed loans. In turn, slower credit growth adversely affected the domestic economy, which exacerbated fiscal risks due to the limited room available for economic stimuli as a result of low tax revenues.

The Indonesian economy posted 4.8% (yoy) growth in 2015, down from 5.0% (yoy) the year earlier and below the Bank Indonesia projection of 5.4-5.8%. External sector performance decreased significantly, reflecting the deep export contraction. Due to the heavy reliance on natural resources exports, rupiah depreciation did not improve export performance in general. Meanwhile, manufacturing exports confronted a range of challenges stemming from sluggish demand for exports and a large import content amidst exchange rate depreciation. A decline in export earnings also affected domestic demand, particularly private consumption and non-building investment. In line with the export contraction and drop in domestic demand, imports also experienced a sufficiently deep contraction. By sector, economic moderation that initially affected the primary sector ultimately spread to other sectors.

Economic moderation undermined employment conditions and welfare. Accordingly, the level of unemployment increased slightly, accompanied by less elasticity of employment absorption in regard to economic growth. Furthermore, a decline in labor utilisation was observed to affect the mining, agriculture and manufacturing sectors. In contrast, the construction sector absorbed additional labor due to the increased realisation of various infrastructure projects. In line with unemployment conditions, public welfare also declined slightly which reflected in the increase of poverty rate and lack of improvement in the Gini coefficient.

Despite the general economic downturn recorded in 2015, recovery momentum gained traction during the second half of the year on the back of fiscal stimuli introduced by the Government. Against a backdrop of low tax revenues, fiscal reform policy, primarily in the form of subsidy reductions, provided space to stimulate the economy. Fiscal stimuli stemmed from increased government spending, specifically capital spending linked to government-led infrastructure projects. Domestic economic momentum improved risk perception and restored confidence in the economy, which was further bolstered by Bank Indonesia policy to consistently maintain macroeconomic stability. Despite widespread uncertainty disrupting global financial markets, Bank Indonesia eased macroprudential policy to stimulate the domestic economic recovery. The range of policies introduced has successfully catalysed domestic economic growth in the second half of 2015.

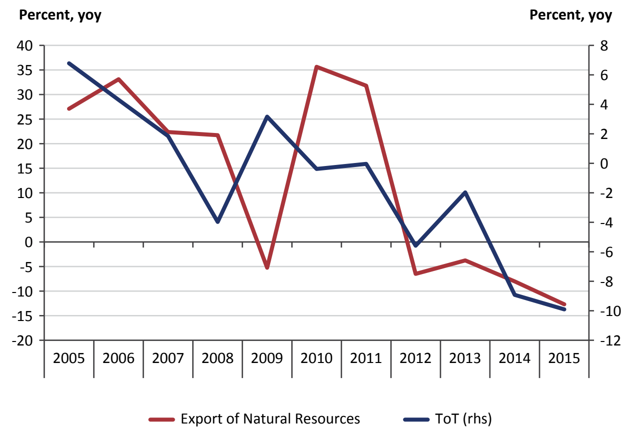
Moving forward, Bank Indonesia and the Government will continue to strengthen coordination in order to support further economic momentum, while preserving macroeconomic stability. Paying due consideration to the relatively limited knock-on effect of fiscal stimuli in the private sector, policy shall be directed towards building on existing economic momentum. To that end, the Government will continue and accelerate prevailing structural reforms. Meanwhile, Bank Indonesia will prudently loosen its monetary policy stance in order to reinforce confidence in the economy, which will contribute favourably to economic growth, macroeconomic stability and the financial system.

3.1. GDP – EXPENDITURE SIDE

Economic growth in 2015 stood at 4.8% (yoy), down from 5.0% (yoy) the year earlier despite early indications of recovery in the second half of the year. A deep slowdown occurred in the first semester of 2015, which began to reverse in the second semester (Table 3.1). Accordingly, during the first half of the reporting year, domestic demand, consumption and investment tailed off significantly in line with the export decline. The drop in private consumption was due to the base effect of the General Election contested in 2014, which precipitated a contraction in the consumption of non-profit institutions serving households (NPISH). Meanwhile, government consumption and investment also faced administrative constraints in the form of ministerial/institutional reorganisation. Hence, in the second semester, government fiscal stimuli was able to boost the momentum of economic recovery. In addition to the increase in government consumption, public investment also surged due to the expansion of infrastructure projects. The spillover of fiscal stimuli on the private sector began, albeit limited. Consumer confidence also began to improve, driving household consumption, particularly non-food consumption, towards the end of the year. In addition, non-building investment also began to rebound in line with positive business sentiment. In general, domestic demand was the main source of economic growth in 2015, amidst weak external conditions.

Global economic moderation and the declining of global commodity prices in 2015, weakened export performance in Indonesia. Exports from Indonesia were dominated by natural resources and as a consequence, falling global commodity prices significantly undermined the terms of trade (ToT) (Chart 3.1). Lower global commodity prices also led to export contraction, particularly for mining commodities, most notably affecting coal. Nonetheless, policy to extend export licenses for mineral concentrates (particularly copper) after smelter development had proceeded, successfully offset a deeper export contraction. Meanwhile, manufacturing exports failed to recover despite rupiah depreciation due to weak global demand

Chart 3.1. **Terms of Trade and Export of Natural Resources**



and the large import content of exports. The export decline was evidenced by the steep decline in exports to a leading trade partner, namely China, falling 20% on the year earlier. The drop stemmed primarily from commodity-based exports that dominate the export structure to China.[1] Nevertheless, automotive exports from Indonesia performed positively, with robust growth reported over the past two years (Table 3.2).

In line with lower revenues triggered by the export decline, households were also less inclined to consume. The downward consumption trend affected secondary and tertiary goods (non-food consumption) despite rebounding slightly towards the end of the year. In general, household consumption remained solid, surpassing conditions immediately after the global financial crisis, when growth of just 4% was reported at the end of 2009. A number

Table 3.1. **GDP Growth by Expenditure**

Percent, yoy

	2012	2013	2014*	2015**				
				I	II	III	IV	Total
Household Consumption	5.49	5.43	5.16	5.01	4.97	4.95	4.92	4.96
Non - Profit Institution Serving Household (NPISH) Consumption	6.68	8.18	12.19	-8.07	-7.99	6.56	8.32	-0.63
Government Expenditure	4.53	6.75	1.16	2.91	2.61	7.11	7.31	5.38
Gross Fixed Capital Formation	9.13	5.01	4.57	4.63	3.88	4.79	6.90	5.07
Building	8.13	6.74	5.52	5.47	4.82	6.25	8.21	6.23
Non Building	11.73	0.63	2.03	2.35	1.32	0.73	3.10	1.87
Export	1.61	4.17	1.00	-0.62	-0.01	-0.60	-6.44	-1.97
Import	8.00	1.86	2.19	-2.19	-6.97	-5.90	-8.05	-5.84
GDP	**6.03**	**5.56**	**5.02**	**4.73**	**4.66**	**4.74**	**5.04**	**4.79**

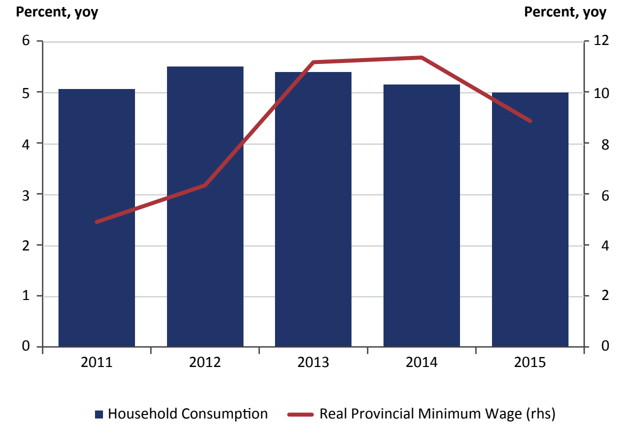
Source: BPS - Statistics Indonesia *preliminary **very preliminary

1 The share of commodity exports from Indonesia to China in terms of total exports from Indonesia accounted for 70% in 2015.

Table 3.2. Non-Oil and Gas Export

Export Commodity	Jan- Dec (USD Billion)		Growth (Percent, ytd)		Share 2014 ytd	Share 2015 ytd
	2014	2015	2014	2015		
Crude Palm Oil	20.0	17.8	8.6	-10.9	13.6	13.5
Coal	20.8	16.0	-14.5	-23.4	14.2	12.1
Clothes	7.7	7.6	-0.5	-1.3	5.2	5.7
Electronic Equipment	6.1	5.6	-1.5	-9.3	4.2	4.2
Textile	4.7	4.4	3.1	-7.3	3.3	3.4
Vehicle	5.2	5.4	14.5	3.1	3.6	4.1
Crude Rubber	4.8	3.7	-30.9	-21.9	3.3	2.9
Iron Ore and Steel	4.1	3.1	-4.0	-23.0	2.8	2.4
Spareparts	2.3	2.0	1.8	-13.3	1.5	1.5
Furniture	1.8	1.7	2.4	-4.0	1.2	1.3
Plastics	1.2	0.9	10.4	-23.1	0.8	0.7
Others	68.0	63.9	-1.3	-5.3	-52.8	-50.7
TOTAL NON-OIL AND GAS EXPORT	146.5	131.9	0.0	-8.1	1.0	1.0

Chart 3.3. Private Consumption and Real Provincial Minimum Wage



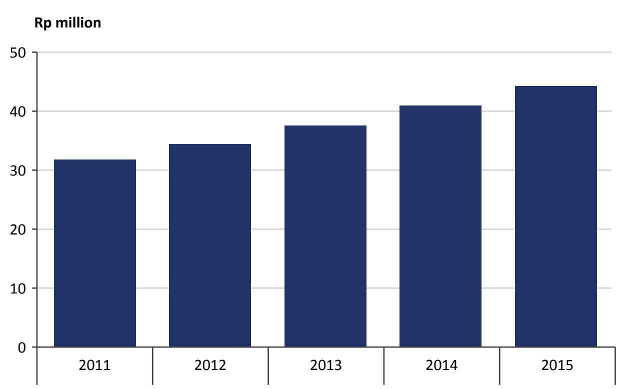
Source: Ministry of Manpower, BPS - Statistics Indonesia, processed

of macro indicators supported resilient consumption, including per capita income that followed an upward trend. Per capita income increased from Rp41.8 million in 2014 to Rp45.2 million (USD3,377.10) in 2015 (Chart 3.2). In addition, public purchasing power was maintained on the back of a hike in the real Provincial Minimum Wage (UMP). Over the past five years, the average increase in the provincial minimum wage has exceeded 7%, further jumping to 8.9% in 2015 (Chart 3.3). The increase in the provincial minimum wage has become a reference for wage hikes in various sectors, particularly formal labor.

To negate a deeper decline in consumption due to lower revenues from natural resources, households tended to dip into their savings to support consumption. Consequently, individual savings in rupiah followed a slower growth trend, indicating consumption smoothing, after a number of periods of increased savings accumulation, in particular when commodity prices soared (Chart 3.4). In addition to savings, cash withdrawals using credit cards have also increased over the past year, offering further indications of consumption smoothing.

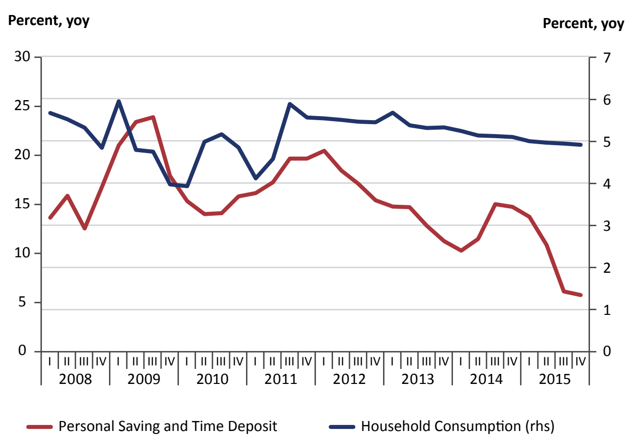
Against a backdrop of declining private consumption, the fiscal stimuli introduced in the second semester of 2015 restored optimism and drove economic momentum. After stagnating in the first half of the year due to government nomenclature reorganisation, public spending accelerated significantly in the second semester. Accordingly, government procurement increased to Rp170.5 trillion (40.9%, yoy) in the second semester after achieving just Rp60.1 trillion (8.1%, yoy) in the first semester. In

Chart 3.2. Income per Capita



Source: BPS - Statistics Indonesia

Chart 3.4. Household Consumption and Saving Growth



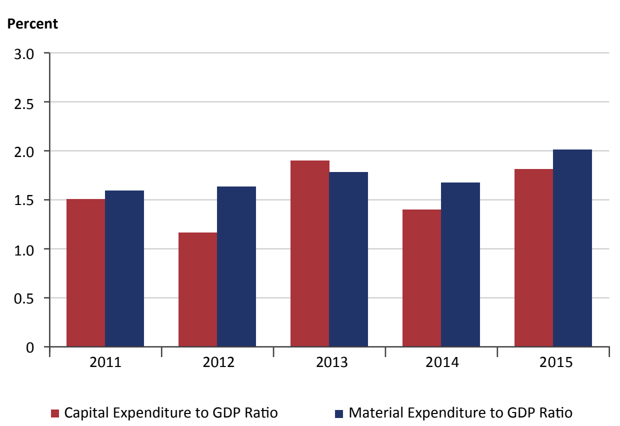
Source: BPS - Statistics Indonesia, processed

addition, government stimuli in the form of increased capital spending during the second semester supported infrastructure investment performance. Capital spending by the central government soared from just Rp30.2 trillion (6.7%, yoy) in the first semester to Rp178.4 trillion (49.9%, yoy) in the second semester. In general, actual capital spending in 2015 accounted for 1.8% of GDP (Chart 3.5). The dramatic increase in capital spending stemmed from expedited government infrastructure projects as part of the structural reform agenda. Amidst weak external and domestic private demand, fiscal stimuli were the main drivers of economic growth momentum, which boosted confidence in the economy, particularly amongst consumers, and helped improve household consumption, especially of non-foods, towards the end of the year (Chart 3.6).

Although interest in private investment remained weak in 2015, the domestic economic recovery in the second half of the year drove optimism in the economic outlook. After following a downward trend during the first half of the year, investment began to show signs of improvement, in particular public infrastructure investment. Meanwhile, limited private non-building investment endured. Lower revenues due to dwindling demand for exports and domestic demand, accompanied by depreciatory pressures on the rupiah, spurred potential corporate risks through declines in financial performance. Risks primarily affected domestic-oriented corporations with a high import content along with highly indebted corporations with foreign loans. Such conditions ultimately eroded economic confidence and suppressed investment through to the third quarter of the year. The decline in non-building investment, which had previously been rooted in the primary sector, subsequently spread to the secondary and tertiary sectors (Chart 3.7). Nonetheless, economic gains in the fourth quarter, stemming from fiscal stimuli, restored economic optimism and non-building investment began to pick up (Chart 3.8).

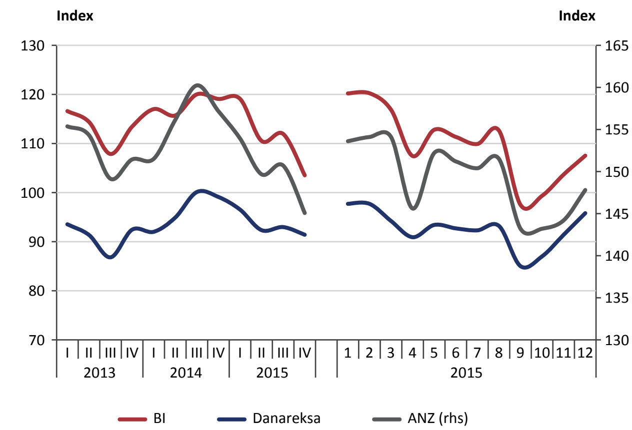
The business climate also improved, reflecting an advancement in Indonesia's ease of doing business rating, which further bolstered the investment outlook. The rating jumped from 120 to 109 in 2016 (Table 3.3).[2] The improvement in Indonesia's rating was supported by a number of reforms undertaken during the past year. Facilitating investment, the Government streamlined the business licensing process, taxation, and access to bank

Chart 3.5. Infrastructure Spending and Capital



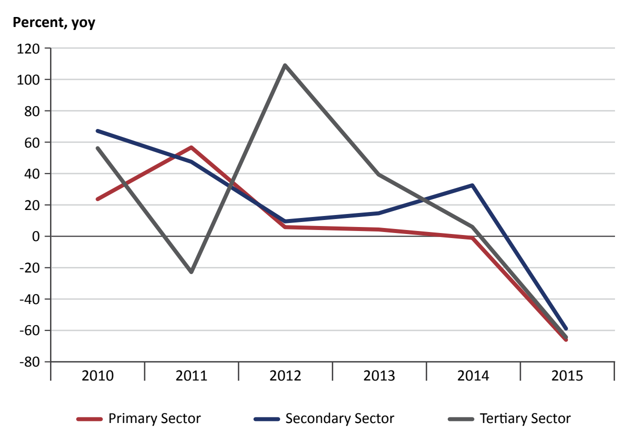
Source: Ministry of Finance, processed

Chart 3.6. Consumer Confidence Index



Source: ANZ Roy Morgan and Danareksa

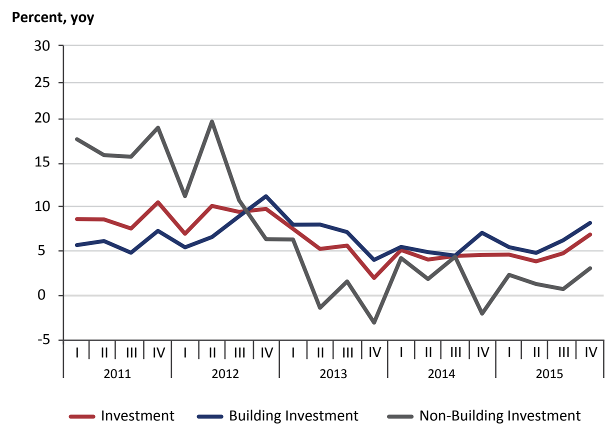
Chart 3.7. Investment by Sector



Source: Investment Coordinating Board

2 Indonesia's Doing Business (DB) rating in 2015 was 120 referring to the new method employed in the 2016 DB survey. Meanwhile, in the official 2015 publication, using the old method, Indonesia placed 114th.

Chart 3.8. Real Investment



Source: BPS - Statistics Indonesia

credit. The most significant improvements were made in terms of taxes, with the Government formulating an easier and cheaper tax payment scheme. To that end, the Government introduced an online payment scheme as a social safety net, while lowering the ceiling on tax for the workforce. Consequently, Indonesia's tax ranking improved significantly from 160 to 148. Looking ahead, the investment outlook of Indonesia will improve further in line with the 2015 launch of Government Policy Package I-VIII, with the majority of the policies therein focused on enhancing the investment climate while encouraging infrastructure development.

Import growth also contracted in line with weak export performance and sluggish domestic demand. In real terms, the import decline affected all types of goods, including consumer goods, capital goods and raw materials, with the most notable contraction affecting capital goods (Chart 3.9). Such conditions were in line with the investment slump, particularly non-building investment. In addition, the loss of confidence in the economy led to demand being partially met through inventory, which further obviated the requirement for imports. Notwithstanding, imports of capital goods began to pick up in the final quarter of the year, indicated by a shallower contraction.

3.2. GDP – PRODUCTION SIDE

Economic moderation occurred in almost all economic sectors, despite indications of gains in several sectors during the second half of the year. Triggered by sliding international commodity prices due to weak demand, the performance of commodity-based sectors declined, including (i) the mining and quarrying sector; and (ii) agriculture, forestry and fisheries. In fact, the mining and quarrying sector was observed to contract throughout 2015. In turn, declines in commodity-based sectors spilled over to erode the performance of other sectors. In addition to lower revenues, backward-forward linkages between sectors also exacerbated the declines. A downturn was also reported in the secondary sector, primarily the manufacturing industry. Furthermore, less demand for heavy equipment, spare parts and other components to support extractive sectors further compounded the manufacturing industry decline. Congruously, the performance of supporting industries, such as electricity and gas, also deteriorated due to decreasing production activities. The slowdown subsequently spread to the tertiary sector, including wholesale and retail trade, car and motorcycle repairs as

Table 3.3. Ease of Doing Business in Indonesia

INDICATOR	INDONESIA				
	2014	2015	2015*	2016	
Doing Business Rank	120	114	120	109	↑
Starting a Business	175	155	163	173	↓
Dealing with Construction Permit	88	153	110	107	↑
Getting Electricity	121	78	45	46	↓
Registering Property	101	117	131	131	→
Registering Credit	86	71	71	70	↑
Protecting Investor	52	43	87	88	↓
Paying Taxes	137	160	160	148	↑
Trading Across-Borders	54	62	104	105	↓
Enforcing Contracts	147	172	170	170	→
Bankruptcy Settlement	144	75	73	77	↓

* ranked revision refers to the new methodology used in Doing Business 2016
Source: World Bank

Chart 3.9. Non-Oil and Gas Import

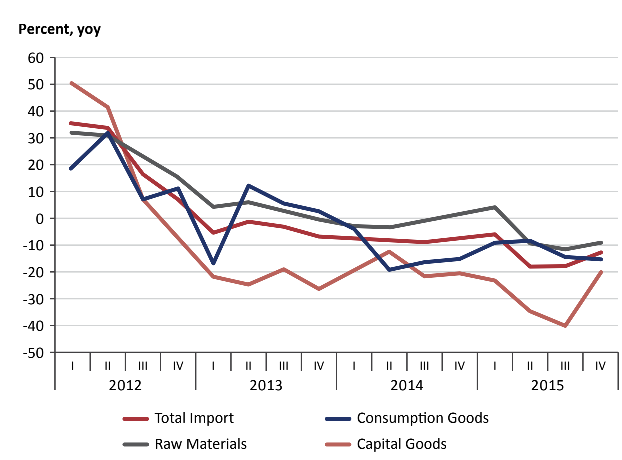


Table 3.4. **GDP Growth by Industrial Origin**

Percent, yoy

	2012	2013	2014*	2015**				
				I	II	III	IV	Total
Agriculture	4.59	4.20	4.24	4.01	6.86	3.34	1.57	4.02
Mining and Quarrying	3.02	2.53	0.72	-1.32	-5.20	-5.66	-7.91	-5.08
Manufacturing Industries	5.62	4.37	4.61	4.01	4.11	4.51	4.35	4.25
Electricity	10.06	5.23	5.57	1.73	0.76	0.56	1.81	1.21
Water Supply	3.34	3.32	5.87	5.39	7.76	8.75	6.77	7.17
Construction	6.56	6.11	6.97	6.03	5.35	6.82	8.24	6.65
Trade and Car Repair	5.40	4.81	5.16	4.12	1.70	1.39	2.77	2.47
Transportation and Warehousing	7.11	6.97	7.36	5.78	5.92	7.26	7.67	6.68
Accommodation, Food, and Water Supply	6.64	6.80	5.77	3.37	3.75	4.48	5.79	4.36
Information and Communication	12.28	10.39	10.10	10.09	9.66	10.74	9.74	10.06
Financial Services	9.54	8.76	4.68	8.57	2.63	10.36	12.52	8.53
Real Estate	7.41	6.54	5.00	5.26	5.03	4.78	4.25	4.82
Business Services	7.44	7.91	9.81	7.36	7.64	7.63	8.13	7.69
Government Administration	2.13	2.56	2.38	4.73	6.29	1.27	6.70	4.75
Education Services	8.22	7.44	5.55	5.03	11.71	8.08	5.32	7.45
Health Services	7.97	7.96	7.96	7.14	7.48	6.33	7.44	7.10
Other Services	5.76	6.40	8.93	7.98	8.06	8.11	8.15	8.08
Taxes Less Subsidies on Products	15.05	21.80	5.13	16.64	27.30	36.01	46.55	31.98
Gross Domestic Product	**6.03**	**5.56**	**5.02**	**4.73**	**4.66**	**4.74**	**5.04**	**4.79**

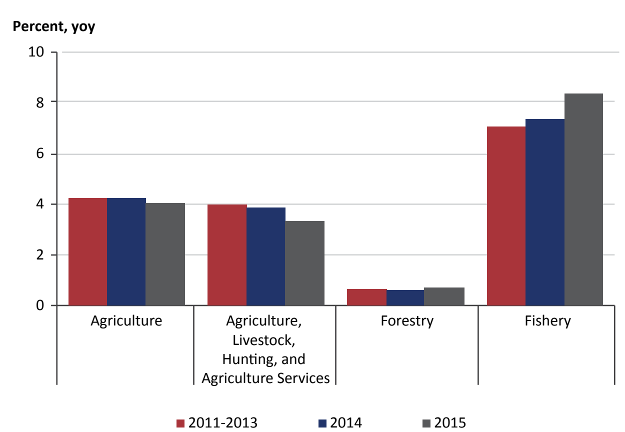
Source: BPS - Statistics Indonesia *preliminary **very preliminary

well as several services sectors. In the second semester, however, fiscal stimuli in the form of infrastructure projects drove construction sector gains, followed by limited gains in the trade sector, transportation and warehousing sector as well as several services sectors but the improvements were not felt in all sectors.

Growth of agriculture, forestry and fisheries tended to slow due to weak demand amidst the El Nino weather anomaly. Tumbling crude palm oil (CPO) prices adversely impacted the plantation subsector, with growth decelerating from 5.94% the year earlier to just 3.54% in 2015. Domestic policies in the form of a progressive export tax and mandatory B15 biodiesel use prevented further CPO declines, however. Policy to collect a CPO Supporting Fund, which began in July 2015, had a net positive effect in the medium term in relation to replanting and downstream industries. Meanwhile, robust food crop production growth prevented deeper declines in the agricultural subsector. Production of rice, maize and soybean grew respectively by 5.85%, 4.34%, and 2.93% on the previous year. The El Nino weather phenomenon had only a limited impact on food crop production, while the performance of the fisheries subsector improved on larger fishing catches and greater aquaculture fish production (Chart 3.10).

After the decelerating trend experienced since the end of 2012, mining sector performance contracted deeply in 2015 due to global economic moderation that eroded demand and simultaneously perpetuated the international commodity price slide. Policy in a number of countries to reduce sources of energy with high-pollutant emissions further reduced demand. Commodity prices plummeted, primarily coal as a leading commodity of Indonesia, which led to the closure of production at numerous small mining firms. Coal production in 2015 totalled just 380 million tons, below the Government's target of 425 million tons and falling from 458 million tons the year

Chart 3.10. **Growth of Agricultural Industry**



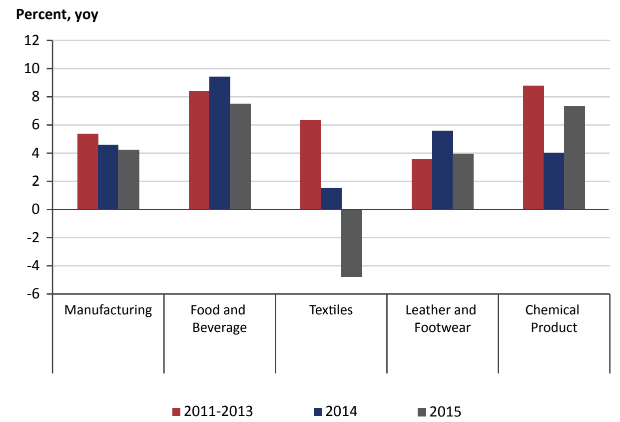
Source: BPS - Statistic Indonesia

earlier. Consequently, the coal and lignite mining subsector contracted -20.9% (yoy) in 2015 (Chart 3.11).

Growth of the secondary sector also slowed in 2015. The mining sector contraction undermined performance in sectors with close linkages, such as the heavy equipment industry. The production of heavy equipment fell in line with weaker sales data, achieving just one-third of that recorded in the previous year. Weak export performance and domestic demand placed pressures on the manufacturing industry. Several subsectors experienced strong pressures, including textiles and clothing, wood, and wood articles, leather and footwear as well as food and beverages (Chart 3.12).

Fiscal stimuli bolstered construction sector performance but the gains did not spread to other sectors. On an annualised basis, construction sector performance slowed, but improvement was seen in the second half of the year. Construction sector growth accelerated from below 6% (yoy) in the first semester to 6.8% (yoy) and 8.2% (yoy) in the third and fourth quarters respectively. Nonetheless, the trickle-down effect of the fiscal stimuli on other sectors was much more limited. In general, the wholesale and retail sector, car and motorcycle repairs, accommodation, food and beverages, transportation and warehousing as well as corporate services slowed significantly in line with economic moderation. Towards the end of the year, however, the performance of several sectors began to pick up due to gains in the construction sector, including the wholesale and retail sector, car and motorcycle repairs, transportation and warehousing as well as several services sectors.

Chart 3.12. Growth of Manufacturing Industry

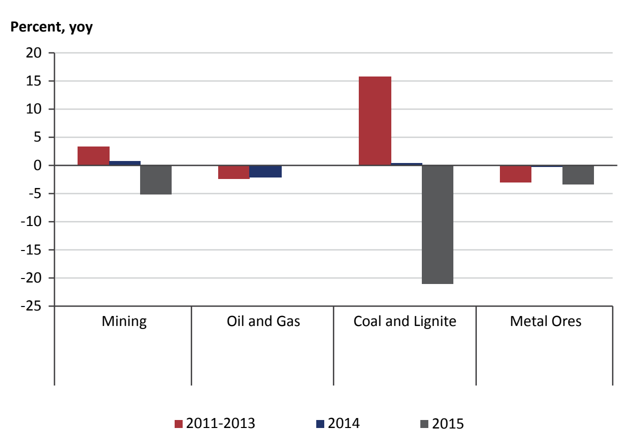


Source: BPS - Statistics Indonesia

3.3. CORPORATE AND HOUSEHOLD PERFORMANCE

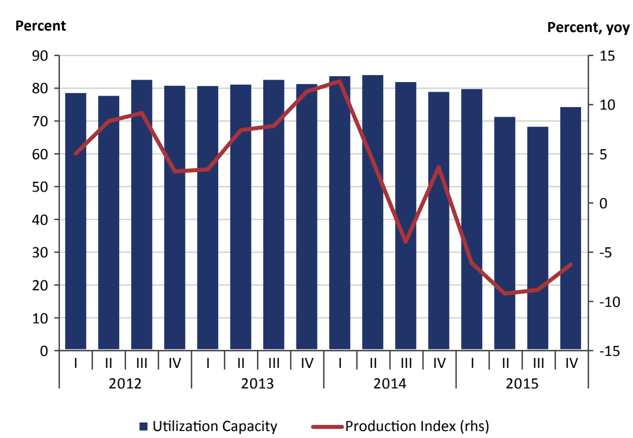
Corporate performance deteriorated as a result of economic moderation. Weak external and domestic demand reduced production, reflecting declines in the production index and production capacity utilisation in 2015 (Chart 3.13). Less production drained corporate revenues as reported in the financial statements, particularly of commodity-based corporations. This condition was further compounded by sliding global commodity prices (Chart 3.14).[3] Consequently, as the performance of the commodity sector declined, the commodity-driven domestic economy weakened public

Chart 3.11. Growth of Mining Industry



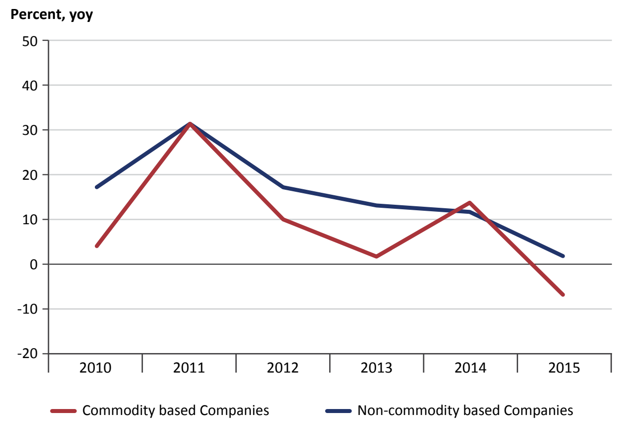
Source: BPS - Statistics Indonesia

Chart 3.13. Utilization Capacity and Production Index



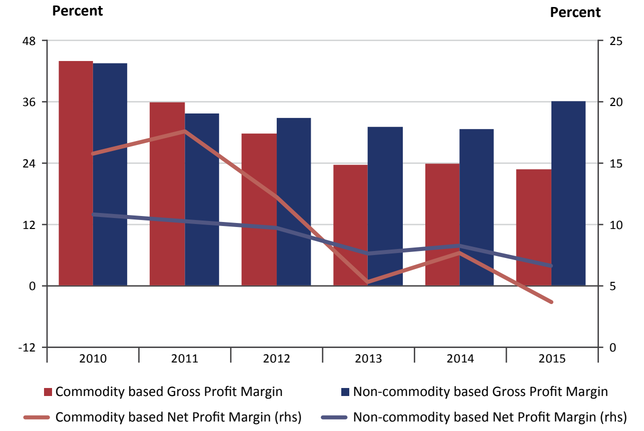
3 The assessment of corporate performance used data from 163 public companies listed on the Indonesia Stock Exchange.

Chart 3.14. Income of Listed Companies



Source: Bloomberg, processed

Chart 3.15. Gross and Net Profit Margin



Source: Bloomberg, processed

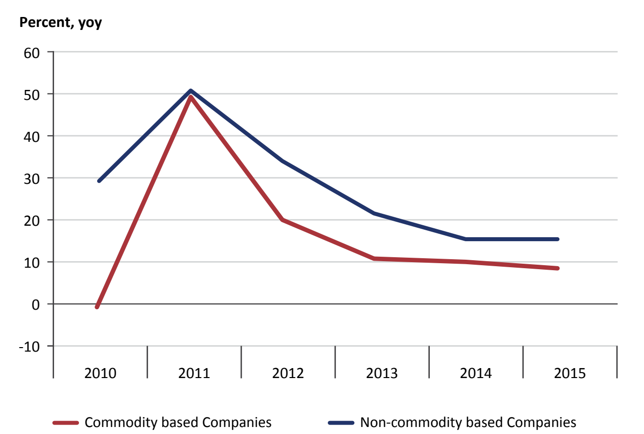
purchasing power. Furthermore, the revenues of other sectors also suffered, with some firms operating in the manufacturing industry reporting income contractions. Nevertheless, corporate revenues, particularly in the construction sector, began to rebound in the final quarter of the year.

The declines in corporate income were inadequately offset by lower expenses, which consumed profits. Lower revenues were accompanied by lower cost of goods sold and operating costs, albeit of more limited magnitude. In addition to lower sales volume, a lower cost of goods sold was precipitated by a contraction in terms of input costs, namely raw materials and energy. Firms using imported raw materials benefitted from lower commodity prices through less pressures on the cost of production as the rupiah depreciated. Consequently, lower input costs led to a more resilient gross profit margin at non-commodity based corporations. Meanwhile, for commodity-based corporations, drastically lower selling prices lowered revenues and also gross profit margin (Chart 3.15). On the other hand, businesses also undertook measures to enhance efficiency through lower operating costs. Reductions to operating costs were limited, however, due to the more fixed nature of the costs. As a result, the net profit margin of commodity-based companies narrowed.

Decreasing corporate profits could have potentially stifled further expansion. Declining corporate profits affected nearly all economic sectors, most notably commodity-based companies. Deteriorating financial conditions also limited future investment opportunities, reflecting an ongoing decline in retained earnings since 2011 (Chart 3.16). Data at the micro level confirmed that the proportion of retained earnings at the majority of corporations in 2015 decreased on the previous year.

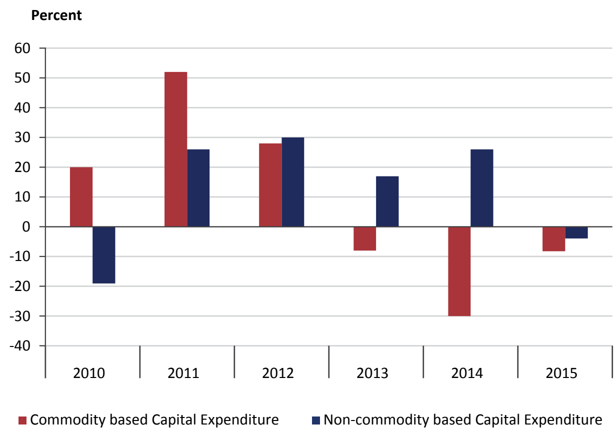
In addition to deteriorating financial conditions, a loss of business confidence also limited business expansion. The majority of issuers corroborated a decline in actual capital spending in line with a decrease in net profit, especially at commodity-based firms where a deep net profit contraction was reported, which acted as a disincentive to capital spending. At non-commodity based firms, however, capital spending still declined in general, with the exception of basic industry and property (Chart 3.17). Weaker financial performance also undermined confidence in economic conditions, reflecting corporate proclivity to reduce inventory in order to meet demand (Chart 3.18). Nevertheless, business sentiment rebounded towards the end of 2015, accompanied by an increase of private

Chart 3.16. Retained Earning of Listed Companies



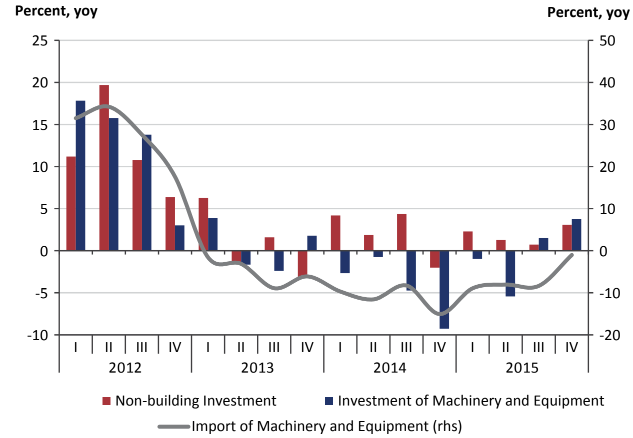
Source: Bloomberg and IDX, processed

Chart 3.17. **Net Profit and Capital Expenditure**



Source: Bloomberg and IDX, processed

Chart 3.19. **Machinery Import and Non-building Investment**



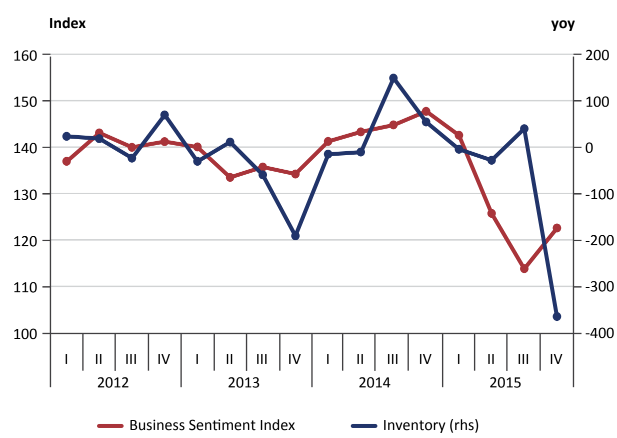
investment, particularly in machinery and equipment (Chart 3.19).

The production slump also led to a decline in household income, which indicated by the decrease in the index of consumer income (Chart 3.20). Lower consumer income triggered a shift in household behavior in terms of consumption and saving. Survey results revealed that the buying of durable goods index declined, confirming less non-food consumption. Furthermore, significant declines in household consumption were seen to affect clothing, housing and household equipment, contrasting robust consumption of basic necessities.

Despite slowing, household consumption remained resilient. Households responded to the indirect effect of economic moderation on income by reducing consumption and dipping into savings as a form of consumption smoothing. Households were more inclined to save when commodity prices were high but have subsequently saved less since 2012. In 2015, individual savings declined sharply in line with the growing portion of income used to meet consumption needs (Chart 3.21). In addition, households also smoothed consumption in line with growing optimism regarding the vastly more promising economic outlook (Chart 3.22).

Receipts, excluding household income, also helped maintain resilient consumption. The results of the Household Balance Sheet Survey (SNRT) conducted by Bank Indonesia in 2015 revealed that household income originating from production and services was insufficient to cover total household costs, which included the routine and non-routine expenses (Chart 3.23). Nonetheless,

Chart 3.18. **Business Sentiment and Inventory**



Source: Danareksa and BPS - Statistics Indonesia

Chart 3.20. **Household Income and Expenditure**

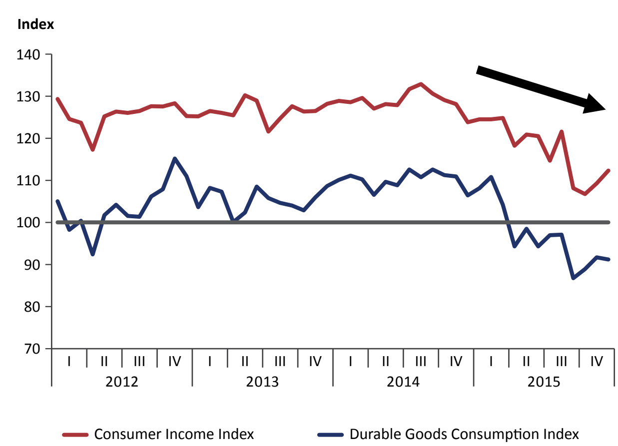


Chart 3.21. Share of Consumption, Saving, and Household Installment

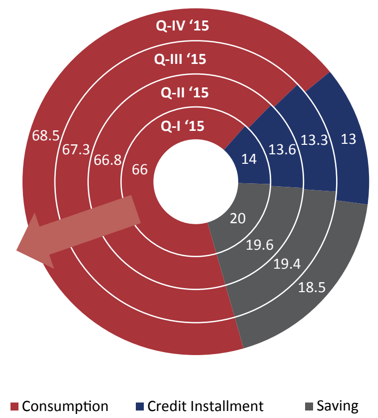
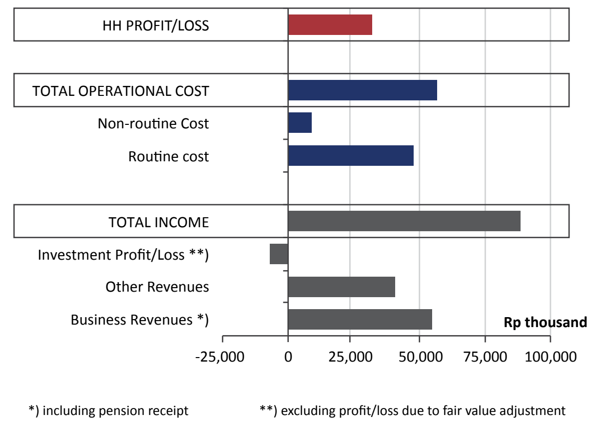


Chart 3.23. Household Income vs Operational Cost

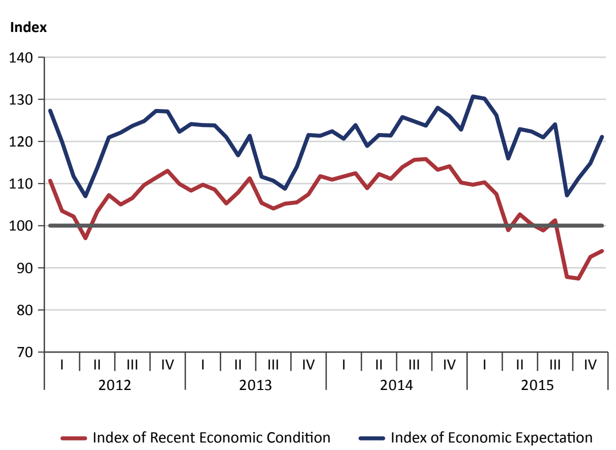


other receipts from third parties, including government assistance/transfers, in this instance, helped meet the needs of households. Fiscal stimuli through Social Assistance program was subsequently expanded 3.1% in 2015 from the previous year (Chart 3.24). Fiscal transfers under the auspices of social protection included School Assistance, Financial Aid for Poor Students and the Family Hope Program (PKH). Taking into consideration the various sources of income available, households booked a net surplus overall in 2015.

3.4. EMPLOYMENT AND WELFARE

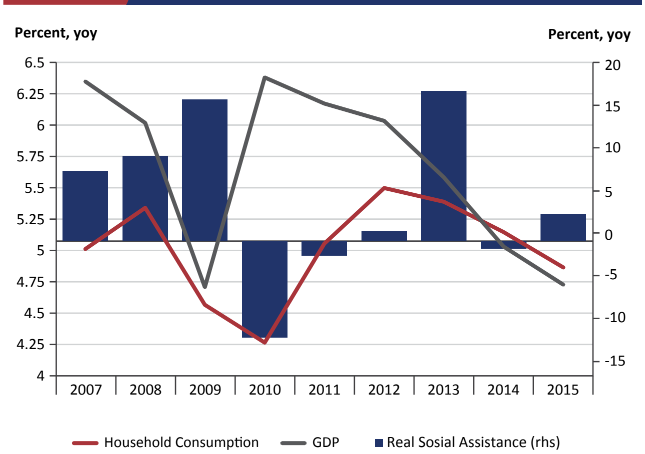
Domestic economic moderation undermined employment conditions. Therefore, the unemployment rate increased in August 2015 to 6.2% from 5.9% the year earlier (Table 3.5), with unemployment up from 7.5 million persons in 2014 to 7.6 million in 2015. The rise in unemployment stemmed from low additional labor absorption in line with the domestic economic slowdown. With growth of just under 5%, the domestic economy only absorbed an additional 200 thousand workers in 2015 (August 2014 – August 2015).

Chart 3.22. Index of Recent Economic Condition and Economic Expectation



Indicators of employment growth also demonstrated a low level of labor absorption in 2015. Job openings (vacancies) followed a downward trend in 2015 (Chart 3.25).[4] Slowing employment growth was in line with sluggish economic growth and also a decline in the elasticity of labor absorption in regard to economic growth. From 2010-

Chart 3.24. GDP, Household Consumption, and Social Assistance



Source: CEIC, processed

4 The job vacancy index is the result of utilising the Big Data by Bank Indonesia.

Table 3.5. **Labor Force and Unemployment**

in million people, unless otherwise stated

No.	Main Activities	2013		2014		2015	
		Feb	Aug	Feb	Aug	Feb	Aug
1	Productive Age (above 15 years)	178.1	180.0	181.2	183.0	184.6	186.1
	- Labor Force Participation (%)	69.2	66.8	69.2	66.6	69.5	65.8
2	Labor Force	123.2	120.2	125.3	121.9	128.3	122.4
	- Full Time Worker (%)	64.6	62.4	64.8	64.7	66.4	65.8
	- Part Time Worker (%)	18.4	22.3	21.1	21.4	20.0	20.1
	- Partial Unemployment (%)	11.1	9.2	8.4	7.9	7.8	8.0
	- Open Unemployment (%)	5.9	6.2	5.7	5.9	5.8	6.2

Source: BPS - Statistics Indonesia, processed

2012, each 1% increase in GDP absorbed an additional 500,000 workers, halving thereafter to just 250,000 in 2013-2015.

Hence, the fiscal stimuli introduced in 2015 had a positive impact on employment. By sector, most additional workers were absorbed into the construction sector as public investment picked up in the third quarter of 2015, in line with the implementation of government infrastructure projects (Chart 3.26). Such conditions alleviated further increase in unemployment, considering several sectors, especially tradeable sectors, suffered from a shrinking workforce, including the agricultural sector, mining sector and manufacturing industry due to unconducive externalities. The mining sector experienced a dramatic decline in the workforce due to the closure of various small-scale (coal) mines as a result of sliding commodity prices that could no longer offset production costs.
It is important to note, however, the improvement in workforce quality. In terms of education, the composition of the workforce educated to a primary level dropped from 47.1% to 44.3%, while the portion of those educated to a tertiary level increased from 9.8% to 11%.

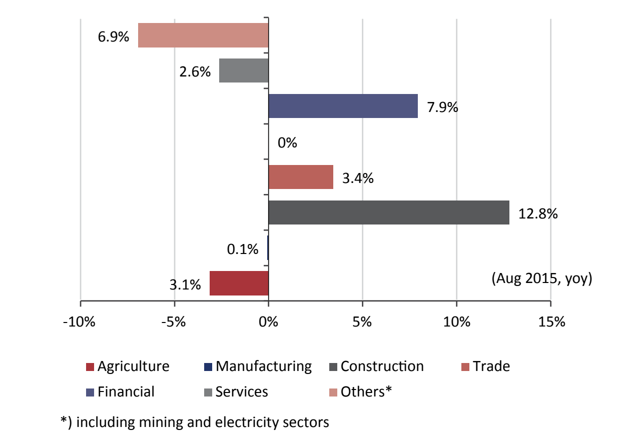
In line with the increase in unemployment, public welfare also deteriorated, reflecting a bump in the percentage of the poor population on the previous year (Chart 3.27). In September 2015, poor people numbered 28.5 million (11.13%), up from 27.7 million (10.96%) the year before. The increase in poor people stemmed from domestic economic moderation coupled with inflationary pressures, which pushed the poverty line in September 2015 up 10.40% (yoy) to Rp344,809 per capita per month, compared to 6.61% (yoy) in September 2014. Nonetheless, welfare tended to improve in the second half of 2016 as the number of poor people declined relatively in line with early signs of economic momentum and fiscal stimuli through various assistance programs.

Income inequality has yet to show signs of improvement. The poverty gap index, as a measure of the intensity of poverty, increased in 2015 on the average of the previous

Chart 3.25. **Availability of Employment and GDP**

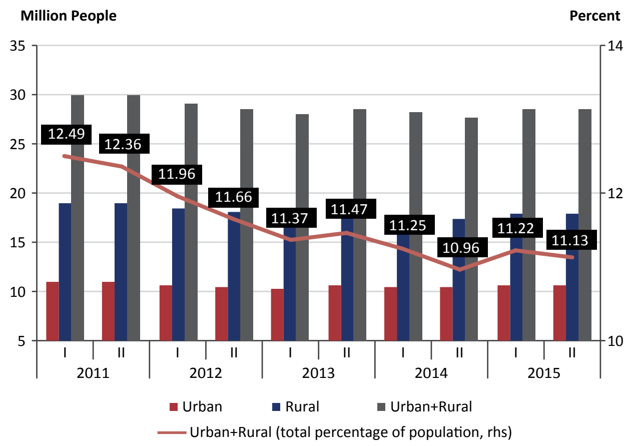
Source: BPS - Statistics Indonesia, processed

Chart 3.26. **Changes in Numbers and Share of Labor by Economic Sector**



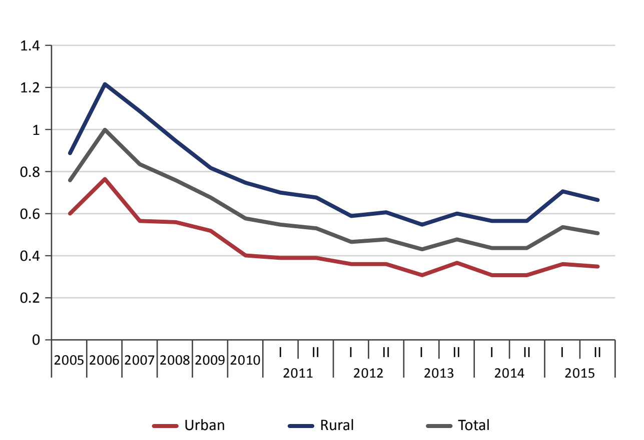
Source: BPS - Statistics Indonesia, processed

Chart 3.27. Level of Poverty



Source: BPS - Statistics Indonesia, processed

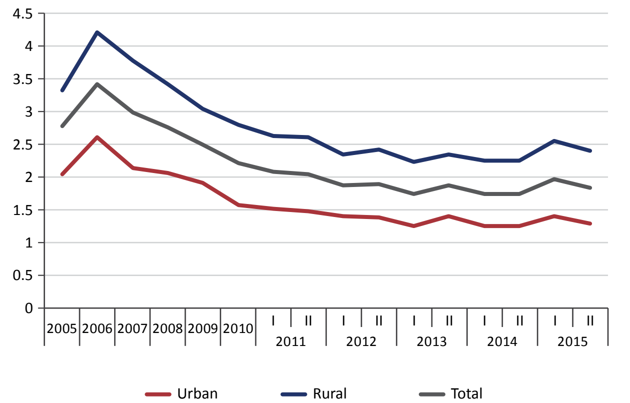
Chart 3.29. Poverty Severity Index



Source: BPS - Statistics Indonesia, processed

year (Chart 3.28).[5] Similar trends were observed for the poverty severity index, which increased on the year earlier (Chart 3.29). The index shows that disparity in spending between poor people also increased.[6] Another inequality indicator, namely the Gini coefficient, further confirmed income inequality, remaining at around 0.41 for the past five years.

Chart 3.28. Poverty Gap Index



Source: BPS - Statistics Indonesia, processed

5 The poverty gap index measures the average poverty gap in the population as a proportion of the poverty line. A higher index indicates a further distance, on average, the poor are from the poverty line or the average percentage shortfall in income for the population from the poverty line.

6 The poverty severity index is a measure of spending disparity between poor people. A higher index value is indicative of greater inequality between poor people.

Loading and unloading activities at the port mirror trade activity and are a key component of Indonesia's Balance of Payments (BOP). Despite a BOP deficit recorded in 2015, the current account deficit was observed to narrow while the capital and financial account also showed early signs of improvement in the fourth quarter.

Chapter 4

Balance of Payments

External sector fundamentals in Indonesia remained sound throughout 2015, supported by a narrower current account deficit and maintained capital and financial account surplus. The narrower current account deficit was bolstered by gains in the trade account, services account, and income account. On the other hand, the capital and financial account surplus was maintained despite widespread uncertainty in global financial markets. Overall, Indonesia's balance of payments (BOP) recorded a modest deficit because the capital and financial account surplus was inadequate to fully offset the current account deficit. Nonetheless, the 2015 BOP deficit was not considered large due to the significant improvements in the capital and financial account achieved in the fourth quarter.

In 2015, current account performance improved despite unconducive global conditions coupled with unresolved domestic structural issues. Current account gains were supported by an improvement of trade surplus as the import decline outpaced the corresponding decline of exports. Real non-oil and gas exports from Indonesia in 2015 enjoyed positive growth on the back of solid agricultural export volume. Nevertheless, sharp price corrections eroded the value of non-oil and gas exports. Additionally, rupiah depreciation was not exploited optimally, which would have boosted the competitiveness of export products from Indonesia. Such conditions were exacerbated further by sliding global commodity prices, including oil. Consequently, Indonesia's export performance declined on the previous year, in line with a weaker terms of trade (ToT).[1]

Regarding imports, domestic economic moderation, rupiah depreciation, and energy subsidies reforms affected import performance. Rupiah depreciation triggered relatively more expensive import prices, thus reducing shipments. Furthermore, government policy to cut energy subsidies raised the price of fuel and, therefore, lowered domestic consumption and reduced the need for oil imports. Such developments led to a steeper decrease in imports than the corresponding export decline, thereby boosting the trade surplus in 2015. The import decline began to ease in the fourth quarter of 2015 as the domestic economy rebounded, which curbed the overall import decline for the year.

In terms of the financial channel, the capital and financial account surplus was maintained in 2015 in spite of global economic moderation and growing uncertainty in global financial markets. Notwithstanding, capital and financial account performance deteriorated significantly during the first three quarters of 2015 but subsequently rebounded in the final quarter after global uncertainty eased and optimism in the auspicious economic outlook was restored. Such conditions reignited non-resident investor interest in long-term investment in Indonesia in the form of direct investment. Furthermore, the domestic economic uptick in the fourth quarter, coupled with attractive rate of returns in Indonesia, increased foreign capital in portfolio investment. Regarding other investments, a combination of unconducive global and domestic conditions prompted a net outflow of resident and non-resident capital and lessened demand for corporate funding through foreign loans in the first semester. In the second semester, however, other investments bucked the prevailing trend and recorded a surplus that continued until the end of 2015. Therefore, the capital and financial account surplus was maintained in 2015, despite narrowing on the year earlier. The narrower capital and financial account surplus was inadequate to fully offset the current account deficit. Consequently, the balance of payments (BOP) deficit in 2015 stood at a moderate USD1.1 billion (Table 4.1). Congruously, Indonesia's International Investment Position (IIP) recorded a smaller net liability in 2015 than the previous year (Table 4.2).

Consistent with the BOP deficit in 2015, the position of official reserve assets also declined as compare to the previous year but remained at a level considered safe. The declined in the official reserve assets was due to government external debt services and Bank Indonesia utilised the reserve assets to stabilize the rupiah in line with its fundamental value. The move was in pursuance of Bank Indonesia's avowed commitment to maintain rupiah stability and, therefore, macroeconomic and financial system stability. Despite declining, the position of reserve assets was still maintained at a level of USD105.9 billion, equivalent to 7.4 months of imports and servicing government external debt. Furthermore, Bank Indonesia perceived the position of official reserve assets as adequate to support external sector resilience and preserve sustainable economic growth in Indonesia moving forward.

Dwindling demand for offshore funding, in line with the domestic economic slowdown, alleviated the spiralling growth of external debt in 2015. The position of external debt increased in 2015, however, due to long-term foreign loans, while short-term debt eased. In terms of the risk profile, the position of external debt was considered relatively secure because only a small portion allocated to short-term non-affiliated nonbank corporate external debt, which is associated with the highest risk profile. In addition, Bank Indonesia also mitigated the risks linked to nonbank corporate debt by issuing Bank Indonesia Regulation (PBI) No. 16/21/PBI/2014 concerning the Implementation of Prudential Principles in Managing External Debt of Nonbank Corporation. By the end of 2015, implementation of the Bank Indonesia Regulation (PBI) had successfully improved efforts at nonbank corporations to mitigate risk by applying prudential principles when managing external debt.

Looking ahead, the current account deficit is predicted to widen as the domestic economy rebounds but remain within a safe limit. A surge of non-oil and gas imports, while the corresponding exports remain flat, will swell the current account deficit. Limited increases in global demand due to the global economic downturn, coupled

1 The terms of trade refers to the ratio of export prices to import prices.

Table 4.1. **Indonesia's Balance of Payments**

USD million

Items	2014*				Total*	2015**				Total**
	I	II	III	IV		I*	II*	III*	IV**	
I. Current Account	**-4,927**	**-9,585**	**-7,035**	**-5,953**	**-27,499**	**-4,159**	**-4,296**	**-4,190**	**-5,115**	**-17,761**
A. Goods, net	3,350	-375	1,560	2,448	6,983	3,063	4,125	4,141	1,953	13,281
- Export	43,937	44,505	43,606	43,245	175,293	37,827	39,685	36,086	34,743	148,341
- Import	-40,588	-44,880	-42,046	-40,797	-168,310	-34,764	-35,561	-31,945	-32,790	-135,060
1. General Merchandise	2,832	-703	1,192	2,153	5,474	2,690	3,810	4,047	2,004	12,551
- Export	43,414	44,171	43,232	42,944	173,760	37,450	39,366	35,728	34,397	146,941
- Import	-40,581	-44,874	-42,039	-40,791	-168,286	-34,760	-35,557	-31,680	-32,392	-134,389
a. Non Oil and Gas	5,581	2,475	4,326	4,922	17,304	3,947	5,932	6,158	2,987	19,024
- Export	35,822	36,657	35,970	36,560	145,008	33,068	34,722	32,038	30,698	130,526
- Import	-30,241	-34,182	-31,644	-31,638	-127,704	-29,122	-28,790	-25,880	-27,711	-111,502
b. Oil	-6,056	-6,137	-6,037	-5,672	-23,903	-3,184	-3,658	-3,521	-2,753	-13,115
- Export	3,500	3,885	3,590	2,831	13,806	1,927	2,611	1,786	1,500	7,823
- Import	-9,556	-10,022	-9,627	-8,503	-37,709	-5,111	-6,268	-5,307	-4,253	-20,938
c. Gas	3,308	2,959	2,904	2,903	12,074	1,927	1,535	1,410	1,770	6,643
- Export	4,092	3,629	3,672	3,553	14,946	2,455	2,034	1,904	2,198	8,592
- Import	-785	-670	-768	-649	-2,873	-528	-498	-494	-429	-1,949
2. Other Goods	518	328	368	295	1,509	372	315	94	-51	730
- Export	524	333	374	302	1,533	376	319	358	346	1,400
- Import	-6	-5	-6	-7	-24	-4	-4	-264	-398	-670
B. Services, net	-2,131	-2,831	-2,486	-2,561	-10,010	-1,845	-2,651	-2,151	-1,846	-8,493
C. Primary Income, net	-7,230	-7,912	-7,313	-7,236	-29,692	-6,805	-7,195	-7,452	-6,576	-28,028
D. Secondary Income, net	1,085	1,534	1,204	1,397	5,220	1,428	1,426	1,272	1,354	5,479
II. Capital and Financial Account	**6,388**	**14,492**	**14,535**	**9,574**	**44,989**	**5,087**	**2,241**	**279**	**9,529**	**17,136**
A. Capital Account	1	7	3	15	27	1	0	2	14	17
B. Financial Account	6,387	14,484	14,532	9,559	44,962	5,086	2,241	277	9,516	17,120
- Assets	-5,393	-2,960	-3,786	1,353	-10,786	-8,302	-8,524	-3,787	340	-20,273
- Liabilities	11,780	17,445	18,318	8,206	55,748	13,388	10,765	4,064	9,175	37,393
1. Direct Investment	2,023	4,353	5,752	2,661	14,788	1,695	3,467	1,782	2,315	9,259
a. Assets	-2,883	-2,407	-2,226	-2,871	-10,388	-3,451	-3,394	-1,345	-1,237	-9,427
b. Liabilities	4,906	6,760	7,979	5,532	25,176	5,146	6,860	3,127	3,553	18,686
2. Portfolio Investment	8,730	8,046	7,409	1,883	26,067	8,509	5,592	-2,218	4,825	16,707
a. Assets	465	-991	1,299	1,814	2,587	24	-737	-683	393	-1,003
b. Liabilities	8,265	9,037	6,110	69	23,481	8,484	6,329	-1,535	4,431	17,709
3. Financial Derivatives	-140	45	-20	-40	-156	93	-3	231	-301	20
a. Assets	239	64	11	128	441	205	229	196	37	667
b. Liabilities	-379	-19	-32	-168	-597	-112	-232	35	-338	-647
4. Other Investment	-4,225	2,040	1,390	5,056	4,262	-5,210	-6,815	483	2,677	-8,866
a. Assets	-3,214	375	-2,871	2,283	-3,426	-5,080	-4,622	-1,955	1,148	-10,510
b. Liabilities	-1,011	1,666	4,261	2,773	7,688	-130	-2,192	2,438	1,529	1,645
III. Total (I + II)	**1,462**	**4,907**	**7,500**	**3,621**	**17,489**	**928**	**-2,055**	**-3,912**	**4,415**	**-624**
III. Net Error and Omissions	**605**	**-610**	**-1,025**	**-1,211**	**-2,241**	**375**	**-870**	**-654**	**675**	**-474**
IV. Overall Balance (III + IV)	**2,066**	**4,297**	**6,475**	**2,410**	**15,249**	**1,303**	**-2,925**	**-4,565**	**5,089**	**-1,098**
VI. Reserves and Related Items	**-2,066**	**-4,297**	**-6,475**	**-2,410**	**-15,249**	**-1,303**	**2,925**	**4,565**	**-5,089**	**1,098**
Memorandum:										
- Reserve Assets Position	102,592	107,678	111,164	111,862	111,862	111,554	108,030	101,720	105,931	105,931
- In Months of Imports & Official Debt Repayment	5.7	6.1	6.3	6.4	6.4	6.6	6.8	6.8	7.4	7.4
- Current Account to GDP Ratio (%)	-2.3	-4.3	-3	-2.7	-3.1	-2	-2	-1.9	-2.4	-2.1

* preliminary figures
** very preliminary figures

Table 4.2. **Indonesia's International Investment Position**

USD million

Items	2014*				Total*	2015**				Total**
	I	II	III	IV		I*	II*	III*	IV**	
Indonesia's International Investment Position	**-367,160**	**-373,572**	**-392,390**	**-394,466**	**-394,466**	**-394,825**	**-380,044**	**-348,011**	**-380,672**	**-380,672**
- Direct Investment, net	-187,974	-190,734	-203,339	-202,359	-202,359	-198,494	-196,562	-186,711	-194,672	-194,672
- Portfolio Investment, net	-174,323	-179,939	-191,531	-192,656	-192,656	-202,455	-192,960	-163,295	-189,369	-189,369
- Financial Derivatives, net	98	37	21	30	30	1	61	-13	91	91
- Other Investment, net	-107,554	-110,614	-108,704	-111,342	-111,342	-105,431	-98,613	-99,712	-102,653	-102,653
- Reserves	102,592	107,678	111,164	111,862	111,862	111,554	108,030	101,720	105,931	105,931

* preliminary figures ** very preliminary figures

with soft global commodity and oil prices, will impeded export performance. On the other hand, growing domestic demand as the economy recovers will be met through a rise in non-oil and gas imports. In addition, predominantly government-led efforts to accelerate infrastructure development will also heighten import activity, especially imports of capital goods.

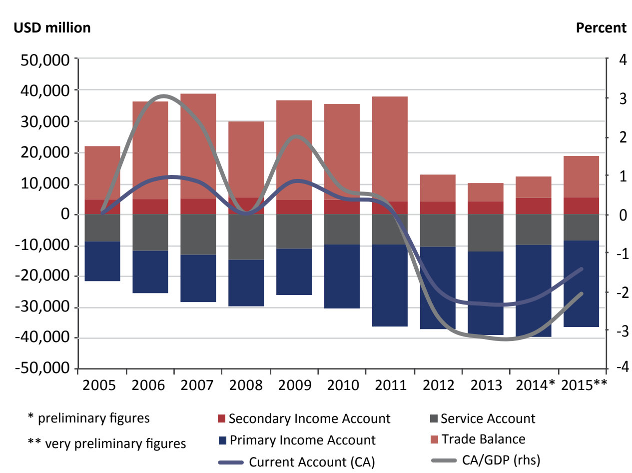
The capital and financial account performance is projected to improve with a significantly larger surplus envisioned. Consequently, the balance of payments should record a surplus, thus driving increases in the position of reserve assets. Global and domestic economic momentum, bolstered by structural reforms and the Government's I-VIII Policy Package in 2015, should prompt a deluge of non-resident capital inflows through direct investment. Furthermore, the expected gradual increase in the Federal Funds Rate (FFR) will also maintain the influx of portfolio capital inflows. Congruously, the other investment deficit will also improve as companies withdraw more foreign loans in line with the promising domestic economic outlook. The capital and financial account surplus is expected to exceed the current account deficit, thus precipitating a surplus balance of payments (BOP) once again. BOP performance is forecasted to improve, supported by an appropriate monetary and macroprudential policy mix along with policy coordination enhancement between Bank Indonesia and the Government. Nonetheless, global developments will continue to demand vigilance, particularly in terms of the economic downshift in China and the ongoing international commodity price slide, which could undermine the BOP overall performance.

4.1. CURRENT ACCOUNT

Against the inauspicious backdrop of global economic moderation, tumbling international commodity prices, and a domestic economic slowdown, the current account deficit improved in 2015. The current account recorded a deficit of USD17.8 billion in 2015, equivalent to 2.1% of GDP, down from USD27.5 billion the year earlier or 3.1% of GDP. The current account gains were supported by larger surpluses reported in the trade balance and secondary income account as well as narrower deficits in the services account and primary income account (Chart 4.1).

The trade balance posted a growing surplus in 2015 on the back of a larger non-oil and gas trade balance surplus combined with a narrower oil and gas trade balance deficit. The increase in non-oil and gas trade balance surplus in 2015 was driven by a decline in non-oil and gas imports that surpassed the corresponding export decline, affecting all goods, including consumer goods, raw materials, and capital goods. Dwindling domestic demand prompted the decline of consumer goods imports in line with less household consumption, which was accompanied by weaker sales data amidst economic moderation, thus suppressing demand for investment and working capital. Less demand for investment ultimately eroded imports,

Chart 4.1. **Current Account Development**



particularly of raw materials and capital goods. In addition, rupiah depreciation precipitated further declines of non-oil and gas imports as imported prices became relatively more expensive. Meanwhile, sluggish external demand due to the global downtick spurred the non-oil and gas export decline, which was further compounded by the unrelenting international commodity price slide. Moreover, Indonesia's export dependence on natural resources left the country reeling from low commodity prices. Furthermore, the low competitiveness of export products in comparison to competing countries undermined the favourable impact of rupiah depreciation.

The oil and gas trade balance deficit narrowed after oil imports decreased as a result of energy price reforms that reduced oil consumption and, therefore, the need for imports. Policy to remove energy subsidies and provide fixed fuel subsidies by the Government, which ultimately raised fuel prices, successfully depressed domestic fuel consumption. The domestic economic slowdown also reduced fuel consumption through lower demand. In addition, the significant drop in the international oil price throughout 2015 also lowered oil imports.

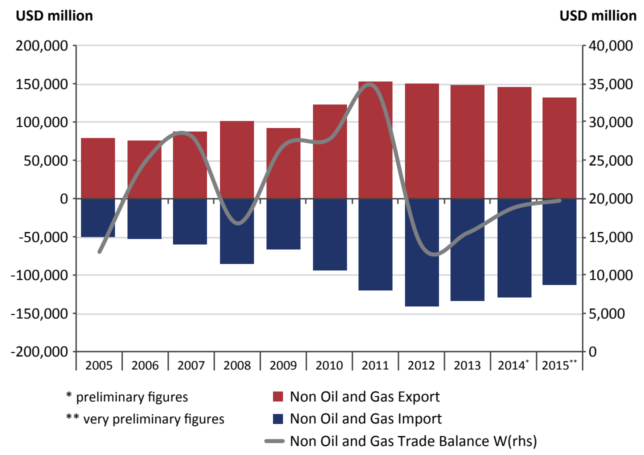
Further improvements on the current account were supported by narrower services account and income account deficits. The services account in 2015 was bolstered by lower payments of freight transportation services together with a growing travel services surplus. Meanwhile, the income account benefitted from a smaller primary income account deficit due to fewer direct investment dividend payments and a wider secondary income account surplus as a result of increasing remittances from Indonesian migrant workers (TKI).

Non-Oil and Gas Trade Balance

The non-oil and gas trade balance registered a growing surplus in 2015 as the main contributor to the narrower current account deficit and continued the prevailing upward trend since 2013. In 2015, the non-oil and gas trade balance recorded a surplus totalling USD19.8 billion, up from USD18.8 billion the year earlier. A 12.4% decline in non-oil and gas imports that exceeded the 10.0% drop in exports was instrumental in the larger surplus (Chart 4.2).

The fragile economic recovery in advanced countries, together with slower growth in developing countries, weakened demand for products exported from Indonesia. Weaker global demand was reflected in the exports to 10 leading trade partners of Indonesia, which all experienced declines with the exception of the Philippines (Table

Chart 4.2. Development of Non-Oil and Gas Trade Balance



4.3). Indonesian exports to the United States contracted by 3.5% despite the modest U.S. economic growth and robust consumption reported. Exports of manufacturing products, such as electrical equipment, processed foods, and processed natural rubber, as the backbone of Indonesian exports to the United States, declined. Such conditions were symptomatic of the weak competitiveness of Indonesian exports compared to competing countries. Furthermore, textile exports to the U.S., representing the largest Indonesian export component to the U.S., also contracted as a result of growing competition from Vietnam and Bangladesh.

Export growth to India, Japan, and China also decelerated. To India, exports of coal and crude palm oil (CPO) were primarily affected but shipments of copper ore and articles of non-precious metals actually enjoyed positive export performance in line with robust economic growth in India. Meanwhile, the economies of Japan and China were more lacklustre, which drove down demand from both countries, in particular for coal. Exports of textiles, measuring instruments and articles of non-precious metals to Japan also suffered, while exports of processed wood to China slumped. In contrast, exports of CPO and textiles to China still posted growth in positive territory.

Torpid export performance in Indonesia was primarily attributable to sliding commodity prices, reflecting lower prices of leading export commodities from Indonesia on the international market. The prices of the 10 leading export commodities from Indonesia fell by 7.1% in 2015 (Table 4.4), most notably affecting coal and CPO. The export price of coal fell by 13.7% in 2015, which saw coal exports slump by 23.4%. In addition to price factors, coal exports were also down by 12.3% in terms of volume as a

Table 4.3. **Non-Oil and Gas Exports by Country**

Items	Share (%)		Annual Growth (%, yoy)									
			2014*					2015**				
	2014*	2015**	I	II	III	IV	Total	I*	II*	III*	IV**	Total**
United States of America	10.8	11.6	2.6	7.6	6.5	5.5	5.6	-1.1	-0.4	-4.8	-7.6	-3.5
China	11.2	10.0	-2.7	-17.8	-24.8	-39.1	-22.2	-36.5	-13.1	-9.6	-13.8	-19.5
Japan	10.0	9.9	-12.6	-11.4	-5.6	-4.8	-8.7	-5.4	-8.4	-12.9	-17.1	-11.1
India	8.3	8.8	-13.9	-16.9	19.8	-7.1	-5.6	7.3	18.1	-27.0	-14.2	-5.1
Singapore	6.7	6.5	2.3	23.4	8.1	12.5	11.6	1.7	-19.4	-9.2	-16.8	-11.4
Malaysia	4.4	4.7	-19.9	-6.8	-8.0	-7.2	-10.6	3.5	0.2	-7.3	-9.8	-3.4
South Korea	3.9	4.1	-11.0	-6.5	2.9	-3.0	-4.6	0.1	0.4	-6.3	-16.8	-5.7
Thailand	3.4	3.5	-5.7	-10.4	2.8	-2.7	-4.2	-6.4	-4.0	-11.6	-10.2	-8.0
Philippines	2.7	3.0	-2.1	6.7	9.4	-0.1	3.4	-2.0	4.2	7.2	-7.2	0.8
Australia & Oceania	3.1	2.8	36.5	39.3	13.8	-15.6	15.2	-36.4	-17.0	7.4	-21.6	-17.5
Total of 10 Countries	**64.5**	**64.9**	**-5.1**	**-4.4**	**-1.2**	**-10.7**	**-5.5**	**-9.6**	**-4.4**	**-10.0**	**-13.5**	**-9.4**

* preliminary figures
** very preliminary figures

result of less demand from China, consistent with domestic policy to reduce coal use in order to combat rampant pollution and promote alternative sources of energy.

Demand for CPO exports remained resilient despite global economic moderation and lower international prices. The export price of CPO in Indonesia fell by 18.1% in 2015, which prompted a 10.7% drop in CPO exports. The lower CPO price in Indonesia was in line with sliding international CPO prices according to World Bank data, falling from an average of USD821 per metric ton (MT) in 2014 to USD623 per MT in 2015. Notwithstanding soft prices, demand for crude palm oil (CPO) actually increased in 2015 despite the global economic downswing, reflecting a 14.6% increase in export volume. Such conditions were indicative of growing demand for CPO year on year as the global population expands and awareness builds concerning alternative energy sources. Robust growth of CPO export volume also stemmed from the 0% export duty imposed on the product. The average international CPO price in 2015 failed to hit USD700 per MT, which is the threshold for export duties to apply. Consequently, the majority of CPO producers opted to export the product directly rather than by-products or derivatives. Consistent with sliding

Table 4.4. **Export of 10 Main Non-Oil and Gas Commodities**

Items	Share (%)		Growth (%, yoy)																	
			Nominal						Real						Price Index					
				2015**						2015**						2015**				
	2014*	2015**	2014*	I*	II*	III*	IV**	Total**	2014*	I*	II*	III*	IV**	Total**	2014*	I*	II*	III*	IV**	Total**
Vegetable Oils	13.7	13.6	9.2	-12.6	6.0	-16.9	-17.9	-10.7	11.5	11.1	36.2	9.0	-1.0	14.6	-22.1	-21.2	-22.4	-23.7	-22.1	-18.1
Coal	14.2	12.1	-14.5	-17.7	-24.9	-24.9	-26.5	-23.4	-14.3	-7.0	-12.6	-13.2	-19.9	-12.3	-12.6	-11.6	-14.1	-13.6	-12.6	-13.7
Textile	8.8	9.4	0.6	-2.6	-2.7	-5.8	-4.8	-4.0	2.1	2.0	2.9	-0.4	0.7	1.5	-5.4	-4.5	-5.5	-5.4	-5.4	-3.9
Electricity	6.9	6.7	-5.7	-12.1	-11.8	-14.0	-14.7	-13.2	0.0	-5.9	-4.6	-7.8	-12.8	-7.5	-6.1	-6.5	-7.5	-6.9	-6.1	-2.6
Base Metal	6.2	5.8	5.5	-3.7	-16.1	-18.7	-24.9	-16.2	3.7	1.9	-8.5	-0.3	-5.8	-3.3	-13.4	-5.4	-8.2	-18.4	-13.4	-4.7
Processed Food	4.3	4.8	17.8	3.5	-0.4	-6.9	1.4	-0.6	12.1	3.4	-0.4	4.2	13.4	5.1	-5.4	0.1	-0.1	-10.5	-5.4	0.4
Processed Rubber	4.8	4.4	-24.5	-31.7	-13.2	-6.6	-12.1	-16.8	-16.4	-23.8	-4.0	17.2	19.3	-0.2	-16.6	-10.4	-9.5	-19.8	-16.6	-9.8
Vehicles and Parts	3.6	4.1	14.8	9.4	20.5	3.8	-16.4	3.3	12.3	3.0	14.1	1.1	-19.5	-1.4	4.8	6.2	5.5	2.7	4.8	5.9
Machineries	4.1	3.9	6.0	-15.8	-13.4	-9.1	-23.1	-15.5	6.5	-14.8	-12.4	-8.5	-21.3	-14.3	-1.4	-1.3	-1.1	-0.6	-1.4	-0.5
Processed Wood	2.7	2.9	11.3	-2.2	0.4	-4.2	-3.5	-2.3	10.1	12.8	31.9	34.8	40.6	29.6	-24.6	-13.3	-23.9	-28.9	-24.6	-7.6
Total of 10 Commodities	**69.3**	**67.6**	**-1.8**	**-11.0**	**-8.1**	**-13.6**	**-16.3**	**-12.2**	**-0.6**	**-2.6**	**2.9**	**1.4**	**-2.9**	**0.0**	**-12.3**	**-8.6**	**-10.6**	**-14.7**	**-12.3**	**-7.1**

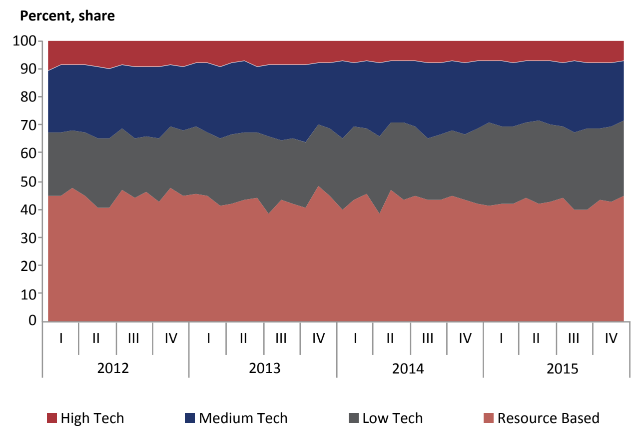
* preliminary figure
** very preliminary figure

commodity prices on the international market, Indonesia's terms of trade (ToT) decreased from 81.6 in December 2014 to 73.6 in December 2015.

Global economic moderation tended to affect demand for manufacturing products more than primary products from Indonesia, which rely to a greater extent on natural resources. The impact of the slowdown on manufacturing prices, however, was less pronounced than on the prices of primary products. In 2015, the volume of manufacturing exports fell by 7.4%, while the export volume of primary products enjoyed growth of 17.5%, buoyed by agricultural exports. Crude palm oil (CPO) was one such commodity that propped up export volume. In addition, agricultural exports were also supported by a greater export volume of coffee, fruits, and vegetables as well as pulp. Nevertheless, sliding commodity prices throughout 2015 triggered a precipitous drop in the export prices of primary products, falling from -4.4% in 2014 to -25.7% in 2015. Conversely, manufacturing product prices remained in positive territory, decreasing from 1.9% growth in 2014 to 0.5% in 2015 (Table 4.5).

Manufacturing export prices were relatively unaffected by the global economic slowdown but manufacturing exports were still plagued by structural issues. The structure of manufacturing products was still dominated natural resources (Chart 4.3), which left exports exposed to changes in commodity prices. Lower commodity prices, similar to trends throughout 2015, place pressures on manufacturing exports. Moreover, the import content

Chart 4.3. Composition of Indonesia Manufacturing Exports



Source: United Nations Industrial Development Organization (UNIDO)

of manufacturing products in Indonesia is high, thus preventing optimal exploitation of rupiah depreciation as raw materials become relatively more expensive. The manufacturing products that suffered the largest declines in 2015 include rubber products, clothing, and organic chemicals.

Exports of rubber products contracted by 7.0% in 2015 due to lower prices and volume despite a growing share in several export destination countries over the past few years. The contraction was felt most strongly by exports to Japan, Australia, and Germany. In contrast, exports to the United States achieved positive growth in 2015

Table 4.5. Non-Oil and Gas Exports According to SITC

Items	Annual Growth (%, yoy)									
	2014*					2015**				
	I	II	III	IV	Total	I	II*	III*	IV**	Total**
A. Primary Product										
Nominal	-9.0	-9.4	0.8	-13.4	-8.0	-10.2	-5.7	-16.2	-18.4	-12.7
Real	-3.4	-10.6	-0.4	0.4	-3.9	14.3	25.7	18.7	12.5	17.5
Price Index	-5.8	1.4	1.2	-13.8	-4.4	-21.4	-25.0	-29.5	-27.4	-25.7
B. Manufacturing Product										
Nominal	9.2	8.6	6.8	3.4	6.9	-4.9	-4.5	-4.9	-13.3	-6.9
Real	10.3	8.2	3.2	-1.3	5.0	-8.0	-7.4	-4.2	-10.3	-7.4
Price Index	-1.0	0.4	3.5	4.7	1.9	3.3	3.2	-0.7	-3.4	0.5
C. Others										
Nominal	41.3	20.8	-24.3	-32.2	-4.9	-26.1	-17.8	-14.0	-6.8	-17.0
Real	60.6	26.9	-23.4	-28.9	1.1	-22.2	-11.6	-2.1	1.7	-9.7
Price Index	-12.0	-4.9	-1.2	-4.7	-5.9	-4.9	-6.9	-12.2	-8.4	-8.1
Total										
Nominal	-0.3	-0.9	3.0	-6.5	-1.3	-8.0	-5.3	-10.9	-15.8	-10.0
Real	2.8	-2.6	-0.2	-2.2	-0.7	2.3	7.8	4.7	-3.4	2.8
Price Index	-3.0	1.8	3.2	-4.4	-0.7	-10.0	-12.1	-14.9	-12.8	-12.4

* preliminary figure
** very preliminary figure

Table 4.6. Indonesian Export of Rubber Products to Major Destination Countries

Items	Share 2015 (%)**	Growth (%, yoy)							
		2014*				2015**			
		I	II	III	IV	I*	II*	III*	IV**
Unites States of America	34.5	19.4	-6.6	-20.6	0.2	16.5	18.4	59.8	31.5
Japan	9.3	-10.1	5.2	0.5	-18.7	-18.3	-24.3	-21.6	-9.8
Australia	4.3	-17.6	3.1	4.2	-12.3	21.7	-4.4	-26.6	-10.5
Germany	4.2	-9.4	27.1	15.7	9.9	-1.6	-19.9	-6.6	-20.6
Malaysia	4.1	-35.4	-14.0	-23.1	-15.9	27.7	-16.3	-14.9	1.6

* preliminary figure
** very preliminary figure

(Table 4.6). Declining exports to Japan began with a decreasing market share over the past five years (2009-2014) while the shares of competitors, including China and Vietnam, have increased. In Australia, however, despite slower growth in 2015, the market share of Indonesia has increased over the last half decade (Table 4.7), indicating that Indonesia has successfully exploited the declining shares of competitors, such as Japan and South Korea, to gain market share in Australia. Nonetheless, China and Thailand were even more successful in terms of grabbing market share in Australia. On the U.S. market, the share of Indonesian exports has increased but yet again the shares China and Thailand increased even more impressively from 2009-2014.

Clothing exports fell by 1.3% in 2015 on volume but began to show signs of improvement in the third quarter (Table 4.8). The share of Indonesian clothing on the U.S. market as the main export destination has fallen persistently over the past five years (Table 4.9). In contrast, the share of clothing from Vietnam and Bangladesh, as the leading competitors, has increased. The dwindling share of Indonesian clothing is indicative of weak competitiveness compared to Vietnam, Bangladesh, and China. Competition has recently become even tighter after Europe provided a number of concessions to exporters from countries with low GDP, such as Vietnam, Cambodia, and Bangladesh. Nonetheless, since the third quarter of 2015, export growth to the U.S. and a number of other large countries was observed to rebound.

Exports of organic chemical products have fallen since October 2014, contracting 31.8%, due to price factors and volume in 2015. Exports initially declined to China and Japan but have more recently also decreased to India and the United States (Table 4.10). Nevertheless, declining exports to China have started to ease. In addition, from 2009-2014, Indonesia's position as supplier of organic chemicals to China improved from 10th to 7th, increasing 0.9% (Table 4.11). Indonesia's closest competitor, Malaysia, has improved over the same period from 9th to 8th, with share increasing by 0.2%. Moving forward, Malaysia has the potential to erode Indonesia's market share of chemical products. In terms of prices, organic chemical

Table 4.7. Market Share of Rubber Exporters in Japan, Australia, and the U.S.

Japan Market				Australia Market				U.S. Market			
Country of Origin	Share (%)			Country of Origin	Share (%)			Country of Origin	Share (%)		
	2009	2014	Δ		2009	2014	Δ		2009	2014	Δ
China	23.6	28.9	5.3 ↑	China	17.3	22.9	5.5 ↑	China	23.4	25.9	2.5 ↑
Thailand	16.3	15.7	-0.6 ↓	Japan	23.3	19.2	-4.1 ↓	Canada	18.4	12.9	-5.4 ↓
Indonesia	13.8	8.3	-5.5 ↓	Thailand	6.7	9.1	2.4 ↑	Japan	13.8	9.9	-3.8 ↓
South Korea	9.7	6.6	-3.1 ↓	South Korea	5.9	3.7	-2.2 ↓	Mexico	6.7	8.1	1.4 ↑
U.S.	7.9	6.4	-1.5 ↓	Germany	4.0	3.6	-0.5 ↓	South Korea	6.8	7.3	0.5 ↑
Vietnam	1.2	4.6	3.4 ↑	Spain	4.4	3.3	-1.1 ↓	Thailand	3.6	4.8	1.2 ↑
Germany	4.6	4.5	-0.1 ↓	Indonesia	2.2	3.0	0.9 ↑	Germany	4.5	4.5	0.0 ↑
France	2.0	2.7	0.7 ↑	Malaysia	1.9	2.4	0.5 ↑	Indonesia	1.9	2.5	0.6 ↑
Phillippines	1.7	2.4	0.7 ↑	India	1.5	1.7	0.2 ↑	France	2.1	2.1	0.0 ↓
Spain	1.2	2.4	1.2 ↑	France	2.2	1.5	-0.7 ↓	Chile	0.0	1.8	1.8 ↑

Source: UN Comtrade

Table 4.8. Indonesian Export of Clothing Products to Major Destination Countries

Items	Share 2014 (%)*	Share 2015 (%)**	Growth (%, yoy)							
			2014*				2015**			
			I	II	III	IV	I*	II*	III*	IV**
United States of America	49.4	49.9	-6.3	-3.9	-3.1	1.6	-7.2	-0.7	5.6	1.6
Japan	8.8	9.3	7.8	1.7	0.9	5.4	5.5	-3.3	5.5	10.1
Germany	7.4	6.2	9.5	24.7	-5.3	-7.8	-14.5	-21.9	-15.3	-13.3
South Korea	3.7	3.9	21.1	-3.5	-5.9	-4.2	-2.8	19.8	16.1	-12.0
England	3.5	2.8	-3.0	10.3	-14.5	-21.7	-28.9	-25.5	-19.4	-6.8

* preliminary figure
** very preliminary figure

export prices fell in step with lower CPO prices as a leading component of organic chemicals. Furthermore, the low international oil price, which had dropped to a level below the CPO price, made biodiesel prices uneconomical. Additionally, the 0% export duty on CPO compels producers to export directly hence limited the supply of CPO for organic chemicals downstream industries.

As non-oil and gas exports declined, so too did non-oil and gas imports. Non-oil and gas imports fell by 12.4% in 2015 compared to 3.9% the year earlier, affecting all commodity groups due to lower prices and volume. Fewer imports of consumer goods were the result of dwindling demand in line with less household consumption. Lower consumption was accompanied by weaker sales while players onfidence in the domestic economy were limited, thereby undermining demand for investment and working capital. Less demand for investment ultimately eroded imports, particularly of raw materials and capital goods. In addition, rupiah depreciation precipitated further declines of non-oil and gas imports as imported prices became relatively more expensive.

Table 4.9. Market Share of Clothing Exporters in the U.S.

Country of Origin	U.S. Market		
	Share (%)		
	2009	2014	Δ
China	39.1	38.1	-1.0 ↓
Vietnam	7.4	10.4	3.0 ↑
Indonesia	**5.8**	**5.5**	**-0.2 ↓**
Bangladesh	5.0	5.4	0.4 ↑
Mexico	5.0	4.3	-0.7 ↓
India	4.3	4.1	-0.3 ↓
Honduras	3.0	2.9	-0.1 ↓
Cambodia	2.7	2.8	0.1 ↑
El Salvador	1.8	2.1	0.2 ↑
Sri Lanka	1.8	2.1	0.2 ↑

Source: UN Comtrade

Imports of consumer goods contracted by 9.9% in 2015 due to volume as a result of less household consumption (Table 4.12). Meanwhile, import prices fell in line with lower global prices. The import decline of consumer goods was attributed primarily to fresh/dried fruits (dropping 15.7% on 2014), fresh/frozen vegetables (13.6%), and processed edibles (3.0%). Further import declines were offset by medicaments (including veterinary medicaments) that surged 5.8% as well as imports of weapons and ammunition (9.7%).

The import decline of consumer goods was also accompanied by export contractions, hence driving down demand for imports of raw materials. Price corrections increasingly impeded raw material imports, dropping 12.3%. The decrease predominantly affected imports of livestock feed (17.0%), automotive components and equipment (15.9%), hydrocarbons, halogenates and sulphonates (24.4%) as well as other plastics in primary form (17.5%). Imports of electric circuit breakers and connectors prevented a further import decline of raw materials, however, recording positive growth of 4.8%.

The 15.6% decline in imports of capital goods was due to weaker demand in line with less investment activities. Prices actually increased by 12.5%, which prevented further declines of capital goods imports. The main contributors to the decline were telecommunications equipment and parts (29.2%), automatic data processing machinery and parts thereof (6.2%) as well as other specialised machinery for specific industries (9.2%). The pace of decline, however, was curbed by positive import growth of heating and cooling equipment (13.2%).

Oil and Gas Trade Balance

The oil and gas trade balance recorded a deficit totalling USD6.5 billion in 2015, improving on the USD11.8 billion deficit posted in 2014. The gains were mainly supported by a narrower oil deficit stemming from a deeper oil import

Table 4.10. Indonesian Export of Organic Chemical Products to Major Destination Countries

Items	Share 2014 (%)*	Share 2015 (%)**	Growth (%, yoy)							
			2014*				2015**			
			I	II	III	IV	I*	II*	III*	IV**
China	25.4	18.7	107.9	26.7	-9.5	-48.9	-62.6	-50.4	-41.4	-35.2
Netherlands	7.0	10.5	48.2	59.2	60.1	10.4	12.8	3.1	-20.8	19.3
Japan	6.0	7.9	-28.8	-8.1	-47.8	7.0	0.4	-22.8	4.3	-18.0
India	7.2	7.9	99.4	139.1	31.2	4.2	-20.6	-18.2	-40.2	-18.0
United States of America	6.6	7.4	13.4	78.3	3.0	-10.5	-16.2	-35.7	-26.2	-12.1

* preliminary figure
** very preliminary figure

contraction than export contraction. Therefore, the oil trade deficit narrowed 45.1% from USD23.9 billion to USD13.1 billion over the same period. The global oil price tumbled throughout 2015 due to oversupply from OPEC and non-OPEC countries, which was a salient factor of lower oil exports. Oil exports halved from USD13.8 billion in 2014 to USD7.8 billion in 2015. Nonetheless, oil export volume actually increased from 142.7 million barrels in 2014 to 155.7 million in 2015 as oil lifting surged from 788 thousand barrels per day to 791 thousand barrels per day respectively. In addition, weaker domestic demand for fuel provided the opportunity for a greater oil export growth.

Low international oil prices dragged the imported oil price down 42.1%. Consequently, oil imports fell sharply from USD37.7 billion in 2014 to USD20.9 billion in 2015. In addition to price corrections, fewer oil imports were also the result of a decline in import volume from 356.7 million barrels to 345.6 million barrels over the same period in line with less domestic fuel consumption stemming from economic moderation and government energy reforms. The energy reform policy applied by the government since the end of 2014 drove up fuel prices and reduced consumption, thereby narrowing the oil trade deficit.

The gas trade balance remained positive, recording a surplus of USD6.6 billion in 2015, down from USD12.1 billion the year earlier. The narrower surplus was ascribed to a deeper contraction of gas exports than imports. The 42.5% decline in gas exports was due to lower gas export prices in line with the sliding global oil price. Meanwhile, gas imports fell by 32.2% in 2015 on price factors, contrasting the increase in gas consumption that was met by greater gas lifting.

Services Account, Primary Income Account, and Secondary Income Account

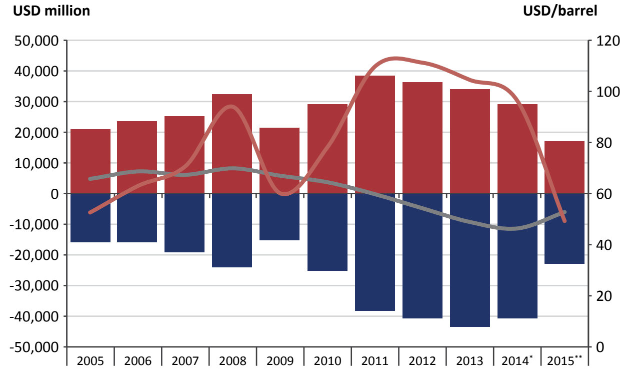
The services account performed better in 2015, recording a narrower deficit and thus supporting gains in the current account. The services account deficit reduced 15.1% on the previous year due to a smaller transportation services deficit, specifically freight, consistent with fewer imports

Table 4.11. Market Share of Organic Chemical Product Exporters in China

Country by Origin	China Market		
	Share (%)		
	2009	2014	Δ
South Korea	21.6	22.9	1.3 ↑
Japan	17.4	13.7	-3.6 ↓
Saudi Arabia	7.5	9.7	2.2 ↑
Unites States of America	6.9	6.2	-0.7 ↓
Singapore	2.6	5.1	2.5 ↑
Thailand	3.3	4.1	0.8 ↑
Indonesia	**1.8**	**2.7**	**0.9 ↑**
Malaysia	2.1	2.3	0.2 ↑
Iran	2.3	2.3	0.0 ↓
Germany	2.5	2.0	-0.5 ↓

Source: UN Comtrade

Chart 4.4. Development of Oil and Gas Trade Balance and Oil Prices



* preliminary figure
** very preliminary figure
Oil and Gas Export
Oil and Gas Import
Oil and Gas Trade Balance
Crude Oil Prices (rhs)

Chart 4.5. Services Account Development

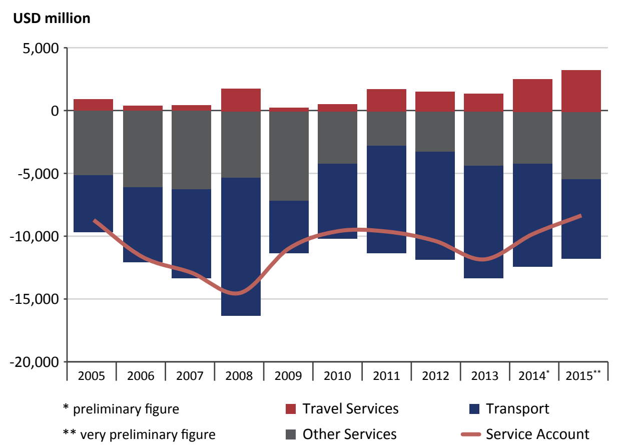
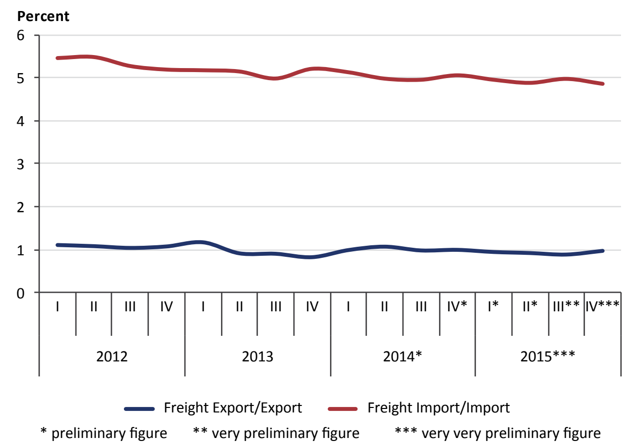


Chart 4.6. Freight Transportation Ratios



of goods (Chart 4.5). In addition, the services account was further bolstered by travel services receipts, which enjoyed a bump as visits by international travellers increased.

Government-led structural reform policy in the maritime sector still requires further honing in order to overcome the persistent services deficit, particularly freight services. The large and persistent deficit is symptomatic of extremely limited sea freight services using domestic vessels. Such conditions were further corroborated by the freight import to import ratio at around 5%, while the freight export to export ratio stood at just 1% (Chart 4.6).

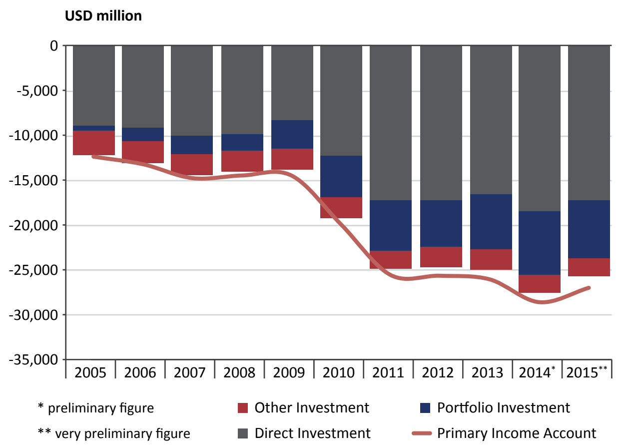
In terms of services, Indonesia remains an attractive tourist destination. Tourist visitors to the archipelago increased from 9.5 million in 2014 to 9.7 million in 2015. The increase, however, was not accompanied by a commensurate rise in tourist spending while visiting Indonesia due to U.S. dollar appreciation against the rupiah. Most foreign travellers visiting Indonesia originated from Singapore, Australia, Malaysia, Japan, and China, with Bali, Jakarta, and Batam cited as the favourite destinations. Consequently, travel services receipts in 2015 increased from USD10.3 billion the year earlier to USD10.7 billion.

Table 4.12. Non-Oil and Gas Imports by Groups of Goods

Items	Annual Growth (%, yoy)									
	2014*					2015**				
	I	II	III	IV	Total	I*	II*	III*	IV**	Total**
A. Consumption Goods										
Nominal	4.8	-8.8	-7.6	-10.3	-6.1	-8.8	-9.3	-14.9	-6.3	-9.9
Real	-2.6	-17.6	-14.5	-13.7	-13.1	-7.7	-7.1	-13.0	-6.1	-8.1
Price Index	7.6	10.7	8.0	3.9	8.1	-1.2	-2.4	-2.2	-0.3	-1.9
B. Raw Materials										
Nominal	-6.2	-4.8	-0.8	-1.7	-3.4	-1.7	-15.2	-17.7	-13.8	-12.3
Real	-1.7	-2.2	0.3	2.9	-0.8	5.2	-8.0	-10.3	-6.4	-4.4
Price Index	-4.7	-2.6	-1.0	-4.5	-2.7	-6.6	-7.9	-8.3	-8.0	-8.3
C. Capital Goods										
Nominal	-7.1	-0.8	-7.1	-4.0	-4.7	-8.7	-21.7	-20.6	-10.9	-15.6
Real	-17.7	-11.0	-19.8	-19.0	-15.5	-21.5	-32.8	-29.2	-15.7	-26.3
Price Index	12.8	11.6	15.8	18.5	12.8	16.3	16.5	12.2	5.7	14.5
Total										
Nominal	-5.6	-4.2	-2.9	-3.1	-3.9	-3.9	-16.3	-17.4	-11.4	-12.4
Real	-6.1	-6.9	-7.6	-6.3	-6.6	-4.7	-16.4	-16.4	-9.1	-11.9
Price Index	0.6	3.0	5.1	3.4	2.8	0.8	0.2	-1.1	-2.5	-0.5

* preliminary figure
** very preliminary figure

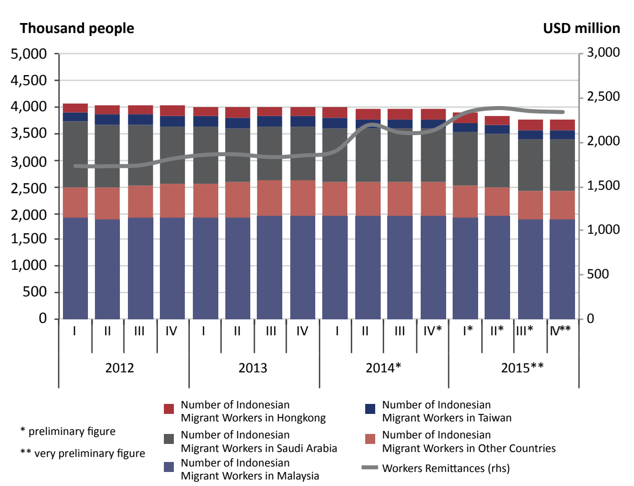
Chart 4.7. Development of Primary Income Account



The primary income account also improved, with the deficit narrowing from USD29.7 billion in 2014 to USD28.0 billion (Chart 4.7). The narrower deficit stemmed from a decline in the position of Foreign Financial Liabilities (FFL) as less non-resident investment entered Indonesia. Accordingly, a lower attribution of direct investment income was recorded in line with less direct investment activity in 2015. Further gains in the primary income account were stifled by an increase in interest payments on government bonds, consistent with the larger position of public portfolio investment liabilities.

Current account performance was also bolstered by a growing secondary income account surplus. In 2015, the secondary income account surplus stood at USD5.5 billion, up from USD5.2 billion the year earlier (Chart 4.8). An increase in remittances from Indonesian migrant workers

Chart 4.8. Number of Indonesian Migrant Workers and Worker's Remittance



(TKI) placed abroad from USD8.3 billion to USD9.4 billion shored up the secondary income account surplus due to a rise in the average TKI wage in a number of placement countries, including Hong Kong, South Korea, Taiwan, and Malaysia, despite a decline in the actual number of Indonesian migrant workers (TKI) from 3.9 to 3.7 million.

4.2. CAPITAL AND FINANCIAL ACCOUNT

Global economic moderation, uncertainty in global financial markets, and the domestic economic slowdown placed pressures on capital and financial account performance. Notwithstanding, the economic rebound late in the year served to boost the capital and financial account surplus significantly in 2015. Bureaucratic reforms and efforts to improve the investment climate garnered domestic investment. Positive domestic economic growth that even accelerated in the final quarter of 2015 successfully restored non-resident investor confidence in Indonesia and boosted direct investment. Growing uncertainty in global financial markets due to ambiguity surrounding the timing and magnitude of the proposed Federal Funds Rate (FFR) hike combined with yuan depreciation as China's economy slowed eroded non-resident capital inflows into portfolio investment instruments through to the third quarter of 2015. Nonetheless, the easing of FFR hike uncertainty, the momentum of domestic economy growth recovery in the second semester of 2015, and attractive investment returns reignited non-resident capital inflows to portfolio investment instruments in the fourth quarter of 2015. Furthermore, other investments, which experienced a deficit due to a deluge of capital outflow from the private sector in the first half of the year, recorded a surplus again in the second semester, thereby reducing a deeper deficit for the year in general. The net liability of non-resident investment in Indonesia in 2015 decreased in line with the smaller capital and financial account surplus. Such conditions were reflected in the declining net liability of Indonesia's International Investment Position (IIP).

Direct Investment

Non-resident direct investment (on the liabilities side) recorded a net inflow of USD18.7 billion as non-residents remained upbeat concerning the domestic economic outlook. Non-resident capital inflows to long-term investments were corroborated in the Business Survey conducted by Bank Indonesia in 2015, which indicated expansive domestic business activity throughout the year. Therefore, actual foreign direct investment (FDI) recorded by the Indonesia Investment Coordinating Board (BKPM) increased 17.8% on the previous year. Nonetheless, relatively strong spillover pressures from global and domestic economic moderation reduced capital inflows on the previous year, totalling USD26.0 billion.

On the assets side, growing uncertainty in global financial markets, along with the global economic downswing, reduced resident investments abroad. In 2015, direct investment on the assets side fell from USD10.4 billion to USD9.4 billion, primarily affecting equity capital, while investments in debt instruments continued to rise. Consequently, direct investments in 2015 recorded a net surplus totalling USD9.3 billion, down from USD14.8 billion the year earlier. Congruously, the net liability of direct investments in Indonesia's International Investment Position (IIP) also declined from USD202.4 billion in 2014 to USD194.7 billion.

Based on country of origin, most foreign direct investment (FDI) flowed from Singapore, followed by Japan (Chart 4.9). The value of investment from the two countries amounted to USD12.1 billion in 2015, representing 84.2% of total FDI. On the other hand, ASEAN member countries were remain leading investors in Indonesia with a share of 61.3% of foreign direct investment (FDI), totalling USD8.8 billion.

By economic sector, the actual FDI in 2015 was concentrated in the manufacturing industry as well as the agricultural, fisheries, and forestry sector (Chart 4.10). The value of investment in the manufacturing industry was recorded at USD3.7 billion, with Singapore and Japan as the main investors. The agricultural, fisheries, and forestry sector, which has historically not been a favoured investment destination, followed a growing investment

Chart 4.9. **Foreign Direct Investment by Major Investor Countries**

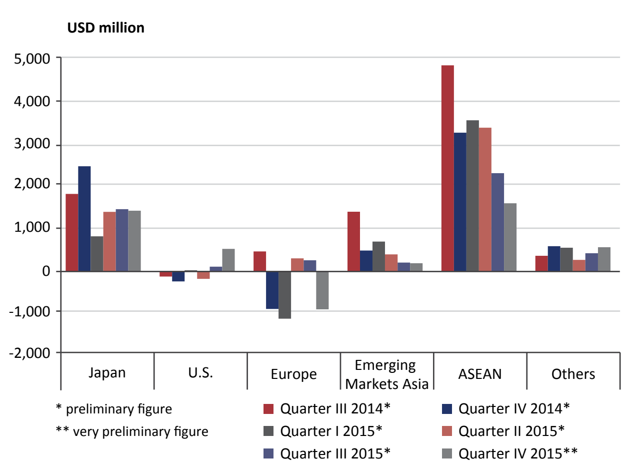
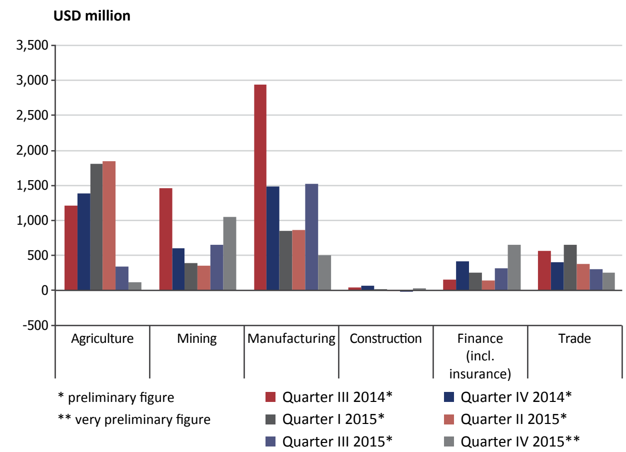


Chart 4.10. **Foreign Direct Investment by Economic Sectors**



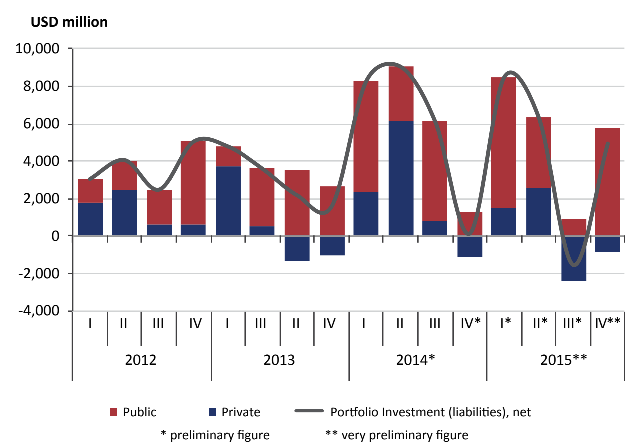
trend from 2013 to 2015. The value of investment in this sector totalled USD4.6 billion in 2015, with Singapore noted as the leading investor.

Based on distribution, Indonesia Investment Coordinating Board (BKPM) data shows that foreign direct investment (FDI) in 2015 was more equitably spread throughout the archipelago. The share of such investment outside of Java increased from 43.1% in 2014 to 45.6%, concentrated in East Kalimantan, West Kalimantan, North Sumatra, and Central Sulawesi. Based on economic corridor, however, most FDI outside of Java found its way to Kalimantan, Sumatra, Sulawesi, Maluku, Papua as well as Bali and Nusa Tenggara.

Portfolio Investment

Non-resident portfolio investment in Indonesia still recorded a surplus in 2015, totalling USD17.7 billion, for which the position gained momentum in the fourth quarter of 2015 (Chart 4.11). The surplus was, however, still lower than that recorded in the previous year, standing at USD23.5 billion. Global economic developments, including the global economic slowdown and potential speculation on the proposed FFR hike along with escalating global financial risks after the People's Bank of China (PBoC) devalued the yuan, precipitated more prudent investment activity in developing countries. Nevertheless, attractive returns and the favourable perception of non-resident investors in the economic outlook of Indonesia, coupled with stronger growth in the fourth quarter of 2015, boosted global investor interest in Indonesia towards the end of year. On the assets side, resident portfolio investments abroad recorded a deficit of USD1.0

Chart 4.11. **Foreign Portfolio Investment in Indonesia**



billion, consistent with the net buy of foreign portfolio instruments by residents.

Rupiah denominated portfolio instruments were the main contributor to portfolio investment inflows. Although lower than the previous year, non-resident inflows to rupiah government bonds (SUN) recorded a net inflow of USD7.7 billion. Meanwhile, foreign capital recorded a net outflow from Bank Indonesia Certificates (SBI) totalling USD0.1 billion, which was relatively unchanged from the previous year. Congruently, the position of non-resident rupiah SUN holdings surged from 41.6% at the end of 2014 to 42.9 at the end of 2015, while the position of non-resident SBI holdings fell from 2.1% to 0.0% over the same period. On the stock market, growing uncertainty in global financial markets over the FFR hike issue, which peaked in the third quarter of 2015, compelled non-resident investors to sell shares. Nonetheless, the net sell of shares by non-residents began to ease in the fourth quarter. Consequently, a net sell of just USD1.5 billion was reported for 2015 in general.

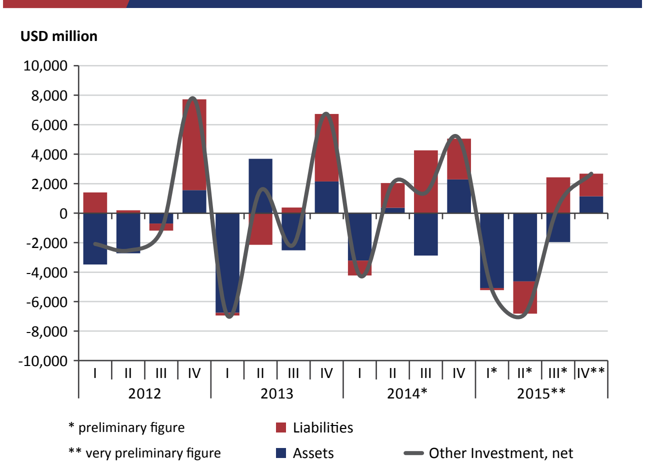
On the other hand, non-resident investors also expanded holdings of long-term government debt securities, including global bonds and sukuk. In 2015, the government issued global bonds to the tune of USD8.9 billion, consisting of global bonds (USD7.5 billion), euro bonds (€1.25 billion) in July 2015 and Samurai bonds (¥100 billion) in August 2015. In addition, the government also issued global Islamic bonds (sukuk) totalling USD2 billion in May 2015. Consequently, the net liability position of portfolio investment in Indonesia's International Investment Position (IIP) in 2015 totalled USD189.4 billion, down from USD192.7 billion the year earlier.

Other Investments

Other investment transactions experienced pressures in the first semester of 2015, when a significant deficit was recorded. In 2015, other investments posted a deficit of USD8.9 billion, contrasting the USD4.3 billion surplus registered in the previous year (Chart 4.12). The deficit primarily stemmed from a deficit of other Indonesian investments abroad (assets side), which expanded considerably from USD3.4 billion in 2014 to USD10.5 billion. Furthermore, the deficit was also contributed by a decline in the other investments surplus of non-residents in Indonesia (liabilities side) from USD7.7 billion to USD1.6 billion. Nonetheless, the other investments surplus began to recover in the third quarter and subsequently gained momentum in the fourth quarter on the assets and liabilities sides. Against this background, a deeper deficit of other investment transactions was avoided and the net liability of other investments in Indonesia's International Investment Position (IIP) fell from USD111.3 billion in 2014 to USD102.7 billion in 2015.

By institutional sector, the private sector contributed USD8.4 billion to the other investment deficit in 2015, reversing the USD8.5 billion surplus recorded the year earlier. The private sector deficit was primarily attributable to a larger deficit of resident asset placements abroad, which more than tripled from USD3.4 billion in 2014 to USD10.5 billion, mainly in the form of private sector deposits held at banks abroad. In addition to the increase in assets, the private sector other investment deficit also stemmed from a significantly smaller surplus on the liabilities side, decreasing from USD11.9 billion to USD2.1 billion as less non-affiliate private external debt was withdrawn in line with domestic economic moderation.

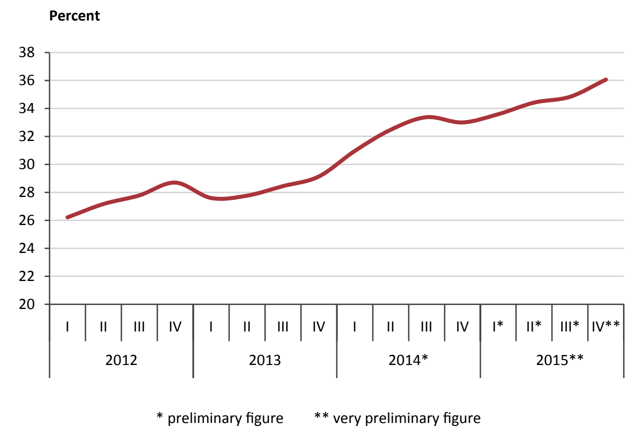
Chart 4.12. **Development of Other Investment**



Furthermore, a decline in non-resident deposits held at domestic banks also eroded the surplus on the liabilities side.

A deeper other investment deficit was avoided by corresponding improvements in the public sector. Accordingly, other investments of the public sector in 2015 recorded a deficit of USD0.5 billion, improving from a deficit of USD4.2 billion the year earlier. The improvement came from an increase in withdrawals of foreign loans by the government to offset the fiscal deficit. Withdrawals of foreign loans by the government increased from USD4.0 billion to USD4.8 billion, the majority of which was in the form of program loans. Meanwhile, government external debt repayments actually decreased slightly from USD5.3 billion to USD4.9 billion in 2015.

Chart 4.13. Ratio of External Debt to GDP



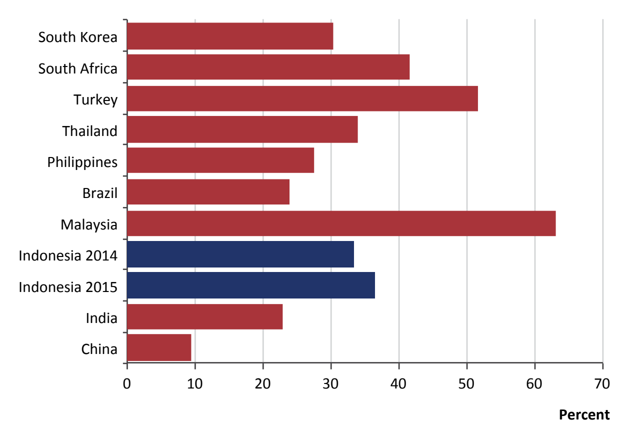
External Debt

Based on the original maturity profile, the external debt in Indonesia increased during 2015 due to long-term external debt in both the private and public sectors. Conversely, the position of short-term external debt declined in the private and public sectors as the domestic economy cooled. The structure of external debt was sound, with long-term debt dominating short-term debt in both the private and public sectors. In general, the external debt increased from USD293.8 billion in 2014 to USD310.7 billion. Congruous with the increase of external debt accompanied by slower GDP growth, the ratio of external debt to GDP was observed to rise from 33.0% to 36.1% over the same period but remained relatively sound and comparable to other peer group countries (Chart 4.13 and Chart 4.14). In addition, Indonesia's external debt growth slowed from 10.4% in 2014 to just 5.8% in 2015 due to the domestic economic slowdown.

The private sector continued to dominate external debt in 2015 with a share of 54.0% of the total, the majority of which was long-term (72.5% of total private external debt). The private external debt at the end of 2015 was USD167.7 billion, up from USD164.0 billion the year earlier due to an increase in long-term debt. Growth of private external debt slowed significantly, however, from 15.1% in 2014 to 2.2% due to fewer loan agreements and debt securities as the need for funding eased in line with economic moderation.

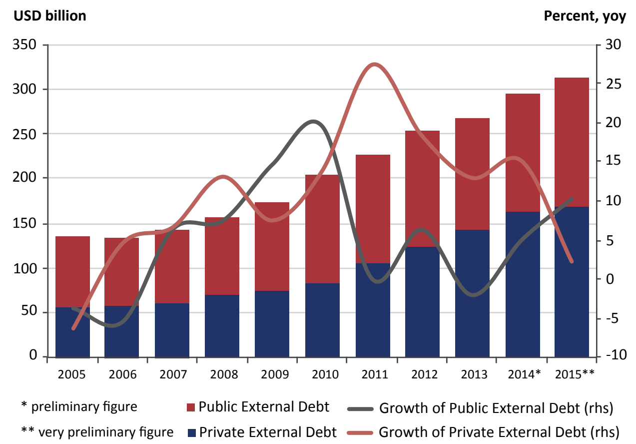
Conversely, the growth of public external debt, accounting for 46.0% of the total, accelerated from 5.0% in 2014 to 10.2% due to an increase in long-term debt (93.4% of total public external debt) as the Government sought to accelerate economic development. Congruently, the position of public external debt increased from USD129.7 billion in 2014 to USD143.0 billion (Chart 4.15). The increase stemmed primarily from larger non-resident holdings of government bonds as the deluge of foreign capital inflows in the form of portfolio investment were maintained and the government issued more global bonds and sukuk. The government external debt in the form of government bonds surged 19.5% on the previous year. Meanwhile, the need to fund the state budget deficit and infrastructure projects compelled the government to withdraw more foreign loans than in 2014. Consequently, public external debt in the form of loan agreements experienced a moderate 0.6% bump on the previous year from USD53.9 billion to USD54.2 billion.

Chart 4.14. Ratio of External Debt to GDP of Peer Group Countries



Source: World Bank (2014)

Chart 4.15. **External Debt Growth by Group of Borrowers**



Based on the remaining maturity profile, slower growth of external debt was caused by weaker growth of long-term external debt coupled with a decline in the short-term external debt (Chart 4.16). Growth of long-term external debt at the end of 2015 decelerated from 11.8% to 8.8%, while growth of short-term external debt contracted by 6.3%, reversing the positive 5.3% recorded in 2014. Consequently, the structure of external debt in Indonesia was considered heathier as long-term debt became more dominant in both the private and public sectors. The ratio of short to long-term external debt improved in 2015 from 25.3% the year earlier to 21.8%. Based on the group of borrowers, both the private and public sectors contributed to gains in the ratio. In terms of the public sector, the ratio of short to long-term external debt improved from 8.7% to 7.0%, while in the private sector the ratio improved from 42.5% to 38.0%.

Based on the risk profile, long-term external debt with a lower risk profile tended to dominate the private external debt. Furthermore, the outstanding of private external debt originating from affiliates was also fairly dominant, which is generally considered safer because the loan originates from a parent company, thereby guaranteeing the debt. In December 2015, the outstanding of long-term private external debt amounted for 77.7% of the total private external debt. Private external debt originating from an affiliate (short and long-term) stood at USD50.1 billion in 2015, accounting for 33.7% of the total.

The largest private external debt risk profile was associated with short-term non-affiliate nonbank debt but the portion of such debt in 2015 remained relatively small. In December 2015, the position of short-term non-affiliate nonbank corporate external debt stood at USD16.4 billion, accounting for just 9.8% of total private external debt and only 5.3% of total external debt (Chart 4.17). To mitigate the various risks linked to (nonbank corporation) external debt, including currency risk, liquidity risk, and overleverage risk, Bank Indonesia issued Bank Indonesia Regulation (PBI) No. 16/21/PBI/2014 concerning the Implementation of Prudential Principles in Managing External Debt of Nonbank Corporation. Furthermore, to monitor implementation, Bank Indonesia also subsequently released Bank Indonesia Regulation (PBI) No. 16/22/PBI/2014 regarding the Reporting of Foreign Exchange Flows and Reporting the Implementation of Prudential Principles in Managing External Debt Nonbank Corporation. Consequently, every indebted nonbank corporation with foreign loans operating in Indonesia is required to hedge at a certain ratio. Such corporations are also required to maintain adequate foreign currency assets to cover their corresponding maturing foreign currency

Chart 4.16. **External Debt Position by Remaining Maturity**

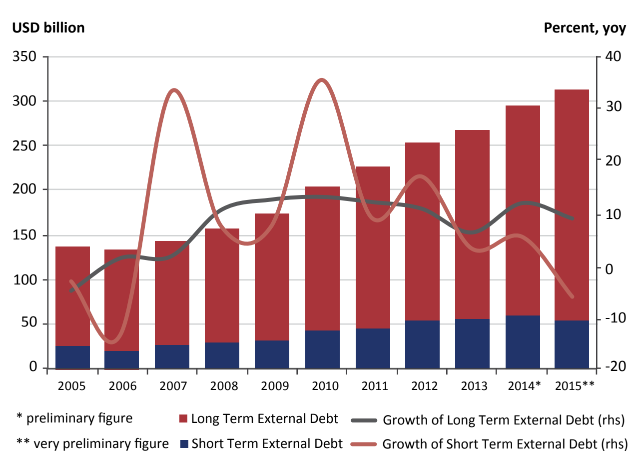
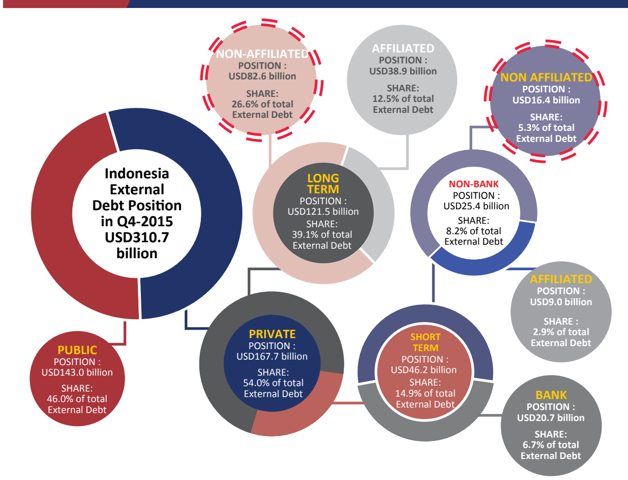


Chart 4.17. **Composition of Indonesia External Debt ***



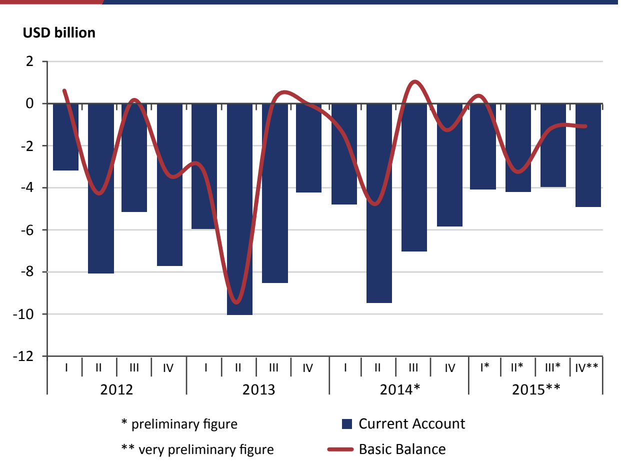
*External Debt Position by Remaining Maturity liabilities at a specific ratio, while meeting minimum rating requirements pursuant to prevailing regulations. As of the end of 2015, the implementation of the Bank Indonesia Regulation (PBI) showed an improvement on the nonbank corporations application of prudential principles, thereby successfully mitigating the risks associated with the external debt.[2]

4.3. EXTERNAL SUSTAINABILITY

In general, external sustainability indicators were sound in 2015. Sources of long-term financing to manage the current account deficit improved in line with the capital and financial account surplus as well as a smaller current account deficit. Consequently, the basic balance (Chart 4.18), which deteriorated in the second quarter of 2015, rebounded in the final two periods of the year.

In terms of solvency, a smaller portion of net liabilities in Indonesia's International Investment Position (IIP) to GDP evidenced gains. Other solvency indicators, however, demonstrated mounting pressures on external sector performance in Indonesia compared to the year earlier, albeit remaining at normal levels, due to domestic economic moderation combined with a decline in sources of foreign exchange receipts in the current account on the balance of payments to service external debt through to the third quarter of 2015. External sector pressures also originated from declining non-debt creating inflows as a relatively secure source of financing. After the economy rebounded in the third quarter of 2015, several solvency indicators also started to recover at the end of the year.

Chart 4.18. BOP Basic Balance



Regarding liquidity, external pressures on Indonesia's economy remained at normal levels. At the end of 2015, the amount of official reserve assets stood at USD105.9 billion, falling from USD111.9 billion the year earlier. Nonetheless, recent trends in the fourth quarter of 2015 indicated incremental growth in the position of foreign exchange reserves in line with accelerating domestic economic growth (Table 4.14). In addition, the position of reserve assets was equivalent to 7.7 months of imports or 7.4 months of imports and servicing short-term government external debt, which is well above international adequacy standards of three months (Chart 4.19). Moreover, the capacity of the reserve assets to meet the monetary system requirements of the domestic private sector was also relatively sound, reflected on a stable ratio of reserve assets to money supply. The increase in the position of foreign exchange reserves, coupled with the decline of short-term external debt, in the fourth quarter of 2015 boosted liquidity indicators towards the end of the year.

The Tier 1 Debt Service Ratio (DSR) (World Bank methodology) remained within norms in 2015 despite jumping from 23.1% to 29.1%.[3] The increase primarily stemmed from fewer current account receipts in 2015. In order to follow prudential principles, Bank Indonesia also used a more conservative methodology to calculate the Tier 2 Debt Service Ratio (DSR) by including trade credit to non-residents.[4] Based on risk, trade credit, which accounts for a relatively large share in the calculation of Tier 2 DSR, has a comparatively low risk profile. When calculated using the aforementioned methodology, Tier 2 DSR in 2015 exceeded Tier 1 DSR, increasing from 51.7% the year earlier to 61.7%. The private sector contributed to the increase in the debt service ratio (DSR) (Chart 4.20). Prudential principles were applied in conjunction with efforts to mitigate the risk of private sector default through constant monitoring of PBI implementation concerning the Implementation of Prudential Principles in Managing External Debt of Nonbank Corporation.

2 An in-depth discussion is presented in Box 4.1.

3 The Tier 1 Debt Service Ratio (DSR) represents a calculation methodology of the World Bank. Accordingly, Tier 1 DSR is the ratio of total external debt repayments (principal and interest) to current account receipts, where total external debt repayments include long-term external debt principal payments and total long and short-term external debt interest payments.

4 The Tier 2 Debt Service Ratio (DSR) is a calculation methodology of the World Bank that includes short-term loans and trade credit in order to more prudently managing external debt. The Tier 2 Debt Service Ratio (DSR) is defined as the ratio of total external debt repayments (principal and interest) to current account receipts, where total external debt repayments include external debt principal and interest payments in the form of direct investments, excluding those from subsidiaries operating internationally, as well as loans and trade credit to non-affiliates.

Table 4.13. External Solvency Indicators

Indicator		Description	2010	2011	2012	2013	2014*	2015**
Solvency Ratio								
1.	Indonesia's Net IIP / GDP	The ratio used to measure share of IIP to whole domestic economy	38.2	35.3	36.4	35.9	44.3	44.2
2.	External Debt / GDP	The ratio of external debt role to finance domestic economy	26.5	25.0	27.4	29.1	33.0	36.1
3.	External Debt / Goods and Services Exports	The ratio used to measure share of external debt to income from goods and services exports.	121.5	105.8	119.6	129.8	147.8	182.5
4.	Net External Debt[1)] / Current Account Receipts[2)]	The ratio used to measure capability of current account income in servicing external debt net.	35.5	31.2	36.8	49.6	57.2	71.7
5.	Net Direct Investment Liabilities / GDP	The ratio used to measure direct investment role to domestic economy	22.7	22.1	21.5	21.9	26.9	27.5
6.	Non-debt creating inflow / GDP	The ratio used to measure non-debt capital inflows role to domestic economy finance	34.4	32.0	32.5	30.4	38.4	37.3

[1)] Total of Goods and Services Exports Income and primary and secondary income
[2)] The difference between the debt component on KFLN side and AFLM side in IIP Indonesia
* preliminary figure
** very preliminary figure

Therefore, to ensure the optimal contribution of nonbank corporations to the economy without triggering domestic economic instability, nonbank corporations are now required to: (i) mitigate risks associated with external debt activities; and (ii) pay due regards to general business management practices.

Table 4.14. External Liquidity Indicators

Indicator		Description	2010	2011	2012	2013	2014*	2015**
Liquidity Ratio								
1.	Foreign Exchange Reserves / Imports of Goods and Services	Indicators used for measuring the adequacy of foreign exchange reserves in servicing the needs of goods and services imports	66.2	58.3	53.0	47.0	55.4	64.0
2.	Foreign Exchange Reserves / Broad Money (M2)	Indicators used to measure the potential impact of the decline in confidence against domestic currency	35.4	33.3	31.9	27.8	31.8	31.2
3.	Foreign Exchange Reserves / Short-Term Foreign Debt (remaining maturity)	Indicators used for measuring the adequacy of foreign exchange reserves in servicing short-term foreign debt based on remaining time period	224.2	235.5	206.4	176.6	188.8	190.7

* preliminary figure
** very preliminary figure

Chart 4.19. Foreign Exchange Reserves Development

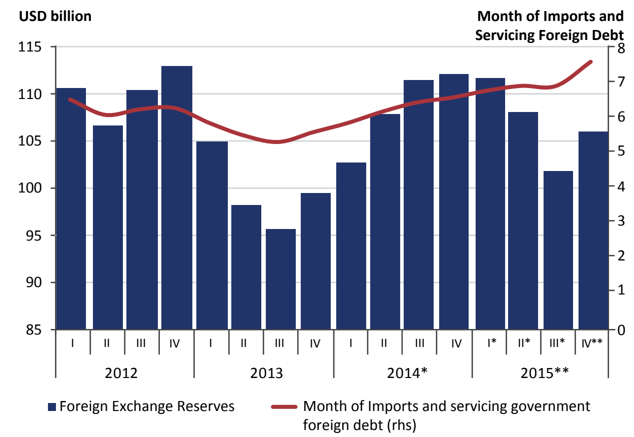


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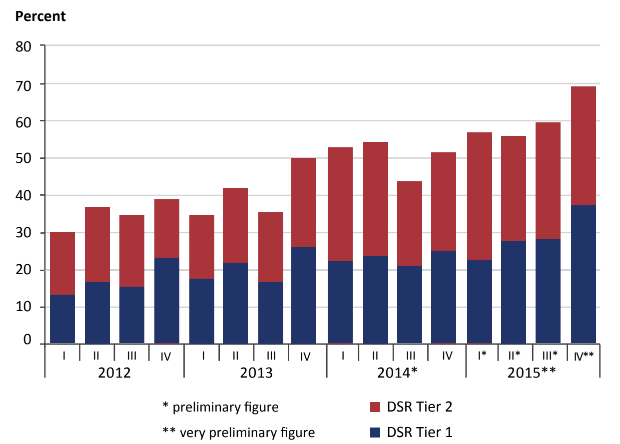
Chart 4.20. Indonesia's Debt Service Ratio



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Box 4.1 Assessment on the Implementation of Prudential Principles in Managing External Debt of Nonbank Corporation

The application of prudential principles (KPPK) involves nonbank corporation activity to mitigate currency risk, liquidity risk, and overleverage risk linked to the external debt held. Such activities are regulated pursuant to Bank Indonesia Regulation (PBI) No. 16/21/PBI/2014 concerning the Implementation of Prudential Principles in Managing External Debt of Nonbank Corporation. According to the regulation, nonbank corporations are required to calculate their foreign currency assets and liabilities from period 0 up to three months and from three months to six months from the end of the reporting quarter. In 2015, therefore, nonbank corporations were required to apply prudential principles based on an assessment of foreign currency assets and liabilities for the two aforementioned periods, by maintaining:

1. A minimum hedging ratio of 20% of the difference between foreign currency assets and foreign currency liabilities that will mature within three months and from three to six months after the end of the reporting quarter. The minimum hedging ratio must be met by all nonbank corporations with a value of foreign currency assets below the value of foreign currency liabilities that will mature within three months and from three to six months after the end of the reporting quarter; and

2. A minimum liquidity ratio of 50%. Therefore, corporations are required to maintain foreign currency assets with a value of at least 50% of the value of foreign currency liabilities that will mature within three months of the reporting quarter.

Nonbank corporations were required to begin submitting a KPPK report to Bank Indonesia in the first quarter of 2015, during the transition period. Thereafter, KPPK reporting became mandatory starting the third quarter of 2015 financial report, with sanctions imposed on those nonbank corporations failing to comply. Meanwhile, sanctions for failure to adhere to the KPPK provisions became effective for foreign currency asset and liability data in the fourth quarter of 2015.

Moving forward, Bank Indonesia will continue to strengthen external debt management in order to provide an optimal contribution to the national economy. Commencing in 2016, the application of prudential principles will require nonbank corporations holding external debt to:

1. Maintain a minimum hedging ratio of 25%;

2. Maintain a minimum liquidity ratio of 70%; and

3. Maintain a minimum credit rating. Nonbank corporations seeking to withdraw foreign currency loans, commencing 1st January 2016, shall be required to comply with a minimum credit rating equivalent to BB- as affirmed by a rating agency approved by Bank Indonesia.

In the following year, on 1st January 2017, hedging transactions in compliance with KPPK shall mandatorily be conducted with banks operating in Indonesia. The policy aims to deepen the domestic foreign exchange market.

An Assessment of KPPK Implementation through to the Third Quarter of 2015

The number of nonbank corporations reporting KPPK has increased in each reporting period. Based on the third quarter of 2015 data, the number of nonbank corporation that held external debt reached 2,543 corporations. Eighty five percent of these corporations had reported their obligation of KPPK, an improvement from 70% in the previous quarter. The corporations' compliance on the KPPK regulation also increased. Regarding the minimum hedging ratio, nonbank corporations hedged 192% of the required value for the upcoming 0-3 months, increasing from 105% in the previous quarter (Chart 1).

Chart 1. Hedging Value to Hedging Liabilities for 0-3 Months Periods

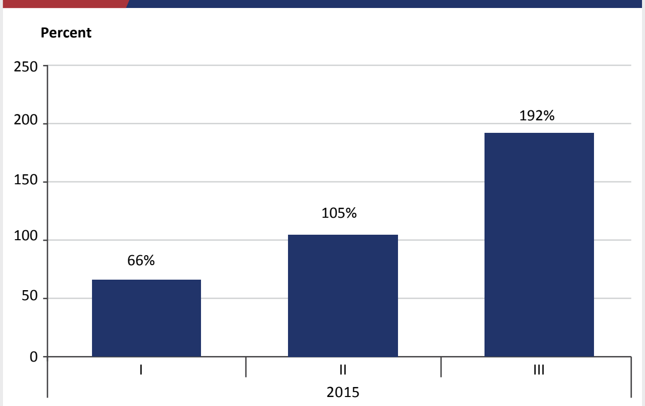


Chart 2. Hedging Value to Hedging Liabilities for 3-6 Months Periods

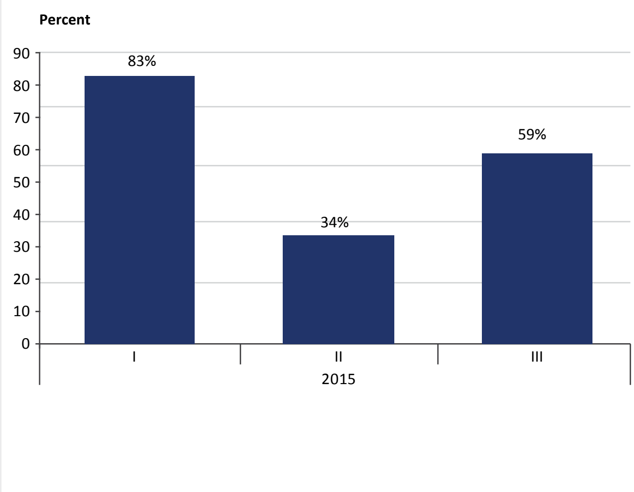
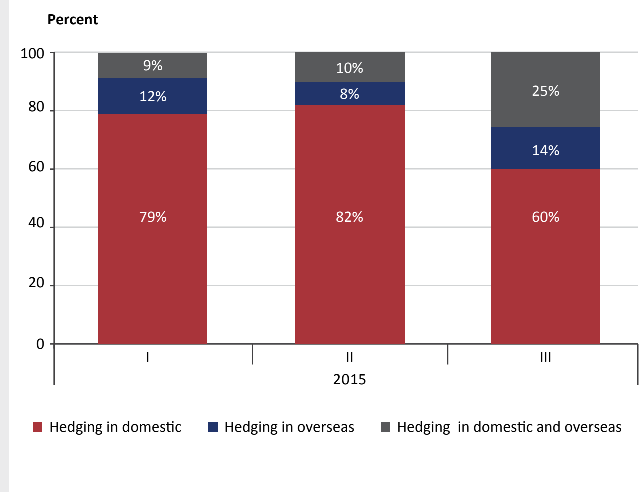


Chart 4. Hedging Distribution for 0-3 Months Periods



In terms of complying with the minimum hedging ratio for the upcoming 3-6 months, nonbank corporations hedged 59% of the total required, up from 34% in the second quarter of 2015 (Chart 2). Concerning the liquidity ratio, 83% of nonbank corporations had successfully complied with the ratio, up from 82% in June 2015 (Chart 3). Greater KPPK compliance was consistent with the number of corporations engaged in hedging activities (Chart 4 and 5), the majority of which was conducted with domestic banks.

KPPK provisions, which became effective in 2015, have been successful in managing foreign currency demand from nonbank corporations, thereby dissipating pressures on the rupiah. In addition, the implementation of prudential principles has increased the proportion of derivative transactions to 35% of total corporate foreign currency transactions, up from 33% in 2014. Looking forward, more derivatives activities by domestic corporations is expected to drive domestic foreign exchange market deepening efforts.

Chart 3. Rapporteurs of Borrowing Activity Based on Prudential Principle According to the Compliance of Liquidity Ratio Fulfillment

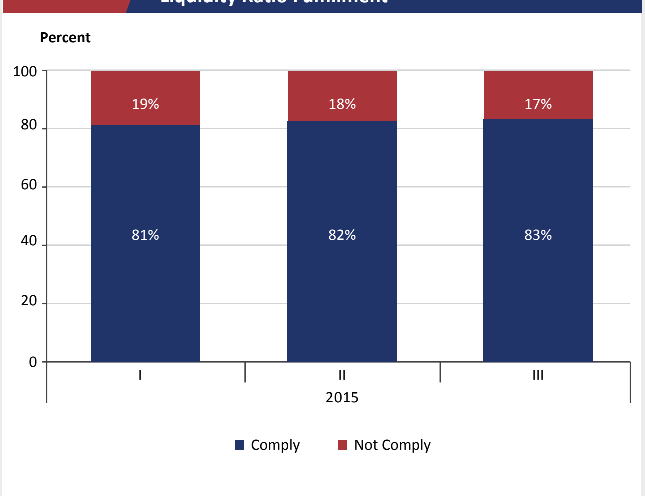
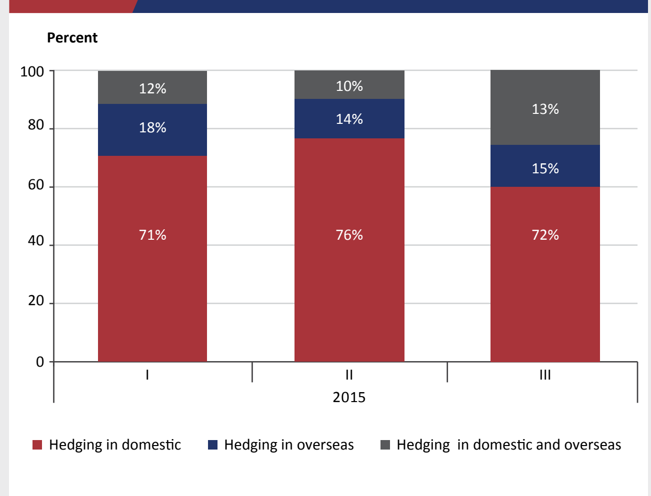
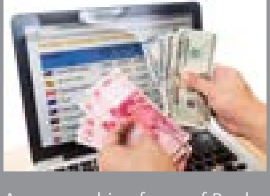


Chart 5. Hedging Distribution for 3-6 Months Periods





An overarching focus of Bank Indonesia's policy mix is to maintain rupiah stability, reflected in its value against other currencies. In 2015, rupiah stability confronted the arduous challenges of domestic and external pressures.

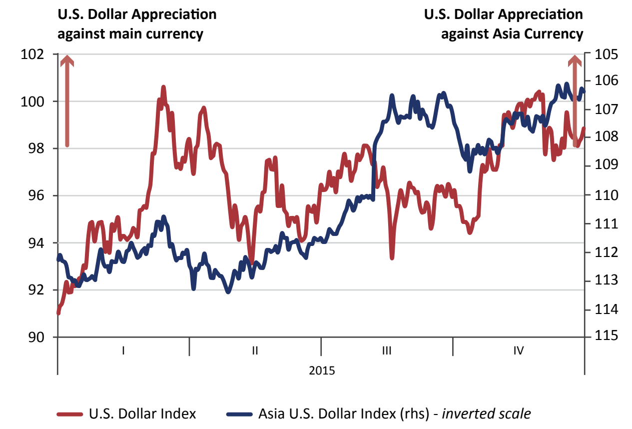
Chapter 5

Exchange Rate

In 2015, the rupiah was subjected to intense depreciatory pressures stemming primarily from external pressures. The main external sources of exchange rate pressures were linked to the U.S. monetary policy normalization, the debt crisis in Greece, yuan devaluation, and the global monetary policy divergence. Meanwhile on the domestic front, pressures originated from the domestic economic slowdown. Depreciatory pressures on the rupiah were prevalent from the first until third quarter of the year, peaking in September 2015. The rupiah subsequently entered a more stable period after Bank Indonesia, the Government, and the Financial Services Authority (OJK) announced a series of stabilization policies and uncertainty eased on global financial markets in relation to the timing of the Federal Funds Rate (FFR) hike.

Rupiah stability encountered a variety of escalating risks throughout 2015, mostly external. Uncertainty surrounding the timing of FFR hike as a part of U.S. monetary policy normalization, the Greek debt crisis, unexpected yuan devaluation, and global monetary policy divergence were cited as the primary external factors affecting the rupiah movement. The ubiquitous uncertainty exacerbated volatility on global financial markets and affected negatively on non-resident capital inflows to financial assets in emerging economies, including Indonesia. Against a backdrop of widespread global uncertainties, rupiah exchange rates were further pressured by domestic economic moderation that had spilled over in part from the global economy. In addition, dwindling Indonesia's exports performance undermined the supply of foreign exchange, thus further compounding rupiah performance.

Chart 5.1. U.S. Dollar Development Index



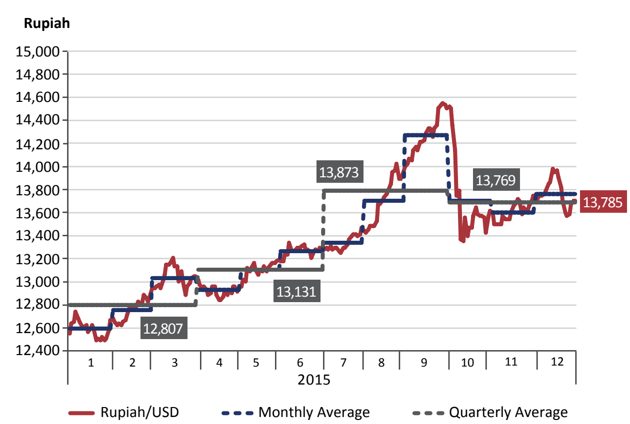
Source: Bloomberg, processed

Intensifying domestic and external risks caused the rupiah depreciation more in 2015 than the year earlier. The rupiah depreciated 10.2% (yoy) in 2015 compared to 1.7% (yoy) in 2014. Furthermore, rupiah volatility increased from 10.2% to 11.1%. Notwithstanding the challenges, a synergy of monetary policy and structural reforms instituted by Bank Indonesia, the Government, and the Financial Services Authority (OJK), primarily from September 2015, helped to stabilize the rupiah through to the end of 2015. In the fourth quarter of 2015, the rupiah finally rebounded against the U.S. dollar as well as the currencies of peer countries.

Exchange rate pressures were also felt in other emerging countries due to intense external risk factors. Pressures in emerging countries were further exacerbated by monetary policy divergence in advanced economy countries that supported USD appreciation. On the one hand, loose monetary policy adopted by the European Central Bank (ECB), People's Bank of China (PBoC), and Bank of Japan (BoJ) led to euro, yuan, and yen depreciation correspondingly. On the other hand, however, the Federal Reserve was seeking to normalize its monetary policy stance. Such monetary policy divergence sparked broad U.S. dollar appreciation against the majority of global currencies. Consequently, the USD index appreciated from 90.3 in 2014 to 98.6 in 2015 (Chart 5.1). Therefore, depreciatory pressures on the currencies of emerging countries against the USD were unavoidable.

Rupiah depreciation loomed large from the first until the third quarter of 2015, before entering a more stable period in the final quarter of the year. Depreciatory pressures on the rupiah surfaced in the third week of January 2015 with rupiah volatility recorded at 10.5% in the first quarter of 2015, which subsequently eased to 5.7% in the following quarter. External shocks intensified, however, in the third quarter, primarily attributable to unexpected yuan devaluation by PBoC and uncertainty over the proposed FFR hike in the U.S., which pushed the rupiah to its lowest level (Rp14,698 per USD) (Chart 5.2). PBoC devalued the yuan in order to liberalize its exchange rate framework to be more market determined. The move came at a time of economic moderation, however, coupled with economic rebalancing to strengthen domestic consumption, which prompted uncertainty concerning the direction of economic policy in China. Furthermore, the turmoil in China occurred during an episode of widespread uncertainty surrounding the timing and magnitude of U.S. monetary policy normalization, thereby amplifying pressures on financial markets and exchange rates.

Chart 5.2. Rupiah Exchange Rate



As a response to mounting exchange rate pressure in the third quarter of 2015, Bank Indonesia, the Government, and OJK released a series of synergic stabilization policies, encompassing structural reforms, prudent monetary policy, various exchange rate stabilization measures, domestic foreign exchange market structure strengthening, and a series of economic policy packages.[1] The stabilization measures introduced by Bank Indonesia followed three strategic pillars. In this context, Bank Indonesia strived to maintain currency stability through measured intervention on the foreign exchange market, while maintaining the adequacy of reserve assets, and also improved regulations concerning foreign currency transactions against the rupiah. In addition, Bank Indonesia strengthened monetary operations to manage liquidity in the banking system and anchored market expectations. Bank Indonesia also monitored domestic foreign exchange market transactions for unusual activity and minimized speculative activity. In terms of financial market deepening, a number of regulations were amended to boost foreign currency supply and minimize speculation.

In the fourth quarter 2015, exchange rate stability returned and foreign capital flowed back into the country as external risk factors eased due to greater clarity regarding the direction of U.S. normalization policy after the FOMC meeting in December 2015. The rupiah stabilized and non-resident capital inflows returned until the end of the year. Non-resident investors had anticipated that the U.S. benchmark rate would rise gradually, thus limiting the impact on the domestic financial market volatility. Foreign investors sought to buy government bonds on rising yields in Indonesia that were more attractive than government bonds in other peer countries, which was further bolstered by rupiah stabilization measures taken by Bank Indonesia, the Government, and OJK as well as the favourable market perception concerning the promising domestic economic outlook.

In 2015, policy synergy successfully controlled rupiah volatility and depreciation compared to conditions in peer countries. The rupiah rebounded in October 2015 as foreign capital flowed back into the country during the fourth quarter. Furthermore, domestic risk factors eased, reflecting an improvement in credit default swaps (CDS) to a level of 230 after sinking to 282 at the end of September 2015. Consequently, rupiah depreciation was more limited (-10.2%) than the Brazilian real (-32.9%), South African rand (-26%), Turkish lira (-20.4%), and Malaysian ringgit (-18.6%). Congruously, the position of official reserve assets in Indonesia fell just USD5.9 billion, or 5.3%, in 2015, a more moderate decrease than observed in other countries such as Malaysia, Turkey, México, South Africa, and Russia that dropped respectively by 19%, 10%, 9%, 8%, and 6%.

5.1. EXCHANGE RATE DYNAMICS

Rupiah exchange rates were particularly dynamic in 2015. On average, the rupiah depreciated 11.3% from Rp11,876 per USD in 2014 to Rp13,392 per USD in 2015, compared to just 1.7% depreciation recorded in 2014. In general, the rupiah followed a depreciating trend from the first three quarters of the year, with depreciatory pressures escalating in the third quarter. Thereafter, however, the rupiah began to stabilize in the fourth quarter of 2015 as uncertainty eased on global financial markets. Non-resident capital subsequently began to flow back into the country and investor expectations in the domestic economic outlook were buoyed by the release of stabilization measures by Bank Indonesia, accompanied by a series of structural policies issued by the Government (Chart 5.3).

During the first two quarters of 2015, rupiah depreciation was kept relatively under control. Accordingly, the rupiah recorded limited depreciation of 5.3% (qtq) in the first quarter of 2015 to a level of Rp13,074 per USD before easing to just 1.9% (qtq) in the subsequent period to a level of Rp13,333 per USD. Exchange rate pressures in the first two quarters of 2015 primarily originated from broad USD appreciation against global currencies. A stronger USD index was consistent with ongoing U.S. economic improvements that strengthened the preconditions required to tighten U.S. monetary policy, additional stimuli introduced by the European Central Bank (ECB), and the deadlocked fiscal negotiations in Greece. Nonetheless, the aforementioned risk factors were thereupon offset by a number of positive domestic and international developments that prevented further rupiah depreciation. On the domestic side, the trade balance recorded a growing surplus and the outlook rating was revised upwards by Standard and Poor's from stable to positive in May 2015. On the external side, a more dovish statement in FOMC June 2015, allaying concerns over the proposed FFR hike by the Federal Reserve.

In the third quarter of 2015, however, pressures intensified on the rupiah, driving the currency down to its lowest ebb in 2015. Pressures predominantly stemmed from external factors due to unexpected yuan devaluation policy in China combined with widespread uncertainty surrounding the

1 A more detailed explanation of the policies instituted to maintain exchange rate stability is presented in Chapter 11.

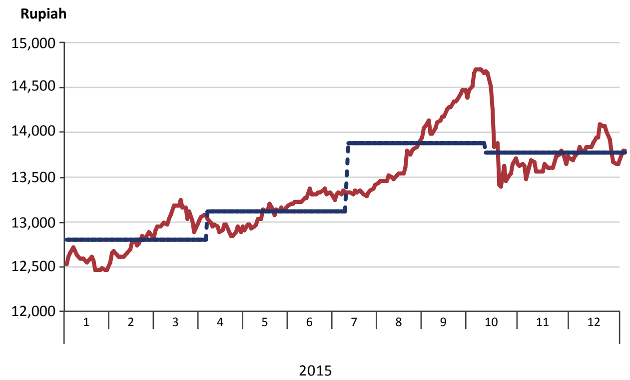
Chart 5.3. **Event Analysis of Rupiah Exchange Rate**

Quarter I 2015
- Average Rp12,807/USD (depreciation 4.4% qtq)
- End-of-Period Rp13,074/USD (depreciation 5.3% qtq)
- Volatility 10.5%

Depreciation pressure increases in line with increasing global uncertainty, among others sourced from: worries increase in the Federal Funds Rate (FFR) which triggers a strengthening U.S. dollar and concerns over the Greek debt negotiations that corrects risk appetite of global investors towards domestic assets.

Quarter II 2015
- Average Rp13,131/USD (depreciation 2.5% qtq)
- End-of-Period Rp.13,333/USD (depreciation 1.9% qtq)
- Volatility 5.7%

Rupiah depreciated by more mild pressure, but still higher than the historical average. A source of pressure comes from the domestic economic slowdown and the continuing strengthening of dollar index (DXY), which is supported by additional QE by the ECB in the middle of high concerns about the plan to increase the FFR by the U.S.



Quarter III 2015
- Average Rp13,873/USD (depreciation 5.3% qtq)
- End-of-Period Rp14,650/USD (depreciation 9% qtq)
- Volatility 11.5%

In Quarter III-15 downward pressure is increasing in line with peers currency depreciation. Sources of pressure came mainly from external dynamics related to the FFR increased planned by the Fed post improvement in U.S. GDP QII-15, as well as the implementation of yuan devaluation that cause volatility in global financial markets. From home front, pressure comes from the prospect of slowing domestic economic growth.

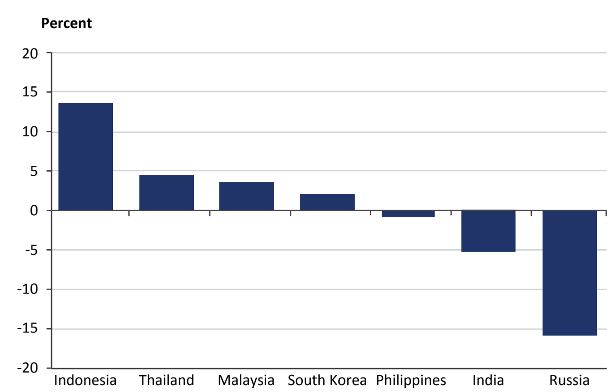
Quarter IV 2015
- Average Rp13,769/USD (appreciation 0.8% qtq)
- End-of-Period Rp13,785/USD (appreciation 6.3% qtq)
- Volatility 16.9%

Rupiah appreciated in Quarter IV-15 triggered by improvedsentiment towards emerging economies after the dovish FOMC Sept-15 andthe release of U.S. employment data is lower. The uncertainty about when FFR rise has also been wane. Meanwhile, from domestic, optimism overgovernment policy package raises optimism over the domestic economy.

normalization of U.S. monetary policy. Domestically, slower economic expansion affected negatively on exchange rate performance, which prompted a fall in non-resident holdings of domestic financial assets and hurt the rupiah further. Consequently, the rupiah depreciated 9% (qtq) to a level of Rp14,650 per USD in the third quarter of 2015 from just 1.9% (qtq) in the previous period. Furthermore, rupiah depreciation expectations increased, indicated by the average difference between the one-month non-deliverable forwards (NDF) and spot rate, which widened from 104 points to 168 points in the second quarter of 2015.[2]

Notwithstanding, the rupiah entered a period of relative stable in the fourth quarter of 2015 as non-resident capital flowed back into domestic assets. The deluge of foreign capital flows, primarily to government bonds, was triggered by more competitive yields than in peer countries (Chart 5.4). Furthermore, foreign capital inflows were maintained by investor confidence after Bank Indonesia, the Government, and OJK announced a series of stabilization policies. Consequently, non-resident capital inflows surged to USD2.27 billion in the fourth

Chart 5.4. **Treasury Bond Investment Returns Quarter IV 2015**



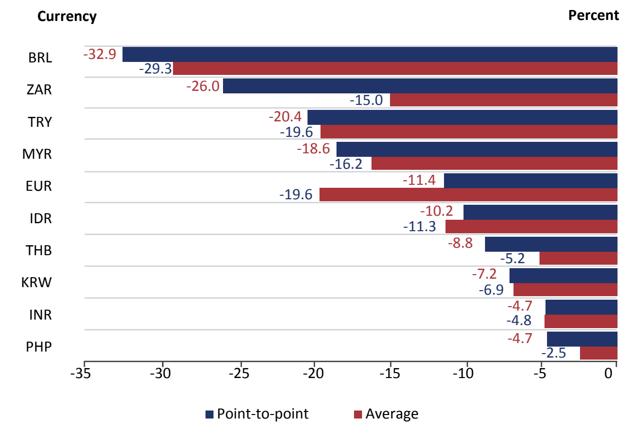
2 NDF is a forward transaction on an offshore market without submitting a notional amount at maturity. NDFs illustrate offshore market perception of future rupiah exchange rates.

quarter, contrasting the net outflow of USD1.85 billion in the third quarter.

The rupiah also appreciated as a result of less external uncertainty linked to the Federal Reserve's plan to raise its benchmark rate. External risks eased after the FOMC meeting in September 2015, relaying a more dovish statement. Expectations of the timing of the hike shifted from the fourth quarter of 2015 to the first quarter of 2016 , which precipitated rupiah appreciation in October 2015 in step with the majority of peer countries' currencies but to a greater degree. In addition, expectations of future depreciation were more managed, as indicated by a narrower gap between the NDF and spot rate (143 points).

After the FOMC meeting on 27-28th October 2015, pressures accumulated again on global financial markets as expectations of the planned FFR hike moved forward to the fourth quarter of 2015. Nevertheless, the impact was less pronounced due to clear communication from the Federal Reserve concerning the timing and gradual path of the policy rate hike. At several forums, officers from the Federal Reserve expressed more succinctly that the U.S. economy was ready to move on the normalization of monetary policy at the FOMC in December 2015. Confirming the timing of the hike helped market players anticipate the move, which triggered a positive market response. Consequently, the FFR hike in December 2015 did not spark financial market shocks. In fact, the rupiah actually appreciated 1.6% between the FFR hike and the end of 2015 in line with the deluge of foreign capital flowing into domestic financial assets (Chart 5.5).

Chart 5.6. Changes In Rupiah Exchange Rates and Peers In 2015



The amplitude of external pressures during 2015 also affected the currencies of most peer countries. Notwithstanding, solid economic fundamentals in Indonesia ensured currency depreciation was not felt as deeply as in Brazil, South Africa, Turkey, and Malaysia (Chart 5.6). In addition, the increase in volatility that accompanied rupiah depreciation was also experienced in the majority of peer countries. In 2015, rupiah volatility increased from 10.2% to 11.1%, which was still lower than that reported in Brazil, Turkey, South Africa, Malaysia, and South Korea (Chart 5.7).

Rupiah depreciation in 2015 was also congruent with limited non-resident inflows to rupiah assets. During 2015, inflows of non-resident stood at USD5.1 billion, down from USD15.4 billion the year earlier. Limited inflows to SUN instruments were recorded, amounting

Chart 5.5. Exchange Rate Peer Countries After FFR Increase in December 2015

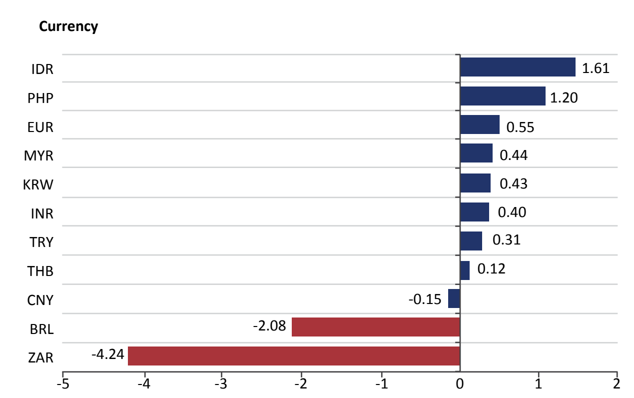


Chart 5.7. Rupiah Volatility and Peers

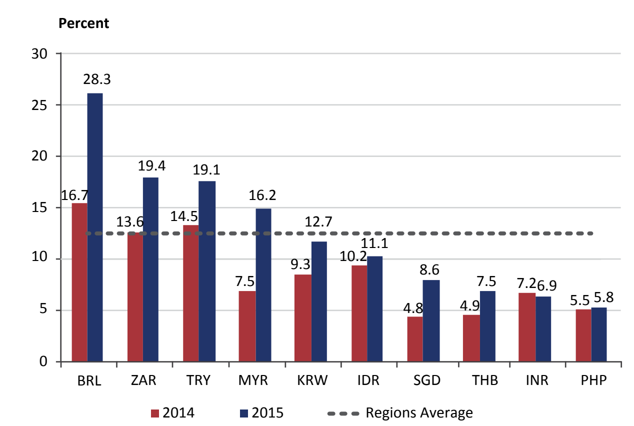


Chart 5.8. Flow of Funds of Non-Resident

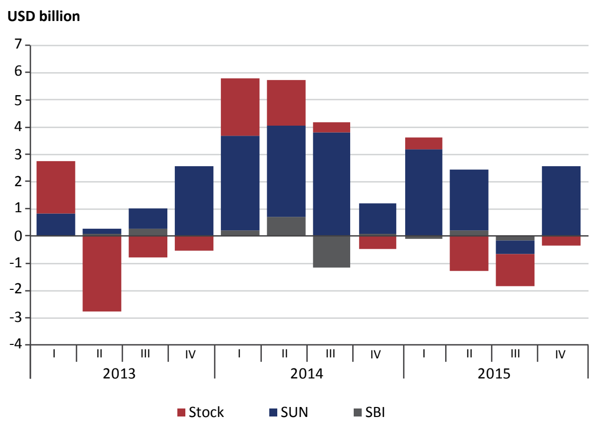
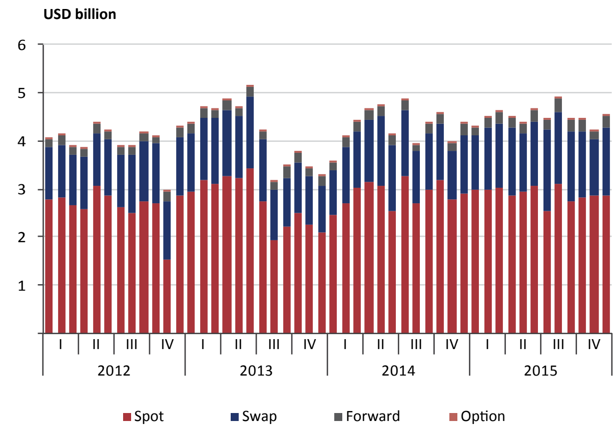


Chart 5.10. Domestic Foreign Exchange Transactions



to just USD7.6 billion. However, a fall in non-resident holdings were reported in terms of stocks and Bank Indonesia Certificates (SBI), totalling USD2.3 billion and USD135 million respectively (Chart 5.8). The fall in foreign holdings of rupiah assets primarily stemmed from traders due to the risk of U.S. monetary normalization policy. Trader holdings nosedived from 35% in 2012 to 13% in 2015, which actually improved the structure of foreign holdings of government bonds. At the end of 2015, real money dominated government bond holdings, increasing from 54% in 2012 to 60%. Meanwhile, the holdings of other market players also surged from 11% in 2012 to 27% as numerous new investors appeared on the market since 2014 (Chart 5.9).

5.2. DOMESTIC FOREIGN EXCHANGE MARKET STRUCTURE

An increase in transaction volume and daily average trading activity were indicative of deeper domestic financial markets. The increase in foreign exchange transaction volume was observed in spot, forward, and swap instruments. Furthermore, average daily foreign exchange transaction volume increased from USD4.3 billion in 2014 to USD4.5 billion in 2015, equivalent to 11.7% (Chart 5.10). The ratio to GDP also increased from 0.48% in 2014 to 0.52% of GDP in 2015 (Chart 5.11).

A growing portion of derivative transactions rather than spot transactions further evidenced gains in terms of the structure of the domestic foreign exchange market. The composition of derivatives on the domestic foreign

Chart 5.9. Foreign Government Bond Ownership

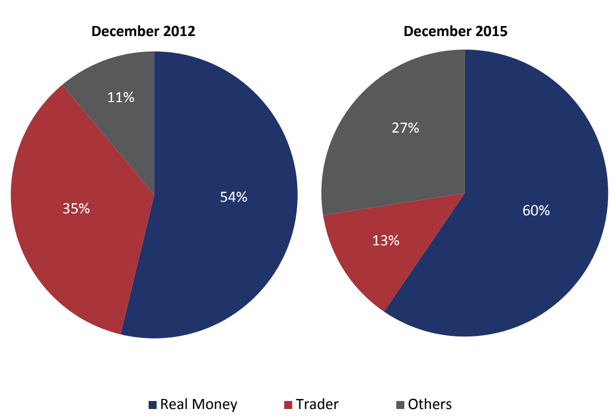


Chart 5.11. Ratio of Foreign Exchange Transactions to GDP

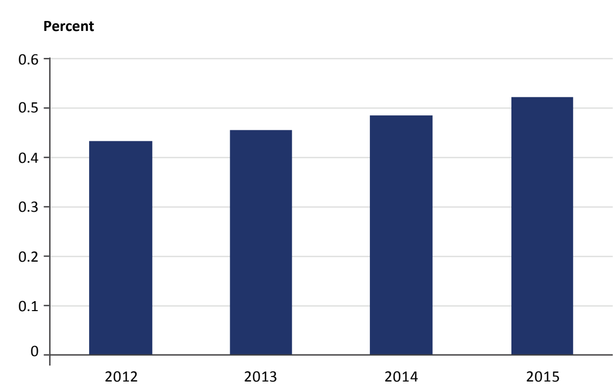


Chart 5.12. **FX Spot vs FX Derivatives Composition**

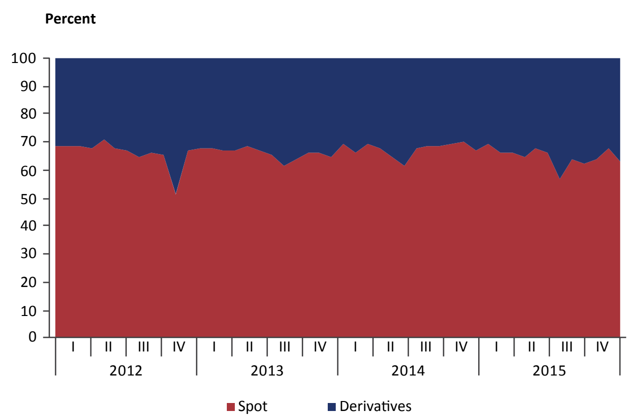
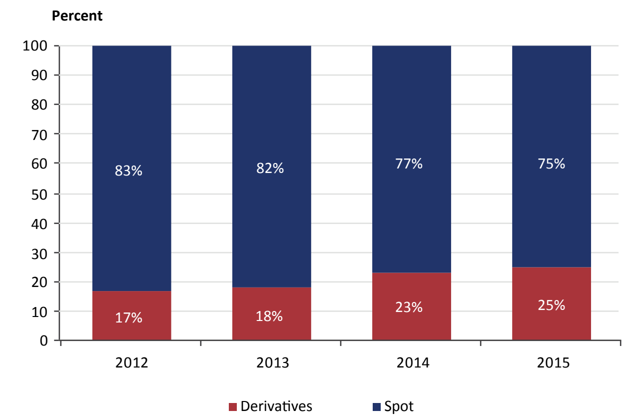


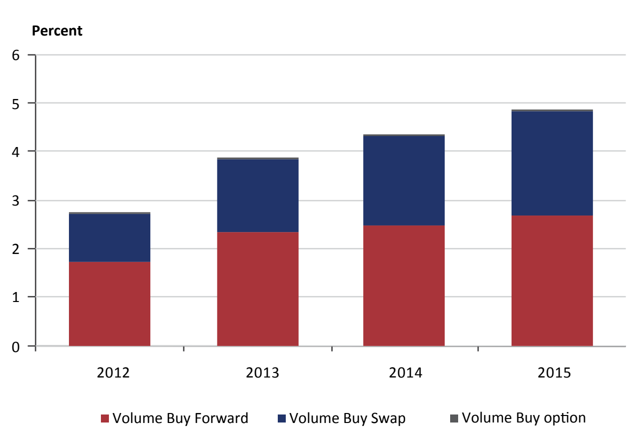
Chart 5.14. **Proportion of The Distribution in Corporate Foreign Exchange Demand**



exchange market swelled from 33% in 2014 to 35% in 2015 (Chart 5.12) in line with Bank Indonesia policy to provide greater market flexibility in order to hedge. This was achieved by relaxing a number of regulations and applying prudential principles in managing external debt of nonbank corporation (PBI No. 16/21/PBI/2014), effective from 1st January 2015. The new regulation requires all indebted nonbank corporations with foreign loans to hedge on the difference between the foreign currency assets and foreign currency liabilities with a maturity of up to six months. On the other hand, derivative transactions also experienced robust growth due to expectations of rupiah depreciation in 2015.

The implementation of prudential principles in managing external debt of nonbank corporation helped improve the demand structure for foreign exchange amongst corporate players. Consequently, the volume of corporate foreign exchange purchases for derivative instruments increased to 4.83% of GDP in 2015 from 4.13% the year earlier (Chart 5.13). The portion of corporate foreign exchange purchases allocated to derivative instruments also increased from 23% in 2014 to 25% in 2015 (Chart 5.14). Consequently, corporate demand for foreign exchange became more calculated in the mid of dwindling supply from non-residents.[3] Increasing corporate foreign exchange purchases of derivative instruments was accompanied by more limited demand for spot transactions, the volume of which dropped from USD10.4 billion in 2014 to USD9.6 billion in 2015.

Chart 5.13. **Ratio of Volume of Foreign Exchange Buy in Derivatives to GDP**



Domestic foreign exchange market deepening efforts continue to face a number of arduous challenges. Increased demand for foreign exchange due to greater market activity, both spot and derivative instruments, has not been met by an adequate increase in foreign exchange supply. Therefore, the domestic foreign exchange market is highly dependent on supply from non-residents. In 2015, the domestic foreign exchange market experienced a state of net demand that exceeded that reported in 2014 due to less supply from non-residents as flows of foreign capital to rupiah instruments slowed (Chart 5.15). Meanwhile, foreign exchange supply from domestic players also evaporated. Consistent with weaker export performance, export proceeds transferred to domestic banks also took a hit in 2015, falling from USD132 billion the year earlier to USD117 billion. In addition, the proportion of export earnings converted into rupiah as effective supply on the

3 A more thorough explanation on the development of nonbank hedging transactions is presented in Box 4.1. Assessing the implementation of prudential principles in managing external debt of nonbank corporation.

Chart 5.15. Foreign Exchange Supply-Demand

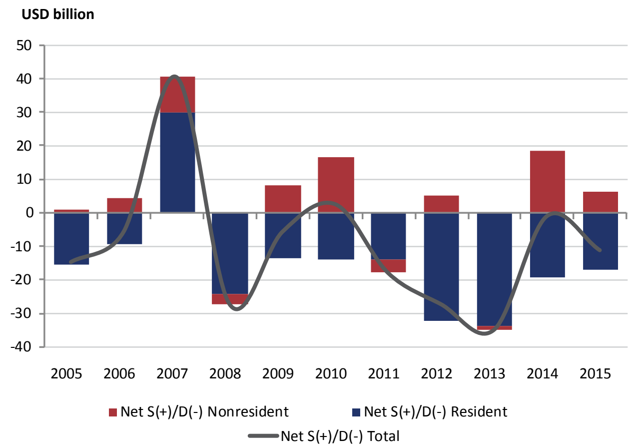
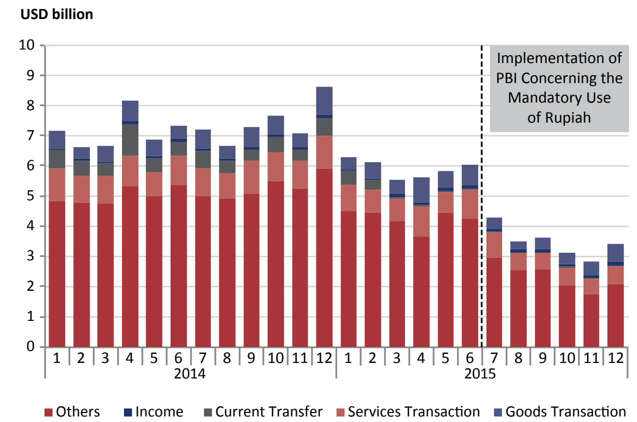


Chart 5.17. Foreign Exchange Transaction between Resident

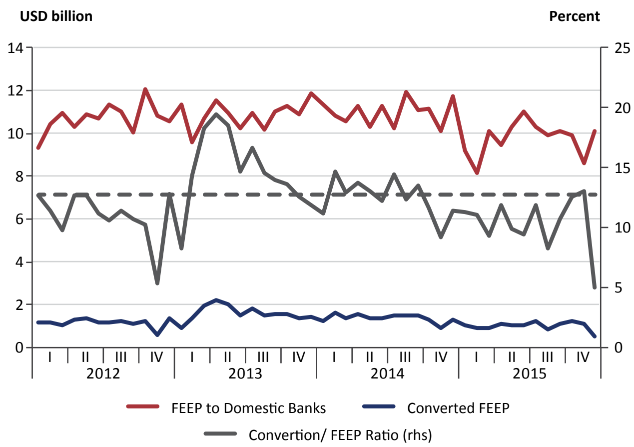


domestic foreign exchange market also shrank to 10% of the total transferred to domestic banks from 13% in 2014.

Anticipating pressures due to a potential foreign exchange supply and demand mismatch, Bank Indonesia introduced policy to boost supply on the domestic foreign exchange market. Steps were done through an amendment to the regulation concerning foreign exchange transactions against the rupiah to increase the threshold on forward transactions without underlying assets, extending the scope of underlying assets, and introducing forward intervention transactions.

Implementation of mandatory rupiah use within the territory of the Republic of Indonesia has had a favourable impact on exchange rate stability. Since Bank Indonesia Regulation (PBI) No. 17/3/PBI/2015 concerning mandatory rupiah use within the territory of the Republic of Indonesia came into effect on 1st July 2015, the monthly average of foreign currency transactions settled between residents has fallen from USD7.27 in 2014 to USD3.46 in 2015 (Chart 5.17).[4] Less use of foreign currencies for transactions between residents has reduced demand for foreign exchange and therefore, bolstered rupiah exchange rate stability.

Chart 5.16. Effective Foreign Exchange Supply from Foreign Exchange Export Proceeds (FEEP)



4 Payment transactions settled through banks operating in domestic. Excluding transactions with the central bank, foreign exchange trade, deposits, overbooking transactions, transactions of less than USD10,000, and funds from received from the Overseas Current Account (OCA).

In 2015, controlled volatile food (VF) inflation, consistent with adequate supply and tumbling international commodity prices, contributed to the successful attainment of the inflation target. VF inflation fell sharply compared to the previous year and even dropped below the historical average for the past four years due primarily to deflation of chilli and shallot prices as well as limited rice inflation.

Chapter 6

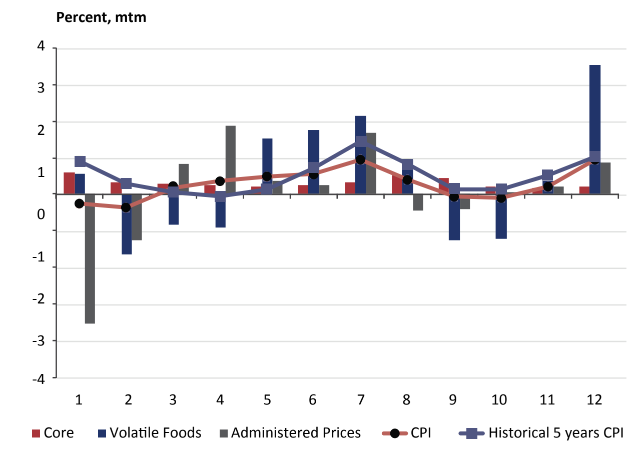
Inflation

The consistent monetary policy to safeguard macroeconomic stability, accompanied with policy coordination between Bank Indonesia and the Government, succeeded in curbing inflation in 2015. Global and domestic economic conditions supported the low rate of inflation at 3.35% (yoy) in 2015. The fall in world oil prices was a key factor of low inflation in administered prices amid the domestic energy subsidy reforms. While the correction in global food prices and Government policies related to food production and distribution, helped control inflationary pressure in volatile foods. Looking ahead, the coordination between Bank Indonesia and the Government under the Inflation Monitoring and Controlling Team (TPI) and their regional level counterparts (TPIDs) will be further strengthened to consistently achieve the inflation target.

The Consumer Price Index (CPI) inflation at 3.35% (yoy) in 2015 was within the inflation target range (4%±1%, yoy) and represented the lowest level of inflation in the past five years (Chart 6.1). The curbing of inflation in 2015 is observed in the monthly inflation dynamics during the second half of the year, consistent with the historical trend but at a much lower level (Chart 6.2). The deflation at the beginning of the year, in departure from the historical trend, was prompted by lower fuel prices and plentiful harvests of certain strategic food commodities. Overall, cost-push inflation in 2015 was minimal in contrast to the two preceding years marked by substantial cost-push pressures that spurred high levels of inflation.[1]

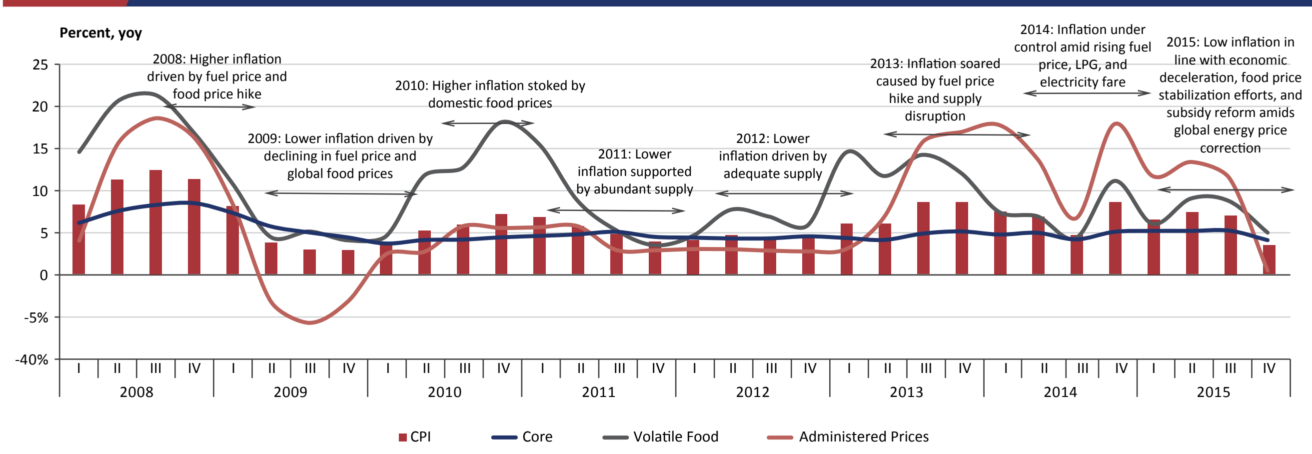
Despite the low inflation in 2015, measures for controlling inflation face considerable challenges in the future. The challenge in controlling core inflation lies mainly in managing inflation expectations to be more in line with the Government-set inflation target and safeguarding exchange rate stability. In the volatile foods (VF) inflation category, the limited infrastructure in the agriculture sector and limitations in policy instruments for price stabilization could lead to steep fluctuations in strategic food commodity prices at different times of the year. Meanwhile, consistency in energy reforms involving more appropriately targeted reallocation of energy subsidies has the potential to create inflationary pressure in administered prices (AP) should an upward correction take place in global energy prices.[2] Considering the substantial challenges for controlling inflation that lies ahead, strengthening the coordination between Bank Indonesia and the Government is necessary to consistently achieve the inflation target. Furthermore, in order to overcome the structural challenges of inflation control at the national and local government levels, the Inflation Monitoring and Controlling Team (TPI) and the Regional Inflation Monitoring and Controlling Team (TPID) have produced an Inflation Control Roadmap for 2015-2018, which serves as guidelines for inflation control policy initiatives.[3]

Chart 6.2. Monthly Historical Inflation Pattern



Source: BPS - Statistics Indonesia, processed

Chart 6.1. Event Analysis of Inflation



Source: BPS - Statistics Indonesia, processed

1 Inflation in 2013 and 2014 was recorded at 8.38% and 8.36% (yoy), driven mainly by high inflation in energy commodities (due to increased in fuel prices) and food commodities.

2 At this time, the Government still provides subsidies for 3 kg bottled LPG and electricity consumers with use restricted to 450 VA to 900 VA. In addition, automotive diesel still benefits from a fixed subsidy of Rp 1,000/liter.

3 See Box: Accountability for Achievement of the 2015 Inflation Target.

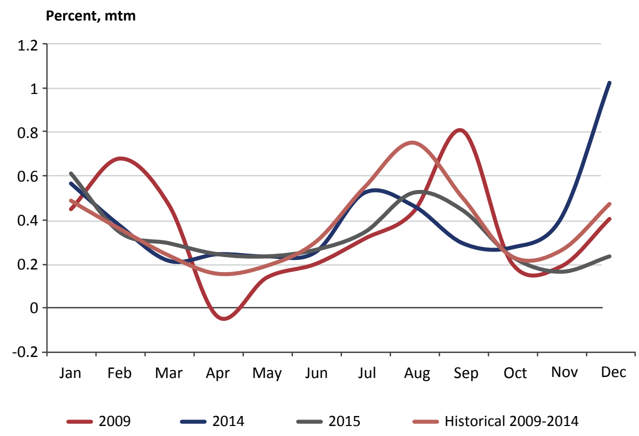
6.1. CORE INFLATION

Price increases for core inflation items remained well under control in 2015. Core inflation reached 3.95% (yoy) at the end of 2015, down from 4.93% (yoy) in the preceding year and the lowest level achieved for the past decade (Chart 6.3). The decline in core inflation took place mainly in the second half of the year (Chart 6.4), affecting on both core traded and non-traded commodities (Chart 6.3).[4] This decline was prompted by low global commodity prices, weakened domestic demand and subdued inflation expectations.

The lower level of core inflation was in line with the moderate level of cost push pressure. Cost push pressure driven by increases in fuel prices and VF prices fluctuations was quite limited. Low world oil prices kept upward pressure on administered prices inflation to a minimum. Government policy for curbing fluctuations in transportation fares also helped control second-round effects during the fuel price hikes.[5] Ongoing correction in global food commodity prices and plentiful domestic supply also resulted in a decline in core food inflation. There was a decline in contribution to inflation from core commodities that represent derivatives of VF items (such inflation in rice with accompanying dishes) and derivatives of food imports, such as noodles (Table 6.1).

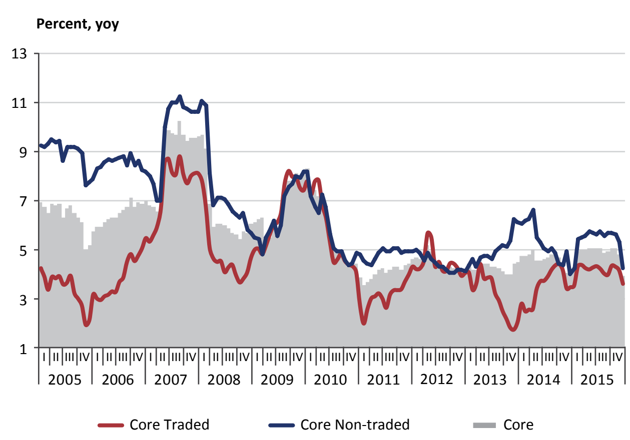
As expected with mild economic growth, which was even below that of previous years, demand-side pressure was again minimal. The economic slowdown that had begun in 2011 continued to bite with economic growth slipping to 4.8% in 2015, the second lowest level achieved in the past 10 years after the 4.6% growth achieved in 2009. This contributed to mild inflationary pressure from the domestic demand side. The depressed level of purchasing power was confirmed by thin growth in the retail sales index and consumer confidence index (Chart 6.5). Price increases for commodities with elastic demand progressively eased, as demonstrated by non-traded non-food core inflation (Chart 6.6).

Chart 6.4. Historical Core Inflation Pattern



Source: BPS - Statistics Indonesia, processed

Chart 6.3. Core Traded and Non-traded Inflation



Source: BPS - Statistics Indonesia, processed

Table 6.1. Contribution to Core Food Inflation

No.	Commodities	2014	2015
Inflation			
1	Rice and Side Dish	0.18	0.14
2	Noodle	0.11	0.07
3	Sugar	-0.03	0.05
4	Mineral Water	0.04	0.04
5	Pastries	0.04	0.03
6	Grilled chicken	0.03	0.03
7	Porridge	0.05	0.03
8	Soup	0.04	0.02
9	Cake	0.03	0.02
10	Barbecued Chicken	0.04	0.02
Deflation			
11	Garlic	0.00	-0.0006
12	Purebred Chiken Egg	0.00	-0.0004
13	Fish	0.00	-0.0003

Source: BPS - Statistics Indonesia, processed

4 In analysis by underlying components, core inflation is formed from traded and non-traded components. Traded components depict core inflationary pressure from externals, while non-traded inflation represents domestic inflationary pressure. On the other hand, the definition of traded inflation is the category of goods traded in exports and imports, as reflected in the balance of trade.

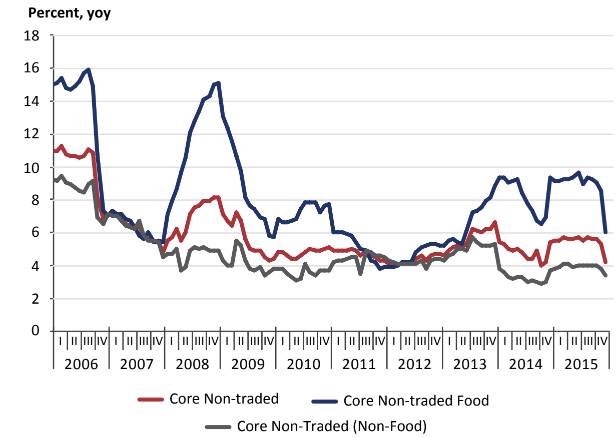
5 Under Regulation of the Minister of Transportation No. 31 of 2015, fare increases are permitted if energy price increases result in a 20% increase in the costs of providing transportation.

Table 6.2. Contributors to Core Non-food Inflation

No.	Commodities	2014	2015
Inflation			
1	House Rental Rates	0.12	0.13
2	Car	0.08	0.10
3	Contract House Tariff	0.11	0.10
4	Non Foreman Worker	0.07	0.08
5	Academy/College	0.04	0.06
6	House Keeper Salary	0.05	0.06
7	Elementary School	0.05	0.05
8	Junior High School	0.05	0.04
9	Senior High School	0.03	0.04
10	Gold Jewelery	-0.02	0.04
Deflation			
11	Cement	0.06	-0.02
12	Steel Bar	0.01	-0.01
13	Bricks	0.00	-0.01

Source: BPS - Statistics Indonesia, processed

Chart 6.6. Core Non-traded Inflation



Source: BPS - Statistics Indonesia, processed

The rupiah weakened considerably during 2015, but impact on domestic prices was contained. In 2015, the rupiah depreciated 11.33% (average, yoy) with the maximum depreciation recorded in September at 4.4% (mtm). At the beginning of the year, core inflation was running high at about 5% (yoy), above the normal level of 4.9% (yoy). This condition was due to the second round effects of the fuel price hike in November 2014. Even so, average monthly core inflation in 2015 was the lowest for the past five years at about 0.32% (mtm). A number of factors influenced the limited impact of exchange rate depreciation to inflation. First, the relatively subdued inflation expectations of economic actors during the period of exchange rate depreciation, as shown in the September survey (Chart 6.7). In December, inflation expectations eased in line with various exchange rate stabilization measures introduced by Bank Indonesia that brought stability and appreciation to the exchange rate. Second, the lingering weakness in public purchasing power led business to opt for temporary cuts in margins rather than to raise prices and then face the risk of losing market share (Chart 6.8). The subdued impact from exchange rate depreciation on price increases provided momentum for core inflation to return to a track consistent with historical performance. Following this, the rupiah appreciation in October accompanied by low demand-pull and cost-push pressure brought core inflation at year-end to below the historical average. The mild impact of rupiah depreciation on consumer prices and its effect on reducing retailer margins was evident from the disparity between wholesale

Chart 6.5. Real Sales Growth

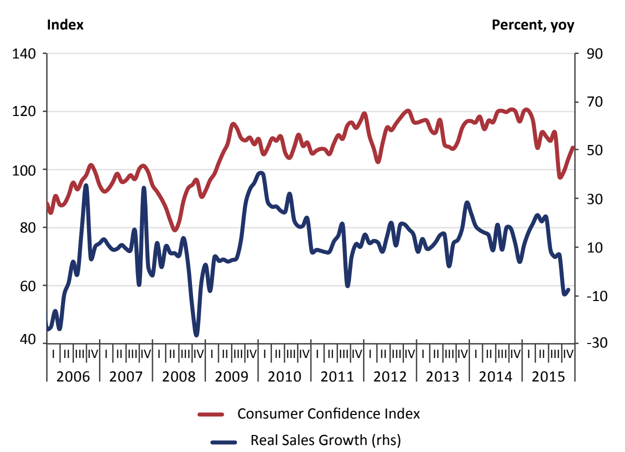
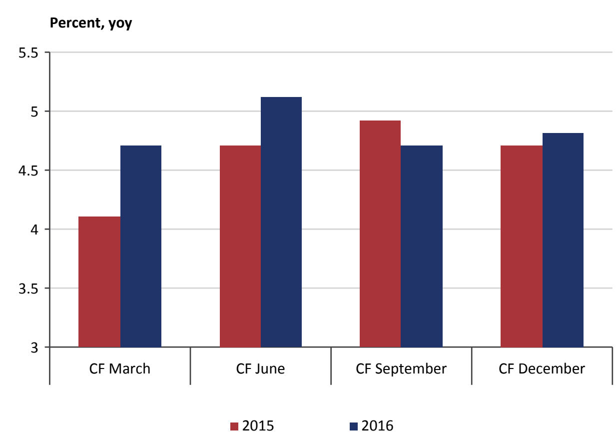


Chart 6.7. Consensus Forecast Expectation



Source: Consensus Economics

Chart 6.8. Margin Per Unit and Selling Price

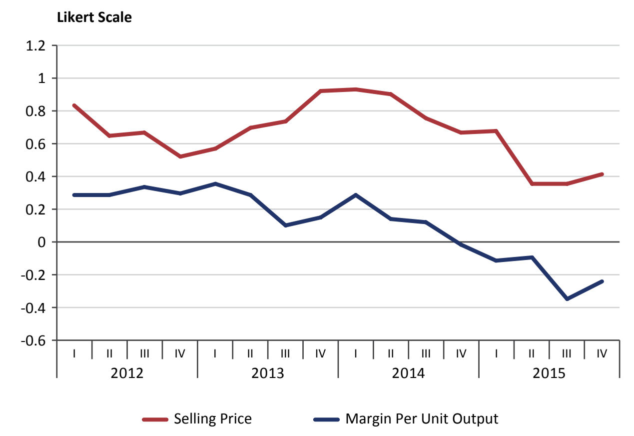
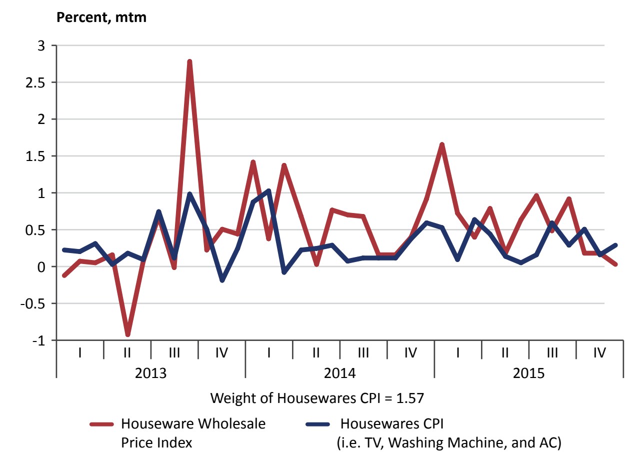


Chart 6.10. Housewares WPI and CPI Inflation



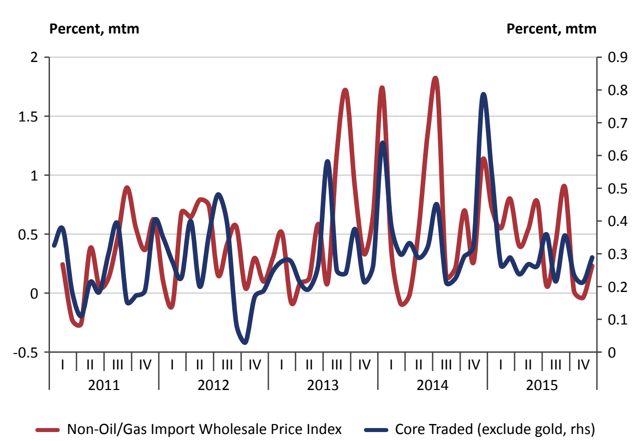
Source: BPS - Statistics Indonesia, processed

price index inflation for non-oil and gas imports and core traded items during 2015 (Chart 6.9). This disparity was particularly noticeable in some sectors, including household appliances, motor cycles and computers (Chart 6.10). The monetary policy consistently applied by Bank Indonesia with the aim of anchoring inflation expectations within the targeting range succeeded in curbing the impact of exchange rate depreciation on prices.

Subdued inflation expectations played a vital role in keeping core inflation under control. The consistency of the Bank Indonesia policy mix throughout 2015 succeeded in containing the impact of exchange rate depreciation on prices and curbing inflation expectations. Moderate short-term inflation expectations were reflected in the retailer and consumer index for inflation expectations during the period of the fuel price hike at the end of the first quarter of 2015, which was lower in comparison to expectations at the time of the previous fuel price hike (Charts 6.11 and 6.12). This points to growing confidence among economic actors that the shock of a fuel price hike will not have excessive impact, which is partly attributable to Government policy to minimize the second round effects of fuel price increases. The subdued inflation expectations of 2015, supported by domestic and global economic conditions, kept core inflation from excessive fluctuation and made the economy more resilient to shocks that did occur, such as depreciation in the rupiah and fluctuating adjustments in energy prices.

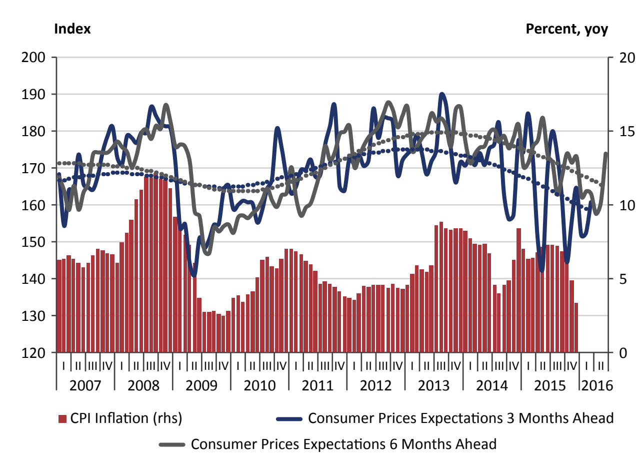
Going forward, indications for the medium-term point to further decline in inflation expectations. In the results of the Consensus Forecast (CF) survey (Chart 6.13), average inflation expectations 24 months forward

Chart 6.9. Import WPI Inflation and Core Traded Inflation



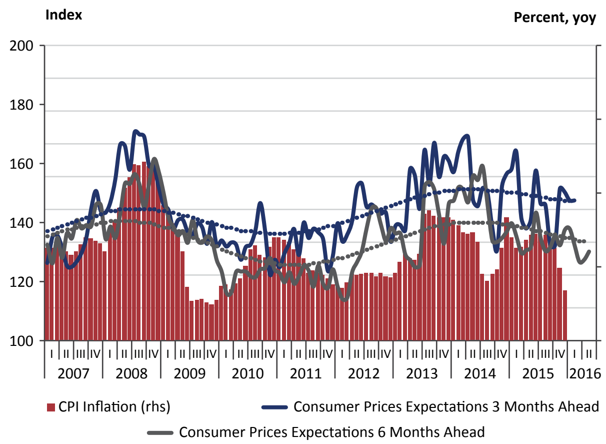
Source: BPS - Statistics Indonesia, processed

Chart 6.11. Consumer Prices Expectations



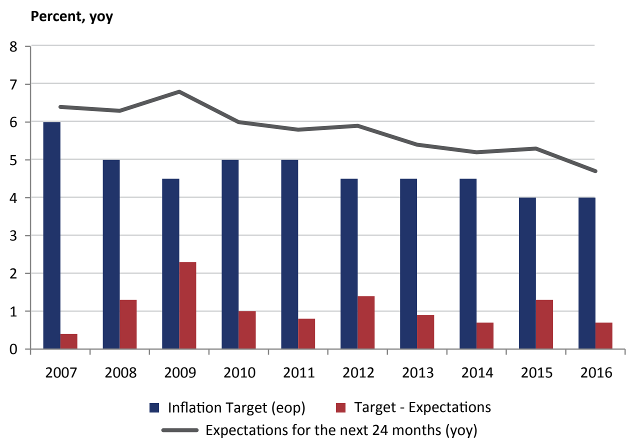
Source: BPS - Statistics Indonesia, processed

Chart 6.12. Retailers Expectations



Source: BPS - Statistics Indonesia, processed

Chart 6.13. 24 Months Inflation Expectations



Source: Consensus Economis, processed

showed a downward trend from 6.4% (yoy) in 2007 to 4.7% (yoy) in 2016.[6] This easing of expectations is consistent with the prescribed gradual decline in the path of the inflation target. Despite the difference that persists between inflation expectations and the target, the co-movement between the two indicates that the inflation target, which is set every 3 years, has created a stronger anchoring of inflation expectations. The downward trend in inflation expectations is also visible in many countries. Nevertheless, there are indications that countries implementing the Inflation Target Framework (ITF) have experienced more significant decline in inflation expectations.[7]

Although inflation expectations have eased in a general sense, the management of inflation expectations still represents a challenge for inflation control going forward. In the long-term, inflation expectations will maintain a downward trend and become more anchored. Even so, issues of concern persist, such as the higher level of expectations compared to both the inflation target and other countries in the region. Where inflation expectations are a key determinant in forming core inflation and future inflationary pressure, management of future expectations for achievement of the inflation target has not only gained importance, but also becoming increasingly fraught with challenges. Looking forward, improvement in the domestic and global economy will boost demand-side pressure that in turn will lead to increase core inflationary pressure. The continuation of energy reforms by the Government will also stoke pressure in the core category should there be any increase in world prices for energy commodities and downward pressure on the rupiah. On the other hand, the inflation target is prescribed to follow gradual decline, with targets of 4±1% in 2016-2017 and 3.5±1% in 2018. Inflation expectations will become more strongly anchored if the inflation target is consistently achieved and thus strengthens the credibility of the central bank and monetary policy. In conclusion, improved credibility of the central bank will keep inflation expectations more strongly anchored and thus create a virtuous circle between the two.

6.2. VOLATILE FOODS (VF) INFLATION

VF inflation was remarkably low. Recorded at 4.84% (yoy), VF inflation plunged dramatically in comparison to the previous year and came below the historical level for the past four years. The decline in VF inflation came in response to lower inflation in miscellaneous chilli peppers compared to the previous year (Table 6.3). In addition, the limited increase in rice prices despite a strong El Nino effect and the correction in global food prices helped keep VF inflation well in hand during 2015.

This subdued VF inflation is reflected in the milder monthly dynamics of VF inflation compared to one year before (Chart 6.14). In the second half of 2015, the VF inflation recorded at 0.33% (ytd), well below that of the same period in the year before (2.22% ytd). The mild VF inflation in the second half of 2015 resulted most substantially from the plentiful harvest of miscellaneous chilli peppers in response to favourable weather conditions and special measures taken by the Government related to expansion

6 Inflation expectations in 2007 and 2016 based on the figures of the Consensus Forecasts for January 2006 and January 2015.

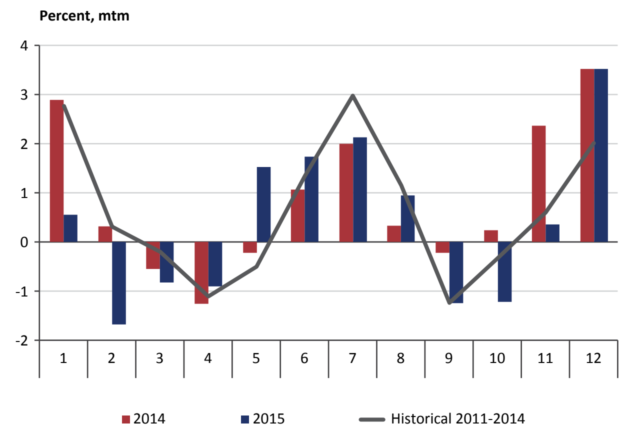
7 See Mehrotra and Yetman (2014) and Mishkin and Schmidt-Hebbel (2007).

Table 6.3.	Inflation/Deflation Contribution of 9 Strategic Food Commodities

Commodities	2009	2013	2014	2015
Rice	0.26	0.14	0.36	0.31
Chicken Meat	0.07	0.10	0.07	0.15
Chicken Egg	-0.01	0.03	0.07	0.09
Garlic	0.18	-0.04	0.03	0.07
Beef	0.02	0.07	0.03	0.05
Onion	0.03	0.31	-0.17	0.15
Fried Noodle	-0.04	0.02	0.07	-0.04
Bird's Eye Chili	0.01	0.07	0.15	-0.13
Chilli	-0.05	0.32	0.41	-0.39

Source: BPS - Statistics Indonesia, processed

Chart 6.14. Volatile Foods Historical Pattern



Source: BPS - Statistics Indonesia, processed

of agricultural lands. In the second half of 2015, the lower VF inflation compared to the same period one year earlier resulted from a harvest of miscellaneous chilli peppers well beyond the seasonal trend, price corrections for chicken meat and eggs as a result of adequate supply, price correction for cooking oil due to low global CPO prices and limited rice inflation despite the strong El Nino.

The Government played a significant role in controlling food prices. The Government's inflation control in food prices focused mainly on stabilizing prices during the holy fasting month of Ramadan and mitigating the strong impact of El Nino in the fourth quarter of 2015. Price stabilization during Ramadan involved market operations for strategic food commodities, including rice, meat, garlic and shallots. To mitigate the strong impact of El Nino, the Government reinforced its buffer stocks of rice through such actions as imports of 700 thousand tons of rice by the National Logistics Agency (BULOG), distribution of the 13^{th} and 14^{th} month Welfare Rice (Rastra) and special measures for expansion of agricultural land and improvements to irrigation. Added to this the Government's deregulation of food imports (beef, horticultural products, corns, and soy beans) helps to maintain the supply of food and stability in national food prices.

The price stabilization program was also supported by the maritime highway system aimed at reducing price disparities among the regions. The development of the maritime highway system is a measure for provision of a regular, scheduled maritime shipping routes with the operation of shipping services (under a subsidy scheme) supported by improved port facilities. The goal of this program is to link the major ports around the archipelago. With these transport links between seaports, a system of connectivity will be created for smooth distribution of goods extended to remote areas and reducing disparities in prices among regions. The Ministry of Transportation now has operated three of the six routes that are stipulated under the Decree of the Director General of Maritime Transportation Number AL.108/6/2/DJPL-15 concerning route networks for operation of the public service obligation for cargo transport within the framework of the maritime highway system, as follows:

a. Route Code T-1: Tanjung Perak - Tual - Fak Fak - Kaimana - Timika - Kaimana - Fak Fak - Tual -Tanjung Perak. (Operated by KM. Caraka Jaya Niaga III - 32).

b. Route Code T-4: Tanjung Priok - Biak - Serui - Nabire -Wasior - Manokwari - Wasior - Nabire - Serui - Biak - Tanjung Priok. (Operated by KM. Caraka Jaya Niaga III - 22).

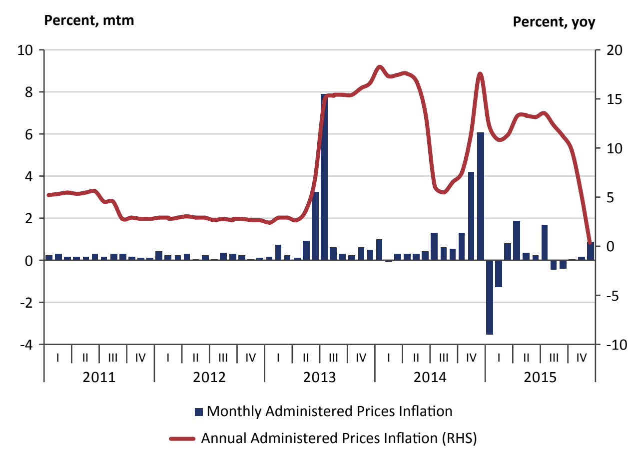
c. Route Code T-6: Tanjung Priok - Kijang - Natuna - Kijang - Tanjung Priok. (Operated by KM. Caraka Jaya Niaga III - 4).

Although VF inflation was mostly low during the year, in December it mounted briefly above the historical level. This is an indication that various structural problems have not been fully overcome, and therefore considerable challenges remain for the future of inflation control. The lack of optimum infrastructure development in the agriculture sector and limitations in policy instruments for price stabilization have resulted in widely fluctuating prices for strategic food commodities at different times of the year. In regard to agricultural infrastructure, there has been inadequate progress in the construction of warehouses for storage of harvested strategic food commodities. Because of this, food commodity prices soared during the planting season and plunged when the harvest season arrived. In a similar vein, the policy instruments for stabilizing food prices are still limited to setting the government floor price for rice procurement, market operations, and distribution of Welfare Rice (Rastra). The benchmarks of indicative prices for red chilli peppers, shallots, chicken, and beef have also not performed well in curbing price fluctuations occurring from time to time.

6.3. ADMINISTERED PRICES (AP) INFLATION

Low pressure from administered prices in 2015 is explained largely by the fall in world oil prices. In early 2015, the Government implemented an energy reform policy in support of more appropriately targeted allocations of subsidies (Picture 6.1).[8] The energy subsidy reform linked the selling price of gasoline and automotive diesel to the Mean of Platt Singapore (MOPS) prices and the exchange rate.[9] Similarly, the adjustment in calculation of the electricity billing rate links the selling price for electricity with the Indonesia Crude Price (ICP), the exchange rate and inflation. Selling prices for 12 kg bottled LPG gas also depend heavily on world gas prices. AP inflation was recorded at 0.39% (yoy), having fallen dramatically in comparison to the previous year and also below the historical level for the past four years

Chart 6.15. Inflation Administered Prices

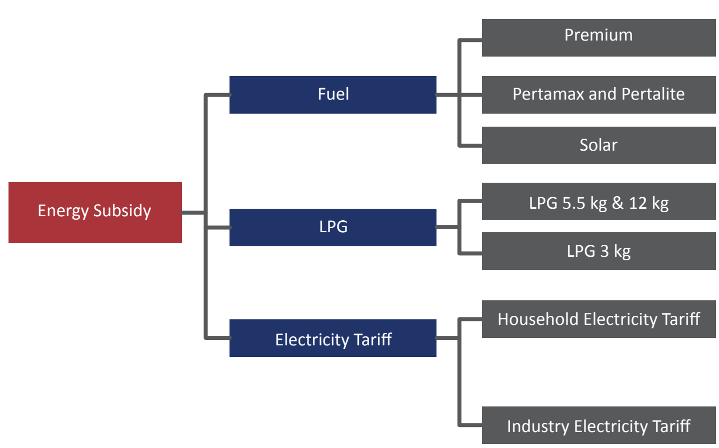


Source: BPS - Statistics Indonesia, processed

(Chart 6.15). Price movements for some AP commodities during 2015 are presented in Table 6.4.

Fuel prices underwent deflation (Chart 6.16). The fall in world oil prices early in the year prompted the Government to announce cuts in fuel prices on two occasions in January 2016. On 1 January 2015, the Government lowered the price for RON 88 Premium gasoline by Rp950 per liter and for automotive diesel by

Picture 6.1. Subsidy Reform in the Energy Sector



Policy	Timeline
Market Price considering domestic economy	Jan 1 2015
Market Price	Jan 19 2015
Fixed Subsidy: Rp1,000/L	Jan 1 2015
Market Price	2015
LPG 3 kg increased by Rp1,000 per kg	2016
Market Price (>2,200 VA) Market Price (1,300-2,200 VA)	2014 2015
Electricity subsidy reduction for 450VA-900VA	2016
Market Price (I3 and I4)	2014

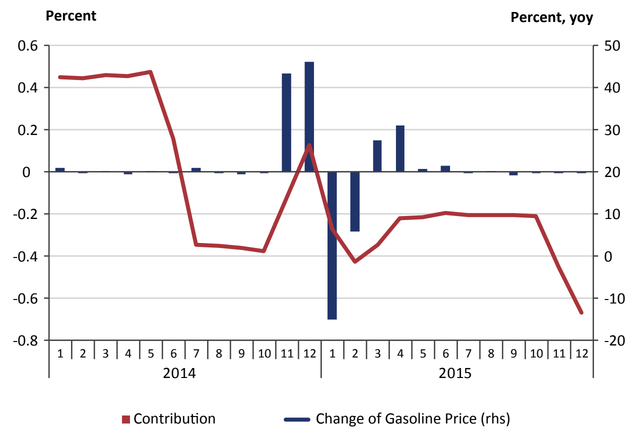
8 The electricity subsidy reform is stipulated in Regulation of the Minister of Energy and Mineral Resources No. 31 of 2014. Similarly, the fuel subsidy reform is set forth in Regulation of the Minister of Energy and Mineral Resources No. 4 of 2015 as amended by Regulation of the Minister of Energy and Mineral Resources No. 39 of 2015.

9 The Government continues to subsidise automotive diesel at a rate of Rp1,000 per liter and kerosene, for which the price is set at Rp2,500 per liter.

Table 6.4. Change of Several Administered Prices in 2015

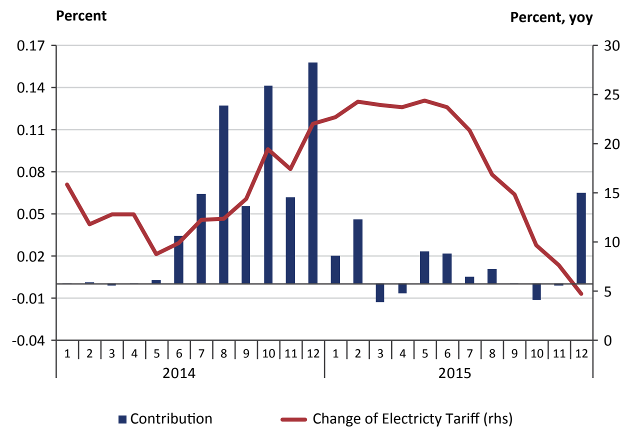
	Fuel		Electricity Tariff		Liquid Petrolium Gas (LPG)	Airfare	Toll Tariff
January	Jan 1: Price correction amounted Rp900/L for RON 88 gasoline and Rp250/L for subsidized solar	Jan 14: Price correction amounted Rp1,000/L for RON 88 gasoline and Rp850/L for subsidized solar	Jan 1: Electricity Tariff Adjustment for Industry, Business, Government Offices, and Household with Power above 2,200 VA			Lower limit air freight rates rose by 10% from the previous.	
February			Household electricity tariff with power above 2,200 VA down from Rp1,496/ kwh in January to Rp1,468/kwh in February.				
March	March 1: Price hike amounted Rp200/L for gasoline RON 88.	March 28: Price hike amounted Rp500/L for gasoline RON 88 and subsidized solar.	Household electricity tariff with power above 2,200 VA down from Rp1,468/ kwh in January to Rp1,426.6/kwh in February.		March 1: LPG 12 kg price hike amounted Rp5,000/tube or Rp417/kg.		
August			Household electricity tariff with power above 2,200 VA down from Rp1,547.9/ kwh in July to Rp1,546.6/kwh in August.				
September	Sept 4: Upper limit rates of the air transport rose by 10% from the previous, while the lower limit tariff corrected by 10% of previous provisions.		Household electricity tariff with power above 2,200 VA down from Rp1,546.6/ kwh in August to Rp1,523.4/kwh in September.		Sept 15: LPG 12 kg price correction amounted Rp6,000/tube or Rp500/kg		
October	Oct 9: Price correction amounted Rp200/L for subsidized solar.		Household electricity tariff with power above 2,200 VA down from Rp1,523.4/ kwh in September to Rp1,507.3/kwh in October.	Oct 7: Industrial electricity tariffs discounts I3 and I4 by 30% for electricity consumption at midnight (23:00) till morning (08:00).			
November							Nov 1: Toll tariff hike average amounted 15%.
December			Dec 1: Household electricity tariff adjustment with power of 1,300-2,200 VA down from Rp1,352/kwh in September to Rp1,508.8/kwh in October.	Household electricity tariff with power above 2,200 VA down from Rp1,532.8/ kwh in November to Rp1,508.8/kwh in December.			

Chart 6.16. Inflation Development and Contribution of Gasoline Inflation



Source: BPS - Statistics Indonesia, processed

Chart 6.17. Inflation Development and Contribution of Electricity Inflation



Source: BPS - Statistics Indonesia, processed

Rp250 per liter. On 14 January 2015, the Government again cut the price for RON 88 Premium gasoline, this time by Rp1,000 per liter, and for automotive diesel by Rp850 per liter. In line with the dynamics of world oil prices and the exchange rate, further changes in prices for RON 88 Premium gasoline and automotive diesel were announced in March and October 2015.[10] For the year as a whole, despite an increase in fuel prices in March, government policy for controlling transport fares was able to curb the second round effects of this hike in fuel prices.[11]

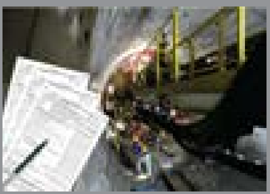
In addition, inflation in electricity tariff was also low, consistent with the decline in world oil prices. This low inflation is due to the factors influencing tariff adjustment, which is the ICP, exchange rate and inflation. During 2015, electricity billing rates were reduced on six occasions.[12] The low fluctuation in electricity inflation under this policy was also prompted by the phased increases in electricity billing rates since 2014. As a result, the contribution of electricity to inflation in 2015 was 0.15%, down from the 2014 level of 0.69% (Chart 6.17).

For the future, the challenges in control of AP inflation will be considerable. These challenges in controlling AP lie in the risk of upward movement in world oil prices and exchange rate depreciation. Furthermore, the government plan to increase prices for 3 kg bottled LPG gas and to upgrade 900 VA electricity customers to 1300 VA will be an added factor stoking pressure in AP inflation. For this reason, the Bank Indonesia and Government coordination of inflation control needs to be strengthened further to keep inflation at the prescribed level. Coordination of the magnitude and timing of energy price adjustments is vital in the effort to control AP inflation.

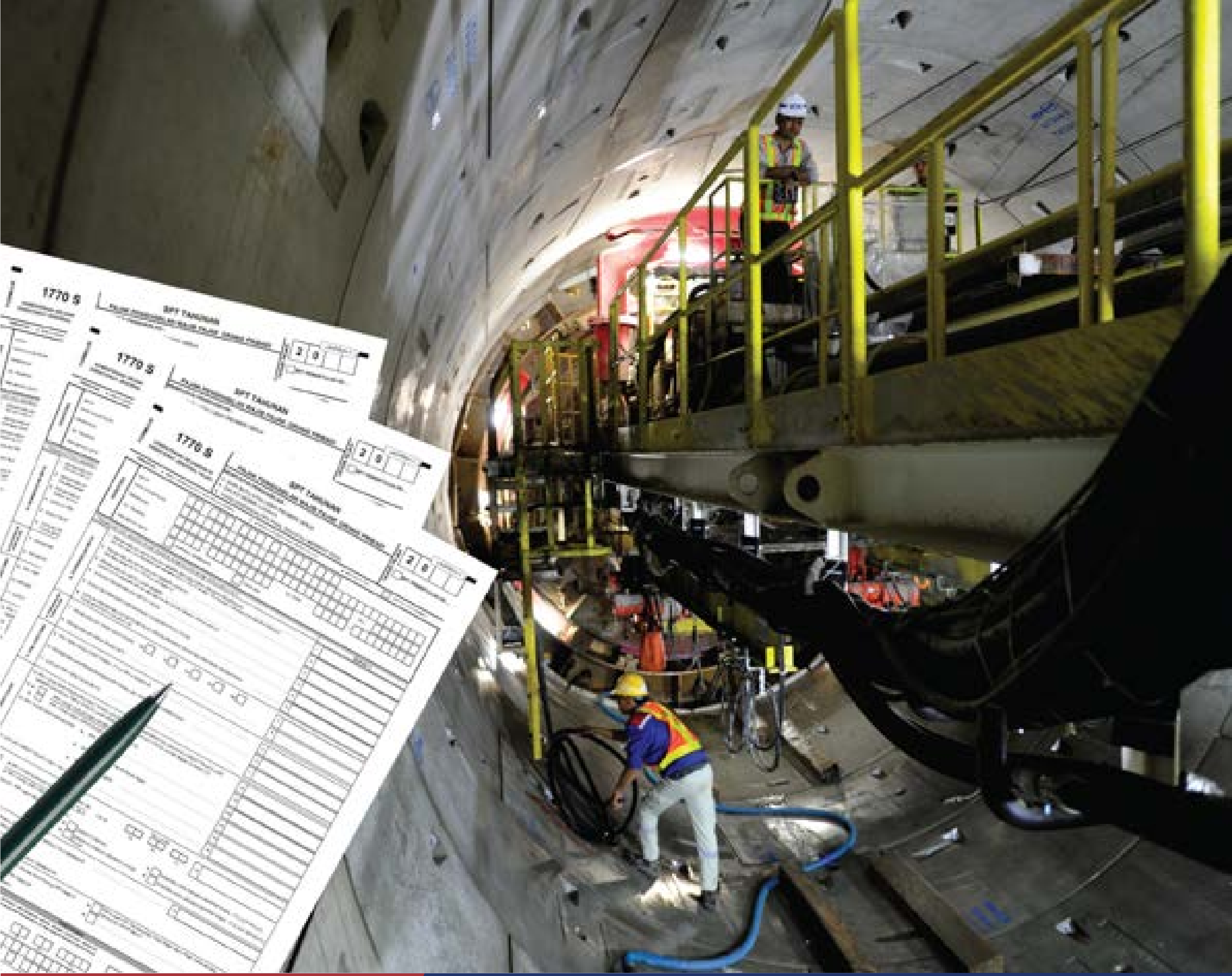
10 On 1 March 2015, the Government raised the price for RON 88 Premium gasoline by Rp200 per liter and on 15 March 2015 raised prices for RON 88 Premium and automotive diesel by Rp500 per liter. Under the Third Economic Policy Package in October 2015, the Government lowered the price for automotive diesel by Rp200 per liter.

11 To curb the second round effects of fuel price increases on transport fares, the Government promulgated Regulation of the Minister of Transportation No. 31 of 2015 on 10 February 2015. This regulation permits fares to be increased if an adjustment in energy prices result in a 20% change in the costs of providing transportation. One component in the cost of providing transportation is the price of automotive diesel, which accounts for about 39% of these costs. The steepest price increase for diesel in 2015 took place on 28 March on that year. At that time, automotive diesel price was raised from Rp6,400 per liter to Rp6,900 per liter. This represents a 7.8% increase, and therefore the effect of that on the cost of providing transportation was less than 20%.

12 Electricity billing rates were reduced six times, in February, March, August, September, October, and December.



In 2015, low international commodity prices severely eroded state revenues. On the other hand, the Government continued to actively spend, particularly on infrastructure, in order to counteract economic moderation. Nonetheless, the state budget deficit was successfully maintained at a healthy level below 3% of GDP.



Chapter 7

Fiscal

In 2015, the deficit of the Revised State Budget (APBN-P) was successfully secured at the level of 2.5% of the gross domestic product (GDP) amid domestic economic slowdown and falling commodity prices. The increase in the deficit was attributable to the lower domestic revenues than the target amid government attempts to boost fiscal stimulus. Even though the fiscal stimulus failed to deliver in the first half of 2015, government spending picked up rapidly in the other half. The increase in government expenditure, especially capital expenditure, in the second half of the year was instrumental in building up a momentum for domestic economic growth.

Amid pressures on the economy, the Government was still able to prop it up by keeping the deficit below 3% of GDP. The continuing decline in commodity prices that began in 2011 had elevated taxes to an increasingly significant position in state revenue. Due to economic slowdown and tax compliance issues, the tax revenue target that was put on a higher growth path under the Revised State Budget (APBN-P) could not be reached. Recognizing the importance of government spending as part of counter-cyclical measures in the economy, the Government opted for the consequences of the widening of deficit to 2.5% from 1.9% of GDP in the Revised State Budget (APBN-P). With sub-national fiscal realization estimated to remain in surplus at 0.2% of GDP, the overall deficit became lower than 2.5% of GDP.[1] Such deficit was well below the maximum limit of 3% of GDP stipulated under the Law on State Finances.

Throughout 2015, fiscal stimulus was provided on both the government revenue and expenditure sides. On the revenue side, stimulus was provided in various forms of tax incentives aimed at boosting consumption and incentives for investment, for example, by increasing the amount of Non-Taxable Income (PTKP) from IDR24 million to IDR36 million per Individual Taxpayer (OP). On the expenditure side, stimulus was provided mainly in the form of productive spending such as capital expenditure increase and the provision of interest subsidies under the People's Business Credit (KUR) program. Capital expenditure realization had increased by 43.1% from IDR147.3 trillion to IDR209.0 trillion. This increase was much higher compared to the last year's negative growth of 19.4%. Meanwhile, a 10% subsidy was accorded to the KUR interest rate, resulting in a drop of the rate from 22% to 12% in 2015. In the light of the lack of revenue generation, the room for fiscal stimulus in 2015 was significantly influenced by energy subsidy reduction policy. During 2015, fuel subsidies decreased by 74.7% from IDR240.0 trillion in 2014 to IDR60.8 trillion and electricity subsidies went down by 42.7% from IDR101.8 trillion to IDR58.3 trillion. Such decline in energy subsidies would have provided a sufficiently ample room for fiscal maneuver if revenue had not decreased. Fiscal stimulus absorption that was still limited throughout the year 2015 also appeared to be influenced by institutional factors which required increased institutional capacity.

Realization of macro assumptions that was quite different from that of the assumptions under the 2015 Revised State Budget (APBN-P) was the main reason for the failure to reach government revenue target (Table 7.1). The state revenue which recorded a 3.0% contraction was mainly influenced by a 36.3% decrease in Non-Tax State Revenues (PNBP) (Table 7.2). This decrease was related to the oil price level as well as oil and gas lifting prices that were lower than assumed. Meanwhile, tax revenue in 2015 was still capable of chalking up a positive growth of 8.2%, higher than that in 2014, which stood at 6.5%. In spite of this, however, with a higher tax revenue target set under the 2015 Revised State Budget, taxes could only reach 83.3% of the target (a tax shortfall of around IDR250 billion), lower than that achieved in 2014, which accounted for 92.0% of the target (Table 7.3). It was suspected that less than optimal tax revenue was also influenced by the weakening of macro economic conditions and underperforming tax compliance. This condition impacted on the Central Government's tax ratio that went down from 10.9% in 2014 to 10.7% in 2015.

Table 7.1. Macroeconomic Assumptions

Macroeconomic Assumption	2014			2015		
	State Budget	Revised Budget	Realization	State Budget	Revised Budget	Realization*
Economic growth yoy (%)	6.0	5.5	5.0	5.8	5.7	4.8
Inflation yoy (%)	5.5	5.3	8.4	4.4	5.0	3.4
Exchange rate (Rp to USD)	10,500	11,600	11,870	11,900	12,500	13,392
Average of 3-month SPN (Government Treasury Bills) interest rate (%)	5.5	6.0	5.8	6.0	6.2	5.97
Indonesia Crude Oil Price-ICP (U.S. dollar/barrel)	105	105	97	105	60	49.2
Indonesia Oil Lifting (thousand barrels per day)	870	818	794	900	825	777.6
Indonesia Gas Lifting (thousand barrels oil equivalence per day)	1,240	1,224	1,221	1,248	1,221	1,195

Source: LKPP 2014 and *Press Release of Ministry of Finance on January 22, 2016

1 Bank Indonesia's estimation.

On the expenditure side, administrative issues and structural constraints were suspected as the reasons why the multiplier effects of fiscal stimulus were still not optimal yet. Transitional administration included adjustment related to the budget nomenclature ministries/agencies led to the distribution of spending, especially spending on infrastructure, became effective in the third quarter of 2015. In addition, numerous infrastructure-related classic constraints, such as land acquisition and licensing issues were still impeding the progress of development. The same had also happened to the distribution of KUR that was still below the target because of the timing of the credit launching that had just commenced in the second half of 2015. Various obstacles in fiscal stimulus distribution and persistently weak global economic condition were suspected of causing the private sector to take a wait-and-see attitude that was quite persistent during 2015.

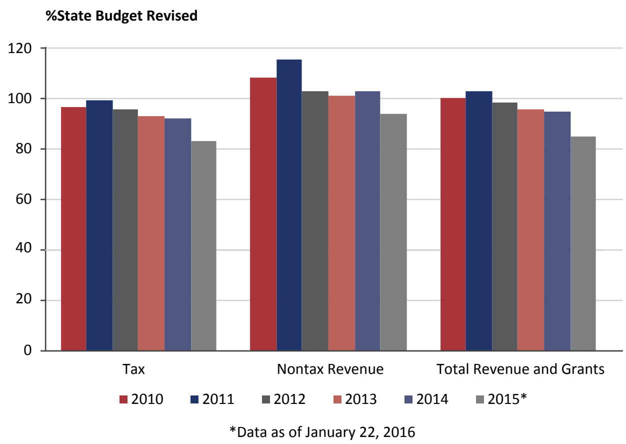
Realized deficit that was higher than targeted under the 2015 Revised State Budget had led to a significant increase in financing needs, especially in the second half of 2015. Widening to IDR292.1 trillion, the deficit was financed with the issuance of additional Government Securities (SBN) amounting to IDR416 trillion, program-based loans and standby loans that impacted on the increase in debt service ratio to around 26% of GDP. Anticipatory measures taken by the government to address the needs for extra financing had once led to turmoil in bank liquidity, especially in December. Unlike the patterns of yesteryears, in December 2015, the government's financial operations created an impact that led to the contraction of bank liquidity, despite an expansionary impact on liquidity for the entire year of 2015. These changes once led to a significant increase in liquidity demand that was reflected in the rising interest rates on the Interbank Money Market (PUAB). Due to a wide range of anticipatory measures taken to address the widening of such deficit, at the end of the transaction year the Government still generated the Budget Financing Surplus (SiLPA) of IDR26.1 trillion (Table 7.2).

Table 7.2. State Budget Realization 2014-2015

Items	Revised Budget 2014	Budget Realization 2014				Revised Budget 2015	Budget Realization 2015*			
	Rp Trillion	Rp Trillion	%GDP**	%yoy	% Revised Budget	Rp Trillion	Rp Trillion	%GDP**	%yoy	% Revised Budget
A. Total Revenue	**1,635.4**	**1,550.5**	**14.7**	**7.8**	**94.8**	**1,761.7**	**1,504.5**	**13.0**	**-3.0**	**85.4**
I. Domestic Revenue	1,633.1	1,545.5	14.7	7.9	94.6	1,758.4	1,494.1	12.9	-3.3	85.0
1. Tax Revenue	1,246.1	1,146.9	10.9	6.5	92.0	1,489.3	1,240.4	10.7	8.2	83.3
- Domestic Taxes	1,189.8	1,103.2	10.5	7.1	92.7	1,440.0	1,206	10.4	9.3	83.7
- International Trade Taxes	56.3	43.6	0.4	-8.0	77.6	49.3	35	0.3	-20.0	70.8
2. Nontax Revenue	386.9	398.6	3.8	12.4	103.0	269.1	253.7	2.2	-36.4	94.3
II. Grants	2.3	5.0	0.0	-26.3	216.5	3.3	10.4	0.1	105.6	313.6
B. Total Expenditure	**1,876.8**	**1,777.2**	**16.9**	**7.7**	**94.7**	**1,984.1**	**1,796.6**	**15.6**	**1.1**	**90.5**
I. Central Government Expenditures	1,280.3	1,203.6	11.4	5.8	94.0	1,319.5	1,173.6	10.2	-2.5	88.9
1. Ministries/Institutions Expenditure	678.1	626.4	5.9	13.1	92.4	795.5	724.7	6.3	15.7	91.1
2. Non-ministries/Institutions Expenditure	602.2	577.2	5.5	-1.1	95.8	524.1	448.9	3.9	-22.2	85.7
II. Transfer to Regions and Village Fund	596.5	573.7	5.4	11.8	96.2	664.6	623.0	5.4	8.6	93.7
1. Transfer to Regions	596.5	573.7	5.4	11.8	96.2	664.6	623.0	5.4	8.6	93.7
2. Village Fund	-	0.0	-	-	-	20.8	20.8	0.2	-	100.0
C. Primary Balance	**(106.0)**	**-93.3**	**-0.9**	**-5.3**	**88.0**	**(66.7)**	**-136**	**-1.2**	**45.9**	**204.0**
D. Surplus/Deficit	**(241.5)**	**-226.7**	**-2.2**	**7.2**	**93.9**	**(222.5)**	**-292**	**-2.5**	**28.9**	**131.3**
E. Financing (Net)	**241.5**	**248.9**	**2.4**	**5.1**	**103.1**	**267.0**	**329**	**2.9**	**32.3**	**123.4**
I. Domestic Financing	254.9	261.2	2.5	7.6	102.5	287.0	307	2.7	17.7	107.1
II. Foreign Financing	(13.4)	-12.3	-0.1	112.4	92.0	(20.0)	10	0.1	10.1	-52.0

Source: Ministry of Finance , *Based on realization update per January 22, 2016, **Based on GDP nominal base year 2010

Chart 7.1. **Component of Tax Revenue to Revised State Budget Target Achievement**



*Data as of January 22, 2016

Source: Ministry of Finance, processed

7.1. STATE REVENUE

Global economic slowdown, decreased lifting costs and commodity price correction that increases in tax revenue could not offset were the reason for the failure to reach Government revenue target. State revenue only accounted for 85.4% of the target set under the Revised State Budget (APBN-P), which was quite low compared with the one achieved in 2014 that amounted to 94.8% and got contracted by 3.0% compared to the corresponding period last year (Chart 7.1). This development was mainly due to declining commodity prices and global economic condition that remained weak and thus impacted on Non-Tax State Revenue (PNPB) that went down significantly. The decrease was primarily due to revenues from natural resources that recorded a negative growth of 57.5% (Chart 7.2).

Table 7.3. **Tax Shortfall Estimation**

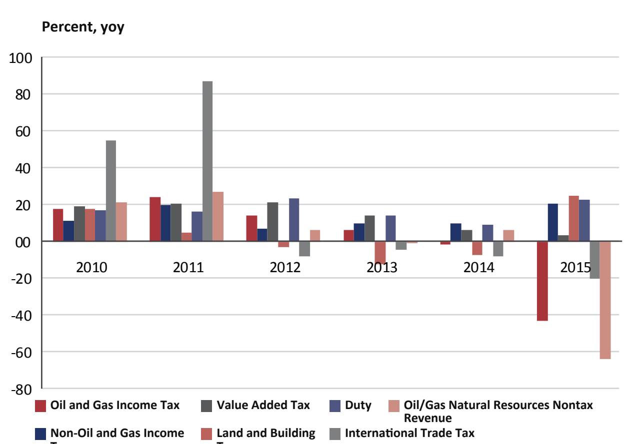
Institution	Tax Shortfall
World Bank	Rp296 trillion
IMF	Rp235 trillion
Center for Indonesia Taxation Analysis	Rp250 trillion

*) Total of Tax Shortfall includes
Source:: http://finansial.bisnis.com

The decline in Non-Tax State Revenue (PNPB) could not be offset by increased tax revenues. The tax revenue growth of 8.2% in 2015 was in line with realized economic growth of 4.79% and inflation of 3.35%. Of the high tax revenue target of IDR1,489.3 trillion, however, only 83.3% was realized, lower than last year's that accounted for 92% of the target set under the Revised State Budget (APBN-P). With this target, government tax ratio was targetted to increase by 2% of GDP from 10.9% in 2014 to 12.9% in 2015. Some analysts believed that this tax revenue target was way too high given the ongoing economic slowdown (Table 7.3).

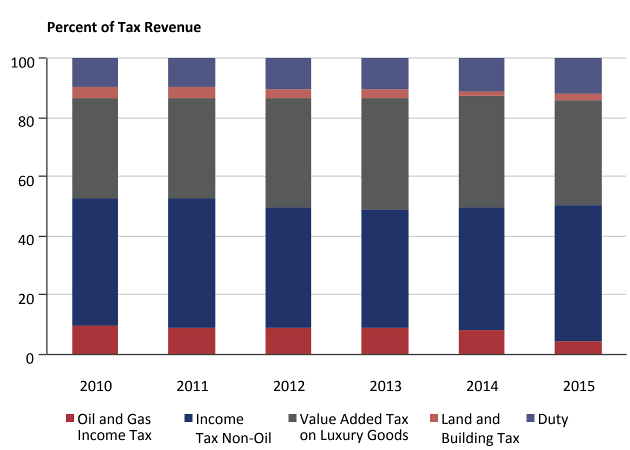
The Government had rolled out a series of policies in order to anticipate the downward trend in the tax to GDP ratio, in line with the inauguration of the year 2015 as the Tax Education Year. The policies included, among other things, a tax penalty relief policy introduced through the issuance of Finance Minister Regulation No. 91/PMK.03/2015 on the Reduction or Elimination of Administrative Sanctions due to Late Filing of Tax Returns, Tax Return Corrections, and Late Payment or Deposit of Taxes. The regulation was a legal means to provide incentives for the elimination of administrative sanctions if taxpayers made corrections to

Chart 7.2. **Annual Growth of Tax Revenue Component Comparison**



Source: Ministry of Finance, processed based on LKPP and Press Release of 2015 Provisional Realization Update January 22, 2016

Chart 7.3. **Composition of Taxes Revenue**

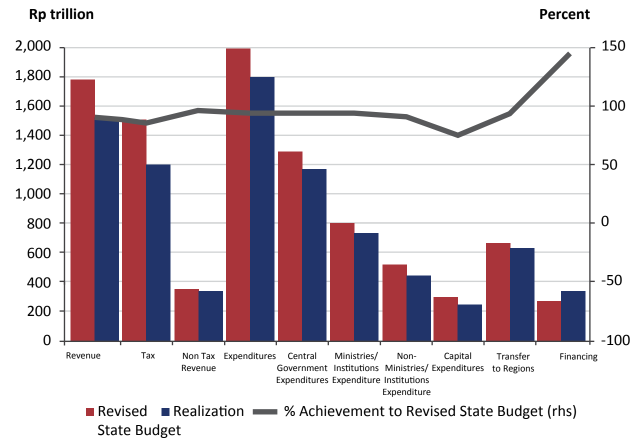


Source: Ministry of Finance, processed based on LKPP and Press Release of 2015 Provisional Realization update January 22, 2016

Chart 7.4. **Tax Ratio Development**

Source: Recent Indicator of Bank Indonesia and Ministry of Finance, processed from Press Release of 2015 Provisional Realization update January 22, 2016

Chart 7.5. **Realization of 2015 Revised State Budget Achievement**



Source: Ministry of Finance, processed based on provisional realization December 31 2015 update January 22, 2016

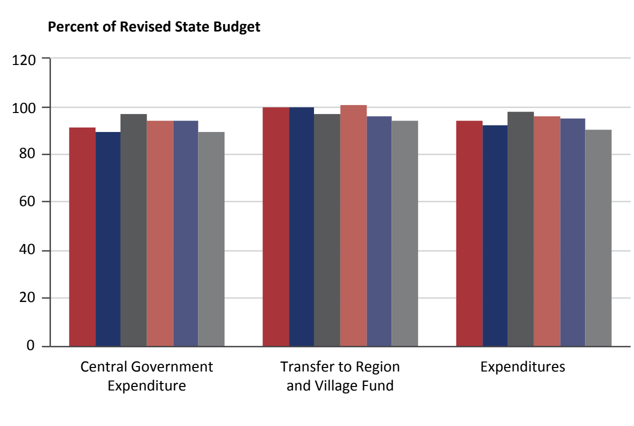
their tax returns (SPT). In addition, the Government had also adopted some law enforcement measures including, among others, *gijzeling* (incarceration) or corporal punishment forcibly imposed on taxpayers for failure to pay off their tax liability. The government had also issued the so-called reinventing policy including the provision of incentives for companies registering for revaluation of assets in 2015. This policy had been able to generate a tax revenue of IDR20.1 trillion. With these various policies, the Non-Oil and Gas Income Tax (PPh) posted a better performance compared to other types of state revenue. In terms of its composition, the non-oil and gas income tax revenue provided the greatest contribution to the domestic tax revenue. The portion of non-oil and gas income taxes accounted for 45.8% of all domestic tax revenues, followed by revenue gains from Value Added Taxes (VAT) and taxes on the sale of luxury goods (PPnBM) that amounted to 35.1% (Chart 7.3).

The portion increased slightly from 41.6% in 2014 due to the decline of oil and gas income tax revenues. In nominal terms, non-oil income taxes had increased by 20.5% (yoy), while the total VAT and luxury goods taxes recorded a contraction of 0.1% (yoy), mainly influenced by a decrease in import VAT. The decline in VAT and luxury goods tax revenues reflected slowing economic activity. The realization of oil and gas income tax decreased significantly by 43.2%, in line with falling oil prices and lifting costs. With these developments, the Central Government's tax ratio in 2015 stood at 10.7%, lower than that of in 2014 which stood at 10.9% (Chart 7.4).[2]

7.2. STATE EXPENDITURE

Achievement of state spending in 2015 was lower than the achievements of 2014 and 2013. It reached 90.5% of the ceiling of the Revised State Budget with Central Government spending being realized at 88.9% of the target set under the Revised State Budget (Chart 7.5 and 7.6). This was mainly due to budget absorption being hampered by nomenclature issues throughout the first semester of 2015. Although the 2015 Revised State Budget was approved in February 2015, issues arising from changes in the nomenclature for ministries/government agencies (K/L) and preparations for the Islamic Eid-ul-Fitr holidays had made absorption become truly effective only after entering the second half of 2015.

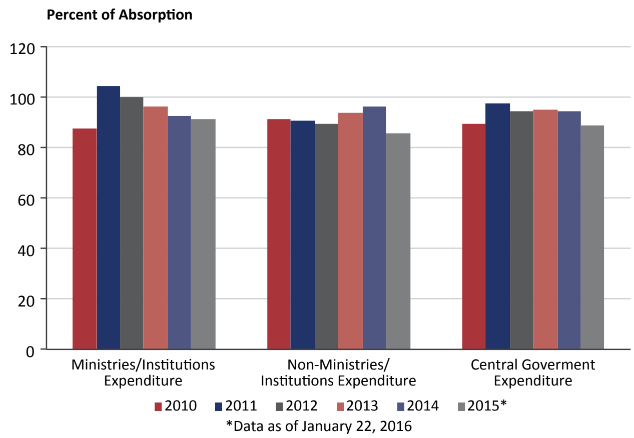
Chart 7.6. **Expenditures Achievement**



Source: Ministry of Finance, processed based on LKPP and Press Release of 2015 Provisional Realization Update January 22, 2016

2 This refers to *tax ratio* in a narrow sense, that is, the ratio of Central Government tax to GDP.

Chart 7.7. Absorption of Ministries/Institutions Expenditure and Non-Ministries/Institutions Expenditure



Source: Ministry of Finance, processed based on Press Release of 2015 Provisional Realization Update January 22, 2016

Overall, K/L spending absorption reached 91.1% while non K/L spending absorption reached 85.7% (Chart 7.7). K/L spending realization grew by 15.6%, compared to the 2014 growth of 13.1%. Meanwhile, the contraction of non K/L spending reached 19.8%, more than the 2014 contraction of 1.1%. Shifting in K/L and non K/L spending items reflected the continuation of reallocation of spending, visible from government policies to reallocate spending from energy subsidies to more productive types of spending, such as capital expenditures

Contraction of central government spending in 2015 was primarily due to a decrease in subsidies. Subsidies went down by 52.6% compared to last year's realization, most of which was due to a IDR222.7 trillion drop in energy subsidies from IDR341.8 trillion to IDR119.1 trillion with the biggest cut coming from the reduction of government spending on petroleum-based vehicle fuel (BBM), LPG (liquified petroleum gas) fuel, and biofuel (BBN) subsidies by 74.7% from IDR240.0 trillion in 2014 to IDR60.8 trillion in 2015. This decline was related to the government policy to phase out subsidies on 'Premium' gasoline and to introduce a fixed subsidy on diesel fuel at IDR1,000 per liter. Meanwhile, electricity subsidy fell by 42.7% from IDR101.8 trillion in 2014 to IDR58.3 trillion in 2015.

The savings made from such subsidies reduction had not been able to be optimally absorbed by other central government spending. Nevertheless, changes in the nomenclature for line ministries/agencies led to a significant increase in the realization of government spending on capital and goods only by the third quarter of 2015. Realized spending on goods and capital in the third quarter grew by 34.8% (yoy) and 58.7 % (yoy), respectively. Such increase in spending still continued in the fourth quarter as seen in goods and capital spending that posted a high growth of 56.1% (yoy) and 50.4% (yoy), respectively.

Accounting for only 75.8% of the target set under the Revised State Budget (APBN-P), capital expenditure realization in 2015 grew 41.9% (yoy). This substantial growth was driven by accelerated implementation of government infrastructure projects, particularly those of the Ministry of Public Works and Public Housing. Such capital expenditure acceleration had become the main engine of growth in investment, particularly in the construction sector in the third and fourth quarters of 2015 amid a wait-and-see attitude on the part of the private sector.

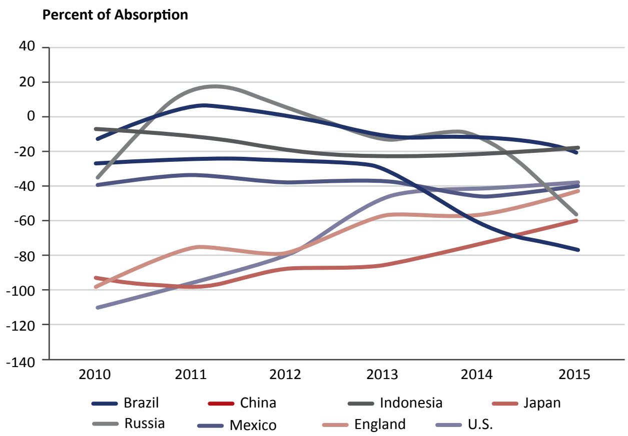
Social Assistance Realization slightly decreased by 0.9% (yoy) with absorption towards target reaching 90.1% of the Revised State Budget (APBN-P). This was in line with the spirit of reallocation of subsidies to spending to support government policies related to the strengthening of social protection and poverty reduction acceleration programs to reduce gaps among groups of various income levels. Measures taken to address the situation included, among others, (i) the implementation of a cash transfer program called Family Welfare Deposit Program (PSKS) made accessible through Family Welfare Card (KKS) issued to Target Households (RTS) including to Persons with Social Welfare Issues (PMKS), (ii) the provision of assistance to stimulate the development of productive economic business activities, and (iii) the implementation of Family Hope Program (PKH) that provides conditional cash transfers to Very Poor Families (KSM).

7.3. FINANCING

Substantial tax shortfall had affected on increasing financing. Such additional deficit was subsequently addressed by expanding the issuance of state securities and loans. The press release issued by the Ministry of Finance on January 22, 2016 said that the actual deficit on December 31, 2015 reached IDR292.1 trillion or 2.5% of GDP.

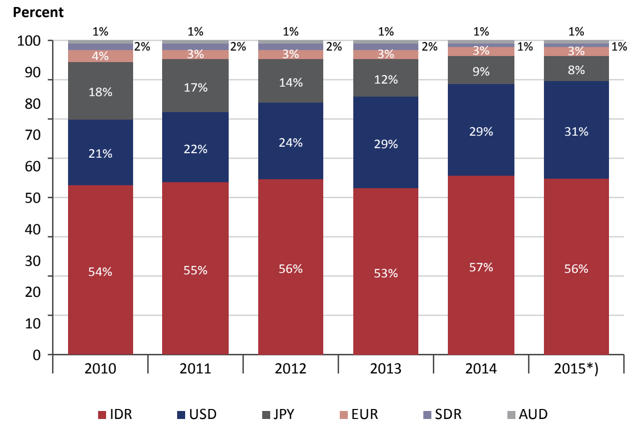
With such development, fiscal financing realization in 2015 reached IDR318.1 trillion, increasing by 34% (yoy) and exceeding the 43.0% target. Domestic financing went up by 23.4%, exceeding the 22.9% target while net foreign financing reached IDR20.0 trillion instead of the negative turnout of the same amount initially predicted. The exceeding of such financing generated a Budget Financing Surplus (SiLPA) of IDR26.1 trillion. The increase in the

Chart 7.8. **Trend of Fiscal Deficit in Several Countries**



Source: International Monetary Fund, World Economic Outlook Database, October 2015 and Ministry of Finance

Chart 7.10. **Composition of Government Bond Denomination**



Source: Central Government's Debt Profile January 2016, Directorate General of Budget Financing and Risk Management Ministry of Finance

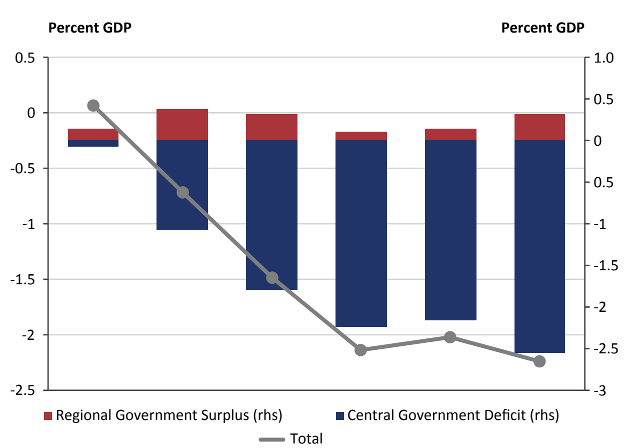
deficit was still lower than in some other countries, such as USA, Japan, Brazil, and the United Kingdom (Chart 7.8). Overall, with an estimated total of sub-national budget realization recording a surplus of 0.2% of GDP, the total deficit was still way well below the limit stipulated under Law No.17 of 2003 on State Finances that was set at a maximum of 3% of GDP (Chart 7.9).

In order to meet its financing needs, the Government re-implemented the front loading strategy. Overall, the net issuance of Government Securities (SBN) throughout 2015 reached IDR361.6 trillion (Chart 7.10). The portion of Central Government debts derived from state securities increased from 74.2% in 2014 to 75.7% in 2015, with the portion of rupiah-denominated SBN slightly down compared to 2014, that is, to 56% from 57%. The portion of SBN denominated in foreign currencies increased in line with the Government's diversification efforts including the issuance of Samurai Bonds. Yields on state securities rose for different loan tenures compared to 2014 (Chart 7.11).

Realization of financing had impacted on the increase in government debt ratios, though still being far from the maximum limit of 60% of GDP. The ratio of Central Government debts to GDP as of December 31, 2015 stood at 26.8% of GDP, which was a slight increase compared to the 2014 ratio of 24.7% (Chart 7.12). The ratio was still below the maximum limit of debt ratio set under Law No.17 of 2003 on State Finances of 60% of GDP, and was better than those of other countries.

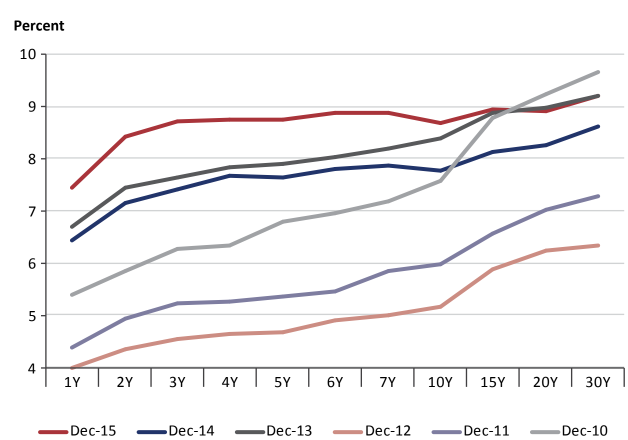
In order to accelerate the 2016 State Budget programs, the Government prefunded the 2016 State Budget. In December 2015, the Government issued Global Bonds

Chart 7.9. **Aggregate Deficit Government Estimation**



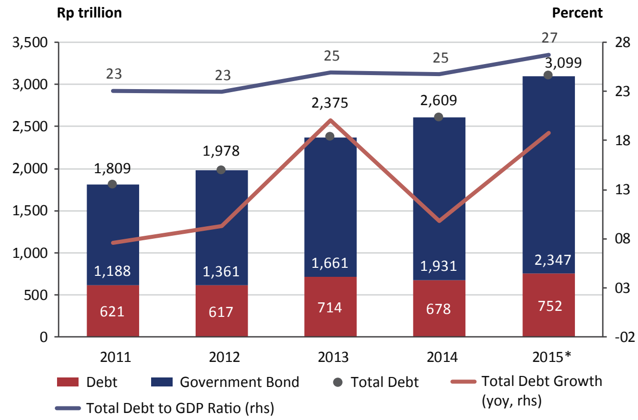
Source: Processed based on LKPP and Provisional Realization Projection December 31, 2015 Press Release update January 22, 2015
Regional Government Surplus is provisional estimation.

Chart 7.11. **Government Bond Yield**



Source: Central Government's Debt Profile January 2016, Directorate General of Budget Financing and Risk Management Ministry of Finance

Chart 7.12. Government Debt to GDP Ratio



*) Based on provisional figures realization revised budget 2015

Source: Ministry of Finance, processed based on LKPP and Press Release of Provisional Realization update January 22, 2015

Table 7.4. Net Claims on Government (NCG) 2013-2015

Rp billion

Explanation	Dec-13	Dec-14	Dec-15	Total 2015
Total Inflow	152,410	170,068	278,153	1,846,178
Total Outflow	221,605	173,383	230.,686	1,993,973
Net Contraction/ (Expansion) Rupiah	-69,195	-3,315	47,467	-147,794
Cumulative	-193,711	-170,790	-147,794	

worth USD3.5 billion and made Private Placement worth IDR15 trillion, thus bringing the total prefunding to around IDR63 trillion, which was equivalent to 12% of the planned gross SBN issuance in 2016. Efforts to provide faster financing for 2016 spending accompanied by an increase in tax revenues throughout December 2015 had affected on changes in the pattern of bank liquidity. Based on historical patterns, the financial operations of the government in December would lead to an expansionary effect in line with increased government spending. However, in December 2015, the prefunding policy and the significant increase in collected taxes impacted on liquidity contraction. This led to the decline in the net liquidity expansion of the government throughout the entire year of 2015 amid increased nominal deficit compared to previous years (Table 7.4). This change had quite an impact on the liquidity of banks in December 2015.

Domestic stock and bond markets experienced pressures congruent with widespread uncertainty on global financial markets. Nevertheless, financial system stability was maintained.

Chapter 8

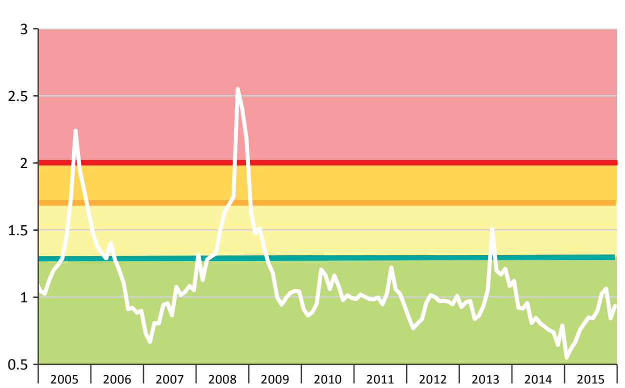
Financial System

The financial system stability has been maintained despite heightened pressures. Since the domestic economy has yet to fully recover coupled with an increase in credit risk as perceived by banks, easing macroprudential policy in supporting loans growth had a limited impact. Loans growth, including loans extended to micro, small, and medium enterprises (MSMEs), were relatively limited in 2015 and lower than earlier predicted. Despite this, strong capital support managed to help ensure the resiliency of the banking industry amid weakening in the financial performance of banks. In the financial markets, unconducive domestic and global conditions also put pressures on the stock and bond markets.

The financial system stability was still maintained at a safe level despite the slowdown in the domestic economy which started back in 2014. Policies which were taken by Bank Indonesia, the Government, and the Financial Services Authority (OJK) were able to rein in the risk of instability in the financial sector. One of the indicators which was used by Bank Indonesia to assess the stability of the financial system was the Financial System Stability Index (FSSI).[1] During 2015, the FSSI rose to a level of 0.93 from 0.79 in 2014, yet still quite far from the threshold of 2 (Chart 8.1).

In 2015, the performance of the banking industry, the Nonbank Financial Industry, and the capital markets experienced a slight slowdown in line with the slowing domestic economic growth. Nonetheless, facing several challenges, the national banking industry was still fairly resilient, as reflected in the high capital adequacy ratio and credit risk which was under control. Meanwhile, the Nonbank Financial Industry generally also showed a downturn in performance in 2015 as reflected in the slowing assets growth of financing companies, the insurance companies, and pension fund companies. From the risk side, the risk associated with financing companies and the insurance companies also increased, as reflected in the increase in the ratio of Non-Performing Financing (NPF) and the ratio of gross claims to gross premiums. The performance of the bond and equity markets also weakened in line with the heightened risks in the financial markets. The weaker performance of the bond and equity markets in 2015 was reflected in the higher yield on 10-year Government Bonds, the declines in the Jakarta Stock Exchange Composite Index (JCI), along with higher volatility of returns from Government Bonds and stocks.

Chart 8.1. **Financial System Stability Index**



Amid slowing loans growth, nonbank financing experienced an increase. The increase in nonbank financing was mostly undertaken by non-financial companies such that the market share for financial companies declined. The increase in nonbank financing was related to the more stringent lending standards for banks in channelling loans which was in accordance with the increased lending risk perceptions of banks. Against this backdrop, companies resorted to alternative financing besides bank loans, i.e. nonbank financing either from the stock market, bond and Islamic bond (sukuk) market, as well as the Medium-term Notes (MTN) market and Negotiable Certificates of Deposit (NCD).

8.1. BANKING PERFORMANCE

In 2015, the performance of the banking industry experienced a slight slowdown in line with the slowing domestic economic growth. Although bank intermediation slowed, the banking industry's profitability was still able to maintain its positive growth. Loans growth in 2015 slowed to 10.4% from 11.6% in 2014. As a result of this slowdown, the Return on Assets (ROA) and the Net Interest Margin (NIM) also experienced a decline, albeit still staying at fairly high levels.

Amid various challenges, the resiliency of the banking industry was still quite strong, as reflected in the high capital adequacy ratio and controlled loans risk. The Capital Adequacy Ratio (CAR) in 2015 rose to 21.2% from 19.5% in 2014. This level of CAR was far higher than the levels in other regional countries which had high CAR levels, such as Thailand with CAR of 17%. Credit risk was still maintained at a fairly low level, with Non-Performing-Loans (NPLs) of 2.5%, or up only slightly compared with the level at the end of 2014 of 2,2%. This condition encouraged banks to be more cautious in facing a slowing economy by maintaining their ability to absorb risks.

To maintain the economic growth momentum, Bank Indonesia issued a number of accommodative macroprudential policies to support loans growth. These macroprudential policies included: easing the Loan to Value (LTV) ratio, extending the basis for sources of bank funding by introducing the Loan to Funding Ratio (LFR), policies to develop Micro, Small, and Medium Enterprises (MSMEs), and policies to strengthen bank capital through Countercyclical Capital Buffer (CCB) requirements. These policies were able to contain the slowing loans growth

1 Components which make up the Financial System Stability Index (FSSI) are the Financial Institutions Stability Index which comprises the pressure, intermediation and bank efficiency components and the Financial Markets Stability Index.

which had fallen to 9.7% before increasing to above 10% and reducing NPLs which had reached 2.8% before falling to around 2.5%.

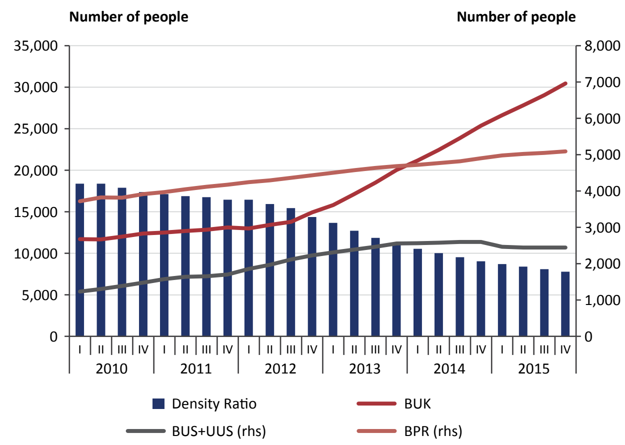
The Developments, Performance, and Risks of Commercial Banks

The structure of Indonesia's financial system in 2015 was still dominated by Commercial Banks and Rural Banks (BPR). This was reflected in the ratio of total assets of the banking industry to those of financial institutions which reached 78.2%.[2] Nonetheless, weak banking intermediation did lead to slowing growth of banking assets. Institutionally, the number of commercial banks declined from 119 banks to 118 banks and the number of BPR declined from 1,643 to 1,637. Nevertheless, total assets of the banking industry still increased from Rp5,615.1 trillion to Rp6,132.8 trillion in 2015, or increased by 9.2%. This increase was less than the previous year's increase of 13.4%. The increase in total assets was supported by the expansion of bank network infrastructure, as reflected in the increase in the number of commercial bank offices from 25,477 to 30,662 and the number of Rural Bank offices from 4,895 to 5,100.

The growth of bank office networks highlights the efforts of banks to expand and realize greater financial inclusion for the people. Greater financial inclusion was, among other things, reflected in a decline in the ratio of the number of bank offices to the population (the density ratio). The density ratio in 2015 shows that one bank office served 7,741 people, an improvement from the previous year's figure of 9,021 people (Chart 8.2).[3] Spatially, most regions in Indonesia already have a fairly good density ratio (Chart 8.3). A number of regions which still have a high density ratio represent a challenge for the banking industry to expand their office networks to these areas.

In 2015, bank loans grew at a slower pace of 10.4% compared with 11.6% in 2014, due to the impact of the slowing domestic economy. The slowing domestic economy encouraged companies to reduce their demand for working capital loans. Besides the weaker demand from companies, banks were also more cautious in channelling loans in order to keep credit risk at a safe level. Nevertheless, the lending standard index experienced a decline in the second half of 2015 to 5.9 at the end of

Chart 8.2. **Number of Bank Office and Density Ratio Year 2010-2015**



2015 in line with the beginning of nascent momentum of economic recovery (Chart 8.4).[4] In 2015, Bank Indonesia issued a number of regulations which were aimed at halting the slowing loans growth, i.e. by easing LTV, expanding sources of bank funding via the LFR regulation, and by developing MSMEs. Easing LTV is intended to give banks room to boost loans to the property and automotive sectors. Meanwhile, the LFR regulation is intended to give banks room to increase their intermediation role more widely by not only relying on bank deposits. These two policies were implemented in the context that macroprudential policy plays a countercyclical role, i.e. in arresting the slowing pace of loans growth as well as economic growth.

Although bank intermediation tended to slow, the role of banking in financing economic activities still increased. This was evident in the loans to GDP ratio which rose to 45.6% in 2015 from 40.1% in 2014. Yet if compared to other countries in the region, such as Malaysia, the ratio was still quite low. The ratio of loans to GDP in Malaysia had already reached 123.1% in 2015 (Chart 8.5).

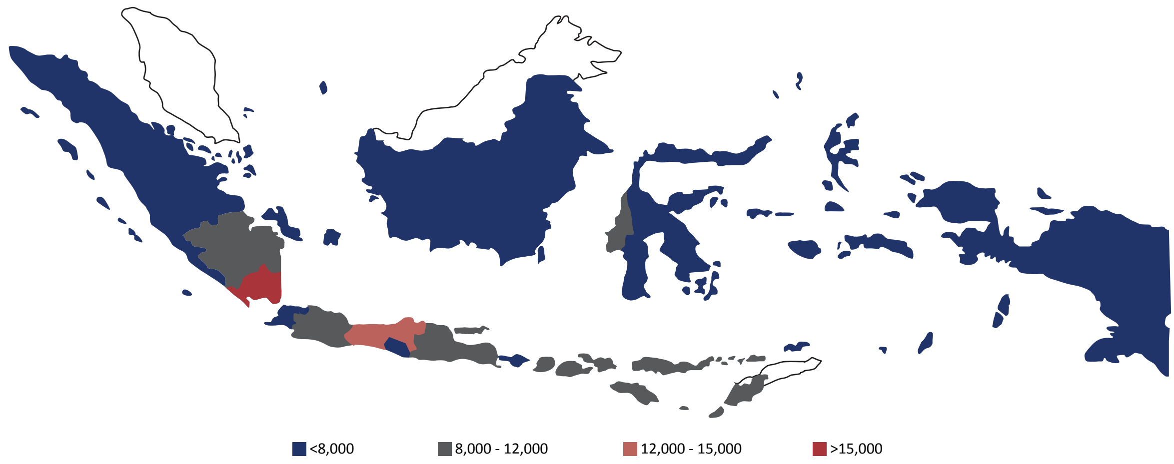
Based on its type of use, working capital loans (KMK) and consumption loans (KK) experienced a slowdown, while investment loans (KI) grew at a slightly faster pace. KMK grew at a slower pace of 9.0% at the end of 2015 compared with 2014's figure of 10.8%. Meanwhile, KI actually grew at a faster pace at the end of the year of 14.7% compared with 13.2% in 2014 (Chart 8.6). The slowing growth in KMK owed to weak demand and faster loan repayments by companies due to the slowdown

2 Study of Stability of Financial System, September 2015 edition.

3 Correction to data on a number of conventional bank (BUK) offices which was issued by the Financial Services Authority in Indonesia's Banking Statistics.

4 The index which shows changes in perceptions toward the level of stringency in bank lending.

Chart 8.3. **Spatial Distribution Density Ratio**



in economic activity which hit the performance of companies. Meanwhile, KK grew at a slower pace of 9.1% compared with 11.5% in 2014. Most consumption loans originated from the households sector, comprising Housing Loans (KPR) and Multiuse Loans. The weaker performance of companies was also behind the decline in household incomes, thereby reducing consumption loans. Nonetheless, the slowing pace of consumption loans was successfully reined in by easing the LTV regulation.

On a sectorial basis, the slow loans growth occurred in nearly all sectors of the economy with the sharpest slowdown in the mining, trading, and other sectors due to the decline in commodity prices which caused corporate performance to decline, either companies which produce or trade related commodities (Chart 8.7). In the first stage, the most highly affected sector was the mining sector. Nevertheless, the impact of the slowdown spread to the trading sector as the second round effect from declining commodity prices, especially in subsectors related to commodity exports trade. The second round effect resulted in a deeper slowdown in loans growth compared with the slowdown which occurred in 2014. In the mining sector, the performance of the coal subsector which produces one of the country's main commodities experienced a significant decline. Significantly weaker exports demand impacted on the worsening corporate business prospects such that demand for loans also declined. Due to the high risks faced by this subsector along with the delayed business expansion or restructuring of bad loans, companies which became debtors tended to repay their loans earlier than scheduled. Meanwhile, loans extended to other sectors as well as consumer loans which are mostly Housing Loans (KPR) and Multiuse loans also

Chart 8.4. **The Development of the Standard Lending Index**

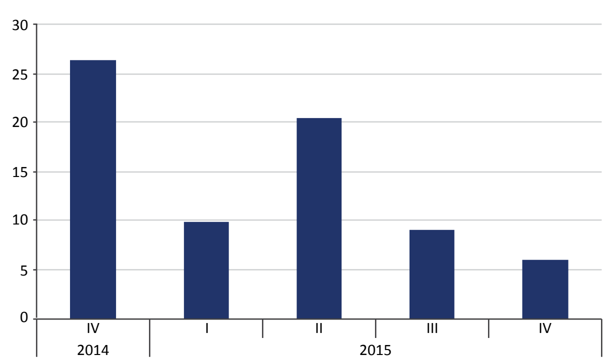


Chart 8.5. **Credit to GDP Ratio**

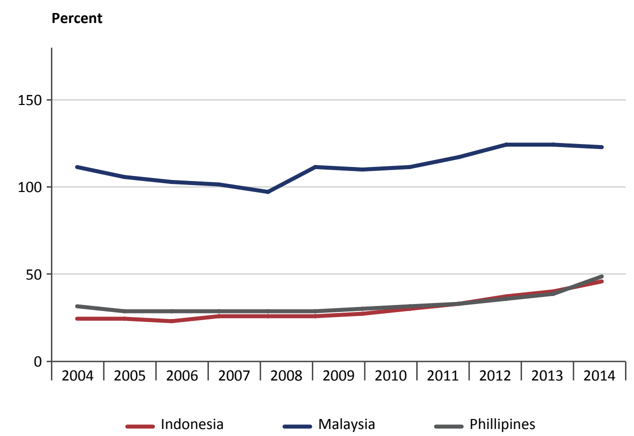


Chart 8.6. Total Credit Growth and Per Type of Use

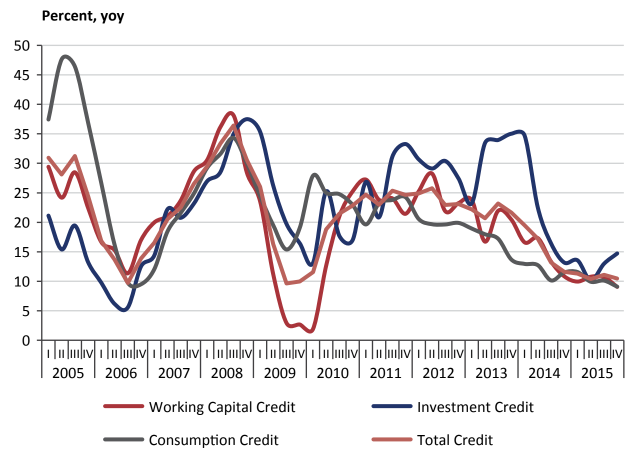


Chart 8.8. NPLs of Commercial Bank

experienced a fairly sharp slowdown due to the prolonged impact from the weaker corporate performance which, in turn, led to lower household incomes.

Bank credit risk tended to increase in 2015 although it still remained firmly within the safety threshold of 5%. The ratio of gross NPLs in 2015 rose to 2.5% from 2.2% in 2014 (Chart 8.8). The increase in NPLs mainly owed to weaker company performance in sectors which were hit by the impact of falling commodity prices. Given these conditions, sectors which experienced an increase in NPLs mainly originated from the mining, transportation, and trade sectors. Despite deteriorating compared to other sectors, the NPLs ratio for these three sectors was still in the safe range of below 5%.

For the mining sector, the increase in NPLs owed to the decline in the performance of mining companies on the back of lower demand, especially for coal, and falling prices in international markets. Deterioration in this sector had been evident since the previous year, although it gradually began to improve in late 2015. In line with this, banks reduced their loans channeled to this sector and were more proactive in taking efforts to settle previously channeled loans. The increase in credit risk in the transportation and trade sectors mainly owed to the second round effect from lower demand and falling commodity prices. In the transportation sector, the transportation of commodities by sea was impacted the most. Meanwhile, in the trade sector, the most heavily affected activity was commodity exports.

Chart 8.7. Loan Growth of Five Largest Economic Sector

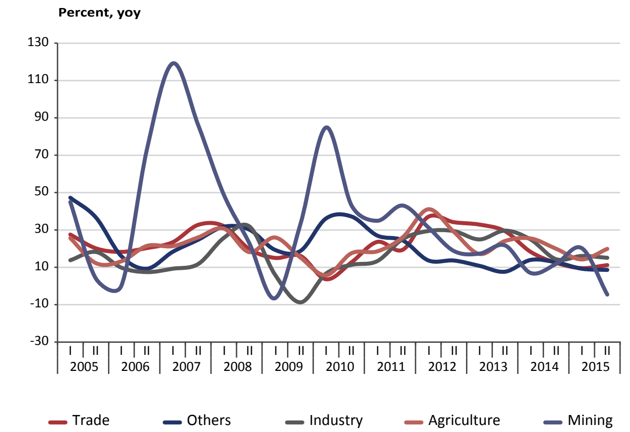
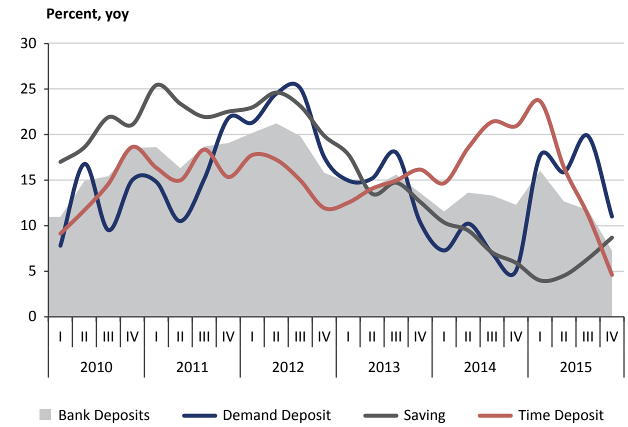


Chart 8.9. Growth of Bank Deposits



From the funding side, growth in bank deposits slowed to 7.3% at the end of 2015 compared with 12.3% in 2014 as loans growth slowed (Chart 8.9). The slowdown in the growth of bank deposits was related to factors including efficiency efforts made by banks through reducing funding costs which originated from costly funds in an effort to maintain the level of profitability. Besides that, the lower growth of bank deposits was also caused by declines in people's incomes, owing to weaker corporate performance, and the impact from the increase in the amount of securities held by Nonbank Financial Institutions in 2015.

The efficiency strategy of banks had resulted in fairly significant declined in deposit rates since early 2015. The decline in the cost of funds was accompanied by decreases in lending rates, although with a lagging effect and of less magnitude, such that the interest rates spread tended to widen (Chart 8.10). Although the growth in deposits slowed, liquidity in the banking sector during 2015 was relatively stable because loans growth also slowed. This was reflected in the relatively stable ratio of liquid assets to deposits which only fell slightly from 20.5% in 2014 to 19.4% at the end of 2015 (Chart 8.11). This liquidity ratio was still far above the safe level of 8.5%, indicating that banking conditions were still safe in face of the risk of a decline in liquidity which may occur.

The lack of recovery in the banking intermediation function led to a decline in the profitability and efficiency of the banking industry as reflected in a rise in ROA d and an increase in ratio of Operating Expenses to Operating Income (BOPO). The downturn in performance despite the ability of banks to reduce their cost of funds was due to the increase in provision expenses arising from the

Chart 8.10. Average Lending Rates, Rupiah Time Deposit Rates and BI Rate

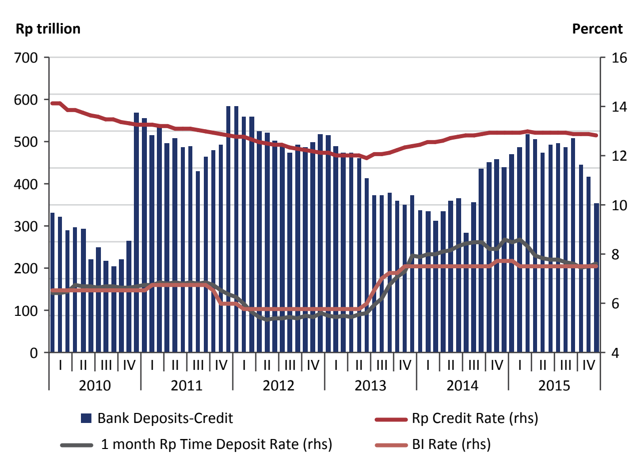
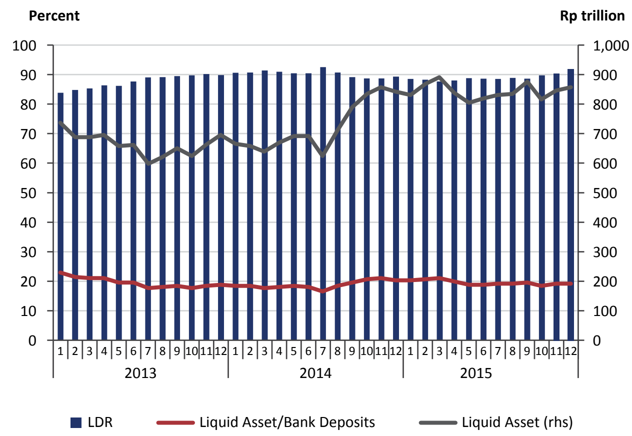


Chart 8.11. LDR and Liquid Assets/Bank Deposits Ratio



slower loans growth which was accompanied by higher credit risk. Nevertheless, compared with other regional countries, the ROA in Indonesia's banking sector was still higher. The decline in the ROA was driven by the decline in the NIM due to tepid loans growth which had already led to a decline in interest income (Chart 8.12). The NIM at the end of 2015 was recorded at 5.2%, or lower than in the previous year (5.5%). Despite the decline, the NIM of banks in Indonesia was still far higher than in other countries in the region, such as Malaysia and Singapore where the NIM ranged between 1.6%-2.0%. Furthermore, the increase in provision expenses and the decline in interest income led to an increase in the BOPO ratio from 75.1% in 2014 to 82.2% at the end of 2015 (Chart 8.13).

Indonesia's banking sector continues to act prudently in addressing the increase in external risks and the slowdown

Chart 8.12. Return on Assets (ROA)

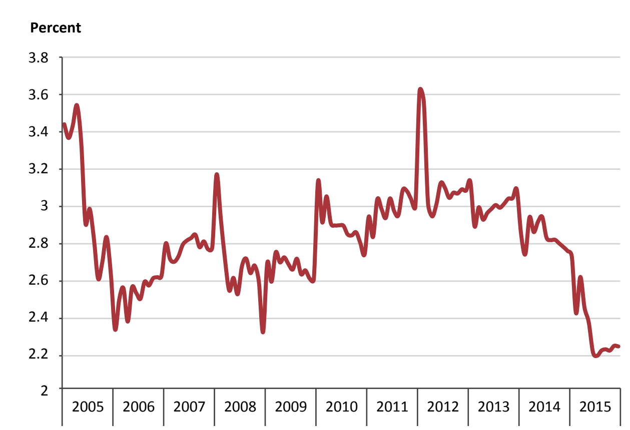
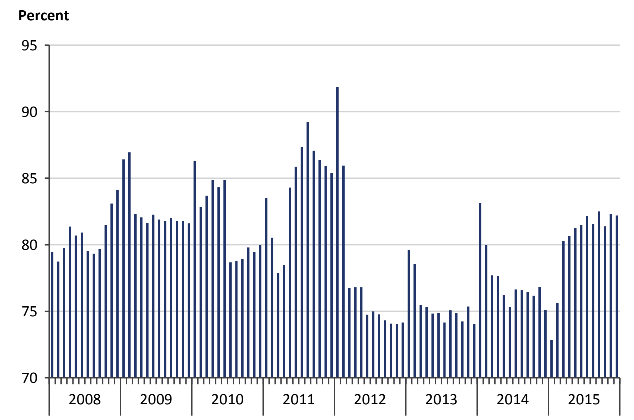


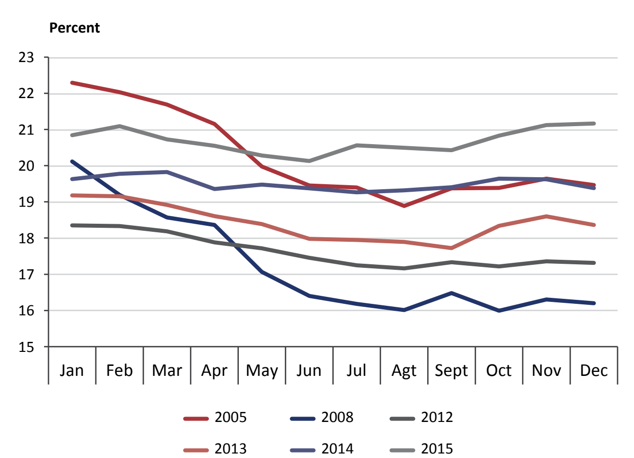
Chart 8.13. Operating Expenses to Operating Income



in domestic economic growth. In this regards, Indonesia's banking sector already witnessed an increase in the capital ratio in 2015 to cushion potential risks. Banking capital rose from Rp722.2 trillion in 2014 to Rp938.1 trillion at the end of 2015. The Capital Adequacy Ratio (CAR)at the end of 2015 was recorded at 21.2%, or higher than the previous year's 19.4% (Chart 8.14). The increase in capital was not only intended to maintain resiliency toward potential risks but also to prepare banks to face the enactment of the provisions of Basel III which stipulates higher capital ratios.

On a regular basis, Bank Indonesia undertook assessments on the CAR of banks toward credit risks and market risks by carrying out stress tests, either industry wide or on individual banks. Assessments of capital adequacy were tested against credit risk and market risk. The stress test

Chart 8.14. Capital Adequacy Ratio



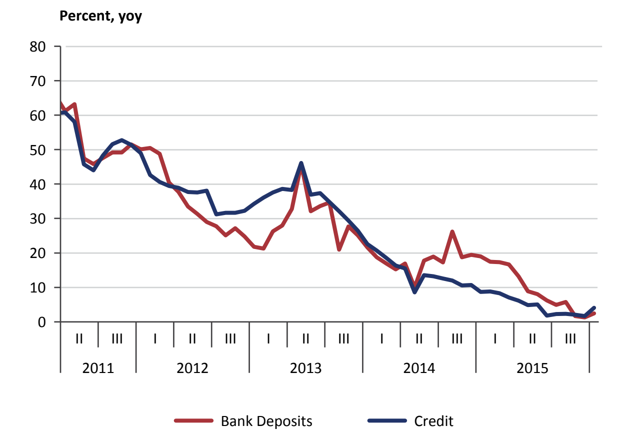
on credit risk was undertaken by taking into account the impact of an increase in NPLs toward the capital of banks. Meanwhile, the stress test on market risk was undertaken by taking into account the impact of an increase in interest rates, the exchange rate, and the decline in Government Bond (SBN) prices. The impact of the risk of rising interest rates on banks was measured through net assets exposure and short-term rupiah liabilities (below 1 year) based on the maturity profile data of the bank. The appraisal of capital adequacy toward the risk of exchange rate weakness was measured through the scenario of exchange rate depreciation. Meanwhile, the exposure of a bank's SBN portfolio in the trading and Available-for-Sale (AFS) categories was used to assess the vulnerability of banks toward the risk of falling SBN prices. The results of the stress test by using the worst-case scenario showed that despite a deterioration in banking conditions, the banking industry in general still had fairly strong capital adequacy. This was reflected in the CAR which was still above the safe limit. In the event of a sharp economic downturn, the integrated results of the stress test showed that there were a number of banks which need capital injections to maintain their CAR above the risk profile.

The Developments, Performance, and Risks of Sharia Banking

Developments in sharia banking were relatively stagnant in 2015. From the institutional side, the number of Sharia Commercial Banks (BUS) was recorded at 12, with 1,990 offices, or down from 2,151 offices in the previous year. Meanwhile, the number of Sharia Business Units (UUS) was unchanged at 22 UUS, with 311 offices. From the assets side, sharia banking's total assets at the end of 2015 reached Rp296.3 trillion, up by Rp23.9 trillion or 8.8% from 2014. Given this, the market share of the total assets of sharia banking to total assets of the banking system reached 4.8% or down slightly compared to the previous year.

Weak banking intermediation and heightened financing risk also affected sharia banking. In line with the slowdown in the channelling of bank loans, growth in the sharia banking industry's financing in 2015 slowed to 4.1% from 8.7% at the end of 2014 (Chart 8.15). The slowdown was also seen in the performance of bank deposits from 19.0% at the end of 2014 to 2.4% at the end of 2015. The deeper slowdown in sharia banking intermediation compared to that of the banking industry in general, with fairly high NPF of 4.8%, showed a slight improvement over the previous year's level of 5% (Chart 8.16).

Chart 8.15. Islamic Banking Intermediation



The slowdown in sharia banking intermediation was accompanied by weaker performance. In terms of profitability, there was stagnation for sharia banks at fairly low levels, as indicated by ROA which was far below that of the banking industry. The ROA of sharia banks in 2015 of 0.49% improved slightly from 0.41% in 2014. The low profitability ratio was accompanied by capital ratios which were lower than the industry's. The CAR of sharia banks in 2015 of 15.0% was down from 2014's level of 15.7%.

The Developments, Performance, and Risks of lending to MSMEs

The slowdown in domestic economic growth also led to a slowdown in demand for loans to Micro, Small, and Medium Enterprises (MSMEs) due to the fall in demand for goods and services. Meanwhile, the increase in credit risk perceptions encouraged banks to be more cautious in channelling loans. In 2015, MSMEs loans reached Rp790.5 trillion or only up 8.0% (yoy), or slower than the growth in 2014 of 15.1% (yoy). The slowdown in MSMEs lending was seen in nearly all sectors of the economy, such as the manufacturing sector where growth reached only 10.0%, or lower than 2014's 19.6%. The lower demand for goods and services also impacted on other sectors, such as the mining sector which originated from supporting MSMEs (truck rentals, equipment, and wages) and the transportation sector which experienced contractions of 19.2% and 4.6%, respectively.

Based on the business classification, the slowdown in MSMEs lending was mainly seen in the micro enterprises where growth reached 11.2%, much lower than the previous year's 33.4%. This is related to the strategies of banks, especially banks with limited networks and human resources, which tended to hold back from microenterprise lending due to rising NPLs. These banks were more focused on making efforts to reduce their NPLs in 2015. Meanwhile, lending to small enterprises showed brisker growth, up from 1.3% in 2014 to 6.4% in 2015.

The market share of MSMEs lending to total bank lending in 2015 reached 19.3%, or lower than 2014's 19.7%. It was mainly absorbed by the wholesale and retail trade sector reaching 52.2% (Rp412.7 trillion). Based on business classification, most MSMEs loans were channelled to medium sized enterprises with a share of 48.6%, followed by small sized enterprises with a share of 29.1%, and micro enterprises with a share of 22.3% (Chart 8.17). Meanwhile, based on project location, the absorption of MSMEs loans are still centerd on Java with a share of 57.8%, followed

Chart 8.16. NPF Development of Islamic Banking

Chart 8.17. MSMEs Lending Development

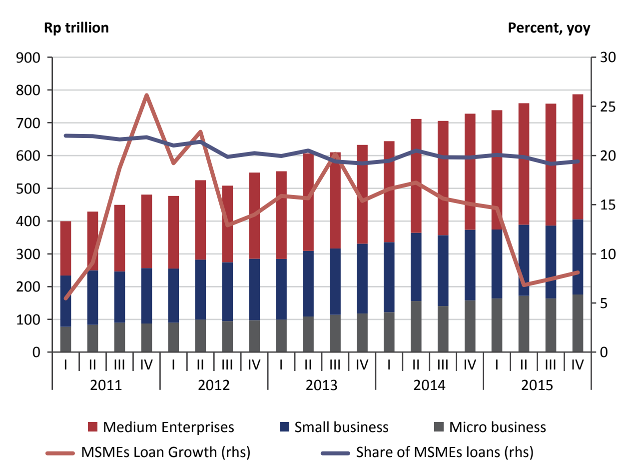


Table 8.1. People's Business Credit Scheme 2015

Items	Micro People's Business Credit	Retail People's Business Credit	Indonesia Migrant People's Business Credit
Business fields	Agriculture, fisheries, manufacturing, and related trade		Especially the placement of Singapore, Malaysia, Brunei, Hong Kong, Taiwan, South Korea and Japan
Ceiling	up to Rp25 million	> Rp25 million up to Rp500 million	up to Rp25 million
Source of funds	100% of funds provided by People's Business Credit executing bank		
Delivery mechanisms	- Directly from the executing bank - Through the linkage institutions (channeling)		- Directly from the executing bank - Through the linkage institutions (channeling or syndication)
Interest rate	12% (effective per annum) or can be adapted to the flat rate equivalent)		
Time period	- A maximum of 2 years for Working Capital Loan - Maximum of 4 years for Investment Loan	- A maximum of 3 years for Working Capital Loan - Maximum of 5 years for Investment Loan	The maximum working time during the term and do not exceed 3 years
Guarantee company	Perum Jamkrindo and PT. Askrindo		

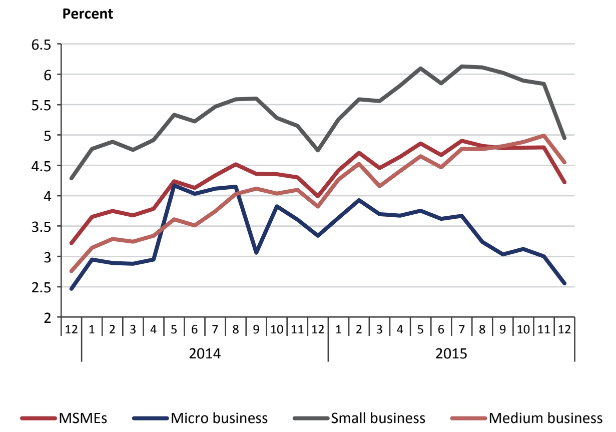
by Sumatra (20.3%), and Sulawesi (7.1%). The majority of MSMEs loans in these three areas were absorbed by the wholesale and retail trade sector at 50.7%, 51.3%, and 62.5% respectively.

To continue to support the channelling of loans to MSMEs which play a strategic role in the economy, Bank Indonesia issued a regulation in 2015 which provides incentives and disincentives for commercial banks in achieving their targets for channelling MSMEs loans. At the end of 2015, commercial banks were required to fulfil the early stages of the minimal MSMEs loans/financing ratio of 5% from the total loans/financing, while keeping the NPLs ratio below 5%. The majority of banks had already fulfilled the MSMEs loans ratio above 5%, and most of them were also able to maintain the NPLs ratio of MSMEs loans and NPLs of total loans below 5%.

Furthermore, the Government launched its new People's Business Credit (KUR) scheme through the Regulation of the Coordinating Minister for Economic Affairs (Permenko) No.6 Year 2015 concerning the Guidelines for People's Business Credit on 7 August 2015 (Table 8.1). The new KUR scheme comprises KUR Micro, KUR Retail, and KUR TKI with targeted KUR lending in 2015 of Rp30 trillion with an interest rate of 12%. Furthermore, to encourage the channelling of KUR, the Government changed the KUR scheme by issuing Permenko No. 8 Year 2015. The changes made include the following: (i) adding to the services sectors which previously only included the agriculture, fisheries, manufacturing, and trade sectors, (ii) not mandatory to have additional collateral, (iii) extension of the loan term, and (iv) channelling mechanism through linkages either channelling or executing. Banks appointed to channel KUR Micro and KUR Retail are BRI, BNI, and Bank Mandiri. Meanwhile, for KUR TKI the appointed banks are Sinarmas Bank and Maybank Indonesia with guarantees from Perum Jamkrindo and PT Askrindo.

From August 2015 until 31 December 2015, realisation of the new KUR scheme had just reached Rp22.8 trillion or 75.9% of the target. The amount channelled comprised Rp14.1 trillion (70.5% of the target) of KUR Micro, Rp8.7 trillion (96.2% of the target) of KUR Retail, and Rp4.7 billion (0.5% of the target) of KUR TKI. The shortfall in the KUR target for 2015 was related to several factors including the relatively short period for channelling KUR (five months), the limited number of channelling banks, along with a lack of socialisation of the new KUR scheme and implementing regulations. Besides that, the channelling

Chart 8.18. NPLs Ratio of MSMEs Loans



of KUR was also still concentrated in the areas of Java (East Java, Central Java, and West Java) with as many as 1,003,663 debtors.

The risks associated with MSMEs loans also increased in 2015. The ratio of NPLs of MSMEs loans in 2015 reached 4.2%, or up from 4% in 2014 (Chart 8.18). The deterioration in the NPLs of MSMEs loans mainly owed to the worsening financial conditions of debtors arising from the business slowdown due to declining purchasing power. Besides that, the deterioration in the NPLs of MSMEs loans also arose because of the lack of good analysis and monitoring undertaken by banks in channelling MSMEs loans. The high ratio for NPLs of MSMEs loans was mainly seen in the wholesale and retail trade sector, which contributed significantly to the formation of NPLs of MSMEs in 2015 at 49.2%. Meanwhile, the ratio of NPLs of MSMEs loans in the wholesale and retail trade sector reached 4%, or up from 3.8% in 2014. Based on the business classification, NPLs increased in the small and medium-sized enterprises, which in 2015 were recorded at 4.9% and 4.5% respectively. This level of NPLs was higher than in 2014 which reached 4.7% and 3.8% respectively. Nevertheless, the NPLs of micro businesses fell to 2.6% from 3.3% in 2014. This reflected the behavior of banks which tended to rein in the channelling of micro business loans, given the risk of rising NPLs, thereby prompting banks to focus more on improving NPLs.

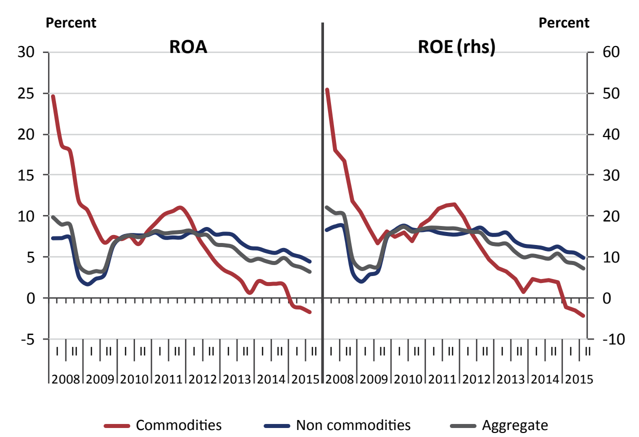
8.2. THE PERFORMANCE OF THE CORPORATE SECTOR AND HOUSEHOLDS

Although the performance of the corporate sector worsened in 2015, it still remained fairly resilient. Corporate profitability experienced a decline which reduced the ability of companies to repay their debts. In addition, as exchange rate volatility increased in 2015, companies tended to reduce applications for credit and started to repay their outstanding loans.

In general, the performance of the corporate sector weakened in Indonesia, as reflected in lower profitability and reduced ability to completely repay corporate debts. The ROA and ROE, as profitability indicators, tended to decline in 2015. ROA fell from 4.9% at the end of 2014 to 3.2% at the end of September 2015. Meanwhile, ROE dropped from 10.9% at the end of 2014 to 7.3% at the end of September 2015 (Chart 8.19). This decline in profitability meant that the proportion of debt to equity increased, as reflected in the Debt to Equity Ratio (DER) which edged up from 1.2 at the end of 2014 to 1.3 in September 2015 (Chart 8.20). The weaker corporate financial performance mainly stemmed from the slowing domestic and global economic growth which led to declines in commodity prices.

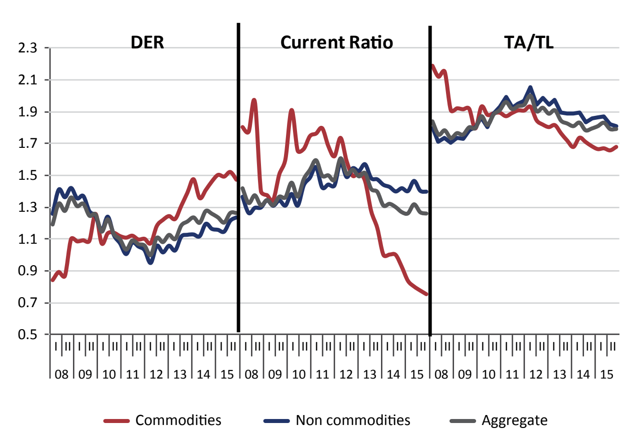
The continued downtrend in commodity prices since 2012 impacted the performance of companies which had exposure to commodities. Companies pursued various strategies in the face of commodity price declines, one of them being to raise export volumes, although also experiencing higher costs and narrower margins. As a result, companies operating in the commodities sector were less able to service their debt, as reflected in the Debt Service Ratio (DSR) which increased sharply from 144.5% in 2014 to 255.6% in 2015 (Chart 8.21). Besides that, the Interest Coverage Ratio (ICR) dropped from 2.6 in 2014 to 1.7 in 2015 (Chart 8.22).

Chart 8.19. Listed Companies Profitability Ratios



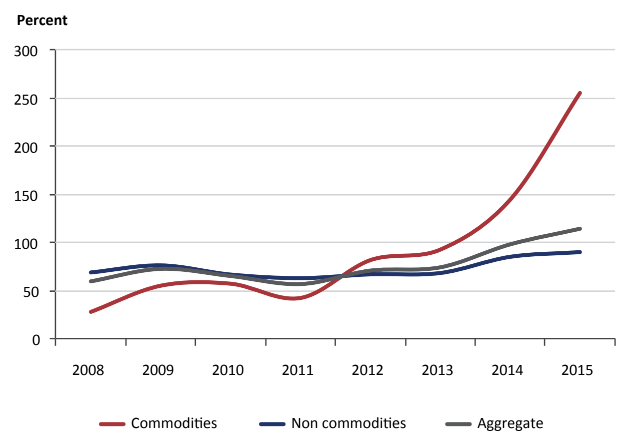
Source: Financial statements BEI and Bloomberg, processed

Chart 8.20. The Development of Listed Companies Debt



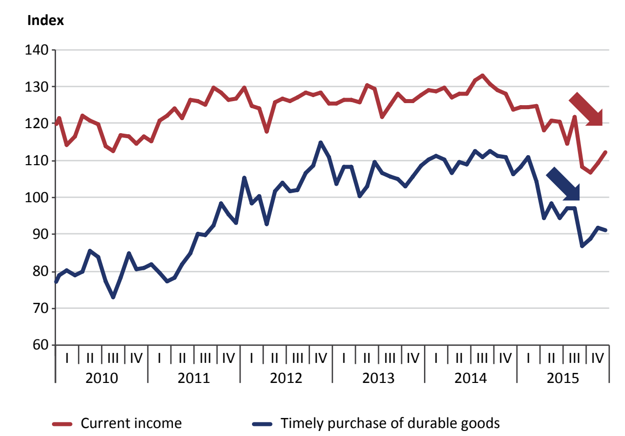
Source: Financial statements BEI and Bloomberg, processed

Chart 8.21. **Debt Service Ratio of Listed Companies**



Source: Financial statements BEI and Bloomberg, processed

Chart 8.23. **Household Income**



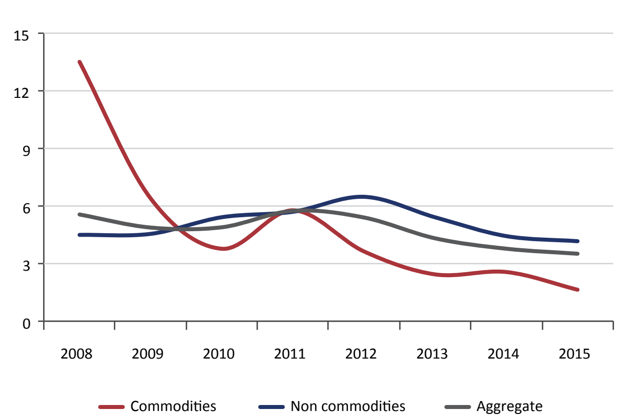
The weaker performance of companies led to lower demand for bank loans, especially compounded by the acceleration of loan repayments by corporations to reduce the risk of exchange rate volatility. Besides that, the weaker corporate performance also led to an increase in the credit risk faced by banks, which, in turn, had an impact on the overall performance of banks. Besides affecting the performance of banks, the decline in the performance of companies also adversely affected household incomes as reflected in the decline in the incomes index from 123,8% at the end of 2014 to 112,3% at the end of 2015 (Chart 8.23).

The decline in incomes was also reflected in the increase in the DSR of households from 13.0 at the end of 2014 to 13.2 at the end of 2015. This increase in the DSR of households indicates the increasing portion of instalments toward incomes. Besides that, the decline in incomes was also reflected in the growth in bank deposits owned by individuals which was lower than the growth in non-individual deposits (Chart 8.24). Besides bringing about a decline in the bank deposits owned by individuals, the decline in incomes also contributed toward the slowing growth and the increase in the NPLs ratio of consumption loans.

8.3. NONBANK FINANCIAL INDUSTRY AND PERFORMANCE OF THE FINANCIAL MARKETS

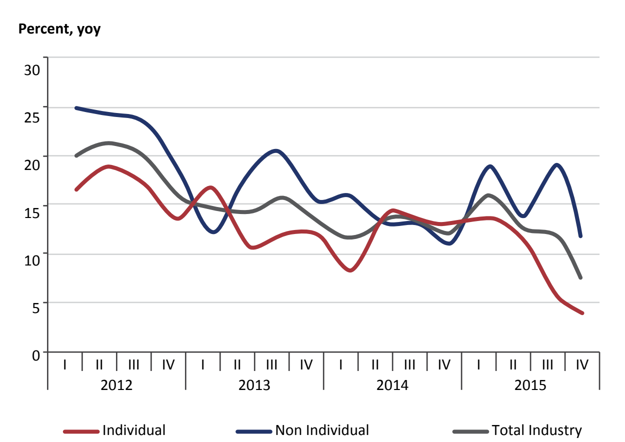
The Nonbank Financial Industry (LKNB) showed weaker performance in 2015. Financing companies, insurance and pension fund companies recorded a slowdown in assets

Chart 8.22. **Interest Coverage Ratio of Listed Companies**



Source: Financial statements BEI and Bloomberg, processed

Chart 8.24. **Bank Deposits Based on Ownership**



growth in line with the slowing economic growth in 2015. Meanwhile, pawnshop services recorded brisker assets growth in 2015 of 10.9%, or higher than the previous year's figure of 6.0%. From the risk side, as economic growth slowed, the LKNB risks also increased. Financing companies' risks rose, as reflected in the increase in the NPF ratio, albeit still remaining at a low level. Besides that, for the insurance companies, there was an increase in the risks at the operating level as shown by the ratio of gross claims toward gross premiums. Nonetheless, from another aspect, the insurance companies' liquidity risk was still relatively well controlled as reflected in the high level of the ratio of current assets to current liabilities.

The performance of the financial markets, either the bond or stock markets, also showed a decline in 2015. In the bond market, the weaker performance was reflected in the 10-year SBN yield which rose from 7.80% in 2014 to 8.75% in 2015. As for the stock market, the weaker performance was reflected in the decline in the JCI to 4,593.01 at the end of 2015, or down 12.13% from its level at the end of 2014 of 5,226.95. In line with this weaker performance, the risks in the bond and stock markets also increased. The increased risk in the bond market was reflected in both the increase of the 10-year SBN yield and the higher volatility in 10-year SBN yields. Meanwhile, the increased risk in the stock market in 2015 was reflected in the declines in the JCI and the higher JCI volatility.

Meanwhile, nonbank financing in 2015 experienced an increase. This nonbank financing was mostly undertaken by non-financial companies such that the share of financial companies declined. Nonbank financing, either through the stock market, bond market, or corporate sukuk, along with the MTN market and NCD in 2015 reached Rp136.1 trillion, or up from Rp111.4 trillion in 2014. This increase reflected, at least in part, the more stringent lending standards by banks in channelling loans in line with the increase in loan risk perceptions by banks. This condition encouraged companies to use alternative financing besides loans, i.e. nonbank financing either from the stock market, bond market, or corporate sukuk, along with the MTN market and NCD.

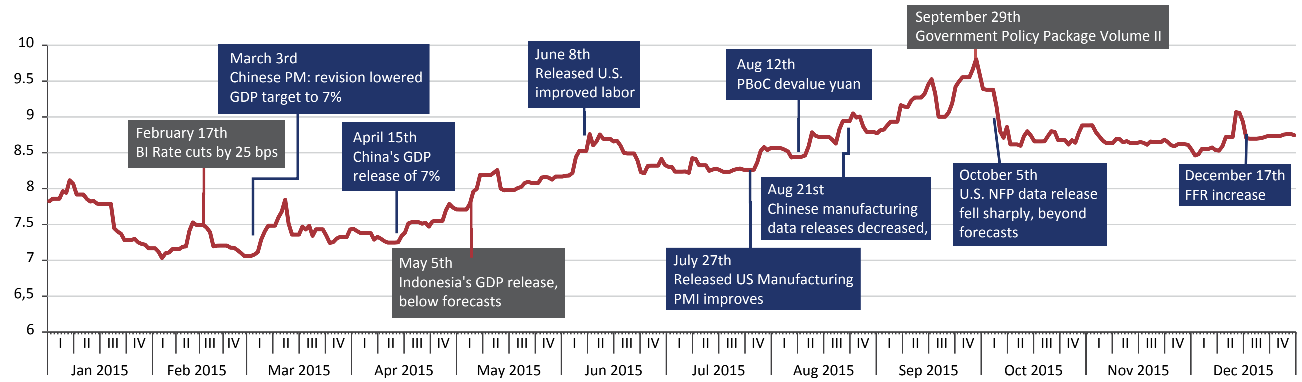
The Performance of the Nonbank Financial Industry (LKNB)

The LKNB generally recorded a slowdown in assets growth in line with the slowdown in economic growth in 2015. Financing companies, insurance and pension fund companies recorded slower assets growth in 2015, reaching 1.3%, 4.6%, and 10.2%, respectively, or down compared to the previous year's figures of 5%, 17.1%, and 13.7%. Meanwhile, pawnshop services recorded brisker growth in assets in 2015, reaching 10.9%, or higher than 6.0% in the previous year. The better performance of pawnshop services was also seen in the brisker growth in pawnshop services financing which grew by 12.3%, or higher than the growth in 2014 of 5.3%. One of the factors driving the faster growth in pawnshop services financing was the stronger demand in the business sector, such as convection and contracting services companies, to obtain short-term capital each year by pawning their assets to be more productive.

On the side of financing provided by financing companies, the financing growth in 2015 slowed to -0.8% from 5.2% in 2014 in line with the slowdown in economic growth in 2015. Based on the type of financing, leasing still recorded negative growth of -5.0%, although still an improvement compared to -5.5% in 2014. Meanwhile, consumer finance and factoring recorded positive growth reaching 0.5% and 14.1%, respectively, or slowing from 10.2% and 22.3% in 2014. Based on the type of financing, consumer finance still dominated the financing of financing companies with a contribution of around 68.0% from the total financing, or up from 67.12% in 2014. Meanwhile, leasing is the second largest type of financing with a share at the end of 2015 of 29.0%, or slightly down from 30.3% in 2014. In nominal terms, the amount of financing during 2015 reached Rp363.3 trillion in the form of consumer financing (Rp247.1 trillion), leasing (Rp105.4 trillion), factoring (Rp10,7 trillion), and credit cards (Rp95.0 billion). As such, as in previous years, the focus of financing companies is still on consumer financing, especially short-term consumer financing.

From the risk side, as the economic growth slowed, the financing companies and insurance companies risk also increased, as reflected in the increase in the NPF ratio and the ratio of gross claims compared to gross premiums. The NPF ratio in the first half of 2015 rose slightly from 1.41% at the end of 2014 to 1.44% in June 2015. Despite the increase, the NPF ratio was still maintained at a low level in line with the intensification of efforts by financing companies to collect bad financing. Meanwhile, for the insurance companies, the increase in business risk was reflected in the ratio of gross claims to gross premiums in the first semester of 2015 which reached 71.3% or up from 62.4% in the second semester of 2014. Nevertheless, the insurance companies' liquidity risk was relatively well maintained as reflected in the still high ratio of current assets to current liabilities.

Chart 8.25. **Yield SBN 10 Years and Sentiment Factors in 2015**



Source: Bloomberg, processed

The Performance of the Bond Market

The performance of the bond market weakened in 2015, as reflected in the increase in the SBN yield. The 10-year SBN yield at the end of 2015 was recorded at 8.75%, up 95 bps compared to 7.80% at the end of 2014 (Chart 8.25). In the primary market, the performance of the SBN market also showed a decline as reflected in the SBN yield which trended upwards. The SBN yield for 1 year tenors which were last offered in 2015 were recorded at 6.94% or up from 6.82% at the end of 2014. The weaker performance reflected, at least in part, the global economic sentiment, especially related to the continued slowdown in China's economic growth, uncertainty in global financial markets, especially surrounding FFR hikes and yuan devaluation, along with monetary policy divergence among advanced economies. Meanwhile, domestically, the release of worse-than-expected economic growth data also had a negative impact on the performance of the bond market.

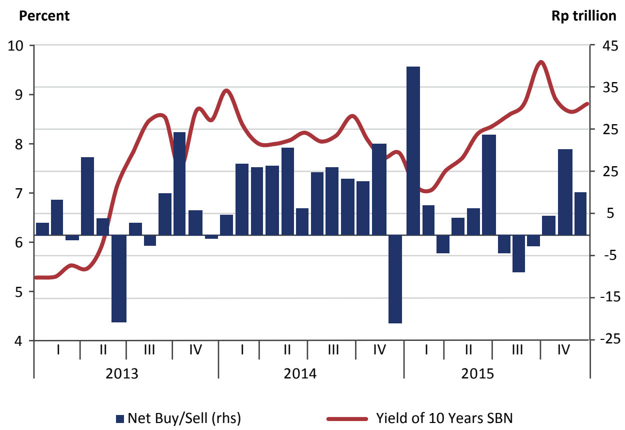
Bond market risk also increased in 2015 affected by declines in bond market performance indicators. This was reflected in increases in 10-year SBN yields in 2015. Besides that, the volatility of 10-year SBN yields in 2015 was recorded at 0.65 or up from 0.31 in 2014. Indonesia's Credit Default Swap (CDS) also deteriorated as reflected in the increase in the CDS from 160.31 at the end of 2014 to 222.92 at the end of 2015.

The market dynamics in 2015 were marked by an increase in the SBN yield in the first quarter or 2015 as investor confidence improved. This stronger optimism was a response to the policy mix of Bank Indonesia and the government in maintaining stability and undertaking structural reforms to promote further economic growth. BI policy which lowered the BI rate in February 2015 met with a positive response from the market with inflation expected to remain benign. Since the second quarter of 2015 to the end of 2015, the SBN showed weaker performance, as reflected in the SBN yield which continued to increase. Below market ecpectation economic growth in China, yuan devaluation policy by the People's Bank of China (PBoC), and mounting fears of FFR hikes, following the release of stronger U.S. data and manufacturing, created negative sentiment which pushed up SBN yields.

The uptrend in SBN yields could be contained thanks to the coordination of Bank Indonesia and the Government through its policy mix in facing pressures in the financial markets. The Government's policy packages, especially the Government's policy package No. 2 on 9 September 2015 (which was focused on improving the investment climate and maintaining stability of the rupiah exchange rate) had a positive impact on lowering SBN yields. In the same period, easing concerns on FFR hikes in line with the release of Nonfarm Payroll (NFP) data which unlike the market had predicted posted a decline, also helped push down SBN yields further. Nonetheless, the SBN yield at the end of 2015 was recorded at 8.75% or up 95 bps compared to 7.80% at the end of 2014.

The performance of the SBN market in 2015 which tended to weaken was also reflected in the weaker activities of non-resident investors who purchased SBN. During 2015, non-resident investors were net buyers in the SBN market to the tune of Rp96.1 trillion, or less than the figure of Rp137.5 trillion in 2014. In the first quarter of 2015, non-resident investors actually undertook quite large

Chart 8.26. SBN Yield and Net Foreign Buy/Sell

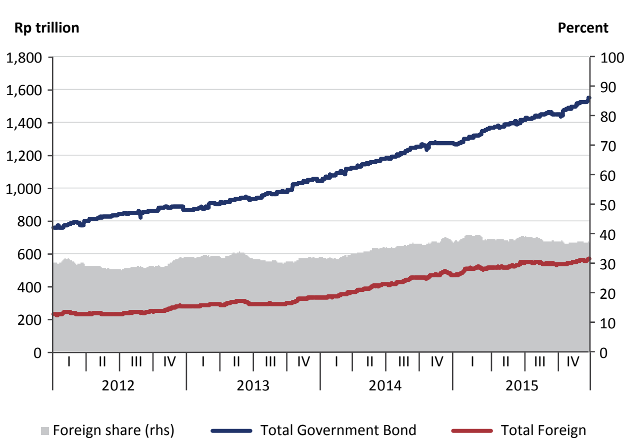


Source: Bloomberg, processed

net buying which reached Rp42.7 trillion as optimism improved in response to the policy mix of Bank Indonesia and the Government (Chart 8.26). Nonetheless, in the third quarter of 2015, non-resident investors were net sellers due to greater uncertainty in the global financial markets arising from weaker-than-expected economic growth in China, devaluation of the yuan, along with mounting concerns of FFR hikes. These conditions changed in the last quarter of 2015 as the uncertainty in the global financial markets eased thanks to growing optimism as steps to stabilize the rupiah were taken by Bank Indonesia and a series of economic policy packages were taken by the government.

The role of non-resident investors in the SBN market was still quite big. The share of non-resident investor holdings in the SBN market during 2015 was relatively stable

Chart 8.27. Share of Foreign Investor Ownership on the Government Securities



Source: Ministry of Finance, processed

at around 37%. On average, the share of non-resident investor holdings in the SBN market in 2015 was recorded at 37.4%, or up from 34.5% in 2014 (Chart 8.27). The fairly large contribution of non-resident investors in SBN holdings has implications on the strength of the external factors influencing the dynamics of the SBN market as well as translating into higher risks should there be a reversal of sentiment.

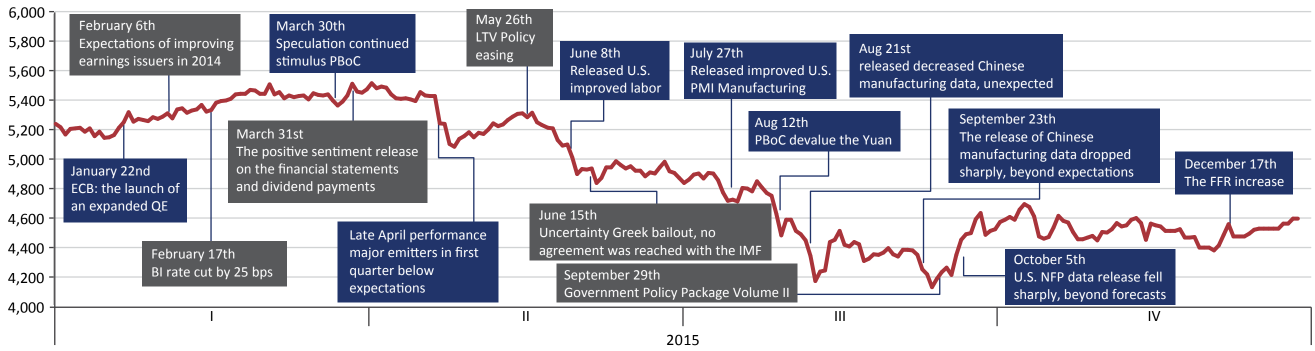
The Performance of the Stock Market

The domestic stock market also showed weaker performance, as reflected in the declines in the JCI to 4,593.01 at the end of 2015, or down 12.13% from its level at the end of 2014 of 5,226.95. In the first quarter of 2015, the JCI managed to eke out gains on better corporate earnings expectations for 2014 and positive sentiment on the release of financial reports and dividend payments by listed companies. Meanwhile, positive sentiment from global economic developments at the beginning of 2015 also helped push up the JCI. This positive sentiment on the external front included the launch of ECB policies at the end of January 2015 to expand QE and speculation of a further stimulus by the PBoC at the end of March 2015.

Stock market risk also showed an increase in 2015, as reflected in the declines in the JCI and increased JCI volatility. The JCI volatility in 2015 was recorded at 407.7, or up from 256.3 in 2014. This increased volatility owed, at least in part, to the dynamics of the JCI which showed a downtrend starting in the second quarter of 2015. In the second quarter until the end of 2015, the performance of the JCI weakened. Beginning with the negative sentiment on the performance of blue chips in the first quarter of 2015 which was below expectations, the JCI started to show a downward trend at the beginning of April 2015. Meanwhile, from the external side, negative sentiment from several factors which hit the bond market also weighed on stock prices (Chart 8.28).

The policy mix of Bank Indonesia and the government was able to stem the declines on the JCI. Like in the bond market, the downtrend in the JCI could be arrested thanks to coordination between Bank Indonesia and the government through its policy mix in facing financial market pressures, including government policy packages, especially the Government's policy package No.2 dated 9 September 2015. Easing market concerns in relation to the expected postponement of FFR hikes in October 2015 also helped push the JCI higher at the end of 2015. Nevertheless, overall in 2015, the IHSG reached 4,593.01

Chart 8.28. **JCI and Sentiment Factors in 2015**

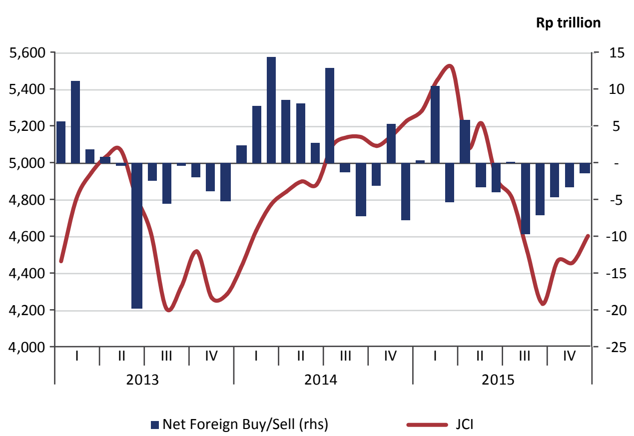


Source: Bloomberg, processed

at the end of 2015, or down 12.13% from its level at the end of 2014 of 5,226.95.

The weaker performance of the stock market in 2015 was also reflected in the high level of net selling by non-resident investors in the stock market. In 2015, non-resident investors were net sellers in the stock market to the tune of Rp22.6 trillion, while in 2014, non-resident investors undertook Rp42.6 trillion of net buying (Chart 8.29). Looking at the quarterly dynamics, in the first quarter of 2015, non-resident investors still undertook net buying of Rp5.4 trillion, supported by positive sentiment in the stock market, including better expectations of corporate performance, benign inflationary expectations, as well as ECB policy at the end of January 2015 to expand QE. Nonetheless, since the second quarter of 2015, selling pressure by non-resident investors increased

Chart 8.29. **JCI and Net Foreign Buy/Sell**



on the back of negative sentiment, especially from the external side, including devaluation of the yuan, mounting concerns of FFR hikes, and weaker-than-expected economic growth in China. As in the bond market, net selling pressure started to ease, especially in the last quarter of 2015, as uncertainty in the global financial markets started to recede and domestic developments started to improve. Since the second quarter of 2015 until the end of the year, non-resident investors undertook Rp26.6 trillion of net selling.

The role of non-resident investors was still quite large in the stock market. The share of non-resident investors (buying) in trading value was fairly volatile, yet fairly large (>30%). On average, the share in trading value of non-resident investors in the stock market in 2015 was recorded at 42.2%, or slightly up from 42,0% in 2014. The fairly large contribution of non-resident investors in trading value reflects the strength of the external factors influencing the dynamics of the stock market as well as the sizeable risk of a reversal in the stock market.

Nonbank Financing

Nonbank financing increased in 2015 but with a declining share of the financial sector. Nonbank financing in 2015 reached Rp136.1 trillion, or up from Rp111.4 trillion in 2014 (Table 8.2). The nonbank financing in 2015 was mostly undertaken by non-finance sector companies such that the share of the financial sector declined. The decline in the share of the financial sector was mostly seen in financing through the stock market. This decline in the share of the financial sector in the stock market (or the greater role of the non-financial sector) is an

Table 8.2. **Total Non-Bank Financing**

indicators	2014	2015
Total Non-Bank Financing	**111.4**	**136.05**
Total o/w Financial Sector Issuers	52.3	60.4
Share of Financial Sector (%)	47.0	44.4
Stock	**47.7**	**53.5**
Stock o/w Financial Sector Issuers	9.8	3.9
Share of Financial Sector (%)	20.5	7.3
Bonds and Sukuk	**48.7**	**62.4**
Bond o/w Financial Sector Issuers	33.4	42.3
Share of Financial Sector (%)	68.5	67.7
MTN and Promissory Notes + NCD	**14.9**	**20.1**
MTN, NCD o/w Financial Sector Issuers	9.2	14.2
Share of Financial Sector (%)	61.3	70.6

Source: OJK and KSEI, processed

indication of the deepening of financing through the stock market. Meanwhile, the share of the financial sector was still dominant in other nonbank financing, either through bonds or through Medium-term Notes (MTN) and Negotiable Certificates of Deposit (NCD).

Nonbank financing either through the stock market, bond market or corporate sukuk along with the MTN market and NCD showed an increase in 2015 compared to the previous year. This increase could at least in part be attributed to the more stringent lending standards of banks in channelling loans which was in accordance with the increased lending risk perceptions of banks. This condition encouraged companies to use alternative financing besides loans, either from the stock market, bond market or corporate sukuk, along with the MTN market and NCD.

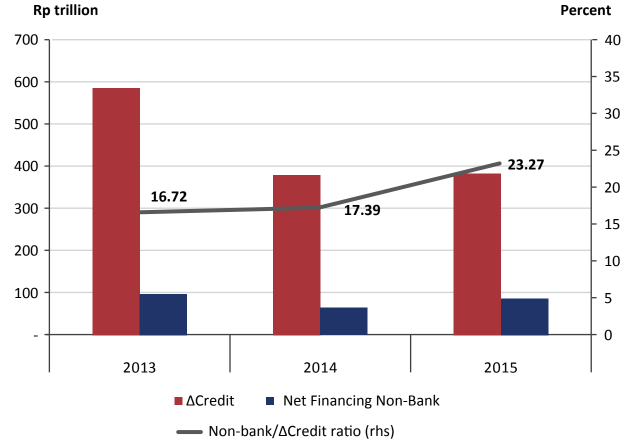
The amount of financing in the stock market in 2015, either through rights issues or Initial Public Offerings (IPO), reached Rp53.5 trillion, or up 12.3% compared with Rp47.7 trillion in 2014. The increase in financing in the stock market was supported by an increase in financing either through rights issues or IPO. Financing from rights issues in the primary market reached Rp42.3 trillion, or up by 7.3% from Rp39.2 trillion in 2014. Meanwhile, the amount of financing through Initial Public Offerings (IPO) was recorded at Rp11.3 trillion, or up 35.8% from Rp8,3 trillion in 2014 (Table 8.3). The increase in financing through the stock market was driven by companies in the infrastructure, property, consumer goods industry, and mining sectors. The increase in financing in the stock market came on the back of expectations of improving economic conditions in Indonesia, especially related to renewed economic growth momentum in the third quarter of 2015.

The issuance of corporate bonds and sukuk in 2015 reached Rp62.4 trillion, or up 28.1% from Rp48.7 trillion in 2014 (Table 8.4). After taking into account the maturing corporate bonds and sukuk, the net issuance of corporate bonds and sukuk during 2015 reached Rp26.9 trillion, an increase by more than threefold compared to the net issuances in 2014 of Rp7.1 trillion. The increase in financing through corporate bonds in 2015 mainly originated from companies in the infrastructure and finance sectors. The increase in issuances of corporate bonds, as alternative nonbank financing, appears to be related to the relatively low interest rates for bond issuances compared to bank lending rates in 2015.

Meanwhile, issuances of MTN and NCD during 2015 reached Rp20.1 trillion, or rise by 34.6% from Rp14.9 trillion in 2014. Nevertheless, the relatively high level of MTN and NCD issuances stems, at least in part, from the relatively high amount of MTN and NCD which fell due in 2015. As such, some of the MTN and NCD issuances are to replace the maturing MTN and NCD in 2015. After taking into account the maturing MTN and NCD, issuances of MTN and NCD in 2015 only reached Rp8.9 trillion, or down from Rp11.5 trillion in the previous year. Like in the previous year, issuances of MTN and NCD were dominated by companies operating in the financial sector.

The role of nonbank financing increased in 2015. Overall, the ratio of nonbank financing and bank lending in 2015 was recorded at 35.4%, or higher than the ratio in 2014 of 29.2% (Chart 8.30). The increasing trend was also

Chart 8.30. **Credit Changes and Net Financing Non-Bank**



Source: OJK, processed

Table 8.3.	IPO Financing and Right Issue

IPO

Sectoral	Realization of 2014			Realization of 2015		
	Number of Issuers	Value*	Share (%)	Number of Issuers	Value*	Share (%)
Agriculture	1	0.2	2.4	-	-	-
Mining	1	0.3	3.9	1	0.8	7.4
Basic Industry	2	1.8	21.8	-	-	-
Various Industry	-	-	-	2	0.3	2.6
Consumer Goods Industry	1	0.1	1.2	1	0.9	7.7
Property and Real Estate	1	0.4	5.2	5	3.5	30.7
Infrastructure, Utilities, and Transportation	4	3.2	38.8	-	-	-
Finance	6	0.5	6.1	3	0.1	1.2
Trade, Services, and Investment	4	1.7	20.6	3	5.7	50.3
Total	**20**	**8.3**	**100**	**15**	**11.27**	**100**

Right Issue

Sectoral	Realization of 2014			Realization of 2015		
	Number of Issuers	Value*	Share (%)	Number of Issuers	Value*	Share (%)
Agriculture	1	10.8	27.6	-	-	-
Mining	3	1.9	4.9	1	5.4	12.7
Basic Industry	2	6	15.4	2	0.7	1.6
Various Industry	-	-	-	-	-	-
Consumer Goods Industry	-	-	-	1	20.8	49.2
Property and Real Estate	-	-	-	4	11.2	26.5
Infrastructure, Utilities, and Transportation	4	4.9	12.6	-	-	-
Finance	8	9.3	23.6	10	3.8	8.9
Trade, Services, and Investment	3	6.3	16	1	0.4	1.1
Total	**21**	**39.2**	**100**	**19**	**42.25**	**100**

*) in Rp trillion
Source: OJK, processed

still valid if the refinancing of maturing bonds, MTN and NCD which had a fairly large proportion were taken into account. After taking into account these factors, the ratio of nonbank financing to bank lending in 2015 still recorded an increase, up from 17.4% in 2014 to 23.3% in 2015. The increase in the ratio of nonbank financing to bank lending was also partly due to the decline in the channeling of loans.

Table 8.4. Corporate Bond and Sukuk Funding

Bond

Sectoral	Realization of 2014			Realization of 2015		
	Number of Issuers	Value*	Share (%)	Number of Issuers	Value*	Share (%)
Agriculture	-	-	-	-	-	-
Mining	-	-	-	-	-	-
Basic Industry	1	1.7	17.6	-	-	-
Various Industry	-	-	-	-	-	-
Consumer Goods Industry	1	2	20.7	-	-	-
Property and Real Estate	1	0.5	5.2	1	0.3	10.7
Infrastructure, Utilities, and Transportation	2	2	20.7	-	-	-
Finance	5	3.5	35.8	3	2.5	89.3
Trade, Services, and Investment	-	-	-	-	-	-
Total	**10**	**9.6**	**100**	**4**	**2.8**	**100**

Sustainable Public Offering of Bonds/Sukuk

Sectoral	Realization of 2014			Realization of 2015		
	Number of Issuers	Value*	Share (%)	Number of Issuers	Value*	Share (%)
Agriculture	-	-	-	-	-	-
Mining	-	-	-	-	-	-
Basic Industry	-	-	-	-	-	-
Various Industry	-	-	-	-	-	-
Consumer Goods Industry	1	0.25	0.6	1	0.5	0.8
Property and Real Estate	4	2.9	7.4	7	4.9	8.3
Infrastructure, Utilities, and Transportation	3	4	10.2	4	12.5	21
Finance	20	29.9	76.6	29	39.8	66.7
Trade, Services, and Investment	3	2	5.1	3	1.9	3.2
Total	**31**	**39.1**	**100**	**44**	**59.62**	**100**

*) in Rp trillion
Source: OJK, processed

Box 8.1 Strengthening of the Financial Sector Through Implementation of International Standards Regulation

Indonesia as a member of several international forums such as G-20[1], the Financial Stability Board (FSB), or the Basel Committee on Banking Supervision (BCBS) is bound by commitments to follow a number of international assessments. These assessments are aimed at assessing the resilience of the financial system to shocks and adherence to international standards. In 2016, Indonesia will face two international assessment processes, namely: the Financial Sector Assessment Program (FSAP) and the Regulatory Consistency Assessment Program (RCAP).

Financial Sector Assessment Program (FSAP)

FSAP is aimed at assessing the developments and stability of a country's financial sector in a comprehensive manner. Indonesia's participation in FSAP demonstrates Indonesia's commitment as a member of G-20 and FSB. Members of these two forums are required to follow the implementation of FSAP once every five years[2]. The FSAP which will be carried out in 2016 is the second FSAP, after the first FSAP in 2009/2010.

FSAP will assess the stability and health of the financial sector, whilst also assessing the potential contribution of the financial sector on growth and development. FSAP does not evaluate the health of individual financial institutions, and is not aimed at predicting or avoiding financial crises. Instead FSAP seeks to identify the source of the main vulnerabilities which can trigger crises in the financial sector.

Assessments of the financial sector stability will be carried out by undertaking reviews of the resiliency of the banking and nonbank sectors; stress-testing; systemic risk analysis including linkages between banks and nonbanks along with domestic or cross-border spillover; the microprudential and macroprudential framework; the quality of bank and nonbank supervision; oversight of Financial Market Infrastructure – FMIs; and evaluation of financial safety nets to effectively respond to systemic pressures. In relation to development aspects, FSAP assesses the need to develop institutions, markets, infrastructure, inclusivity; the quality of the legal framework and the payments system along with settlement; the identification of obstacles to competition and sector efficiencies; matters related to financial inclusion and retail payments; along with assessing its contribution to economic growth and development.

Bank Indonesia plays a crucial role in implementing FSAP 2016. This is considering that the FSAP coverage after the global financial crisis emphasised assessments of the macroprudential framework which is the authority of Bank Indonesia. Besides that, assessments of FMIs in the payments system also came under the authority of Bank Indonesia. In the macroprudential area, FSAP assessments were undertaken facing the macroprudential framework with coverage including the following: systemic risk in Indonesia's financial system, tools for identifying and monitoring systemic risk, the macroprudential framework along with implemented policies, linkages between the financial sector and institutions along with potential spillover, and institutional arrangement in jurisdictions. Besides that, assessments of the stress testing undertaken will also be reported in reports which focus on discussing stress-testing issues. In relation to the Payments System, the Payments System infrastructure which is organized by Bank Indonesia is considered as financial markets infrastructure (the payments system and securities settlement system) that must meet international standards for FMIs. FSAP assessments in the area of FMIs are aimed at seeing the effectiveness of the oversight FMIs framework or developments in regard to implementation of Principles for Financial Market Infrastructure. The usefulness of FSAP for the public including other national authorities along with investors is as a baseline assessment toward financial system stability in a particular jurisdiction. Because of that, FSAP is a strategic and crucial assessment for Indonesia. The results of FSAP assessments will become feedback for the authorities in Indonesia to improve the resiliency and stability of Indonesia's financial system going forward.

1 The G-20 members are Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, the U.K., the United States, and the European Union (represented by the European Commission and the European Central Bank).

2 Countries which are not G-20/FSB members yet designated by the IMF as countries with systemically important financial sectors are also required to join FSAP every five years. The list of countries with systemically important financial sectors and which are required to follow assessments is determined based on the size and interconnectedness of those countries' financial sectors. Countries deemed to have systemically important financial sectors by the IMF are Australia, Austria, Brazil, Belgium, Canada, China, France, Germany, Hong Kong, India, Ireland, Italy, Japan, Luxemburg, Mexico, the Netherlands, Russia, Singapore, South Korea, Spain, Sweden, Switzerland, Turkey, the U.K., the United States.

Regulatory Consistency Assessment Program (RCAP).

RCAP is the response from BCBS to the lessons learnt from the global financial crisis concerning the importance of implementing the Basel framework which is comprehensive, on time, and consistent. BCBS takes the view that public confidence in the resilience of the banking system, the effectiveness and public confidence in prudential ratios, and a level playing field cannot be expected, unless the Basel framework (the framework of Basel II, II.5, and III which will subsequently be referred to as the Basel III framework) is adopted and consistently implemented.

The purpose of implementing RCAP is to ensure the consistent implementation of the Basel III framework such that it can make a contribution toward global financial stability. RCAP consists of two different areas yet which are complementary, namely: i) monitoring the timeliness of adoption of the Basel III standards and ii) evaluating the consistency and completeness of the adoption of the Basel III standards, including evaluation of the significance of any deviation in the domestic regulatory framework with the Basel III standards. The findings of the assessments are expected to be able to provide insights concerning any existing or potential gaps in the domestic regulation toward financial stability. This feedback is expected to be able to help jurisdictions to make necessary reforms such that domestic regulations are more in line with Basel standards.

Prior to 2016, the scope of RCAP's focus included assessments on the adoption of the Basel III capital framework, the Liquidity Coverage Ratio (LCR), and the Systemically Important Banks (SIBs) framework. Assessments of the Basel III capital framework had already begun in 2012 so that nearly all BCBS member countries have already finished assessments on the consistency and completeness of their domestic regulation toward the Basel III capital framework. For LCR, the initial assessments were carried out in 2014 with assessments on the LCR of BCBS member jurisdictions which were issued in 1Q 2015. Meanwhile, for the SIBs framework, new assessments have been carried out since 2015. In line with the developments of the adoption of other Basel standards in accordance with the timeline already set by BCBS, the scope of RCAP will be widened starting in 2017, i.e. that is to also include the assessment of the consistency and completeness of the adoption of the standards for the Net Stable Funding Ratio (NSFR) and the Leverage Ratio.

RCAP for the purpose of monitoring the timeliness of the adoption of Basel III standards has already been followed by Indonesia on a regular basis every year. Meanwhile, RCAP for the purpose of evaluating the consistency and completeness of the adoption of Basel III standards in Indonesia will be followed by Indonesia for the first time in 2016. The scope of RCAP in Indonesia for the purpose of assessing the consistency and completeness of Indonesia's regulations includes the Basel III capital framework and LCR. In this regard, Bank Indonesia actively participates in regulation of macroprudential matters, such as regulation concerning the obligation to form a Countercyclical Capital Buffer (CCB) which was also the scope for Basel III capital framework. Besides that, Bank Indonesia also became a member of the RCAP Indonesia team for nearly all areas evaluated in RCAP. This is because the assessments toward the consistency and completeness of Indonesia's regulations compared with Basel III were also scrutinized by Bank Indonesia as the macroprudential authority.

The findings from RCAP will become feedback for the authorities of Indonesia's financial sector to coordinate the regulatory framework with the Basel framework. Nonetheless, Indonesia's specific characteristics still need to be given attention in order to strengthen the regulatory regime in Indonesia. With RCAP feedback, it is hoped that the resilience of the banking system can be improved further, an important matter in increasing the resilience of Indonesia's financial system.

Throughout 2015, Bank Indonesia consistently instituted various payment system and rupiah currency management (SPPUR) policies. In terms of rupiah currency management policy, Bank Indonesia provided mobile cash services to meet the demand for currency of appropriate denominations, on time and fit for circulation.

Chapter 9

Payment System and Currency Management

In 2015, payment systems and currency management were operated efficiently and smoothly, both by Bank Indonesia and the industry. On the side of payment system operated by Bank Indonesia, this was reflected in the reliability and availability of its systems, as well as in its effective contingency plans. Meanwhile, the operation of payment systems by industry also experienced no significant disruptions. In terms of currency management, the demand for cash was satisfied by the availability of currency in sufficient quantities, in appropriate denominations, in a timely manner, and in a condition fit for circulation.

Over the course of 2015, national payment systems performed well in supporting economic activities as well as the stability of the financial and monetary systems. The performance of the payment systems operated by Bank Indonesia was reflected in their reliability and availability as well as in the implementation of effective contingency plans that enabled Bank Indonesia's payment system services to process smoothly financial transactions associated with the economic activities carried out by the public, government, and business. Furthermore, payment systems operated by industry endured no significant disruptions. Meanwhile, in terms of currency management, positive achievements were reflected in the availability of currency in sufficient quantities, in appropriate denominations, in a timely manner, and in a condition fit for circulation. The efforts of Bank Indonesia to continue strengthening its policies in the field of payment systems and currency management played an integral part in maintaining the performance of national payment systems. In terms of payment systems, Bank Indonesia continued to focus on strengthening its infrastructure in order to improve the reliability and security of its payment systems. In addition, during 2015 Bank Indonesia implemented five integrated general policies aimed at strengthening currency management. These were to maintain sufficient Bank Indonesia cash position, to improve the quality of currency circulating in society, to expand its cash distribution network and cash services, to strengthen communication as to the characteristics of authentic currency, and to step up efforts to prevent and counter the circulation of counterfeit rupiah banknotes.

In terms of payment systems, the value of transactions performed through the payment systems operated by Bank Indonesia and the payment system industry over 2015 grew slower at 9.4%, compared to the previous year's figure of 11.0%, in line with the slowdown in domestic economic growth. Meanwhile, the volume of transactions grew by 18.6% from the previous figure of 18.0%. During 2015, national payment systems managed to process 5.5 billion transactions with a value of Rp33.3 thousand trillion. As to the value of transactions performed through the payment systems operated by Bank Indonesia alone, this increased by 9.1%, slightly smaller than the previous increased of 9.8%.

Furthermore, with respect to the payment system industry, Bank Indonesia pursued a policy of expanding the use of non-cash payment systems and instruments, including card-based payment instruments (CBPIs), electronic money, and fund transfers. The effort to expand the use of non-cash payment systems and instruments by Bank Indonesia sought to create synergies with the Government and the payment systems industry. In addition to the policy of expanding the use of non-cash payment systems and instruments, Bank Indonesia also sought to continually encourage the payment system industry to improve the security of its payment system operations. This was done in order to maintain public confidence in non-cash payment systems and instruments. This policy had positive results as evidenced by an increase in payment transactions using non-cash payment systems and instruments.

On the currency management front, the amount of currency in circulation (UYD) grew at a higher rate compared to the previous year's 5.7%, reaching 11.0%, or Rp586.8 trillion, by the end of 2015. In terms of trends, the dynamic of UYD growth in line with developments in economic activities. Growth in currency started to slack by mid-2015 but, subsequently, began increasing in the third quarter of the year in line with improving domestic economic growth. This upward trend in UYD growth was also confirmed by the withdrawal of currency (outflows) by State Budget distributing banks, which began to increase in the same period on the back of improvements in government consumption growth. Meanwhile, cash in vault slowed in line with the stagnant growth of bank deposits over 2015. Nevertheless, consistent with these economic dynamics, Bank Indonesia was still able to provide currency in sufficient quantities, in appropriate denominations, in a timely manner, and in a condition fit for circulation.

To ensure the sufficient availability of currency and its denominations, a variety of important measures were taken. These included encouraging money printing companies to increase their printing capacities, increasing the number of Cash Custodians (Kas Titipan) in areas previously unreached by Bank Indonesia's cash services, and enabling the exchange of money through Mobile Cash units in crowded places, as well as in rural areas and the outermost islands in the Republic of Indonesia. The number of bank branches providing Cash Custodian services rose from 30 in 2014 to 35 by the end of 2015, meaning that the coverage of Bank Indonesia's cash services increased from 61% of all cities/regencies in Indonesia in 2014 to 66% in 2015. Bank Indonesia also applied a clean money policy through improving the quality standards of its money treatment process (improved soil level) in both Bank Indonesia cash working units and in banks, in order to improve the quality of currency in circulation in society. In addition, to further protect the public, Bank Indonesia bolstered its coordination with all elements of the Coordinating

Agency for Eradication of Counterfeit Money (Botasupal) and other relevant government agencies through a variety of education activities aimed at familiarizing the public with the characteristics of authentic rupiah banknotes, while also stepping up efforts to prevent and counter the circulation of counterfeit rupiah banknotes. The various currency management policies pursued by Bank Indonesia showed good results. This was reflected, among other ways, in an improved quality level of currency circulating in society and increased public awareness and bank compliance in reporting the discovery of counterfeit rupiah to Bank Indonesia, as well as the disclosure of counterfeit currency supply networks by the Indonesian Police before this money made its way into public circulation.

9.1. PAYMENT SYSTEM PERFORMANCE

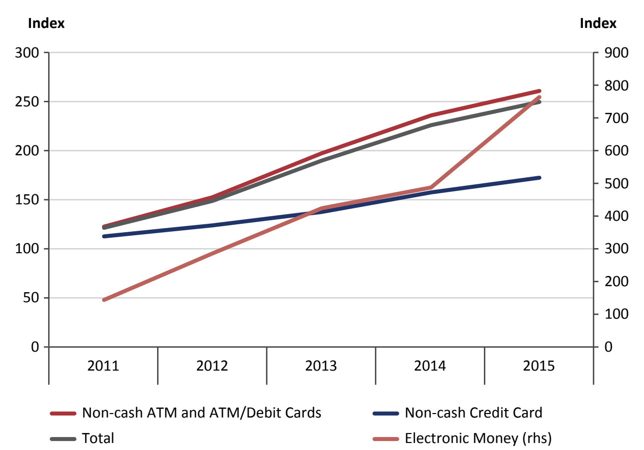
In general, the payment systems operated by Bank Indonesia ran efficiently and smoothly, in 2015. This was the result of Bank Indonesia's efforts to strengthen payment system infrastructure and to implement an effective continuity plan. These policies was designed so that the payment systems operated by Bank Indonesia would be always available and able to process the financial transactions associated with the economic activities carried out by the public, government, and business.[1] In addition, improvements were made to Business Continuity Management (BCM) and Standard Operating Procedures (SOP) as part of the Business Continuity Plan for Bank Indonesia's payment systems. Similarly, the payment systems operated by the banking industry also ran efficiently and smoothly. Bank Indonesia, along with the Government and banking industry, consistently encouraged the expansion of public access to non-cash payment instruments, as a follow-up on the declaration of the National Non-Cash Movement (GNNT) in 2014.

Bank Indonesia's policies, which for the most part were consistently geared towards maintaining public confidence in non-cash payment instruments, achieved ever more positive results. This was reflected in the increasing number of non-cash payment instruments within society and the growing proliferation of transactions using these types of instruments. In addition to efforts to maintain public confidence in non-cash payment instruments, Bank Indonesia also took measures to broaden public access to these instruments. These measures saw an increased use of non-cash payment instruments, as reflected in the rise of the non-cash payment system index. The public non-cash payment system index increased from 225 in 2014 to 249 in 2015 (Chart 9.1). The increase in this index serves as an indicator of the success of the measures taken after the declaration of the GNNT.

Looking at individual types of non-cash payment instruments, over the period from 2011-2015, the electronic money payment system index recorded the most marked improvement. This index increased from 142 in 2011 to 762 in 2015 (Chart 9.1). This dramatic increase was in part due to electronic money being the most recently developed non-cash payment instrument, but also due to the results of synergies between Bank Indonesia, the Government, and the banking industry. An example of such a synergy was the support Bank Indonesia gave to the Government to help it distribute social assistance program to the public (Government to Person funding), which was done using electronic money whereas previously such disbursements were made in cash. Furthermore, the indexes for credit cards and ATM cards (including ATM/debit cards) rose respectively from 112 and 123 in 2011 to 173 and 260 in 2015.

Furthermore, the support of retail payment systems in economic activity was demonstrated by the rising value of retail payment system transactions. Retail payment system transactions, consisting of the Bank Indonesia National Clearing System (SKNBI), Card-Based Payment Instruments (CBPIs), electronic money, and fund transfers, in 2015 enjoyed a 25.5% share of the total

Chart 9.1. Non-cash Payment System Index



1 In the first quarter of 2015 a malfunction occured in the Data Communication Network for accessing a payment system operated by Bank Indonesia. However, with the application of an effective continuity plan, the payment system service continued to operate properly.

Chart 9.2. Ratio of Retail Transactions to GDP

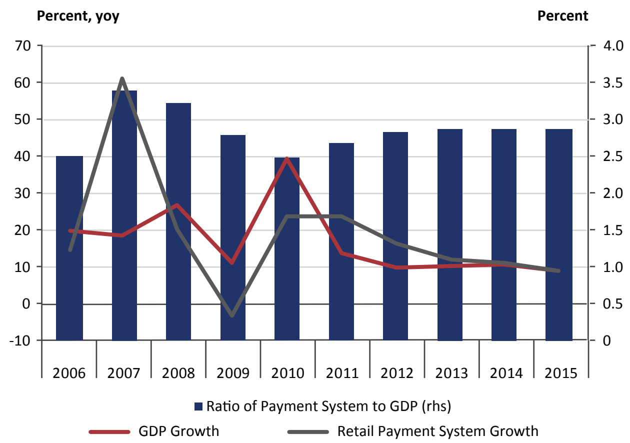
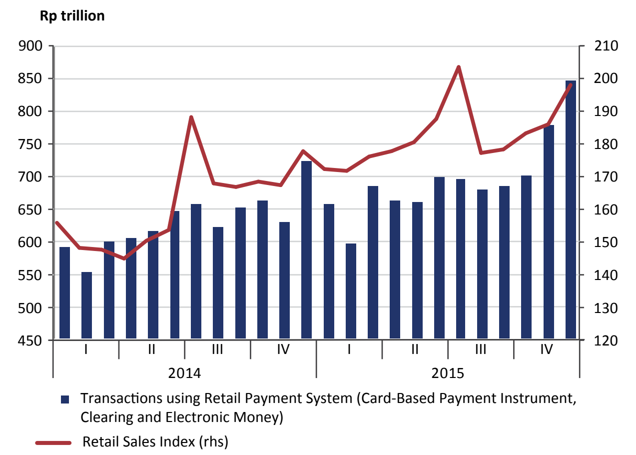
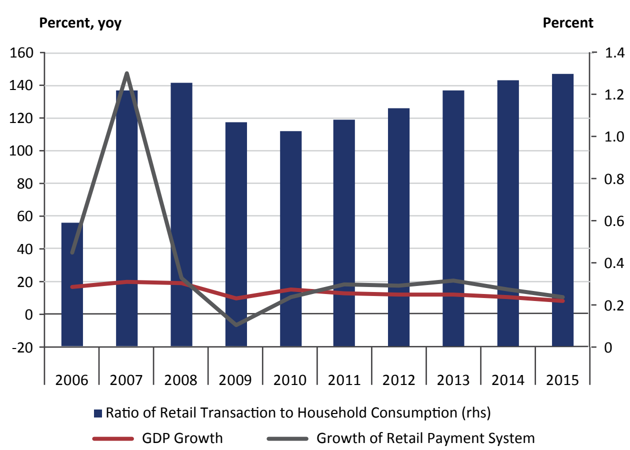


Chart 9.4. Retail Sales Index and Retail Transaction



value of payment system transactions which supported economic activity, amounting to Rp8.5 thousand trillion. Compared to the previous period, the value of retail payment system transactions represented an 11.7% increase from Rp7.6 thousand trillion. This increase was in line with the rise in the ratio of the value of retail payment system transactions to GDP, up from 0.72 in 2014 to 0.74 in 2015 (Chart 9.2). Meanwhile, the ratio of the value of retail payment system transactions to consumption also saw an increase, from 1.29 in 2014 to 1.31 in 2015. This indicates that people are growing increasingly accustomed to using non-cash payment instruments to finance consumption spending (Chart 9.3). These figures also confirm the strong relationship between the development of retail payment system transactions and the retail sales index (Chart 9.4).

Chart 9.3. Ratio of Retail Transaction to Household Consumption



Non-Cash Payment Systems Operated by Bank Indonesia

Bank Indonesia Real Time Gross Settlement (BI-RTGS)

Through the application of an effective continuity plan and infrastructure strengthening policy, the BI-RTGS system in 2015 generally ran smoothly and effectively. Among other things, this was reflected in the availability and capability of the BI-RTGS system as the estuary of all high value payments' settlement in Indonesia. Similarly, in terms of liquidity, participants in the BI-RTGS system retained sufficient funds to maintain successful transactions. Liquidity adequacy, among others, was reflected in the low level of unsettled transactions, the relatively small use of the Intraday Liquidity Facility (FLI) and the decline in turnover ratio.

The BI-RTGS system successfully settled 11.0 million transactions with a value of Rp112.7 thousand trillion over the course of 2015. This transaction volume represented a 37.8% decline from the previous period when 17.7 million transactions were settled. However, the value of the transactions represented a 1.7% increase over the previous period's figure of Rp110.9 thousand trillion. This increase in the value of BI-RTGS transactions was largely influenced by a rise in transactions between clients, foreign exchange transactions, and capital market transactions. Meanwhile, the average daily volume of transactions in the BI-RTGS system amounted to 45 thousand transactions at a value of Rp458.2 trillion (Chart 9.5).

The decline in the volume of payment transactions through the BI-RTGS system was brought about by the capping policy on the minimum transaction amount using the BI-RTGS

Chart 9.5. BI-RTGS Transaction

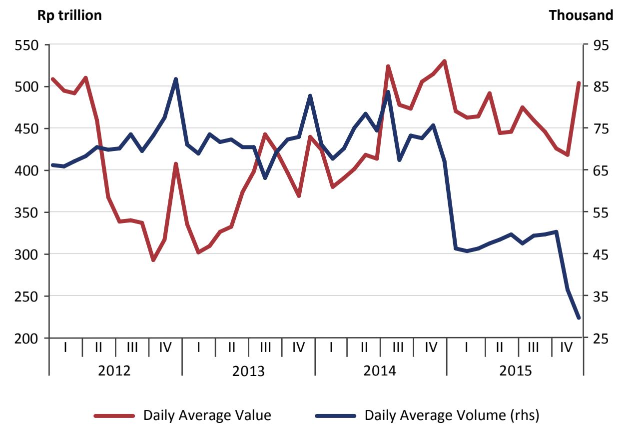
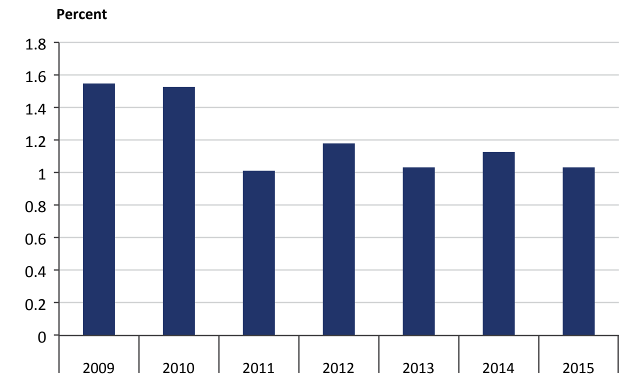


Chart 9.6. BI-RTGS Turn Over Ratio



system. The minimum transaction amount through the BI-RTGS system was raised to Rp500 million when the BI-RTGS Gen II System was implemented on 16 November, 2015. This represented an effort to mitigate operational risks at the early implementation of the BI-RTGS Gen II System. The enforcement of a minimum cap is only a temporary measure until the June 2016.

With respect to unsettled transactions, these were relatively few in 2015. In terms of transaction volume, unsettled transactions accounted for 0.004% of the total, while in terms of transaction value this figure was 0.027%. These relatively small percentages for unsettled transactions were the result of Bank Indonesia's policies which always seek to prioritize the importance of participants in the BI-RTGS system managing their liquidity. With such relatively small percentages, the unsettled transactions that did occur did not disrupt the smooth operation of the BI-RTGS system as a whole. With respect to the Intraday Liquidity Facility (FLI), there were only two occasions on which this was used in 2015. The low level of FLI usage coupled with the small proportion of unsettled transactions during 2015 indicated that, in general, participants in the BI-RTGS system retained sufficient funds to settle transactions. The liquidity adequacy of participants in BI-RTGS system was also reflected in the banking industry's turnover ratio indicator which decreased from 1.17 in 2014 to 1.04 in 2015 (Chart 9.6), illustrating a reduced dependence of participants on incoming transactions.

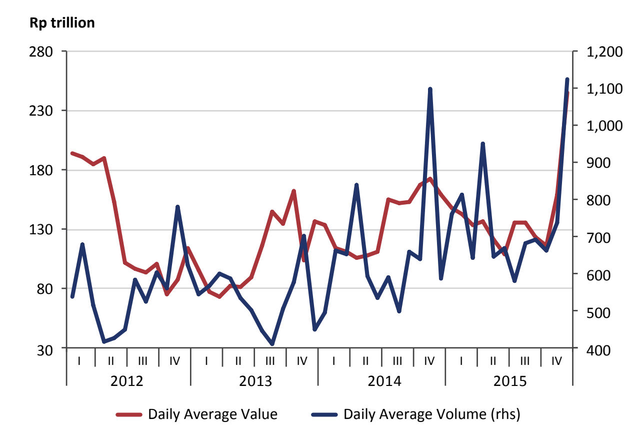
The Bank Indonesia Scripless Securities Settlement System (BI-SSSS)

During 2015, 183.6 thousand securities transactions were traded through BI-SSSS with a value of Rp34.9 thousand trillion. This volume represented a 15.2% increase over 2014 when 159.5 thousand transactions took place. In line with the increase in volume, the transaction value for securities in BI-SSSS of Rp34.9 thousand trillion represented a 4.1% rise from the previous figure of Rp33.57 thousand trillion. Meanwhile, in 2015 the average daily volume of BI-SSSS transactions was 747 with a value of Rp142.0 trillion (Chart 9.7).

The Bank Indonesia National Clearing System (SKNBI)

Over the course of 2015, 113.5 million SKNBI transactions were performed with a value of Rp3.2 thousand trillion.[2] This transaction volume represented an increase of 5.5%

Chart 9.7. BI-SSSS Transaction



2 SKNBI is an electronic funds transfer system that consists of debit and credit clearing in which the settlement of each transaction is conducted nationally.

compared to the SKNBI transaction volume in 2014 of 107.6 million transactions. The value of SKNBI transactions was also up 13.1% from the previous year's figure of Rp2.9 thousand trillion. The average daily volume of transactions performed through SKNBI stood at 441.2 thousand transactions with a value of Rp13.1 trillion (Chart 9.8). The rise in transactions through SKNBI was mainly due to the increased maximum credit clearing limit as well as the increase in the minimum transaction value limit through BI-RTGS from the previous Rp100 million to Rp500 million as of December 15, 2014, following the implementation of the BI-RTGS Generation II System in 2015.

Non-cash Payment Systems Operated by the Payment System Industry

Card-Based Payment Instruments (CBPIs)

The number of payment transactions with Card-Based Payment Instruments (CBPIs), which include ATM cards, ATM/debit cards, and credit cards, during 2015 showed an upward trend. The number of CBPIs used by the public increased by 12.5% to 137.1 million from the previous figure of 121.9 million instruments. Around 4.9billion transactions were performed using CBPIs in 2015 with a value of Rp5.2 thousand trillion. This represented a 12.1% rise in transaction volume from that in 2014 when 4.3 billion transactions were performed. The value of CBPIs transactions, meanwhile, increased by 10.2% over the value of such transactions in 2014. In terms of daily averages, the volume and value of CBPIs transactions in 2015 were recorded at 13.3 million transactions and Rp14.2 trillion per day respectively (Chart 9.9). The upward trend in CBPIs transactions was largely due to ATM card

Chart 9.8. **National Clearing (SKNBI) Transaction**

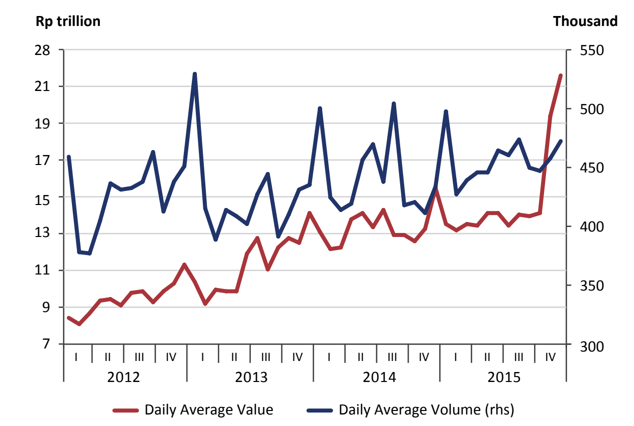
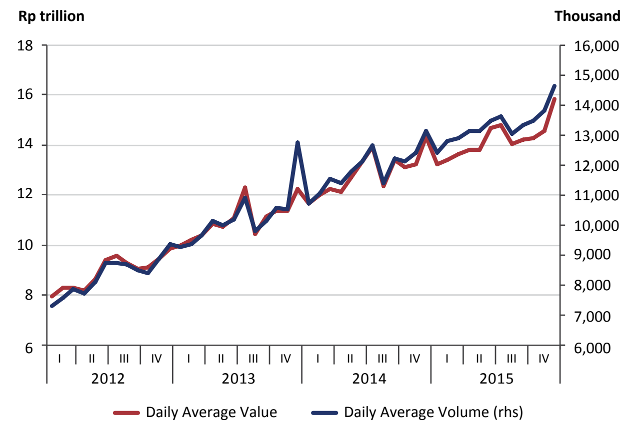


Chart 9.9. **Card Based Payment Instrument Transaction**



and ATM/debit card transactions. The increased volume and value of CBPIs transactions was supported by an increase in the supporting infrastructure for performing such transactions, like ATM and EDC machines. As of the end of 2015, there were approximately 97.8 thousand ATM units and 1 million EDC units in the country, an increase of 9.25% and 19.29% respectively from 2014, or in terms of numbers an additional 89.6 thousand ATM units and 842.6 thousand EDC units.

ATM Cards and ATM/Debit Cards

Bank Indonesia's policy of expanding the use of non-cash payment instruments showed positive results. This was reflected by an additional number of ATM cards and ATM/debit cards in circulation as well as an increase in transaction volume and value.[3] The number of ATM cards and ATM/debit cards in circulation in 2015 rose by 13.66% to 121 million cards from the previous year's figure of 105.8 million cards. In line with an increased number of cards in circulation, the number of transactions using ATM cards and ATM/debit cards also rose. Transaction volume went up by 12.18% to 4.9 billion transactions from the previous figure of 4.4 billion transactions. Furthermore, the value of transactions also increased by 10% to Rp4,897.7 trillion from the previous year's figure of Rp4,445.1 trillion. In terms of daily averages, the volume of ATM card and ATM/debit card transactions in 2015 stood

3 ATM Cards are a CBPI that can be used to make cash withdrawals and/or fund transfers. The obligation of the cardholder is fulfilled in real time by directly reducing funds saved in the cardholder's account. ATM/Debit Cards are a CBPI that can be used to make payments on obligations arising from economic activities, including spending transactions. The obligation of the cardholder is fulfilled in real time by directly reducing funds saved in the cardholder's account.

Chart 9.10. ATM and ATM/Debit Transaction

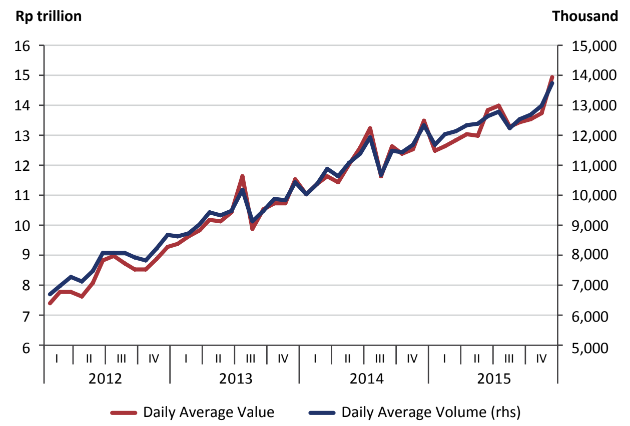
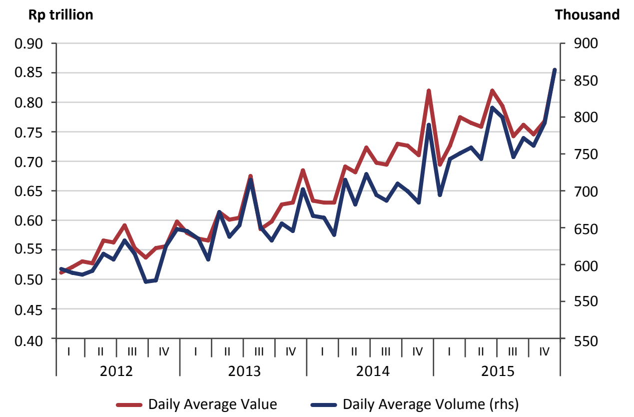


Chart 9.11. Credit Card Transaction



at 12.5 million transactions with a value of Rp13.4 trillion (Chart 9.10).

Credit Cards

The number of credit cards in circulation in 2015 stood at 16.9 million cards, up 5.1% from the previous figure of 16.0 million cards.[4] Meanwhile, the number of transactions using credit cards in 2015 was recorded at 281.3 million transactions with a value of Rp281.3 trillion. Credit card transaction volume showed growth of 10.62% from the previous year's volume of 254.3 million transactions. Likewise, the value of credit card transactions also rose by 10.0% from the previous year's value of Rp255.1 trillion. In terms of daily averages, the volume of credit card transactions in 2015 stood at 770.8 thousand transactions with a value of Rp768.6 billion per day (Chart 9.11).

By type of use, the proportion of cash advances rose in terms of both transaction volume and value. In 2015, the proportion of cash advances out of total credit card use, in terms of volume and value, stood at 2.4% and 2.7% respectively. This represented an increase from the 2014 levels of 1.5% and 1.9% respectively. The volume and value of cash advance transactions in 2015 amounted to 6,607 transactions with a value of Rp7.4 trillion. These figures were 80% and 55% higher than the respective figures recorded in 2014 of 3,777 transactions with a value of Rp4.9 trillion. Meanwhile, Non-Performing Loans (NPLs) remained in a relatively safe position despite a slight increase from 2.02% at the end of 2014 to 2.59% at the end of 2015 (Chart 9.12).

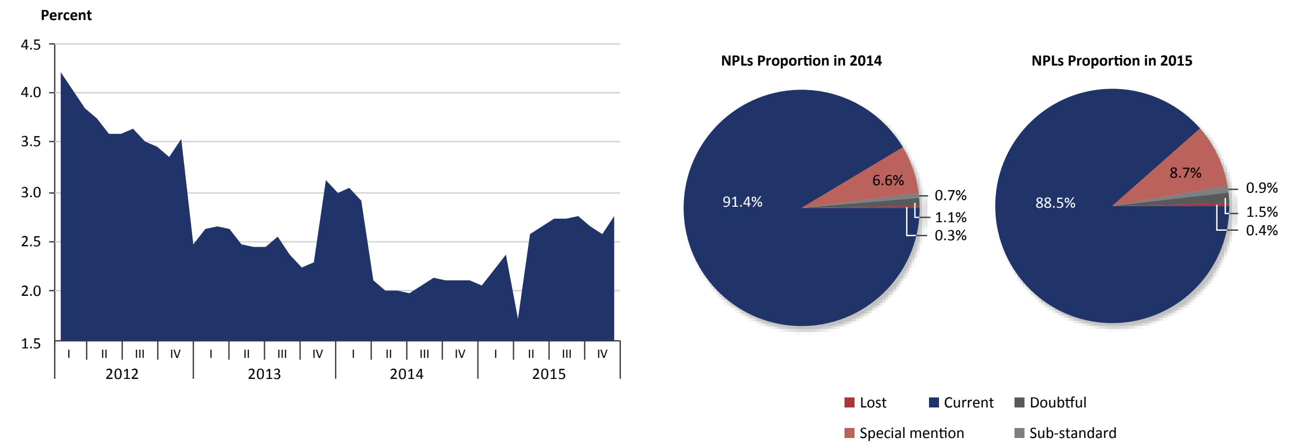
Electronic Money

In order to increase the use of payment system instruments, in particular retail instruments that can be used by the entire society, Bank Indonesia, together with the Government and the payment system industry, continued to encourage the use of electronic money. In 2015, the Government began distributing social assistance to people by means of electronic money, whereas previously this was done using cash.[5] In addition, the increased use of electronic money was also a result of the follow-up measures taken after the declaration of the National Non-Cash Movement (GNNT) in the previous period. These follow-up measures included the implementation of electronic parking transactions (e-Parking), the launch of the Bandung Smart Card, and the National Non-Cash Movement Festival. This range of measures managed to increase the number of electronic money instruments in circulation, as well as the volume and value of electronic money transactions.

4 Credit cards are a CBPIs that can be used to make payments on obligations arising from economic activities, including spending transactions and/or cash withdrawals, in which the obligation of the cardholder is fulfilled initially by the acquirer or issuer, and the cardholder undertakes to make payments at an agreed time, either all at once (charge card) or in instalments.

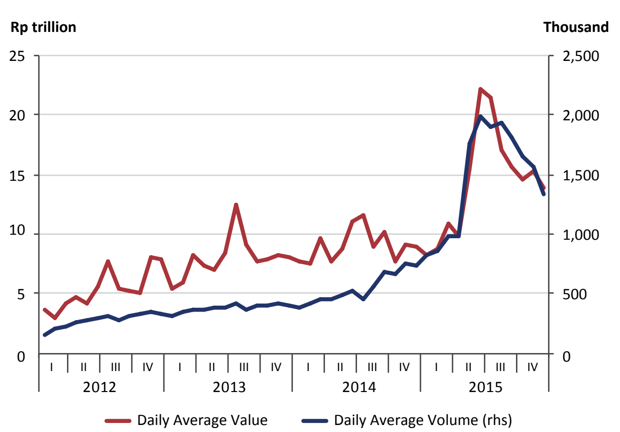
5 Electronic money is a payment instrument that involves the following elements (1) issued based on the amount of money paid initially by the user to the issuer; (2) the amount of money is stored electronically in media such as a server or chip; (3) used as a means of payment to merchants who are not electronic money issuers; and (4) the amount of electronic money paid by the user and managed by the issuer does not constitute savings as stipulated in the legislation governing banking.

Chart 9.12. NPLs of Credit Card



Compared with the position in 2014, the number of electronic money instruments in circulation in 2015 decreased by 4.0% to 34.3 million instruments from the previous period's 35.7 million instruments. This decline was caused by the removal of instruments associated with dormant accounts by electronic money issuers.[6] However, in contrast, the volume and value of electronic money transactions climbed significantly, amounting to a total of 535.6 million transactions and Rp5.3 trillion respectively. The positive growth reflected in these figures represented an increase in the volume and value of electronic money transactions of 163.4% and 59.1% respectively from the previous period's figures of 203.4 million transactions and Rp3.3 trillion. In terms of daily averages, the volume of transactions was recorded at 1.5 million transactions with a value of Rp14.5 billion per day (Chart 9.13). The improvement in electronic money transaction performance was greatly affected by regulations that required the use of electronic money for several transactions, included Jakarta Commuter Trains (KCJ) and the TransJakarta Busway, as well as measures by some companies to pay salaries via electronic money, and the distribution of government social assistance program to the public using electronic money.

Chart 9.13. Electronic Money Transaction



Nonbank Fund Transfer Operations

A total of 26.5 million fund transfers through nonbank fund transfer operators (TD BB) took place during 2015, with a value of Rp80.7 trillion.[7] The largest share of these fund transfers was made up of domestic fund transfers, which accounted for 57.4% of the total volume of transactions performed through nonbank fund transfer operators. Meanwhile, in terms of value, these transactions were dominated by incoming transactions with a 54.4% share of the total value (Chart 9.14). In order secure the transfer of funds from Indonesian migrant workers, Bank Indonesia sought to actively educate and familiarize prospective Indonesian migrant workers set to leave the country about fund transfers. Bank Indonesia also encouraged Indonesian migrant workers and prospective migrant workers to use non-bank fund transfer operators that have been licensed in their respective countries.

6 A dormant account is an account that is no longer active or has not been used for performing a transaction for a certain period of time.

7 A fund transfer consists of a series of activities that begin with an instruction from the sender of origin to move a certain amount of funds to a recipient named in the fund transfer instruction and end with the receipt of the funds by the recipient.

Chart 9.14. Share of Fund Transfer Transaction Volume and Value

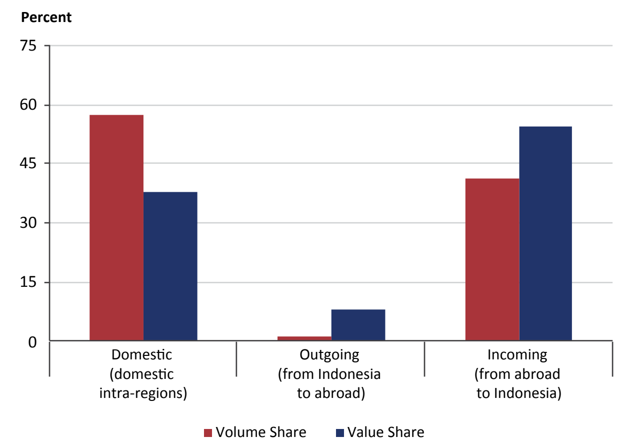
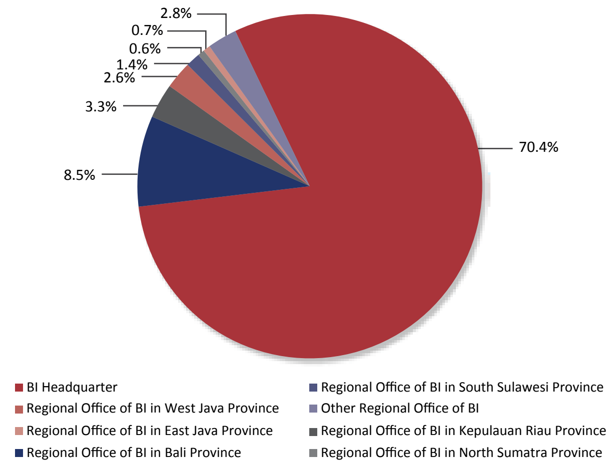


Chart 9.15. Share of Non-bank Operator in 2015



Nonbank Foreign Exchange Business Activities (KUPVA BB)

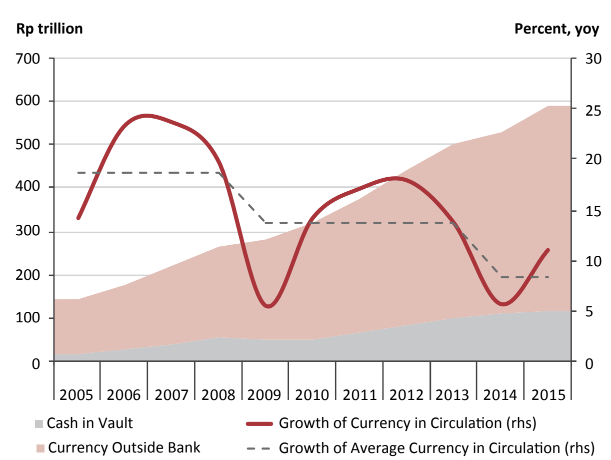
In 2015, the volume of sales and purchases of foreign banknotes (UKA) by KUPVA BB increased.[8] The value of such transactions increased 3.9% to Rp226.7 trillion from Rp218.0 trillion in 2014. The largest contribution to the buying and selling of UKA was made under the supervision of Bank Indonesia's Headquarters working area, amounting to Rp159.5 trillion or 70.4% of total foreign banknote transactions in Indonesia. The next biggest contributions were made by the Bank Indonesia Regional Representative Offices in the provinces of Bali and the Riau Islands, amounting to Rp28.9 trillion and Rp11 trillion respectively. The two Regional Representative Offices of Bali and the Riau Islands accounted for a 12.7% and 4.9% share of the overall value of UKA transactions respectively (Chart 9.15).

9.2. CURRENCY MANAGEMENT PERFORMANCE

In 2015, the value of currency in circulation (UYD) grew by 11.0% to reach Rp586.8 trillion, higher than the previous year's growth of 5.7%. In terms of trends, this growth in UYD echoes back to the average growth trajectory from 2009 - 2013, which stood at 13.7% per year (Chart 9.16). On a monthly basis, growth of UYD was affected by seasonal factors in certain periods, especially religious holidays (the period of Ramadan and Christmas) and public holidays. The most amount of money in circulation was recorded at the end of Ramadan in 2015, amounting to Rp604.2 trillion, an increase of 7.0% from the same period in 2014 when Rp564.5 trillion was in circulation (Chart 9.17).

In terms of denominations, the proportion of Rp100,000 banknotes had continually increased over recent years, from 35.4% of the total in 2005 to 62.8% in 2015. This was followed by the Rp50,000 denomination which accounted for 28.4% of all banknotes in circulation (Chart 9.18). The 11,0% growth in currency in circulation was largely supported by the growth in circulation of Rp100,000 and Rp50,000 banknotes, which stood at 12.2% and 9.4% respectively (Chart 9.19). These increases were driven by the public preference for larger denominations of rupiah because of practicality and efficiency. Also, these particular denominations

Chart 9.16. Currency in Circulation



8 Nonbank KUPVA operators are limited liability companies whose intent and purpose is to engage in the business of buying and selling foreign banknotes and purchasing traveler's cheque.

Chart 9.17. Daily Movement of Currency in Circulation

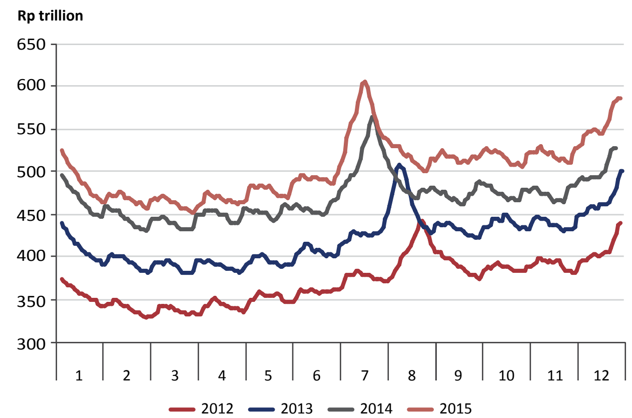
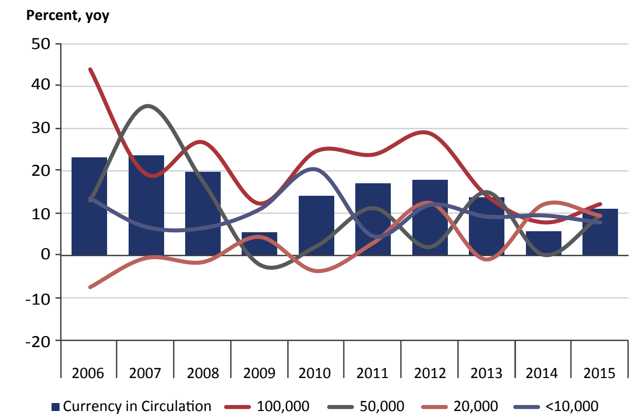


Chart 9.19. Growth of Currency in Circulation by Denomination



of banknotes were generally easier to access and obtain. This was confirmed by a survey conducted in several major cities in 2015 which indicated that the Rp100,000 and Rp50,000 banknotes were more easily obtained through Automatic Teller Machines (ATM).[9] The availability of these two denominations through ATM machines means that they were especially common given that the number of ATM machines in 2015 grew by 9.2% to 97,845 and the number of ATM/Debit cards grew by 13.7% to 120.3 million cards. Furthermore, the value of cash withdrawals via ATMs also increased by 9.4% to Rp2,100.8 trillion during 2015.

Movements in UYD were also reflected in the flows of currency through Bank Indonesia, which in 2015 experienced a net outflow of Rp56.4 trillion, higher than the net outflow in 2014 of only Rp27.9 trillion. The currency withdrawn by banks from Bank Indonesia (outflow) amounted to Rp566.3 trillion, or growth of 10.6%. Meanwhile, the currency deposited by banks in Bank Indonesia (inflow), some of which is money not fit for circulation, only amounted to Rp509.9 trillion, up 5.3% (Chart 9.20). In terms of seasonal patterns, the dynamics of cash transactions were affected by certain events that typically precipitate high outflows, such as Ramadan, which fell in July, Christmas, and the year-end holidays in December, after which a net inflow to Bank Indonesia was restored in the following few months. Outflow during the Ramadan period in 2015 amounted to Rp140 trillion, up 12.2% compared to the previous year's Ramadan.

Chart 9.18. Composition of Currency in Circulation by Denominations

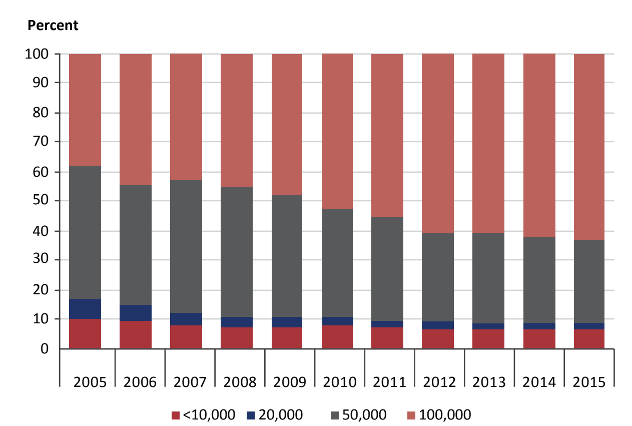
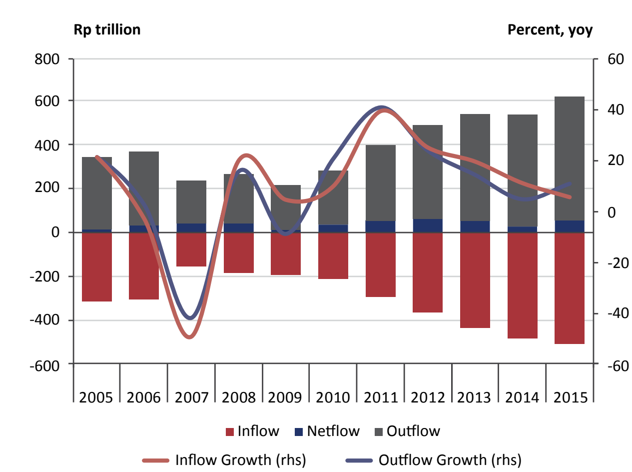
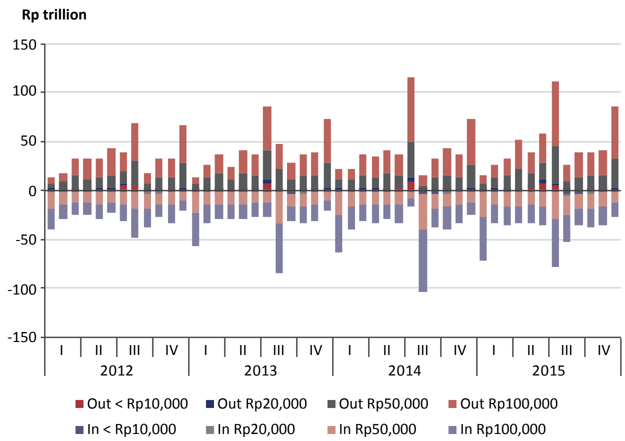


Chart 9.20. Outflow and Inflow through Bank Indonesia



9 A survey of 487 respondents was conducted in Makassar, Banjarmasin, Denpasar, Surabaya, Semarang, Bandung, Palembang, Padang, Medan and Jakarta.

Chart 9.21. Cyclical Pattern of Inflow and Outflow through Bank Indonesia

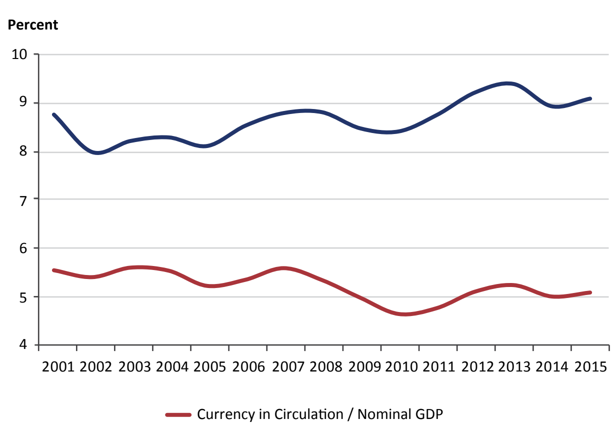


Meanwhile, outflow in the Christmas and year-end holiday period reached Rp85.6 trillion, up 17.5% compared to 2014 (Chart 9.21).

Currency as an Indicator of Economic and Liquidity

The continually prominent role played by currency in domestic economic activities was reflected in the ratio of UYD to GDP. In recent years, the ratio of UYD to GDP has been relatively stable at an average of 5.1%, or consistently in the 4.6-5.6% range. Meanwhile, the prominent role of currency in the economy's liquidity is reflected in the ratio of UYD to Household Consumption. In 2015, this ratio stood at 9.1%, higher than the previous year's figure of 8.9%, despite the slowing growth of household consumption (Chart 9.22). This was also confirmed by the growth pattern of UYD which was in

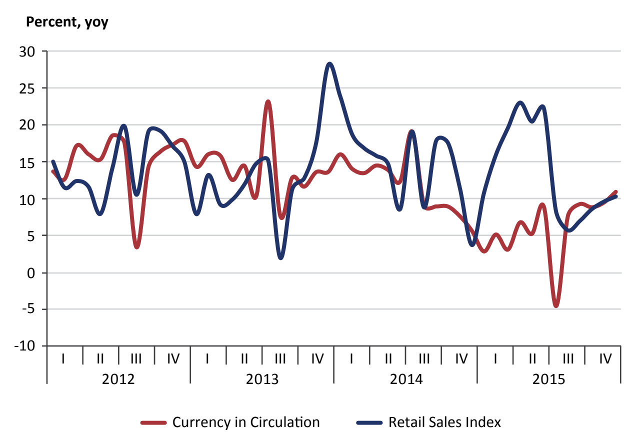
Chart 9.22. Ratio of Currency in Circulation to GDP and Household Consumption



line with the growth of the Retail Sales Index (IPE). The growth pattern of UYD and IPE showed a decline in the first 2 or 3 months of 2015, and 1 or 2 months after Ramadan. Conversely, UYD and IPE rose at other periods, particularly in the months leading up to Ramadan and ahead of the Christmas and year-end holidays (Chart 9.23).

In recent years, the movement of UYD has remained within the projected range with a deviation closer to the lower limit of UYD projections.[10] This reflects the fact that the growth of UYD has been consistent with on-going weak economic growth (Chart 9.24). However, once seasonal factors are eliminated from the UYD growth trend, a bottoming-out from the lowest point in mid-2015 is evident.[11] This is in line with the economic growth rate which began to rise in the third quarter of 2015, reaching 4.74%, and continued to do so in the fourth quarter to 5.04% (Chart 9.25). The onset of an increase in UYD growth in the second half of 2015 was supported by increased government spending from the withdrawal of currency (outflow) by banks distributing the state budget. This was reflected in the growth of government consumption which began to increase in the third quarter of 2015, reaching 7.11%, and continued to do so in the fourth quarter of 2015 to 7.31% (Chart 9.26).

Chart 9.23. Growth of Currency in Circulation and Retail Sales Index



10 Currency in Circulation (UYD) projections are calculated using the Error Correction Model, which is influenced by several macroeconomic variables, namely economic growth, inflation rates, interest rates, and the BI Rate.

11 Seasonal factors refer to increased demand for currency at times of religious holidays, such in the Ramadan/Idul Fitri period as well as the Christmas and end of year holiday period.

Chart 9.24. Projection and Actual Currency in Circulation

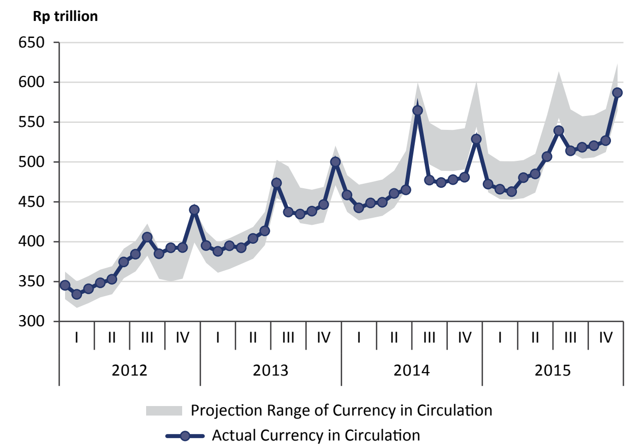
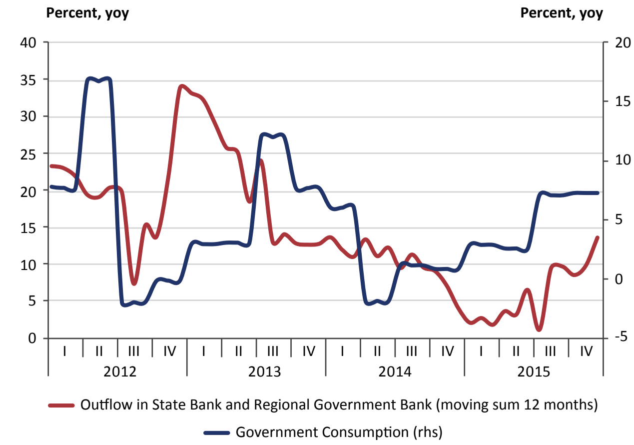
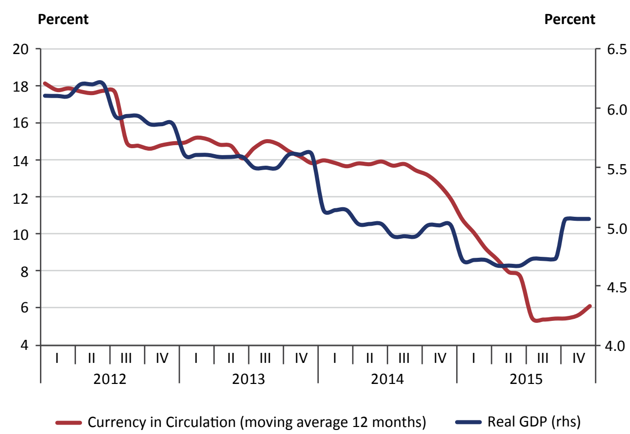


Chart 9.26. Growth of Currency Outflow in State Banks and Regional Government Banks, and Real Government Consumption



In terms of liquidity, another currency indicator, namely Cash in Vault (CiV), continued its slowing growth until the end of 2015.[12] This was in line with slowing growth in the bank deposits (DPK) in rupiah denominations in the same period (Chart 9.27). These movements in the growth of CiV and DPK were also confirmed by the slower growth in Interbank Currency Transactions (TUKAB) in Jakarta and its surrounding areas in the same period (Chart 9.28) [13]

Chart 9.25. Growth of Currency in Circulation and Real GDP



12 Cash in Vault (CiV) is a component of currency in circulation (UYD) held in the treasury of banks including in ATMs (Automatic Teller Machines). Another component of UYD is Currency outside Banks (CoB), which refers to currency circulating in society outside of the banking system.

13 Interbank Currency Transactions, or TUKAB, refer to activities between banks which include the demand, supply and exchange of rupiah currency that is still fit for circulation in order to meet needs in terms of amounts and/or type of denominations, in accordance with Bank Indonesia provisions.

Impact of Policy Implementation on Currency Management Performance

Throughout 2015, Bank Indonesia implemented a variety of currency management policies. The impact of the implementation of these policies was reflected in the availability of currency in sufficient quantities, in appropriate denominations, in a timely manner, and in a condition fit for circulation. As a first step in the implementation of its current management policies, Bank Indonesia continued to maintain the availability of currency throughout 2015 in order to ensure the smooth operation of cash payment transactions in every economic activity. This was reflected in Bank Indonesia's cash position ratio which stood at an average of 5.1 months of outflow throughout 2015, higher than the previous year's average figure of 3.1 months of outflow.

Chart 9.27. Growth of Cash in Vault and Bank Deposits

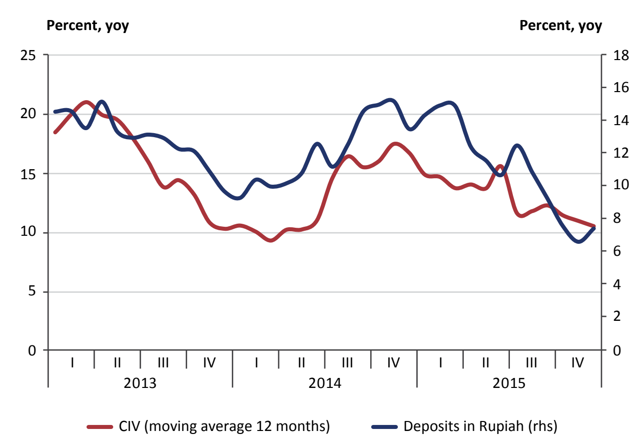


Chart 9.28. Growth of Cash in Vault and Interbank Cash Exchange (TUKAB)

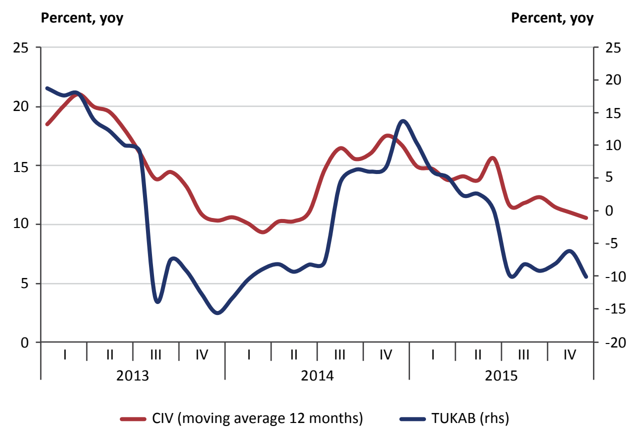
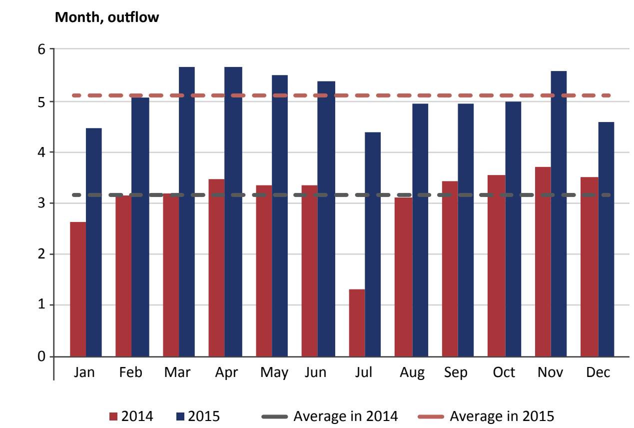


Chart 9.29. Ratio of Cash Position to the Average of Monthly Outflow

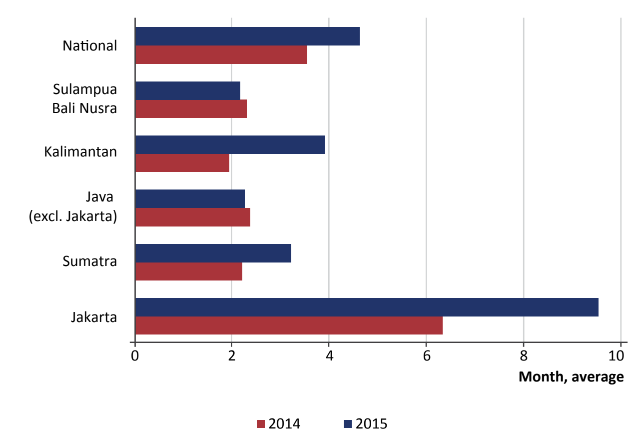


The highest cash position ratio came about in March and April of 2015, reaching 5.7 months of outflow in line with the reverse flow of currency from banks to Bank Indonesia after the Christmas and year-end holiday period in 2014, as well as the presence of a supply of printed money from The Indonesian Government Security Printing and Minting Corporation (Perum Peruri). In contrast, the lowest cash position came about in July 2015, reaching 4.4 months of average outflow triggered by the high level of currency withdrawals by banks in the 2015 Ramadan period (Chart 9.29). By area, the highest cash position ratio was at Bank Indonesia's Headquarters, reaching 9.4 months of outflow. This high cash ratio was intended to maintain the National Iron Stock (ISN) that has to be provided by Bank Indonesia in anticipation of withdrawals from banks, the majority of which are headquartered in the Jakarta area (Chart 9.30).[14]

The availability of currency in sufficient quantities is an integral result of the implementation of Interbank Cash Exchange (TUKAB) policy since 2011. This policy has prompted banks to first meet its rupiah currency liquidity needs from transactions with other banks. In the event that these currency needs are not met, banks can then fulfil their currency needs by making withdrawals from Bank Indonesia. In 2015, the number of TUKAB transactions in the Jakarta area stood at Rp66.3 trillion, a drop of 10.0% from the previous year's figure of Rp73.6 trillion (Chart 9.31). The contribution of TUKAB in meeting the currency needs of banks over the last 5 years has been an average of 50.1%, even though there was a fall in 2015 of 40.5%. This was caused by the slowing growth of bank deposits in 2015, meaning that the need for currency to be exchanged through TUKAB mechanisms also decreased (Chart 9.32).

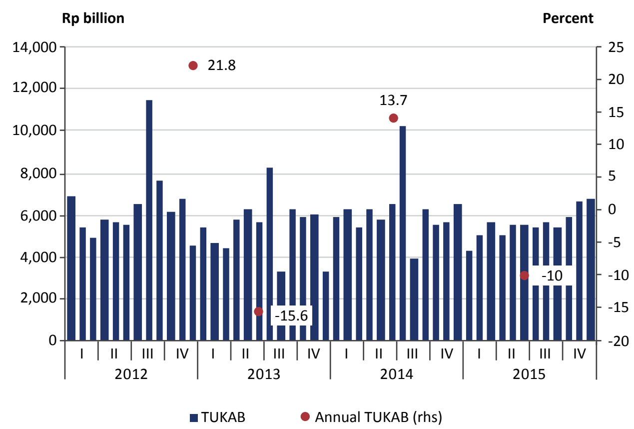
With the availability of currency in sufficient quantities in 2015, Bank Indonesia pursued a policy of reform in terms of its currency and cash services distribution. This policy involved infrastructure development (capacity building), by opening Bank Indonesia Regional Representative Offices in the province of West Sulawesi in October 2015 and collaborating with banks to open 6 new Cash Custodians in various areas of Indonesia

Chart 9.30. Ratio of Cash Position to the Average of Monthly Outflow According to Regions



14 The National Iron Stock is a standby inventory in anticipation of an increase in demand for currency that was not predicted at the time of preparation of the Currency Demand Estimation at the beginning of the year, and which could be precipitated, for example, by a rise in the fuel or electricity price in the current year. Setting the iron stock at 20% of projected currency in circulation (UYD) is in accordance with the best practices of other countries, for example the Central Bank of Spain and Central Bank of Korea.

Chart 9.31. TUKAB in Jakarta and Surrounding Area



previously unreached by Bank Indonesia's cash services in a direct sense.[15] By opening this Bank Indonesia Regional Representative Offices in West Sulawesi, one Cash Custodian in the city of Mamuju terminated its operations. This development meant that the number of Cash Custodians in 2015 was 35 commercial banks with 368 commercial bank branches spread throughout Indonesia. These figures were higher than those in 2014 when there were just 30 Cash Custodians managed by commercial banks with 267 commercial bank branches.

In 2015, total withdrawals through Cash Custodians to the value of Rp47.4 trillion were made, an increase of 31.1% on the previous year's figure of Rp36.1 trillion (Chart 9.33). This strong growth occurred largely in the second semester of 2015 in line with the addition of Cash Custodians and the religious holidays that fell at this time. In terms of region, these increases were most prominent in Cash Custodians in the provinces of Central Kalimantan, South Sumatra, and Papua. With the previously mentioned enhancement of capacity building, Bank Indonesia's cash services coverage reached 66%, or 338 cities/regencies in Indonesia in 2015. This figure was higher than the corresponding figure from 2014 of 61%, or 316 cities/regencies in Indonesia.

In addition to expanding the scope of its cash services to new areas through Cash Custodians, Bank Indonesia also continued to facilitate the exchange of money by means of Mobile Cash units across Indonesia, including in the country's remote areas and outermost islands.[16] These efforts were reflected in the 25.7% growth of money exchanges from Rp1.5 trillion to Rp1.8 trillion in 2015 (Chart 9.34). This high growth mainly occurred in the third quarter of 2015, and during the period of Ramadan/Eid Al Fitr 2015.

Bank Indonesia also consistently sought to raise the quality of currency in circulation in society (clean money policy), in all regions of Indonesia. This policy sought to improve soil levels, or maintain the quality of money in circulation by setting standards as to the state of soiled or mutilated

Chart 9.32. TUKAB Pattern in Jakarta and Bank Deposits

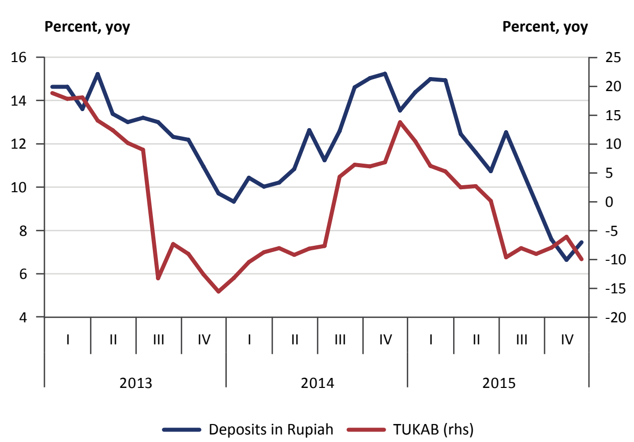
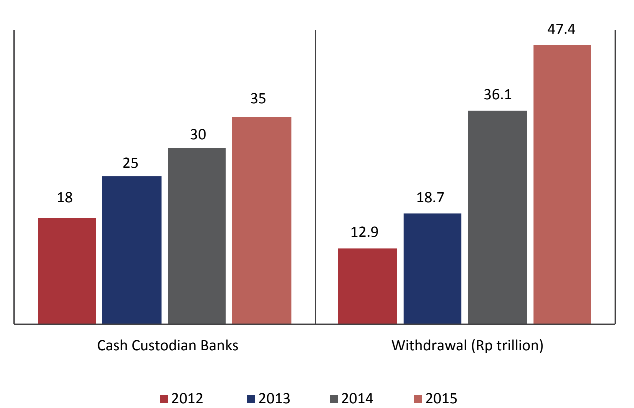


Chart 9.33. Number of Cash Custodian and Rupiah Withdrawal



15 Custodial Cash is an activity whereby supplies of currency are kept in a bank designated by Bank Indonesia in order to ensure a sufficient supply of bank cash and to meet the currency needs of the public in specific areas/regions.

16 Mobile Cash is a currency exchange facility provided by Bank Indonesia to the public, or other parties working with Bank Indonesia, which uses modes of transport; it is done through a retail mechanism (to the public) and a wholesale mechanism (to banks).

Chart 9.34. Rupiah Withdrawal Through Mobile Cash

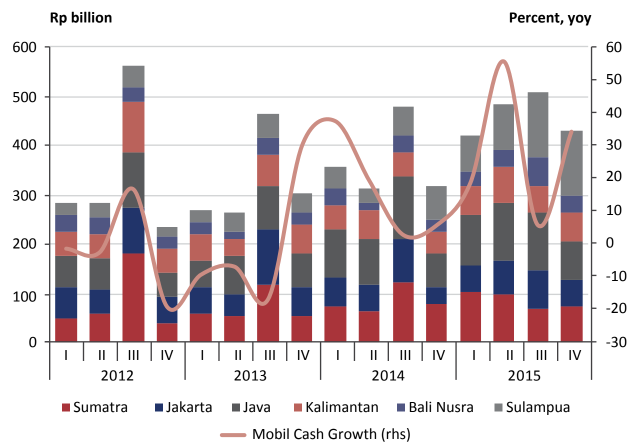
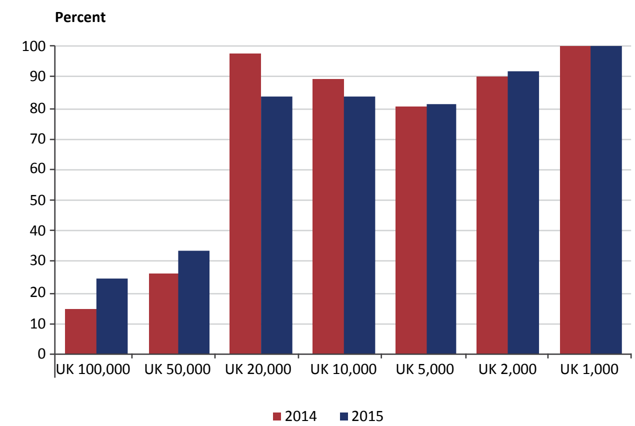
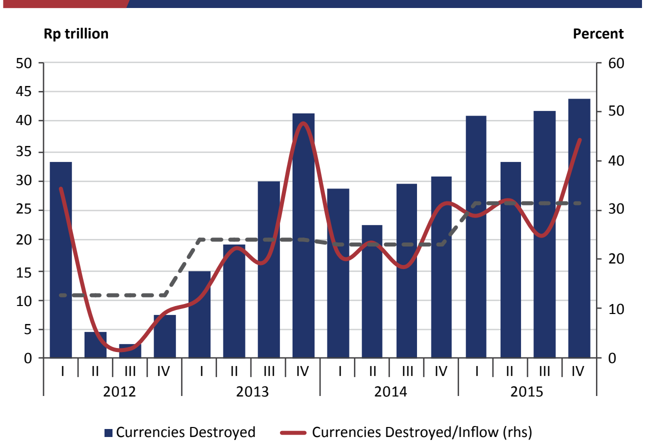


Chart 9.36. Ratio of Money Destruction to Inflow by Denomination



money, and to maintain standards for the processing and sorting of money fit for circulation (ULE) from that deemed unfit for circulation by Bank Indonesia and banks. Under the policy, the amount of money unfit for circulation (UTLE) deposited by banks in Bank Indonesia, which then went on to be destroyed and replaced with new fit for circulation money, increased. Over 2015, the value of destroyed UTLE stood at Rp160.3 trillion, up 43.6% over the previous year's figure of Rp111.6 trillion. This increase in destroyed UTLE was much higher than the increase in inflow, which stood at just 5.3%. With this development, the ratio of destroyed UTLE to inflow was 31.4%, higher than the previous year's ratio of 23.0% (Chart 9.35). In terms of denomination, more large banknotes were destroyed than small banknotes, bearing in mind that generally small banknotes are much more soiled or worn than large banknotes (Chart 9.36).

Chart 9.35. Destruction of Currency Unfit for Circulation



The successful implementation of currency management policies during 2015 was reflected in the results of a survey on the quality of currency fit for circulation in several towns in border areas and remote areas.[17] The survey results showed that the currency quality index in these towns in border areas and remote areas stood at 6.8, higher than the original target figure of 4. In terms of denominations, large banknotes (Rp100,000, Rp50,000, and Rp20,000) were indicated as being of a higher quality than small banknotes (Rp10,000, Rp5,000, and Rp2,000). Regionally, the currency quality index for large banknotes was the highest in the town of Ketapang, and the lowest in the town of Jeneponto. Meanwhile, the currency quality index for small banknotes was also the highest in the town of Ketapang, and the lowest in Sidangkalang, Kabanjahe, and Brastagi.

In addition, Bank Indonesia continued to strengthen coordination with all elements of the Coordinating Agency for Eradication of Counterfeit Money (Botasupal), in particular with the Indonesian National Police, to prevent the circulation of counterfeit money in the society. Moreover, Bank Indonesia also kept up efforts aimed at improving the compliance of banks in reporting rupiah of dubious authenticity to Bank Indonesia, and also organized activities aimed at educating the public about the characteristics of authentic currency and the prevention of counterfeit currency. The success of this coordination was reflected in an increased discovery of counterfeit currency in 2015, amounting to 313,538 notes, up 156.8% from the

17 A survey of 466 respondents was conducted in Southwest Sumba, West Manggarai, Sanggau, Ketapang, North Hulu Sungai, Rembang, Pekalongan, Sawahlunto-Sijunjung, Jeneponto, Mojokerto, Sampang/Pamekasan, Sidangkalang-Kabanjahe-Brastagi, Subang, Banyu Asin - Sungai Lilin, and Amlapura.

Chart 9.37. Ratio of Counterfeit Money to Currency in Circulation

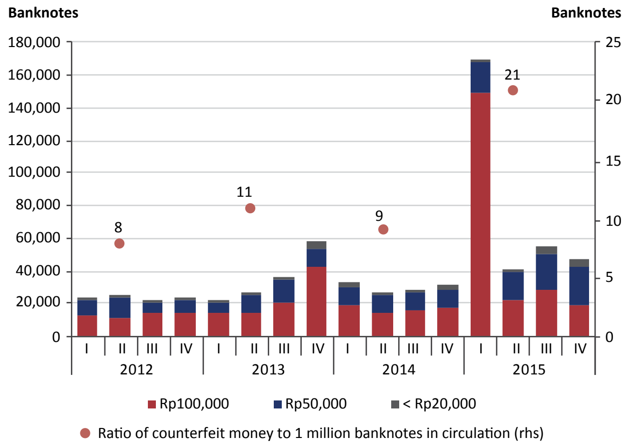
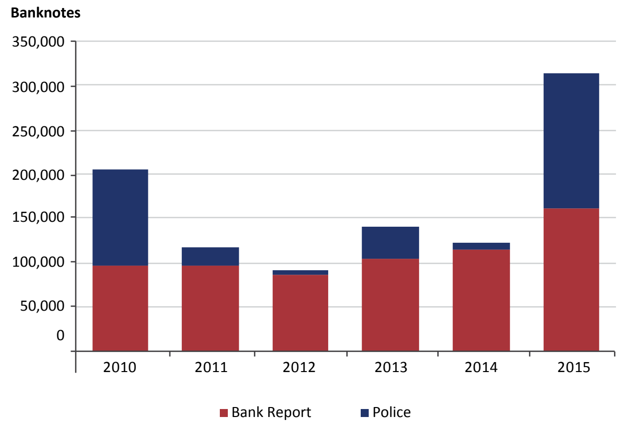


Chart 9.38. Finding of Counterfeit Money by Police and Bank Report



previous year's figure of 122,091 notes. Of the counterfeit banknotes discovered, most were in denominations of Rp100,000 and Rp50,000, with 209,752 notes (a 71.7% share) and 70,626 notes (a 24.1% share) respectively. In terms of distribution, the majority of counterfeit banknotes were discovered in Java, especially the province of East Java and Jakarta. These developments meant that the ratio of counterfeit currency in circulation rose from 9 notes to 21 notes per one million notes in circulation (Chart 9.37). The large amount of counterfeit money discovered was largely due to the active role played by the police in uncovering counterfeit money in circulation in 2015, particularly in the area of Jember in the first quarter of 2015 where 122,000 notes were discovered. In addition, the increased amount of counterfeit money discovered was also thanks to the compliance of banks in reporting counterfeit money to Bank Indonesia (Chart 9.38).

Box 9.1 Strengthening of the Payment System Infrastructure

The Bank Indonesia National Clearing System (SKNBI) Generation II

The public is now able to perform fund transfers more easily, quickly, and affordably by means of the national clearing system. Whereas previously Fund Transfer Services by means of clearing could be performed 4 times a day, now they can be performed 5 times a day, at 09.00, 11.00, 13.00, 15.00, and 16.15 WIB, while Check Clearing Services can be performed 4 times as opposed to the previous one time. With these additional services, customer funds will be delivered within a maximum of 4 hours. This has been enabled by the onset of operations of the Bank Indonesia National Clearing System (SKNBI) Generation II on Friday, 5 June 2015.

Faster transfer times represent the first phase in the development of the Fund Transfer and Check Clearing Services of two phases in the development plan for the SKNBI Generation II. In the future, Bank Indonesia will develop a Multiple Transfer Service, a service which can process the transactions of more than one recipient and sender (multiple parties) aimed at facilitating a variety of routine payment/ billing transactions.

SKNBI Generation II, whose services are available from 06.30 WIB until 16.00 WIB (extended to 9.5 hours from the previous 8 hours), represents an improvement on SKNBI Generation I which had been in operation for 10 years. The improvements in SKNBI Generation II also include expanded participation access for Non-Bank Fund Transfer Operators specifically for Fund Transfer Services. This enables the public to perform fund transfers to any part of Indonesia securely, cheaply, and efficiently.

In order to enhance customer protection, transfer processing time obligations have been established for Sending Banks and Receiving Banks. Sending Banks have to forward fund transfers no later than 2 hours after receiving the mandate from a customer. Furthermore, Receiving Banks must record transfers in customer accounts no later than 2 hours after the settlement at Bank Indonesia. A maximum clearing fee has been set at Rp5,000 (five thousand rupiah). Considering that these two provisions require an adjustment to the internal systems of each SKNBI Generation II Participant, a transitional period has been stipulated which will take effect from 1 January, 2016.

There are several differences between performing transfers through SKNBI and Bank Indonesia Real Time Gross Settlement (BI-RTGS). Firstly, SKNBI settlements are performed at the end of the period (netting) while RTGS settlements are performed individually (gross). Secondly, in terms of amount limits, customer transactions can be processed through SKNBI to a maximum value of Rp500,000,000 (five hundred million rupiah) per transaction, whereas transactions through RTGS must be of a minimum value of Rp100,000,000 (one hundred million rupiah) per transaction. Thirdly, the fees charged by Bank Indonesia on SKNBI Participants are lower, amounting to Rp750 (seven hundred and fifty rupiah) per transaction, whereas for BI-RTGS the fee is Rp15,000 (fifteen thousand rupiah) per transaction.

In order to support the implementation of SKNBI Generation II, Bank Indonesia issued Bank Indonesia Regulation No. 17/9/PBI/2015, dated June 5, 2015, concerning the Operation of Fund Transfers and Scheduled Clearing by Bank Indonesia, Bank Indonesia Circular Letter No. 17/13/DPSP, dated June 5, 2015, concerning the Operation of Fund Transfers and Scheduled Clearing by Bank Indonesia and Bank Indonesia Circular Letter No. 17/14/DPSP dated June 5, 2015 concerning Customer Protection in the Operation of Fund Transfers and Scheduled Clearing Through the National Clearing System of Bank Indonesia. With the new system, the security and smooth operation of the payment system, as well as consumer protection, are expected to be further improved.

Bank Indonesia Real Time Gross Settlement (BI-RTGS) and Bank Indonesia Scripless Securities Settlement System (BI-SSSS) Parties

Payment system transaction activities in society are at present increasingly secure, fast, and reliable thanks to updated technology and improved customer protection. This was realized through the implementation of three updated BI systems on 16 November, 2015, namely BI-RTGS, Bank Indonesia Scripless Securities Settlement System (BI-SSSS), and Bank Indonesia Electronic Trading Platform (BI-ETP) Generation II. In addition to improving

Table 1. Comparison of SKNBI Generation I and II

NO.	ITEM	GENERATION I	GENERATION II
1.	Message Format	Propietary message format	ISO 20022 (xml format)
2.	Identification of Participants	Clearing Code	Bank Identifier Code (BIC)
3.	Type of Service	- Single Debit - Credit Transfer	- Single Debit Transfer - Single Credit Transfer - Multiple Debit Transfer - Multiple Credit Transfer
4.	Participant Scope	Bank	- Bank - Participants of Non-bank Funds Transfer
5.	Debit Clearing	Per region	Centralization
6.	Settlement of Funds Transfer	4 periods in 2 cycles	5 settlement periods
7.	Settlement of Debit Clearing	3 time zones in accordance with the time zone	4 clearing zones in accordance with the requisite
8.	Consumer Protection	Regulation on the onward transfer of funds to the customer on the same day	Regulation about the deadline for forwarding funds transfer orders and forwarding funds to customer accounts
9.	Minimum Prefund Provision for Funds Transfer	Minimal Rp1,-	-

the quality of its technology and communications networks, Bank Indonesia also sought to enhance customer protection by instructing that a mandatory maximum time limit for bank in processing customer fund transfers. Banks are now obliged to process customer fund transfers no longer than 1 hour after the receiving bank has obtained the funds in the BI-RTGS System.

The BI-RTGS system is an electronic fund transfer system between participants, for the most part banks. This system accommodates customer fund transfers in large amounts that can be settled instantly per transaction. BI-SSSS is used as a means of transaction with Bank Indonesia and for administering securities electronically. Meanwhile, BI-ETP is a Bank Indonesia means of transaction linked to monetary operations, Government transactions in the management of Government Securities (SBN), and money market transactions between banks, either by conventional banks (Interbank Money Market/PUAB) or sharia banks (Sharia Interbank Money Market Sharia / PUAS).

The implementation of the BI-RTGS, BI-SSSS, and BI-ETP Generation II Systems was based on the following five important considerations; improving the efficiency and capability of risk mitigation systems in accordance with international best practices; improving the ability to be connected (interoperability) with other infrastructure in financial markets/systems, both domestic as well as cross-border; accommodating the dynamics of both global and domestic financial markets/systems including policy changes both from BI and the Government; accommodating the development of an increasing transaction volume; and updating the technology of the BI-RTGS and BI-SSSS Generation I systems that have been operating for over 10 years.

For banks, the implementation of the Generation II systems will provide them with the opportunity to better manage their priority transactions and liquidity. In addition, money market transaction needs can also be well accommodated with these systems as information on money market transactions can be more easily obtained. Meanwhile, customer protection is also enhanced by the setting of time limits for processing BI-RTGS transactions as well as limits on BI-RTGS transaction charges - of Rp35,000 (thirty five thousand rupiah). These are both advantageous to customers in that they provide certainty as to transfer time and costs.

To support the implementation of these Generation II systems as well as to mitigate the risks that may arise from them, Bank Indonesia will issue related provisions and apply a transitional period for fund transfer settlement through the BI RTGS and SKNBI systems, as follows:

Table 2. **Settlement Transition of Fund Transfer through BI RTGS system and National Clearing System (SKNBI)**

Nominal Transactions		Validity Period
BI-RTGS	SKNBI	
The minimal limit of transaction is (flooring) Rp500 million	No limit	From 16 November 2015 until 30 June 2016
The minimal limit of transaction (flooring) is Rp100 million	The maximum limit of transaction is Rp500 million	From 1 July 2016

With the implementation of these Generation II systems, it is expected that national payment system activities will take place securely and smoothly, and will meet the needs of any developments in Indonesian financial markets. This, in turn, will support the stability of the financial system.

Regionally, economic moderation in 2015 was felt most grievously in areas reliant on commodities from natural resources. Consequently, efforts were required to diversify the economic structure, while paying due consideration to the potential of each respective region.

Chapter 10

Regional Economy

As global demand and prices for natural resource commodities declined, most provinces experienced slower economic growth in 2015, except for those in the Eastern Indonesia Region (KTI). A significant economic growth in KTI was attributable to, among others, the favorable result of downstreaming and diversification of the economy towards the industrial sector. On the fiscal side, an increase was seen in the central government's transfer and infrastructure spending despite their less than optimum use. In regards to prices, inflation remained under control in most provinces. Financial stability remained intact amid the slower credit expansion for corporate and household across the provinces.

Slower growth marked the economy of most provinces in 2015, except for those in KTI. Natural resource commodity prices that continued to decline and the relatively slow pace of global economic recovery had affected export and investment performance of the Indonesian regions. This condition had a significant impact on the economies outside Java, which are highly dependent on the export of natural resource commodities in the mining and plantation industries. Nevertheless, the slowdown did not impact all the provinces which have economies are based on natural resources like it did in 2014. The economy of KTI in 2015 experienced the highest growth compared to their historical growth in the last five years, which, among others, was attributable to the positive impact of a consistent natural resource-based downstreaming program.

The economic slowdown in provinces which economies are based on natural resources was related to the limited diversification of the economic structure. The structure of natural resource-based provincial economies proved to be more susceptible to fluctuations in natural resource commodity prices. The economic slowdown, especially in the last two years, confirmed the vulnerability of economic structures in a number of provinces outside Java which economies are based on natural resources, that is, in oil and gas producing provinces of Aceh, Riau, East Kalimantan and West Papua, the coal producing province of East Kalimantan and a few provinces in Kalimantan, and in South Sumatra Province, as well as mineral and metal concentrate producers spread in several provinces in KTI, Kalimantan, and Sumatra. As far as plantation industries are concerned, the volatility of commodity prices also affected the economic resilience of regions that depend on natural resources, including palm oil and rubber producing provinces in Sumatra and Kalimantan and producers of cocoa and copra in Sulawesi.

The economic vulnerability of provinces which economies are based on natural resources is also subjected to structural factors associated with rapid depletion of non-renewable natural resources. The growth contraction of a number of oil and gas producing provinces in Sumatra and Kalimantan was due to not only the significant impacts ofcontinuing decline in oil and gas prices in 2015, but also aging refineries and depletion of oil and gas reserves. The impacts of the decline in production and productivity of oil and gas exploration has compromised efforts to promote the downstreaming of oil and gas sector across regions. Today's oil and gas prices, which are far lower than their historical figures, has become a disincentive for both new exploration and investment in the oil and gas sector. This condition constitutes a fundamental economic challenge in oil and gas producing provinces or other provinces which economies are based on non-renewable natural resources, if no immediate action is taken to diversify the economic structure.

On the other hand, positive results have been obtained from a downstreaming program on mining resources in some provinces whose production is able to keep up the acceleration of economic growth particularly in KTI. This is especially true for the downstreaming of the mineral resources through investment in the construction of smelters, some of which have been running in a number of provinces in Sulawesi. The implementation of downstreaming policies has yielded significant positive effects to the economy of KTI, as indicated in the performance of the construction business and labor absorption. The operation of the new smelters has successfully contributed to the improvement in the performance of industrial and service businesses. However, efforts to promote the downstreaming program at regional levels is still met with challenges.[1] Of the 19 companies that have planned to build smelters in KTI, only seven have shown significant progress including two that commenced operations in 2015. Some constraints found in smelter development included issues related to energy supplies, land acquisitions, permits, environmental destructions, and financing aspects.[2]

Economic linkages between one region and another were responsible for spreading the economic slowdown from natural resources (SDA) based regions to non-SDA based ones. The decline in export revenues in a number of provinces outside Java had led to the weakening of consumers' purchasing power and households' consumption of goods and services that are mostly came from Java. The slowdown in inter-provincial export performance was confirmed in 2015. However,

1 Downstreaming program on plantation commodities such as palm oil in Sumatra was restrained by the currently lower commodity prices in which the export duties on CPO became relatively not so much different from those on its derivative products. In addition, the effectiveness of the use of biofuels which was initially intended to reduce domestic dependence on imported oil and gas, was also relatively limited. In the oil and gas sector, a downstreaming program through the development of petroleum refining and petrochemical industries driven by tax incentives, such as in Kalimantan, was also limited because of the huge cost of the investment.

2 Support on structural reforms by local governments was particularly directed to overcome trade facilitation and land acquisition issues. Some local governments have operated the one stop service (OSS) system and downsized the total number of licenses, although most of them were still not fully integrated. Some local governments have also supported the process of land acquisition including through coordination with a number of related government institutions (National Land Agency and the Ministry of Environment).

consumption growth that was supported by government spending would enable Java to withstand a deeper economic slump.

For main industries, the aggregate slowdown in growth had occurred in both tradable and non-tradable industries. As far as tradable industries are concerned, slowdown especially occured in the manufacturing industry, particularly in Java. The agricultural sector recorded improvement with increased production of food crops, especially in Java, while the performance of plantation industries in provinces outside of Java was still in decline. The mining industry had also recorded some improvement despite growing at a negative level. A significant improvement in mining sector in the KTI was able to offset the slowdown in the same industry in Sumatra and Kalimantan. As for non-tradable industries, wholesale and retail trading businesses experienced a slowdown in provinces outside Java, along with the decline in the performance of export of natural resources. Meanwhile, the construction sector slowed down in all provinces except in KTI, despite the expansion of government infrastructure projects.

Inflation rates declined throughout all the country's provinces in 2015, especially in the administered prices category. The decline in inflation recorded in Java and Sumatra was due to the sustainable supply and smooth distribution of foodstuffs. The impact of El Nino weather phenomenon in 2015 was relatively moderate on most areas of Java that served as the country's national food production center. On the other hand, Kalimantan and KTI experienced relatively higher inflationary pressures due to frequent disruption in foods distribution as there are still a limited connectivity, capacity, and quality of infrastructure.

From the aspect of regional bank financing, credit slowdown occurred in all provinces although financial stability was maintained. The sharpest decline in credit growth was recorded in Kalimantan and Java. The economic slowdown had also led to the slowdown in bank deposit across all provinces. In spite of this, the stabilization policy adopted by Bank Indonesia had been able to safeguard financial stability in the entire regions with credit risk kept below the safe limit. Meanwhile, on regional fiscal side, it's support to the economy is relatively insufficient due to lower budget absorption in 2015. The insufficiency in regional spending capability to stimulate the economy is also a result of the decline in regional revenues because of economic slowdown. Moreover, there are indications of increased fiscal risks in some provinces that were experiencing a decline in the revenue share of natural resource commodity export. On the other hand, there had been increased in central government's transfer and infrastructure spending in most provinces.

Looking ahead, the commitment and priority to accelerate structural reforms, especially through the development of strategic infrastructure in the area, is believed to be supporting the economic performance. The continued development of various infrastructure projects across regions is supported by the central government budget and through a significant increase in Special Transfer Funds to the regions.[3] In accordance with the National Medium-term Development Plan (RPJMN) target for a 2015 – 2019 period, the development of infrastructure in 2016 focused on the 35 thousand MW electricity power construction project which is becoming a major structural problem throughout the region, as well as agricultural infrastructure projects that support food security in regions. Connectivity supporting infrastructure development across regions (roads, ports, and airports) is also a priority in the Government's Annual Work Plan (RKP) for 2016, which will support the increased competitiveness of the economy.

Structural reforms across provinces had also emphasized diversification of economic structure by taking into account the potential of available resources. Structural reforms in provinces outside Java were directed at building natural resource-based manufacturing industries with higher added value that could serve as suppliers of raw materials for the manufacturing industry in Java. Meanwhile, structural reforms in Java were directed at integrated industrial transformation by prioritizing and strengthening of the integration of domestic and global industries as well as the making of Indonesia as a global production base. This had become a crucial factor in dealing with inter-regional competition that went beyond national borders in the era of the ASEAN Economic Community (AEC) and in controlling the domestic market.

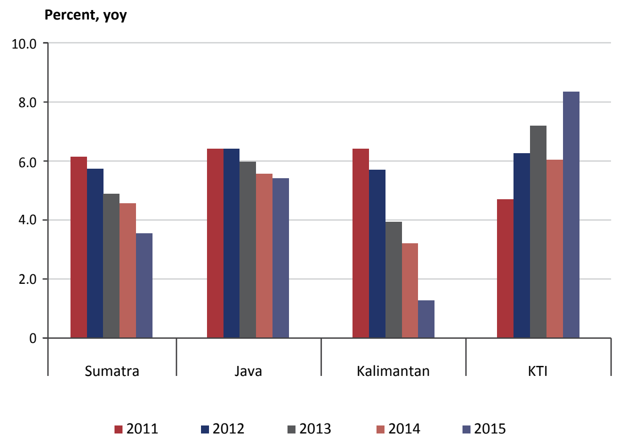
10.1. REGIONAL ECONOMIC GROWTH

Dynamics of Regional Economic Growth

Economic growth in 2015 slowed in all provinces, except in provinces in KTI. The deepest economic slowdown was experienced by provinces in Kalimantan and Sumatra (Chart 10.1). Meanwhile, the economic slowdown in Java, which has the largest share of the national economy

3 Of the 14.2% increase in the transfer of funds to provinces in 2016, the special transfer funds for infrastructure rose to the highest, reaching about a 266% increase (from IDR58.8 trillion in 2015 to IDR156.4 trillion in 2016).

Chart 10.1. Regional Economic Growth in 2015



Source: BPS-Statistics Indonesia, processed

and relatively more diversified sources of growth, was relatively moderate (-0.1% compared to its economic growth in 2014). Unfavorable global condition was the major cause of regional economic slowdown exacerbated through the decline in primary commodity export performance. Export growth was negative in Sumatra, Java and Kalimantan. On the other hand, exports in KTI were able to post a double-digit growth of 18.8% (yoy), thanks to the export of mining commodities, which drove the improvement of KTI's economy whose share was about 11.3% of GDP (2.3% higher than the annual growth in 2014). KTI's export improvement had also been a factor that increased investment in the region by 9.1%.[4]

The deepest economic slowdown in 2015 was primarily experienced by major oil and gas producing provinces. Aceh and East Kalimantan had recorded negative growth, while Riau was still capable of positive growth (Picture 10.1).[5] A slowdown in oil and gas mining sector as a result of the decline in world oil prices had also affected the performance of a number of related businesses, including the industrial sector, wholesale and retail trading businesses as well as construction businesses, all of which had recorded low growth. In addition, the sharp decline in the receipt of Revenue-Sharing Fund had put pressure on the economy in which spending was held back by limited fiscal capacity. Provinces outside Java, which were dependent on natural resources and experiencing quite a pronounced economic deceleration, were the coal producing ones, namely East Kalimantan and South Kalimantan.

The decline in Java's economic performance with the largest regional GDP share (58%) was instrumental in preventing the national economy from gaining full recovery. Slowing economic growth in Java was attributable to not only the effect of global economic slowdown but also the weakening of domestic economy. Export of manufactured goods that dominated the economic structure of Java was under pressure, both on overseas and domestic destination markets. Domestically, the decline in the export of manufactured goods from Java to provinces outside Java was due to the weakening of consumption in those provinces whose economy is based on natural resources. The phenomenon of Java's economic slowdown was also due to the declining competitiveness of its manufacturing industry.[6] In spite of this, however, robust consumption in Java was able to withstand further economic slowdown. The construction of various infrastructure projects supporting both connectivity or agriculture also had contributed to sustaining Java's economy, particularly in terms of investment and labor absorption.[7]

Improvement in KTI economy came from an increase in the output production of mining and industry. After the ban on the export of raw minerals in 2014, re-issuance of export permits for mine concentrates had provided a base effect factor on KTI economic performance, particularly in Papua and West Nusa Tenggara (Picture 10.1). The development of downstreaming policy characterized by the operation of smelter plants had also supported the economic performance of KTI regions especially Sulawesi with the operation of the two smelters in 2015. Construction of infrastructure projects in KTI, too, was a factor that could

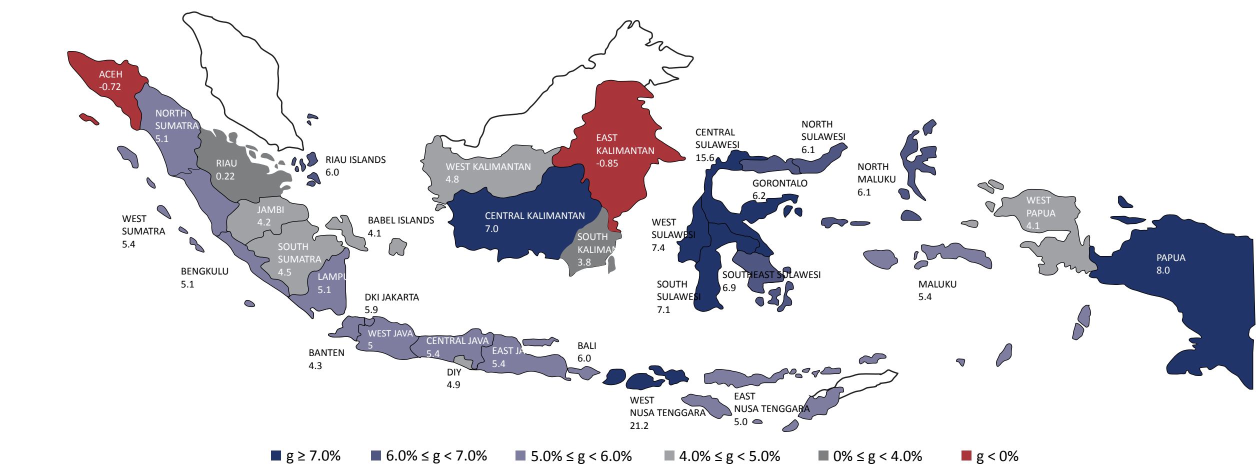
4 On the other hand, the growth of investment in Sumatra, Java and Kalimantan was slowing down, despite the support of the Government's infrastructure investment projects. Investment growth in these three regions was recorded at 3.3% (yoy), 4.3% (yoy), and 2.19% (yoy) respectively.

5 The economic growth of the provinces of Aceh, Riau and East Kalimantan in 2014 was still within the positive zone. Contraction of economic growth in the three provinces was a factor that lowered growth of Sumatra and Kalimantan. Depletion of oil and gas reserves had contributed to the decline in the performance of the oil and gas sector in these three provinces and in Aceh, which was also affected by the base effect factor of the cessation of the Arun gas refinery operations. Although efforts to convert Arun refinery into an LNG regasification plant had been made, its operation was still on a limited scale.

6 The decline in industrial competitiveness in Java was reflected in the decline in the share of industry in the regional GDP in the last 10 years. The decline in the share of the largest industries in the period was recorded in the provinces of East Kalimantan, Banten and Aceh.

7 Expansion of infrastructure projects in Java, which was mainly on transport infrastructure, was also a positive influence on the development of transportation and warehousing businesses, the business of providing accommodation and food and drink, as well as information and communication business. This condition was confirmed in Jakarta which has been conducting a large-scale transport infrastructure development (mass rapid transit).

Picture 10.1. **Regional Economic Growth in 2015 (2010 Base Year)**



Source: BPS-Statistics Indonesia, processed

give a positive impact (or multiplier effects) spreading from construction sector to transportation and warehousing businesses, and to financial services and insurance businesses as well. In terms of economic structure, the portion of the economy of provinces in KTI to the national economy had consistently increased over the last four years, thus indicating a signal of progress and equal development distribution.[8]

Sources of Sectoral Growth of Regional Economy

Agricultural sector grew in most regions in 2015. This was supported by the increase in the production of food crops whose biggest contribution came from increased rice production in Java. Java's agricultural sector increased significantly to 3.4% (yoy) in 2015, after growing 1.3% (yoy) in 2014. Special initiative in agricultural policy through the development of production infrastructure and facilities helped boost the performance of agricultural sector amid the risk of El Nino. The effect of El Nino on food crops production tended to be greater in regions outside Java, which rely on rain-fed land. Land conversion remained a challenge for the performance of agricultural enterprises, one of which was indicated from the decline in food crops production in West Java Province as a result of rapid urban and industrial zone development.

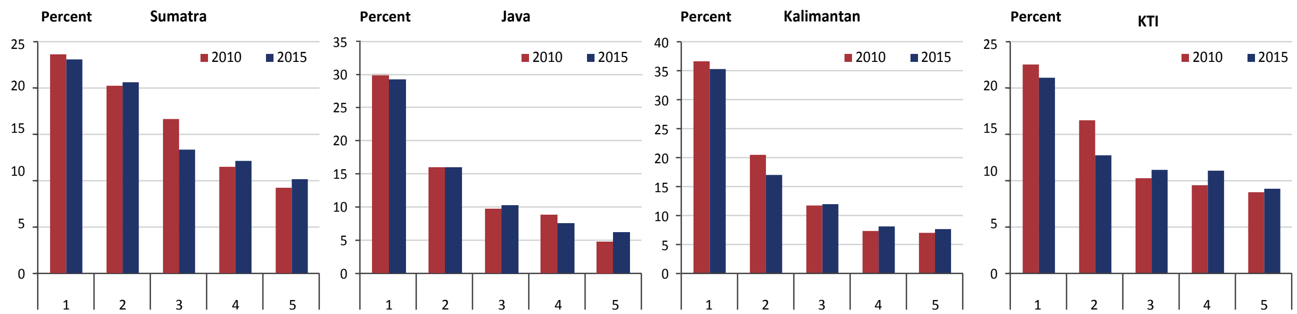
The continuing decline of the performance of plantation industries in all regions outside Java had prevented agricultural sector from posting a higher growth.

Weakening global demand and prices had become the main factor behind the decreasing performance of plantation industries. The underperformance of the plantation industries in Sumatra and Kalimantan was attributable to the decline in the export of palm oil and rubber. Meanwhile, the output of plantation industries in KTI was affected by weaker exports of cocoa, cloves, and nutmeg. The impact of extreme weather caused by El Nino and forest fires had led to the decline in the performance of plantation production in Sumatra and Kalimantan. The decline in palm oil production due to forest fires in both regions was estimated at approximately 15%. In general, the portion of agricultural sector in the regional GDP in most regions was lower than 10 years ago, which was strongly influenced by the performance of plantation industries (Chart 10.2).

Improved performance in the mining industries only occurred in KTI that grew by 18.8% (yoy) and became the main driver of growth of its economy. In addition to the re-issuance of licenses for exporting mineral and metal concentrates, the downstreaming on mining commodities that had been ongoing in KTI had also contributed to the improved performance of the regions' mining industries as the need for smelters' raw materials was growing. Meanwhile, the use of technology to help increase the productivity of oil and gas refineries was relatively still insufficient. This was reflected on the lifting of oil and gas in 2015 that tended to be lower than the previous year. The more permanent downward trend in production due to aging wells had been experienced by most of the oil and gas refineries in Sumatra and Kalimantan. Moreover, newly operated refineries such as the Cepu Block in Java had not reached their optimum production capacity yet.

8 Although progress has been made, equal development distribution outside Java, especially in KTI, was still in need of attention, especially as far as Human Development Index (HDI) is concerned.

Chart 10.2. Share of Regional GDP by Main Industrial Origin in The Region



1. Agriculture
2. Manufacturing
3. Mining
4. Wholesale and Retail Trades
5. Construction

1. Manufacturing
2. Wholesale and Retail Trades
3. Construction
4. Agriculture
5. Information and Communication

1. Mining
2. Manufacturing
3. Agriculture
4. Construction
5. Wholesale and Retail Trades

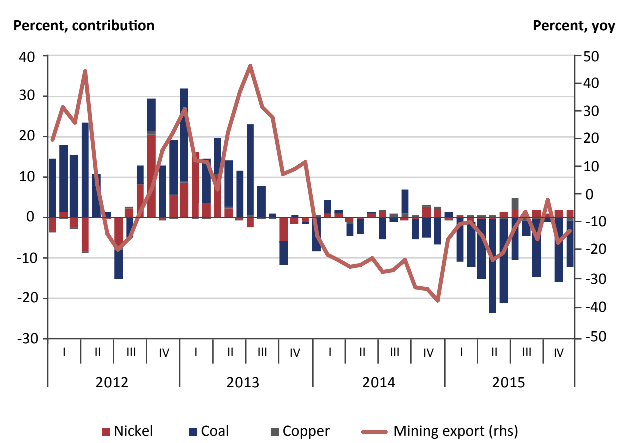
1. Agriculture
2. Mining
3. Wholesale and Retail Trades
4. Construction
5. Manufacturing

Source: BPS-Statistics Indonesia, processed

Mining industries slowed significantly in Kalimantan and Sumatra (Chart 10.3). The annual growth of mining industries in Kalimantan and Sumatra had contracted by 3.9% (yoy) and 2.8% (yoy) respectively. Mining operations in Kalimantan, whose share to the regional GDP was the largest, contracted for the first time within the last 5 years. The contraction was caused by the sharp decline in coal production, which went down by 75% compared to 2014, due to the decline in global demand, especially from China, and the lack of domestic demand. Meanwhile, the slowdown of mining industries in Sumatra was not as intense as in Kalimantan because Sumatra's economy was relatively more diversified. There was even an indication that coal production in South Sumatra had increased to meet the needs of a number of steam power plants, which began operation in 2015.[9]

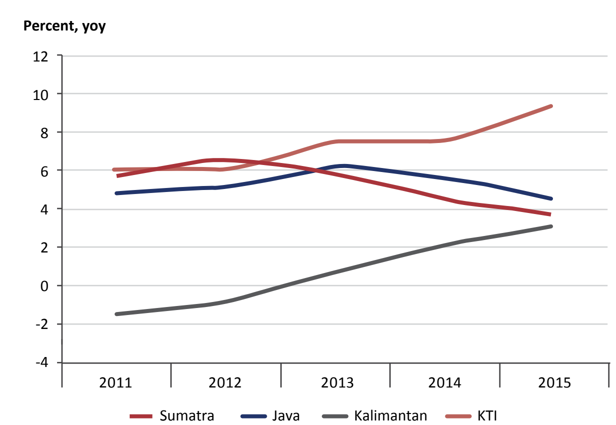
Manufacturing sector grew at a slower pace in Java, Sumatra, and Kalimantan (Chart 10.4), corresponding to the drop in export demand and the weakening of domestic demand for manufactured goods in Java, including motor vehicle products, textiles, and textile products (Chart 10.5). A liaison survey on businesses in the manufacturing sector confirmed that sales performance was mostly lower than 2014. The manufacturing sector, especially in Java, was also burdened by the dependency on the import of raw materials and an increase in production costs that affected

Chart 10.3. Mining Growth in Kalimantan and KTI



Source: BPS-Statistics Indonesia, processed

Chart 10.4. Regional Manufacturing Growth



Source: BPS-Statistics Indonesia, processed

9 A steam power plant with a capacity of 1,060 MW had been operated in southern and central Sumatra and another one with a capacity of 580 MW had been operated in northern Sumatra.

Chart 10.5. Java Manufacturing Export

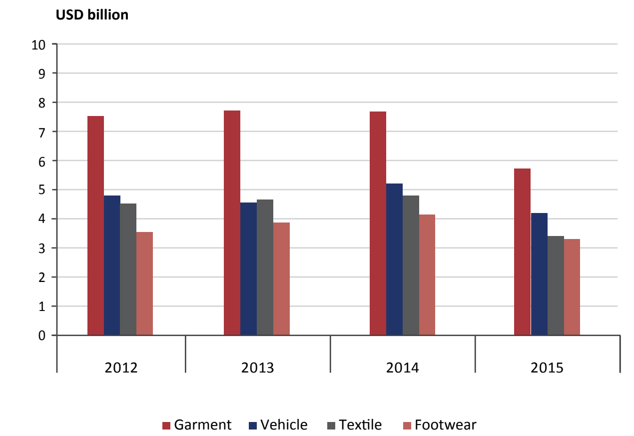
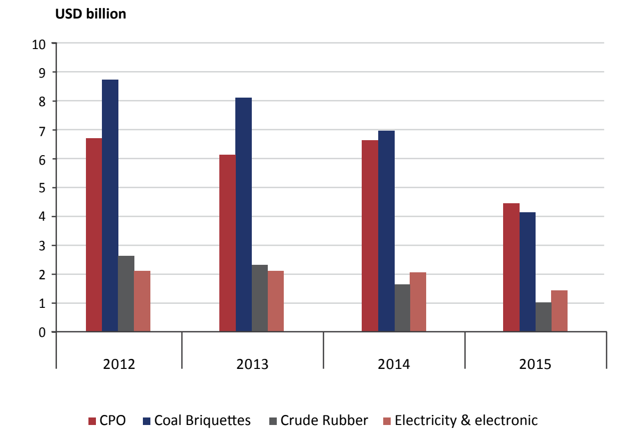


Chart 10.6. Sumatra and Kalimantan Manufacturing Export



competitiveness. The weakening of domestic consumption in regions outside Java had also posed a challenge for the sale of manufactured products in Java. In addition, the export of products from natural resource-based industries in Sumatra and Kalimantan such as palm oil and processed rubber products had also fell, mostly due to lower global demand (Chart 10.6).

On the other hand, manufacturing sector grew in KTI in line with the implementation of downstreaming policy. The operation of the Donggi Senoro LNG plant in Central Sulawesi Province and the operation of a number of ferronickel smelters in Central and Southeast Sulawesi provinces in 2015 had became the driving force behind increased industrial growth in KTI. Rapid industrial growth in KTI was also supported by financing from the banking sector which was recorded to have the highest growth. The progress of industrialization in KTI in recent years was reflected in a shift in the structure of growth across the regions (Chart 10.2). The decline in the share of regional GDP in mining sector was compensated by an increase in the share of manufacturing sector. This confirmed the existence of diversified economic structure and supported the indication of higher KTI's potential output growth.[10]

The performance of wholesale and retail trading sectors was declining in most regions, particularly in Kalimantan and Sumatra due to the weakening of people's purchasing power and limited revenues from the export of mining commodities. This was made worse by forest fires and haze disasters that disrupted economic activities in both regions. Sales turnover was estimated to decline in few provinces in Kalimantan and Sumatra by 40% -50% and 20% -30% respectively during the occurrence of haze. This was confirmed by the fact that the growth in household consumption and consumer confidence index was lower in Kalimantan and Sumatra, and the slowdown in credit expansion for wholesale and retail trading sectors in most regions. Wholesale and retail trading sectors in Java were still able to grow higher. This condition was affected by the commencement of large-scale infrastructure development and income improvement in the agricultural sector. Simultaneous regional elections in 263 provinces, districs, and municipalities had also had an impact at a moderate level. However, household consumption in Java declined slightly in 2015 in line with the moderation in consumer confidence. Meanwhile, wholesale and retail trading sectors were still able to grow higher in KTI, sustained by an increase in consumption and investment, in both mining (smelter) and infrastructure construction.

Construction sector grew slower in most regions in 2015, amid increasing intensity of infrastructure development. The slowing of construction performance, especially in Kalimantan and Sumatra, was the result of the lack of private construction projects. Construction sector in both regions slowed down considerably from 7.6% (yoy) to 2.8% (yoy) and from 7.0% (yoy) to 4.2% (yoy) respectively, thus contributing to increased credit risk in the construction business. The performance of the construction sector in Java slowed slightly as it grew by 4.8% (yoy) amid the ongoing construction of a number of agricultural infrastructure projects (dams and irrigation) and transport connectivity projects as well, such as the Jakarta Mass Rapid Transport (MRT) system, the Trans-Java highway, and airport expansion projects. Meanwhile,

10 On the other hand, the potential outputs of the other regions still tended to decline. Potential output was calculated using HP Filter with Regional GDP data from 2008 to 2015.

construction sector in KTI posted a higher growth, spurred by infrastructure and smelter construction projects. These developments boosted an increase in the rate of growth of the construction sector from 8.3% (yoy) to 9.6% (yoy) in KTI.

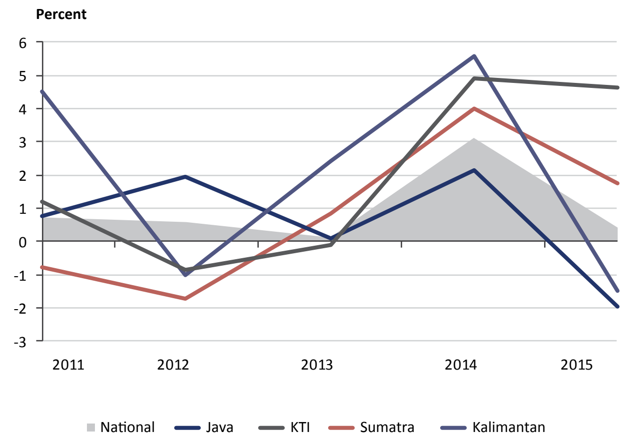
The progress of the government infrastructure projects that supported construction sector performance was evident in many regions. Based on monitoring and evaluation data from the Team for the Evaluation and Monitoring of Budget Realization (TEPRA), the realization of physical projects, especially in Sumatra and Kalimantan, was inline with the progress of power plants and new airports construction projects.[11] Of the total additional capacity of the steam power plants and mini gas power plants of 2,600 MW, approximately 63% were located in Sumatra. The large-scale airport projects in Kalimantan in 2015 included the expansion of the Supadio airport in Pontianak, West Kalimantan, and the construction of the Muara Teweh airport in North Barito and the Maratua airport in East Kalimantan. As far as agricultural infrastructure was concerned, construction was focused on 16 reservoirs spread in different regions. There were three reservoirs (Payaseunara and Marangkayu Rajui in Aceh and East Kalimantan respectively) that were nearing completion in 2015. Meanwhile, the progress of road construction was also visible in several regions, including, among others, the Trans-Sumatra toll road project and the Trans-Java toll road project (connecting the cities of Pejagan-Pemalang, Semarang-Solo and Solo-Ngawi).

Regional Employment and Welfare Condition

Growth in labor force decreased in all provinces across the country in 2015, particularly in Kalimantan and Java (Chart 10.7).[12]. Due to the uncertainty and volatility of natural resource-based economy, the majority of the workforce in provinces whose economy depends on natural resources were presumed to look for work in other provinces that had more favorable prospect of employement or went somewhere else in order to pursue higher education.

Economic contraction in Kalimantan, which occurred throughout the year, had led to the increase in unemployment rate, in correspondence with termination of employment in the mining sector. The

Chart 10.7. Growth of Regional Labor Force

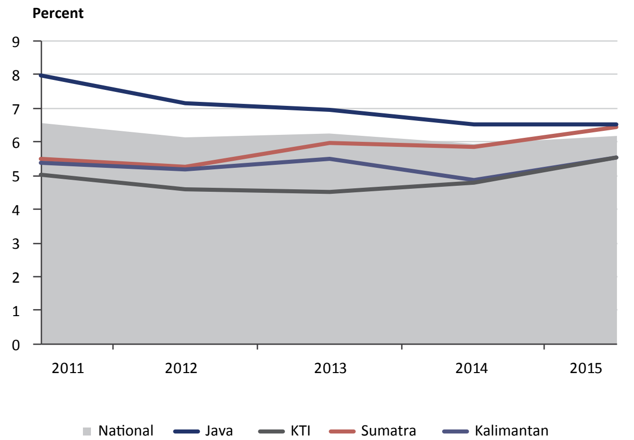


Source: BPS-Statistics Indonesia, processed

highest unemployment rate (7.5%) was recorded in East Kalimantan. Labor force had also declined quite significantly in Java, although open-unemployment rate tended to remain stable (Chart 10.8). In Java, agriculture and trade sectors that were still experiencing growth had helped labor absorption and increase in construction activity, due to the development of a number of large-scale infrastructure projects. On the other hand, the underperformance of a number of manufacturing subsectors had contributed to the unemployment level in Jakarta (7.2%) and West Java (8.7%) which were above the national average.

The growth of labor force in Sumatra and KTI had also decreased in 2015. The impact of the economic slowdown was reflected in increased unemployment, particularly

Chart 10.8. Regional Unemployment Rate



Source: BPS-Statistics Indonesia, processed

11 TEPRA data came from financial and physical project realization reporting submitted by regional Governments every month.

12 Residents who belong to the country's labor force are people of working age population (15 years and older) who are employed or self-employed, or have a job but are temporarily out of work and those who have no job.

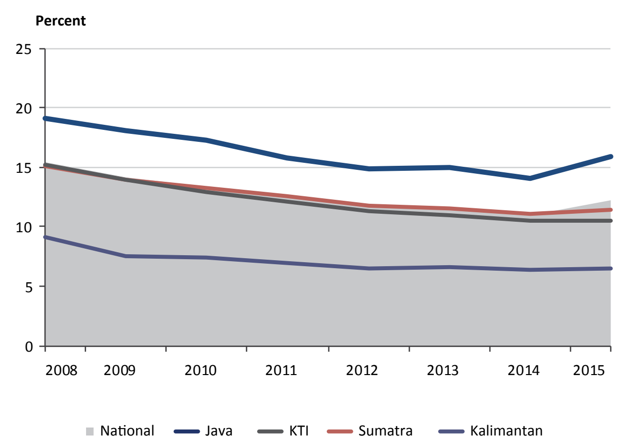
in Sumatra, which reached 6.4%. Provinces in Sumatra with a high unemployment rate were Aceh (9.9%) and Riau (7.8%). Meanwhile, unemployment rate in KTI was the lowest nationwide. The unemployment rates of most provinces in KTI were below the national average except in East Kalimantan, North Sulawesi, Maluku and West Papua. The lowest unemployment rate in KTI was recorded in Bali (2%).

Distribution of unemployment across provinces showed an increasingly narrowing trend (Chart 10.9). This indicated higher inter-provincial labor force movement, thus implying more optimal absorption in the labor market.

Hence, the distribution pattern of the unemployment rate showed that most of the provinces whose ratio to the regional GDP was quite small were the ones that had a relatively larger informal sector, which enabled them to absorb more labor.

Poverty rate increased in all provinces in line with economic slowdown in 2015. The poverty rate in KTI rose quite considerably, far above the national average in spite of economic expansion at the same time (Chart 10.10). Of the total 13 provinces in KTI, 11 were recorded to have a poverty rate that reached double digits. Papua, West Papua, and East Nusa Tenggara were the regions with the highest poverty rates in the last 5 years. Jakarta with a larger and more diversified economy had the lowest poverty rate compared to other provinces in the last 5 years. The informal sector which tended to play a dominant role in Jakarta appeared to serve as a buffer against economic slump. Kalimantan whose economic growth was the weakest compared to other regions had, in recent years, been able to keep poverty rate at the lowest end.

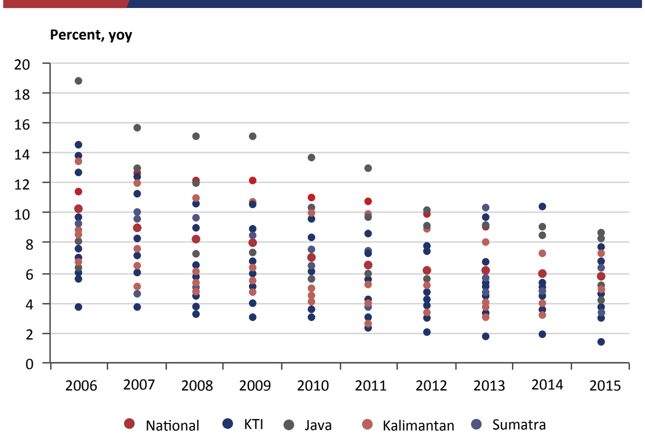
Chart 10.10. Regional Poverty Rate



Source: BPS-Statistics Indonesia, processed

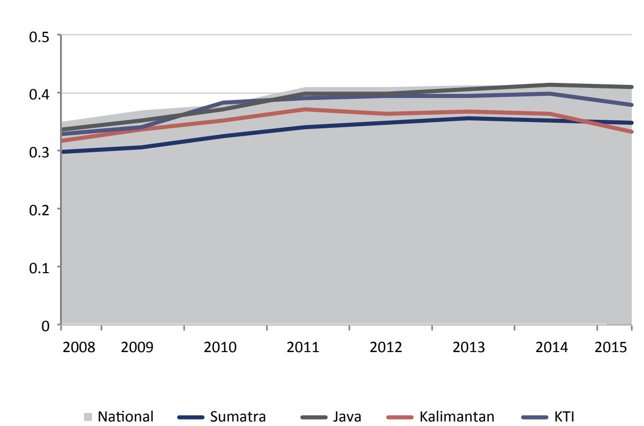
The gini ratio had also indicated lack of significant improvement to address inequality in most provinces. The gini ratios in Java and KTI were higher than in other regions in 2015 (Chart 10.11). However, inequality in KTI tended to decline in 2015, whereas in Java it was still equivalent at the national average level (0.41). Spatially, the highest gini ratio was recorded in the provinces of West Papua (0.44), DKI Jakarta (0.43), and the Special Region of Yogyakarta (0.43). Significant reduction in gini ratio occurred in North Sulawesi and Bali, while in Sumatra and Kalimantan the gini ratio was below the national average. The trend within the last 5 years indicated that gini ratio tended to increase as the effect of the boom in natural resource commodity

Chart 10.9. Regional Disparities in Unemployment Rate



Source: BPS-Statistics Indonesia, processed

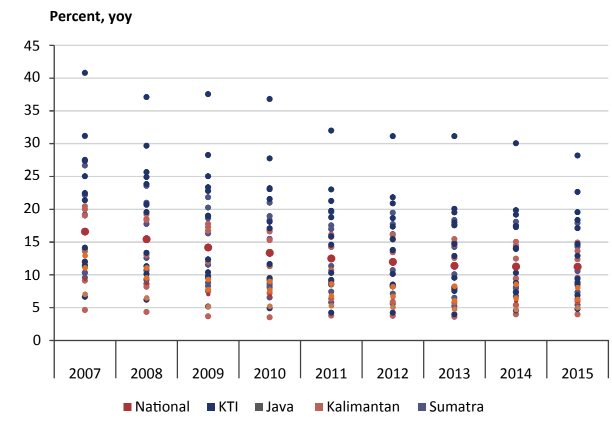
Chart 10.11. Gini Ratio



Source: BPS-Statistics Indonesia, processed prices which reduced the inclusiveness of economic growth in some regions.

In general, the distribution of poverty in various provinces also showed an increasing tendency of narrowing. In 2015, the lowest poverty rate was recorded in Jakarta (3.6%) and the highest was recorded in Papua (28.4%). The overly wide disparity in the levels of poverty between Jakarta and Papua reflected the severity of poverty in KTI in comparison to Java. Poverty rates below the national average were for the most part recorded in KTI and Sumatra (Chart 10.12) whereas in Java and Kalimantan the distribution of poverty tended to be below the national average.

Chart 10.12. **Regional Disparities in Poverty Level**



Source: BPS-Statistics Indonesia, processed

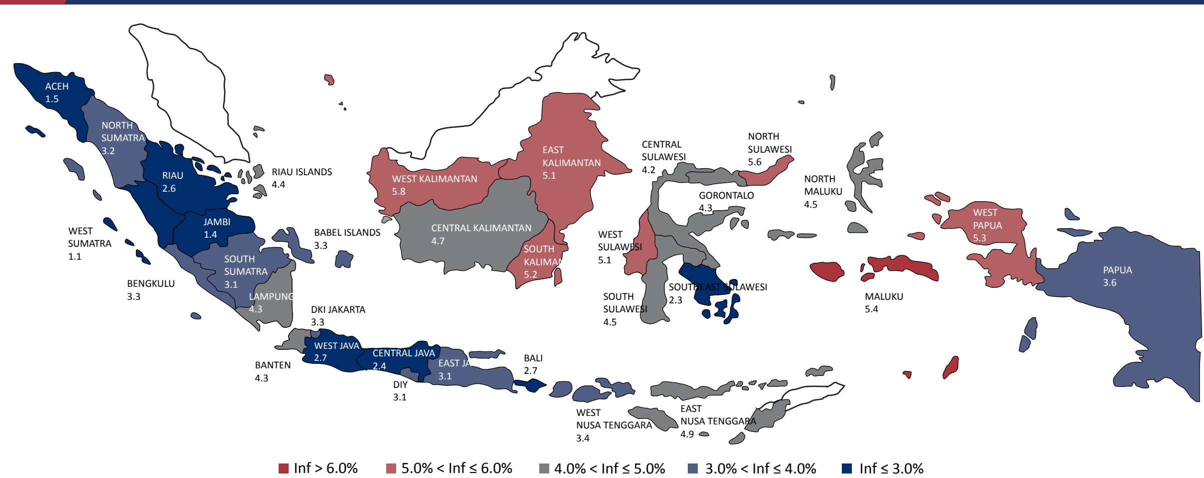
10.2. REGIONAL INFLATION

Regional Inflation Dynamics

The decline in regional inflation rates in 2015 occurred throughout the country, especially in Java and Sumatra.[13] As in 2014, sustained supply and smooth distribution of food commodities (Picture 10.2) were also instrumental in checking inflation in these two regions. The impact of El Nino that occurred in 2015 was relatively moderate on most areas of Java that served as the national food production center.

On the other hand, Kalimantan and KTI were experiencing relatively higher inflationary pressure due to disruption in the distribution of goods and services because of insufficient transport connectivity and limited infrastructure capacity and quality. The impact of the reduction in fuel prices was uneven spatially, due to variations in freight rates that were set through local government legislation.[14] In that regard, the Regional Inflation Monitoring and Controlling Team (TPID) continued to actively play its role of supporting measures to control inflation at regional levels through coordination

Picture 10.2. **Regional Inflation in 2015 (Percent, yoy)**



Source: BPS-Statistics Indonesia, processed

13 The share of Java and Sumatra's inflation rates, which stood at 62% and 19.6% respectively (according to the 2012 Cost of Living Survey), was the highest nationwide. Of the 14 provinces in Java and Sumatra, only one province in the Western Part of Java and two provinces in the Southern Part of Sumatra which recorded inflation rates above the national average.

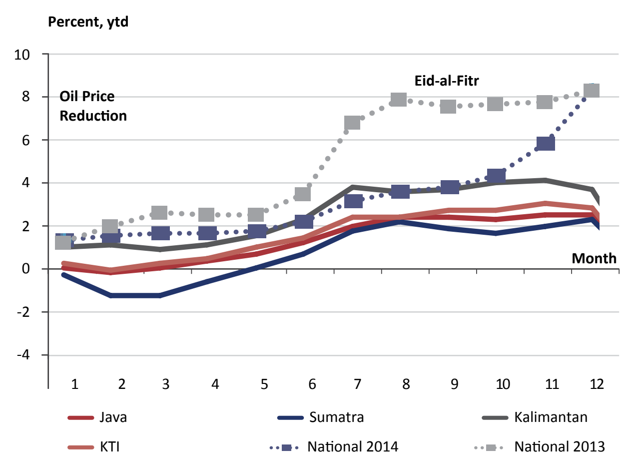
14 Variations in regional transport fare adjustments after the decline in fuel prices in January 2015 referred to a tariff reduction range of 5-10% under the regulation of the Minister of Transportation. In addition, the timing for transport fare adjustment also differed among regions due to the local regulations on transport fare setting mechanism that had to take into account the inputs from the local organizations of land transportation owners and operators.

of short-term policies and policies that were directed to address a more structural factor of inflation.

Inflationary pressure during the Eid-al-Fitr period in 2015 that was more moderate than the average over the last few years was also a factor that brought down inflation in most regions. The economic slowdown that occurred in 2015 had affected consumer purchasing power and demand, especially in Sumatra, Java, and KTI. Minimum disruption in the distribution and adequacy of food supplies in most regions had also helped control regional inflation during the Eid-al-Fitr period. On the other hand, inflation in Kalimantan during the Eid-al-Fitr period tended to be higher, driven by rising food prices and air freight rates (Chart 10.13).

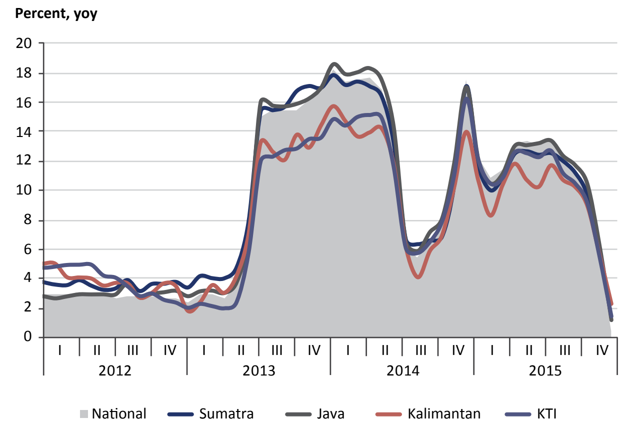
Spatially, Sumatra and Java recorded the lowest inflation rates in 2015 due to moderate demand and adequate supplies. Inflation rates in Sumatra and Java were recorded at 3.05% (yoy) and 3.12% respectively, the lowest within the last 6 years (Chart 10.14). The fall in inflation rates in Sumatra was brought about by a significant reduction in inflation in West Sumatra, Bengkulu, Jambi, and Aceh. The lowest inflation rate nationwide was recorded in West Sumatra (1.08%).[15] In Java, the largest decline in inflation occurred in Banten, Jakarta, and Central Java. Increased production of food crops in Java had helped secure the availability of food supplies and the stability of food prices.

Chart 10.13. Pattern of Regional Inflation



Source: BPS-Statistics Indonesia, processed

Chart 10.14. Development of Regional Inflation 2012-2015



Source: BPS-Statistics Indonesia, processed

Despite being lower than in 2014, inflation rates in Kalimantan and KTI in 2015, which were recorded at 5.12% and 4.06% respectively, were higher than the national inflation figure. The highest inflation in Kalimantan occurred in West Kalimantan Province (5.79%). Although demand was likely to weaken in line with significant economic slowdown in Kalimantan, limited transport connectivity and transportation facilities were still a major cause of inflation. Inflation in the sub-group of transportation was specifically an issue in West Kalimantan, due to the frequent increase in air freight rates. In KTI, provinces with relatively high inflation rates were Maluku, West Papua, North Sulawesi, and West Sulawesi. The highest inflation rate nationwide that reached 6.15% was recorded in Maluku.

Inflation that was still quite high in KTI was affected by foodcommodity prices, especially those of freshly caught fish commodities that were greatly weighted in the inflation basket. Moreover, in contrast to the condition of Kalimantan, the significant increase in KTI's economic growth was also a factor that led to stronger demand.

The impact of forest fires and the haze from the smoke of the forest fires on regional inflation was more concentrated in Kalimantan. Although the intensity of forest fires and the resulting haze were relatively more extensive in Sumatra, the damaging impact of the haze was more prevalent in Kalimantan.[16] Disruption of flights and distribution of goods by road, river and air adversely affected the availability of supplies and price stability in

15 West Sumatra recorded the highest inflation rate in 2014 and experienced the most significant decline in inflation in 2015, which stood at 9.67%. Operation of agribusiness terminals and collaboration between city governments were considered as one of the factors that contributed to the stabilization of food prices.

16 Although there was a disturbance in the distribution of goods in Sumatra, there were adequate supplies. It is caused also by the declining demand, associated with the lack of public mobility in conducting trade activities

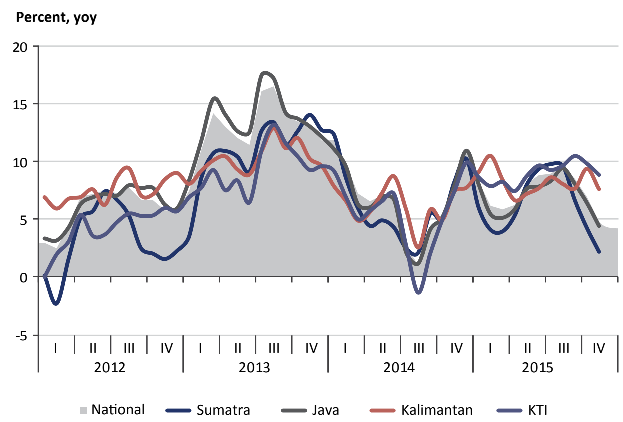
Kalimantan, especially in West Kalimantan and Central Kalimantan, which were the worst hit by the haze.

Sources of Regional Inflation

Significant decline in the administered prices inflation was mainly responsible for lower regional inflation in 2015. This happened mainly as a result of the cut in fuel prices and transport fares adjustment. The most significant impact of the reduction in fuel prices and transport fares was indicated in Kalimantan at the beginning of the year. In addition to land transport tariff reduction policy, adjustment made to river transport tariffs had also significantly affected the distribution cost of goods in Kalimantan. Sampling in a number of regions showed that the highest land transport tariff reduction was recorded in Sumatra (11.4%), followed by Java (9.8%), and Kalimantan (5.5%). However, compared to land transport fare adjustment after the increase in fuel prices in 2014, the tariff reduction in 2015 was far more moderate throughout all regions. On the other hand, there had been an increase in the price of household fuels (BBRT) and economical electricity tariff adjustments that applied throughout the region. The impact of regional inflation as a result of BBRT adjustment was subjected to disparities between the distribution costs and local government regulations that set the highest retail prices of LPG.[17] On average, the highest selling price of LPG was recorded in Sumatra, followed by Kalimantan and KTI. The average selling price of LPG in Java was lower due to lower distribution costs which, in turn, were due to the established transport infrastructure.[18]

Inflation under the foodstuff category contributed to the varying degree of decline in regional inflation in 2015 across the regions. The deepest decline in inflation under the foodstuff category was recorded in Sumatra and Java (Chart 10.15). This was in line with the relatively moderate demand, the adequacy of food supplies, as well as the smooth distribution of foodstuffs. Slightly declining demand as a result of forest fires and haze that lasted from February to October 2015 was also a factor that led to inflation decline under the foodstuff category in Sumatra.

Chart 10.15. Foodstuff Inflation



Source: BPS-Statistics Indonesia, processed

Inflation under the foodstuff category experienced a decline in Sumatra, especially in the sub-category of spices that recorded a 28% decrease for the whole year.[19] Meanwhile, the decline in inflation under the foodstuff category in Kalimantan and KTI was more moderate, sustained by well-maintained supply, especially in the sub-category of grains, meat, and spices.

Controlled inflation of rice commodity in some regions was due to sustainable supply of rice produced domestically.[20] It was monitored that the rate of inflation of rice commodity in Java was lower than its historical figures (7.5%, yoy); so, it helped decrease the inflation of food items under the foodstuff category in the region (Chart 10.16). Despite being subjected to the effects of El Nino in 2015, the production of rice in Java was indicated to have increased due to the improvement of productivity and optimization of irrigation networks. In Kalimantan, the decline in rice commodity inflation was relatively lower, as a result of which inflation of food items under the foodstuff category didn't decrease much.

Inflationary pressures on commodities subjected to core inflation were relatively restrained in 2015, except

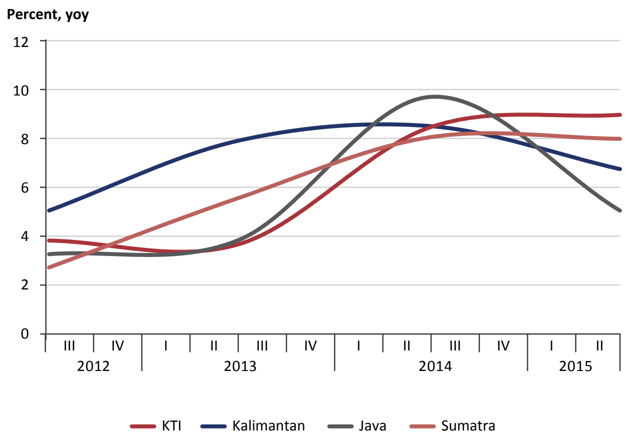
17 The impact of electricity tariff adjustment on regional inflation, too, was varied, influenced by the number of consumers in each group of electrical power subscription that differed from region to region. In connection with economical electricity price adjustment in 2015, which was targeted at subscribers of 3500-6500 watts of power, the impact on Java was relatively greater compared to other regions.

18 The average selling price of LPG in Java was around 11.7% lower than in Sumatra (calculated using official selling prices by Pertamina marketing regions after a price hike in January 2015).

19 A drastic reduction of inflation in the sub-category of spices in Sumatra might offset inflation in rice commodity that was higher in 2015 (7.98%) compared to the previous year.

20 Projected rice production based on Forecast Figure II (ARAM II) indicated an increase both in Java and outside Java in 2015. In spite of this, there were a number of regions that were more strongly affected by El Nino than the other, and thus affected the performance of local rice production. The impact of El Nino in KTI tended to expand, especially in the northern part of KTI (Gorontalo and North Sulawesi), but the decline in production was relatively moderate thanks to the addition of agricultural land. Rice inflation in KTI in 2015 nearly reached 9%, the highest compared to all other regions.

Chart 10.16. Inflation of Grains Sub-Category



Source: BPS-Statistics Indonesia, processed

for Kalimantan. Inflationary pressures on commodities subjected to core inflation mainly came from processed food commodities. In addition to the demand and the weakening of the exchange rate of the rupiah that affected the production costs of processed food, there were also factors associated with domestic raw material prices. The volatility of the prices of local foodstuffs such as rice, beef, and chicken had driven the increase in the rate of inflation of finished food products such as rice and its side dishes. In Java, finished food products accounted for 18% of the overall CPI inflation in 2015. In Sumatra, Kalimantan and KTI, the contribution of the prices of finished food products to inflation was 14%, 21%, and 13% respectively. The greatest increase in the prices of finished food products was recorded in Kalimantan (10.6% yoy). This was attributable not only to food price hikes, but also increased BBRT prices.[21] Disparities in inter-regional distribution costs were also responsible for causing selling price variations of finished food products including processed food manufactured by industry.

Inflation in commodites included in core inflation in the entire region was also affected by the adjustment of wages and cost of living. A significant increase in minimum wages in some provinces had also contributed to the increase in core inflation due to wage adjustments in services.[22] The increase in the cost of living, especially in the housing and education categories contributed substantially to the overall CPI inflation in most regions. Housing costs were responsible for the largest inflation in Sumatra, which stood at 13%, followed by Kalimantan and KTI at 12% and 10% respectively. In Java, the cost of living's contribution to inflation was only 9%. In addition to the increase in demand and the public income level, a shortage of housing supply and construction costs that were relatively higher had also affected the inflation in housing cost category in regions outside Java. Another cost of living component that also affected regional inflation in 2015 was the cost of education whose contribution was the largest to the overall CPI inflation recorded in Sumatra and Java, each of which stood at 5%.

Challenges of Regional Inflation Control

The challenge of controlling inflation was strongly associated with increased food production and productivity. It was urgent to pay attention to the improvement (revitalization) of agricultural infrastructure in Java and agricultural infrastructure development outside Java.

Most recent data indicated that approximately 59% of irrigation networks under the authority of city/ district governments and approximately 53% of the irrigation network under the authority of provincial governments were in a damaged condition. A larger allocation to agricultural infrastructure financing in 2015 became the starting point of efforts to push for increased agricultural production and productivity through improved irrigation systems.

Inter-provincial trade cooperation is also a challenge in the medium to long run as far as controlling regional inflation is concerned. Trade cooperation, especially in order to maintain the supply of food commodities throughout the whole country is indispensable. This is linked to whether there is a food surplus or deficit from province to province and also to the production sustainability that affects food trade regulation. Realization of trade cooperation between one province and another is currently not quite optimal

21 The increase in volatile food inflation in Kalimantan confirmed the transmission of price inflation from foodstuffs to finished food product commodities. The upward trend in core inflation in Kalimantan that had been ongoing in recent years was presumed to be due to lack of efficiency of the logistics system in the region.

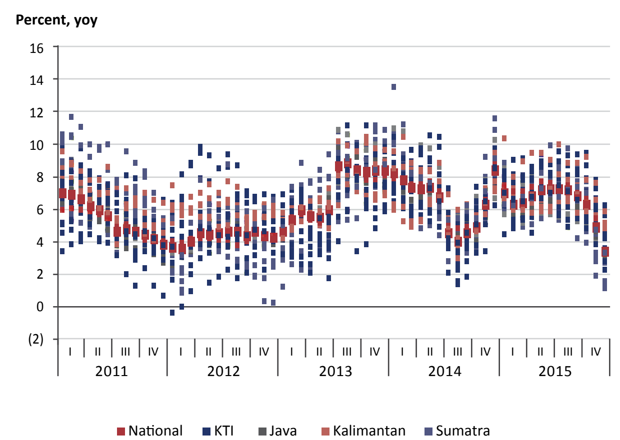
22 Provincial minimum wage (UMP) in the whole area rose at an average of over 10%. The minimum wage in Java increased by an average of 17% with substantial variations between regions. UMP in Banten increased 43%, while in Jakarta increased by 11%. As for the other provinces in Java area, a new UMP was not set. The average minimum wage in districts / cities (UMK) in East Java, Central Java, West Java, and Yogyakarta each rose 18%, 15%, 15% and 8%. In regions outside Java, the provinces with the highest increase in UMP are Bangka Belitung, Gorontalo, and Central Sulawesi with an increase of over 20%.

yet in spite of a number of initiatives that were taken in 2015.[23]

Convergence of regional inflation remained a challenge in controlling regional inflation in 2015. Compared with 2014, the gap between the highest and lowest inflations between regions increased in 2015 (Chart 10.17).[24] Geographically, the largest convergence of inter-regional inflation was seen in Sumatra and KTI as it also increased compared to the previous year.

Meanwhile, inflation convergence between provinces in Java was the lowest and was decreasing significantly. This condition indicated there were still challenges in the distribution and improvement of the trade regulation system. Smooth distribution would have a direct impact on increasing efficiency through reduction in distribution costs which had a significant portion in the structure of logistic cost. A number of connectivity supporting infrastructure development that begun in 2015, had an important role in supporting future inflation control in regions. Effort had been made to address these challenges through the creation of the Regional Inflation Control Roadmap. Inflation control policies and programs were expected to be more measurable and more focused on structural inflation risks that became the priority of the Regional Inflation Control Team (TPID) throughout the provinces.

Chart 10.17. Regional Inflation Convergence



Source: BPS-Statistics Indonesia, processed

10.3. REGIONAL FISCAL

In aggregate, total local budgets revenue increased 16,7% in 2015 despite economic slowdown.[25] Such significant increase results from the increase in transferred funds that included fiscal balance transfer and special autonomy funds (7.9%) and the provision of village funds amounting Rp20.77 trillion (under the 2015 Revised State Budget). An increase in local budgets (APBD) that was quite significant was indicated in parts of Java and KTI. Meanwhile, the increase in the local budgets in Sumatra and Kalimantan was relatively moderate. Of all the provinces, only East Kalimantan Province allocated a budget that was lower than in 2015, due to an expected decline in oil and gas revenue sharing funds (DBH). On the other hand, a handful of some other provinces whose economy was also based on natural resources such as Aceh, Riau, South Sumatra, South Kalimantan and West Papua, allocated a higher budget and yet the increase was moderate.

Realization of Local Revenue

Local fiscal realization showed a lower performance in 2015, especially in terms of revenue as regional economic slump in most regions led to lower revenues from taxes and levies, which constituted a major source of Local Revenues (PAD). On the expenditure side, amid an increase in the number of transfers to regions allocated for the development of strategic infrastructure projects, local governments were still unable to properly address annually recurring issues. This condition indicated fiscal stimulus failure to withstand worsening economic slowdown in 2015.

In aggregate, local revenue realization in 2015 was lower than the previous year due to a decrease in Local Revenues (PAD) and fiscal balance transfer. The PAD realization was forecasted to reach 108.3% in 2015, lower than the previous year and the average over the last 3 years (Table 10.1). Due to economic slowdown affecting trading and service-based business activities, targetted reveneus from various types of taxes and levies could not be achieved.[26]

23 Inter-provincial trade cooperation that was realized in 2015, including among others between the Government of the Province of the Special Capital Region of Jakarta and the Government of West Java Province in order to meet the need for rice in Jakarta and between the Government of the City of Pontianak and the Government of City of Probolinggo was focused on meeting the need for shallots in Pontianak.

24 In a longer period of time, the convergence of regional inflation rates would tend to narrow down, probably as a result of economic slowdown that had been ongoing over the last 3 years.

25 Total regional budget allocation for expenditure amounted to IDR922.4 trillion, representing approximately 42% of the total state expenditure (of the Central Government and Regional Governments).

26 The decline in trading and service-based business activities had reduced the amount of revenue generated from motor vehicle tax, motor vehicle fuel tax, hotel and restaurant tax, advertisement tax, and land and building (property) tax.

Table 10.1. Estimation of Regional Budget Realization in 2015

	2014			2015			
	Regional Budget	Realization		Regional Budget	Average 3 Years	Realization*	
Revenues	**759.5**	**799.4**	**105.3%**	**859.9**	**108.4%**	**882.96**	**102.7%**
Own-source Revenue	180.4	199.7	110.7%	222.9	116.1%	241.44	108.3%
Regional Fiscal Balance Funding	482.2	476.0	98.7%	498.6	101.6%	475.19	95.3%
Other Regional Legitimate Revenues	96.9	123.6	127.6%	138.4	-	166.32	120.2%
Expenditures	**817.7**	**764.0**	**93.4%**	**922.4**	**92.4%**	**864.38**	**93.7%**
Personnel	326.7	313.0	95.8%	371.1	109.9%	346.09	93.3%
Goods and Services	182.5	165.6	90.8%	202.8	96.8%	187.94	92.7%
Capital	213.7	181.0	84.7%	228.1	91.3%	206.03	90.3%
Others	94.7	104.3	110.1%	120.4	-	124.32	103.2%

Source: Directorate General of Fiscal Balance, Ministry of Finance (*estimation using preliminary data at the beginning of March 2016)

The amount of fiscal balance transfer had also decreased as the amount of revenue sharing funds (DBH) from natural resource processing as well as from tax sources such as income taxes had also decreased below the target due to layoffs in a number of provinces. Meanwhile, the amount of other local official revenues was higher than targetted, despite being lower than the one earned in 2014.

In order to strengthen local autonomy and implementation of infrastructure development, fiscal balance transfer to regions had increased significantly in the 2015 Revised State Budget. After the revision of the State Budget, fiscal balance transfer had increased by 2.7% and were broken down into Special Allocation Fund (DAK), Special Autonomy Fund (Otsus), Special Fund for the Special Region of Yogyakarta, and Village Fund.[27]As a result, DAK got an additional allocation of Rp25.8 trillion or twice the amount alloted to it under the state budget prior to the revision to support districts / municipalities in under-developed and border regions whose financial capacity was relatively low. Increased DAK was also meant to support the commitment of priority programs in infrastructure sector. Papua and Aceh in 2015 also obtained an additional Special Autonomy Fund to help finance infrastructure development.

In the meantime, under the Revised State Budget, the amount of allocated village funds was doubled to Rp20.8 trillion in order to accelerate development in rural and under-developed regions.[28] However, the realization of fiscal balance transfer in 2015 was lower than their allocation, due to the decline in oil and gas revenue sharing funds (DBH), in line with the trend of oil and gas prices that continued to weaken. Realization of fiscal balance transfer only reached 95.3%, lower than in 2014 and the average recorded 3 years ago.

Realization of Local Expenditure

Absorption of local spending in 2015 was estimated to be no higher than the previous year. Realized regional spending was projected to reach around 93.7%, with the realization of personnel expenditure tending to be slightly lower. The allocation of personnel expenditures, which grew 13.6% in 2015, indicated lower absorption compared to previous years. However, the portion of personnel expenditure to total expenditure in 2015 was 13.2%, slightly increased over the previous year. Meanwhile, spending on goods and services as well as capital expenditure grew by 11.1% and 6.8% respectively in 2015, and it was forecasted that both would go far below the average in the last 3 years. Absorption of spending on goods and services was projected to reach around 92.7% while absorption of capital expenditure hovered around 90.3%. A number of constraints both in terms of administration and on-the- spot implementation were responsible for the low absorption of spending on goods and services as well as capital goods.

27 The amount of funds allocated by the Central Government to be transferred to regional Governments had increased by 11.4% from 2014, with funding coming from reallocation of fuel subsidies. The transfers made in 2015 to regional Governments accounted for 33.3% of the total expenditure set under the 2015 Revised State Budget, or 1.5% higher than those made in 2014.

28 The presidential Nawa Cita (Nine Ideals) vision includes the concept of nation building starting from the periphery by strengthening regional and village economies.

Geographically, it was indicated that the largest regional spending absorption was recorded in Kalimantan and KTI.[29] Realized spending in the two regions accounted for around 93.5% and 92.9% respectively with the highest spending absorption projected in Central Kalimantan and Gorontalo. In Sumatra and Java, spending absorption reached about 91.1% and 88% respectively. The lowest spending absorption was recorded in Jakarta, at mere 68.9%, as a result of the prolonged delay in the fixing of its budget and the trimming of some budget posts under its revised budget for efficiency. The other provinces whose budget absorption was also low, according to the data from the Team for Evaluating and Monitoring the Realization of State and Regional Budgets (TEPRA), were Central Java (72.5%) and Banten (73.6%).

Spending absorption tended to be lower in provinces whose economy was based on oil and gas resources. This might be a result of the significant decline in the amount of oil and gas revenue sharing fund (DBH) that had became the source of funding for their budgets, even though in nominal terms, the DBH increased by 11.2% in 2015. Under this condition, adjustments to spending realization were indicated in order to reduce potential budget deficit that was limited to 3.25-6.25% of PAD for 2015.[30] Another factor that also affected the condition was the downward trend in the accumulation of unused budget (SILPA) in a number of provinces whose budgets depended on oil and gas revenue sharing funds (DBH).

The low spending absorption in 2015 was also attributable to the delay in budget ratification in a number of provinces. A compilation of dates on which regional governments ratified their budgets in 2015 showed an improved trend in ratification schedule with 431 out of 548 provinces and districts/ municipalities managing to ratify their budgets on time in December 2014. However, there were indications that the number of local budgets whose ratification took place way beyond the first quarter of 2015 was greater, one of which was that of Jakarta. Delays in the ratification of Jakarta's budget whose amount was quite significant (about 7.3% of the aggregate local budgets), had had a quite significant impact on the performance of local budget absorption nationwide. Factors delaying local budget ratification included, among others, incomprehensive budgetary planning which led to lengthy deliberations, whose time period was even prolonged by a transition period due to a change in local leadership.

In realizing capital spending, there were also issues concerning land acquisition at local level. Challenges met in the process of land acquisition were critical and sensitive issues in some provinces. Although there had been clearer legal and statutory bases and mechanisms for land acquisition, in reality, land acquisition in some regional regions turned out to be a prolonged process. Besides causing delays and uncertainty, this had also affected the multi-year budget planing in a number of provinces.

Regional Fiscal Challenges and Effort to Accelerate Budget Absorption

Low regional spending absorption had led to extensive placement of government funds in the banking sector. As of June 2015, the placement of local government funds in the banking sector still showed an upward trend, just as in 2014. As of June 2015, regional government funds in the banking sector reached Rp279.8 trillion, the highest in the last 3 years. Of these, 37% belonged to regional governments in Java. A number of factors affected this condition, including a significant increase in the transfer of funds from the state budget to regional governments' coffers that was not accompanied by the strengthening of budget absorption capacity of regional governments. This condition was exacerbated by indications that a massive amount of village funds kept by the governments of some districts/ cities had not been transferred to designated villages.[31] Idle funds accumulating in banks were also responsible for making the amount of unused budget (SiLPA) quite high at the end of the year. This had also confirmed the lack of fiscal support to withstand regional economic slowdown in 2015.

Structural regional fiscal challenges also included persistent dependency of regional financing sources on fiscal balance transfer. PAD was still unable to fully cover total financing cost in most regions. In 2015, decreased revenue sharing funds (DBH) in provinces whose economy was dependent on the export of natural resources had suppressed their self-financing sources. This was also reflected in the decline in fiscal capacity in most regions

29 Projected target of spending actually realized by each regional government at the end of 2015 (monitored and evaluated by the Team for Evaluating and Monitoring the Realization of State and Regional Budgets (TEPRA)).

30 Minister of Finance Regulation Number 183/PMK.07/2014 on the Maximum Cumulative Limit of Deficit of Regional Budget (APBD), the Maximum Limit of Deficit of Regional Government Budget (APBD) and the Maximum Cumulative Limit of Regional Loans for the 2015 Budget Year.

31 This was mainly due to administrative issues pertaining to the ratification of revised village budgets (APB) that included additional village fund allocations derived from Revised State Budget (APBN-P).

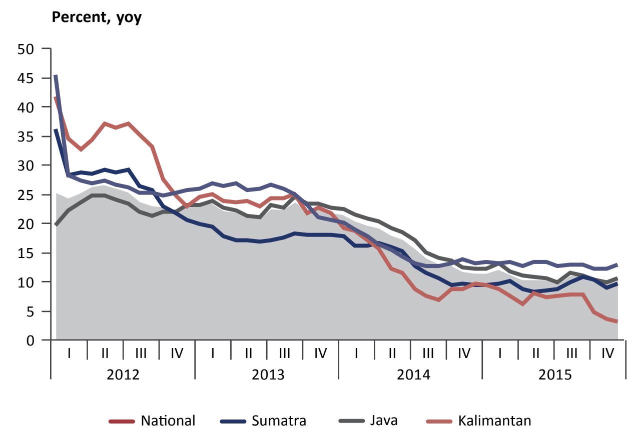
outside Java. Nonetheless, provinces with very high fiscal capacity other than Jakarta, that is, East Kalimantan, West Papua, and North Kalimantan, still continued to rely on exports of natural resources. The ratio of PAD to regional GDP in KTI was the lowest, while the highest, which was recorded in Kalimantan, was also affected by the efforts of local authorities to anticipate a decline in DBH.

A range of different initiatives had been undertaken by both the central government and the regional governments to accelerate the absorption of budget spending in 2015. Measures taken by the central government in general included the application of stricter monitoring of the reporting system on regional financial realization through the Team for the Evaluation and Monitoring of Budget Realization (TEPRA), revision of procurement rules, technology optimization to accelerate procurement (e-catalogs / the Government Procurement Agency (LKPP), e-procurement), and the imposition of an incentive (reward) and punishment system in order to encourage regional budget absorption (regional incentive funds). The Ministry of Home Affairs had also specially formed a team that would conduct direct monitoring of budget realization at regional levels.

10.4. REGIONAL FINANCIAL STABILITY

In 2015, corporate lending slowed down in all regions, particularly in Kalimantan and Java, which declined by 6% and 2.1% respectively compared to previous year. Lending to mining businesses in Kalimantan experienced the greatest pressure with a growth contraction of 2.8%, down 21.4% from 2014 (Chart 10.18).[32] The decline in the growth of credit extended to the mining industry both in Kalimantan and Sumatra, had impacted on the performance of credit extended to other businesses, primarily to those in the mineral processing and business support service industries (such as transportation and warehousing services, information and communications services, financial services, real estate, and corporate services). Meanwhile, the deepest slowdown of corporate lending in Java was recorded in the industrial sector both for working capital and investment purposes, as well as in the construction business. The growth of credit chanelled

Chart 10.18. Development of Regional Credit



to industry and construction businesses in Java decreased by 5.3% and 16.5% respectively compared to 2014.[33]

Corporate credit slowdown in Sumatra was the most moderate, sustained by credit that still kept on growing in the wholesale and retail trading sector and the industrial sector whose share was the largest in Sumatra.[34] Credit growth in the wholesale and retail trading sector stood at 10.9%, while credit extended to the industrial sector grew by 15.2%. Growth in corporate loans in KTI had also slowed but at moderate level thanks to economic performance that still kept on improving. Corporate loans whose growth was high in KTI were the ones extended to the industrial sector (41.6%), the agricultural sector (28.3%), the mining sector (12.1%), and the corporate service sector (9.7%).

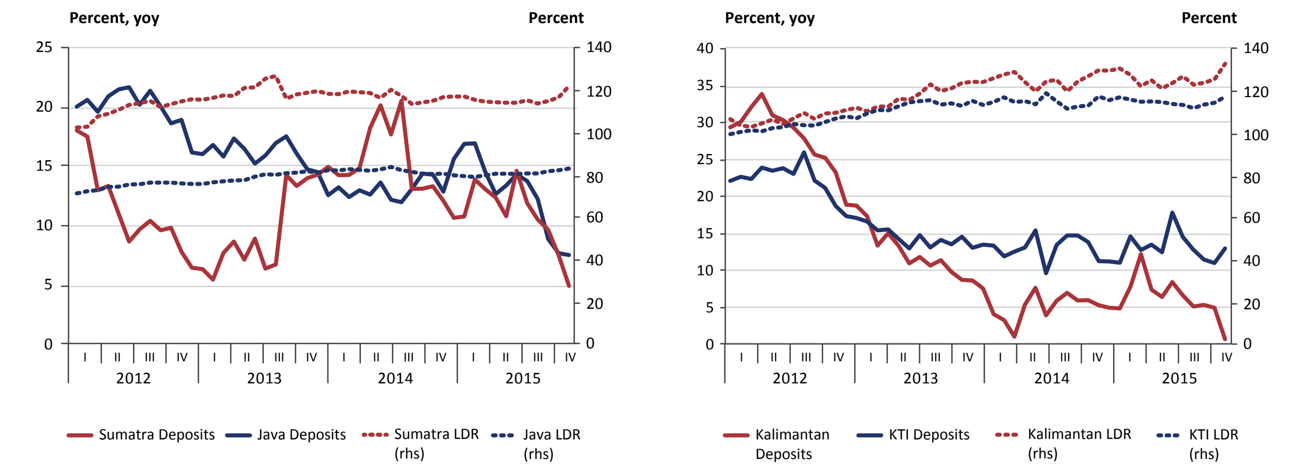
Credit financing from domestic sources through bank deposits (DPK) had also experienced a slowdown in all regions along with the decline in household savings. DPK growth slowed significantly in Java and Sumatra, which had the largest share (88.2%). DPK only grew by 6.9% in Java and 6.8% in Sumatra, much lower than its 2014 growth in the same regions by 12.9% and 12.1% respectively (Chart 10.19). With the growth of bank deposit lower than credit growth, the loan to deposit ratio (LDR) increased in all regions except in Kalimantan. Historically, Java had the lowest LDR, that is, around 83% in 2015. All regions

32 Credit extended to mining businesses in Kalimantan still grew by 17.39% (yoy) in 2014. The same could more or less be said of the credit chanelled to mining businesses in Sumatra whose growth contracted 5.37% or 24.3% lower than in 2014. However, the extension of credit to mining businesses in Sumatra was, in nominal terms, much lower.

33 The growth of credit chanelled to transportation and warehousing businesses as well as to information and communication businesses in Java had also slowed significantly as the impact of the weakening of the activity of manufacturing businesses and commercial property project developers.

34 The growth of credit extended to wholesale and retail trading businesses slowed in all regions except Sumatra.

Chart 10.19. Development of Deposits and LDR



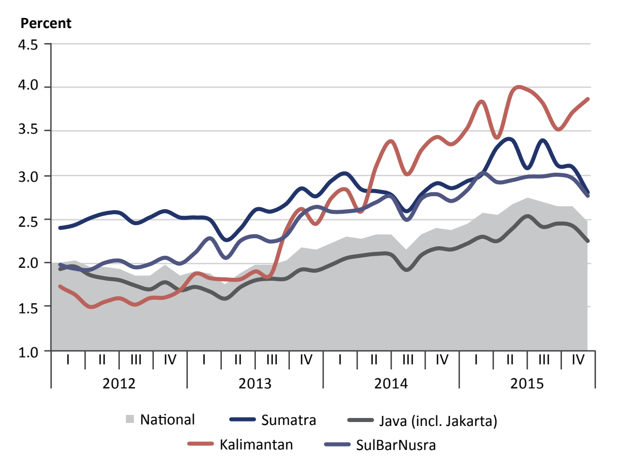
outside Java recorded LDR above 100%, which indicated dependence on sources of financing from Java, especially from Jakarta, the national financial center.

Credit risk was reflected in corporate non-performing loans (NPLs) that increased in all regions in line with the weakening of the ability to pay. In spite of this, however, corporate resilience remained intact. This condition was related not only to the pressure on corporate earnings in the mining and plantation sectors in regions outside Java but also experienced by a number of manufacturing businesses in Java. The highest increase in the rate of corporate NPLs occurred in Java, especially in Jakarta which recorded an increase of 0.4% compared to 2014 (Chart 10.20). Nevertheless, the rate of corporate NPLs in Java (2.4%) was much lower than that in regions outside Java. Corporate NPLs in Kalimantan and Sumatra also grew substantially, reaching 3.7% and 3.1% respectively. The increase in corporate NPLs in KTI was relatively more moderate, that is, 3%.

Based on their sectors, high NPLs rates in the mining industry were recorded in Kalimantan and Sumatra, at 3.7% and 3.1% respectively, and in the industrial sector and the agriculture sector in KTI at 6.6% and 5.5%, respectively. The NPLs rate in the industrial sector in Java was still within a safe limit (2.5%), despite a significant increase from 2014 (1.7%). NPLs rates that were relatively high throughout the regions had also occurred in the construction sector.[35]

Credit slowdown among micro, small, and medium-sized enterprises (MSMEs) had become a phenomenon across the regions. MSMEs credit slowdown was the deepest in Sumatra where such credit only grew 3.6% in 2015, much lower than 13.5% posted in 2014. Similarly, credit growth among MSMEs in Kalimantan was recorded at only 4.5%. The decline in commodity prices and smallholders' weak sales of oil palm and rubber both in Sumatra and Kalimantan had lowered demand for credit financing and compromised payability. On the other hand, credit

Chart 10.20. Development of Non-Performing Loans

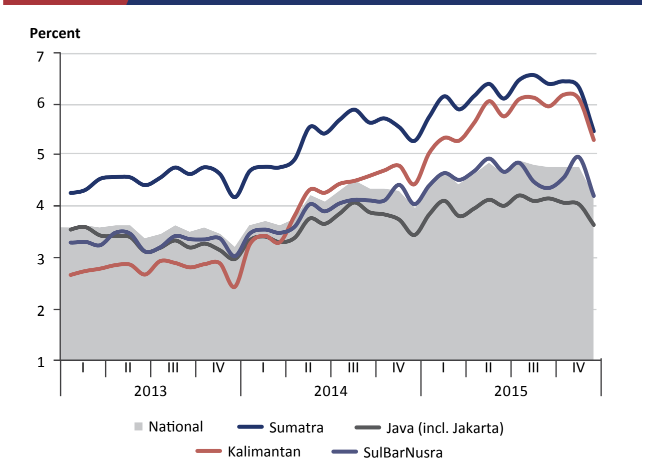


35 Non-performing loans (NPLs) in the construction sector in Kalimantan had reached 10.69%, and in Sumatra and KTI they accounted for 8.58% and 7.12% respectively. The high rate of NPLs in the construction sector was affected by delays in the development of commercial property projects, including industrial infrastructure and facilities, due to the weakening of domestic economic condition.

slowdown for MSMEs in KTI was the most moderate thanks to the region's improved economic conditions in 2015. Highest credit growth among MSMEs was recorded in KTI (9.4%) and Java (7.3%). MSMEs in KTI and Java were able to remain resilient (Chart 10.21) as their non-performing loans were lower than those of their counterparts in Sumatra and Kalimantan, which stood at 6.4% and 6.2% respectively.

Household credit slowed in all regions in 2015. Deepest slowdown in household credit occurred in KTI whose economic condition was better than other regions. Nevertheless, household credit growth in KTI was the highest, reaching 11.5%, followed by Java (10.2%), Kalimantan (9.6%), and Sumatra (9%). In aggregate, the highest increase in non-performing loans among households was recorded in Kalimantan and Java. Based on the type of household credit, the deepest slowdown occurred in multipurpose loans, especially in regions outside Java.[36] Motor vehicle credit slowdown, that was quite significant, also occured in regions outside Java, especially Kalimantan and KTI. Motor vehicle credit growth in Kalimantan had even contracted by 3.1% due to the decline in motor vehicle purchases by mining businesses and their support service providers. Meanwhile, the performance of lending for property purchases experienced the most moderate slowdown. With household credit constituting the largest component of property lending in nominal terms, credit slowdown in the real estate/ property sector (mortgage loans for a landed house (KPR), an apartment (KPA), a shophouse and an office house) mainly occurred in KTI and Java.

Chart 10.21. Development of SME NPLs



36 Multipurpose credit still reached a two-digit growth in a number of regions (Java, KTI, and Sumatra). This was different from motor vehicle loans that posted a one digit growth in all regions in 2015, down from the two-digit growth they posted in 2014 in all regions.

Households credit risk in 2015 remained at a safely guarded level in spite of being on the rise. The increase in NPLs among households in Java was the lowest and all kinds of household loans were still within the performing category. There were expectations that the agricultural sector's improved performance would be able to sustain household economic resilience. In KTI, agricultural sector performance was experiencing a slowdown but the rate of household NPLs was still quite low. Improved performance of its mining and industrial sectors was a factor that supported household economic resilience in the region.

Meanwhile, Kalimantan recorded the largest increase in household NPLs due to declining revenues and the weakening of economic performance. Based on the type of credit, the majority of household non-performing loans came from defaulted apartment loans (KPA), which accounted for 12.9%, most of which were taken out by debtors employed in the mining sector. The decline in the performance of the mining sector in Sumatra had also negatively impacted on the NPLs rate of KPA which, at 5.2%, had crossed the line.

10.5. PAYMENT SYSTEMS AND MONEY CIRCULATION

Rupiah Management Performance

In general, the net outflow of currency occurred in most provinces, whereas only a small number of provinces experienced a net inflow.[37] A very significant growth of net outflow occurred in Java, especially in Jakarta.[38] The changing pattern of net outflows in Java was affected by the government policy to significantly increase the transfer of funds to provinces and the holding of simultaneous regional elections financed mostly by funds obtained from Jakarta. After experiencing net inflows in 2014, Java posted a 137.1% growth of net outflows equivalent to Rp129.5 trillion in 2015. KTI experienced a 61.7% increased in the rate of net outflows as a result of the expansion of the region's economy and the holding of simultaneous regional elections, which were the largest in number.

37 Net inflow refers to the flow of currency coming into the banking system which is then credited back to Bank Indonesia.

38 The large net outflows in the Special Capital Province of Jakarta are also affected by the cash operation of banks, the majority of them are headquartered in Jakarta.

According to their pattern, net inflows were affected by the pattern of usage of, and the demand for, currency by the public, particularly during periods of national religious holidays. Net inflows were also associated with remittances sent by migrant workers to their hometowns. Sizeable net inflows in 2015 were recorded in West Java, Central Java, Yogyakarta, and East Java. Net inflows in these four provinces reached Rp72.9 trillion.

The year 2015 was also marked by the expansion of Bank Indonesia's cash distribution and cash services, which was reflected in the addition of the central bank's cash custodian units providing cash deposit services and the increasing flow of currency withdrawn from Bank Indonesia. Throughout the year 2015, six new cash custodian units that were established in cooperation with local commercial banks to provide cash deposit services were added in Tanjung Pandan, Serang, Batu Licin, Dumai, Tanjung Selor, and Pare-Pare. As a result of the addition, the number of the central bank's cash custodian units managed by 35 regional offices had now totalled 368 throughout Indonesia, much greater than the 267 of them that were operating in 2014. Such significant expansion in cash distribution had increased cash deposit-related net outflows, which increased from Rp14.7 trillion in 2014 to Rp22.9 trillion in 2015, up 55.7% (Chart 10.22). Such net outflows consisted of bank withdrawals amounting Rp47.4 trillion and bank deposits amounting to Rp24.5 trillion, the majority of which was not fit for circulation. Throughout the year 2015, the amount of money exchanged at mobile cashier units amounted to Rp1.8 trillion, up 25.7% compared to Rp1.5 trillion in the previous year. The increase in the exchange of money occurred mainly in KTI and Kalimantan, at 87.7% and 21.9% respectively (Chart 10.23).

Chart 10.22. Pattern of Withdrawal Through Mobile Cash

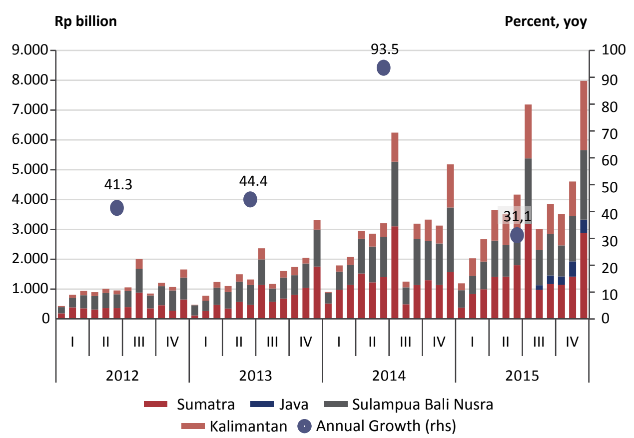
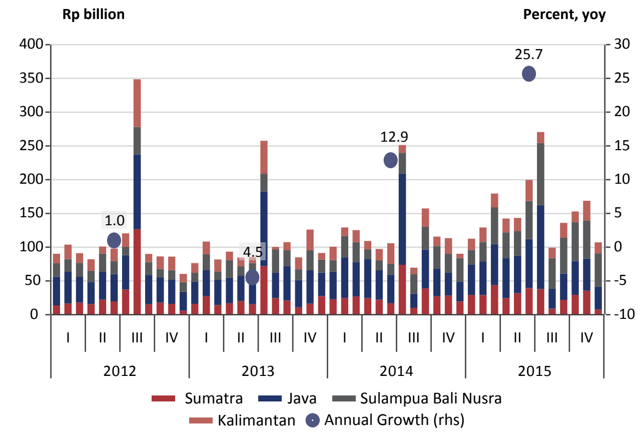


Chart 10.23. Pattern of Money Exchange Through Mobile Cash



Transfer of Money through Non-Bank Service Providers across Provinces

Transfers of money through non-bank money transfer service providers (TD BB) was on the rise both in terms of value and volume in almost all provinces across the country. Java accounted for more than 95% of non-bank money transfers in terms of both volume and value, followed by KTI and Sumatra. The portion of non-bank money transfers in Kalimantan was the smallest compared to that of other regions and went down compared to previous years. Geographically, money transfers through non-bank service providers are closely linked to the hometowns of Indonesian Migrant Workers (TKI) who mostly come from Java (West Java, Central Java and East Java), KTI, and Sumatra.

Types of money transfers through non-bank service providers differ from one region to another.[39] Money transfers that took place through non-bank service providers in Sumatra and Java were either domestic or incoming transfers. On the other hand, most transfers in Kalimantan and KTI are incoming transfers, which account for more than 95% of all the transfers. A relatively small portion of domestic transfers in Kalimantan and KTI was in line with the economic scale of both regions whose growth was still driven mainly by the role of the public sector and major private sector customers as transfers tend to be done through banks.

39 Domestic Transfers of Non-Bank Funds refer to transfers from one region to another within the country whereas the outgoing ones indicate transactions involving transfers from Indonesia to foreign countries and the incoming ones refer to transfers from foreign countries into Indonesia.

Business of Non-Bank Money Changers (KUPVA BB)

The number of Non-Bank Money Changers (KUPVA BB) was increasing in many different regions across Indonesia in 2015. Such increase corresponded to the growth in the number of foreign tourists coming to Indonesia thanks to the addition of visa-free facility to the country's visa policy. The largest increase was recorded in Java (14.1%), followed by Sumatra (4.6%) and KTI (2.8%) but a decline of 12% was recorded in Kalimantan. Approximately 78% of all foreign currency exchange transactions in 2015 took place in Java, and 15.2% in KTI. The lowest volume of foreign currency exchange transactions was recorded in Kalimantan at 0.7%. Java recorded the largest volume of foreign currency exchange transactions as the island's three major cities – Jakarta, Yogyakarta, and Surabaya – were frequented by foreign visitors for business or pleasure. As far as KTI is concerned, foreign currency exchange transactions mainly took place in Bali, which has become a major tourist destination for foreign travellers. The number of licensed non-bank money changers, too, had increased in 2015. The increase in the number of licensed non-bank money changers was recorded at 7.2% this year, or 994 in total. Non-bank money changers were mostly located in Jakarta (39%), Batam (14%), and Denpasar (13%).

The share of various foreign currencies exchanged through non-bank money changers in Sumatra, Kalimantan, Java and KTI varied. In Sumatra, more than 83% of foreign currencies traded were Singapore dollar and Malaysian ringgit due to the large number of Indonesian migrant workers who were sent to work in the two neighboring countries. In Kalimantan, foreign currency exchange transactions in Malaysian ringgit were so dominant they accounted for 65% of the total. In Java and KTI, the foreign currency exchange scene was dominated by U.S. dollar. Specifically in KTI, foreign currency exchange transactions with foreign tourists in Australian dollar, euro, and Japanese yen were also quite large in 2015.

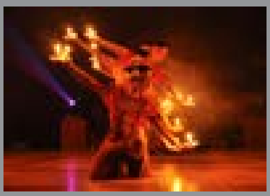
Box 10.1 Strengthening The Role of Economic Advisory

The transformation of regional economies had accelerated in recent years, prompting an increase in the role of institutions at regional levels. This was particularly so since the adoption of regional autonomy policy that gave more powers to regional governments in determining the direction of development in their territories, as well as greater responsibility over the implementation of development policies and programs in their jurisdictions. The complexity of regional economies was also increasing due to the growing economic linkages between one region to another and to the global economy as well. Today's regional economic challenges were also related to structural reform agenda that had been part of government commitment both at central and local levels. Inter-provincial structural reform disparities required strong cross-sector and cross-jurisdiction coordination and cooperation.

In line with the increasing role of regional institutions, Bank Indonesia had also played a role as a strategic partner in helping develop the vision of, and in supporting, regional economic development. Bank Indonesia's participation was directed not only to support the effectiveness of monetary policy so that optimal support could be given to economic activities in the real sector but also to maintain macroeconomic stability, especially in order to control inflation. Partnership between Bank Indonesia and the Government was carried out not only at the central level but also at regional levels through a number of coordination meetings, exchanges of data and information, and cooperation in capacity-building. Some concrete measures that were already implemented in 2015 included a collaboration between Bank Indonesia Regional Offices and the Office of the State Treasury in the preparation of assessment, in exploring the possibilities of concluding a Memorandum of Understanding with a number of ministries / institutions at the central level that would become the basis of partnership between Bank Indonesia and regional governments.

As regards the structural reform agenda aimed at supporting and safeguarding macroeconomic stability and accelerating regional economic growth, Bank Indonesia had also played an active role in it. This was part of measures to strengthen the advisory role of Bank Indonesia in regions. To support this, the central bank had rearranged the carrying out of the tasks of its regional offices in charge of monetary affairs, financial system stability, payment systems, MSMEs, and financial inclusion that were focused on supporting the effectiveness of monetary policy, maintaining macroeconomic stability and promoting sustainable and quality regional economic growth. In addition, Bank Indonesia at the end of 2014 had already set up a working unit that served as a coordinator for each region under its coordination in order to increase and improve the effectiveness of the advisory role of its regional offices in the regions. As one of the realization of the active role that Bank Indonesia played, coordination with the central government and regional governments to support the structural reform agenda had already been carried out through coordination meetings held in regions such as the ones in Ambon, Balikpapan, and Yogyakarta in 2015.[1]

1 To find out more, please refer to Chapter 14.



Similar to the Indonesian Candle Dance that must ensure balance for the best performance, the economic policy mix was directed towards striking an optimal balance for the domestic economy. Furthermore, Bank Indonesia constantly strengthened coordination with the Government and other relevant authorities.

PART III

POLICY RESPONSE

MAINTAINING STABILITY AND STIMULATING GROWTH WITH POLICY MIX

JAN	NONBANK EXT.DEBT MANAGEMENT
FEB	LOWERING POLICY RATE
MAR	IMPROVING FRAMEWORK FOR JIBOR DETERMINATION
APR	
MAY	
JUNE	INCREASING LTV RATIO FOR PROPERTY LOAN AND DECREASING DP FOR MOTOR VEHICLES CREDIT
JULY	LFR & MSMEs CREDIT INCENTIVE
AUG	
SEPT	RUPIAH STABILIZATION PACKAGE (1)
SEPT	RUPIAH STABILIZATION PACKAGE (2)
OCT	
NOV	MONETARY POLICY EASING BY LOWERING RR
DEC	GREATER ROOM FOR MONETARY EASING

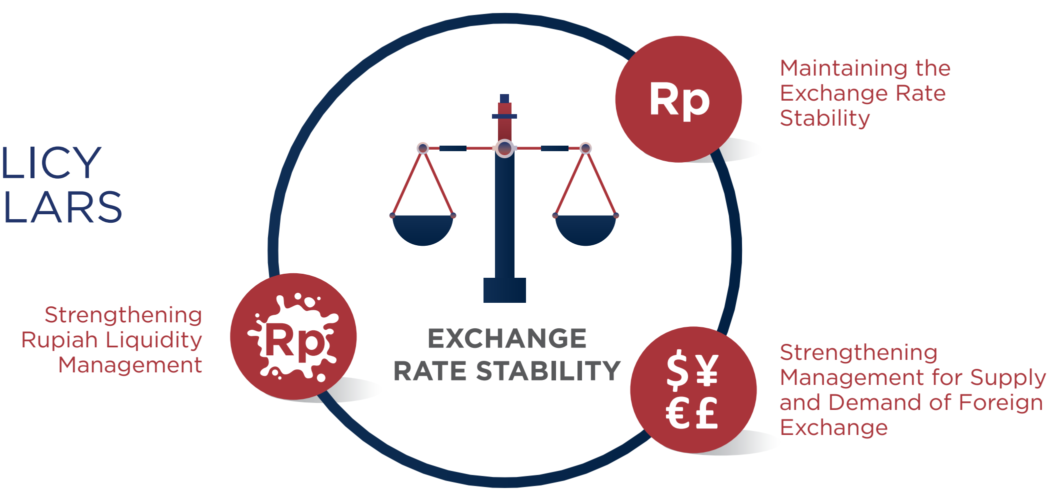
PHASE 1

Maintaining Stability With TIGHT BIAS MONETARY POLICY and Promoting Economic Growth With ACCOMMODATIVE MACROPRUDENTIAL POLICY

PHASE 2

UTILISING EASING MONETARY POLICY ROOM and ACCELERATING The Implementation Of STRUCTURAL REFORMS

3 POLICY PILLARS



PART III

POLICY RESPONSE

During 2015, the economy faced three macroeconomic policy challenges that demanded be properly managed. The first policy challenge concerned the efforts to safeguard macroeconomic and financial system stability amid heightened uncertainties on global financial markets. These uncertainties arose primarily from the uncertainty over monetary policy normalization in the United States, concerns over the fiscal negotiations with Greece, and the unexpected devaluation of the yuan. The uncertainty on global markets triggered risk-off behavior by investors that led to contraction in foreign capital inflows on the domestic financial market. This was accompanied by stronger downward pressure on the rupiah that had to be managed carefully to avoid negative impact on the macroeconomic stability.

The second challenge concerned efforts to bolster growth in a domestic economy in slowdown from the fallout of weakening global economic growth. The global economic slowdown accompanied by continuing decline in commodity prices led to significant pressure on performance of export and resource-based sectors of the economy. This pressure even spread to non-resource sectors. The potential for prolonged slowdown in domestic economic growth had to be mitigated in order to nurture positive sentiment for the domestic economic outlook. In view of the prolonged global economic slowdown, efforts to bolster economic growth by stimulating domestic demand would be key to the economic recovery process in the short-term. The third policy challenge concerned the need to accelerate implementation of structural reforms. The various structural problems in the domestic economy had escalated the negative impact of external shocks on both macroeconomic stability and domestic economic growth. It therefore became vital to step up the implementation of structural reforms in order to reinforce the foundations of the Indonesian economy as a basis for creating sustainable economic growth.

To address these challenges, Bank Indonesia and the Government continued to strengthen synergy in macroeconomic policy management. The policy mix pursued by Bank Indonesia focused on measures to safeguard macroeconomic and financial system stability. This policy mix was also reinforced by close coordination between Bank Indonesia, the central and regional governments, and other authorities. To generate momentum for stronger economic growth, Bank Indonesia pursued measures that involve the use of accommodative macroprudential policies. This policy was implemented in synergy with an increased fiscal stimulus by the Government to accelerate the process for recovery of economic growth. In addition, the Government and Bank Indonesia worked tirelessly to strengthen coordination in accelerating the pace of structural reforms. In this regard, the Government launched the Economic Policy Packages I-VIII, a series of policies aimed at speeding up improvements to infrastructure and enhancing greater domestic economic competitiveness. The Government's efforts to accelerate structural reforms were also supported by Bank Indonesia policies for building greater resilience and efficiency in the domestic economy.

From Bank Indonesia side, the measures for safeguarding macroeconomic stability focused on bringing inflation back to the inflation target, curbing the current account deficit to a more prudent level, and managing the stability of the rupiah exchange rate. Against this background, Bank Indonesia worked throughout 2015 to strengthen the monetary policy mix through policy actions involving interest rates, the exchange rate, monetary operations, capital flows management, and strengthening the buffer of international reserves. In the meantime, Bank Indonesia also undertook a selective relaxation of macroprudential policies and lowered the statutory reserve requirement aimed at generating momentum for economic growth. These policies sought to expand capacity of bank financing by providing additional liquidity to boost lending. The relaxation on macroprudential and monetary policies involved measured actions that took into account their impacts on the financial system stability. As an effort to support structural reform, Bank Indonesia took further actions for deepening of the financial market, improvement of financial inclusion, and strengthening of the payment system. In financial marketing deepening, the objective was to create a resilient and efficient financial market. Alongside this, the financial inclusion policy sought to improve access to economic financing, while payment system policy focused on strengthening the payment system infrastructure in order to bring about a secure, reliable, and efficient payment system with the requisite capacity to support economic efficiency.

The thrust of interest rate policy, like before, was on achievement of the inflation target, reduction of the current account deficit, and safeguarding exchange rate stability. Regarding inflation, the tight bias interest rate policy focused on managing inflation expectations and domestic demand in order to bring down inflation quickly to within the targeted range of 4±1%. With inflation expectations still running high in early 2015, Bank Indonesia (BI) kept the BI Rate on hold at 7.75% in January 2015. In February 2015, Bank Indonesia brought the BI Rate back to the level before the increase of BI Rate in November 2014. This normalization was achieved by lowering the BI Rate by 25 bps after assessing that projected inflation at the end of 2015 would be back on the target. Bank Indonesia kept the BI Rate steady at 7.50% until the end of 2015. Bank Indonesia on one hand confident that the interest rate at the prescribed level remained commensurate with efforts to curb domestic demand and imports in order to bring down the current account deficit to a more prudent level. The reduction in the current account deficit in turn lowered domestic demand for foreign currencies. On the other hand, Bank Indonesia also regarded the prescribed interest rate as sufficiently competitive to attract a greater supply of foreign currency, mainly through foreign capital inflows. This combination was expected to relieve excessive downward pressure on the rupiah fuelled by mounting uncertainties on global financial markets. The interest rate policy proved effective in safeguarding macroeconomic stability as reflected in inflation held to within the 2015 inflation targeting range of 4±1%, a reduction in the current account deficit to about 2% of GDP, and the strengthening of the rupiah during the fourth quarter of 2015.

This achievement in inflation also owes much to intensified coordination among agencies under the Inflation Monitoring and Controlling Team (TPI) and Regional Inflation Monitoring and Controlling Teams (TPIDs) that curbed inflation within the 2015 target range of 4±1%. Inflation in 2015 was recorded at 3.35%, down sharply from the inflation of 2014 that reached 8.36%. The more robust coordination ensured the smooth operation of distribution and supply amid the impact of the El Nino, thus safeguarding price stability in volatile foods. This success was also reflected in the subdued inflation over the 2015 Eid-ul-Fitr festive season, which came below the average inflation for the period over the previous four years. The mild volatile foods supported by stability in administered prices prompted a decline in inflation expectations with the result that in 2015, core inflation fell to 3.95% compared to 4.93% in 2014.

The tight bias monetary policy also sought to mitigate the impact of divergence in global monetary policies that has triggered a shift and increased volatility of capital flows into emerging market economies, including Indonesia. The interest rate policy was sufficient to lift some of the pressure for depreciation of the exchange rate, although external influences remained dominant. Global pressures mounted in the third quarter of 2015 with growing sentiment over the increase in the FFR and a surprise devaluation of the yuan. These developments put limits on room for manoeuvre in monetary policy and therefore necessitated support from exchange rate policy and management of international reserves. For this purpose, Bank Indonesia worked in synergy with the Government to launch the Economic Policy Package I on 9 September 2015 and the Economic Policy Package II on 30 September 2015. In these policy packages, Bank Indonesia launched a series of policies for safeguarding the rupiah exchange rate built on the three pillars of: (i) maintaining a stable exchange rate for the rupiah (ii) bolstering management of rupiah liquidity, and (iii) reinforcing the management of foreign exchange supply and demand.

Bank Indonesia stayed constantly active on the market to maintain the stability of the rupiah. Bank Indonesia intervened on the spot and forward markets to create equilibrium between demand and supply of foreign currency, thus curbing volatility in the rupiah exchange rate. In September 2015, Bank Indonesia acted to bolster supply and demand for foreign exchange by changing the frequency of FX Swap auctions from twice to once a week, reducing the limit on foreign currency purchases supported by underlying documents, and issuing foreign currency Bank Indonesia Securities (SBBIs). Meanwhile, to strengthen the management of rupiah liquidity, Bank Indonesia made adjustments to the auction mechanism for open market operations (OMOs) by switching from variable rate tenders (VRTs) to fixed rate tenders (FRTs). The range of OMO instruments was diversified further with variations in tenor that include: i) 3 and 6-month Bank Indonesia Certificates of Deposit (SDBIs), ii) 9 and 12-month Bank Indonesia Certificates (SBIs), and iii) Government Securities reverse repo with a 2-week tenor. The added range of monetary operations (MO) instruments, besides strengthening liquidity management, also sought to create a term structure for MO interest rates consistent with the monetary policy stance in order to strengthen policy signals on the money market.

In 2015, Bank Indonesia also announced policies aimed at providing more fundamental support for rupiah exchange rate stability. On 1 January 2015, Bank Indonesia began implementing rules on the application of prudence principle in non-bank corporate external debt management. In a concurrent measure to reduce domestic transactions that make use of foreign currencies and thus also increase foreign exchange demand, Bank Indonesia launched a policy for mandatory use of the rupiah currency within the territory of the Republic of Indonesia. This policy reduced the volume of foreign exchange transactions among residents that had previously been conducted in foreign currencies. Other coordination with the Government involved measures to encourage longer retention of export proceeds within Indonesia. The Government provided an incentive by reducing the tax on time deposit interest paid by exporters who willing to hold their export proceeds in domestic banks. This measure is expected to attract export proceeds previously parked abroad, and in doing so strengthen international reserves.

Strengthening the buffer of international reserves also formed part of the Bank Indonesia strategy for readiness to cope with sudden shocks arising from external sentiment. While ensuring adequate international reserves as a first line of defense, Bank Indonesia also strengthened the international financial safety net as a second line of defense. The second line of defense facilities consist of regional cooperation on financial arrangements and bilateral cooperation with partner nations, including the following: the ASEAN Swap Arrangement (ASA), the Chiang Mai Initiative Multilateralization (CMIM), and the Bilateral Swap Arrangement (BSA) between Bank Indonesia and the Bank of Japan (BoJ). Bank Indonesia also collaborates under Bilateral Currency Swap Arrangements (BSCAs) with the Bank of Korea (BOK), the People's Bank of China (PBoC), and the Reserve Bank of Australia (RBA) to promote bilateral trade using the local currencies of both nations party to such agreements. The BI-PBoC BCSA may also be used to meet short-term liquidity needs. The series of policies put in place to stabilize the exchange rate and buttress lines of defense succeeded in calming the jitters of market actors and foreign investors, enabling rupiah depreciation to be managed more effectively compared to peer nations.

To help gaining momentum for economic growth, Bank Indonesia pursued accommodative macroprudential policies during 2015. In June 2015, Bank Indonesia relaxed macroprudential policy by raising the Loan to Value (LTV) ratio or Financing to Value (FTV) ratio for property loans and lowering down payments for motor vehicle credit. To expand the funding basis for banking intermediation, Bank Indonesia took measures to encourage the issuance of securities now factored into the Loan to Funding Ratio (LFR) that has replaced the Loan to Deposit Ratio (LDR). The introduction of the LFR will provide the banking system with greater room for intermediation, which will not rely solely on bank deposit (DPK). In a subsequent action to promote lending to MSMEs, Bank Indonesia introduced an incentive of an increased limit for the LFR target for banks able to meet a target for lending to MSMEs while maintaining a prudent NPLs ratio. This relaxation of macroprudential policy was envisaged to spur a recovery in credit growth, which had fallen to a low of 9.7% (yoy) in July 2015. To support these efforts for recovery in credit growth, Bank Indonesia also lowered the primary reserve requirement in rupiah from 8% to 7.5% with effect from 1 December 2015. For the full year, credit growth ultimately reached 10.4% (yoy) while economic growth came to 4.79%.

To support more sustainable economic growth, Bank Indonesia also worked actively to coordinate with the Government in implementing structural reforms. Structural reform policies focused on measures to improve infrastructure, strengthen competitiveness, and achieve food, energy, and water security, as well as on sustainable development financing. To put these policies into place, the Government announced the series of phase I-VIII economic policy packages. Not only did Bank Indonesia extend support for the design of these economic policy packages, but it also held a number of National Coordinating Forums to develop a common vision elaborated in a concrete strategy for development of priority sectors. In the National Coordination Forums, the priority sectors on which discussions focused were development of a maritime-based economy in Ambon, energy security in Balikpapan, and development of the industry and tourism sectors in Yogyakarta.

To support structural reforms, Bank Indonesia was also active in promoting financial market deepening and financial inclusion. Financial market deepening was carried out by expanding the scope of market actors, adding to the variety of financial market instruments and promoting efficient price formation. At the same time, to improve public access to financial services, financial market deepening also involved the payment system with measures such as Digital Financial Services, as well as development of the MSMEs sector. MSMEs development will not only provide greater access to financing from financial institutions, but also promote equitable distribution of economic activity and benefits. MSME development was also brought into alignment with the Nine Priority Programs (Nawa Cita) launched by the Government to bolster leading sectors. Consistent with development of leading sectors, Bank Indonesia also played a role as a counterpart in the People's Business Credit (KUR) Policy Committee to support the channelling of Government-subsidised credit.

To support the growing scale of economic activity, Bank Indonesia also took action to reinforce the infrastructure of the payment system. In 2015, Bank Indonesia launched the Second Generation BI-RTGS, the Second Generation BI-SSSS, and the Second Generation SKNBI. This is intended to improve security, reliability, and speed in settlement of transactions for greater efficiency and to provide optimum support for the economy. Bank Indonesia also kept working to promote the use of non-cash payment instruments in transactions in order to improve security and efficiency. Under a later initiative for promoting financial literacy and inclusion, Bank Indonesia also expanded the reach of the Digital Financial Services (DFS) programme, which represents part of the National Non-Cash Movement (GNNT). Alongside these measures, Bank Indonesia supported cash payments by continually ensuring the availability of sufficient volume of rupiah currency in a range of denominations. The quality of rupiah currency in circulation has been improved under the clean money policy, even in the remote areas of the nation. The drive to circulation and provision of rupiah currency in border regions was intensified under reforms for currency distribution and cash services for implementation of mandatory use of the rupiah within the territory of the Republic of Indonesia.

Consistent implementation of these various policies mix proved capable of safeguarding the performance of the Indonesian economy amid a range of external sector shocks. The positive performance in the economy was reflected in steady improvement in macroeconomic and financial system stability and the onset of recovery in domestic economic growth. Improved macroeconomic stability was indicated by achievement of the 2015 inflation target of 4±1%, a reduction in the current account deficit to about 2% of GDP, and control retained over stability in the rupiah, which even gained value during the fourth quarter of 2015. Regarding the financial system, banking system resilience stayed robust, bolstered by high levels of capital adequacy and supported by a range of macroprudential policies. Economic growth also began gaining momentum for recovery during the second half of 2015.

Looking forward, the positive effect of the various policies implemented thus far will provide support for economic recovery in 2016. There is confidence that the economic policy packages I to VIII launched by the Government will provide stronger assurance for business in embarking on greater investment and expansion of their business activities. Meanwhile, support from Bank Indonesia policies in making prudent use of the room for monetary policy easing and accommodative macroprudential policies will provide added thrust for the momentum of economic recovery. Strengthened by the results of structural reforms, the momentum for economic recovery is expected to create a robust basis for the Indonesian economy to achieve sustainable growth in 2016 and build greater capacity for withstanding external shocks.

Monetary policy in 2015 was consistently directed towards maintaining macroeconomic stability amidst a range of serious challenges. In addition, monetary policy was supported by increasingly transparent and effective communication in order to emphasise Bank Indonesia's avowed commitment.

Chapter 11

Monetary Policy

Monetary policy in 2015 was directed towards mitigating the undesirable effects of ubiquitous global economic uncertainty on macroeconomic stability. To that end, Bank Indonesia adopted a tight-bias monetary policy stance, underpinned by rupiah stabilization policy. Congruous with maintained macroeconomic stability, Bank Indonesia prudently eased its monetary policy stance in order to stimulate the domestic economy. The disciplined and prudent monetary policy stance adopted by Bank Indonesia preserved macroeconomic stability while providing sufficient space for economic recovery, reflecting inflation that returned to its target corridor, a narrower current account deficit, rupiah stability and increased domestic economic momentum.

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Monetary policy, which was geared towards maintaining macroeconomic stability, faced a number of onerous challenges in 2015. Growing uncertainty blighted global financial markets due to the proposed Federal Funds Rate (FFR) hike by the Federal Reserve, while monetary policy in other advanced countries tended to remain accommodative, which compounded depreciatory pressures on the rupiah. Consequently, the rupiah depreciated against the U.S. dollar from the beginning of 2015 until September of the same year. Strong and persistent pressures on the rupiah subsequently exacerbated inflationary pressures and triggered financial system instability. In addition, sustained exchange rate depreciation pressures undermined sentiment in terms of the domestic economic outlook, which was moderating as a result of unconducive global economic conditions. Under such circumstances, measures to maintain macroeconomic stability in order to successfully improve the perception of sustainable economic growth became imperative because any decline in the outlook could have derailed rupiah stability.

Monetary policy in 2015 was focused on mitigating short-term currency risk and controlling macroeconomic stability. Furthermore, monetary policy aimed to alleviate excessive pressures on the rupiah, while maintaining rupiah stability in accordance with its fundamental value. , This consistent strategy returned inflation to within the target corridor set for 2015-2017, namely 4±1%, and narrowed the current account deficit to a healthier level. As has been reported previously, Consumer Price Index (CPI) recorded comparatively high inflation in 2014 at 8.36% (yoy) due to a series of fuel price hikes. Meanwhile, the current account deficit was considered relatively wide in 2014 at 3.1% of GDP due to dwindling global demand and sliding international commodity prices. Consequently, Bank Indonesia instituted measures to control macroeconomic stability as a prerequisite for strengthening the structure of the domestic economy to be more solid and resilient. Macroeconomic stabilization was achieved through policies on interest rates, the reserve requirement, open market operations, exchange rates, and capital flows, while supporting financial market deepening.

The tight-bias monetary policy stance was maintained until October 2015 and was shored up by a rupiah stabilization policy package. The BI Rate was held at 7.50% from February until yearend 2015. The tight-bias stance was also supported by a rupiah stabilization policy package in September 2015, containing three salient pillars, namely stabilising the rupiah consistent with the currency's fundamental value, strengthening rupiah liquidity management, including the term structure of open market operations, as well as strengthening foreign exchange supply and demand management. Accelerating financial market deepening further supported the rupiah stabilization policy package.

Mitigating the impact of moderating economic growth on economic stability, the primary reserve requirement in rupiah was lowered. Accordingly, the reserve requirement was reduced by 0.5% to 7.50% on 1st December 2015. The domestic slowdown and rupiah depreciation triggered economic instability, reflecting a build-up of corporate risk that ultimately eroded investment. Furthermore, weaker corporate performance prompted an accumulation of risk in the banking sector. In addition, economic moderation narrowed fiscal space to stimulate growth. Addressing the potential economic slump, Bank Indonesia sought the appropriate policy response to maintain the favourable perception held by economic players. Consequently, Bank Indonesia lowered the primary reserve requirement in rupiah because looser monetary policy through a BI Rate reduction was considered too risky against the inauspicious backdrop of widespread global uncertainty, which could have led to a potential foreign capital reversal and heightened depreciatory pressures on the rupiah.

Close coordination with the Government and other related authorities supported the monetary policy stance adopted, while maintaining economic stability and propping up the economic recovery. Inflation in 2015 was controlled within the target corridor of 4±1% at 3.35% (yoy). Moreover, the current account deficit also narrowed to a healthier 2.1% of GDP, which bolstered external sector resilience. Meanwhile, rupiah depreciation was successfully mitigated and the currency even rebounded during the final quarter of the reporting year. Macroeconomic stability was further supported by sufficient liquidity in the economy in line with demand, indicated by slower broad money (M2) growth as the domestic economy moderated. Lending rates and deposit rates were also lowered, consistent with weaker demand due to the economic downshift.

11.1. INTEREST RATE POLICY AND THE RESERVE REQUIREMENT

Bank Indonesia's interest rate policy in 2015 was consistently directed towards hitting the inflation target for 2015-2017 of 4±1% as well as narrowing the current account deficit to a healthier level. Measures to control inflation to within the target corridor were pivotal in 2015 considering that inflation had skyrocketed to 8.36% in 2014, far exceeding the target of 4.5±1%.[1] In addition, efforts to narrow the current account deficit to a sounder level were also the focus of policy in 2015 due to the large 3.1% of GDP deficit recorded in 2014.

Low inflation at the beginning of 2015 was conducive to lowering the BI Rate in February. Several indicators at the beginning of the year evidenced dissipating inflationary pressures after the fuel price hike that took place in November 2014. Furthermore, the inflation expectations of consumers and retailers were noted to follow a downward trend during the first quarter of 2015. The Consensus Forecast also confirmed lower inflation expectations amongst economic players, returning to the target corridor of 4±1% by the end of 2015. Against such a favourable backdrop, Bank Indonesia decided to lower its policy rate 25 bps in February 2015 to 7.50%, accompanied by a 25 bps reduction to the Deposit Facility rate, while the Lending Facility rate was held at 8.00%.

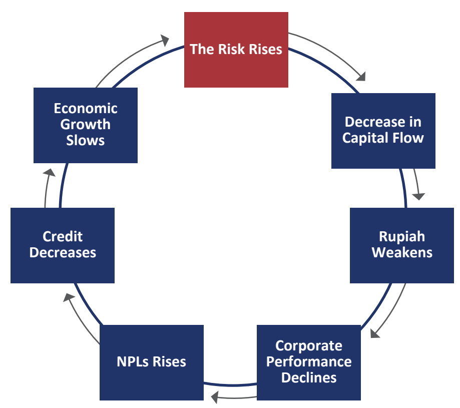
Growing global uncertainty affected global capital flows and heightened domestic macroeconomic instability again in the third quarter of 2015 due to the planned FFR hike. Global uncertainty peaked in August 2015 after the People's Bank of China (PBoC) unexpectedly devalued the yuan in order to stimulate the flagging economy. Escalating global risk ultimately forced investors to seek perceived safe haven assets and reduce placements in emerging market countries. Such conditions placed intense pressures on emerging market currencies, including the rupiah. Consequently, the rupiah followed a depreciating trend in 2015, peaking in the third quarter.

Measures to mitigate rupiah depreciation were intensified in order to maintain macroeconomic stability and sustainable economic growth. Excessive rupiah depreciation could have amplified inflationary pressures, undermined corporate performance and disrupted financial system stability, while damaging sentiment in terms of the deteriorating domestic economic outlook. Therefore, it became imperative for the related authorities to introduce measures to maintain positive investor perception in economic sustainability despite the intense depreciatory exchange rate pressures being felt. Concerns on economic prospects will further increase the risks to the economy and thus placed even more pressure on the rupiah (Diagram 11.1).

Bank Indonesia responded to the unfavourable conditions by directing interest rate policy to mitigate the risk on rupiah depreciation and control macroeconomic stability in general. Monetary policy was refocused on alleviating excessive exchange rate pressures, thereby maintaining rupiah stability in accordance with its fundamental value. The move was also consistent with efforts to lower inflation to within the target corridor of 4±1% in 2015-2017 as well as manage the current account deficit to a healthier level. To that end, Bank Indonesia held the BI Rate at a level of 7.50% until December 2015, while maintaining the Deposit Facility and Lending Facility rates at 5.50% and 8.00% respectively. Bank Indonesia policy to hold the BI Rate and Standing Facilities Rate was taken paying due consideration to the persistently high level of short-term global risk.

Mitigating the effect of economic moderation on macroeconomic stability, Bank Indonesia also lowered the primary reserve requirement in rupiah. In November 2015, Bank Indonesia decided to reduce the primary reserve requirement in rupiah from 8.0% to 7.50%, effective from 1st December 2015. The reserve requirement was lowered in line with stronger macroeconomic stability, which provided space to loosen monetary policy. Nonetheless, due to

Diagram 11.1. Economic Challenges in Weakening Rupiah Period



1 High inflation was primarily attributable to the fuel price hike in November 2014.

lingering uncertainty on global financial markets, primarily the result of the proposed FFR hike and monetary policy divergence in Europe, Japan and China, Bank Indonesia prudently eased monetary policy. The reserve requirement was lowered because easing monetary policy through reductions to the BI Rate was considered too risky against the inauspicious backdrop of widespread global uncertainty, which could have led to a potential foreign capital reversal and heightened depreciatory pressures on the rupiah. In that context, looser monetary policy through a lower primary reserve requirement was expected to enhance bank financing capacity in order to support economic activities that had shown signs of picking up since the third quarter.

11.2. EXCHANGE RATE POLICY

To maintain macroeconomic stability, monetary policy is supported by exchange rate policy, which aims to maintain exchange rate stability in line with its fundamental value. In that context, Bank Indonesia consistently maintains the exchange rate in line with the forward-looking inflation target and in accordance with the supply and demand of foreign exchange on the market based on economic and financial market fundamentals. Exchange rate stability in critical to control inflation on a downward trend, especially when depreciatory pressures heighten. Through anchored inflation expectations, the pass-through effect of exchange rate depreciation can be controlled. In addition, exchange rate stability also restores confidence in the economic outlook of Indonesia.[2]

Bank Indonesia constantly stabilize the rupiah in line with its fundamental value in order to maintain macroeconomic and financial system stability. Measured foreign exchange market intervention is necessary to dampen shocks that appear from supply and demand imbalances. Bank Indonesia follows a dual intervention strategy, namely rupiah stabilization through selling actions on the foreign exchange market accompanied by purchases of tradable government securities (SBN) on the secondary market. Dual intervention strategy not only supports rupiah exchange rate stability but also safeguards adequate rupiah liquidity. The policy also reinforces Bank Indonesia's SBN holdings as a monetary policy instrument. Exchange rate policy is further supported by a maintained position of international reserve assets as a first line of defense in response to growing global uncertainty.

Bank Indonesia intensified exchange rate stabilization policy during 2015 in response to escalating depreciatory pressures, particularly in the third quarter. Accordingly, Bank Indonesia released a set of measures to help stabilize the rupiah (Table 11.1). The policy package

Table 11.1. Policy Package 9th September and 30th September

Policy	Strategy
Maintaining Rupiah Exchange Rate Stability	• Control of the volatility of the exchange rate • The purchase of government securities in the secondary market • Forward intervention to balance supply and demand in the forward market
Strengthening Rupiah Liquidity Management	• Adjustment on OMO auction mechanism of form variable rate tender (VRT) into fixed rate tender (FRT) • Adjustment on OMO auction pricing • Issuance of SDBI tenor of 3 months and 6 months • Issuance of SBI tenor 9 months and 12 months • Issuance of government securities based on RR tenor 2 weeks
Strengthening Foreign Exchange Supply and Demand Management	• Lowering the limit of foreign exchange purchases by proving the underlying documents • Strengthening policies to manage demand and supply of foreign currency in the forward market • Adjustment of FX swap auction frequency from 2 times per week to 1 time per week • Adjustment FX TD auction mechanism from a variable rate tender (VRT) into fixed rate tender (FRT), adjusting pricing and tenor extension up to 3 months • Issuance of Securities Bank Indonesia (SBBI) foreign exchange • Reduction of the minimum holding period for SBI to 1 week • Strengthening information Foreign Exchange Flows (LLD) • Coordination with the Government on granting tax incentives to exporters deposits that stores Export Proceeds (DHE) in Indonesian banks or converting into rupiah

2 A full discussion on the rupiah exchange rate is presented in Chapter 5, Exchange Rate.

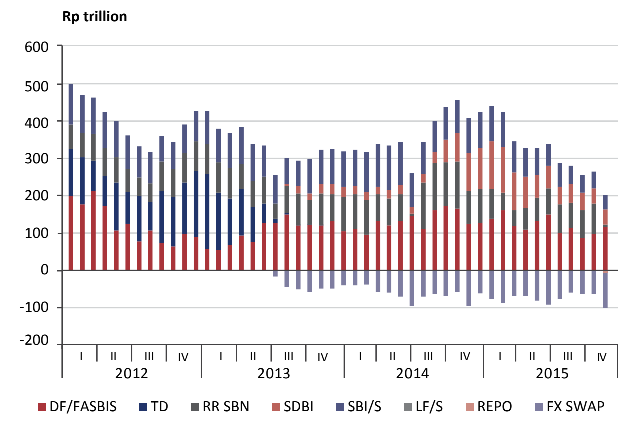
was also synergic with the policies introduced by the Government to maintain domestic economic momentum. The aforementioned panoply of policy measures was implemented immediately, which effectively supported macroeconomic stability as well as sustainable and inclusive economic growth.

Strengthening Rupiah Liquidity Management and Developing Open Market Operation (OMO) Instruments

Rupiah liquidity was controlled through BI monetary policy in order to support the desired policy direction. Monetary operations are used to manage liquidity and balance demand and supply, while transmitting monetary policy to financial market rates. Liquidity management is achieved through monetary operations in the form of open market operations (OMO) and standing facilities. During the first half of 2015, Bank Indonesia undertook a number of measures to strenghthen monetary operations, including simplifying OMO auctions by terminating 9-month Bank Indonesia Certificates (SBI) and instead holding the inaugural auction of 9-month Bank Indonesia Certificates of Deposit (SDBI). The use of SBN held by Bank Indonesia was also optimised through reverse repo SBN and by reducing the frequency of SDBI auctions from six times to twice monthly.

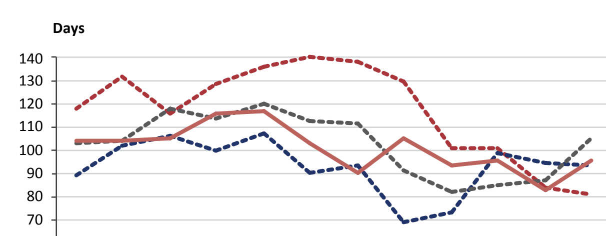
Congruent with the direction of monetary operations, Bank Indonesia constantly strengthened liquidity management to support efforts to stabilize the rupiah. To that end, Bank Indonesia adjusted the pricing of OMO auctions, changed the mechanism from a variable rate tender (VRT) to a fixed rate tender (FRT), released SDBI of three and six months as well as issued 2-week reverse repo SBN and reissued tenors of 9 and 12 months. The pricing and mechanism of OMO auctions were adjusted to strengthen rupiah liquidity management and, therefore, support rupiah stabilization. Pricing was adjusted by raising OMO interest rates to mitigate excess rupiah liquidity in foreign exchange transactions that could heighten pressures on rupiah exchange rates. Meanwhile, the OMO auction mechanism was changed from VRT to FRT in order to strengthen policy signals from Bank Indonesia in terms of rupiah liquidity management. The change to the auction mechanism is only temporary and will be reviewed in due course. In addition to managing liquidity, the measures were also taken to maintain consistency and strengthen monetary policy signals. In that context, Bank Indonesia designed the term structure of monetary operation instruments in pursuance of the monetary policy direction adopted.

Chart 11.1. Monetary Operation Instruments Outstanding



During the first half of 2015, the position of monetary operations tended to increase on the year earlier but subsequently declined thereafter in the second semester compared to the same period of the previous year. The average position of monetary operations (MO) in the first half of 2015 increased 11% on the first semester of 2014 (Chart 11.1). Monetary operations were strengthened during that time by simplifying the OMO auctions through the termination of 9-month SBI and release of 9-month SDBI. Bank Indonesia also optimised the use of the SBN held through reverse repo SBN, while reducing the frequency of SDBI auctions from six times to twice per month. Nonetheless, the average MO position in the second semester was down around 35% on the same period of the previous year. Tighter rupiah and foreign currency liquidity management from August 2015 supported exchange rate stabilization policy. After August

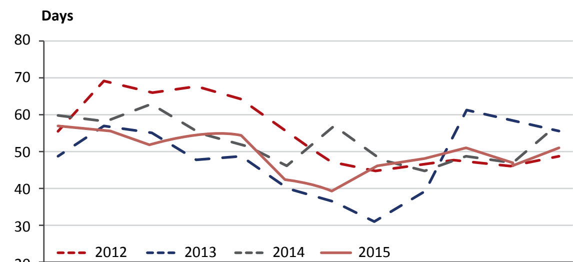
Chart 11.2. The Duration of OM by Tenor



	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec
2012	117	131	116	128	135	139	137	128	101	101	84	82
2013	89	101	106	100	107	91	94	70	74	99	94	94
2014	103	104	118	114	119	112	111	91	83	86	88	105
2015	104	104	105	115	116	103	90	105	94	96	83	96

2012 2013 2014 2015

Chart 11.3. The Duration of OM Instruments by Remaining Maturity



	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec
2012	55	70	67	68	65	54	45	43	45	46	46	47
2013	48	57	54	46	48	37	33	27	35	61	59	55
2014	59	58	63	54	50	43	56	46	42	46	45	56
2015	56	56	51	54	53	40	37	44	45	50	45	50

2015, the duration of monetary operations was increased but not to the level achieved at the beginning of the year. The duration of monetary operations was extended because of a decline in daily surplus liquidity in the banking system along with seasonal factors, which made the banks more conservative in terms of maintaining their short-term liquidity (Chart 11.2 and Chart 11.3).

Strengthening Foreign Currency Supply and Demand Management

One pillar of the exchange rate stabilization package issued by Bank Indonesia contained a set of measures to manage the supply and demand of foreign currency. The policy included reducing the limit on purchasing foreign currency with an underlying document, honing policy to manage foreign currency supply and demand on the spot and forward markets, optimizing foreign currency time deposits, optimising FX Swaps, issuing Foreign Currency Bank Indonesia Securities (SBBI), lowering the minimum holding period of SBI to one week, and strengthening the information on Foreign Exchange Flow (LLD). In addition, Bank Indonesia also coordinated with the Government to provide tax breaks on time deposit rates to exporters that deposit their export earnings at domestic banks or convert their export proceeds into rupiah.

Policy to lower the upper limit on purchasing a foreign currency without an underlying document was instituted in August 2015. Accordingly, the limit on foreign currency purchases through spot transactions without an underlying document was reduced from USD100 thousand to USD25 thousand or equivalent per customer per month. The policy was taken in order to control demand for foreign currency not involved with the real economy. Therefore, transactions associated with the real economy (with an underlying document), such as import payments, paying school fees, the cost of medicaments overseas and servicing external debt, were not restricted.

Subsequently, in September 2015, Bank Indonesia strengthened policy to manage supply and demand of foreign currencies on the forward market. The policy aimed to encourage forward selling transactions and clarify underlying forward buys. Forward selling transactions were encouraged by raising the maximum limit with an underlying asset from USD1 million to USD5 million per transactions per customer. Furthermore, the scope of underlying assets for forward transactions (residents and non-residents) and spot selling (rupiah transfers to non-residents) was extended to include proof of ownership of foreign currency domestically or abroad.

Managing the supply and demand of foreign currency was further strengthened by optimizing foreign currency term deposits. The absorption of liquidity was optimised by extending the auction window time, refining the auction method and stipulating the pricing as well as increasing the number of tenors available. The window time was extended on overnight foreign currency term deposit auctions from 14:00-15:00 WIB to 14:00-16:00 WIB in order to optimize the potential utilisation of foreign currency liquidity by domestic banks. In addition, Bank Indonesia also refined the auction mechanism, stipulated the pricing and made additional, longer tenors available, namely three months, in order to lengthen the absorption of foreign currency term deposits. The auction mechanism was changed from a variable rate tender (VRT) to a fixed rate tender (FRT) to communicate policy stance with greater rapidity. FRT implementation and the stipulation of pricing in line with the market rate had favourable impacts, reflecting increases in foreign currency term deposit transactions and the number of auction participants.

FX Swap instruments were also optimized in order to guarantee the availability of hedging instruments and to support liquidity management in order to balance the supply and demand of rupiah and foreign currencies. In September 2015, as part of the measures to strengthen the policy mix of Bank Indonesia, a 12-month tenor was added to complement the existing FX Swap tenors of 1, 3, and 6 months. The move ensured the availability of hedging instruments for the banking industry and corporate sector. To support liquidity management, Bank Indonesia also adjusted auction frequency and the number of outstanding FX Swaps at certain times. In the near term, the strategy temporarily raised the swap rate, which quickly returned to normal after the market adjusted.

Issuing Bank Indonesia Foreign Exchange Bills (SBBI) and shortening the minimum holding period for SBI were subsequent policy measures instituted. Not only was the policy introduced to manage the supply and demand of foreign currencies but also to strengthen financial market deepening. SBBI is a tradeable instrument with tenors of 6 and 12 months. Issuances of tradable SBBI supported financial market deepening efforts through development of the secondary market. Meanwhile, policy to shorten the minimum holding period of SBI from one month to one week was taken to boost non-resident investor interest in placements in Indonesia. Greater non-resident investment would support foreign currency liquidity management, enhance the effectiveness of monetary operations and accelerate financial market deepening.

In addition to the policies that were implemented to influence the balance between supply and demand of foreign currency directly, Bank Indonesia also strengthened the corresponding information infrastructure. The policy aimed to enhance the effectiveness of LLD management, in particular that related to transparency and information availability. Pursuant to Act No. 24 of 1999 concerning LLD and the Exchange Rate System, Bank Indonesia is authorised to requested information and data on the LLD from residents. In that context, various efforts to strengthen the information contained in the LLD reports were required from Bank Indonesia. One main feature was that Bank Indonesia now requires users of foreign exchange to comprehensively report such use with supporting documentation for transactions exceeding a certain threshold. Consequently, in addition to submitting information, customers with payments and receipts above a certain limit that influence bank checking accounts offshore are required to enclose supporting documentation to the bank.

Bank Indonesia also coordinated with the Government to provide a tax incentive on time deposit rates for exporters that deposit their export earnings at banks in Indonesia or convert their export proceeds into rupiah. The policy is contained in Government Regulations No. 123 of 2015 as an amendment to Government Regulation No. 131 of 2000 concerning Income Tax on Time Deposit and Savings Deposit Interest as well as Discounted Bank Indonesia Certificates (SBI). The progressive incentive is determined by the duration of the placement or full conversion into rupiah. The reduction in income tax on term deposits is to 0% for USD denominated time deposits of more than six months and for rupiah time deposits with a minimum maturity period of six months.

Strengthening International Reserve Adequacy

Bank Indonesia policy to strengthen the supply and demand of foreign exchange was also supported by measures to maintain the position of international reserve as first and second lines of defense. International reserve is a buffer to anticipate shocks that could undermine economic resilience. Accordingly, it became increasingly important to bolster the position of international reserve in 2015 in order to mitigate spiralling global economic uncertainty. By yearend 2015, the position of international reserve was adequate to maintain external resilience despite decreasing on the year earlier (Chart 11.4). The position of international reserve at the end of 2015 stood at USD105.9 billion, down from USD111.9 billion at the end of 2014. The decline stemmed from increased payments to service public external debt as well as rupiah stabilization policy, which eroded foreign exchange reserves but underpinned macroeconomic and financial system stability. Despite the decline, the level of international reserve at the end of 2015 was still equivalent to 7.4 months of imports and servicing public external debt, which is well above international adequacy standards of three months and the average position of reserve assets maintained by peer countries.[3]

Chart 11.4. International Reserve Adequacy for Import and Government Foreign Debt Payment

3 The International Monetary Fund (IMF) stipulates international adequacy standards of around three months of imports.

Table 11.2. Bank Indonesia's Swap Arrangements

No	Facility Type	Purpose	Value	Signing of Agreement	Validity Period	Explanation
1	ASEAN Swap Arrangement	Multilateral cooperation in the form of swap between the USD/yen/ euro and local currency ten ASEAN countries, aiming to provide short-term liquidity support for member countries experiencing balance of payments problems.	USD2 billion (maximum facility that can be drawn by Indonesia amounted to USD600 million)	16 November 2015	2 years	Extension several times since the first signing on November 15, 2005.
2	CMIM	Multilateral cooperation in the form of swaps between USD and ASEAN+3 currencies, aims to overcome liquidity problems due to problems of balance of payment and short-term liquidity in the region.	USD240 billion (maximum facility that can be drawn by Indonesia amounted to USD22.76 billion)	17 July 2014	Unlimited	Amendment of the agreement for the provision of CMIM. The preliminary agreement was signed in March 2010.
3	Bilateral Swap Arrangement BI-BoJ	Bilateral cooperation in the form of a swap between USD and rupiah, aims to prevent and overcome the difficulties of short-term foreign currency liquidity.	USD22.76 billion	12 December 2013	3 years	Extension several times after the first signing in February 2003, with an increase in the value and type of facilities.
4	Bilateral Currency Swap Arrangement BI-PBoC	Bilateral financial cooperation in the form of swap CNY and the rupiah, aims to increase trade and direct investment between Indonesia and China, to support the avability of short-term foreign currency liquidity for the stabilization of financial markets, and other purposes as agreed by both parties.	CNY100 billion (equivalent to Rp175 trillion)	1 October 2013	3 years	Extension. The first signing in March 2009.
5	Bilateral Currency Swap Arrangement BI-BOK	Bilateral financial cooperation in the form of swap KRW and IDR, aims to increase bilateral trade between Indonesia and Korea, as well as to strengthening the financial cooperation for the economic development in both countries.	KRW10.7 trillion/ Rp115 trillion (equivalent to USD10 billion)	6 March 2014	3 years	
6	Bilateral Currency Swap Arrangement BI-RBA	Bilateral financial cooperation in the form of swap AUD and rupiah, aims to increase bilateral trade between Indonesia and Australia, and other purposes as agreed by both parties.	AUD10 billion (equivalent to Rp100 trillion)	15 December 2015	3 years	

Reserve assets were reinforced by the international financial safety net (second line of defense) through regional financial arrangements as well as strategic partnerships with trade partners. Such facilities include the ASEAN Swap Arrangement (ASA), the Chiang Mai Initiative Multilateralization (CMIM) and the Bank Indonesia-Bank of Japan (BoJ) Bilateral Swap Arrangement (BSA) (Table 11.2).

Regionally, Bank Indonesia has entered into a swap arrangement with ASEAN member states in the form of the ASEAN Swap Arrangement (ASA), totalling USD2 billion. On 17th November 2015, the governors of ASEAN central banks extended the arrangement through to 2017. ASA can help meet short-term liquidity requirements for member nations that experience BOP pressures. For the period from 2015-2017, Bank Indonesia is acting as an Agent Bank to coordinate ASEAN Swap Arrangement (ASA) implementation when a participating member activates the facility.

Bank Indonesia has also agreed Bilateral Currency Swap Arrangements (BCSA) with the People's Bank of China (PBoC), Bank of Korea (BOK) and Reserve Bank of Australia (RBA). The arrangements aim to promote bilateral trade and guarantee transaction settlement using home currencies between both signatory countries. To that end, the arrangements are expected to reduce dependence on the U.S. dollar as the vehicle currency, thereby creating rupiah stability. Furthermore, the BCSA with the PBoC can also be utilised to overcome short-term liquidity shortfalls and thus maintain financial market stability. The BI-BOK BCSA, signed in 2014, is valued at Rp115 trillion and shall remain effective until 2017. Meanwhile, the BI-RBA BCSA was signed on 15th December 2015 and facilitates swap transactions denominated in home currencies to the tune of AUD10 billion, equivalent to Rp100 trillion.

11.3. MONEY MARKET AND FOREIGN EXCHANGE MARKET DEEPENING

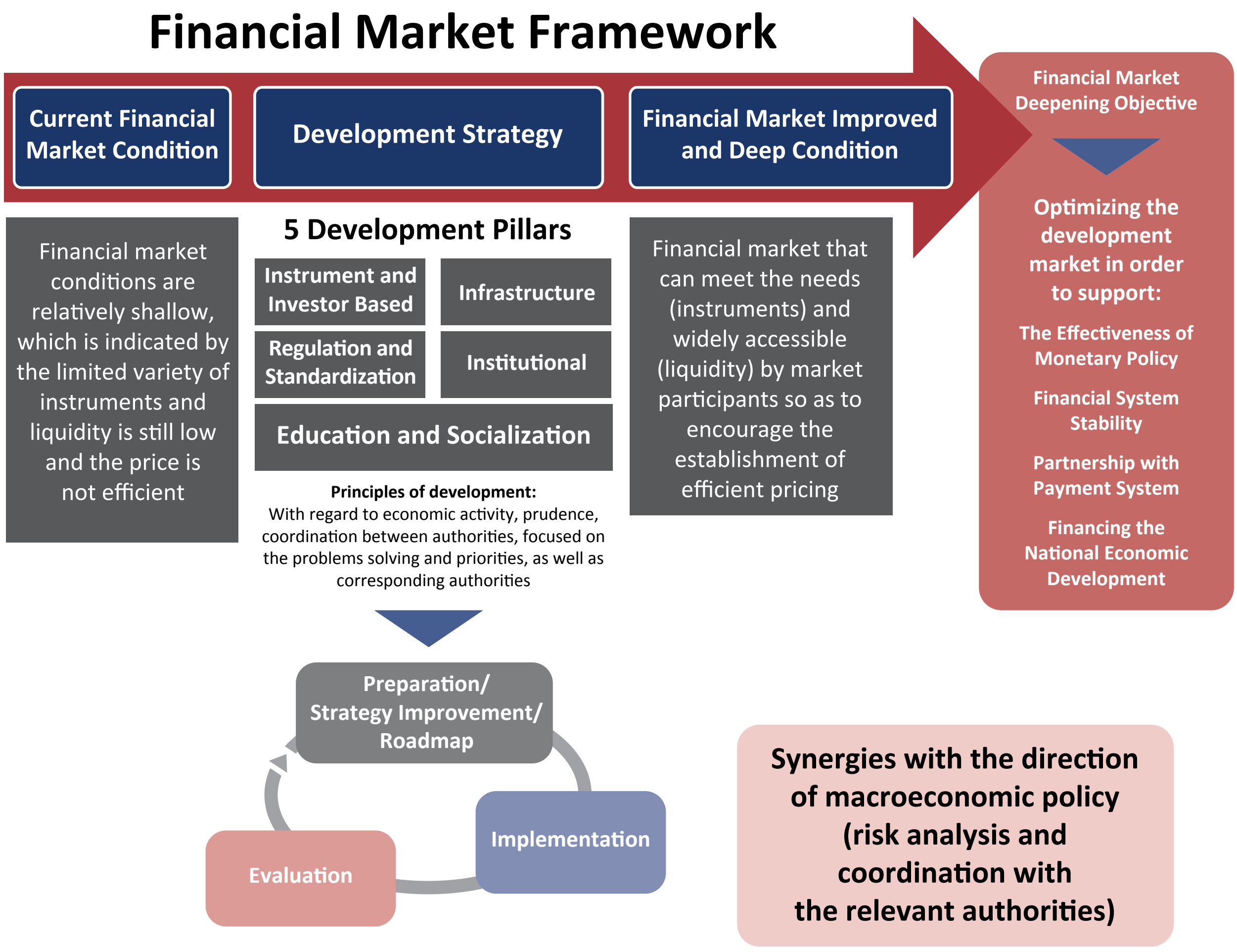
Efforts to deepen and develop the domestic financial markets were enhanced. Financial market dynamics over the past year have demonstrated the importance of deep and liquid markets in order to absorb external and internal shocks. Financial market deepening includes a broad market base, diverse instruments, and efficient pricing. The financial market deepening program also focused on facilitating business players develop their businesses through convenient forms of financing.

The Financial Market Deepening Blueprint was prepared as a guideline for the improvement and development of financial market structure for the upcoming 5-10 years. The Blueprint contains guidance for money market development programs along with the foreign exchange market, sharia financial markets and bond market (coordinative). Financial market development shall be achieved through five salient strategies, namely the development of instruments and the investor base, strengthening regulations and standardisation, infrastructure development, institutional strengthening as well as effective education and dissemination. Development based on the five strategies is expected to create deeper, more liquid and efficient financial markets, thus supporting monetary policy effectiveness, financial system stability and economic development financing (Diagram 11.2).

Financial market development encompasses the conventional and sharia rupiah money markets and foreign exchange markets. For the rupiah money market, the market deepening strategy includes development of the collateralised market to ensure liquidity availability, price efficiency and establishment of the term structure, while expanding interbank access on the uncollateralised or interbank money market and developing money market instruments as a source of liquidity for market players. On the foreign exchange market, however, the market deepening strategy will be focused on diversifying foreign currency instruments and interest rate derivatives. The magnitude of the foreign exchange market deepening strategy will promote foreign currency derivative transactions as an effective and efficient hedging instrument. Furthermore, foreign exchange market deepening will also support market player participation and diversification to help balance the supply and demand of foreign exchange. In addition, foreign exchange transaction transparency and efficiency will be enhanced through market infrastructure development. To develop the sharia economy and financial markets, Bank Indonesia is implementing a strategy to broaden sharia financial market share, to develop sharia financial market instruments and to optimize social funds and empower the real sector.

Coordination between the Government and Financial Services Authority (OJK) will be strengthened in order to develop the corporate bond and government bond markets. Coordination between Bank Indonesia and the Government will emphasise short-term government bond development along with transaction infrastructure and issuances of various bond instruments. Meanwhile, Bank Indonesia coordination with the OJK shall be focused on honing supporting regulations for issuances of corporate bonds, including state-owned enterprises. Supporting such

Diagram 11.2. Financial Market Deepening Framework



efforts, integrated infrastructure is also being prepared for corporate bond transactions.

Foreign exchange market regulations were relaxed to support nonbank corporate hedging activity in pursuance of applying prudential principles in the management of external debt. Deregulation affected derivative transactions between banks and residents as well as non-residents in accordance with Bank Indonesia Regulation (PBI) No. 17/6/PBI/2015 and PBI No. 17/7/PBI/2015. The underlying assets used for foreign exchange transactions by domestic parties were expanded to include financing for trade and investment activities. In addition, derivative transaction liquidity was increased by repealing the minimum tenor requirements for non-resident derivative transactions. Moreover, Cross Currency Swap (CCS) transactions were explicitly included in the derivative transactions regulated, thereby creating greater flexibility for market players to hedge.

Banks were also given more space to manage their intraday foreign exchange position, allowing greater freedom to provide hedging instruments to market players. The regulation requiring banks to maintain a net open position (NOP) every 30 minutes was also repealed through PBI No. 17/5/PBI/2015, dated 29th May 2015, as the fourth amendment to PBI No. 5/13/PBI/2003 concerning the Net Open Position (NOP) of Commercial Banks. By repealing the 30-minute NOP regulation, banks offering foreign exchange transaction services to their customers now enjoy more convenience in terms of managing their position and more flexibility with regards to the squaring position, which was extended until the end of the day. The policy is expected to reduce rupiah intraday volatility.

Efforts to promote hedging activity were also directed at state-owned enterprises with the active involvement of the Government. Accordingly, Bank Indonesia, the Government and law enforcement agreed that the financial consequences of hedging transactions were not to be borne by the state while the transactions were performed consistently, consequentially and accountably pursuant to prevailing regulations. In the second quarter of 2015, the national government-owned electricity company, PT Perusahaan Listrik Negara (Persero), and the state-owned energy company, PT Pertamina (Persero), facilitated by Bank Indonesia, signed hedging facilities (forex line) with three state-owned banks, namely PT Bank Mandiri (Persero) Tbk, PT Bank Negara Indonesia (Persero) Tbk, and PT Bank Rakyat Indonesia (Persero) Tbk. The signing is expected to expand the use of hedging facilities by other state-owned enterprises and private corporations in order to manage currency risk. Intensive socialisation of hedging policy was also provided with the active involvement of the stakeholders in order to enhance the utilisation of hedging facilities. To that end, Bank Indonesia, in conjunction with the Audit Board of the Republic of Indonesia, the Finance and Development Supervisory Agency, the National Police of the Republic of Indonesia, Public Prosecution Service of the Republic of Indonesia, Ministry of Finance and Ministry of State-Owned Enterprises, organised a national seminar entitled "Hedging as an Instrument of Public and Private Financial Governance" at the beginning of May 2015.

The Jakarta Interbank Offered Rate (JIBOR) mechanism was also honed. Most recently, JIBOR was refined through PBI No. 17/2/PBI/2015, dated 26th March 2015, concerning the Interbank Offered Rate. The regulation stipulates that JIBOR shall be based on the indicative interest rate submitted by contributor banks. Seeking to increase JIBOR creditability, since 1st April 2015, Bank Indonesia has required contributor banks to accept transaction requests from other contributor banks in order to borrow and/or lend rupiah at the indicative rate submitted, while meeting the prevailing requirements, otherwise known as the hittable JIBOR.

The refinements to JIBOR are expected to enhance efficiency and reduce financial transaction complexity because all market/economic players are using the same reference rates for all tenors. Furthermore, the money market reference rate for tenors of less than one year shall also complement the yield of government bonds (SUN) with a maturity period of 2-30 years, thereby creating a more credible yield curve, namely from overnight to 30 years. A credible yield curve is important for the monetary transmission channel as it contains market expectations of future economic conditions. In addition, a credible yield curve will encourage new instruments on the market, thus providing alternatives for business owners to expand their businesses and for investors to diversify their portfolios.

Accelerating sharia financial industry development, Bank Indonesia honed the regulation concerning the sharia interbank money market (PUAS) and facilitated agreement on the Sharia Mini Master Repo Agreement (MRA). Accordingly, Bank Indonesia issued PBI No. 17/4/PBI/2015, dated 27th April 2015, regarding the Sharia Interbank Money Market. The regulation expands alternative ways for sharia banks to meet their liquidity requirements through repurchase agreements for sharia-compliant securities, known as Sharia Repo. Sharia repo expands the types of transactions available to Islamic banks, hence complementing the existing sharia instruments, including Interbank *Mudharabah* Investment Certificates (SIMA) and Sharia-Compliant Commodity Trading Certificates (SiKA). On 2nd July 2015, eighteen Islamic banks agreed to use a Sharia Mini Master Repo Agreement (MRA) as a reference document for sharia-compliant repo transactions. The agreement was made paying due consideration to the large untapped potential of the sharia financial industry in Indonesia, where liquidity management remains suboptimal. Therefore, the agreement is expected to enhance liquidity management in the industry, in particular for Islamic banks, while increasing transactions on the sukuk market and sharia interbank money market, which will ultimately expedite financial market deepening.

11.4. MONETARY POLICY TRANSMISSION

The Interest Rate Channel

The rupiah overnight interbank rate experienced a number of significant, albeit temporary, spikes in 2015 before approaching the Deposit Facility (DF) rate again in line with abundant daily liquidity. The interbank rate peaked in September 2015 (Chart 11.5). In that period, the increase in the overnight interbank rate was accompanied by higher rates of longer tenors. For example, the 1-week rupiah interbank rate, which is usually around 6%, jumped to 6.5%. Similarly, the 1-month rate climbed from 6.5% to 8%. In the same month, the swap premium also soared to around 18% for tenors of one month due to a surge in demand for hedging from the corporate sector along with a shift in the supply and demand structure of the rupiah interbank money market. Notwithstanding, the swap premium returned to around 8% by the end of October 2015. Furthermore, relatively loose daily liquidity drove the overnight (O/N) interbank rate back to normal after the dramatic increase. The relatively high level of liquidity was reflected in the average volume of DF placements during the second half of the year, totalling Rp97.2 trillion per day, while the O/N interbank money

Chart 11.5. **Overnight Interbank Call Money Rate**

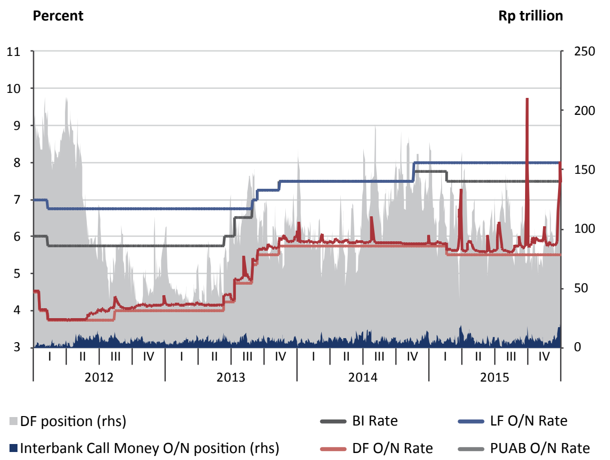
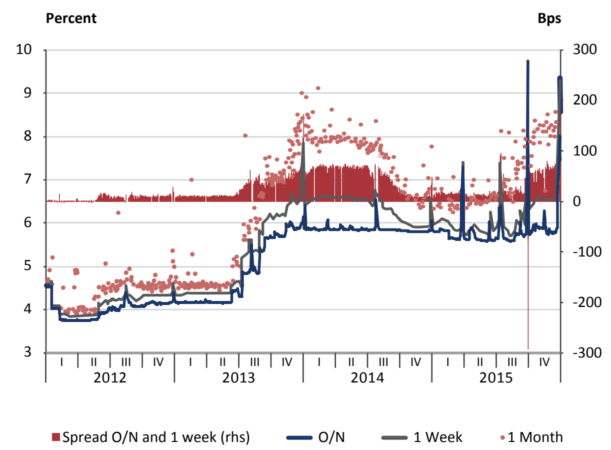


Chart 11.6. **Interbank Call Money Rates**

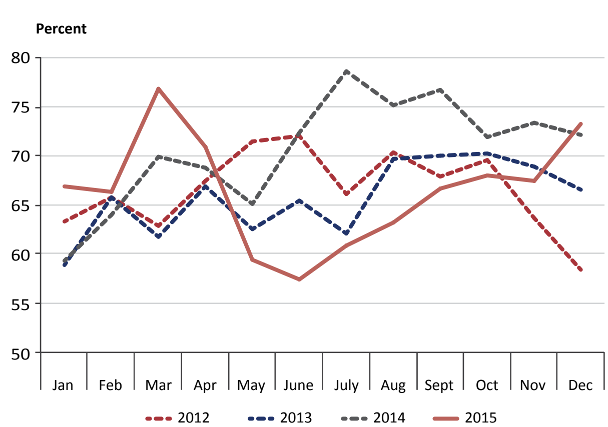


market volume was just Rp6.9 trillion per day. Loose daily liquidity was linked to conservative banks towards yearend as surplus liquidity evaporated and uncertainty blighted global financial markets. In addition, volatility on the interbank money market and swap market was mutually exacerbating.[4]

The undulations of the overnight interbank rate were mirrored by other tenors (non-O/N) with a wider spread as the term premium and risk premium rose. Escalating volatility on the overnight interbank money market throughout 2015 occasioned a wider spread between the overnight and non-overnight rates. Heightened volatility created uncertain bank costs, leading to a higher term premium and affected rates on longer tenors. The (absolute) spread between the overnight and 1-week interbank rates averaged 15bps from January until 21st August 2015, jumping to 46bps thereafter from 24th August until 31st December 2015. In terms of the risk premium, interbank money market heterogeneity, in particular regarding asset size, created market segmentation, which influenced the risk premium of non-O/N interbank rates. Banks engaged in lending had to calculate the credit risk and funding liquidity risk of the borrowing bank amidst domestic bank heterogeneity. Furthermore, relatively minimal market liquidity for non-O/N interbank transactions tended to raise the risk premium of such transactions, hence widening the spread between O/N and non-O/N rates. In 2015, average daily transaction value of 2-week tenor and tenor of longer than 2 weeks were respectively just Rp1.1 trillion, or 9.45% of total interbank money market transactions, and Rp263 billion, or 2.26% of the total (Chart 11.6 and Chart 11.7).

Lower time deposit rates until the third quarter of 2015 were not only the result of loose liquidity but also due to corrections to high rates maintained in 2014 stemming from tighter competition. In 2015, time deposit rates were lowered 84bps to 7.94% as competition amongst banks to attract deposits eased in line with persistently strong deposit growth through to the third quarter and fewer credit disbursements. A greater reduction to deposit rates than lending rates led to a wider interest rate spread in 2015, increasing from 417bps the year earlier to 489bps. The interest rate spread in Indonesia was much broader than that reported the region, such as Malaysia and Singapore, where 1.6-2.0% was normal (Chart 11.8).

Chart 11.7. **Ratio of Overnight to Total Interbank Call Money Transactions**



4 Due to suboptimal arbitration between liquidity on the interbank money market and FX swap market as a result of institutional arrangements in the banking sector. Institutional arrangements include credit lines and different desk functions of the interbank money market and FX swap market.

Chart 11.8. Time Deposit and Credit Interest Rate

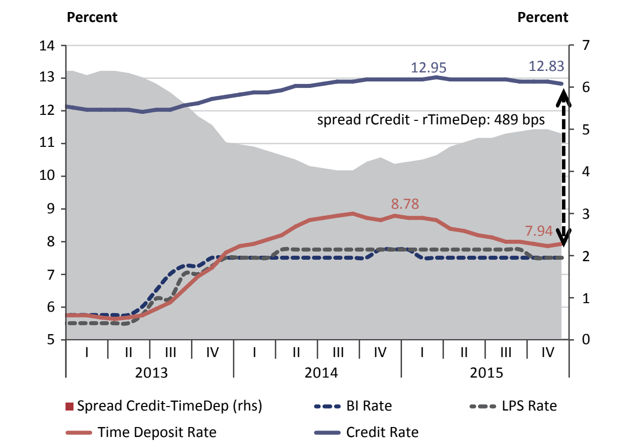
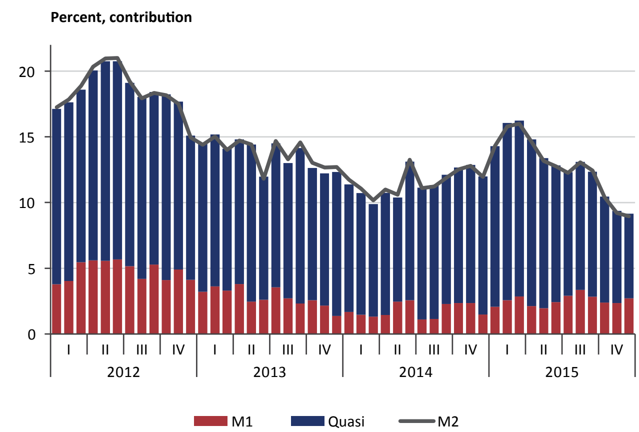


Chart 11.10. M2 Growth and Its Components



The reduction to deposit rates was followed by lower lending rates but of less magnitude and with a lag. The lesser magnitude of change was attributed to high credit risk as non-performing loans (NPLs) tracked an upward trend in 2015. Meanwhile, the lag was due to internal bank processes that require a certain amount of time after lowering the deposit rate. The weighted average lending rate at the end of 2015 was recorded at 12.83%, down 12 bps from 12.95% at the end of 2014. All loan types experienced lower rates of varying magnitude. Compared to the end of 2014, the rate on working capital loans was lowered 33 bps to 12.46% and the rate on investment loans was reduced 24 bps to 12.12%, contrasting the 30 bps hike in the rate on consumer loans to 13.88%. The varying degrees of magnitude, especially the increase to the rate on consumer loans, was the result of higher non-performing loans (NPLs) than the industry average.

The Liquidity Channel

Growth of narrow money (M0) slowed significantly in 2015 from 11.77% in December 2014 to 2.99%. The slowdown was caused by weaker growth of the secondary reserve requirement, which was met through SBI and SDBI, as well as lower bank demand deposits held at Bank Indonesia due to a reduction in the primary reserve requirement implemented in December 2015 and weaker deposit growth. Meanwhile, growth of Currency Outside Banks (COB) accelerated on the previous year. Based on its affecting factors, slower M0 growth was attributed to weaker growth of Net Foreign Assets (NFA) due to rupiah stabilization measures and Net Domestic Assets (NDA) as a result of a lower position of open market operations to meet bank liquidity requirements amidst limited expansion of government accounts (Chart 11.9).

Chart 11.9. M0 Growth and Its Components

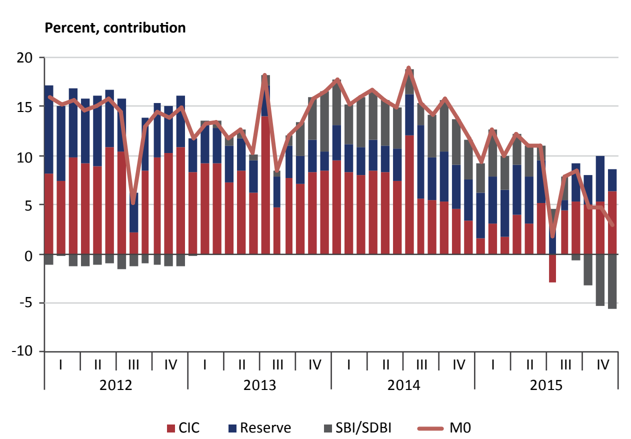


Chart 11.11. Growth M1 and Its Components

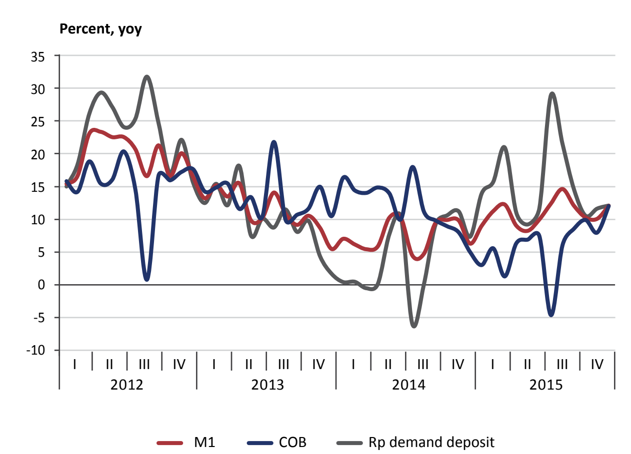


Chart 11.12. **Demand Deposit Growth and Its Components**

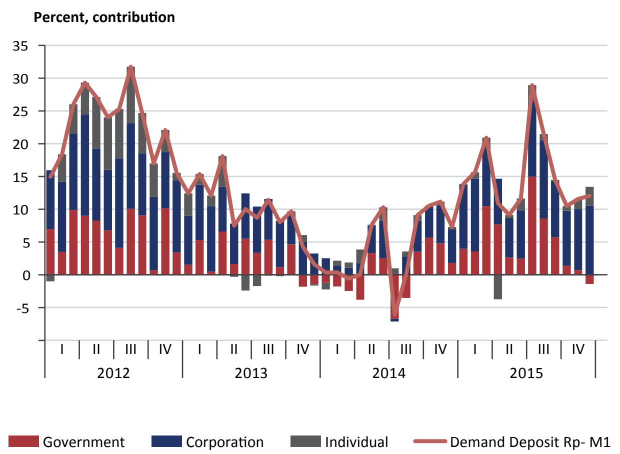
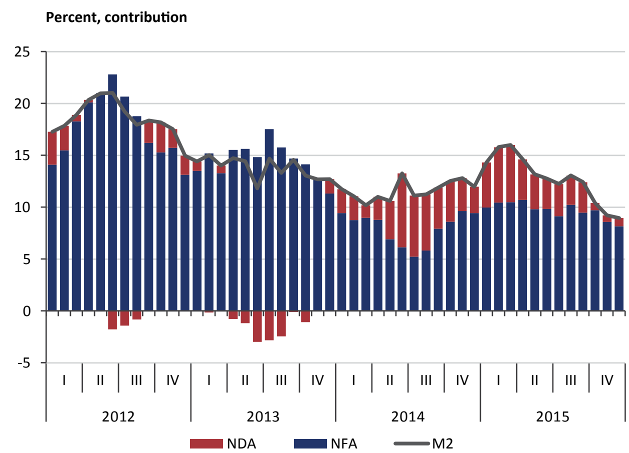


Chart 11.14. **M2 Growth and Its Affecting Factors**



Congruent with slower M0 growth, broad money (M2) growth also decelerated despite robust M1 growth. M2 growth fell from 11.95% in 2014 to 8.95% in 2015, with quasi-money contributing to the decline (Chart 11.10). Quasi-money growth decreased from 13.90% the year earlier to 8.37% in 2015, contrasting M1 growth that nearly doubled from 6.22% in 2014 to 12.00% in 2015. Solid M1 growth was supported by rupiah demand deposits and demand for currency (Chart 11.11 and Chart 11.12). Meanwhile, slower quasi-money growth, which precipitated the decline in M2, was the result of rupiah time deposits as the dominant component (Chart 11.13). Rupiah time deposit growth in 2015 was recorded at 7.55%, down significantly from 24.32% in 2014 because of economic moderation and the falling trend of deposit rates.

Based on the affecting factors of money supply, weaker M2 growth was due to Net Foreign Assets (NFA) and Net Domestic Assets (NDA). NFA growth slowed significantly from 9.3% last year to 3.0% due primarily to rupiah stabilization measures that eroded the NFA of Bank Indonesia. In contrast, the NFA of commercial banks recorded positive growth (Chart 11.14), consistent with the decrease in loans received from non-residents. NDA growth also slowed during the reporting period from 12.9% to 11.1% due to weaker credit growth, which decelerated from 11.6% to 10.45% over the same period as a result of economic moderation coupled with tight-bias monetary policy. Slower credit growth affected nearly all economic sectors, particularly the manufacturing industry, trade, agriculture and construction. Conversely, credit extended to the utilities sector grew significantly in 2015. Nonetheless, the contribution of the utilities sector to

Chart 11.13. **Quasi Money Growth and Its Components**

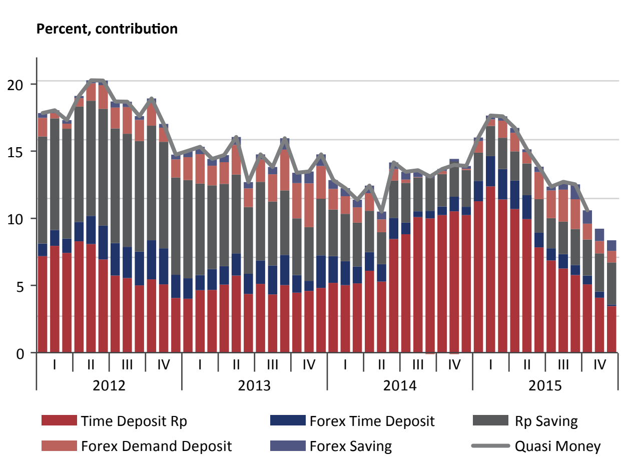


Chart 11.15. **M2 Velocity**

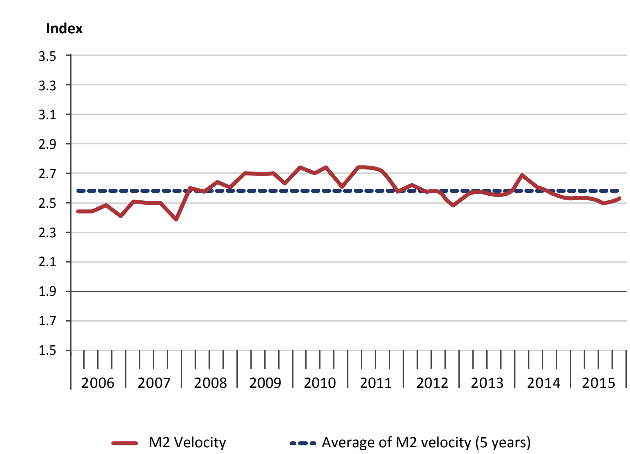
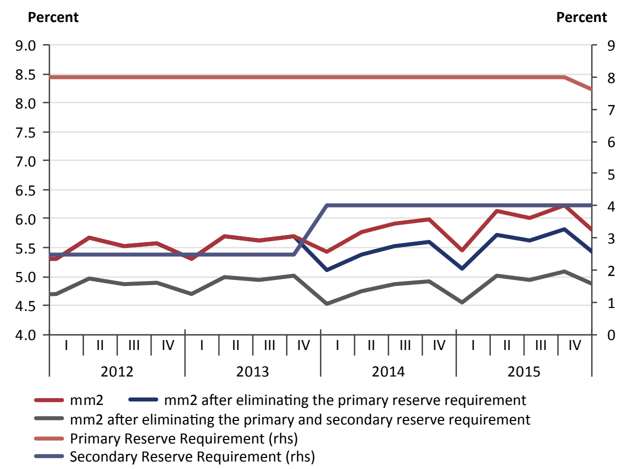


Chart 11.16. Money Multiplier M2 and Reserve Requirement



total credit was relatively small and thus failed to stimulate overall credit growth in 2015.

In general, liquidity in the economy was consistent with economic demand. Against a backdrop of slower M2 growth in 2015 due to domestic economic moderation, the velocity of M2 remained relatively stable. Such conditions are indicative of adequate liquidity to support domestic economic growth without triggering additional price-side pressures (Chart 11.15). Meanwhile, the M2 money multiplier increased slightly at yearend 2015, primarily due to the reduction in the rupiah primary reserve requirement. If the lower reserve requirement is omitted, however, the M2 money multiplier was relatively stable (Chart 11.16).

Bank Indonesia favoured accommodative macroprudential policy throughout 2015 in order to avert deeper economic moderation. To that end, Bank Indonesia loosened the loan-to-value ratio (LTV) and financing-to-value ratio (FTV) for credit and housing loans.

Chapter 12

Macroprudential Policy

In 2015, Bank Indonesia adopted accommodative macroprudential policy to address the issue of slowing credit growth and to safeguard the stability of the financial system. This macroprudential policy included: easing the regulation for giving property and motor vehicle loans, expanding the funding sources for banking intermediation through the Loans to Funding Ratio (LFR) regulation, policies to promote loans to micro small, and medium sized enterprises (MSMEs) and policies to lessen excessive procyclical banking behavior through countercyclical buffer (CCB).

A stable and sustainable economy needs a fairly sizeable contribution from the financial system. Global economic growth which continued to slow in 2015 has already led to heightened risks in the domestic financial system, especially those originating from uncertainties surrounding global economic recovery, falling commodity prices, and the monetary policy responses divergence of several major central banks. From the domestic side, declines in foreign capital inflows along with heightened pressures on the exchange rate - which led to weaker corporate performance - also put pressures on the performance of the financial system. Nevertheless, amid the heightened risks either from global or domestic economic factors, the soundness of the financial system was still maintained in general. The preservation of stability in the financial system played an important role in the development of the intermediation function, an increase in financing, and brought about greater resilience toward facing economic shocks.

As a response to the strong pressure on the stability of the financial system due to the slowdown in economic growth, Bank Indonesia adopted macroprudential policy in 2015 which was accommodative and countercyclical in the framework of supporting the economy and ensuring stability of the financial system. This macroprudential policy is part of Bank Indonesia's policy mix strategy in the framework of responding to global and domestic economic challenges. Macroprudential policy has an important role in preventing and reducing systemic risk which can affect the stability of the financial system. As such, macroprudential policy was focused on safeguarding the resilience of the financial system, supporting the establishment of a balanced and high quality intermediation function, in addition to improving access and efficiency of the financial system.

In June 2015, Bank Indonesia raised the Loan to Value (LTV) ratio or the Financing to Value (FTV) ratio for property loans and reduced the down payment for motor vehicle loans which was expected to increase the demand for loans in the property and automotive sectors. Then, in an effort to give more room to banks to conduct lending activities, Bank Indonesia expanded the funding sources for banking intermediation through the issuance of securities which were included in the Loan to Funding Ratio (LFR) such that banks did not just rely on deposits. Furthermore, Bank Indonesia also continued to encourage the development of MSMEs by providing incentives and disincentives for banks in reaching targets for channelling MSMEs loans. Besides that, Bank Indonesia also issued a regulation on the CCB toward the end of 2015 to strengthen the capital of banks and therefore mitigate systemic risk.

Besides the policies stated above, Bank Indonesia also regularly undertook surveillance and assessments toward financial system stability in the framework of identifying the sources of vulnerabilities and imbalances, especially in the large-sized banks. Based on the findings from these assessments, Bank Indonesia undertook thematic tests and compliance checks. Thematic tests were undertaken to evaluate and further research banking conditions and practices which may potentially create systemic risks. Compliance checks, meanwhile, were directed toward confirming that banks were already in compliance with various regulations issued by Bank Indonesia. Besides that, Bank Indonesia also improved coordination with the related authorities, either those undertaken bilaterally or through the Financial System Stability Coordination Forum (FKSSK), especially in regard to mitigating and handling crises.

The less stringent macroprudential policy stance - which had already been prepared for since the beginning of the year - was able to anticipate the fairly strong pressures on financial system stability in 2015. The maintenance of financial system stability was reflected in the Financial System Stability Index (FSSI) which still stood at a normal level (that is at 0.93 or slightly above its level in 2014 of 0.79). This index reading was still far below the crisis threshold of 2.0. The stability of the financial system was in line with the strong resilience of the banking sector which was indicated in the banks' capital adequacy ratios amid both slowing credit growth and bank financing. This resilience was also supported by the expansion of the state budget and various fiscal stimulus initiatives which were undertaken by the government in 2015.

12.1. EASING OF THE LOAN/FINANCING TO VALUE RATIO (LTV/FTV) REGULATION

The first macroprudential policy easing measure taken by Bank Indonesia in 2015 was the loosening of LTV/FTV for property loans and down payments for motor vehicle loans. This policy was contained in Bank Indonesia Regulation (PBI) No.17/10/PBI/2015 concerning the Loan to Value (LTV) Ratio or the Financing to Value (FTV) Ratio for Loans or Financing of Property and Down Payments for Loans or Financing of Motor Vehicles. The goal of easing LTV/FTV policy and down payments was to encourage recovery of the economy whose growth had slowed, especially through increasing loans/financing to the property and automotive sectors, including funding by using sharia principles. Despite the loosening of LTV/FTV policies and down payments, the concept of prudence was still applied by associating credit or financing easing with meeting the Non-Performing Loans (NPLs) or Non-Performing Financing (NPF) ratio.

This easing covered several matters, especially related to the level of the LTV/FTV ratio with an increase of 10% in all property components namely landed houses, apartments and house-shops/house-offices or for first home ownership, or second or third. Also, the level of the LTV/FTV ratio was differentiated based on the sharia financing agreement, that is the same ratio for *murabahah* and *istisna'* agreements whereas for *musyarakah mutanaqisah* (MMQ) and *ijarah muntahiya bittamlik* (IMBT) agreements the level is 5% higher for property type > 70. As such, the LTV/FTV ratio ranged from 65% until 90% with the ratio becoming higher for smaller types of property and for first home ownership (Table 12.1). By contrast, for larger types of property and post first home ownership, then the ratio will be smaller. For motor vehicle loans, meanwhile, the magnitude of the reduction in the down payment is the same at 5% for 2 wheel vehicles and 3 or more wheel vehicles which are classified as non-productive (Table 12.2).

Easing of this regulation allowed banks to apply a higher LTV/FTV ratio on loans extended to their customers. This provision is applicable for banks which have NPLs ratio for total loans and NPLs ratio for property loans of less than 5%. The same is true if banks reduce down payments for motor vehicle loans/financing (KKB). For banks which have NPLs ratio higher than the stipulated level, then the level of the LTV/FTV ratio used by banks is reduced by 10% for property loans and sharia financing with *murabahah* and *istisna'* agreements while for sharia financing with MMQ and IMBT agreements the ratio is unchanged.

Table 12.2. Downpayments on Automotive Loans

Type of Vehicle	Bank	
	Conventional	Sharia
Two Wheelers	20%	20%
Non-productive three wheelers or more	25%	25%
Productive three wheelers or more	20%	30%

In relation to the pre-purchase of property (indent), the LTV/FTV requirement is unchanged. This reflects the concept of prudence which is adopted by Bank Indonesia. Banks can only give loans or financing for property which is sold on an indent basis for first home loans/financing and where there is a cooperation agreement between the bank and the developer who must be able to complete the property in accordance with the agreement. Besides that, the developer must also provide guarantees, which either originates from the developer itself or another party if the property cannot be completed and/or handed over in accordance with the agreement.

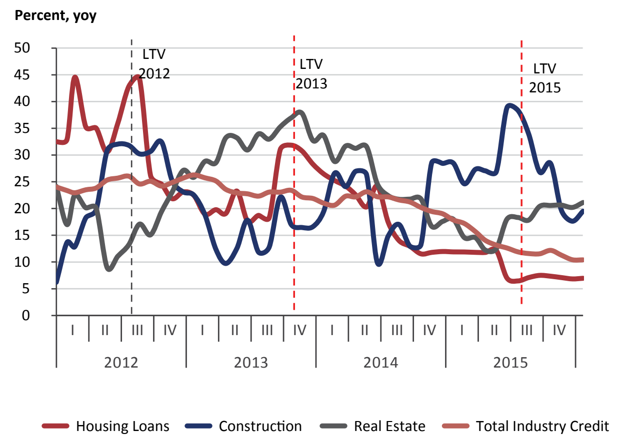
Easing of the LTV/FTV policy was able to arrest the slowdown in property loans growth (Chart 12.1). For real estate loans, meanwhile, growth had accelerated to 21.1% by the end of 2015, or up quite significantly from its lowest level in March 2015 of 13.6% (yoy). Nonetheless, the impact of reducing the size of the down payment for motor vehicle loans has yet to be felt, whereby its growth had continued to slow up to the end of 2015 (Chart 12.2). The slowing growth in motor vehicle loans owed to the decline in the private consumption of secondary goods,

Table 12.1. LTV Ratio Property Credit and Sharia Property FTV Financing

Conventional and Sharia Property Credit (Murabahah and Istishna' Agreement)			
Type of Property (m^2)	Conventional and Sharia Property Credit		
	I	II	III
Landed House			
Type >70	80%	70%	60%
Type 22-70	-	80%	70%
Type ≤ 21	-	-	-
Apartment			
Type >70	80%	70%	60%
Type 22-70	90%	80%	70%
Type ≤ 21	-	80%	70%
Shop House/Office House	-	80%	70%

Sharia Property Credit (MMQ and IMBT)			
Type of Property (m^2)	Sharia Property Credit		
	I	II	III
Landed House			
Type >70	85%	75%	65%
Type 22-70	-	80%	70%
Type ≤ 21	-	-	-
Apartment			
Type >70	85%	75%	65%
Type 22-70	90%	80%	70%
Type ≤ 21	-	80%	70%
Shop House/Office House	-	80%	70%

Chart 12.1. **The Growth of Property Credit**

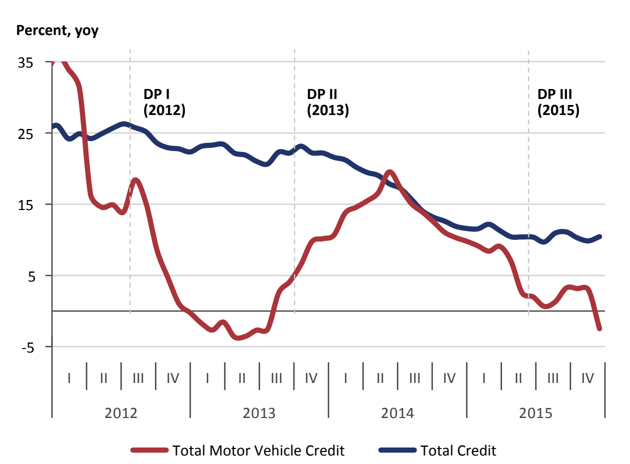


a slowdown in production activity and weaker business activities in line with the slowdown in economic growth in 2015.

12.2. EXPANSION OF INTERMEDIATION FUNDING SOURCES THROUGH THE LOAN TO FUNDING RATIO (LFR) REGULATION

Besides easing the LTV/FTV regulation and down payments to increase the demand for property loans and motor vehicle loans, Bank Indonesia also made efforts to boost the capacity of bank intermediation. Bank Indonesia expanded the funding sources for bank intermediation by issuing securities which are included in the calculation of the LFR such that banks do not have to rely only on deposits.[1] Previously, the Loan to Deposit Ratio (LDR) was used as a performance indicator for bank intermediation and determining the bank intermediation target range used by Bank Indonesia. The use of the LFR indicator to replace the LDR will provide banks with more room to channel loans although with an unchanged target range.

Chart 12.2. **Motor Vehicle Credit Development**



Bank Indonesia saw that it was necessary to expand the funding components for intermediation after initially only including deposits. Expanding the funding components for intermediation became effective on 1 August 2015, by including the securities issued by a bank. Widening the scope of funding sources will give banks more room to expand their lending activities. Bank Indonesia sets the criteria for the securities issued by a bank which can be included in the LFR, namely issuances in the form of medium-term notes (MTN), floating rate notes (FRN), and bonds besides subordinated bonds. These three types of securities must be offered through limited public offerings and have ratings from rating agencies at investment grade at least. Besides that, these securities must be owned by nonbank investors and administered by institutions authorised to give custodian services and settlement of securities transactions.

The target range for the LFR set by Bank Indonesia is the same as the LDR target range which it replaced, that is 78% as the lower limit and 92% as the upper limit. In the event that a bank's LFR falls outside of this range, then Bank Indonesia imposes disincentives in the form of additional statutory reserves which must be deposited at Bank Indonesia. The parameter for disincentives at the lower end (LFR < 78%) is 0.1 and the parameter for disincentives at the upper end (LFR > 92% and CAR < 14%) is 0.2 which are each multiplied by the difference of the bank's LFR and the target, and then multiplied with the deposits of each bank to obtain the figure for the additional amount of reserves requirement. Furthermore, Bank Indonesia also provided incentives by easing the LFR upper limit to 94% for banks which achieve the micro, small and medium enterprises (MSMEs) loans target and have good credit quality, i.e. a NPLs to total loans ratio (gross) < 5% and a NPLs ratio for MSMEs loans (gross) < 5%.

Based on the evaluation up to the end of 2015, the amount of securities which had already been issued by banks experienced an increase after the implementation of the LFR provisions (Chart 12.3). Besides that, extending the coverage of financial intermediation from deposits to

1 Contained in PBI No.17/11/PBI/2015 concerning Changes to PBI No.15/15/PBI/2013 on Statutory Reserves for Commercial Banks in Rupiah and in Foreign Exchange for Conventional Commercial Banks.

Chart 12.3. RR LFR and SSB Issued by Bank

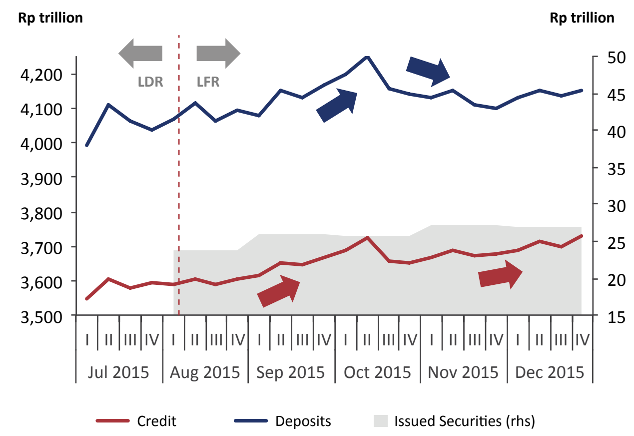
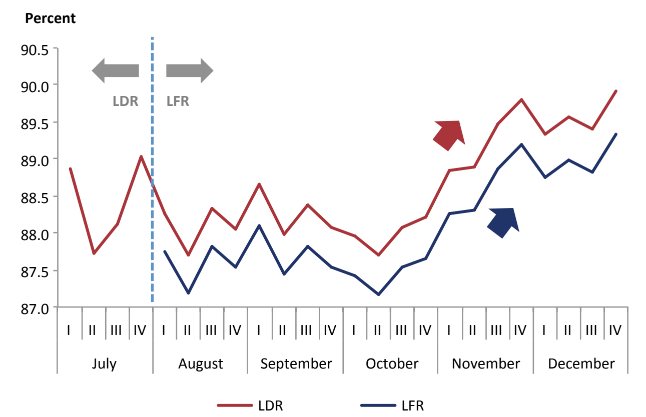


Chart 12.4. Comparison between LDR and LFR



funding also lowered the LFR level (lower than the LDR) thereby giving banks more room to channel more loans (Chart 12.4). Nevertheless, in the same period there was also a slowdown in the growth of banks' deposits with growth in deposits less than the credit growth. This was reflected in the overall slowdown in the economy which reduced corporate earnings and household incomes such that since October 2015 the LFR has increased on the back of a decline in savings.

12.3. POLICIES TO SUPPORT THE DEVELOPMENT OF MSMES

Policies for the development of MSMEs were undertaken to help Bank Indonesia to achieve its goal of controlling inflation from the supply side and also to attain a more balanced intermediation function in the banking sector. The strategy to develop MSMEs was implemented through two main approaches, namely extending and deepening financial infrastructure as well as increasing the capacity of MSMEs. This strategy was realized through various programs such as improving regulations, improving the access to finance for MSMEs, and increasing the capacity of MSMEs.

In line with the enactment of PBI No.17/11/PBI/2015, improvements were also made to PBI No.17/12/PBI/2015 concerning Amendments to PBI No.14/22/PBI/2012 concerning Lending or Financing by Commercial Banks and Technical Assistance in the Framework of the Development of Micro, Small and Medium Enterprises. Completion of this regulation embodies the mix between policies to develop MSMEs and macroprudential policies. For banks which can achieve their MSMEs loans target quicker than expected with a maintained NPLs ratio, they will get flexibility on the LFR upper limit. By contrast, banks which are unable to achieve their MSMEs loans target and/or have a NPLs ratio of 5% or more, they will be given disincentives in the form of a reduced remuneration rate (on reserve requirement) by 0.5% plus 0.1 times the difference between the MSMEs loans ratio which has been set and that reached by the bank. For banks which can achieve their MSMEs loans target yet have a NPLs ratio of 5% or more, their remuneration rate will only be reduced by 0.5%. Besides that, for banks which channel loans/financing to MSMEs they will also be given incentives in the form of training for MSMEs account officers (AO), training for micro and small enterprises (MSEs), facilitating the use of credit ratings for small and medium enterprises (SMEs), the publication of banks' successes, and giving awards to banks.

In order to increase the capacity of MSEs to provide financial information so they can access financing from financial institutions, Bank Indonesia cooperated with the Indonesian Institute of Accountants (IAI) to develop a simple financial statements module for MSEs. This module consists of General Guidelines, Technical Guidelines and a training module for Recording Financial Transactions of Individual MSEs and Small Business Enterprises which are Not a Legal Entity. These activities are a follow-up of the Recording Financial Transactions for MSEs program which was initiated by Bank Indonesia in 2014. Besides that, to make it easier for MSEs to produce simple financial statements, Bank Indonesia has also developed tools/prototype of an early Recording Financial Transactions application which can be accessed by android smartphones and can be downloaded for free from Playstore. The development of early tools/prototype refers to the Technical Guidelines and the Recording Financial Transactions Training Module which had already been developed previously, along with simulations for a number of MSEs and Bank Partner Financial Consultants (KKMB) for further improvement.

In increasing financing in the agricultural sector and as a follow-up from the study undertaken in 2014, Bank Indonesia undertook a value chain financing (VCF) pilot project. This value chain financing program is intended to identify key success factors for VCF financing so that it can be adopted on a wider scale. In the pilot project, restructuring of the value chain was undertaken, including restructuring of planting patterns, institutions, markets and financing which is expected to improve the ability of farmers to access financing. At the end of the pilot project, commercial loans were already channelled on the basis of the VCF scheme to Bank Indonesia's target clusters. The key success factors from the value chain financing included: (i) the involvement of all players in the value chain, (ii) the existence of a structured market, (iii) the adoption of production systems based on market demand, (iv) the application of collective production with the application of technology (planting methods, good agricultural practices, post-harvest processing), (v) assistance for value chain players, and (vi) rural financial services.

In 2015, the development of clusters was still based on staple food commodities or commodities which had become a source of inflationary pressure. The determination of the target clusters was undertaken through the framework of supporting the realisation of Bank Indonesia's main task, namely price stability, especially of volatile food commodities. Bank Indonesia has already managed to replicate three business models for staple foods clusters (red chili peppers, onions and beef cattle) in four provinces, namely Lampung, East Kalimantan, Gorontalo, and South Sulawesi. Besides that, in a bid to promote implementation of the cluster development program, Bank Indonesia also carried out a performance awards program (championship) for staple foods clusters. This program is one way to internalize the importance of the role of Regional Government (Pemda) in developing clusters in an attempt to help control inflation in the regions. From this program, clusters of staple food commodities/the best performing commodities (which were the source of inflation spread across 43 regional Bank Indonesia Representative Offices) were chosen, either founded by Bank Indonesia, Pemda/Dinas or through Pemda cooperation with other parties. Evaluation of the performance of the clusters is based on a number of factors, including social capital, partnerships and networking, competency and expertise, market access, and infrastructure support.

Besides that, Bank Indonesia also completed several studies in 2015, including a study on the strategy to increase the competiveness of MSMEs in facing ASEAN Economic Community (AEC) 2015 and a study related to the goal of increasing the financial access of the poor in either rural or coastal areas. With the enactment of AEC 2015, which is aimed at forming a single market, single production base, a highly competitive region, as well as equitable and globally integrated economic development, it is necessary to determine the position of Indonesian MSMEs relative to the MSMEs of other ASEAN countries, along with strategies to boost the competiveness of MSMEs in facing AEC 2015. The findings of our studies show that to increase the contribution of Indonesian MSMEs in AEC, the performance of Indonesian MSMEs needs to be improved from the aspect of productivity, the contribution towards exports, participation in the global and regional production networks along with the contribution to value added. As such, several factors determining the competiveness of MSMEs need to be improved, whether they are internal factors (human resources, productivity, marketing, innovation) or external (ease of doing business, access to finance and capital, market access, infrastructure and macroeconomic conditions). Besides that, a paradigm shift is needed in policy formulation related to MSMEs, which initially was more concerned with social welfare (excessive protection) toward a greater focus on the business approach through facilitation to gain access. This is because MSMEs need access to inputs (raw materials, human resources, capital goods), as well as financing and markets for the products or services produced.

To improve financial access for those in the fisheries sector who are still unbanked, Bank Indonesia undertook a study on the potential for the unbanked people's finances in coastal areas. The study was conducted at two locations: Demak (Central Java) and North Gorontalo (Gorontalo). Among other things, the study was aimed at identifying business development needs as well as the ways to access financing. The findings of the study show that the existence of unbanked community businesses in coastal areas needs an improvement in the quality and character of the people. As an example, a paradigm change is needed in the people's thinking so they can control their consumptive lifestyles and recognize the importance of saving a portion of their business income for business development. Besides that, efforts are needed to continuously empower and mentor businesses to overcome problems related to the fisheries sector, namely developing alternative livelihoods during bad seasons, improving access to capital, technology and information, as well as global markets, along with developing community institutions through cooperatives. In regard to financial access, financial institutions are needed which are able to reach the people with both savings and loans products which do not involve difficult or complicated procedures.

In the framework of improving financial access for people living in rural or coastal areas, the presence of financial institutions which are able to reach the people in those areas also plays an important role. As such, Bank Indonesia is working with the Asia-Pacific Rural and Agricultural Credit Association (APRACA) to undertake the project "Documenting Global Best Practices on Sustainable Models of Pro-Poor Rural Financial Services in Developing Countries" which is an International Fund for the Agricultural Development (IFAD) project. This project is aimed at developing financial services for people in the agriculture and fisheries sectors and sustained through the application of best practices in accordance with the norms of Indonesian society. The best practices criteria is determined based on inclusion criteria as designated by APRACA, including the products offered (savings and financing), scope, collateral, innovation and good governance.

In its early stage, the best practices of providers of financial services/financing schemes in a number of areas in Indonesia have already been identified. These include the Micro Agribusiness Financial Institution (LKMA) Pincuran Bonjo in West Sumatra, BMT Sidogiri in East Java, and KUD Mina Samudera in Banten. The advantages of these best practices include institutions founded on local initiatives and local resources, independency and showing good performance. The developed financial services include savings which meet the people's needs and loans which do not always require collateral but utilize public figures as guarantors or are made under a system of joint responsibility. These best practices will be implemented in a pilot project in the district of Parigi Moutong (Central Sulawesi) and in the district of West Lombok (West Nusa Tenggara).

It is believed that around 50% of MSMEs in Indonesia are owned by women with generally smaller and informal businesses. This number is quite significant if the businesses are developed and have the potential to propel national economic growth. As such, Bank Indonesia is working with the International Finance Corporation (IFC) to undertake a study on women entrepreneurs in Indonesia. This study is aimed at analysing the health of MSMEs, especially those owned by women, the obstacles encountered, along with giving recommendations to stakeholders. In general, MSMEs face a number of challenges related to their informal status along with limited sources of long-term capital. Nevertheless, the challenges for women entrepreneurs also stem from time limitations related to the dual role of women in business and family. Besides that, women entrepreneurs are also less familiar with technology, especially information technology and communications. To overcome this problem, it is recommended that among other things the process for awarding business licences to women entrepreneurs should be eased, tax deductions should be given to new entrepreneurs, as well as training and financial education, including the adoption of mobile banking which can facilitate access to financial services for women entrepreneurs.

12.4. MANDATORY FORMATION OF COUNTERCYCLICAL BUFFER

Toward the end of 2015, Bank Indonesia issued a policy which was aimed at safeguarding the stability of the financial system namely the Countercyclical Buffer (CCB). This policy is one of the instruments which is aimed at preventing the occurrence of systemic risk due to the excessive channelling of loans through the establishment of an additional CCB's capital buffer. This matter was related to procyclical banking behavior, i.e. the excessive channelling of loans at times when the economy is in an expansionary phase and, by contrast, a lack of lending at times when the economy is in a contractionary phase. As a result, procyclical behavior during the economic expansion phase can heighten potential credit risk. This is reflected in the increase in NPLs in the economy's contractionary phase.

To overcome this problem, policies are needed to improve the resilience of banks. This resiliency can be achieved by reducing the amount of loans channelled in the economy's expansionary phase and forming additional capital that can be used by banks to cover losses that may occur when an economy is in a contractionary phase.

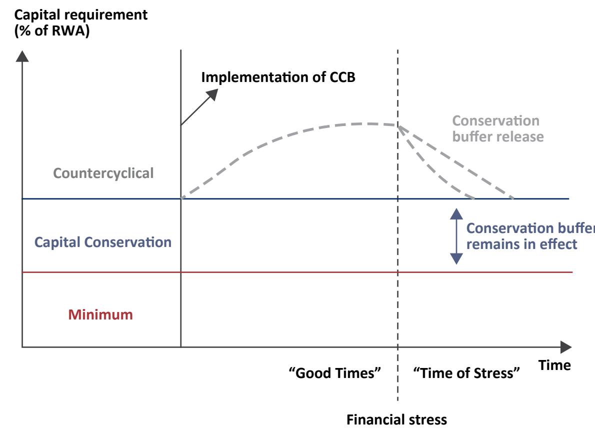
In the framework of strengthening the resiliency of banks in regard to capital, the Basel Committee on Banking Supervision (BCBS) has already introduced additional capital buffers, namely a conservation buffer, CCB and capital surcharge.[2] The CCB is an additional capital which is aimed at procyclical bank lending behavior and raising banking resiliency. CCB policy tends to be time varying: i.e. the CCB rate can change in accordance with macroeconomic conditions and the financial system. The formation of additional CCB capital is done in the expansionary phase, especially when it is believed there exists potential systemic risk from excessive credit growth. Meanwhile, the release of additional CCB capital which has already been formed by banks can be done during the contractionary phase so it can be used in part to support bank lending and recoup losses. Chart 12.5 illustrates the formation and the release of the CCB buffer. As for the CCB rate, it is in the range of 0–2.5% from the Risk-Weighted Assets.

Referring to the BCBS guidelines concerning implementation of CCB and also a study of CCB implementation which has already been carried out by Bank Indonesia, PBI No.17/22/PBI/2015 dated 28 December 2015 concerning the Obligation to Form a Countercyclical Buffer has already been issued. This policy needs to be implemented in Indonesia considering the procyclical behavior in Indonesia's economic growth and bank lending (Chart 12.6).

The decision to implement CCB is not seen as mechanical in the sense that it is not only supported by information from primary and secondary indicators which are quantitative in nature, but also combined with qualitative judgements. The main indicator is a guide which is used to calculate the CCB rate. The main indicator which will be used is the credit to GDP gap. Meanwhile, the complementary indicators come in the form of supporting information which includes the financial cycle, macroeconomic indicators, bank indicators, and asset prices. It is obligatory for CCB to be formed by conventional banks and sharia banks, including foreign banks.

The formation of additional CCB capital is carried out together with the capital conservation buffer and capital surcharge which are fulfilled with the Common Equity Tier

Chart 12.5. Illustration of The Formation and The Release of The CCB Buffer



1 – CET 1 component. The formation of this third buffer is undertaken after fulfilling Capital Adequacy requirements in line with the risk profile.[3] Evaluation of the magnitude and timing of CCB is done by Bank Indonesia at least once in six months. In PBI No.17/22/PBI/2015 concerning the Mandatory Formation of Countercyclical Buffer, Bank Indonesia set the CCB rate at 0% as of 1 January 2016, such that banks have not yet needed to form additional CCB capital.

12.5. SURVEILLANCE AND MACROPRUDENTIAL TESTS

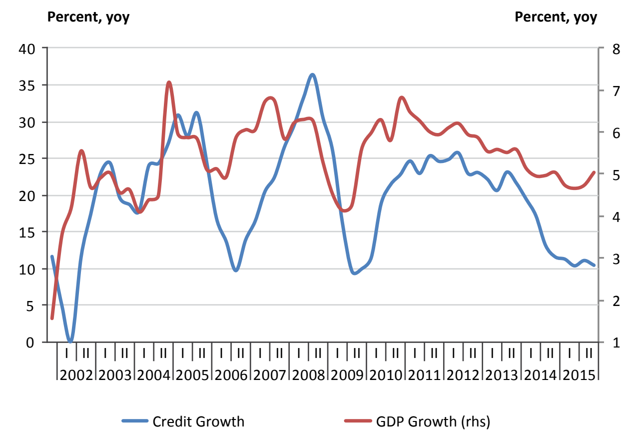
To help achieve macroeconomic stability and maintain stability of the financial system, Bank Indonesia has undertaken surveillance of the financial system and macro-prudential tests of banks on a regular basis. Surveillance and assessments of the stability of the financial system were carried out to identify the sources of vulnerabilities and imbalances, especially at large banks, which can create systemic risk. The tests done included thematic tests and compliance tests on macro-prudential regulations and other Bank Indonesia regulations.

The thematic tests carried out by Bank Indonesia were aimed at gathering information as a basis for further examining banking conditions and practices which may potentially create systemic risks. These tests were based on specific information concerning inherent bank risks. Such risks, if they accumulate, can have an impact not

2 The conservation buffer is additional capital which functions as a buffer in the event of losses during a crisis, while capital surcharges are additional capital which serves to mitigate the negative impact on the stability of the financial system and the economy should banks fail which has a systemic impact through increasing the ability of banks to absorb losses. The conservation buffer applies to banks classified as Commercial Banks Based on Business Activities (BUKU) 3 and BUKU 4, while capital surcharges apply to banks deemed to have a systemic impact (Domestic Systemically Important Bank, D-SIB).

3 The explanation of commercial banks' capital can be seen in regulations which govern the Capital Adequacy of banks.

Chart 12.6. Procyclicality of Economic Growth and Credit Growth in Indonesia



only on banks individually but may also potentially create a further impact, either on other banks or on the banking industry overall. Meanwhile, compliance checks were conducted in the framework of assessing the compliance of banks in implementing and complying with various regulations issued by Bank Indonesia.

During 2015, Bank Indonesia already conducted tests on a number of large banks to assess the latest economic conditions. One of the things observed was related to the trend in the volatility of the rupiah/U.S. dollar exchange rate. Although currencies weakened relative to the U.S. dollar across the globe, Bank Indonesia was particularly concerned by the reasons for the rupiah/U.S. dollar exchange rate volatility. This is because the impact of exchange rate volatility on the domestic economy is quite significant. Besides thematic tests related to exchange rate volatility, tests were also conducted to ascertain the resilience of bank liquidity, along with the readiness of banks to undertake stress tests.

In carrying out tests on banks, Bank Indonesia coordinated with the Financial Services Authority (OJK) as the regulatory and supervisory authority in regard to micro-prudential matters. The sound cooperation between Bank Indonesia and OJK was undertaken via the Macro and Micro Coordination Forum which is continuously improved through the process of sharing information. Besides that, coordination and policy alignment was also carried out in the framework of taking supervisory action against banks which could potentially pose a systemic risk.

Noncash toll payments were just one part of the National Noncash Movement (GNNT) that has, hitherto, successfully increased transaction speed and efficiency. Moving forward, Bank Indonesia shall consistently encourage various electronification initiatives throughout the economy.

Chapter 13

Payment System and Currency Management Policy

Bank Indonesia's payment system policy in 2015 focused on strengthening of infrastructure, including through the implementation of the Bank Indonesia-Real Time Gross Settlement (BI-RTGS) and Bank Indonesia-Scripless Securities Settlement System (BI-SSSS) Generation II as well as the Bank Indonesia National Clearing System (SKNBI) Generation II and the electronification of payments. Bank Indonesia also sought to encourage the obligation to use rupiah currency while in Indonesian territory and reinforced its supervision of this by coordinating with the relevant agencies. In addition, the reform of cash distribution and cash services was also taken to provide rupiah in sufficient quantities, high quality, appropriate denominations, and a timely manner. These measures were backed by the clean money policy and efforts to combat the distribution of counterfeit money.

Payment system infrastructure strengthening policy was Bank Indonesia's main concern in 2015. This was intended to boost the security and reliability of payment systems, enabling them to operate more smoothly and efficiently. Infrastructure strengthening policy was pursued through the implementation of BI-RTGS and BI-SSSS Generation II as well as SKNBI Generation II. The reliability of these systems was an important factor in the improved speed and accuracy of transaction settlements by means of payment systems.

Bank Indonesia also encouraged the expansion of public access to payment system, as well as the establishment of maximum transaction charges to be imposed on the public, in an effort to improve the efficiency of payment system. Meanwhile, in order to maintain public confidence in the system and non-cash payment instruments, Bank Indonesia consistently encouraged the payment system industry to always pay attention to aspects of consumer protection. Through these policies, the public was able to enjoy the benefits of using non-cash to payment instruments as well as become accustomed to use non-cash payment instruments in the transaction which is the main goal of the National Non-Cash Movement (GNNT).

Bank Indonesia's measures in the field of currency management referred to Law Number 7 of 2011 concerning The Currency, and the application of these measures were based on three policy pillars. These pillars were the availability of good quality and reliable of rupiah currency in circulation, the secure and optimal of rupiah currency processing and distribution, as well as excellent cash services. Bank Indonesia consistently strove to meet the demand for currency fit for circulation in order to support economic activities across the territory of the Republic of Indonesia. It is well known that supplying currency in sufficient quantities and a variety of denominations, maintaining the quality of this currency as fit for circulation, and ensuring that it reaches all areas of Indonesia's vast geographical expanse, presents a challenge to Bank Indonesia in carrying out its currency management duties. Besides that, to maintain public confidence in the rupiah currency as a payment instrument, Bank Indonesia faces with the challenge of an increasing circulation of counterfeit money, especially in areas with high levels of economic activity.

These challenges in currency management should be addressed with concrete effort of Bank Indonesia by taking various rupiah currency management policies. In 2015, these policies included maintaining the sufficiency of its cash position. Furthermore, reforms to the way in which currency distribution and cash services were an important aspect for Bank Indonesia in its gradual expansion of the availability of good quality rupiah currency to all parts of Indonesia. To this end, the role of banks and cash in transit operators continued to be optimized in support of Bank Indonesia's efforts to circulate currency effectively. Similarly, effort to strengthening coordination with ministries/institutions and cooperation with state-owned enterprises were also very important, in particular to maintain the smooth distribution of currency to all areas in Indonesia.

To maintain the quality of currency in circulation in the society, Bank Indonesia had pursued policies to improve the quality standards of rupiah currency deposited by banks. This policy resulted in a rise in the amount of currency unfit for circulation which was destroyed by Bank Indonesia. This policy was undertaken while paying due regard to the sufficiency of Bank Indonesia's cash position and maintaining the supply of printed currency from Perum Peruri (The Indonesian Government Security Printing and Minting Corp.). In terms of consumer protection, Bank Indonesia accelerated efforts aimed at familiarizing the public with the characteristics of authentic currency, in terms of both frequency and range of activities, including media and public activities. This range of activities was expected to result in the public becoming more adept at recognizing the characteristics of authentic currency. The activities were also aimed at getting the public to avoid using counterfeit currency. Moreover, to contain the spread of counterfeit currency, Bank Indonesia sought to enhance the compliance of banks in reporting the finding of counterfeit money to Bank Indonesia. Bank Indonesia also coordinated with the Indonesian National Police and other law enforcement agencies in disclosing cases of counterfeit currency distribution to serve as a deterrent for those contemplating becoming involved in the crime of counterfeit money production.

13.1. PAYMENT SYSTEM POLICY

The payment system is the infrastructure of the financial system whose smooth operation needs to be maintained in order to support transactions by the public, government and business. To that end, the role of payment systems is very strategic in supporting the stability of the monetary and financial systems. As the authority in the area of payment systems, Bank Indonesia consistently takes policies that support the realization of payment systems that are secure, reliable and efficient. These policies include strengthening infrastructure to improve the security and reliability of payment system, as well as expanding access to payment system to improve efficiency through non-cash instruments. In addition, Bank Indonesia and the payment system industry have also made various efforts to improve public confidence, and convenience to the public, in performing transactions using payment systems by paying attention to the issue of consumer protection.

The Implementation of Payment System Infrastructure Strengthening in Bank Indonesia

Infrastructure strengthening is intended to bring about secure, efficient, and smooth payments systems with different types of services and an ever greater accessibility for the wider community. To enhance the retail payment system infrastructure, Bank Indonesia is implementing gradually the SKNBI Generation II. SKNBI Generation II uses the latest technology and international standards in order to accommodate cross-border transactions while paying due regard to the issue of consumer protection. SKNBI Generation II also improves transaction speeds by increasing the number of times fund transfers can be settled in a day from four to five. In addition, the existence of a Service Level Agreement (SLA), or time limit for delivering funds through SKNBI, also enhances consumer protection.

Based on its development phases, SKNBI Generation II is divided into two stages. The first phase is for the development of existing services (individual fund transfer services and individual debit clearing services). The second phase, meanwhile, is for the development of multiple credit transfer and multiple debit transfer services for servicing the public's regular payments needs. The first phase of SKNBI Generation II was implemented in June 2015, while the second phase will be implemented in the first quarter of 2016.

Besides SKNBI Generation II, the development of payment systems have also been realized through the implementation of three Generation II major Indonesian financial infrastructure systems. The first of these is BI-RTGS which is a high value transfer and settlement system (high value payment system). The second is BI-SSSS which is a system for the settlement and administration of securities, especially Government Securities (SBN) and Bank Indonesia Securities (SBBI), while the third system is the Bank Indonesia-Electronic Trading Platform (BI-ETP) which is a transaction system for SBN, SBBI and Money Market auctions (trading platform). All three of these updated systems were implemented on November 16, 2015.

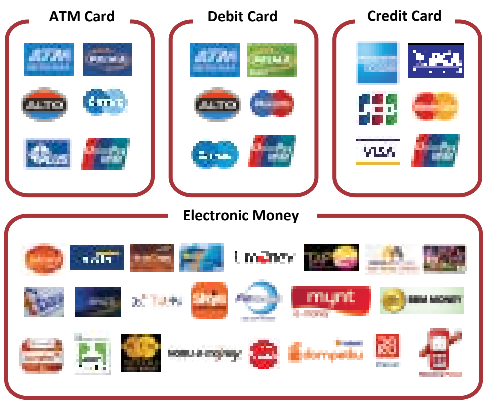
The implementation of these three systems marks a new era in the operation of payment systems in Indonesia. This new era in payment system operations represents a response to ever evolving business and technological needs. These business needs are associated with the development of more efficient liquidity management, an increasing diversity of securities, and convenience in performing transactions. Meanwhile, the use of the latest hardware and software infrastructure as well as standardized messages is to accommodate the latest technology, as is the updating of the BI-RTGS and BI-SSSS Generation I systems which were already 10 years old. With specific regard to message standardization, which sees the adoption of the ISO 15022 message format as the international standard for payment systems, participants will find it easier to make interconnections between the BI-RTGS, BI-SSSS and BI-ETP Generation II systems and the related internal systems of each participant, extending also at a later stage to cross-border interconnections. With the shift from Generation I to Generation II, the reliability of the infrastructure and operation of the BI-RTGS and BI-SSSS systems is expected to improve, thereby enhancing the efficiency of these systems and making it easier for Bank Indonesia and the Government to make policy changes with respect to carrying out SBN transactions and administration.

Developments in the Technical Development Stages of the National Payment Gateway (NPG)

The development of information technology has had a positive impact on electronic retail payment systems. This impact is evident from the use of non-cash payment instruments, such as Card-Based Payment Instruments (CBPIs) and Electronic Money, which grows significantly from year to year. Even though in terms of numbers, volume and value, CBPIs and electronic money transactions are growing, these instruments are still not fully able to meet the needs of the public. This is due to the fact that the electronic retail payment infrastructure in Indonesia is not yet at an optimal level. This is reflected, among other things, in the ongoing fragmentation of retail payment system service providers, whereby these providers are unable to provide an equivalent service to the other. Furthermore, each of these payment system service providers also has members that are not connected to each other (Picture 13.1). Such a situation causes limitations and inequality in public access to payment system services.

Implementation of electronic retail payment system infrastructure is still not efficient given that the

Picture 13.1. **Digital Financial Services Development**



interconnections and interoperability among payment service providers do not occur effectively. The existence of multiple switching service operators that are not connected results in banks/operators having to become a member of all the existing switching operators. Meanwhile, the presence of various payment channels that are not inter-operational leads to the public only being able to enjoy limited services. This situation also makes it difficult for Bank Indonesia to access and administer retail payment system transaction data and information in a comprehensive manner. As the central bank, its ability to carry out supervision, risk mitigation, and policy decisions pertaining to payment systems and the stability of the financial system is thus compromised. The data of retail payment systems are not yet available, among others, including CBPIs transaction data (local and international), electronic banking transaction data (e-banking), and electronic commerce transaction data (e-commerce).

Consider these issues, Bank Indonesia plans to develop a National Payment Gateway (NPG) with the aim of integrating various payment channels to facilitate electronic payment transactions. The NPG implementation plan has involved a series of in-depth studies and has drawn lessons from the best practices of other countries. At present, policy research being conducted includes a comparative analysis of thirteen sample countries that have implemented an NPG. The formulation of an NPG implementation policy in Indonesia requires meticulousness and prudence in addressing existing payment gateways (switching), both domestic and global. As the authority, Bank Indonesia still gives due consideration to existing switching providers with a view to creating healthy competition, cost efficiency in the processing of payment transactions, as well as innovative services that support the needs of the public. To this end, Bank Indonesia feels that the use of the currently available retail payment infrastructure should be streamlined and optimized.

The results of benchmarking against other countries reveal that, in essence, there are two groups of infrastructure topologies used to support an NPG, a centralized model and distributed model. Whichever model is to be used, Bank Indonesia has the authority to determine the operational model as well as the institutions which will become operators. In general, the completion of the NPG implementation in Indonesia will be divided into four phases, beginning with the releasing of a basic NPG policy in 2016, which will be followed by the development of the first phase, then with an NPG service coverage expansion policy, and ending with the final phase of development.

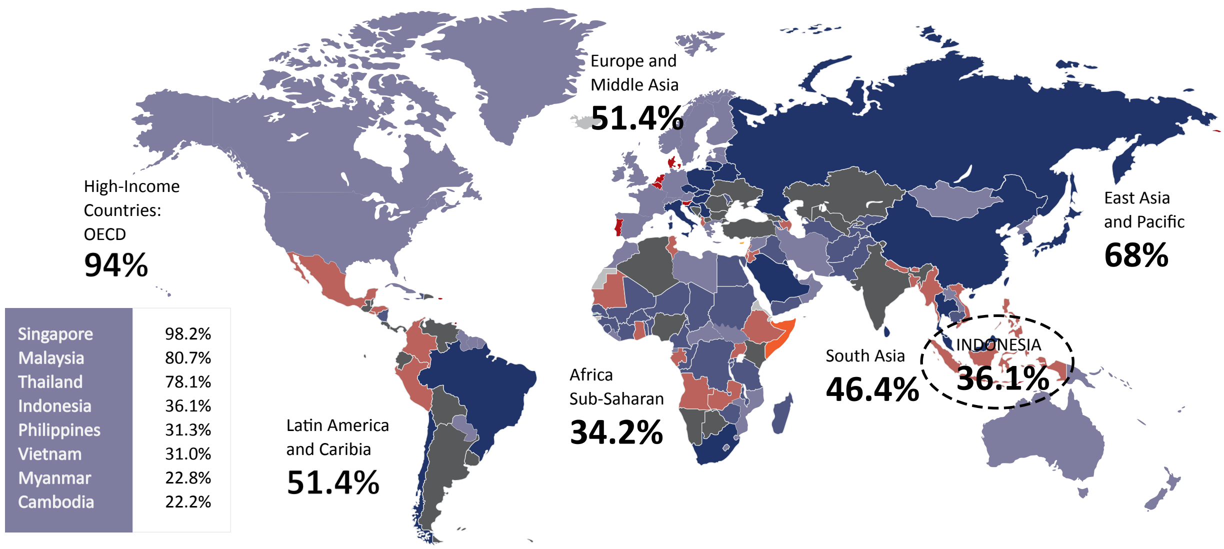
In 2015, Bank Indonesia completed more than 80% of the preparation of the NPG design concept including the definition, functions and service coverage of the NPG, the NPG development phases, development priorities, ownership and operation of the NPG, as well as various development methods that will be employed. This NPG design concept will serve as a reference for Bank Indonesia and the payment system industry in developing a range of payment transaction services for the public that are integrated in line with the needs of the national economy. With the emergence of the NPG, retails payment systems in Indonesia are expected to become more efficient, secure and reliable, while of course prioritizing national interests. As the regulator, Bank Indonesia will regulate prices, brands as well as mechanisms in line with its authority as the payment system authority.

Financial Inclusion

Bank Indonesia's Financial Inclusion policy in 2015 was a continuation of its 2014 policy whereby it focused on financial education, the formulation of supporting measures/regulations, as well as intermediary facilities and distribution channels. The measures formulated by Bank Indonesia were intended to improve and expand public access to financial institutions. Results of a World Bank survey showed the level of financial inclusion in Indonesia in 2014 to be at 36.1%, up from the 2011 of 19.6% (Picture 13.2).[1] Compared to other countries in the area, this figure was still relatively low compared to the level of financial

1 Global Findex, World Bank, 2015.

Picture 13.2. **Financial Inclusion in Indonesia**



Source: Global Findex – World Bank, 2014

inclusion in East Asia and the Pacific which stood aat 69.0%.

Meanwhile, the level of financial literacy among the Indonesian public was still classified as low to moderate, as seen in a number of indicators.[2] First, the level of public recognition of financial institutions stood at 35.2. Of all financial institutions, the most recognized by the public were Banks (76.0%), followed by Post Offices (63.0%), Cooperatives (59.0%), and Pawnshops (58.9%). Second, the level of public knowledge of basic financial concepts (the concepts of inflation, insurance, interest, and investments/shares) stood at 54.5. Third, the attitude of the public towards financial management, as measured by their attitude towards saving and attitude towards looking at the future, was not spontaneous in nature and was always oriented towards achievements, with a value of 61.2. Fourth, public behavior in financial management, as measured by the aspects of financial planning, financial oversight, avoiding excessive expenditure, covering unexpected expenses, planning for the future, utilizing information, living self-sufficiently and product selection had a value of 63.1.

As an early step in improving financial literacy among the public, Bank Indonesia formulated a Financial Inclusion (FI) education strategy to act as a guideline in providing financial education to the public. This FI strategy comprises the following three pillars: (i) policies that analyze of the implementation of FI education program, assessments of survey results, roadmaps, and monitoring; (ii) a program consists of a) materials grouped into financial attitudes, behavior and knowledge, b) materials for publication in the media, including print, electronic, and social media, c) FI education mechanisms in the form of campaigns/ dissemination of information, Training of Trainer (ToT), and Training of Beneficiary (ToB); (iii) FI education targets, namely the public and influencers. In its execution, the FI education strategy was more focused on mass educational activities by means of campaigns and dissemination of information, both directly to the public and through print, electronic, and social media. During 2015, Bank Indonesia in cooperation with relevant ministries/institutions carried out a range of FI education programs, such as financial education for: Indonesian migrant workers (TKI) and prospective migrant workers (in conjunction with the National Agency for the Placement and Protection of Indonesian Migrant Workers (BNP2TKI, the Ministry of Manpower, the World Bank, ILO, Tifa, and banks), inhabitants of outlying islands, pupils and students, housewives, farmers/fishermen/small traders, recipients of government aid, and micro, small, and medium enterprises (MSMEs) entrepreneurs.

Efforts to improve financial literacy were also realized through the Digital Financial Services (DFS) program. The development of this program, which was launched in July 2014, was quite good with the emergence of DFS in all provinces of Indonesia. The increasing proliferation of DFS

2 Survey on Financial Inclusion in Indonesia, Bank Indonesia, 2015.

was reflected in a rising number of DFS operating banks and DFS agents. Up to December 2015, there were 5 DFS operating banks and as many as 69,548 DFS agents serving the public in 461 regencies/cities (Chart 13.1). The number of holders of electronic money has reached 1,145,486 people who between them held Rp43.1 billion in funds. There were various types of transactions performed by people through DFS agents. The most common was electronic cash deposits (top-ups) accounting for 44.8% of total transactions, followed by person to account transfers (44.7%), and routine payment transactions (6.2%). The average transaction value through DFS agents was Rp44,891, with an average largest transaction - the initial transaction (initial deposit) - of Rp380,917, and the average smallest transaction, in the form of a top-up, of Rp27,398 (Chart 13.2). The average value of transactions through DFS agents was in accordance with the outline of how much unbanked people could afford to spend.

In 2015, various programs were also conducted to improve financial access for the public by using a community approach, one of them targeting the Muslim community through a strategy of Islamic Financial Inclusion. In this case, Bank Indonesia conducted a pilot project involving three telecommunications company (telco) as DFS operators and pesantren (Islamic boarding school) communities as DFS agents. The considerations given for involving these telco in the trial included that the telco are accustomed to serving the mass market, excel in communication technology, and have electronic money applications that integrate with mobile phone numbers. Meanwhile, the considerations given for involving the pesantren included that they are well known as influencers, have communities and business units with experience in servicing the payment of *zakat*, *infaq*,

Chart 13.1. **Digital Financial Services Development**

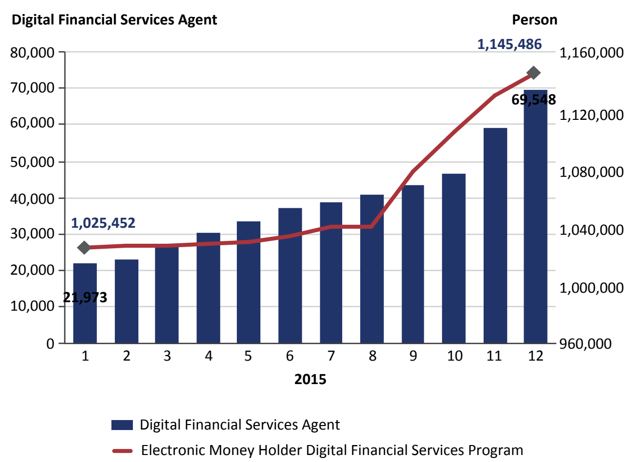
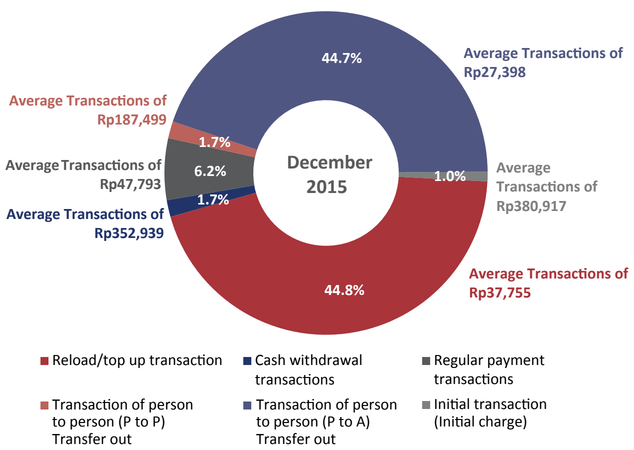


Chart 13.2. **Average Transactions of DFS**



sadaqah (ZIS - religious tax, donations, charity) as well as microfinance transactions in the vicinity of the pesantren. In terms of products, electronic money is a perfect instrument to use for attracting the Muslim community to engage in DFS transactions, bearing in mind that electronic money does not involve the element of interest, which is deemed to result in usury (*riba*), and therefore does not contravene Islamic principles. The components of this pilot project formed part of Bank Indonesia's efforts to synergize its policy of expanding financial access by focusing on the development of DFS as a point of access, using electronification policies to develop the DFS ecosystem.

Bank Indonesia also assisted the Government with the distribution of non-cash social assistance to the public (Government to Person) through Digital Financial Services (DFS) and Post Offices. The distribution of Prosperous Family Savings Program (PSKS) aid has benefits for the government, operators, and recipients alike. The government benefits in terms of increased transparency, cost efficiency, and precision targeting. Meanwhile, operators benefit in terms of the emergence of new markets for product development, and increased revenues from transaction fees. As for recipients, they also benefit in terms of lower fund withdrawal fees, greater time efficiency in withdrawing aid funds, and greater connectedness with banks to facilitate the saving of money and improve security in the saving of money. At the macro level, the distribution of non-cash social aid will have an impact in stimulating local economic growth, improving financial inclusion, improving the public's quality of life, and reducing poverty in the long-term.

Follow-up to the Implementation of the National Non-Cash Movement (GNNT)

In addition to the expansion of the Digital Financial Services (DFS), an electronification program was carried out in the framework of improving financial literacy. Bank Indonesia prepared an electronification roadmap in support of the National Non-Cash Movement (GNNT) which was launched in August 2014. The purpose of this roadmap is to provide direction and guidance to all stakeholders in support of the electronification program.[3] The increase in non-cash transactions through the electronification program has had a positive impact on the economy. The assessment results show that the increase in non-cash transactions of 10% correlated to a rise in consumer spending of 0.5%. Consumer spending, meanwhile, is a contributor to economic growth, thereby increasing the prospect of a virtuous cycle between non-cash transactions and economic growth.[4]

Bank Indonesia collaborated with ministries/institutions and other relevant authorities to increase the number of non-cash retail transactions among the public, especially with the use of electronic money instruments. Bank Indonesia has signed 45 manuscripts of Memorandum of Understandings (MoU) and Cooperation Agreements with Ministries/Institutions, both at the central and regional levels. As a follow-up measure to these MoUs, Bank Indonesia, together with the Indonesian Ministry of Manpower and the National Agency for the Placement and Protection of Indonesian Migrant Workers (BNP2TKI), implemented the use of non-cash transactions and the expansion of financial access in the placement and protection of migrant workers (TKI). In addition to measures carried out in Indonesia, Bank Indonesia also encouraged the use of non-cash instruments through formal remittance channels for remittances of migrant workers from abroad. Through these actions, the entire process of TKI fund transactions and administration is expected to be more efficient and transparent.

A number of electronification programs were implemented, the benefits of which were immediately felt by the public in 2015. Electronification in the transport sector was carried out, among other ways, by the implementation of e-tickets for the TransJakarta busway system and KAI Commuter Jabodetabek/KCJ (Greater Jakarta Commuter Trains), as well as the implementation of e-parking, in cooperation with the Jakarta Government Department of Transportation, in several areas that already had electronic parking terminals (TPE). Meanwhile, with regard to the implementation of electronification in the regions, these included electronic-based retribution payments (*e-retribusi*) in traditional markets in Palembang, the Bandung smart card (electronic money - still in the first phase - for shopping, parking and bus tickets, which will be further developed for the payment of health and education services, in Bandung), the transfer of Civil Servant salaries in Banjarmasin, the transfer of contract employee salaries in all Central Kalimantan Government agencies, Regional Development Banks Bali Mobile (the payment of tax and retributions to the Denpasar city administration through mobile banking), and e-ticketing at the Galala-Poka crossing in Ambon.

To raise public awareness for the use of non-cash transactions in 2015, Bank Indonesia also held the National Non-Cash Movement (GNNT) festival. The GNNT festival promoted the theme of "Love Non-cash, Love the Rupiah" through various interactive activities and payment system services and product displays aimed at enhancing public understanding of the issue. The inspiration behind promoting the expansion of non-cash transactions was also apparent in a number of initiatives carried out in various regions through Bank Indonesia Regional Representative Offices, including the implementation of a Less Cash Society (LCS) at various universities, such as Sultan Ageng Tirtayasa University (Serang) and Pattimura University (Ambon). Socialization and education were also done to the officers and staff in ministries/institutions, Local Governments, and the public at large.

Implementation of Chip Technology and a Six-Digit Online PIN for ATM/Debit Cards

In order to realize secure payment systems, Bank Indonesia applied a policy of implementation of chip and technology a 6-digit online PIN on the ATM/Debit cards. The use of a chip card for ATM/Debit was based on considerations that there had been a decrease in fraudulent transactions involving credit cards since they were fitted with chips in early 2010. The use of a chip was also an effort to prevent the falsifying and skimming of cards, while the implementation of the 6-digit online PIN sought to improve security, particularly in cases of lost and stolen cards. In addition, these actions were also intended to encourage efficiency through interoperability and increase the self-sufficiency of national industry.

3 The definition of electronification is a unified and integrated effort to transform payments from using cash to non-cash. The purpose of electronification is to transform all payment methods from manual to electronic, transform most payment mechanisms from physical to digital, and change limited access into widespread access (inclusive).

4 Global Insight (2003). The Virtuous Circle: Electronic Payments and Economics Growth. San Francisco: Visa International.

Bank Indonesia issued a number of provisions to support the implementation of the chip technology and 6-digit online PIN for ATM/Debit cards. The first of these provisions was outlined in Bank Indonesia's Circular Letter No.17/51/DKSP governing changes to withdrawal and transfer limits via ATM machines.[5] For those ATM cards with a magnetic stripe, the maximum daily limit for cash withdrawals is Rp10,000,000 and the maximum daily limit on interbank transfers is Rp25,000,000. Meanwhile, for those ATM cards with chip technology, the maximum daily limit for cash withdrawals is Rp15,000,000 and the maximum daily limit on interbank transfers is Rp50,000,000. The second of the provisions was outlined in Bank Indonesia Circular Letter No.17/52/DKSP containing adjustments to the schedule for the implementation of national standards on chip technology and the 6-digit online PIN for ATM/Debit card transactions.[6] The implementation of the chip technology, which was previously scheduled for no later than December 31, 2015, was extended to no later than December 31, 2021. Meanwhile, the implementation of the 6-digit online PIN for ATM/debit cards that use a magnetic stripe was extended to no later than June 30, 2017. For the application of chip technology, all ATM/Debit cards issued by issuers Indonesia, along with their supporting facilities, shall use national standard chip technology no later than December 31, 2021. Issuers can still use magnetic stripe technology for deposit accounts with a maximum balance of Rp5,000,000 based on a written agreement between the issuer and customer.

These provisions form part of Bank Indonesia's measures to consistently encourage the use of non-cash instruments by the public at a low cost. Adjustments to the schedule for the implementation of national standards on ATM/Debit cards were made by taking into consideration the fact that the majority of ATM/Debit card operators were not yet fully ready to implement national standards on chip technology and the 6-digit online PIN. To encourage greater readiness, Bank Indonesia is providing incentives for using cards with chip technology in the form of an increase in the maximum limit on cash withdrawals and transfers for ATM/Debit cards.

5 Bank Indonesia Circular Letter No. 17/51/DKSP, dated December 30, 2015, regarding the Third Amendment to Bank Indonesia Circular Letter No. 11/10/DASP, dated April 13, 2009, regarding Operations of Card-Based Payment Instruments.

6 Bank Indonesia Circular Letter No.17/52/DKSP, dated 30 December 2015, regarding the Implementation of National Standards on Chip Technology and the Use of a 6 (Six) Digit Online Personal Identification Number for ATM and/or Debit cards.

Implementation of the Regulation Obliging the Use of Rupiah in the Territory of the Republic of Indonesia (NKRI)

In the context of the policy mix, the Regulation obliging the use of the rupiah in the territory of the Republic of Indonesia has effectively managed to uphold the sovereignty of the rupiah as the currency of the Republic of Indonesia. Since the enactment of this regulation in July 2015, the number of domestic non-cash transactions using the U.S. dollar has begun to decline sharply.[7] This indicates that the obligation to use the rupiah in the territory of the Republic of Indonesia has had a positive impact in supporting efforts to manage the demand for foreign currency and the stability of the rupiah. This is also reflected in the results of a survey on perceptions regarding this regulation, using a sample of Travel Agencies in four areas - Batam, Jakarta, Surabaya, and Bali. In general, almost all the sample companies surveyed already knew about Law No. 7 of 2011 and the enforcement of the provision on the Obligation to Use the Rupiah in the Territory of the Republic of Indonesia, as issued by Bank Indonesia. In terms of price quotations, the majority of the travel agents sampled in Jakarta and Bali provided these in foreign currency. Conversely, the majority of the travel agents sampled in Batam and Surabaya did not provide price quotations in foreign currency. The main reason that price quotations were still being provided in foreign currency was that the exchange rate of the rupiah to foreign currency was constantly fluctuating or unstable, and another reason was to accommodate foreign customers. Revenues in foreign currencies during the three months after the implementation of the Bank Indonesia regulation showed a decline, whereas revenues in rupiah showed an increase. Furthermore, the travel agencies sampled expressed their willingness to list their travel prices, both domestically and abroad, in rupiah.

With respect to the implementation of the regulation obliging the use of the rupiah, Bank Indonesia coordinated with, and disseminated information to, the Coordinating Ministry of Economic Affairs, Ministry of Finance, Ministry of Energy and Mineral Resources, Ministry of Foreign Affairs, Ministry of Religious Affairs, Ministry of Transportation, Ministry of Industry, Ministry of Tourism and Creative Economy, the Financial Services Authority, the Investment Coordinating Board, the Commodity Futures Trading Supervisory Agency, Ministry of Communications and Information, and related associations. Coordination

7 Bank Indonesia Regulation No. 17/3/PBI/2015 and Bank Indonesia Circular Letter No. 17/11/DKSP on the Obligation to Use the Rupiah in the Territory of the Republic of Indonesia.

and dissemination was carried out in relation to strategic infrastructure projects, reference rates, transaction activities in the industrial sector, trade, financial services, oil and gas, transportation, and Hajj pilgrimages.

Payment System Consumer Protection

Bank Indonesia continues to enhance consumer protection in terms of payment systems. According to the provisions in Bank Indonesia Regulation No.16/1/PBI/2014 and Bank Indonesia Circular Letter No.16/16/DKSP, consumer protection is to be provided by Bank Indonesia in the form of education, consultation and facilitation for each individual who uses the services of a payment system, such as ATM card and credit card holders. The scope of consumer protection for those who use payment systems extends to fund withdrawal/transfer instruments, fund transfer activities, Card-Based Payment Instruments (CBPIs), electronic money, and the provision/depositing of rupiah currency.

As of December 2015, Bank Indonesia had received 1,870 customer complaints in the year. The majority of these were related to credit cards, with 1,361 complaints or 75.0% of the total. This was followed by complaints about ATM/Debit cards with 195 complaints or 10.7% of the total, and complaints about fund transfers with 188 complaints or 10.4% of the total (Chart 13.3). Customer complaints submitted to Bank Indonesia concerned payment system products used by parties other than the owner, the misuse of data - such as skimming, phishing or vishing - and credit card billing ethics.

In addition to receiving customer complaints, Bank Indonesia also received requests for information related to various payment system issues and products. Over 2015, Bank Indonesia received and followed up on 23,377 such requests for information. The majority of these requests for information were related to the obligation to use the rupiah in Indonesian territory, with 17,810 requests or 76.2% of the total (Chart 13.4). This was followed by requests for information related to the provision and depositing of money, with 3,067 requests (13.1%), and requests for information about fund transfers, with 595 requests (2.2%).

To raise public awareness, Bank Indonesia also held events to disseminate information on consumer protection in payment system services in several cities in Indonesia like Solo, Aceh, and Mataram. With respect to non-cash transactions, the GNNT Festival was held with the theme of "Love Non-cash, Love the Rupiah", in which 13 payment system service operating banks, 1 payment system innovation developing company, and 1 Non-Bank Foreign Exchange Business (KUPVA BB) participated. This event was held to encourage the public to use non-cash payment instruments and, at the same time, to encourage all parties to use the rupiah, as the currency of the Republic of Indonesia, for all daily transactions.

Bank Indonesia also improved consumer protection, in the operating of the SKNBI Generation II system, through its fee and time policy. This was done through provisions on time limits for the forwarding of funds to customers and maximum transaction fees that banks can impose on customers. For SKNBI, the time limits for the forwarding of funds are 2 hours after acceptance and 2 hours after the settlement of the funds in the bank account. Banks have to immediately forward a fund transfer instruction to

Chart 13.3. Portions of Complaint on Payment System

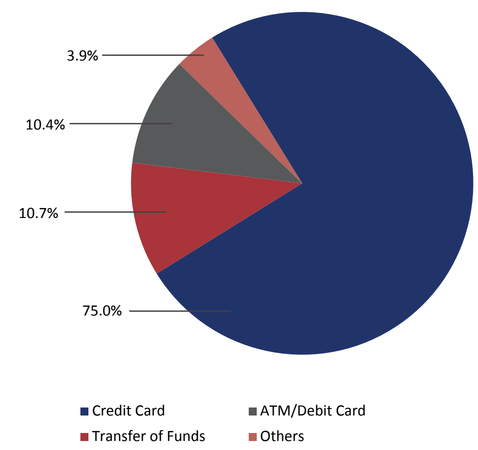
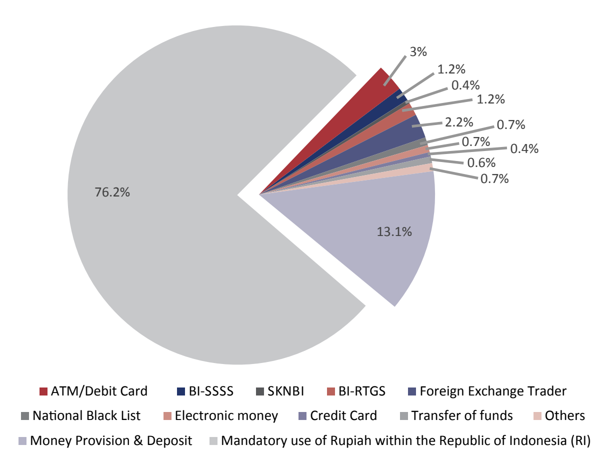


Chart 13.4. Request of Information Payment System



Bank Indonesia within 2 hours of the bank receiving the fund transfer instruction from a customer, and the bank receiving the funds is required to forward the fund transfer to the customer's account within 2 hours after the SKNBI fund settlement. Meanwhile, with relation to the setting of a maximum upper limit on SKNBI fund transfer fees which may be imposed by banks on customers, this amount was set at Rp5,000 per transaction, while the transaction fee charged by Bank Indonesia on participants was set at Rp750 per transaction. In addition to consumer protection aspects, the establishment of fund transfer also considered the cost recovery from the implementation and operation of the systems concerned.

As to the imposition of a fee per transaction in the BI-SSSS Generation II system, the highest fee that can be charged for a BI-RTGS system single credit transaction is Rp23,000 (Table 13.1). Furthermore, in order to enhance customer protection through transparency and to encourage efficiency on the part of Participants, Bank Indonesia also imposed a maximum fund transfer fee through the BI-RTGS system that banks can charge customers of Rp35,000. In addition, Bank Indonesia also required Banks that provide fund transfer services through the BI-RTGS system to inform all customers of the fees that apply to them, including the fees imposed by Bank Indonesia on Participants as well as the size of fees imposed by Banks on their customers.

Implementation of the Interconnection of Bank Indonesia's Government electronic Banking (BIG-eB)

One of the tasks of Bank Indonesia as the central bank is to provide specialized banking services to strategic partners, including the Government in this case the Ministry of Finance, the Deposit Insurance Corporation, and the Financial Services Authority. The services provided are primarily in the form of current account management as well as providing an electronic and online facility that can be used to obtain information and process financial transactions. This electronic facility, known as BIG-eB, can now be accessed by the Ministry of Finance.

To provide service excellence to its strategic partners, Bank Indonesia continued to e develop the BIG-eB after conducting a review of the business process and performance requirements of BIG-eB, both from the perspective of customers and Bank Indonesia. In general, the objectives of the development of BIG-eB are: (i) to support the process of collecting financial information more quickly and accurately by customers in the context of forecasting and preparing financial statements; (ii) to improve the efficiency and effectiveness of customer transaction settlements, particularly through the implementation of the Treasury Single Account (TSA) by the Ministry of Finance; (iii) to mitigate operational risks associated with the settlement of customer transactions and improve good governance in Bank Indonesia through the use of secure and reliable information technology; and (iv) to support the policies and credibility of Bank Indonesia, as well as strengthen cooperation and coordination among agencies.

In 2015, various developments to BIG-eB took place. These developments included: (i) additional types of transactions in order to accommodate the clearing transaction settlement process, as well as foreign exchange and future date transfers; (ii) additional types of reports to meet the various information needs of customers and application providers; and (iii) infrastructure capacity building in order to improve service performance. Moreover, consideration is currently being given to expanding BI's internet banking access so that it can be used by multiple users, rather than just by the Ministry of Finance.

Table 13.1. Transaction Tariff of BI RTGS Generation II System

Type of Fee	6.30 AM until 10.00 AM	10.00 AM until 14.00 PM	14.00 AM until CUT OFF
Single Credit Transaction	Rp9,000.-	Rp18,000.-	Rp23,000.-
Multiple Credit Transactions	Rp35,000.-	Rp35,000.-	Rp50,000.-
Single credit inter-Participants Transactions for customers in terms of TSA	Rp0.-	Rp0.-	Rp0.-

The Use of Central Bank Money (CeBM)

The use of Central Bank Money (CeBM) constitutes one of the recommendations in the Principles for Financial Market Infrastructures (PFMIs) issued by the Bank for International Settlement (BIS) and the International Organization of Securities Commissions (IOSCO). The use of CeBM is aimed to mitigate the possibility of credit risk and liquidity risk arising in the execution of fund settlements on securities transactions. Credit risk arises because of the possibility of default by payment banks on their obligations, while liquidity risk arises if, after the settlement of payment obligations, the participant or operator is unable to change the assets from the payment bank into other liquid assets.

In line with this situation, Bank Indonesia implemented the use of CeBM for the settlement of securities transactions in the capital market on June 18, 2015. The use of CeBM is allocated for Government Securities (SBN) and non-SBN transactions initiated by custodian banks (Table 13.2). In this regard, Bank Indonesia together with the Financial Services Authority (OJK), Indonesian Central Securities Depository (KSEI), and capital market participants in the custodian bank group have implemented the first phase of CeBM use. In the first phase, all custodian banks are required to perform fund settlements with KSEI through the BI-RTGS system for all capital market transactions in rupiah currency. The inauguration of the first phase of CeBM use, which took place on June 29, 2015, represents a new chapter in Indonesia's financial system. The use of the BI-RTGS system for capital market transaction fund settlements between KSEI participants and KSEI itself (as the Central Securities Depository (CSD) operator for stocks, corporate bonds and other securities issued by the private business sector) also represents a fulfilment of one of the international standards required in adherence to the principles for financial market infrastructures, known as PFMIs.

With the use of CeBM, fund depositing and withdrawal activities in the framework of securities transaction settlements in the capital market by custodian banks, which to date have only been performed through five payment banks, in the future will be performed by the transfer of funds between the checking account of banks and the checking account of KSEI in the BI-RTGS system. Another advantage of this mechanism is the creation of competitive neutrality in that every bank can perform capital market transaction settlements and are not dependent on a specific payment bank. In addition, the use of CeBM will improve liquidity management efficiency for each bank because there is no need to have an account at another institution for the purpose of capital market transaction settlements.

Strengthening of Legal Aspects in Payment System Operations by BI

Provisions of BI-RTGS and BI-SSSS Generation II

Certain legal aspects needed to be strengthened to support the development and operation of the BI-ETP, BI-RTGS, and BI-SSSS Generation II systems. As a legal basis for the operation of the three systems and in the context of adjustments to provisions on the size of transaction fees, price caps, and the transparency of information in the use of the BI-RTGS and BI-SSSS Generation II systems, Bank Indonesia issued Bank Indonesia Regulation No. 17/18/PBI/2015 on Transaction Operations, Securities Administration, and Immediate Fund Settlements. This regulation was also supported by Bank Indonesia Circular Letter No. 17/30/DPSP regarding the Execution of Immediate Fund Settlements through the Bank Indonesia - Real Time Gross Settlement System. In addition, to accommodate the development of monetary operations

Table 13.2. Stages of Development of Use CEBM for Settlement of Securities Transactions in Capital Market

C-BEST Participant	Securities in USD		Securities in IDR	
	SBN	Non-SBN	SBN	Non-SBN
Hybrid 1 → implemented on June 18, 2015				
Custodian Bank	x	x	√	√
Securities Company	×	×	×	×
Hybrid 2 → implemented in the first quarter of 2016				
Custodian Bank	×	×	√	√
Securities Company	×	×	√	×
Hybrid 3 → Further study				
Custodian Bank	×	×	√	√
Securities Company	×	×	√	√
Full CeBM → Further study				
Custodian Bank	√	√	√	√
Securities Company	√	√	√	√

Hybrid: Combines the use of CeBM and CoBM to settle the funding of securities transactions based on denominated securities, types of securities and participants with the implementation of the BI-RTGS.

Full CeBM: The settlement of all securities transactions in foreign currency and IDR in the capital markets using CeBM.

transactions and transactions in financial markets, as well as the use of infrastructure under development for transactions in financial markets, Bank Indonesia also updated its provisions regarding the auction and administration of Government Securities by issuing Bank Indonesia Regulation No. 17/19/PBI/2015 regarding the Second Amendment to Bank Indonesia Regulation No. 10/13/PBI/2008 concerning the Auction and Administration of Government Securities.

Provisions of SKNBI Generation II

To provide a legal umbrella to the operation of fund transfers and clearing scheduled through the implementation of SKNBI Generation II, Bank Indonesia issued Bank Indonesia Regulation No. 17/9/PBI/2015 on the Operation of Fund Transfers and Clearing Scheduled by Bank Indonesia. The main points of improvement in the administration of SKNBI Generation II include: (i) the expansion of membership access so as not to be limited to Commercial Banks; (ii) the addition of services for routine transactions; (iii) the centralization of check clearing Services; and (iv) the enhancement of protection for SKNBI participating customers. In the initial stage of the implementation of SKNBI Generation II, which took effect on June 5, 2015, the operating of SKNBI was limited to fund transfer services and check clearing services, while participation was limited to banks. For the next stage, SKNBI services included Regular Payment Services and Regular Billing Services, while membership was extended to fund transfer operators as well as banks.

13.2. CURRENCY MANAGEMENT PERFORMANCE

Bank Indonesia's mission when it comes to currency management is to meet the rupiah currency needs of society by providing currency in sufficient quantities, in appropriate denominations, in a timely manner and in a condition fit for circulation. In order to execute this mission as well as to fulfil the mandate of Law No. 7 of 2011 on the Currency, Bank Indonesia carries out six stages of rupiah currency management. These stages are the planning, printing, issuing, circulating, revoking and withdrawing, as well as destroying. Bank Indonesia is the institution authorized to make issuance, circulation, as well as the revocation and withdrawal. Meanwhile, the planning, printing, and destroying are carried out by Bank Indonesia in coordination with the Government. In addition, developments in macroeconomic conditions and financial markets also played an important role in Bank Indonesia's implementation of currency management policies during 2015.

Broadly speaking, Bank Indonesia pursued five rupiah currency management policies in 2015. Firstly, it sought to maintain the adequacy of its cash position. Second, it sought to improve the quality of rupiah currency in society (clean money policy). Third, it sought to expand its currency and cash services distribution network. Fourth, it sought to enhance its communication with the public regarding the Characteristics of Authentic Rupiah Currency. And fifth, it sought to prevent, counter and combat the production and distribution of counterfeit rupiah currency.

Maintaining the Sufficiency of Bank Indonesia’s Cash Position

In order to meet the demand for currency withdrawals from banks in 2015, Bank Indonesia took measures to maintain the sufficiency of its cash position at all Bank Indonesia offices, both head offices and regional. As in 2014, Bank Indonesia set a cash position adequacy level using the National Iron Stock (ISN) amount indicator of 20% of projected Currency in Circulation (UYD) of the current year and Minimum Cash to the value of 1.5 months of bank withdrawals (outflow).[8] Bank Indonesia’s cash position ratio stood at an average of 5.1 months of outflow over the course of 2015, up from the previous year’s figure of an average of 3.1 months of outflow.

Bank Indonesia's success in maintaining the sufficiency of its cash position at all its offices was achieved through the pursuance of several policies. On the supply side, Perum Peruri (The Indonesian Government Security Printing and Minting Corp) printed an amount of currency in accordance with the amount set by Bank Indonesia. Similarly, in terms of the timing of currency deliveries, Perum Peruri managed to align its printing output with the needs of Bank Indonesia, which increased especially before religious holiday periods. Perum Peruri undertook to meet Bank Indonesia's need for printed currency by modernizing its currency printing equipment, adding a banknote production line, and optimizing its working times. In addition, the smooth distribution of money

8 Minimum cash refers to the minimum supply of cash that must be maintained at all offices of Bank Indonesia, assuming that no cash deposits are made by banks in Bank Indonesia. Factors that need to be taken into account in setting the minimum cash level include distribution and transportation as well as the supply of Perfectly Printed Money (HCS) by Perum Peruri (The Indonesian Government Security Printing and Minting Corp).

between Bank Indonesia's offices was also an important factor in maintaining the sufficiency of its cash position. In this regard, Bank Indonesia continued to improve its cooperation with business entities that operate modes of transportation, such as *PT Kereta Api Indonesia* (National Railway Company), *PT Pelayaran Nasional Indonesia* (National Shipping Company), and other private entities.

On the demand side, since 2011 Bank Indonesia has applied a policy whereby currency withdrawals and/or deposits by banks through Bank Indonesia are to be conducted after banks have engaged in Interbank Cash Exchange (TUKAB).[9] Such transactions are carried out between one bank and another as well as with the mediation of Bank Indonesia through the dropshot mechanism.[10] This policy has had a positive impact on banks in accelerating the availability of rupiah currency in the right denominations. As for Bank Indonesia, the policy has resulted in increased currency management efficiency. Ultimately, Bank Indonesia has been able to manage the growth in withdrawals and deposits of rupiah currency by banks, regardless of economic or cyclical factors (seasonal factors).

During 2015, Bank Indonesia distributed rupiah currency to all its offices to the value of Rp240.4 trillion, an increase of 44.4% on the previous year's figure of Rp166.5 trillion. The largest share of this money was distributed to the Head Office of Bank Indonesia to ensure the availability of cash there, given the large volume of withdrawals by banks, the majority of which are headquartered in Jakarta. As for the regions, the largest share of money distributed to ensure the availability of cash was in the Bank Indonesia offices of North Sumatra Province, South Sumatra Province, and East Java Province, each at around Rp20 trillion.

The adequate availability of rupiah currency was also reflected in the fulfilment of the withdrawal of currency during the period of Ramadan/ Eid al-Fitr and Christmas/ end of year holidays in 2015. As much as Rp140.0 trillion in currency was withdrawn in the Ramadan/Eid al-Fitr period, or 111.8% of cash needs based on the projection of banks. This high realization stemmed mainly from increases in the realization of withdrawals of Rp100,000 and Rp50,000 banknotes. Similarly, in the 2015 Christmas and end of year holiday period, actual withdrawals of currency reached Rp85.6 trillion, or 106.0% of cash needs based on the banks' projection.

Improving the Quality of Currency in Circulation in Society (Clean Money Policy)

The availability of cash at all offices of Bank Indonesia in sufficient quantities served as the launchpad for Bank Indonesia to implement policies to improve the quality of currency in circulation in the community. One of these policies was to improve the soil level of money deposited by banks in Bank Indonesia and processed by Bank Indonesia. This effort to improve soil levels meant that that there was a surge in the amount of currency unfit for circulation that had to be destroyed by Bank Indonesia. To anticipate these conditions, Bank Indonesia started to modernize cash-related equipment in 2015, thereby enhancing the capacity for processing rupiah currency.[11] During 2015, Rp160.25 trillion worth of money not fit for circulation was destroyed, up 43.6% over the previous year. The effect of this was that a greater proportion of cash withdrawals consisted of good quality currency (perfectly printed money from Perum Peruri).

Efforts to enhance the quality of currency in circulation in society were also undertaken through an increase in the amount of money exchanged and frequency of money exchanges by means of mobile cash units.[12] These activities were conducted by Bank Indonesia in cooperation with various other parties such as ministries and related agencies, as well as banks. In addition, the expansion of collaborations with banks in opening Cash Custodians in areas previously unreached by Bank Indonesia's cash services also served as a factor driving the improved quality of currency in society.[13] Results of a survey conducted in 2015 on the quality of currency in circulation in several towns in border areas and remote regions

9 TUKAB is the activity that covers demand, supply and exchange of fit notes and coins (ULE) providing the needs of nominal amount and/or denomination in accordance with the Bank Indonesia regulation

10 Dropshots is a payment policy of currency fit in circulation (ULE) from bank deposits to the same bank (deposit bank) or to other bank. Bank Indonesia does not make detailed circulation and sorting on ULE deposits from the bank. In this particular activities, payments made by Bank Indonesia to the bank are made in one transparent plastic packaging (10 bundles, each bundle consist of 10 packs) which remains intact, sealed and with the label of paying bank

11 The modernization of cash-related equipment consisted of the replacement and addition of cash-related equipment in the form of 26 Banknote Sorting Machines with Shredder (MSUK-R) and 14 Banknote Shredding Machines (MRUK).

12 Mobile Cash is a cash exchange service provided by cash work units at the Head Office and Regional Representative Offices (KPwDN-BI) to the public, banks and other parties using specific means of transportation.

13 Cash Custodian is the activity in entrusted cash owned by Bank Indonesia to a bank appointed with agreement to fulfill banks' cash requirement in order to meet demand for cash of the people in remote areas.

showed a currency quality index in these towns of 6.8, higher than the initially predicted figure of 4.

Expansion of Currency Distribution Network and Cash Services

One of the measures announced in the Architecture of Bank Indonesia's Strategic Function (AFSBI) 2014-2024 in the field of rupiah currency management was the reform of currency distribution network and cash services. This was based on considerations as to how best to expedite Bank Indonesia's mission of meeting currency needs in sufficient quantities in all parts of Indonesia, with the appropriate denominations, in a timely manner, of good quality and in a cost efficient way. Reforms would be made on a multiyear basis with the goal of currency and cash services networks covering the entire territory of Indonesia by 2019. In broad terms, these measures included expanding the role of Bank Indonesia as mandated by the Currency Law and enhancing forms of cooperation with banks and business entities in the area of currency processing services. The results of this action aimed at the reform of currency and cash services distribution networks included infrastructure development (capacity building), as well as improving currency management and business models.

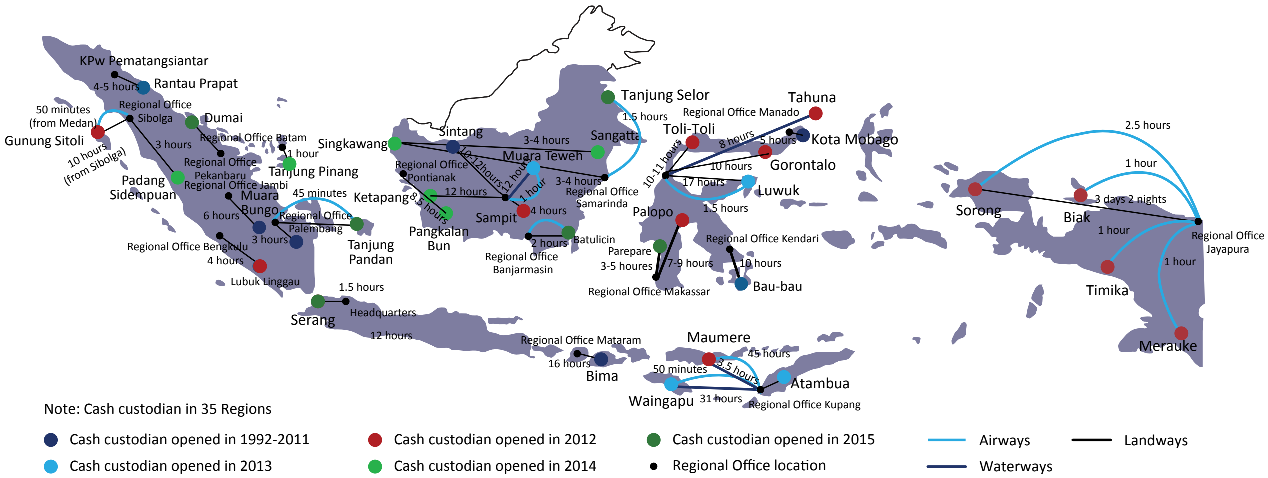
Currency management infrastructure development undertaken over the course of 2015 saw an expansion in the number of Bank Indonesia offices and the Cash Custodians (Table 13.3). The first policy pursued in 2015 was the October opening of a Bank Indonesia office in the province of West Sulawesi, one of the functions of which is currency management. The second policy in the same year was the addition of 6 new Cash Custodians in Tanjung Pandan (June), Serang (August), Batu Licin (August), Dumai (November), Tanjung Selor (December), and Pare-Pare (December), as well as the closing of 1 Cash Custodian in the West Sulawesi town of Mamuju (September). Thus, by the end of 2015, there were a total of 35 Cash Custodians in Indonesia, many of which are located in Sumatra and eastern Indonesia (Picture 13.3). This represented an additional 5 Cash Custodians compared to the 2014 total. These thirty-five Cash Custodians in Indonesia were managed by 14 commercial banks which extending to 368 commercial bank branches. This figure represented an increase over the previous year, when there were 12 managing commercial banks extending to 267 commercial bank branches.

To improve governance and compliance with the terms of operation of Cash Custodians, Bank Indonesia periodically conducted monitoring, both off-site - through its requirements that relevant reports be submitted - as well as on-site - through direct inspections of Cash Custodian managing banks. The purpose of this monitoring was to ensure that the way Cash Custodians were being operated was in compliance with cooperation agreements entered into by Bank Indonesia and the Managing Banks. In addition, the monitoring was also aimed at evaluating the performance of the Managing Banks and ensuring that

Table 13.3. Managing Bank and Office Member of Cash Custodian

No	Managing Bank	Number of Cash Custodian	Location and Number of Bank
1	Bank Mandiri	9	Rantau Prapat (14 bank anggota), Toli-Toli (4), Tahuna (4), Gorontalo (14), Sorong (13), Timika (11), Biak (5), Tanjung Pinang (13), Tanjung Pandan (10)
2	Bank Negara Indonesia	5	Gunung Sitoli (5), Luwuk (8), Muaro Bungo (19), Bau-Bau (7), and Padang Sidempuan (12)
3	Bank Rakyat Indonesia	4	Lubuk Linggau (12), Sampit (7), Waingapu (3), Dumai (15)
4	BPD Kalimantan Barat	3	Sintang (14), Ketapang (12), Singkawang (10)
5	BPD Kalimantan Tengah	2	Muara Teweh (6) and Pangkalan Bun (12)
6	BPD Kalimantan Timur	2	Sangatta (11), Tanjung Selor (3)
7	BPD Nusa Tenggara Timur	2	Maumere (4) and Atambua (4)
8	BPD Sulawesi Selatan & Sulawesi Barat	2	Palopo (13), Pare-Pare (7)
9	BPD Sulawesi Utara	1	Kotamobagu (6)
10	BPD Sumsel Babel	1	Prabumulih (22)
11	BPD Nusa Tenggara Barat	1	Bima (6)
12	BPD Papua & Papua Barat	1	Merauke (8)
13	BPD Jabar & Banten	1	Serang (40)
14	BPD Kalimantan Selatan	1	Batulicin (14)
	Total: 14 Banks	35 bank offices	368 bank office member

Picture 13.3. Map of Cash Custodian Distribution



the physical amount of currency kept in the Managing Banks was consistent with the amounts reported to Bank Indonesia. In general, the results of inspections showed that Cash Custodians were being operated properly and in accordance with the cooperation agreements with Bank Indonesia. Among the aspects that could be improved are rupiah currency exchange services to the public, the storage and separation of currency being held as Custodial Cash from cash actually belonging to the managing bank in the cash vault of the managing bank, and the submission of periodic reports to Bank Indonesia.

Enhancing Public Communication concerning the Characteristics of Authentic Rupiah Currency

To raise public awareness regarding the characteristics of authentic rupiah currency, Bank Indonesia organized public communication activities on an ongoing basis through disseminating information to a variety of different groups in society. These groups included cash handlers (such as bank tellers and minimart cashiers), academics/ students, law enforcement officers and the general public. These dissemination activities were done face to face, by participating in development exhibitions in the regions, as well as through folk/traditional art. In addition, material on the characteristics of authentic rupiah currency now forms part of the syllabus for Central Bank studies at the secondary education and college level nationwide.

In 2015, public communication activities were expanded with the broadcast of a Public Service Announcement (PSA) on the Characteristics of Authentic Rupiah (*3D "Dilihat – Diraba – Diterawang"*), or 'Look, Touch, Examine' on several national TV channels and social media. The public is also now able to download an educational video about the Characteristics of Authentic Rupiah which includes a tutorial on the general features of the rupiah and how to verify its authenticity. Bank Indonesia also set up a rupiah mini-site on the Bank Indonesia website with information about the characteristics of the rupiah, preventing and combating the crime of rupiah counterfeiting, educational activities and games for children, as well as a variety of other interactive games about the rupiah. This material can be downloaded in the form of leaflets and booklets corresponding to the particular user group, which includes the general public, banks and cash handlers, as well as law enforcement officers.

Preventing and Combating the Distribution of Counterfeit Rupiah Currency

To prevent and combat the distribution of counterfeit rupiah currency, Bank Indonesia supported the Indonesian National Police in its task of fighting against the circulation of counterfeit currency. This support took the form of the provision of an analysis laboratory for rupiah currency suspected of being fake as well as access to the Bank Indonesia Counterfeit Analysis Center (BI-CAC) information system. The laboratory is used to examine evidence, in the form of suspected counterfeit rupiah, uncovered by the Indonesian National Police, and also to examine any rupiah discovered of dubious authenticity upon request from a bank to clarify its status. A laboratory analysis can identify the signs of counterfeit rupiah, from the type of paper and ink used to the printing technique used.

Meanwhile, the BI-CAC information system is used as the central database for counterfeit rupiah in support of the duties of the Police in disclosing counterfeit currency production and distribution networks. The results of laboratory and BI-CAC examinations also serve as important input for Bank Indonesia when it comes to improve the quality of security features of rupiah currency to be issued in the future. The presence of BI-CAC also supports Bank Indonesia's mandate, based on the Currency Law, of having the authority to certify the authenticity of rupiah. In line with this mandate, Bank Indonesia frequently provides human resources to give expert testimony in court cases of rupiah counterfeiting.

Law enforcement efforts against those accused of counterfeiting rupiah currency were consistently undertaken by Bank Indonesia in coordination with the relevant law enforcement agencies (National Police and Attorney General). These efforts sought to prosecute alleged perpetrators of counterfeiting to the maximum extent, so as to serve as a deterrent to potential counterfeiters as well as any other people tempted to get involved in the creation and/or distribution of counterfeit currency. Several criminal cases of counterfeiting were tried in 2014-2015, with heavy sentences handed down by Courts, including cases in Jember, East Nusa Tenggara, and Merauke.

Box 13.1 Best Practices in Currency Distribution and Cash Services

In performing its duties in the field of currency management, in particular the distribution of currency and cash services, Bank Indonesia faced with a number of challenges given the geography of Indonesia as a vast archipelago. One of the biggest challenges related to the distribution of money is the limited availability of regular modes and lines of transport which results in a low level of inter-regional connectivity. This is exacerbated by frequently changing weather and climatic conditions. Meanwhile, one of the challenges related to the provision of cash services is that there are still many remote areas, border regions and outlying islands as yet unreached by Bank Indonesia's cash services. These challenges means that the circulation of currency fit for circulation is uneven in Indonesia which, in turn, adversely affects the quality of currency circulating in these regions, much of it having a high soil level.

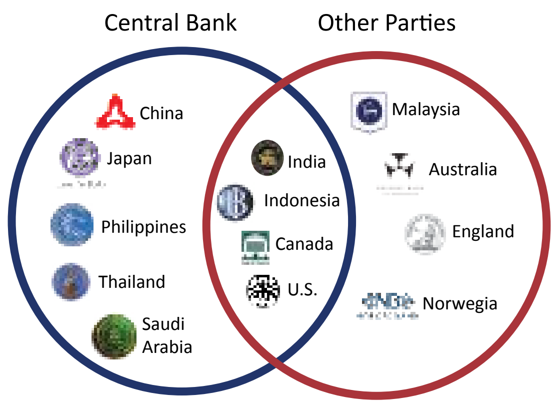
To address these challenges, Bank Indonesia has consistently taken measures to improve its currency management business model, in particular with regard to the distribution of currency and cash services. These measures, among others, include the following: First, Bank Indonesia has cooperated with commercial banks since 1993 to open Cash Custodians in areas with developing economies. The prevailing business model is for Bank Indonesia to deliver money to banks managing Cash Custodians. The managing banks and member banks, meanwhile, jointly incur the costs of operating the Cash Custodian. Second, Bank Indonesia has cooperated with the Small Denomination Currency Exchange Company (PPUPK) and other relevant parties from 2005 to 2008. The business model in effect was for the PPUPK and other parties to obtain a fee from Bank Indonesia whereby the public did not incur the cost of exchanging small denominations of currency. Third, Bank Indonesia transferred the obligation for sorting currency to commercial banks, with the implementation of an updated policy on deposits and withdrawals by commercial banks in 2007.[1] With this updated policy, the previous policy, whereby commercial banks had been able to deposit both currency fit for circulation (ULE) and currency unfit for circulation (UTLE) in Bank Indonesia, became invalid.

The updated policy stipulated that banks must sort rupiah currency into ULE and UTLE. Furthermore, ULE must be prioritized for exchanging with other banks through the Interbank Cash Exchange mechanism (TUKAB). If after the TUKAB mechanism has been used, there remains an excess of ULE, then both the excess ULE and any UTLE can be deposited in Bank Indonesia.

In improving its currency management business model, Bank Indonesia conducted a study of international best practices of currency management as performed by several other central banks. The central banks which formed the focus of the study were from developing countries with similar economic conditions and geographical characteristics to Indonesia. In addition, currency management business models of central banks in developed countries have also been used as a reference for Bank Indonesia in improving its own currency management business model. Best practices in currency management in several central banks are focused on two business models, the currency distribution business model and the cash services business model.

The currency distribution business model in several central banks, is broadly divided into two parts, namely distribution networks and delivery of cash. The currency distribution network model adopted by the central banks generally consists of three forms. First, cash is distributed entirely by the central bank through a network of branches in the territory of the country concerned. Central banks that distribute currency autonomously include those in

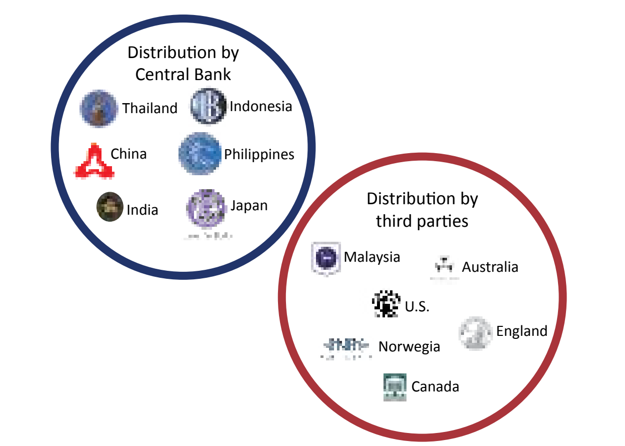
Diagram 1. Distribution Network



Source: Various Central Banks

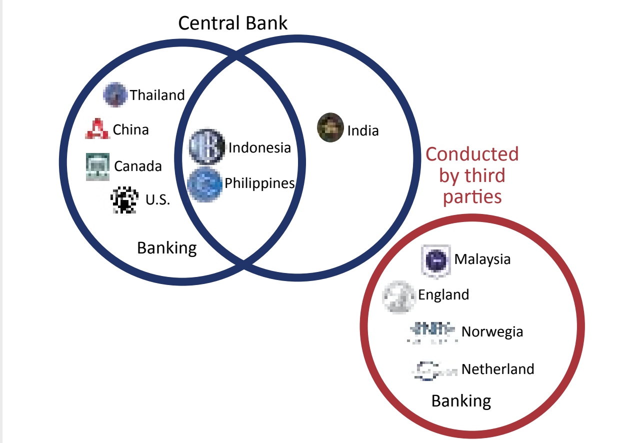
1 Bank Indonesia Circular Letter Number 9/37/DPU, dated December 27, 2007 on Deposits and Withdrawals of Rupiah Currency by Commercial Banks in/from Bank Indonesia, which was repealed and replaced with Bank Indonesia Circular Letter Number 13/9/DPU, dated April 5, 2011 on Deposits and Withdrawals of Rupiah Currency by Commercial Banks in/from Bank Indonesia.

Diagram 2. Implementation of Remittances



Source: Various Central Banks

Diagram 3. Cash Service: Banking-Retail



Source: Various Central Banks

the Philippines, China, Saudi Arabia, Thailand, and Japan. Second, cash is distributed by utilizing other parties, examples of which include Malaysia which uses MEPS (Malaysian Electronic Payment System), Norway which uses Nokas (Norsk Kontantservice), as well as Australia and the UK which utilize cash in transit/CIT companies. Third, is a combination of using the central bank office network and other parties. Central banks which apply this model include India with a Currency Chest and Small Coin Deposits, the United States with a Cash Deposit, Strategic Inventory and Custodial Inventory, and Canada with a Regional Deposit Center. This third model is also applied by Bank Indonesia as exemplified by the role played by Cash Custodians. The application of this business model in Indonesia is due to the fact that Bank Indonesia's office network is unable to reach all of Indonesia's territory directly, owing in part to the limited availability of regular modes and lines of transport to various parts of the country.

The second aspect of the currency distribution business model is the delivery of currency. Depending on the structure of the currency distribution network, the delivery of currency is categorized into one of two forms, either that carried out by the central bank’s internal office network or that carried out by other institutions/facilities in cooperation with the central bank.[2] In other words, it is the structure of the distribution network that affects and determines the way currency is delivered to a particular location. Examples of central banks that deliver currency autonomously include the Philippines, Thailand, Japan, India, China, and Indonesia. In contrast, central banks that appoint other institutions/facilities to deliver currency include the U.S. (*CiT*), the U.K. (*CiT*), Malaysia (MEPS), Canada (*CiT*), Norway (*CiT*), and Australia (*CiT*).

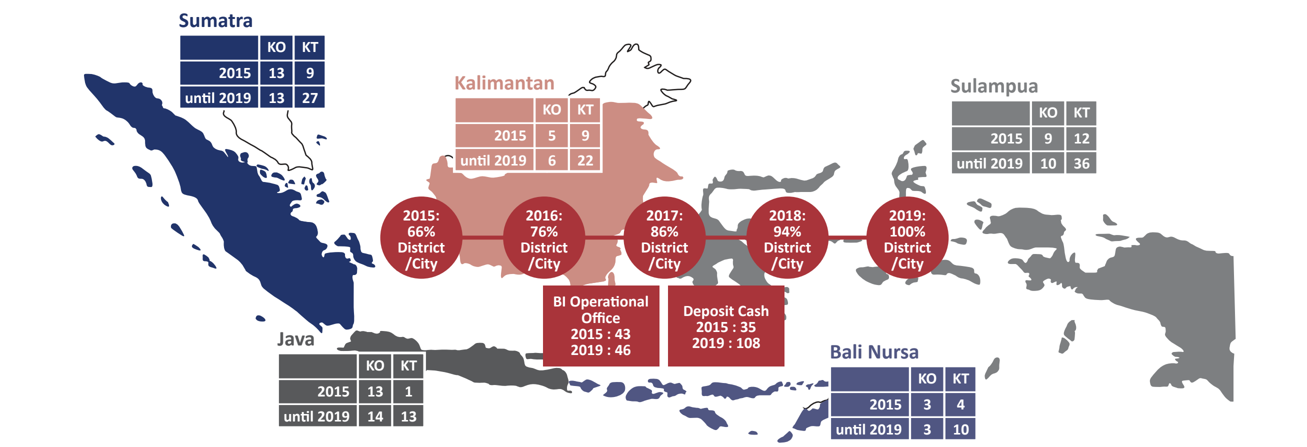
Bank Indonesia currently uses an autonomous currency delivery model in consideration of the fact that it is able to exercise complete supervision of the process in this way, and that the frequency and amount of its currency deliveries can be more flexible in line with the prevailing dynamics of economic developments. However, this results in less efficient distribution costs and requires contracts or cooperation with transport service providers.

Meanwhile, the cash services business model, in broad terms, also consists of two forms, namely cash services operated by central banks themselves and the delegation by central banks of all cash services to another party. Cash services operated by central banks are further divided into two types, cash services only provided to banks (for example in Thailand, China, Canada, and the U.S.), and cash services provided to banks and the retail sector (for example in the Philippines and Indonesia). Meanwhile, central banks that delegate all cash services to another party but only to banks include Norway, Malaysia, the U.K., and the Netherlands.

The main factor underlying the use of this model is that Bank Indonesia can exercise direct supervision of its cash service activities. However, the use of this

2 The Central Bank internal office network mechanism applied by Bank Indonesia is by means of Cash Depot Offices (Kantor Depo Kas/ KDK). In this case, Bank Indonesia's Head Office transfers money directly (remittances) to 11 KDK and 4 Regional Representative Offices (KPwDN-BI). Subsequently, these 11 KDK transfer the money to other KPwDN-BI. The modes of transport used for these activities are trucks, trains, passenger ships, cargo ships, and aircraft.

Picture 1. **Money Distribution Network Coverage Plan - Bank Indonesia Year 2015-2019**



Bank Indonesia Operations Office (KO) performing the function of rupiah money management
KT: Commercial Bank as the organizer of Cash Custodian

model requires a lot of resources and infrastructure to reach all parts of Indonesia. Studies of best practices in currency management in various countries have served as a consideration for Bank Indonesia in improving its currency management activities, particularly with relation to currency and cash service distribution networks. However, the fact that Indonesia is a vast archipelago with continually growing regional economies also needs to be taken into consideration. With respect to this, a number of measures have been prepared for developing the distribution of currency and cash services. First, the banking industry has been encouraged to play a greater role in expanding the coverage and operational efficiency of currency distribution. Second, cash-related infrastructure has been strengthened to increase the effectiveness of distribution throughout Indonesia. Third, the relationship pattern with the banking industry in terms of cash-related activities has been improved.

Reforms to the currency distribution networks and cash service began with a pilot project in 2015 involving four activities. The first activity was the provision of Mobile Cash on a wholesale basis by Cash Custodian managing banks in Merauke, Waingapu and Prabumulih, as well as the provision of a Mobile Cash unit by a Cash in Transit (CiT) company in the province of Bali.[3] The second activity was the dissemination of improvements to the Cash Custodian business model, including the possibility of granting financial schemes to Cash Custodian managing banks. Aspects underlying the improvements to this business model included enhancing cash area infrastructure and security standards, promoting the role of money exchange service counters in Cash Custodians, encouraging the absorption of currency unfit for circulation, and improving the quality of money sorting. The third activity was the distribution of currency from Bank Indonesia offices to Cash Custodians and vice-versa (dropping/fetching), as performed by Cash Custodian managing banks in Merauke and Prabumulih. The fourth activity was the distribution of currency between Bank Indonesia Cash Offices, specifically from the Lampung Regional Representative Office (KPw) to the Bengkulu Regional Representative Office (KPw) in the context of optimizing distribution lines and encouraging the formation of a Cash Depot Office (KDK) in KPw Lampung.

Through these reforms to currency distribution network and cash service being pursued by Bank Indonesia, it is expected that by 2019 Bank Indonesia's cash service coverage will reach all areas of Indonesia.[4] Such an achievement cannot be viewed in isolation, and is thanks in part to the increasing role of industry, both banks and other business entities, in operating currency processing services. In turn, the increased role of industry is also

3 Mobile Cash on a wholesale basis is a currency exchange service intended for other parties besides the public, such as Commercial Banks, Rural Banks, retailers and so forth, whose coverage extends to remote and outlying areas of the Republic of Indonesia.

4 The coverage of currency and cash service distribution networks is calculated using a method based on the number of towns and regencies served by Bank Indonesia offices and Cash Custodians, as well as travel time and available modes of transportation. For example, the coverage of the Aceh Province Regional Representative Office extends to 4 towns/regencies, namely Banda Aceh, Aceh Besar, Sabang Town, and Aceh Jaya.

stimulated by improvements to currency management business models, to which end Bank Indonesia will continue to issue regulations on the execution of currency processing by banks as well as other currency processing operating service companies. This is aimed at standardizing the processing of currency by all parties in order to improve protection of and service to the public. In addition, the possibility of granting financial schemes to industries that perform currency distribution and provide cash services is being examined (Picture 1).

In response to the economic challenges that surfaced in 2015, Bank Indonesia strengthened policy coordination with the Government and other relevant authorities. Such coordination has proven to maintain macroeconomic stability despite extensive uncertainty, while simultaneously creating economic growth momentum.

Chapter 14

Policy Coordination

The complexity and interconnectedness of economic dynamics throughout 2015 compelled Bank Indonesia to strengthen its coordination of policies with both central and local Government and other appropriate regulatory authorities. Bank Indonesia also strengthened its coordination with other central banks and multinational agencies through its participation in international cooperation forums. This policy coordination was carried out within the corridors of maintaining macroeconomic stability, fostering the momentum for growth, and expediting structural reforms.

Despite continued uncertainties with the global economy, Bank Indonesia has maintained stable macroeconomic performance throughout 2015 through strengthening its policy coordination with the Indonesian government and other related authorities. The macroeconomic stability was reflected in the inflation rate remaining within its target range. Volatilities on the Indonesian rupiah exchange rate, due to uncertainties with the Federal Reserve normalizing its policies, the devaluation of the Chinese currency by the People's Bank of China (PBoC), and the limited supply of foreign currencies, was eventually moderated as well, as the Indonesian government issued its series of economic policy packages. Nevertheless, efforts to prevent and manage risks to maintain stability in the financial systems continue to be carried out, due to the fact that potential risks remain within the global financial markets and from the divergent monetary policies between countries.

The coordination between Bank Indonesia and the Indonesian government was carried out across various policy sectors. Apart from maintaining macroeconomic stability, the policy coordination was also focused on fostering the momentum for growth through the coordination of macroprudential policies, particularly those aimed at improving the performance of such real sectors as trade, construction, and manufacturing. Bank Indonesia participated in the Indonesian government's programs of facilitating bank credits, developing micro, small, and medium enterprises (MSMEs), developing the maritime and fisheries sector, and encouraging entrepreneurships. The coordination was carried out in line with a series of Indonesian government's economic policy packages. Furthermore, Bank Indonesia also supported efforts of keeping the momentum of growth by coordinating a secure, reliable and efficient payment system, and money supply management system for the economy.

The final focus of the policy coordination was implementing structural reforms, particularly in deepening the financial market, facilitating the development of the real sector, and further developing the country's payment system and currency management system. Deepening the financial market is expected to improve the economic structure's sustainability through the financial markets, being carried out prudently to maintain stability of the financial system. Developing the real sector was focused on Indonesia's maritime, food security, energy infrastructure, manufacturing, and tourism sectors. Meanwhile, further developing the payment system and currency management system was focused on expanding services to all reaches of Indonesia, which was carried out together with the Ministry of Transportation and the Indonesian National Armed Forces.

14.1. POLICY COORDINATION TO MAINTAIN MACROECONOMIC STABILITY

Bank Indonesia managed to maintain macroeconomic stability through the coordination of its policies regarding inflation, currency exchange rates, and the financial system, with other authorities both within Indonesia and abroad.

Coordination of Policies on Inflation

The inflation rate of consumer prices at 3.35% for 2015, which is within its target range, was achieved through the concerted efforts and policies between Bank Indonesia and the Indonesian government. Inflation of administered prices and volatile food prices, were in particular the focus of Inflation Monitoring and Controlling Team (TPI) and Regional Inflation Monitoring and Controlling Team (TPID) throughout 2015. This was in line with the Indonesian government's energy sector reform, which included the price administration of fuel, electricity, and gas (LPG). Meanwhile, regarding food prices, efforts were carried out to secure supply, improve distribution, further develop market information, and manage market expectations.

The support and contribution of local administrations in managing inflation in the regions further improved, as can be seen in the increasing number of TPID established and programs implemented to secure supply, improve distribution, and effectively manage price information. By the end of 2015, 442 TPID had been established, comprising 34 provincial TPID and 408 regency/city TPID throughout Indonesia. This is an increase from a total of 396 TPID in 2014. With the increasing number of TPID, policy coordination becomes even more crucial, which entitles the TPID National Working Group (Pokjanas TPID) a more significant role in administering inflation management policies between the central government and the regions.

Meanwhile, the coordination of policies regarding inflation between Bank Indonesia, the Indonesian government and local administrations, is conducted through the TPID National Coordinating Meeting (Rakornas TPID), the highest coordination forum outlining inflation management strategies to meet the national inflation target. The main focus of the 2015 Rakornas TPID was optimizing the role of local administrations in maintaining market price stability through expediting infrastructure development and improving market regulations in the regions. This focus is based on the Indonesian government's intention to increase spending on infrastructure that supports its programs of achieving food security and improving logistics and the distribution of goods throughout the country, which requires the participation of the regions. Indeed, the 2015 Rakornas TPID, the sixth of its kind and the first to be convened directly by the President, stressed the importance of managing inflation through active participation and synergy of programs.

As a follow-up of the 2015 Rakornas TPID, an Inflation Control Roadmap has been formulated, outlining national strategies regarding inflation through 2018. The Inflation Control Roadmap also outlines the structural problems relating to inflation management that needs to be addressed, which includes: (i) the local economy's limited capacity to expand, (ii) an overly-dependence on exports of natural resources and imports of raw material, (iii) food production prone to market supply disruptions, (iv) inefficient market structures, (v) an overly-dependence on fuel and gas imports for energy supply, (vi) poor inter-regional connectivity, and (vii) uncertainties in the global economy affecting currency stability. With regards to all these issues, it is therefore clear that inflation management requires the proper planning, coordination, and participation of all stakeholders, be it the central government or the regions.

The Inflation Control Roadmap provides a single reference for policy coordination, while taking into account regional characteristics, and also includes procedures for the identification of issues, medium-term and long-term recommendations, as well as the support and role of Bank Indonesia, the national government, and local administrations (Picture 14.1). The Inflation Control Roadmap is furthermore expected to become a reference for the Indonesian Government Work Plan and Regional Government Work Plan.

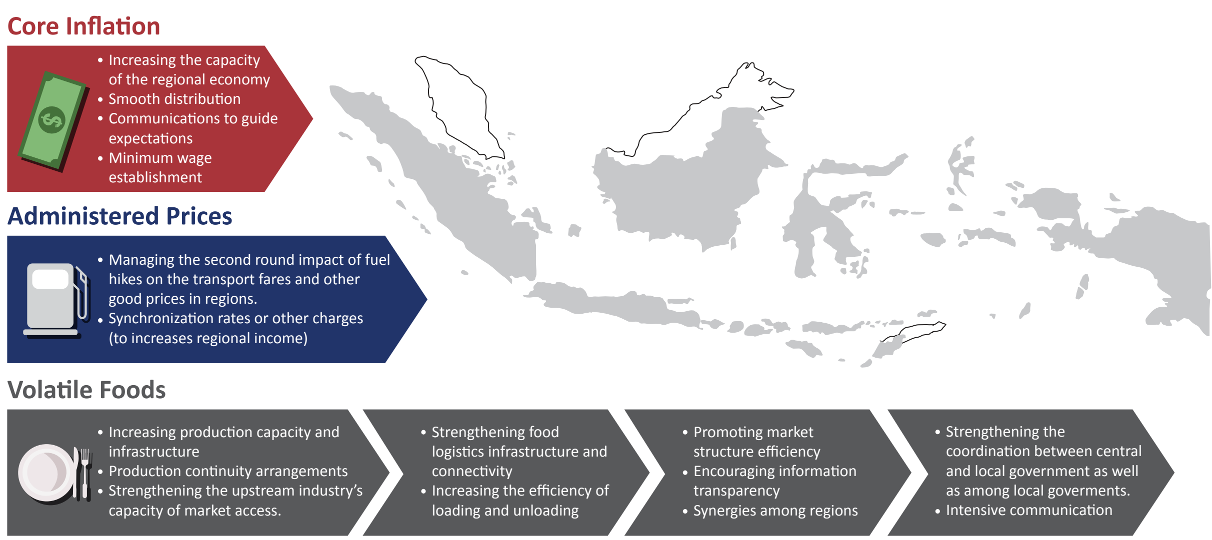
The policy coordination between Bank Indonesia and the Indonesian government relating to the Inflation Control Roadmap has been included in the Indonesian government's first economic policy packages. Bank Indonesia had also issued its own policy package to complement the Indonesian government's economic policy packages, outlining policies in maintaining macroeconomic stability, with a particular focus on inflation management (Picture 14.2).

Coordination of Policies on Currency Exchange Rates

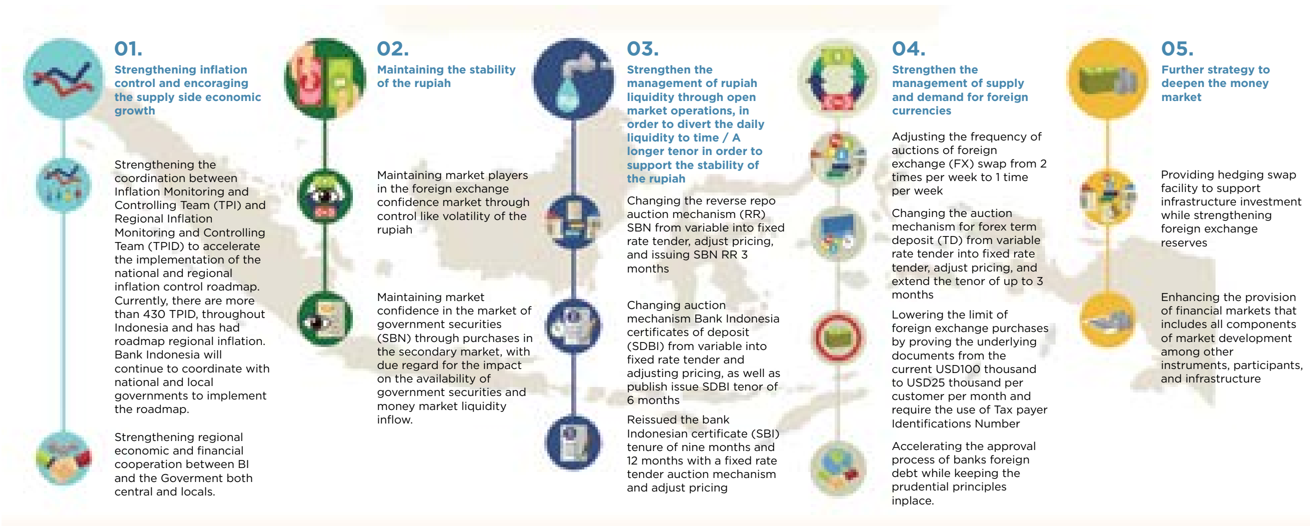
Throughout 2015, the global economic situation had presented many challenges to Indonesia's economy. Global growth was on a slowdown, while uncertainties in the world's financial markets increased due to speculations on the timing of the Federal Funds Rate (FFR) policy and the unexpected devaluation of yuan. As a result, volatility on Indonesia's rupiah currency and turbulences in the domestic financial markets increased, potentially risking macroeconomic stability. The coordination of policies between Bank Indonesia, the Indonesian government and other related authorities, particularly on stabilizing currency exchange rates, was therefore crucial in maintaining broader macroeconomic stability.

The synergy of policies on stabilizing currency exchange rates can be observed in the Indonesian government's first two economic policy packages. Bank Indonesia

Picture 14.1. **Mapping of Inflation Problems Based on Regional Characteristic**



Picture 14.2. **Coordination of Bank Indonesia and the Government in Maintaining Macroeconomic Stability**



issued policy package to complement the government's first economic policy package, focusing particularly on stabilizing the Indonesian rupiah's exchange rate. The policy packages outlined that volatility on the rupiah would be managed together, and carried out through Bank Indonesia purchasing Indonesian Government securities (SBN) in the secondary market. The first economic policy package also outlined coordination in managing the supply and demand of foreign currencies (Picture 14.2).

Coordination in stabilizing currency exchange rates was further carried out with the Indonesian government's second economic policy package. Stabilizing currency exchange rates was even the focus of the policy package as uncertainties on the regional money markets from expectations on the FFR and from China's devaluation further increased. Among the joint policies in the second policy package was tax incentives for exporters that deposit or exchange their export revenues at local banks. Indonesia's Foreign Currency Exchange Flows Report was also improved to better monitor market dynamics, as well as to better meet requirements on transparency and public access to information.

Coordination of Policies on Financial System Stability

Apart from problems with the currency exchange rates, the stability of Indonesia's financial system as a whole was in fact under increasing risks as the world economy in 2015 still saw imbalances in its recovery, weak commodity prices, and divergent policy instruments taken by overseas central bank and monetary authorities as response to uncertainty due to upcoming FFR hike. Bank Indonesia therefore strengthened its coordination with other related authorities regarding the stability of the financial system, focusing in particular on crisis prevention and resolution measures through the Coordination of Financial System Stability (FKSSK). The FKSSK itself had been established since 2012, and comprises Bank Indonesia, the Ministry of Finance, the Financial Services Authority (OJK), and the Deposit Insurance Corporation (LPS).

Consultations and coordination within the FKSSK became more effective, both at the technical level through the Deputies' Meeting forum, and at the board level where the latest updates on the stability of the financial system are assessed and joint recommendations are formulated. This can be seen through the formation of five working groups to better carry out the FKSSK's three main tasks on surveillance for crisis prevention, formulating policy options for crisis management, and formulating guidelines for crisis management.[1]

1 The FKSSK's *Working Group* I and II are tasked with crisis surveillance and prevention, which include formulating indicators to assess the financial system's stability, improving surveillance on the financial system, and managing the exchange of data and information. Working Group III and IV are tasked with formulating policy options for crisis management, which include improving the standard operating procedures to activate the International Financial Safety Net (IFSN) and improving the frameworks for bank crisis resolution. Working Group V, meanwhile, updates crisis management mechanisms in the crisis binder and formulates guidelines for the Financial System Assessment Program (FSAP).

To further improve its effectiveness, the FKSSK on December 23, 2015 carried out its main agenda for the year of running a simulation of its decision-making protocols during a crisis. The simulation's particular focus was evaluating and ensuring that the requirements on the legal procedures for each institution carrying out the Crisis Management Protocols, the crisis binders, and communication procedures were all adequately fulfilled. The FKSSK's 2015 simulation was furthermore distinct from those conducted in previous years, as it was carried out to evaluate the requirements and practicality of a bill on the Financial System Safety Net (JPSK), particularly on the decision-making process of determining whether a crisis has happened, and how to manage banks under crisis, as outlined in the bill. Bank Indonesia's role was also evaluated, particularly on the contribution in assessing the stability of the financial system. The decision-making process that was evaluated in the simulation included: (i) deciding whether impacts from pressures on the currency exchange rate and the financial system has caused their status to be abnormal, (ii) deciding whether to provide short-term liquidity loans to banks experiencing liquidity problems, (iii) deciding whether a bank with liquidity problems has systemic effects, (iv) deciding policy options to lift pressures on the currency exchange rate and the financial system, and (v) finding solutions for failing banks with systemic effects but unfit for Bank Indonesia's liquidity aid.

Apart from strengthening the coordination mechanisms between institutions, Bank Indonesia also worked together in formulating the legal frameworks for crisis management. Both the Bank Indonesia Law and the OJK Law mention that the JPSK Law is the primary legal reference for anticipating and managing any financial system crisis. For this, a bill on the JPSK was thus deliberated and passed into law by the end of 2015. The new JPSK Law outlines the coordination required to monitor and maintain the stability of the financial system, how to manage when the financial system stability is abnormal, and how to manage problematic banks with systemic effects during both normal and abnormal situations.

14.2. POLICY COORDINATION TO SUSTAIN MOMENTUM FOR GROWTH

The momentum for growth must be continuously maintained for the longer-term sustainability of Indonesia's economy, and is even more urgent during such uncertain times of the world economy still reeling to recover from a slowdown. Policy coordination between Bank Indonesia, the national government and local administrations, particularly on macroprudential matters, on the payment system, and on the money supply management, is crucial in the efforts to maintain the momentum for growth.

Coordination of Policies on Growth and Macroprudential Issues

As Indonesia's economy in 2015 experienced a downturn due to declining commodity prices taking a toll on exports, strengthening the domestic real sector and local micro, small, and medium enterprises (MSMEs) was realized as a way out from this situation and revive growth. Stronger policy coordination in the real sector between the Indonesian government and Bank Indonesia was thus needed, and Bank Indonesia, in reference to the Indonesian government's "Nawa Cita" Nine Priority Programs, had begun efforts to support growth of the planned priority sectors throughout the country. Bank Indonesia also participated as a counterpart in the policy committee for the People's Business Credit (KUR) program, helping to evaluate the KUR disbursements for 2014, and providing recommendations for the KUR disbursements in 2015, as outlined in Presidential Decree No. 14/2015 on the Policy Committee for MSMEs Financing, which was issued on May 7, 2015. The Committee followed this up by issuing policies to ease the loan-to-value ratio on mortgages and the down-payments for motor vehicle loans, all of which are expected to stimulate small business activities in the trade, construction and manufacturing sectors.

Bank Indonesia, together with the Ministry of Maritime Affairs and Fisheries, also improved access to financing for MSMEs in the fisheries industry, which is among the Indonesian government's main priority sectors. Financial service facilitators were provided to MSMEs in the maritime sector, assisting them in obtaining credit, introducing less cash financial services to them, and improving the exchange of data and information among the MSMEs. All of this were implementations of the Memorandum of Understanding (MoU) No. 17/1/NK.KKP/GBI/2015 and No.07/MEN-KKP/KB/IX/2015 on Capacity Building and Empowerment for the Maritime and Fisheries Sector, signed between Bank Indonesia and the Ministry of Maritime Affairs and Fisheries on September 10, 2015.

Meanwhile, policies regarding entrepreneurship were for 2015 mainly aimed at encouraging the start-up and growth of local entrepreneurs, through business incubator programs and improving cooperation between stakeholders. An example of this was the follow-up implementation to MoU No. 16/2/GBI/DPAU/NK on Developing Economic Self-Reliance for Islamic Boarding Schools and Improving Less Cash Services at the Ministry of Religious Affairs, signed between Bank Indonesia and the Ministry of Religious Affairs on November 5, 2014. The MoU outlined the development of economic self-reliance and entrepreneurship for Islamic boarding schools through sharia-based economic activities and business incubators, as well as facilitating the setting up of entrepreneurship pioneer projects with consultation services, access to financing, and access to the market.

The entrepreneurship programs were also developed for the penitentiary system, through MoU No. 16/1/GBI/DPAU/NK on the Cooperation to Develop Economic Self-Reliance for the Penitentiary System, signed between Bank Indonesia and the Ministry of Law and Human Rights on September 18, 2014. Technical assistance were provided for both prison officers and prisoners, to cultivate economically valuable agricultural products.

Regarding policies to develop the agriculture sector, Bank Indonesia and the Ministry of Agriculture signed MoU No. 17/2A/NK/GBI/2015 and No. 11/MoU/HK.230/M/12/2015 on December 2, 2015 that outlined: (i) improving the business capacity of the agricultural industry, particularly of commodities that affect inflation, (ii) improving the access to financing for agricultural MSMEs and farmer communities, (iii) building the capacity of agricultural facilitators and financing agencies, (iv) encouraging less cash services, data exchange and information sharing in the agricultural sector, (v) and improving public awareness programs for each task. Bank Indonesia also carried out particular efforts to keep the price of chili peppers at check, by supporting the Ministry of Agriculture program of cultivating chili peppers during the dry season, which was initially launched in East Nusa Tenggara, West Kalimantan, West Java, and North Maluku. The program was then expanded to Bank Indonesia's agricultural business incubator clusters in South Sulawesi, East Java, West Nusa Tenggara, and the Bangka-Belitung Islands.

All the previously mentioned joint policies from Bank Indonesia and the Indonesian government to maintain the momentum for growth were carried out in line with the government's series of economic policy packages, which for 2015 had totalled to eight economic policy packages (Table 14.1). In the first economic policy package, policies to maintain the momentum for growth included expediting the implementation of national priority programs, expediting government spending, and facilitating investments in the property sector. The second economic policy package included such policies as facilitating investments in industrial zones and lifting value-added taxes on the imports of transport vehicles to stimulate growth in the transportation sector. The third economic policy package provided incentives on electricity rates for labor-intensive and less-competitive industries, as well as interest rate cuts and expanding KUR loan. Policies to maintain momentum for growth continued with the fourth economic policy package, in the form of facilitating credit for export oriented and labor intensive MSMEs that are prone to lay offs. The fifth economic policy package provided tax incentives on asset revaluation and eliminated any double taxation on collective contracts for real estate investment funds (KIK DIRE). Incentives were also provided for eight Special Economic Zones (SEZs) in the sixth economic policy package.

In December 2015, the Indonesian government continued its package of policies to maintain the momentum for growth. The seventh economic policy package provided tax incentives for labor-intensive industries and income tax incentives for workers in those labor intensive industries. Lastly, the eighth economic policy package provided incentives for the construction of new oil refineries and lifting import duties on aircraft spare parts.

Bank Indonesia's policy coordination with other related authorities to maintain the momentum for growth was also carried out within the context of international cooperation. Realizing the crucial role of investments as an engine for growth, Bank Indonesia had supported the Indonesian government's pitch in international cooperation forums to focus on the financing of infrastructure projects in emerging markets. Bank Indonesia had in this context participated actively in the formation of the Islamic Investment Infrastructure Bank or the World Islamic Investment Bank (WIIB) to support the financing of infrastructure projects in Islamic Development Bank (IDB) member countries.

Bank Indonesia also supported the Indonesian government in the formation of the G20's Global Infrastructure Hub (GIH), which is expected to act as an information center for infrastructure investments. Indonesia also committed to the G20's growth strategy, which is a comprehensive strategy to ensure robust, sustainable and inclusive growth. For this, Bank Indonesia and the Ministry of Finance participated actively in the final drafting of the G20's Adjusted Growth Strategy, which is the commitment of G20 member countries to maintain the momentum for growth within their own economies, and bolster cooperation to stimulate global economic growth.

Table 14.1. Government Economic Policy Packages in Promoting Economic Growth

Package Vol. I Sept 9, 2015	Package Vol. II Sept 29, 2015	Package Vol. III Oct 7, 2015	Package Vol. IV Oct 15, 2015	Package Vol. V Oct 23, 2015	Package Vol. VI Nov 5, 2015	Package Vol. VII Dec 4, 2015	Package Vol. VIII Dec 21, 2015
• Acceleration of Budget Disbrusment • Acceleration of national strategic projects implementation • Package ease of investment in the property sector	• Providing incentives for industrial zones • VAT Exemption for import of transportation vehicles	• Electricity incentive for labor-Intensive industries with weak competitiveness • The decline in interest rates and expansion of KUR receivers	• Credit facilities for export oriented SMEs from LPEI • Encourage access KUR	• Tax Incentives for Assets Revaluation • Elimination of Double Taxation On Collective Contracts Real Estate Investment Trusts (REITS)	• Developing Special Economic Zones • Providing tax incentives in Special Economic Zones	• Two years income tax incentives for workers in labor incentives and export oriented industries. • Tax incentives for labor intensive industries	• Incentive for construction of new oil refineries for energy security • Incentives for air transportation services industry

Coordination of Policies on the Payment System and Money Supply Management

The momentum for growth requires such support as an optimal and reliable payment system, which is attainable through cross-institutional policy coordination between related ministries and other authorities. In this context, Bank Indonesia, together with the Ministry of Finance, the Ministry of Communication and Informatics, the Ministry of Trade, and the Financial Services Authority (OJK), established the Indonesian Payment System Forum (FSPI). The FSPI, formed by Bank Indonesia Governor Decree No. 17/3/KEP.GBI/2015 on August 25, 2015, directs strategic policies concerning the payment system, synchronizes policies and regulations between institutions, coordinates initiatives and programs relating to the payment system, fosters innovations for the payment system, and gives advice on educational and public awareness programs of the payment system.

Besides acting as a coordinating forum for institutions and authorities related to the payment system, the FSPI also caters to the interests of industry stakeholders on policies and regulations regarding the payment system. Industry stakeholders, as well as the academia, related professionals, and other ministries may serve as discussion partners providing input, advice and assessments on the payment system, in meetings at FSPI's secretariat office in Bank Indonesia.

Apart from setting up the FSPI, other efforts in coordinating policies on the payment system and money supply management include An MoU in March 2015 between Bank Indonesia Governor and the Head of the Financial Transaction Report and Analysis Center (PPATK), on the Prevention and Eradication of Crimes in Money Laundering and Terrorism Financing. The MoU, a revision of a similar MoU in 2010, outlines cooperation in information sharing and improving the information system, in formulating regulations and guidelines on compliance audits, on engaging in public awareness programs, and in the training and assigning Bank Indonesia officials to the PPATK.

Regarding audits of financial transactions, Bank Indonesia will coordinate with the PPATK in enforcing compliance on the reporting of financial transactions according to existing laws on the prevention and eradication of crimes in money laundering and terrorism financing, as well as conducting joint audits. Meanwhile, in regard to improving institutional competence, Bank Indonesia and the PPATK had provided educational and training sessions for each of their officials both separately and jointly. These training sessions include workshops on legislations against crimes in money laundering and terrorism financing, as well as preparatory workshops for the mutual evaluation of the Financial Action Task Force (FATF).

Bank Indonesia and the PPATK as members of the Anti-Money-Laundering Committee have also been cooperating in formulating legal measures to freeze funds of suspected terrorists according to Law No. 9/2013 on Anti-Terrorism-Financing, and coordinating the National Risk Assessment (NRA) involving law enforcers, intelligence agencies, financial institutions, and other authorities. The NRA identifies and analyses risks from money laundering and terrorism financing, to then mitigate those risks through the formulation and enforcement of relevant policy measures and regulations.

Meanwhile, regarding the money supply management, Bank Indonesia has coordinated with other institutions to follow-up Bank Indonesia Regulation (PBI) No.17/3/PBI/2015 on the Use of the Rupiah Currency within the

Table 14.2. Inter-Agency Coordination

No	Institution / Agency	Coordination Topic
1	Financial Services Authority	Insurance companies, mutual funds, and financing companies
2	Ministry of Foreign Affairs	Extraterritorial region and international institutions
3	Ministry of Religion	Cost of Haji and Umrah
4	Ministry of Transportation	Strategic infrastructure and transactions on land, sea, and air
5	Ministry of Industry	The standard reference exchange rate and the textile industry
6	Ministry of Tourism and Creative Economy	Hospitality and tour and travel
7	Directorate of Renewable Energy and Energy Conservation	Strategic infrastructure and quotation Feed-in Tariff (FIT)
8	Directorate of Oil and Gas and SKK Migas	Mapping of upstream oil and gas transactions
9	Directorate of Electricity	Strategic infrastructure and PT PLN with vendor contracts
10	Regulatory Agency for Downstream Oil and Gas (BPH Migas)	Freight rate fixing natural gas through pipelines
11	Directorate General of Taxation	Bookkeeping and Tax
12	Directorate General of Customs and Excise	Duty free shops
13	Capital Investment Coordinating Board	Foreign investment in Indonesia
14	Supervisory Board and the Commodity Futures Trading	Recapitulation futures products traded on the inside and / or outside futures exchange

territory of the Republic of Indonesia. In 2015, a total of 26 accords on the matter had been reached between Bank Indonesia's Regional Offices with their counterpart Regional Police Offices, agreeing on cooperation in carrying out each other's relevant tasks and authorities (Table 14.2). The accords are follow-ups to the "Accord on the Cooperation to Support Bank Indonesia's Tasks and Authorities" signed between Bank Indonesia Governor and the National Police Chief on September 1, 2014, as well as the "Guidelines on the Law Enforcement against Crimes relating to the Payment System and Currency Exchange" signed between Deputy Governor of Bank Indonesia and Chief of the Crime Investigation Agency National Police on September 24, 2014, the "Guidelines on Enforcing the Use of the Rupiah Currency within the Indonesian Jurisdiction and against Crimes relating to the Use of the Rupiah Currency" signed between Bank Indonesia Deputy Governor and Chief of the National Police Crime Unit on November 20, 2015, the "Guidelines on Security Measures for Bank Indonesia and State Valuables" signed between Deputy Governor of Bank Indonesia and Chief of the National Police Mobile Brigade Corps on February 23, 2015, and the "Guidelines on the Supervision of Money-Transporting Security Companies" signed between Deputy Governor of Bank Indonesia and Chief of the Security Maintenance Agency of the National Police on February 26, 2015.

Bank Indonesia had also coordinated with the authorities of other countries through international forums to improve the payment system and the money supply management. The forums include the 2015 Financial Sector Reform and Strengthening (FIRST) Initiative Consultative Group Meeting, the Association of South-East Asian Nations (ASEAN), Working Committee on Payment and Settlement System's (WCPSS) coordination on National Risk Assessment, and the World Bank's Technical Assistance for the Financial Inclusion Support Framework. Bank Indonesia had on the regional scale been particularly active in the ASEAN WCPSS, which for 2015 had focused on improving the region's payment systems to facilitate the liberalization of goods, services, capital, and investments for the ASEAN Economic Community (AEC). This was done by developing the infrastructure for high-value payment systems so that the payment system infrastructure in ASEAN's BCLMV member countries (Brunei Darussalam, Cambodia, Lao PDR, Myanmar and Vietnam) will be on par with those in the ASEAN 5 (Indonesia, Malaysia, the Philippines, Singapore, and Thailand).

Bank Indonesia had also initiated bilateral arrangements regarding the payment system with other countries to facilitate more trade and investments. The bilateral arrangements include developing the necessary payment system infrastructure to facilitate cross-border trade and investment settlements using local currencies. The use of local currencies is expected to reduce the current dependency on the U.S. dollar for cross-border transactions, as well as benefit from less conversion rates and fees.

Regional cooperation through ASEAN's WPCSS also concerned retail transactions, focusing on improving the efficiency of transactions by using card-based payments.[2] Policies relating to this matter include setting transaction

2 Card-based payments for retail transactions are currently managed by international financial service providers.

fees, lifting regulations that are not beneficial to consumers and lifting regulations limiting the operation of domestic service providers. ASEAN's WCPSS also prepared other initiatives relating to the payment systems for member countries to implement after 2015 in achieving ASEAN's 2025 vision.

Bank Indonesia also cooperated with other central banks and international agencies on institutional capacity building regarding payment systems. In particular, Bank Indonesia had worked together with the World Bank on technical assistance programs relating to the Financial Sector Reform and Strengthening Initiative (FIRST), focusing on improving Indonesia's payment system infrastructure in aspects of its legal and regulatory framework, payment system oversight, development of a remittance system, and innovation in payment instruments.

Meanwhile, in preventing and addressing the problem of counterfeit money, Bank Indonesia had thoroughly engaged with other member institutions of the Coordinating Agency for the Eradication of Counterfeit Money (Botasupal).[3] Coordination was carried out with the Indonesian Supreme Court, the OJK, and the PPATK, to strengthen law enforcement against crimes relating to counterfeit money and create a deterrent effect against such crimes.

Bank Indonesia also coordinated with the Ministry of Finance in the annual printing of paper money and minting of coins. This includes planning the rupiah denominations to be issued and each of their amounts, taking into account such macroeconomic variables as the year's estimate on inflation, economic growth and interest rate, as well as the denominations and amounts to be discontinued, replaced or destroyed.

Starting 2015, the printing of rupiah banknotes and minting of coins will be carried out under a multi-year term. For this, Bank Indonesia has coordinated with the Audit Board (BPK), the Public Procurement Agency (LKPP), and the State Minting Company (Perum Peruri), concurring that the multi-year printing of rupiah banknotes and minting of coins for 2015-2017, which had been approved by the Finance Ministry, as admissible, as long as risks concerning the material quality for the banknotes are addressed.

Bank Indonesia also coordinated with the Ministry of Finance on the discontinuation, replacement and destroying of rupiah banknotes and coins. Information on the amount and nominal value of the rupiah currency discontinued, replaced and destroyed had been presented to the Ministry of Finance every quarter, and to the Ministry of Law and Human Rights once a year, before then being published in the year's State Gazette.

Bank Indonesia then coordinated with Indonesian Railways Company and Indonesian National Shipping to distribute the printed banknotes and minted coins, and with the National Police to provide security for the distribution.

Meanwhile, the Botasupal had held its coordination meeting in December 2015 to evaluate the year's efforts in preventing and addressing problems of counterfeit money, and formulate its programs and action plans for 2016 (Picture 14.3). Botasupal's assessment for 2015 concluded that further coordination is needed as the National Police had continued to uncover numerous crimes relating to counterfeit money, as well as increasing amounts of counterfeit money.

Bank Indonesia had conducted particular coordination with the Supreme Court outside the Botasupal forum, in continuing to providing relevant training for court justices. Such training sessions had been carried out with the Supreme Court for 13 years, with topics on banking as well as on the central bank's role and duties. For 2015, the issue of money supply management had been added to the training sessions, and held in four cities throughout the year: Palembang in March, Banjarmasin in May, Manado in August, and Semarang in October, with each

Picture 14.3. Coordinating Agency for Eradication of Counterfeit Money

3 The Botasupal was established by Presidential Regulation No. 123/2012 and comprises the State Intelligence Agency, the National Police, the Attorney General's Office, the Finance Ministry and Bank Indonesia.

session attended by 30 justices from the district, religious, administrative and military courts.

14.3. POLICY COORDINATION TO IMPLEMENT STRUCTURAL REFORM

Structural reform was among the priority agendas of the Indonesian government in 2015, prompting the coordination between Bank Indonesia and other related authorities in such policies as deepening the financing market, as well as reforms on the real sector, the payment system, and the currency management.

Coordination of Policies on the Financial Market Deepening

Deepening the financial market helps strengthen an economy's fundamentals by fostering macroeconomic stability and sustainable growth, and can be achieved by providing adequate liquidity, facilitating transactions, inducing normal market pricing, and minimizing risks.

As part of efforts in deepening the financial market, Bank Indonesia had in 2015 issued three regulations concerning foreign exchanges: on the transactions of foreign currencies and the rupiah between banks and local parties, on the transactions of foreign currencies and the rupiah between banks and foreign parties, and on the banking industry's foreign exchange net position.

The three regulations expand the definition of derivative transactions from previously only forward transactions, swaps and options, to include cross currency swap (CCS) transactions, which is an agreement between two parties to exchange funds and any related interests in different currencies. The regulations also expand the types of transactions considered as underlying, to include income and expense estimations for trade and investment activities. The minimum required period of one week for derivative transactions by foreign parties was also lifted, to improve certainty for the foreign parties in optimizing derivative transactions as hedging for their investments in Indonesia.

Meanwhile, coordination between Bank Indonesia and the Indonesian government was carried out with the government's first two economic policy packages, which had focused on deepening the financial market. Bank Indonesia issued forward market intervention policies to maintain the supply and demand balance in the financial market, and issued Bank Indonesia deposit notes and reverse repos for the Indonesian government's two-week bonds to bolster rupiah liquidity in the money markets. Synergized, both policies are expected to provide positive sentiments for the rupiah currency in the money markets and mitigate potential risks from turbulences in the global economy. This is crucial in driving more sustainable growth amidst the still uncertain situation with the global economy. Overall, coordination of the policies are expected to support efforts in increasing the capacity of domestic trade and investments, by providing more flexibility in the transactions of market players, and thus deepen the financial market as well. The policies had been formulated and implemented prudently and in consideration of their possible impacts to the stability of the financial system, with banks strictly required to adhere to regulations on risk mitigation.

Coordination of Policies on Real Sector Reform

The Indonesian government had set several sectors as priorities in 2015, including the maritime sector, the energy and food sector, as well as the industry and tourism sector. These sectors, however, still needed to undergo structural reforms to be further developed into more resilient and sustainable engines of growth, and thus the coordination of policies to implement the reforms were equally important.

Among the coordination of policies to reform the maritime sector was a national coordination meeting between Bank Indonesia, the Indonesian government and local administrations, on May 25, 2015 in Ambon, Maluku. The meeting managed to build a common vision of reviving Indonesia's maritime based economy, and formulate concrete strategies and technical level measures to do so.

Indeed, developing a maritime based economy is ever more crucial in these challenging times for the world economy, as the economic potential from Indonesia's maritime resources is more than enough to drive higher and more inclusive growth. Indonesia's maritime resources has so far been under developed, as can be seen in the limited exports of fish and other sea produce, as well as the under-developed maritime processing industries. The sea has been considered an economic barrier, and has yet to become a major source of income. This is somewhat ironic as developing a maritime based economy has all the factors needed to drive more inclusive growth, increase prosperity, and improve the economy's structure.

The coordinating meeting on policies to reform the maritime sector had agreed on four strategies to implement, namely: strengthening Indonesia's maritime integrity, managing Indonesia's maritime resources independently and in a sustainable manner, developing Indonesia's maritime infrastructure independently and in an integrated manner, developing human capital for the maritime sector and research on maritime technology, and developing a maritime based culture. All participants of the meeting then coordinated in the needed preparations to promptly implement the strategies.

The energy sector, particularly concerning its infrastructure, was another focus area for structural reform. A meeting to coordinate policies on reforming the energy sector was thus held on August 11, 2015 in Balikpapan, East Kalimantan. The meeting, attended by Bank Indonesia, the Ministry of Finance, the Ministry of Energy and Mineral Resources, the Ministry of Environment and Forestry, the State Electricity Company (PT PLN), the Special Task Force for Upstream Oil and Gas Business Activities (SKK Migas), the provincial administrations of Kalimantan, and the regency and city administrations of East Kalimantan, discussed the challenges and recommendations for both macroeconomic and sectoral policies, as well as financing strategies for energy infrastructure. Achieving energy resilience and independency was particularly important, to support industrialization and thus drive more sustainable and inclusive growth.

The Ministry of Finance provided several fiscal incentives to facilitate the development of energy infrastructure. Among the incentives was a tax holiday of longer tax exemption periods for renewable energy industries and refining industries. Tax allowances for mining industries, smelter industries and power plant companies were also given, in the form of cuts on net income tax, and shorter depreciation and amortization periods. Regarding energy infrastructure financing, the Indonesian government encouraged public-private partnership (PPP) schemes for the land acquisition process, project development, and project insurance through state infrastructure guarantor Indonesia Infrastructure Guarantee Fund.

The Ministry of Environment and Forestry, meanwhile, provided facilities relating to spatial regulations and permits for energy infrastructure projects. The Regional Spatial Plans (RTRW) for Kalimantan provinces had been revised to account for both infrastructure projects and forest areas, in accordance to the Indonesian President's directive that all forest areas of nature reserves, forest conservation areas and plantation areas can be used accordingly for infrastructure projects. The Ministry of Environment and Forestry had also expedited the needed principle permits under its authority for state electric company PT PLN's 35,000MW power plant projects.

The Ministry of Energy and Mineral Resources itself had also provided facilities for permits relating to energy infrastructure projects and other projects concerning Indonesia's energy mix needs. The ministry simplified the permit processing for renewable energy projects from previously 52 procedures to only 29. The oil-and-gas and mining sectors saw similar permit processing procedures simplified. Power projects, meanwhile, saw simpler procedures in setting electric rates, as well as their guarantee periods extended to 25 years.

Structural reforms for Indonesia's industry and tourism sector, meanwhile, is aimed at improving their global competitiveness. A coordinating meeting on policies to reform the industry and tourism sector was held on November 13, 2105 in Yogyakarta, resulting in several policy measures to improve the sectors' competitiveness. Structural reforms for the industry sector in the form of deregulations and de-bureaucratization, relaxing the rules for investment, providing tax incentives for transport vehicles, and simplifying the land use permitting process, were all included in the Indonesian government's economic policy packages. Meanwhile, structural reforms to improve the tourism sector's competitiveness included lifting the visa requirements for 90 countries, facilitating a simpler custom clearance procedure for yachts tourism, and constructing new airports and seaports.

Other policies for structural reforms had been included in the Indonesian government's economic policy packages, and underwent coordination with Bank Indonesia. In the first economic policy package, the processing of business permits was simplified and setting up co-operatives was facilitated. The processing of investment permits in the industry and forestry sector were also simplified, in the second economic policy package. In the fourth economic policy packages, seven regulations concerning wages were issued, including on formulating the minimum wage, on the regional minimum wages, on the minimum wages by sectors, on wage structuring, on allowances on national days, on service fees, and on the basic cost of living. Meanwhile, the processing of permits for sharia-based banking products was simplified in the fifth economic policy package. Investments in water resource projects prior to the Supreme Court cancelling Law No.7/2004 on Water Resources was ascertained in the sixth policy

Table 14.3. Government Economic Policy Packages Structural Reform

Package Vol. I Sept 9, 2015	Package Vol. II Sept 29, 2015	Package Vol. IV Oct 15, 2015	Package Vol. V Oct 23, 2015	Package Vol. VI Nov 5, 2015	Package Vol. VII Dec 4, 2015	Package Vol. VIII Dec 21, 2015
• Simplification of business license throught the local level • Strengthening cooperative institutions	• Trimming the licensing processes of investment for industry as well as environmental and forestry • Accelerate the process of tax allowance and tax holiday	• Remuneration Reform to provide business certainty	• Permit Simplification for new Islamic banking products	• Trimming licensing stages for import raw materials drug • Regulatory reform for water resources exploitation	• Trimming the stages and improving services of land certificate issuance	• Space utilization and land use reform through the One Map Policy

package, while the seventh economic policy package simplified the processing of land certificates. Lastly, the eighth economic policy package had formulated a One Map Policy for further structural reforms (Table 14.3).

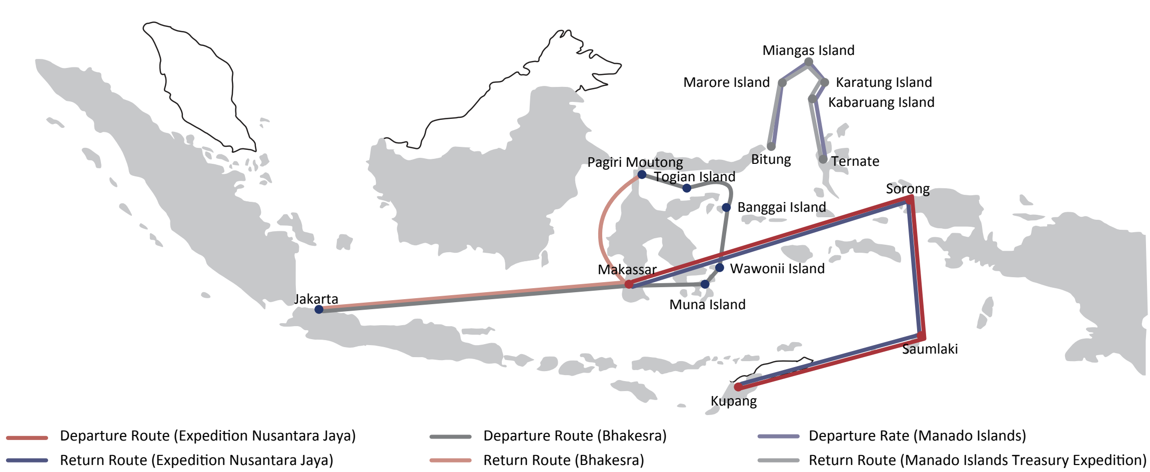
Coordination of Policies on Reforms to the Payment Systems and Currency Management

Indonesia's Currency Law authorizes Bank Indonesia to coordinate with the Indonesian government in the three aspects of currency management, namely: the planning of currency, the printing of paper-notes and minting of coins, and the destruction of money. Structural reforms for the currency management focus on the distribution of money to all areas under the Indonesian jurisdiction.

For this, Bank Indonesia had worked together with the Ministry of Transportation and transportation businesses. Coordination with the Ministry of Transportation included ensuring the distribution of money, enforcing the use of the rupiah currency in all areas under Indonesian jurisdiction, promoting the national non-cash and inclusive financial access programs, ensuring the logistics and distribution of goods for inflation management and driving growth, information sharing, and conducting joint research (Picture 14.4). Coordination in ensuring the distribution of money, was in particular to ensure that the rupiah currency can be reliably transported at all times to all areas under Indonesian jurisdiction, thus ensuring as well the quality and integrity of the rupiah.

Bank Indonesia also worked together with the Coordinating Ministry for Human Development and Cultural Affairs and with the Indonesian Navy, to ensure that the distribution of the rupiah currency and its cash services are available even in the most remote areas and at Indonesia's land border, and thus achieve the goal of ensuring the distribution of the rupiah to all areas under Indonesian jurisdiction by 2019.

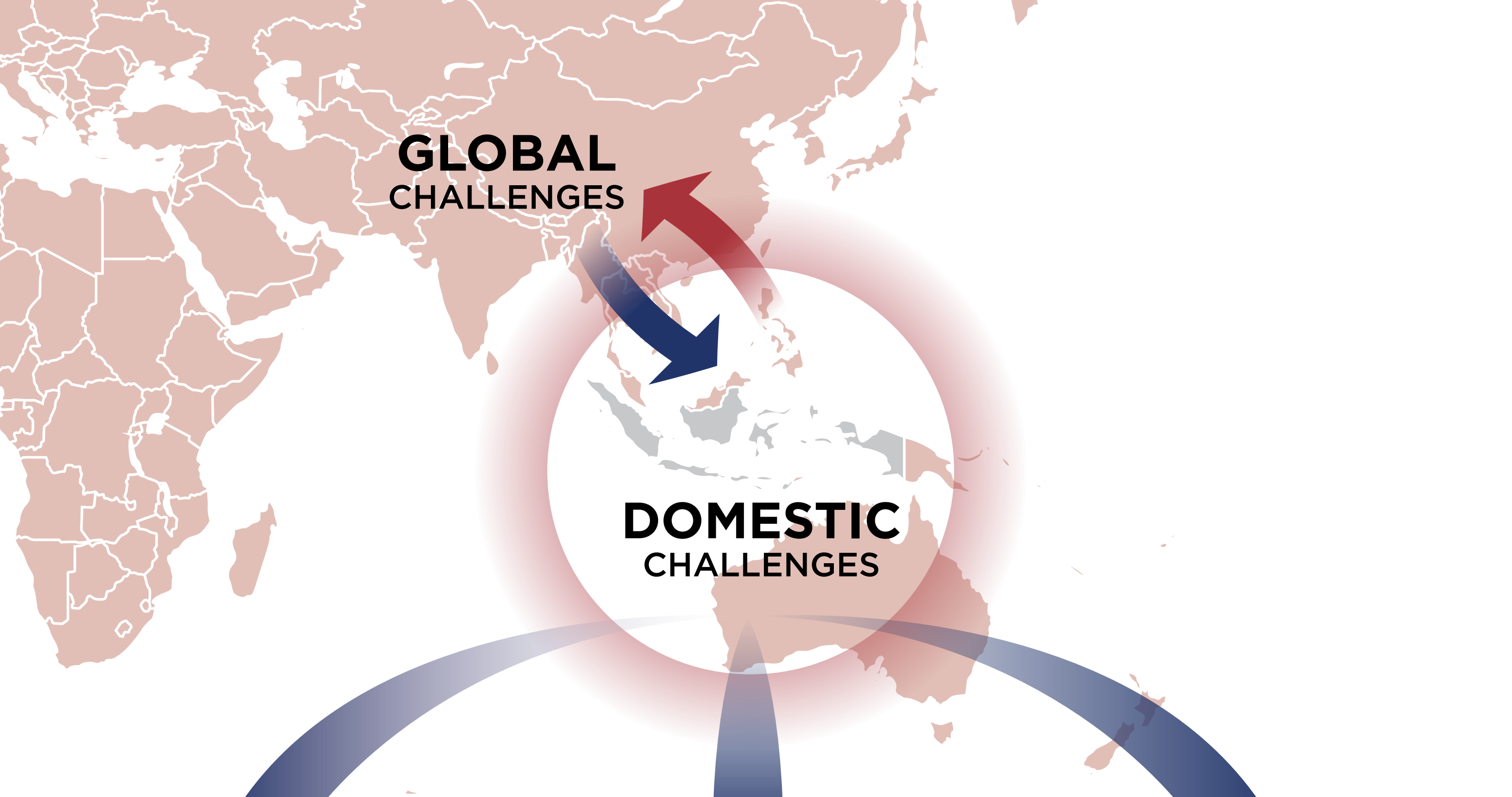
Picture 14.4. Currency Distribution Network and the National Cash Services



The *Srikandi* Dance portrays the intelligence, courage, and expertise of a soldier in using a variety of weapons to be victorious on the battlefield. Indonesia's economy must show similar characteristics to confront a future replete with challenges.

PART IV

CHALLENGES, POLICY DIRECTION, AND OUTLOOK



1 **Prudent Relaxation of Monetary and Macroprudential Policies**

2 **Synergy of Monetary and Fiscal Policy to Promote Growth**

3 **Acceleration of Structural Reform**

POLICY MIX AND STANCE

Indonesia Economic Projection 2016	Medium-Term Prospects 2020
Inflation 4 ± 1%	Inflation 3.5 ± 1%
Economic Growth 5.2 - 5.6%	Economic Growth 6.3 - 6.8%
Current account deficit slightly increased, however remained sound	Current account deficit below the safe limit of 3% of GDP with healthier structure

PART IV

CHALLENGES, POLICY DIRECTION, AND OUTLOOK

The principal challenge from the global economy stems from the still inadequate global growth and continuing decline in global commodity prices. Alongside this challenge, while the global financial markets uncertainty is expected to ease in response to the narrowing divergence in advanced economies' monetary policies, the impact of risks from China's economy calls for vigilance. Although global economic growth is predicted to improve, there is still a downside risk in the growth given the insufficiently solid condition of the U.S. economy and the economic slowdown in China. The U.S. monetary policy normalization is expected to progress gradually, while Europe and Japan are predicted to keep quantitative easing (QE) policies in place, leading to a narrowing of the monetary policy divergence. Although the divergence of monetary policy among advanced countries has begun to ease, the still flagging condition of China's economy could kindle negative investor sentiment towards emerging market economies which in turn might heighten uncertainties on global financial markets. Another global challenge lies in the inception of the ASEAN Economic Community (AEC), which brings both challenges and opportunities for the future. Regarding this, Indonesia has considerable opportunity to become a supplier in the ASEAN and global value chain. However, if domestic products are uncompetitive, Indonesia will simply become a market for the products of other AEC nations.

On the domestic side, the Indonesian economy also faces an array of future challenges with regard to domestic structural problems that have not been fully resolved. The first structural challenge involves achievement of food, energy, and water security, due to the importance of these input factors in the transformation process for industrialisation. In the food sector, the increasingly constrained quantity and capacity of food production is not adequately balanced by improvements in productivity and technology. In addition, demand for food is steadily mounting in line with the increasing population and heavy dependence on rice as food staple due to minimal level of food diversification. In the energy sector, the imbalance in supply and demand of energy persists. On the production side, various obstacles to the development of energy infrastructure have prevented domestic energy production from fully meeting the demand for fuels. On the demand side, the use of alternative fuels has been minimal, far from sufficient to displace the use of non-renewables energy. The second structural challenge is that of increasing the competitiveness of the industry, maritime, and tourism sectors. Regarding *industrial competitiveness*, the industry sector in Indonesia is still heavily based on extractive commodities with low value added. In addition, Indonesia's comparative advantage has also been steadily eroded, particularly in sectors with medium and high technology content. To address this, a strategy is needed to improve competitiveness in investment to create a manufacturing base for supply in the global value chains. In connection with the *maritime sector,* Indonesia faces challenges involving territorial integrity, optimization of natural resources management, and development of a maritime economy. In the *tourism sector*, the principal challenge for developing this industry lies in the limited infrastructure that in turn hampers access for tourists and the time they are able to spend exploring the country. The third structural challenge is that of strengthening capacity to support a sustainable long-term financing and promoting foreign capital inflows in the form of foreign direct investment (FDI). The fourth structural challenge is that of expanding the level of grassroots participation in the economy and of benefits derived from economic development.

These four challenges arising from domestic structural issues are closely tied to a range of problems in key enablers for development, in particular those related to infrastructure, human resources, the business climate, and science and technology. According to a growth diagnostic approach, the most important challenges to the economy in almost every region of Indonesia have their origin in problems with electricity infrastructure, connectivity and quality of human resources. Electricity, a source of energy, is still in short supply, particularly outside Java.

Meanwhile the lack of integration of infrastructure in regard to connectivity hampers efforts to cut logistics costs in domestic value chains, to strengthen internal integration and to improve the competitiveness of Indonesian products. Regarding the quality of human resources, the majority of the work force has only primary and secondary school education, and this is not compatible with the effort to strengthen economic structures in the medium and high technology sectors. Although the business climate is remarkably better compared to the preceding year, further improvements will be necessary, including streamlining of investment licensing, taxation mechanisms, simplification of the bureaucracy, and improvements in government management. In science and technology, there has not been optimum support for improving the competitiveness of production and service sectors and this is an issue that must be watched closely.

Bank Indonesia will keep working to strengthen the monetary, macroprudential, payment system and rupiah cash management policy mix to safeguard macroeconomic and financial system stability while continuing to bolster the momentum of economic growth. In the monetary sector, Bank Indonesia will work consistently and prudently in managing interest rate policy, the reserve requirement, and the exchange rate to keep inflation on track with target, manage the current account deficit at a prudent level, and nurture the momentum now created in economic growth. In this regard, interest rate policy is aimed at managing inflation expectations and domestic demand and maintaining stability in the rupiah exchange rate in line with fundamentals. These in turn will support achievement of the inflation target and a sound current account deficit while supporting the ongoing momentum for growth. The reserves requirement policy will be calibrated prudently to support adequate levels of liquidity that appropriate to the needs of the economy while paying careful attention on macroeconomic and financial system stability. Exchange rate policy will continue focusing on maintaining stability in the rupiah in line with the value of fundamentals. These measures for stability of the rupiah are crucial to support achievement of the inflation target and maintenance of financial system stability and will thus improve the overall performance of the economy.

To bolster the effectiveness of monetary policy, Bank Indonesia will continue strengthening both rupiah and foreign exchange monetary operations. These various policies will be supported by Bank Indonesia, among others, through prudent capital flows management and reinforcement of the international financial safety net through collaboration with international stakeholders in monetary policy and financial system stability.

Bank Indonesia will also continue working on deepening of the financial market and expansion of access to financial services in support of financial system stability, economic efficiency, and sustainable and inclusive economic growth. To move forward with financial market deepening, Bank Indonesia is promoting such measures as use of the General Master Repurchase Agreement (GMRA) and is continuing the development of rupiah and foreign exchange money market instruments. In the context of financial access, Bank Indonesia will pursue a policy for expanding access with focus on development of Digital Financial Services (DFS). Parallel with these measures, the policy direction for MSME development will remain focused on supporting Bank Indonesia's tasks in controlling supply-side inflation and balancing bank's intermediation function. As a balance to the rapid expansion of the payment system, Bank Indonesia has adopted a mission of regulating and safeguarding a secure, efficient, and smoothly-operating payment system. In tandem with the expanding role of the capital market, Bank Indonesia is also helping to protect the security and smooth operation of transaction activity and settlement on this market. To ensure the timely provision of high quality rupiah currency throughout Indonesia in adequate volume and suitable denominations, Bank Indonesia will enhance the coordination with the Government and industry to strengthen the infrastructure for rupiah cash management. Meanwhile, the Government will continue increasing the fiscal stimulus to bolster the momentum for economic growth, increase production capacity, and improve competitiveness. The Government and Bank Indonesia are also working together to accelerate structural reforms to strengthen the key enablers for development, namely quality, equitably-distributed infrastructure, human resources with high levels of expertise, a conducive investment climate and mastery of science and technology. The key enablers for development will be used in support of measures to strengthen food, energy, and water security, boost competitiveness in the industry, maritime, and tourism sectors, expand and increase sources of long-term development funding, and build an inclusive economy. These reinforcing measures will bring about greater diversification in the structure of the Indonesian economy to make it more robust and able to support sustained economic growth.

Indonesia's economic outlook for 2016 is projected to show modest improvement amid limited growth in the global economy. Although global commodity prices are predicted to decline further, the global economic growth is projected around 3.4% in 2016, ahead of the previous year. Indonesia's economic growth is predicted to improve over 2015 to about 5.2-5.6% in 2016. Like before, this growth will be driven by domestic demand and investment. From economic sector point of view, manufacturing is expected to stay the course as the main pillar of the economy, followed by the transportation and communications sector, and the construction sector. These three sectors are set to maintain their leading position, with the construction sector in particular bolstered by construction of Government infrastructure projects. The regional economies are also upbeat for 2016, particularly in the regions of Java, Sumatra, and Kalimantan. With the improvement in economic activity, the current account deficit is projected to slightly increase in 2016, albeit below the safe threshold of 3% of GDP. On the other hand, the capital and financial account is predicted to chart an increased surplus. Taken together, external sector performance in the Indonesia balance of payments in 2016 is set to improve over the previous year. Meanwhile, the inflation forecast for 2016 is expected remains within the target of 4±1%. Moderate and subdued pressure is expected in core inflation, while administered prices inflation is also expected will be lower than in the past year. However, volatile foods inflation is projected to rise slightly in keeping with the El-Nino effect. Financial system stability will remain well in hand, supported by the resilience of the banking system and improving financial market performance. The upbeat outlook for the economy is expected to boost growth in bank deposits (DPK) and credit to 13-15% and 12-14% respectively.

In the medium-term, the Indonesian economy will move towards greater quality, supported by consistency of policy in safeguarding macroeconomic and financial system stability and structural reforms. With implementation of structural reforms under way, the domestic economy is expected to gather momentum. In the medium-term, economic growth is expected to climb steadily towards 6.3-6.8% in 2020. This growth projection is supported by improvement in the global economy, success in structural reforms as visible in construction of infrastructure, streamlining of investment processes, and increased investment in Indonesia. Household consumption will gather strength in line with the growing numbers of the middle class and improvements in social protections. Structural reforms carried out by development of infrastructure will pave the way for increased direct investment and create a conducive business climate. Further reduction in subsidies will create substantial room for Government capital expenditures for development of infrastructure. The current account deficit is predicted to improve in line with the growing competitiveness of Indonesian products. Stronger performance is also envisaged in the capital and financial account in keeping with the progress in the Indonesian economy. Overall, the Indonesia's balance of payments will show significant improvement. From the regional perspective, the increased allocation of transfers to the regions will strengthen regional economies and support equitable development in the regions. With the increased capacity of the domestic economy, achieved through consistent implementation of structural reforms and Bank Indonesia's resolute safeguarding of macroeconomic stability, inflation will be curbed within the targeting range of 3.5±1% over the medium-term. Consistent implementation of structural reforms will be crucial for achieving the positive performance envisaged in the medium-term outlook for the Indonesian economy.

Exploring new areas is always fraught with various challenges. Nevertheless, even the toughest challenges can be overcome with an appropriate strategy and anticipatory measures for all eventualities.

Chapter 15

Economic Challenges and Policy Direction

The Indonesian economy will still face an array of challenges. On the external side, the principal challenge will arise from the risk of continued weak growth in the global economy and decline in commodity prices. On the domestic side, the structural challenges are related to: (i) food, energy, and water security; (ii) competitiveness in the industry, maritime, and tourism sectors; (iii) long-term financing; and (iv) an inclusive economy. Besides this, strengthening is needed in the key enablers for development and the financial system. To this end, the policy mix aims to safeguard stability, generate momentum for economic growth, and accelerate structural reforms. Looking forward, the structure of the Indonesian economy is expected to attain greater diversity and support sustainable economic growth.

The momentum for future growth in the domestic economy will face multiple challenges, both global and domestic. From the global perspective, risks of uncertainty on global financial markets have eased in response to the narrowing of the monetary policy divergence among advanced economies. However, there is a risk of slow-moving world economic growth accompanied by the lingering downward trend in global commodity prices. Despite the decline in risks from uncertainty on global financial markets, global financial markets are still daunted with risk of uncertainty from the prolonged weak condition of China's economy. Under these conditions, foreign capital inflows into emerging markets, including Indonesia, are set to improve albeit on a moderate scale and in spite of the appreciating trend in the US dollar currency. On the regional scale, the growing integration of economies in the region and the sizeable role of China in the economies of other developing countries engender a risk of suffering the consequent impacts of the rebalancing process in China's economy, whether from weakening of commodity prices or through the trading channel or the financial channel.

On the domestic front, efforts to strengthen the domestic economy continue to be daunted by structural issues. First is the challenge of attaining security in food, energy, and water, the three most important inputs necessary to a process of transformation towards industrialization. Second, Indonesia continues to lag behind in global value chains vis-à-vis competitors in the region, given the imbalanced structure of industry and low productivity that leaves Indonesia in relatively weak position regarding the competitiveness of manufactured products. Third is to reinforce the basis for long-term, sustainable financing to support investment as a foundation for turning the wheels of the economy. Fourth is to create equity for the public for the purpose of participating in and reaping the benefits of development and economic growth.

In the face of these challenges, work will continue to reinforce the policy synergy between Bank Indonesia and the Government. At the national level, the policy mix is aimed at safeguarding macroeconomic stability, sustaining economic growth momentum, and accelerating structural reforms in order to create a more diversified economic structure and achieve sustainable economic growth in the medium to long-term. From Bank Indonesia's side, the policy mix will be aimed at macroeconomic and financial system stability and prudent use of the available room for relaxation of monetary and macroprudential policies. On the Government side, policy will be aimed at providing a further boost to the present momentum of economic growth. Aside from this, the Government and Bank Indonesia will work together to accelerate structural reforms to support the creation of robust key enablers for development. This will take the form of quality, equitably-distributed infrastructure, human resources with high levels of expertise, a conducive investment climate, and mastery of science and technology. These key enablers for development will be used to: (i) support the strengthening of food, energy, and water security; (ii) promote competitiveness in the industry, maritime, and tourism sectors; (iii) expand and increase sources of long-term development financing; and (iv) create an inclusive economy.

15.1. ECONOMIC CHALLENGES

Global Economic Challenges

In looking at the future, global economy is set to improve, but will continue to be daunted by various risks that call for vigilance. There are several challenges associated with the uncertainties in the global economy, most importantly the risks from a fragile outlook for global economic growth and continued weakness in commodity prices. Despite the outlook of predicted improvement in global economic growth, there is still a risk of weaker growth. This is partly related to the tepid outlook for improvement in the United State economy, which is the locomotive for the global economy. Added to this, the less than upbeat condition of China's economy also indicates for the risk of lower global economic growth in the near future. As concerns global financial markets, the present uncertainty on financial markets is set to improve, but the condition of the economy in China is still not stable and this could kindle resurgent uncertainty on global financial markets.

Risks of uncertainty on global financial markets have eased with the narrowing of the monetary policy divergence among advanced economies, but careful watch must be maintained for risks from the continued weakness of the economy in China. The narrowing divergence in monetary policy is related to the expected gradual normalization of U.S. monetary policy alongside the continuation of Quantitative Easing (QE) policies by Europe and Japan. Normalization of U.S. monetary policy is expected to move forward in 2016, but with moderate increases in the Federal Funds Rate (FFR) in keeping with the still fragile condition of the U.S. economy. On the other hand, the QE policy maintained in Europe by the European Central Bank (ECB) is certain to remain in place until the first quarter of 2017 and may be prolonged if necessary. However, the risks in China's economy have potential to trigger a reversal of investor sentiment towards emerging markets, which could result in an increased risk premium and volatility in foreign capital inflows. Accordingly, the forecast is for appreciation in the US dollar exchange during 2016. The combination of these different factors has potential to bring pressure to bear on the capital and financial account, macroeconomic stability. and financial system stability.

Commodity prices are expected to decline further in line with the ongoing slowdown in China's economy. In the short-term, the process of rebalancing the economy in China, the world's largest consumer of commodities, will still be accompanied by slowing growth in the domestic economy that will affect demand and prices for global commodities. At the same time, world oil prices are predicted to stay weak in the short-term in the absence of significant production cuts by OPEC and non-OPEC oil exporters. The decline in oil and commodity prices is also driven by the behavior of investors who are shifting investments out of commodities and into US dollar assets. This in turn has potential to bear down on improvement in the current account.

In regard to the risk of strengthening of the U.S. dollar, the role of large foreign funds in corporate financing structures points to another risk. Corporate external debt has been on an upward trend 1since 2010, driven by inexpensive sources of global funds in line with the monetary relaxation pursued by advanced economies. Compared to other countries, Indonesia's corporate dependence on external borrowing is considerable. Corporate dependence on external debt has created a point of vulnerability in the domestic economy at a time of relatively little awareness about hedging of foreign currency liabilities in the corporate world. This condition must be watched carefully, as it could exacerbate risks for the corporate sector in the event of pressure bearing down on the rupiah exchange rate.

The launching of the ASEAN Economic Community (AEC) will create increasingly diversified challenges and opportunities for the future. Indonesia has considerable opportunity to become a manufacturing base for supplying ASEAN and global value chains. The removal of tariff barriers (free trade) will increase the total potential market and domestic products will be expected to be competitive against the products of other countries. However, if the groundwork is not laid properly to seize these opportunities, it is feared that Indonesia will simply become a target market for goods and services produced by other AEC countries.

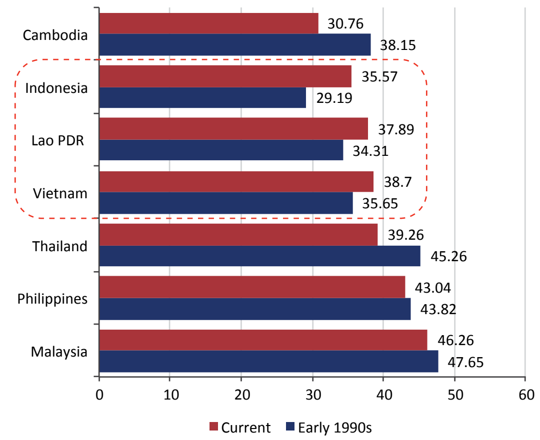
Domestic Economic Challenges

On the domestic side, reaching the target of strong, sustainable, and inclusive economic growth will still face a number of challenges. Despite relatively high average of domestic economic growth rate in the past 10 years, Indonesia is still daunted by structural problems that stand in the way of achieving potential growth. These problems include vulnerabilities in adequate supply of food, energy, and water, the imbalanced structure of industry and low productivity that has left it behind in the global value chain, the persistently shallow structure of the domestic financial market, and widening economic disparities (Chart 15.1).

Based on the policy direction of national development, four pillars of structural challenges should be prioritized for remedial action (Picture 15.1). The four pillars of development priorities are: (i) food, energy, and water security; ii) competitiveness in the maritime, industry and tourism sectors; (iii) sustainable development financing; and (iv) an inclusive economy. Essential to the remedial measures under way is support from key enablers for development, namely quality infrastructure networks with full coverage, availability of quality human resources, a conducive investment climate, and a significant role for science and technology. In addition, macroeconomic and financial system stability is also a prerequisite for building sustainable economic growth.

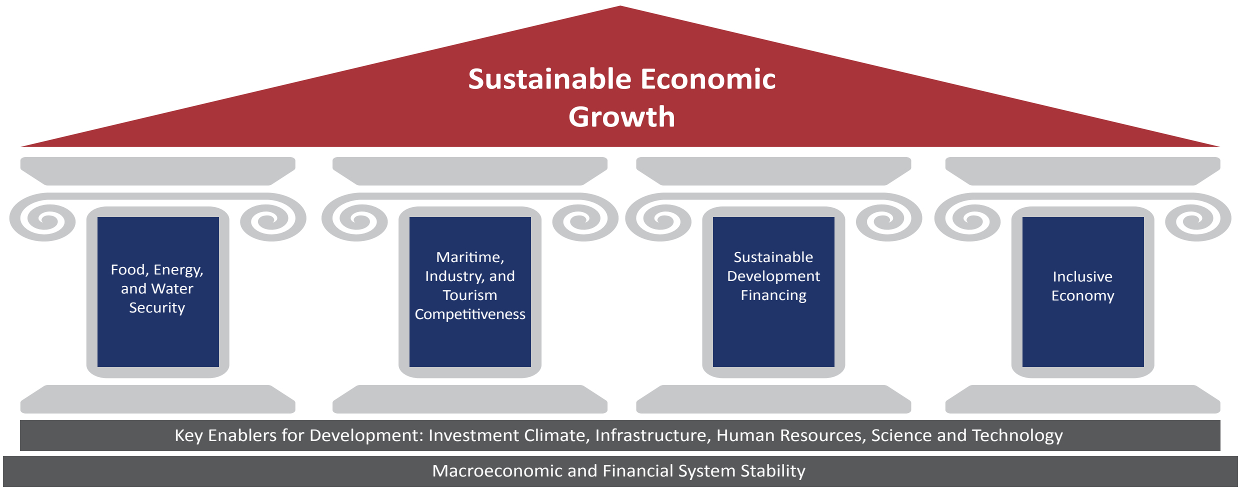
Accordingly, policy priorities will focus on creating robust structures for the domestic economy that will build a sustainable, balanced economy. Economic diversification and structural transformation will have a vital role in supporting economic growth and buttressing domestic

Chart 15.1. Gini Index of ASEAN Countries



Source: World Bank

Picture 15.1. Four Pillars of Structural Challenges



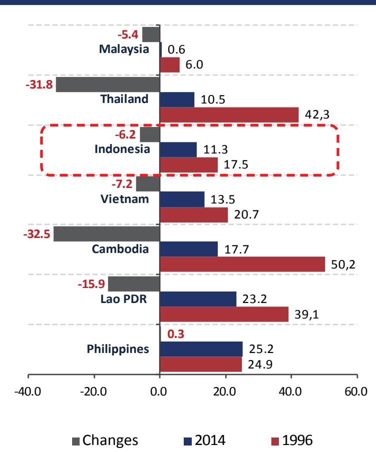
economic resilience against external shocks. Care must be taken to ensure that the economic transformation process moves forward as appropriate for each stage. The transformation will be carried out with attention to the supporting factors of the domestic economy, which include vibrant domestic consumption and a strong labor market, low, stable energy and food prices, robust water security, comprehensive infrastructure and connectivity, a conducive investment climate, growing integration into global supply chains, and diversification of export products, mainly in order to reduce dependence on primary commodities. In addition, it is vital that the low contribution of productivity, which even comes below the average for countries in the South East Asia region (Chen, 1997), is made a focus of concern in policymaking. The growing complexity of structural challenges and the slowing trend in domestic economic growth visible since 2012 underscores the urgency for implementing structural reforms. The acceleration of structural reforms is expected not only to speed up Indonesia's transition to a high income country, but also ensure sustainable and quality economic growth that will bring further reductions in levels of income disparity and poverty (Chart 15.2).

Challenges to Food, Energy, and Water Security

Security in food, energy, and water, which comprise essential human needs, represents a fundamental issue that requires resolution. The growth of the population and increase in life expectancy and incomes will require increased availability of food, energy, and water at affordable prices and in sufficient quantities. Availability and price stability for food, energy, and water, as sectors that generate production inputs, are essential to support productivity and sustainable economic growth. The steady upward trend in food, energy, and water prices in the medium-term, climate and demographic change, rising urbanisation, conversion of land use, and changes in consumption patterns are factors that need to be taken into account in boosting national production of food, energy, and water.

At this time, food security in Indonesia remains comparatively low, particularly in terms of quality and public purchasing power.[1] On the production side, the quantity and capacity of food production is becoming more limited, hampered by limitations in production inputs. This is partly related to the shrinking area of arable land caused by conversion of land use that is not adequately compensated by improvements in agricultural

Chart 15.2. Poverty Rate of ASEAN Countries



Source: World Bank

1 Based on the global food security index.

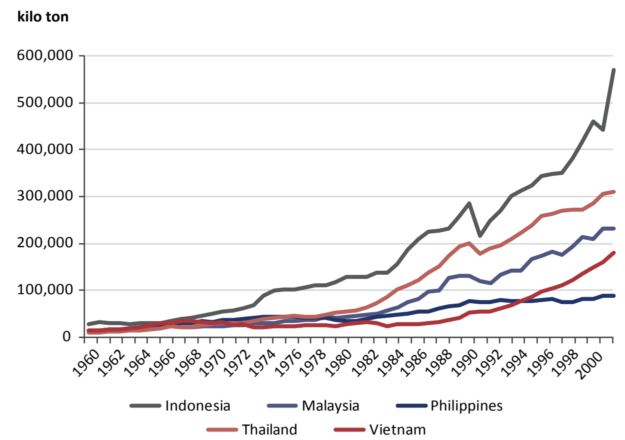
productivity and technology. During the 2006-2013 period, only 47,000 ha of new land was cleared for agricultural use each year, while land conversion for housing areas and industrial estates was moving forward at 100,000 ha per year (National Development Planning Agency, 2015). On the other hand, the steady rise in food consumption has not been matched by commensurate increases in food production.

As far as energy is concerned, while Indonesia has sizeable potential in energy reserves, the country faces the risk of substantial vulnerability in energy security. Domestic energy production is unable to keep pace with the ever-growing need for fuels. The most important problems hampering domestic energy production are obstacles to development of such infrastructure as transmission towers and power plants, in addition to the limited diversification into new and renewable energy.[2] Furthermore, the minimal use of alternatives such as biofuels means that it has not been possible to shift away from the high dependence on fossil fuel resources.[3] This is an area that demands attention, because not only will this lead to increasing scarcity of fossil fuels, but also result in environmental damage and global warming (Chart 15.3). Although the Government has introduced energy reforms, including reductions in the fuel subsidy, the high level of oil and gas imports and limited oil reserves in Indonesia will continue to burden the balance of payments (Chart 15.4). If not managed properly, the current account deficit could potentially leave the economy more susceptible to risks in the medium to long-term.[4]

Availability of water in sufficient quantity and quality is vital to the welfare and health of human beings and the environment. The strengthening of national water security represents a challenge that is faced primarily for meeting needs for consumption, food crop production, and sources of energy. The precarious condition of Indonesia's water security is primarily attributable to the low capacity for water resources management and factors affecting water resources, such as land conversion, relatively limited infrastructure for natural resources, disturbances in watersheds, and water pollution.

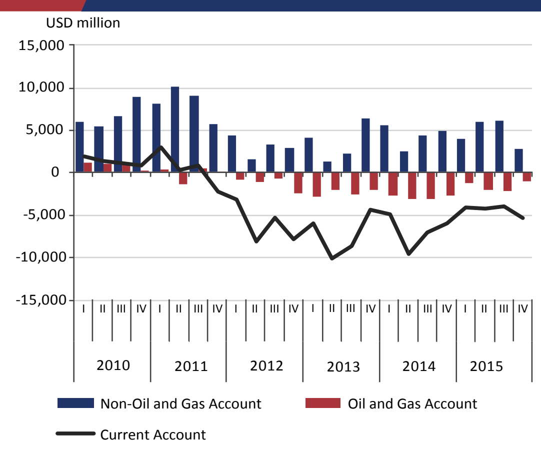
The Government has developed objectives and a policy direction to support achievement of food, energy, and water security, but so far progress is limited.[5] In keeping with efforts to meet future needs for food, energy

Chart 15.3. **CO2 Emissions in ASEAN Countries**



Source: World Bank

Chart 15.4. **Indonesia Balance of Payment**



2 The US Energy Information Association or EIA (2015) predicts world energy consumption to climb from 97.1 quadrillion Btu (2013) to 100.8 quadrillion Btu (2020).

3 Biofuel production accounts for 4.4% of total primary energy production, ranking after crude oil, coal and biomass. Biofuel is consumed in the transportation sector, where it accounts for a 22% share in comparison to 78% for petroleum-derived fuels.

4 Indonesia's emissions now stand at 523 million tons and the country ranks as the world's 9th largest producer of CO2 (World Bank, June 2015). In 2018, CO2 production is predicted to climb from 116 million to 270 million tons. Of this 270 million tons of CO2, 84.5% will be generated from burning coal. In 2015, the Government shifted fuel subsidies into productive sectors, including village funds, ship and port construction, social benefits provided through the prosperous family card and families with hope card schemes, agricultural subsidies, special allocation funds, the Indonesia health card scheme, a border fleet, maritime information and logistics system, infrastructure projects including dams, drinking water, roads and expressways, and support for school attendance under the smart Indonesia card scheme.

5 The four key thrusts of food policy in 2015-2019 are: (i) increased production, (ii) stabilization of prices and supply, (iii) improvement in the quality of food consumption and public nutrition, and (iv) dealing with disruptions to food security.

and water, the Government is aware of the necessity of remedial changes to structures and systems in the agriculture, energy and water management sectors. For the agriculture sector, remedial measures have been pursued through such actions as policy reforms, development and repair of infrastructure, crop production and post-harvest handling, and management of markets. In the energy sector, improvements to be made to energy policy include the development and use of new and renewable energy and energy conservation, management of oil and natural gas including reallocation of the fuel subsidy, provision of electricity needs, and increased value added for mining products such as coal. In water security, the Government has issued the 6th policy package that deals with sustainable and equitable provision of water for the public.

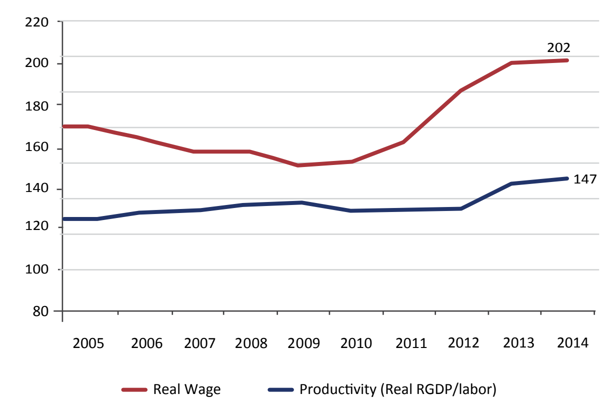
A series of policy packages launched in 2015 sent a positive signal for the direction of renewal in national development. However, it has not been possible to evaluate the success of these packages so far. In the agriculture sector, policy reforms will promote greater efficiency in labor costs and production costs, which will also be combined with higher productivity to raise output by 10%-20%. This in turn may be able to reduce dependence on imported food products, thus keeping food prices more stable and generating higher incomes for farmers.[6] In the energy sector, the development of solar-powered, micro-hydro and biomass power plants will increase availability of energy and the installed capacity of powerplants while improving the electrification ratio and primary energy mix. At the same time, exploration for oil and gas reserves and the operation of the refinery at Cilacap will reduce fuel imports and improve resilience in the supply of fuels. Water security, on the other hand, encompasses people's right to water, conservation of the environment, monitoring and control of water and the role of state in water management.

Challenges to Competitiveness in the Industry, Maritime, and Tourism Sectors

For the future, the Indonesian economy will continue to face structural challenges related to competitiveness in the industry, maritime, and tourism sectors. The strategy for the Indonesian economy cannot perpetually rely on extractive commodities, but must shift more to the competitive advantages of high value added industry. Even so, this strategy faces challenges that mainly concern productivity, diversification, technology content, and integration into the global economy. For this purpose, it is necessary to strengthen non-wage competitiveness through productivity-oriented structural reforms. This is important given that during the past decade, domestic industrial productivity has tended towards stagnation and has not kept pace with pressures for wage increases (Chart 15.5). Therefore, the national industrial development strategy, particularly for labor-intensive manufacturing, cannot depend forever on the low wage regime. These efforts to raise productivity, which constitute a non-cyclical policy, will not only strengthen economic growth in the short-term, but also bring permanent improvement in potential growth.

In the industry sector, economic development is confronted with fundamental structural challenges because the economy is based on extractive commodities with low value added and that may harm the environment, particularly in provinces outside Java. The introduction of the policy prohibiting exports of raw minerals will encourage investment in the downstream side of the mineral resources sector, particularly outside Java.[7] Nevertheless, this must be followed by productivity improvements and diversification of economic sectors to create a more competitive and productive business environment. Economic development outside Java needs to be supported by business players' self-discovery process, that is to say a process of innovation characterised by growth of new industries.[8] However, the

Chart 15.5. Comparison of Real Wage and Manufacturing Productivity (index 2000 = 100)



Source: Ministry of Manpower and BPS-Statistics Indonesia, processed

6 Savings in use of foreign exchange amounted to Rp52 trillion.

7 Based on the Investment Coordinating Board Report (2016).

8 The concept of self-discovery is found in Hausmann, R. and D. Rodrik (2002). "*Economic Development as Self-Discovery*". Economic development requires a process of self-discovery where private agents undertake risky innovations in pursuit of financial incentives. This process involves a reallocation of resources from those that are not viable to those capable of more productive growth, bringing an aggregate benefit to the economy. It is essential for public policy to create an environment that supports this self-discovery.

innovation process requires strong funding and carries the risk of failure, and therefore needs to be supported by the availability of key enablers for development. In this regard, Java is further along the road as it already has more sufficient infrastructure and a better business climate. Meanwhile, the structural reforms outside Java are aimed at strengthening internal integration for the archipelago to become a production base for the world.

Another challenge is the need to maintain the continuity of the industrialization process so that it will be able to drive the economic transformation to become an advanced economy. In Indonesia's position as an emerging market, economic growth is supported mainly by investment, natural resources and energy. As a consequence, to avoid becoming trapped in premature de-industrialization, it is important for Indonesia to catch up with the global economy through improvements in technological capability supported by expertise, improvements to the innovation system, and upgrading in global value chains. Furthermore, to maintain consistency in the policy for improving industrial competitiveness, manufacturing activities need to be structured to form individual clusters of activities supported by other sectors, such as services, trade and connectivity of logistics, energy, and quality manpower.

In regard to technology content, Indonesia's comparative advantage has been steadily eroded, particularly in sectors with medium and high technology content. The deterioration of Indonesia's export competitiveness has occurred mainly in highly dependent sectors, such as electronics and machinery, where Indonesia's export products are less sophisticated than those of regional competitors.[9] On the other hand, the products that still hold an advantage in Indonesia's exports are resource-based products and their derivatives. This is an area of concern, given greater competitiveness in medium and high technology sectors is essential to the creation of industry capable of producing high value added products to international standards. To this end, support from adequate numbers of quality personnel is also a key factor. Besides this, it is also necessary to build the competitiveness of these sectors to support a successful transition for Indonesia to an advanced economy (see Box 15.1).

Furthermore, to deal with the challenges of globalisation, including the AEC, Indonesia needs to build greater attractiveness for investment in order to become a production base supplying global value chains. Indonesia's poor competitiveness in global value chains is evident from the country's limited ability to generate value added after importing raw materials where products are subsequently re-exported to various countries. A comparison among ASEAN countries' characteristics of FDI shows that investment in Indonesia provides employment on a large scale, but is more domestic-oriented. At the same time, other countries in the region are able to attract better quality investment to promote export growth and provide jobs to skilled workers. Indonesia therefore needs to improve its attractiveness as a venue for investment for export to world markets and to take advantage of integration into global value chains in order to expand markets, harness advancements in technology, improve the quality of human resources, and promote the development of small and medium-sized industries. Issues in the quality of human resources are found nearly everywhere in Indonesia. A study by Affandi and Anugrah (2015) points to the highly significant impact from improved quality of human resources in promoting economic growth in Indonesia.[10]

The challenges confronting the maritime sector concern territorial integrity, optimization of natural resources management, connectivity, and development of a maritime economy. One of the issues concerning territorial integrity is related to maritime border agreements with neighbouring countries. While a maritime border agreement has been reached with one neighbour, in this case Papua New Guinea, there are still nine other neighbours with whom Indonesia still has to complete negotiations. In regard to natural resources management, the enormous potential of the capture and farmed fisheries sector has not been managed for optimum benefit, and therefore the scale of Indonesia's exports continues to lag behind that of other countries such as Thailand.[11] At the same time, Indonesia's problems with connectivity arising from inadequate basic infrastructure lie at the cause of poor efficiency in domestic value chains. This is explained by the better availability of power infrastructure, cargo handling ports, digital connectivity, and supporting services in the Java region compared to the maritime region of Eastern Indonesia.

Indonesia's tourism sector still faces infrastructure-related challenges that hamper access for tourists and the time they are able to spend exploring, particularly

9 Based on mapping of product space.

10 For full details, see: Affandi and Anugrah (2015), "*Strategi Pertumbuhan di Indonesia: Pendekatan Growth Diagnostic*", Bank Indonesia.

11 According to the Ministry of Maritime Affairs and Fisheries Report, as of the third quarter of 2012, growth in captured and farmed fisheries reached 5.05% and 3.98% respectively.

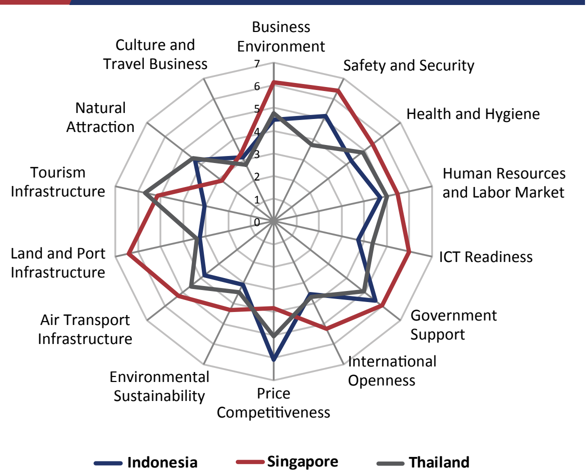
in destinations where tourists are attracted by the stunning beauty of nature. Indicators of competitiveness in travel and tourism place Indonesia in 50th place out of 141 countries.[12] In general, Indonesia still benefits from comparative advantage in terms of prices, natural attractions, and government support, but weaknesses persist in the areas of infrastructure and the supporting environment, such as in health and hygiene, technological progress, tourist facilities, and the capacity of human capital. Besides this, safety and security factors, particularly in relation to terrorism, are still matters of concern to tourists, and this has reduced the potential for domestic tourists (Chart 15.6). This is an area that must be watched closely, given that tourism not only contributes to economic growth and foreign exchange, but is also one sector of the economy capable of providing employment to surplus labor in agriculture.

Challenges for Sustainable Financing of Development

Another challenge that concerns the fundamentals of the Indonesian economy is limited capacity of long-term financing from the formal financial sector in national development. The financial services sector in Indonesia is dominated by the banking sector that has a short-term funding base, and therefore faces the risk of mismatch, while use of the capital market remains very limited. Current efforts to bolster long-term investment financing continue to be constrained by a number of structural issues. First is the high cost of capital in line with the expensive structure of banking liabilities, due to stubbornly high perceptions of risk regarding the real sector and uncertainties. Second is the sizeable portion of foreign ownership of Indonesian Government Bonds and the foreign contribution to share trading, which frequently leads to high volatility in price on secondary markets (Chart 15.7). Third is the still limited availability of long-term financing sources on the capital market, which in fact lags behind the region, as does the capacity and liquidity of Indonesia's financial market (Chart 15.8).

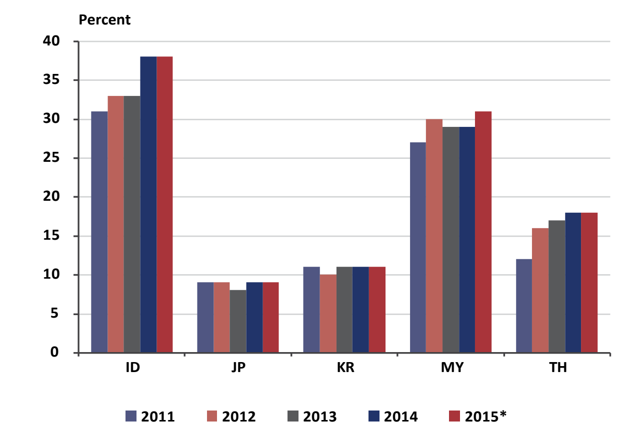
A further challenge for financing national development is the importance of promoting foreign capital inflows in the form of foreign direct investment (FDI). FDI in export-oriented manufacturing is not only a vital source of financing, but also has potential to improve the competitiveness of the relevant industry within the global value chain (Box 15.2).[13] The limitations faced in long-term financing are evident from the changes in the basic balance of the Indonesia balance of payments, which is frequently in deficit.[14] Among the most important issues hampering inflows of FDI into Indonesia are limitations in infrastructure and the slow and complicated procedures for investment licensing. The effect of this is evident in Indonesia's ratio of FDI to GDP, which comes far below that of some neighbouring countries (Chart 15.9).[15]

Chart 15.6. Comparison of Tourism and Travel Competitiveness



Source: World Economic Forum, 2015

Chart 15.7. Foreign Ownership in Government Bonds



*) as of September 2015

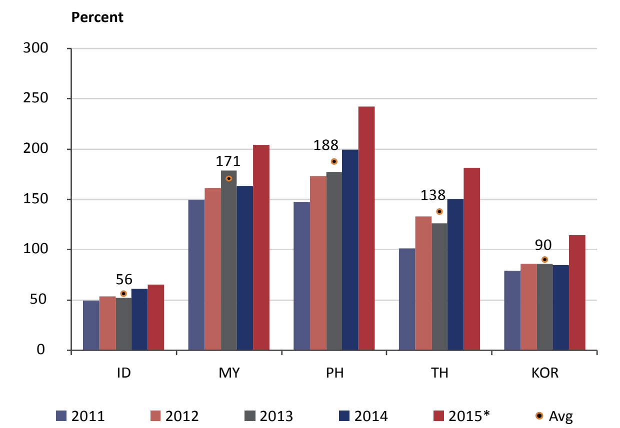
12 Based on the World Economic Forum (2015); the best rating is 1.

13 At 1.8%, Indonesia's ratio of FDP to GDP (2004-2014) is below that of peer countries such as Vietnam (5.9%), Malaysia (3.2%), Thailand (3.0%) and China (2.1%).

14 The basic balance indicates the capacity for funding the current account from long-term funding sources. The basic balance represents the sum of the current account, net direct investment, and other long-term net investment.

15 The present investment policy is guided by Act No. 25 of 2007 concerning Investment. This Act replaced Act No. 11 of 1970 concerning Foreign Investment and Act No. 12 of 1970 concerning Domestic Direct Investment. The reforms are aimed mainly at ease of investment, equal treatment of foreign and domestic parties and provision of legal certainty.

Chart 15.8. Market Capitalization



*) as September 2015

According to data for the past five years, investment has been dominated primarily by the manufacturing sector (Table 15.1), but without focus on export-oriented industries.

Challenges for an Inclusive Economy

The Indonesian economy faces other challenges with stubbornly high disparities in development and lack of equity for the public in participation and reaping the benefits of economic growth. Indonesia's buoyant economic growth at 5.8% over the past five years has not been sufficient for Indonesia to gain entry to the group of upper middle income countries. Although economic gains have reduced the poverty ratio and unemployment levels, this has not brought equitable improvement as reflected

Chart 15.9. Ratio of FDI to GDP

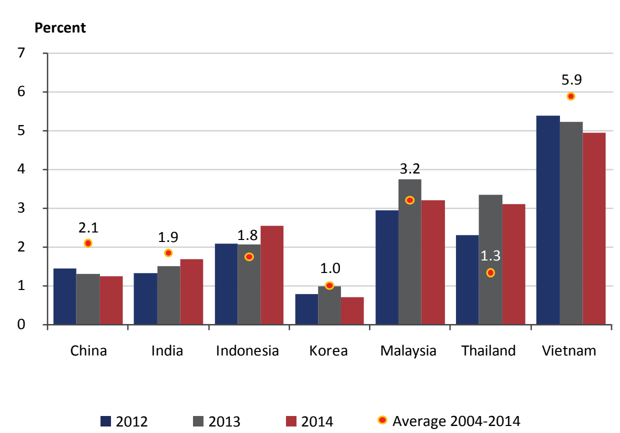


Table 15.1. Share of Investment by Sector

Percent

	2010	2011	2012	2013	2014	2015*
Manufacturing Industries	36.1	42.5	46.7	45.3	34.6	26.0
Mining and Quarrying	13.8	17.8	9.5	13.2	13.5	10.9
Transportation, Warehousing, and Communication	17.4	13.9	15.8	10.4	8.6	8.3
Agriculture	2.1	1.3	6.3	10.1	17.3	32.3
Trade	17.9	12.9	6.5	5.2	8.6	10.7
Financial Intermediaries	3.0	5.2	5.4	2.7	6.8	5.3
Others	8.1	-0.3	3.9	4.3	2.3	4.3
Real Estate and Business Services	0.2	3.0	4.3	4.6	5.9	2.5
Electricity, Gas, and Water	1.5	2.1	1.5	1.9	1.1	-2.3
Fishery	0.4	0.4	0.4	0.4	0.6	1.3
Construction	-0.4	1.7	-0.4	1.8	0.6	-0.1
Health and Social	0.0	0.0	0.0	0.0	0.0	0.7
Government Administration	0.0	0.0	0.0	0.0	0.0	0.0
Education	0.0	0.0	0.0	0.0	0.0	0.0
Hotels and Restaurants	0.0	0.0	0.0	0.0	0.0	0.0
Community Services, etc.	0.0	-0.4	0.0	0.0	0.0	0.0

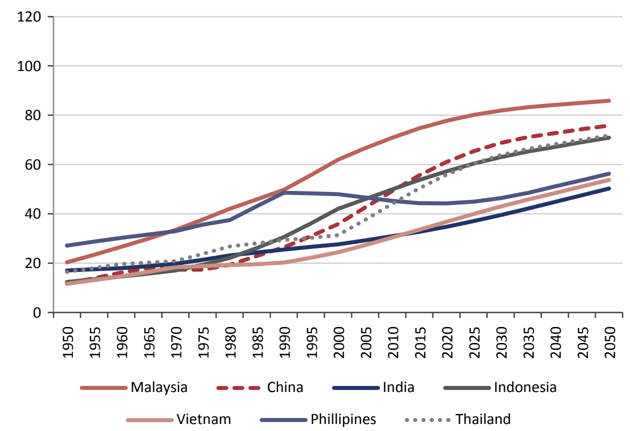
*) as of the third quarter of 2015

in steady rise in the Gini ratio, particularly in Eastern Indonesia. The World Bank (2012) reported that 30 million or 40% of people living in Indonesia are at risk of falling below the poverty line, particularly in the event of food price shocks.[16]

The gap between rural and urban development has led to formation of centers of growth and agglomeration that ultimately fuels migration from rural communities to urban areas (Chart 15.10). With the high rate of urbanisation, it is estimated that 70% of the population will be living in urban areas by 2050 (United Nations, 2012). To address this, policy support is essential, particularly in provision of infrastructure and business climate that supports job creation and a proper living conditions. The minimum provision of quality infrastructure represents one of the most important challenges in promoting economic growth (Chart 15.11), while geographical disparities also exist in community access to basic needs such as education, health care, clean water, electricity, sanitation, telecommunications, and housing. Most affected in all this is Eastern Indonesia. A similar situation exists in the

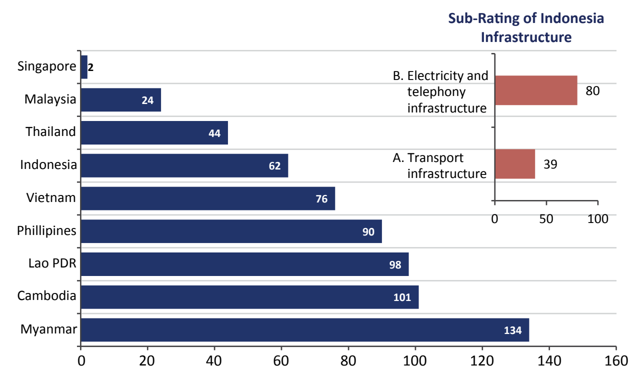
16 As many as 14.3% of the rural population live below the poverty line, significantly higher than the 8.4% of urban dwellers living in poverty (Vujanovic, 2015).

Chart 15.10. Urbanization Level of Asian Countries



Source: United Nations

Chart 15.11. ASEAN Infrastructure Rating



Source: World Economic Forum 2013

financial sector, where access to financial services for people from various income levels in society and living different regions is not inclusive nor available on an equitable basis.

Challenges in Key Enablers for Development

In strengthening the fundamentals of the economy, Indonesia still faces structural challenges related to the key enablers for development, and in particular infrastructure, human resources, and science and technology. Related to infrastructure development, Indonesia needs to sustain the momentum for structural reform by maintaining the credibility, effectiveness, and speed of policy implementation.[17] In the short-term, credibility may influence the behavior of economic agents through their expectations, thus encouraging consumption and investment. Similarly, effectiveness and speed may influence the extent of improvement in potential economic growth.[18] To achieve greater effectiveness, structural reforms also need to take account of development priorities.

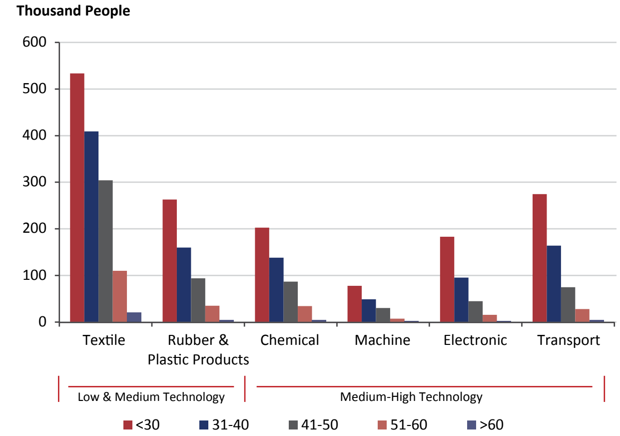
According to the growth diagnostic approach, the most important hindrances to the economy in almost every region of Indonesia are rooted in problems with electricity infrastructure, connectivity, and quality of human resources.[19] Electricity is needed to meet the considerable energy needs for industry in Java and the unmet needs of households and industrial users outside Java. Infrastructure for connectivity, such as ports and roads, are essential to bring down the logistics cost in domestic value chains, strengthen internal integrity, and improve competitiveness and thus pave the way for the entire archipelago to become an export-oriented manufacturing zone. Outside Java, quality of infrastructure is crucial to bring a more competitive business environment in order to promote economic diversification (see Box 15.2). Regarding human resources, it is necessary to increase the numbers of available qualified workers and improve school participation in rural areas. Although Indonesia has gained demographic bonus in terms of working age population, the majority of the workers have completed only primary and secondary school education (Charts 15.12 and 15.13). On the other hand, reinforcing the economic structure in medium-high technology sectors will require large numbers of workers with higher levels of education or skills. As of now, Indonesia still has to deal with a substantial gap in the quality of education of the workforce, as reflected in the PISA scores in science and mathematics that lag considerably behind those of other countries in Asia (Table 15.2). Furthermore, the pace of Indonesia's transformation into an industrialised country must also be supported by improved agricultural productivity in rural areas, particularly in reaching the target of food self-sufficiency. Lower educational levels in rural areas may hamper efforts to improve productivity, and it is therefore necessary to improve school participation in rural areas, particularly in secondary and

17 Credibility means results achieved according to plan, while effectiveness is the percentage of achievement and speed is the time taken for development.

18 The concept of credibility, effectiveness and speed is elaborated in Santoro, M. 2015. *Long-term Gain, Short-Term Pain: Assessing the Potential Impact of Structural Reforms in Chile*. IMF Working Paper.

19 In 2015, Bank Indonesia conducted a Growth Diagnostics study for 11 provinces. For full details, see Box 15.2.

Chart 15.12. Total Employment by Age



Source: The National Labor Force Survey , 2014[20]

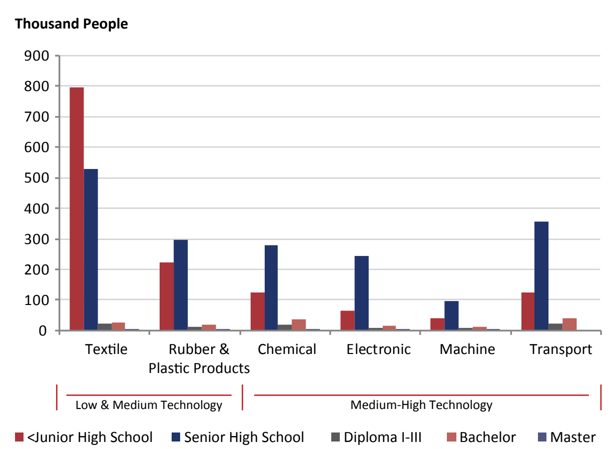
Table 15.2. PISA scores of Several Countries in Asia

Countries	Science	Mathematics
China	613	570
Hong Kong	561	545
Singapore	573	542
Japan	536	538
South Korea	554	536
Taiwan	560	523
Thailand	427	441
Kazakhstan	432	393
Indonesia	375	396
Average in Asia	613	570
Average in OECD	561	545

tertiary education. Balanced levels of productivity between the rural and urban population will have a positive impact in reducing poverty and creating more inclusive economic growth.

Institutional reforms are urgently needed to support improvement in the business climate in order to be globally competitive and to attract investment. The indicator for ease of doing business shows that Indonesia has improved its ranking in this area from 120 (2015) to the 109th place (2016). This positive achievement is explained mainly by improvements in tax payments, construction permits, and access to credit. However, improvements are still needed regarding some issues: (i) time, costs, and procedures in starting a business; (ii) time required and mechanism for tax payments; and (iii) time and costs for processing property registration. In addition, issues related to ease of doing business also arise in the areas of legal certainty, construction permits, and trade facilitation. In trade facilitation, lengthy times and high costs incurred in export-import processing result mainly from hindrances to onshore access and the loading and unloading processes in port. Another aspect that demands attention is the streamlining of bureaucracy and management of government that is oriented towards public services and clean governance.

Chart 15.13. Total Employment by Education



Source: The National Labor Force Survey, 2014[20]

20 Classification of sectors by low, medium and high technology is based on the OECD Technology Intensity Definition (11).

Challenges in Reinforcing Macroeconomic and Financial System Stability

The creation of macroeconomic and financial system stability is a fundamental factor in accelerating structural reforms and providing assurance of sustainable economic growth. The globalisation trend that is fostering a progressive integration of national economies into the global economy can take place through three mechanisms: increasingly competitive trade, global supply chains involving multinational production, and integration of financial markets. To this end, a strong and stable macroeconomic structure represents a prerequisite for strengthening the resilience of the domestic economy, particularly in coping with various shocks arising at home and abroad. For the future, the risks of domestic economic slowdown and lack of equilibrium in the global economic recovery represent concerns that call for vigilance. For this reason, macroeconomic stability must be managed so that market expectations can be guided by inflation target and exchange rate stability. However, these measures are daunted by formidable challenges, particularly with the still high price fluctuations for some food commodities, risk of capital reversal, and the prolonged decline in world commodity prices. For these reasons, coordination of fiscal and monetary policy supported by structural reform policies is essential among other efforts for bolstering macroeconomic stability. This will be done through strengthening of the functions of the capital market and money market, the labor market, the market for goods and services, and also the economic sectors.

Financial system stability also faces daunting challenges, particularly in view of the growing integration of Indonesia's financial system and trade. To support the realization of macroeconomic and financial system stability, efforts must be continued to strengthen macroprudential polices and activities for surveillance of the financial system. These policy responses concerning financial system stability were also pursued in synergy with monetary and payment system policies, as part of the coordination among Bank Indonesia, the Government, and other related authorities. On the other hand, financial system stability must also be supported by equitable availability and provision of rupiah cash in the needed denominations in each region. The highly variability of quality of money, particularly in remote areas and the outermost islands of Indonesia, combined with limited capacity to supply rupiah cash in the needed denominations, poses challenges that must be addressed, and this has become a focus of Bank Indonesia policy. Meanwhile, the increased circulation of counterfeit money in 2015 presents Bank Indonesia with a challenge to maintain credibility and confidence in the rupiah currency as legal tender in Indonesia.

15.2. POLICY DIRECTION

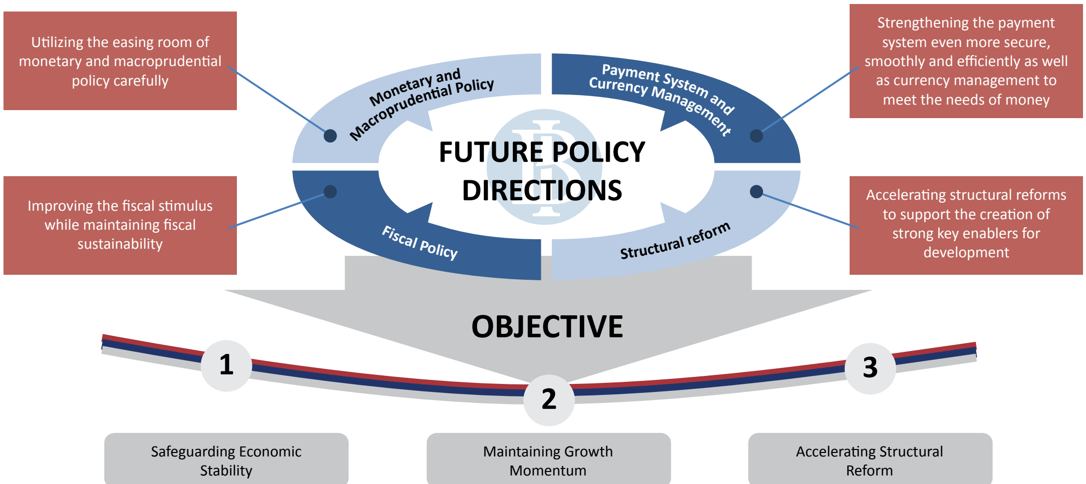
Looking ahead, it is necessary to stay alert to a range of external and domestic challenges to avoid adverse impact on Indonesia's economic performance. To this end, there will be further strengthening of the policy synergy between Bank Indonesia and the Government. The policy mix will focus on safeguarding macroeconomic and financial system stability and bolstering momentum for economic growth to enable achievement of sustainable economic growth in the medium and long-term (Diagram 15.1). From Bank Indonesia's side, the policy mix will be aimed at macroeconomic stability and prudent use of the available room for relaxation of monetary and macroprudential policies. On the Government side, policy will be aimed at providing a further boost to the present economic growth momentum. In addition, the Government and Bank Indonesia will continue work to accelerate structural reforms for the creation of robust foundations for the economy in support of sustainable economic growth.

Bank Indonesia Policy Mix

Bank Indonesia will continue to strengthen the mix of monetary policy, macroprudential policy, and payment system and rupiah cash management policy to protect macroeconomic stability and prudent use of the available room for relaxation of monetary and macroprudential policies. In the monetary sector, Bank Indonesia will work consistently and prudently in applying interest rate, statutory reserve requirement and exchange rate policies to steer inflation in line with the target, manage the current account deficit at a prudent level, and support the momentum created for economic growth. Within this framework, the direction of interest rate policy is to manage inflation expectations and domestic demand while supporting exchange rate stability to be aligned to fundamentals. This policy is consistent with the goal to achieve the inflation target and a sound current account deficit while supporting the ongoing momentum for growth. The reserves requirement policy will be calibrated prudently at all times to support adequate levels of liquidity that commensurates with the needs of the economy while paying close attention to macroeconomic and financial system stability. Exchange rate policy will continue to focus on maintaining stability in the rupiah in line with the value of fundamentals. These measures for stability of the rupiah are crucial to support achievement of the inflation target and maintenance of financial system stability and will thus improve the overall performance of the economy. To strengthen the effectiveness of monetary policy, Bank Indonesia will continue to strengthen both rupiah and foreign exchange monetary operations. These various policies will be progressively supported among others through prudent management of foreign exchange flows and reinforcement of the international financial safety net through collaboration with the various authorities that hold a stake in monetary policy and stability of the international financial system.

In the area of macroprudential policy, Bank Indonesia will pursue strategic actions to strengthen the macroprudential policy framework. First is to define more precisely the functions, duties, and powers for Bank Indonesia in financial system stability. Second, Bank Indonesia will keep coordinating with the Financial Services Authority (OJK) to improve banking capital resilience, safeguard adequate levels of liquidity, and deepen the financial market. Third is to promote equitable distribution of

Diagram 15.1. Framework of Policy Mix in Managing Indonesia's Macroeconomic



growth in credit and deposits in the regions through improvements to the bank intermediation function at the national and regional level. Fourth, Bank Indonesia will collaborate with OJK to keep expanding the role of the sharia-compliant economy and financial system within the Indonesian economy. This will be pursued in part through development of sharia-compliant monetary instruments and financial instruments.

Bank Indonesia will also continue efforts for financial market deepening to improve financial market resilience to shocks and strengthen the market role as an efficient source of financing. Efforts for financial market deepening will be reinforced by building a common vision among different authorities, with particular focus on supporting economic financing. For this purpose, the Coordinating Forum for Development Financing through the Financial Market will be established by the Ministry of Finance, OJK, and Bank Indonesia. This forum will be important to efforts for market deepening and will have the tasks of preparing policy proposals and recommendations for each authority in promoting financial market deepening and expansion. The three authorities are now at the stage of finalising a MoU.

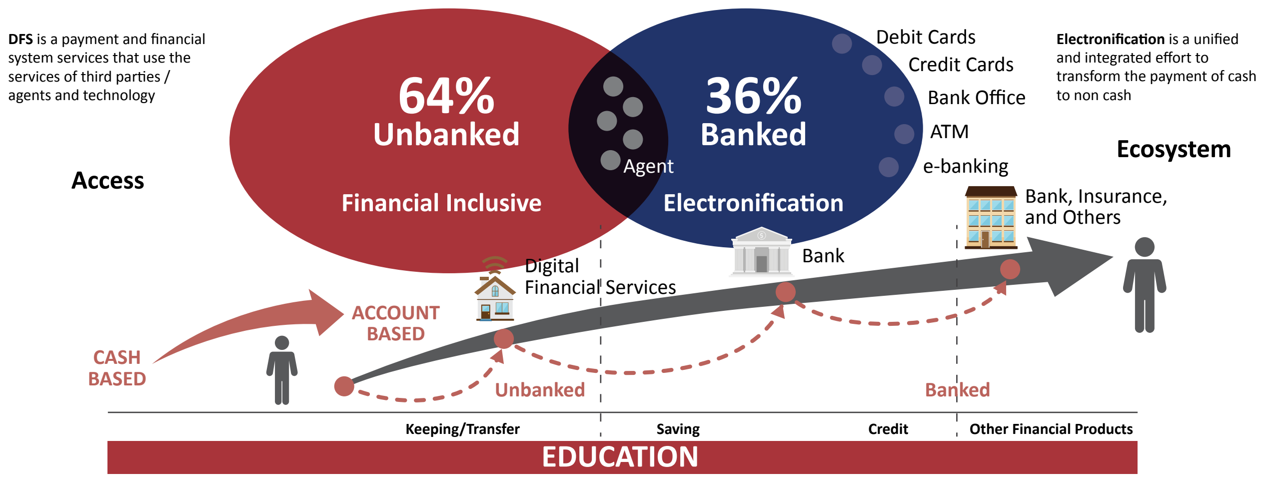
Another important iniatitive is information dissemination and education for all market participants, which will be carried out on a continuous basis in the future. Not all business players share the same vision for the financial market; instead, some opt for very conservative behavior by relying only on self-financing to expand their business. Improvement of financial literacy has become highly important to efforts to expand and deepen the financial market. In this regard, there will be comprehensive and integrated planning of public dissemination, coordination and education programs, which will be undertaken not only with market participants, but also law enforcement, arbitration, auditors, and other relevant agencies.

Efforts will continue with the policy for expanding financial access to support the creation of financial system stability, efficiency in the economy, and inclusive, sustainable economic growth. Bank Indonesia will work on building synergy between the policy for expansion of access with focus on the development of Digital Financial Services (DFS), which serves as a point of access, and the policy for electronification, which creates an ecosystem for DFS (Picture 15.2).[21] This synergy is being pursued because of the awareness that the effectiveness of increasing financial access will be inadequate if conducted through the distribution system alone, in the absences of social adaptation to the ways of using payment services. One form of applying the synergy of this strategy is in Bank Indonesia's efforts to encourage and facilitate the non-cash disbursement of Government assistance, a measure it believes will bring significant improvement in financial inclusion in Indonesia.

Efforts to improve financial access are focused on development of innovation-based digital technology, use of electronification, and innovation of retail payments in financial technology. Development of digital technology-based innovations will be steadily expanded, particularly to resolve the problem related to the lack of bank branches in rural and remote areas. Meanwhile, development of the electronic payments ecosystem will take place by

21 Electronification includes all measures for non-cash processing of retail transactions.

Picture 15.2. Dual Policy



introducing the concept to communities and industry actors as well as in cooperation with the Government. On the other hand, retail payment innovations are needed as an engine for driving the payment system in Indonesia and are therefore expected to promote the use of e-payments in Indonesia and deliver a positive contribution to the economy.

Bank Indonesia will also work continually to promote MSME development through expansion and deepening of the financial infrastructure and building MSME capacity. This will be achieved by increasing MSME financial capacity and access to the banking system through cluster development implemented in an empowered growth approach and by financing in a commercial approach. A key area of attention is ease of access to financial services for MSMEs, including use of the warehouse receipt system, capacity building involving training in recording of transactions and in preparation of financial statements with the use of information technology (smart phones). Furthermore, in order to strengthen the policymaking basis for improving access to financial services, Bank Indonesia will conduct studies related to access to sharia-compliant financial services for certain communities currently not reached by banking services, such as Islamic boarding schools.

For the payment system, the direction of Bank Indonesia policy will remain focused on the regulation and safeguarding of a secure, efficient, and smoothly operating payment system. Bank Indonesia will keep making refinements to a more comprehensive blueprint for the Indonesia's Payment System while considering future trends of payment system both in domestic and on the global level, as well as trends in other payment system-related sectors such as banking, the capital market, information technology, telecommunications, e-commerce, financial markets, financial inclusion, and international best practices. Besides this, the capital market has a steadily expanding role in the domestic economy, and policy direction will therefore focus on ensuring security and smooth operation of transaction activity and settlement, among others by implementation of Central Bank Money (CeBM). Nevertheless, it should be noted that the development of various payment system service innovations (internet, smart phones, Near Field Communication) also has potential to exacerbate risk in various forms, such as operational risk, liquidity risk, and legal risk. It is essential for these risks to be mitigated without obstructing the pace of innovation. This mitigation will require regulation of the infrastructure for processing of payment transactions and encompasses governance, implementation of risk management, prudential principles, and security in the operation of the processing infrastructure for payment transactions.

In the area of rupiah cash management, Bank Indonesia faces complex challenges in achieving the mission of ensuring that rupiah currency needs are met in terms of adequate amounts, appropriate denominations, timely availability, and proper quality throughout the territory of Indonesia. To this end, measures include strengthening of policy coordination with the Government, improvements to rupiah cash processing, and expansion of cooperation with industry. The governance aspect has also been strengthened by: (i) forging closer cooperation with the Government for refinement of policy for multi-year planning of rupiah currency printing and minting; (ii) strengthening of the infrastructure for rupiah currency management through modernisation of rupiah cash processing equipment at all Bank Indonesia offices; (iii) expansion of the role of banks and business enterprises through provision of incentives to the industry operating in remittances and cash services for the banking system and the public; and (iv) mitigation of risks in multi-year planning of currency printing and minting, such as mitigation against the dynamics of macroeconomic indicators, changes in prices and quality of currency materials, and medium-term supply of raw materials. In addition, measures will be taken to strengthen the system for supervision of banks holding cash stocks for distribution and regulation of commercial entities providing rupiah cash management services.[22]

Fiscal Policy

In the midst of the economic slowdown and uncertainty in the financial sector on a global scale, fiscal policy has gained an increasingly important role in turning the wheels of the Indonesian economy. Any weakening of the global economy, fall in commodity prices and declining performance of the domestic economy will put pressure on government revenues and reduce fiscal space.[23] To address this, measures are needed to optimie fiscal policy by directly delivering an economic stimulus through disbursement of government expenditures as well as implementing various structural policies. The Government has therefore launched a series of policy packages to strengthen the fundamentals of the economy and support domestic economic resilience. These policy packages are aimed at increasing production capacity and strengthening competitiveness, improving fiscal resilience, safeguarding the implementation of development priority programs and controlling fiscal risks and safeguarding fiscal sustainability in the medium to long-term.

In the short-term, the Government aims to increase production capacity and competitiveness and to promote the implementation of development priorities with use of the fiscal stimulus. In moving forward with these government measures, there will be inevitable challenges, including limitations of fiscal space and shortcomings in budget absorption accompanied by a tendency for build-up at the end of the year. To overcome these challenges, it is necessary to work for efficient and quality management of the budget in terms of revenues, expenditures, and financing of the state budget.

Concerning revenues, the Government focus on revenue enhancements is directed toward policies for tax revenues and non-tax revenues. Tax revenues will be optimized without disrupting the investment climate and the stability of the economy, while maintaining public purchasing power, strengthening the competitiveness and value added of national manufacturing, and also curbing the consumption of goods subject to excise. In addition, targets for taxation receipts will be achieved under an extra efforts policy with the following actions: (i) optimizing audits with focus on individual high-performing sectors, transfer pricing and fraud; (ii) broadening of the tax base and intensification of tax receipts through measures to optimise use of IT, e-tax invoices and improvements to regulations; and (iii) campaigning 2016 as the year of law enforcement.

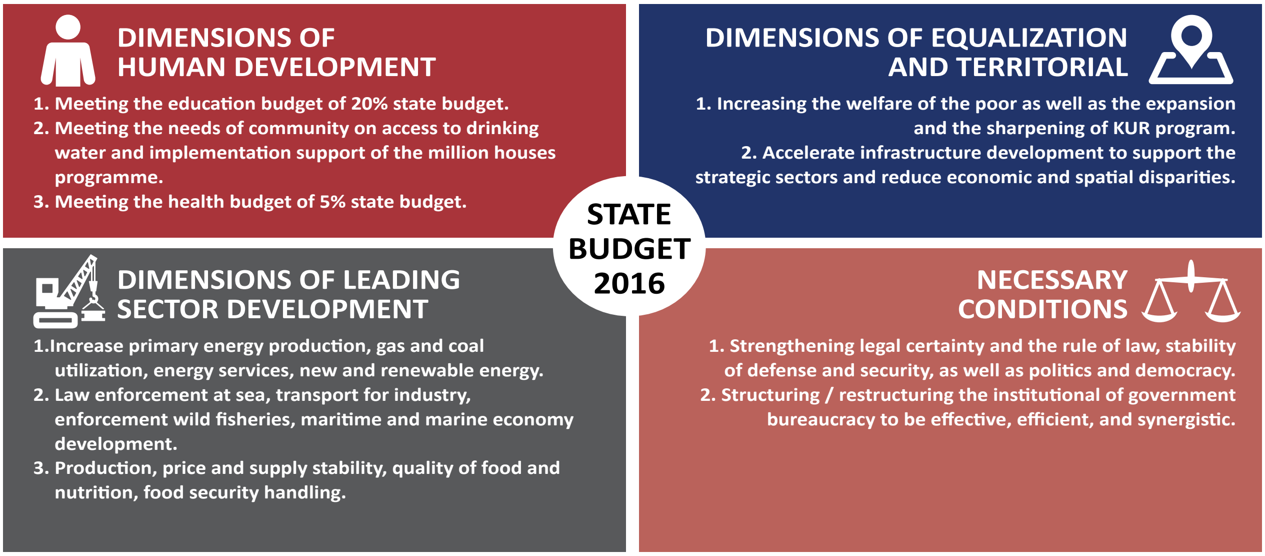
The focus of central government expenditures in the 2016 State Budget encompasses the three dimensions of development and one prerequisite for development to take place (Picture 15.3). The human development dimension is an elaboration of Nawa Cita (nine priority programs) and covers improvements to the quality of human lives through education, housing, drinking water, sanitation, and health care. The dimension of development in leading sectors consists of improvements in productivity and international market competitiveness as well as economic self-reliance, to be achieved by promoting activity in the strategic sectors of the domestic economy. The development priorities are food sovereignty, energy and electricity sovereignty, the maritime, tourism and industry sectors, and science and technology. The aim of the dimensions of equity and regionalization is to improve quality of life through equitable incomes and reductions in development disparities among regions. Besides this, support for continuity of development requires support from legal certainty and law enforcement, security and order, politics and democracy, and governance and bureaucratic reforms. As concerns state expenditures, the Government is striving to enlarge the fiscal space by optimising revenues, further efficiency measures for subsidies and expenditures, control of earmarking and mandatory expenditures, and the strengthening and harmonisation of fiscal decentralization.

Reforms in energy subsidies have been introduced by reallocating energy subsidies to more productive expenditures, consisting of food subsidies, People

22 Regulation of these commercial entities comprises part of the transformation of Bank Indonesia. In general, these regulations will provide guidelines on rupiah cash distribution, rupiah cash processing that includes counting, sorting and packaging, cash in safe, cash replenishment in ATMs and collection of rupiah cash at CDMs, the latter two including monitoring the adequacy of rupiah cash held in ATMs and/or CDMs.

23 Under Act No. 17 of 2003 concerning Government Finances, the fiscal deficit is restricted to no more than 3% of GDP.

Picture 15.3. Coverage Plans of Bank Indonesia Cash Services in 2019

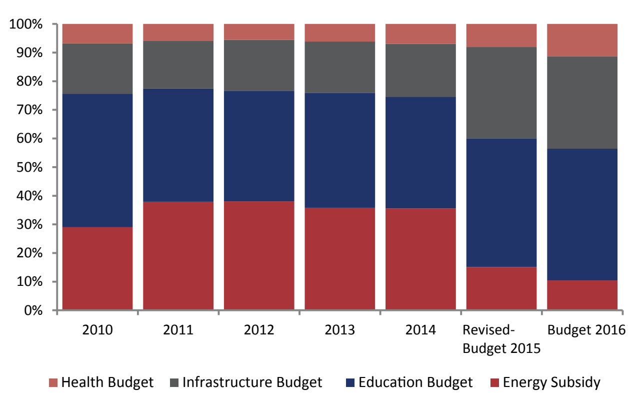


Business Credit program (KUR) subsidised loans, seeds, and Public Service Obligations (Chart 15.14). This policy was subsequently revised in early 2015 by implementing a fixed subsidy scheme for automotive diesel and premium-grade gasoline. These reforms will be continued in 2016, in particular for electricity rates and bottled LPG prices, for even more efficient and appropriately targeted channelling of subsidies, and for reallocation of budget resources to more productive expenditures in infrastructure, education, and health (Chart 15.15). In addition, the direction of fiscal policy will also be aligned with efforts to develop leading sectors and promote equity and regionalization.

Structural Reform Policies

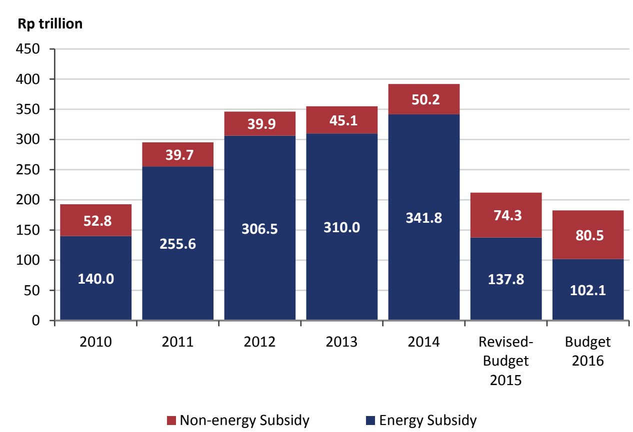
During 2015, the Government launched a number of policy packages for strengthening the fundamentals of the Indonesian economy. Even so, there is still room for improvement by complementing these measures with other structural policies (Chart 15.4). The policy packages generally focused more on enhancing industrial competitiveness and growth, improving the investment climate, development of infrastructure, and development of MSMEs. There were relatively few policies devoted to food and energy or to sustainable financing. Although it is premature to evaluate the impact of these policy

Chart 15.14. Comparison of Energy Subsidy, Education Budget, Infrastructure, and Health



Source: Ministry of Finance

Chart 15.15. Developments of Government Subsidies



Source: Ministry of Finance

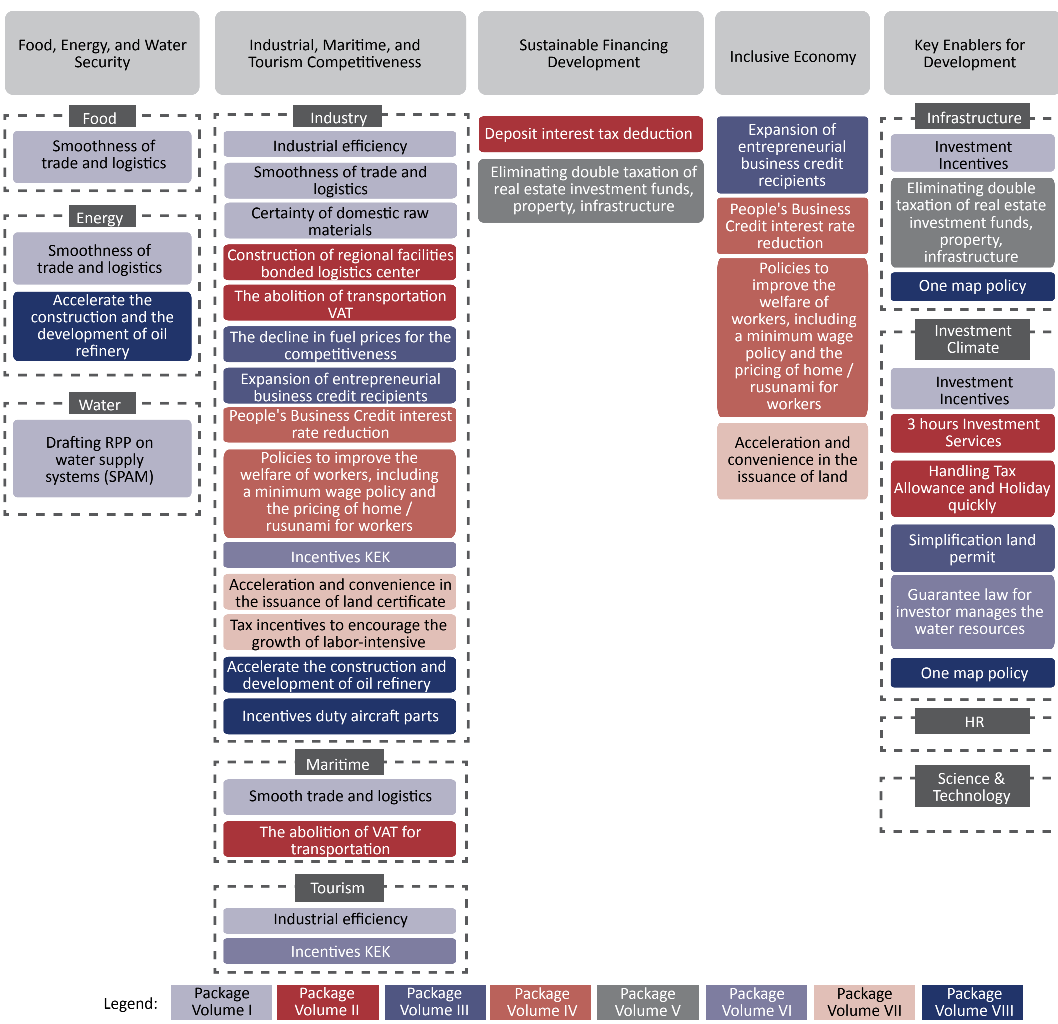
packages, positive signals and trends are emerging from developments in investment and economic growth. For this, the structural reform agenda needs to be taken to a higher level, particularly in responding to related structural issues such as food, energy, and water security, improving the competitiveness of the maritime industry and tourism, sustainable development financing, a more inclusive economy, building stronger human resources, and mastery of science and technology.

The different policy packages seek primarily to strengthen productivity and efficiency in order to improve competitiveness. For food staples, the development policy is essential to respond to the challenge of raising productivity. Regarding energy, there is still a need for policies targeting increased production and efficiency. For industry, the thrust of policymaking is to improve competitiveness, productivity, and technology content. In the maritime sector, the policy direction must aim for strengthening territorial integrity, management of natural resources, connectivity, and economic advancement. The tourism sector is in need of policies aimed at strengthening infrastructure, tourism facilities, and human capacity. Support from sustainable financing requires a policy for expanding long-term funding from domestic and foreign sources. For an inclusive economy, the policy thrust must aim for equitable development and financial access. Regarding human resources and science and technology, policies are needed that will support Indonesia’s success in transitioning to a high-income country.

Strengthening Food, Energy, and Water Security

The vast potential of the agriculture sector has not been harnessed for optimum benefit, and therefore cannot yet undergo transformation to become a source of prosperity and welfare for the people of Indonesia. The agriculture sector still accounts for a relatively small share of the GDP, despite being the source of livelihood for a major proportion of Indonesians (34%), most of whom are

Picture 15.4. **Map of Government Policy Packages in 2015**



classified as poor households. To address low productivity and various problems in production, distribution and marketing, in addition to institutions and policy, comprehensive reform of structural policies is essential. The focus on achieving food security is primarily about increasing production to achieve self-sufficiency, bolstering the stabilization of prices and supply, improving the quality of consumption and nutrition in society, and dealing with disruptions to food security, as set out in a number of policy programs. These programs cover areas including the opening of new land for cultivation, repair and construction of irrigation systems, construction of markets and transportation infrastructure, restoring soil fertility, expansion and construction of warehouses with adequate facilities, development of agricultural and MSME banks, capacity building for farmers, development of grassroots agribusiness, control of food imports and reform of land management regulations.

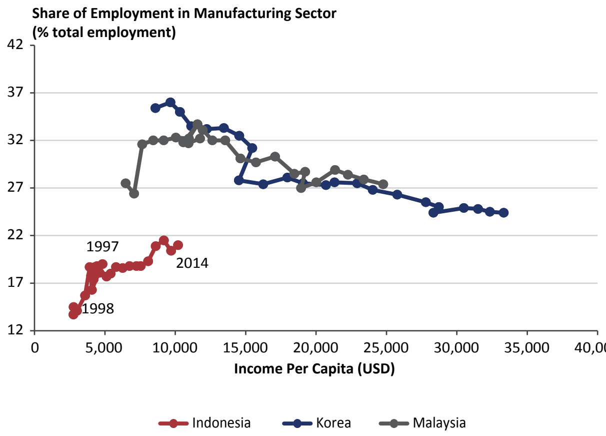
To bring about energy security, the thrust of policy focuses on four priority areas: increased production and reserves of extractive energy, improvement in the energy mix, expanded accessibility and greater efficiency in use of energy and electricity, and more transparent and targeted management of fuel subsidies. The urgency of resolving national energy problems is described in the 2015-2019 Medium-Term National Development Plan (RPJMN), in which energy and electricity sovereignty is among the 7 priorities of the Nawa Cita priority programs for achieving economic self-reliance by generating momentum in the strategic sectors in the domestic economy. Energy sovereignty is a goal for the energy and mineral resources sector. The targeted government revenues from this sector are Rp1,994 trillion, while total investment and funding in energy and mineral resources is targeted at USD273 billion with Rp71.5 trillion to be funded from the state budget. To improve national water security, Government policy has been integrated into conservation of water resources. Policy actions in this area include construction of water reservoirs, improved access to drinking water and sanitation, development of water conservation infrastructure, protection of natural water resources, and expansion and rehabilitation of irrigation systems.

Improving industrial, maritime, and tourism competitiveness

In responding to the challenge of competitiveness in the industry, maritime, and tourism sectors, the Government will focus on implementing a series of development strategies. Industry policy will concentrate on industrial development outside Java, expanding the industry population, reinforcing integration in global value chains and improving competitiveness and productivity. Development of industrial areas outside Java will take place through facilitation for development of industrial estates, centers for small and medium-scale industry, supporting infrastructure for industry and facilities to support the quality of life of personnel. Expansion of the industry population will involve promotion of investment in the downstream development of resource-based industries to meet consumption needs on the domestic and export markets, provide employment on a large scale and integrate into global value chains. The Government will also extend support for small and medium industries to become affiliated with large-scale manufacturing linked to global value chains. To promote competitiveness and productivity, the Government will improve technical efficiency, encourage mastery of science and technology and the art of innovation, and promote higher levels of qualifications in human resources as a part of the labor reform in Indonesia. This also requires the involvement of foreign investors through FDI in expanding the industrial base and improving productivity as part of a comprehensive strengthening of the industry structure in Indonesia. To this end, the Government will take further steps with the institutional reforms already in place to improve legal certainty and bureaucratic efficiency in support of efforts to strengthen Indonesia's industrial competitiveness. The principal strategy is to move through the process for catching up with high income countries by increasing the participation of Indonesian manufacturing in global value chains. This will be supported by improvements in the basic capital for investment, provision of basic capital for development and implementation of a strategy for accessing the global market. The policy direction in support of greater industrialization requires sustained momentum in view of the slowing growth in per capita income in Indonesia due to the limited proportion of Indonesian labor employed in the industry sector (Chart 15.16).

Programs to be undertaken for the maritime sector include strengthening of maritime sovereignty, eradication of illegal fishing, development of national connectivity, and development of a maritime and marine economy. The Government will reach a resolution on marine borders and register small islands with the UN, regulate and control the Indonesian Archipelagic Sea Lanes (ALKI), and bolster marine surveillance and security. Illegal fishing will be curbed by increasing the number of days of coastguard operations and aerial surveillance. Development of national connectivity will involve the expansion of 24 strategic ports to support the nautical highway system and the maritime axis program (Picture 15.5), provision of pioneer routes and vessels, construction of passenger

Chart 15.16. **Investment Incentives**



and cargo vessels for pioneer routes, and revitalisation of dockyard industry locations. Development of the maritime and marine economy will take place through expansion of fishing fleets, particularly of high-tonnage vessels, development of integrated marine and fisheries areas and hatcheries, and development of fish farming areas.

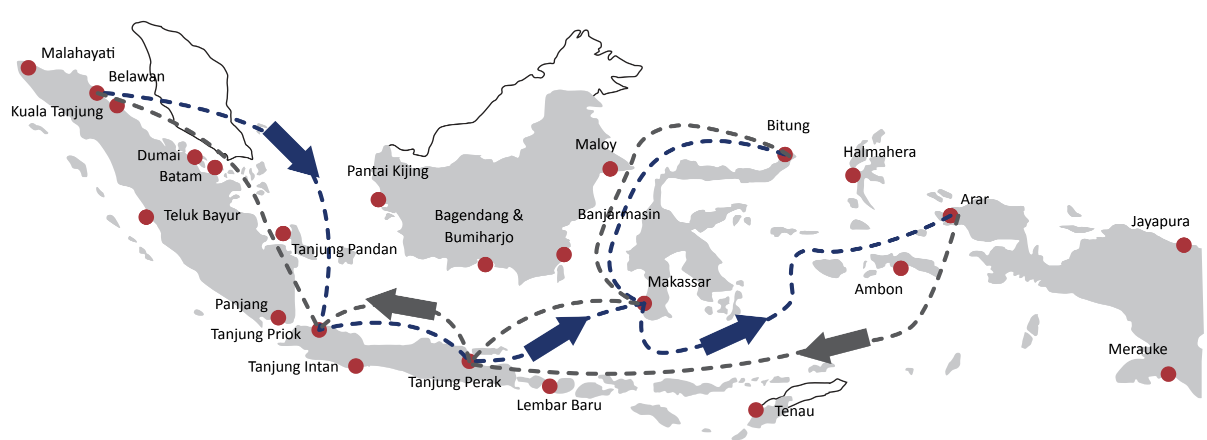
Tourism development will involve facilitating the development of tourist destinations, stronger marketing, building the tourism industry, and institutional reinforcement. The Government has set targets for increased numbers of domestic and foreign tourist visits with foreign exchange earnings projected to reach Rp172.8 trillion. Development of tourist destinations will take place by facilitating the development of tourism zones, strengthening the image of tourism, improving governance, and empowering the public. To boost marketing, the Government will forge closer international cooperation in tourism. Development of the tourism industry will be pursued through local community development, investment facilitation, development of standards and certification, and integration of the tourism ecosystem. For institutional reinforcement, policy will focus on human resources development in collaboration with higher education, facilitation for raising worker skills levels, improving research quality, and change management.

Strengthening the basis for development financing

To respond to the challenge for strengthening the funding basis for economic development, coordinated actions are needed from Bank Indonesia, the Government, and other financial authorities. The main challenge in funding economic development lies in the limited availability of long-term funding sources. The growing integration of Indonesia into the global economy has created opportunities to secure long-term sources of finance, including finance through FDI. To this end, much depends on the Government role in strengthening the fundamentals of the economy, a role that includes infrastructure development and the creation of a more favourable business climate. These improvements are expected to bring positive benefits to Indonesia's internal integration and the nation's attractiveness for offshoring activities by global manufacturers. The role of fiscal policy in optimising fiscal space is also a further area in need of attention.

Regarding the financial market, the funding basis for development will be strengthened within the context of

Picture 15.5. **Development Plan of 24 Strategic Ports**



Source: Ministry of Transportation, 2015 financial sector reforms aimed at sustained efforts for financial market deepening to bring about a more liquid and efficient domestic financial market. The condition of the financial market will be crucial to monetary stability, financial system stability, and financing of domestic economic development. A thriving financial market will offer greater resilience to internal and external pressures and support effective monetary policy transmission while contributing as an alternative financing source for the economy. The Bank Indonesia role in financial market deepening, in response to challenges on the rupiah and foreign exchange money market and the sharia-compliant financial market, is guided by the blueprint for Indonesian financial market deepening. This blueprint sets out the design of the framework, strategy, work program, and roadmap for long-term deepening. On the capital market and other financial markets, Bank Indonesia is an active participant in coordinating with other authorities for fostering the development of these markets. In coordination with OJK, Bank Indonesia will continue seeking solutions for development of the bond market by extending facilities and expediting the issuance of permits for corporate bond issues.

Deepening of the rupiah money market will take place by absorbing surplus liquidity with the use of long-term instruments while expanding the range of money market instruments and bolstering market participants' confidence to engage in transactions. In a related move, Bank Indonesia has prepared a number of policies for developing the repo market. Meanwhile, deepening of the rupiah money market will be pursued by expanding the interbank money market to improve efficiency in unsecured transactions. This will be achieved by promoting growth in interbank credit lines and expanding the role of reference rates with the introduction of a hittable JIBOR. To develop the repo market, Bank Indonesia is collaborating with OJK in encouraging more banks to sign on to Indonesia's Global Master Repo Agreement (GMRA) and to conduct repo transactions using the Indonesia GMRA. BI and OJK will conduct an integrated dissemination and education campaign, working directly to raise awareness and understanding among market participants about repo transactions and the use of the GMRA as a solid transaction agreement. To improve governance in money market transactions, Bank Indonesia will introduce a framework for regulation of the money market, regulation of money market instruments, prudential principles governing transactions, regulation of infrastructure, and reporting and surveillance mechanisms set forth in the Bank Indonesia Regulation governing the Money Market, which will provide a regulatory umbrella for transactions and trading in instruments on the money market. Bank Indonesia will also promote the issuance of negotiable certificates of deposit (NCDs) by establishing criteria for NCDs eligible for trading on the money market. To expand the range of instruments on the money market, Bank Indonesia is now exploring possibilities for development of commercial paper as an instrument for short-term liquidity management for non-bank corporations.

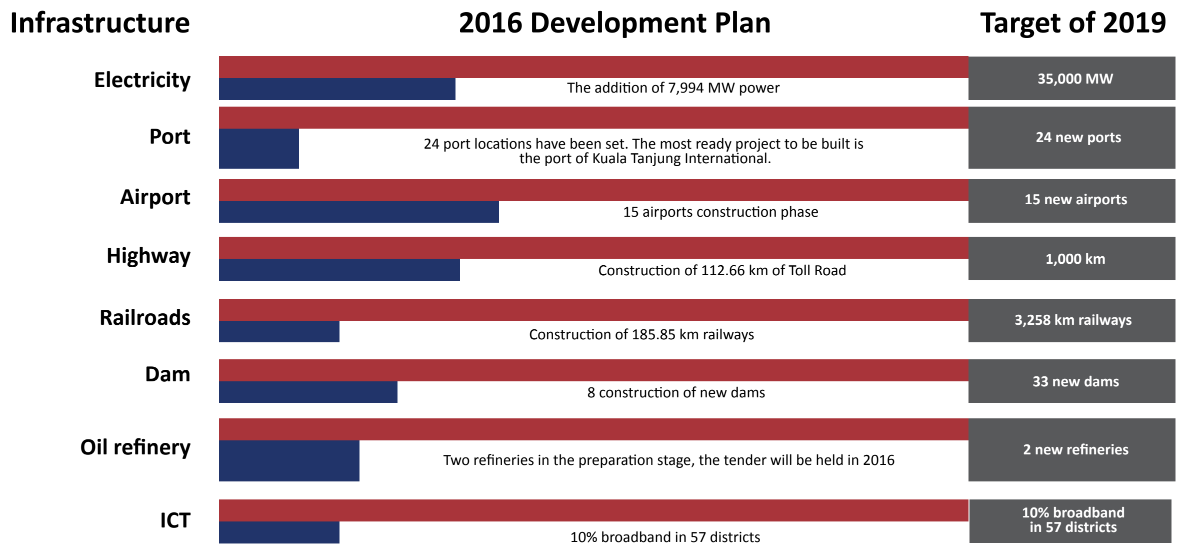
Similarly, the most important objectives for development of the foreign exchange market are to foster the development of foreign exchange market instruments, increase the volume of interbank credit lines, and continue the development of various derivative instruments. Foreign exchange market instruments will be developed in part by providing limited space for development of structured products in support of the hedging obligations that apply to non-bank corporations. To bolster liquidity on the derivatives market, Bank Indonesia will work in coordination with the Ministry of SOEs to promote SOE use of hedging transactions. Bank Indonesia will work towards a standardised format for derivative transaction contracts not only in line with best practice, but also to be more easily understandable for market participants and other stakeholders, as well as to comply with the applicable regulations and be adapted to domestic financial market conditions, thus ensuring that these contracts will be straightforward in their implementation. Bank Indonesia will collaborate with OJK in revisions to a number of regulatory provisions seen as no longer appropriate to present conditions.

Strengthening the Inclusive Economy

Efforts to bring about and strengthen an inclusive economy have become a focus of Government attention as elaborated in a number of policy strategies. The scheme for equitable development among regions is set out in a number of the Nawa Cita policies. In the short and medium-term, the Government will keep working to increase quality and quantity in human development by providing access to basic needs, as well as in equity in development and regionality.[24] In addition, strategic actions have been defined for urban development aimed at creating clean, comfortable and habitable cities, supported by environmental and technology-based enhancements.

24 This encompasses village development, border areas, least-developed areas and development of economic centers outside Java.

Picture 15.6. Infrastructure Development Plan of 2016 and Target of 2019



Source: Committee for Acceleration of Priority Infrastructure Delivery

The drive for strengthening the inclusive economy also requires support from creation of an inclusive financial system. To promote this inclusion, Bank Indonesia is expanding access to financial services that play a vital role in poverty alleviation and reducing income disparities. At this time, the people of Indonesia has relatively limited access to the formal financial system, which has a reach extending to only about 52% of the total population (World Bank, 2010). Only 50% of the public hold their money in banks, which represent the formal financial sector. This calls for proper, structured engagement and cooperation between Bank Indonesia and regulators, government ministries and other government agencies.

Bank Indonesia will also continue efforts to promote efficiency in the national economy through more widespread use of non-cash transactions. The non-cash payments initiative will be promoted in collaboration with the central government, local governments, and the payment system industry, and will involve expansion of digital payments integrated into the development of the National Payment Gateway (NPG). This expansion will take place under the strategic plan for development of the NPG prepared by Bank Indonesia, which covers the business strategy, functions and service coverage, development phases and priorities, ownership and operation and the method for NPG infrastructure development. The strategic plan will serve as a reference for Bank Indonesia, which will have the capability of broad, integrated servicing of many different kinds of retail transactions according to the needs of the national economy while prioritising the role of national participants.

Strengthening the key enablers for development

To build sustainable economic growth, the strengthening of the four pillars of the economy as described above must be supported by structural reforms in the areas of infrastructure, human resources, the business climate, and science and technology. As a theme for the 2016 Work Plan, the Government has pronounced the year of accelerated infrastructure development in order to lay the foundations for quality development through improvement in the public capital stock. The Government has also prepared a list of 225 National Strategic Projects and 30 Priority Projects as a focus for infrastructure development. These projects include enhancing of energy capacity, strengthening of national connectivity, and improvement of digital connectivity (Picture 15.6). It is envisaged that achievement of these infrastructure development targets will have a positive impact on the economy for sustaining the momentum of structural reforms. In the short-term, business and household expectations will remain prudently upbeat, thus encouraging higher investment and consumption. In the long-term, the reforms will bring increased productivity and improvements in competitiveness.

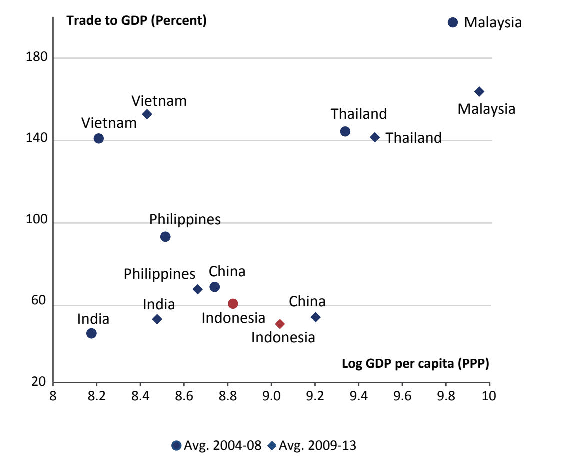
Box 15.1 **Analysis of National Industrial Competitiveness and Strategy in the Era of the ASEAN Economic Community and Free Trade**

The current account deficit sustained by Indonesia since the end of 2011 is explained in part by the flagging performance of Indonesia's exports. This has been influenced by two important factors: the domestic factors of structural problems in industry and trade, and the external factor of the decline in commodity prices. The susceptibility of the current account is related to the structure of Indonesia's exports, currently dominated by resource-based processing industry where performance is dependent on commodity prices. To resolve these issues and optimise the nation's potential, Indonesia needs to undergo an economic transformation by improving the competitiveness of industry on the global market. Industry is central to this transformation as it is the engine of growth for becoming a developed country, creates employment on a large scale, is able to generate substantial value added, and can ultimately become a fundamental source of foreign exchange.

The trade competitiveness diagnostics developed by Reis and Farole (2012) can be used to measure Indonesia's international trade performance and the competitiveness of factors contributing to this export performance. In this analysis, Indonesia's performance is compared with that of its peer countries.[1]

In the first phase, competitiveness is analysed in terms of trade performance (exports) in the four dimensions of intensiveness, extensiveness, quality, and sustainability margin.[2] The analysis show that Indonesia's exports lag behind other ASEAN countries such as Malaysia and Thailand. Indonesia's exports come within the low-middle income country classification, being predominantly resource-based with low value added. Indonesia has undergone a visible decline in performance in all four of these dimensions, with the most important issues in intensive and quality margin.

Chart 1. **Trade Openness**



The intensive margin dimension is represented by trade openness (ratio of exports and imports to GDP), which measures the extent to which an economy is integrated into world trade. In 2009-2013, Indonesia's openness stood at 50%, down from the level in 2004-2008 (60%) (Chart 1). Trade openness in peer countries has mostly increased, with higher levels achieved in countries such as Vietnam (150%) and the Philippines (65%). On the extensive margin dimension, the reach of Indonesia's exports also lags behind that of other countries. In 2013, Indonesia exported a total of 3,906 products, but only about 53% or 2,099 of these products were sold in more than 10 markets. This figure suffers in comparison to China, a country that managed to sell 4,133 products or 88% of the total to more than 10 markets. In addition, Indonesian products have a high death rate, and products that retain high value are resource-based products.

Regarding the dimension of quality margin, Indonesia is superior in primary products but does not compare well in high-tech products (Chart 2).[3] During the past two decades, indications have pointed to a shift in Indonesia's export products from low and high-tech to med-tech and resource-based (Chart 3). Indonesia's exports also have low levels of sophistication and have experienced a downward trend compared to other countries (Chart

1 Specific comparisons were made with Malaysia, Thailand, the Philippines, Vietnam, China and India.

2 The first is the intensive margin created by selling more of the same products in the same market. The second dimension, that of the extensive margin, is new export flows generated by selling new products or selling existing products in new markets. Next, a quality margin is created if there is an increase in the quality and sophistication of the exported products. Products with higher value added in terms of originality (ingenuity), skill and technology will fetch higher prices on the market. The last dimension, that of sustainability margin, evaluates the survival rate of exports, both of new goods and goods that have long been exported.

3 Classification of export products by technology components is possible with the use of the 3-digit SITC based on Hatzichronoglou (1997) and Lall (2000).

Chart 2. **Exports Propotion (2013)**

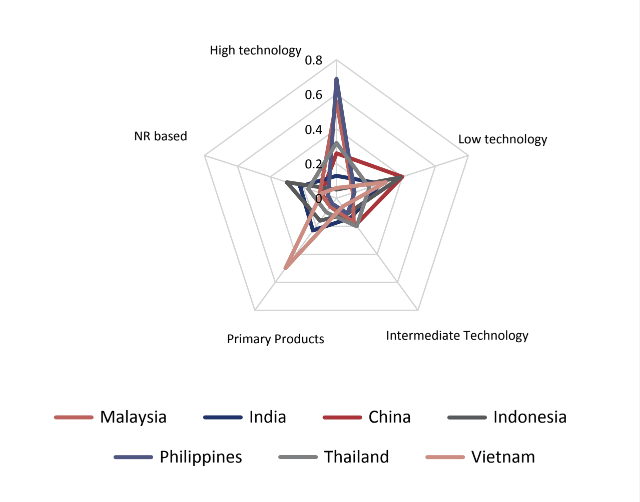
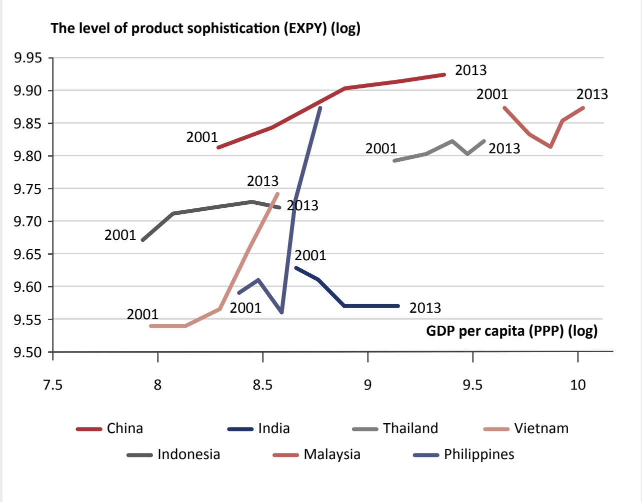


Chart 4. **Product Sophistication (2001-2013)**



4).[4] Another indicator is a product space (Hidalgo et al, 2007), which depicts the network of interproduct linkages in international trade.[5] In product space (Chart 5), a high value product is normally located in the core area, representing an industry cluster with a dense forest of interproduct linkages such as in machinery, metallurgy, and automotive production. Conversely, low value products are found in areas with low density linkages. It is generally easier for a country to produce goods that are close to products that it already manufactures. Therefore, a country that has a comparative advantage in an industry cluster with high density linkages will work faster in upgrading its export products. Analysis of Indonesia from 2000 to 2013 indicates that the product space in Indonesia has moved progressively further from core areas with dense linkages. This is evident in the decline in number of products with comparative advantage in the garments and textiles industry, such as machines, electronics and furniture, where comparative advantage tends to be held by upper-middle countries. According to Hidalgo et al. (2007), the low competitiveness of these industry clusters will hamper transition to a higher income group, meaning that Indonesia faces the risk of a middle income trap.

Chart 3. **Indonesian Export Propotion by Component Technology**

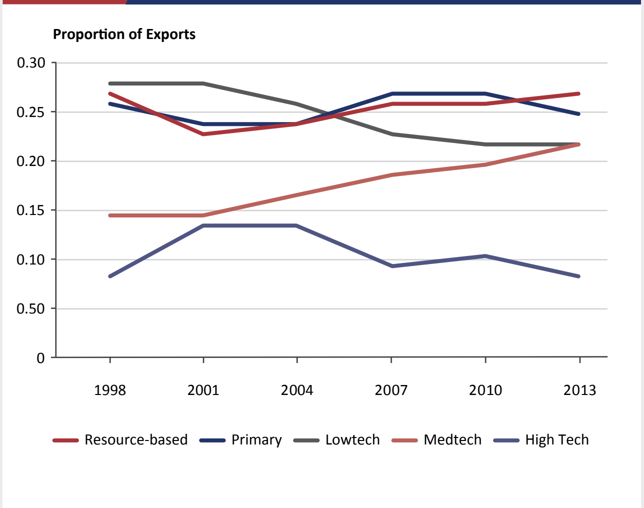
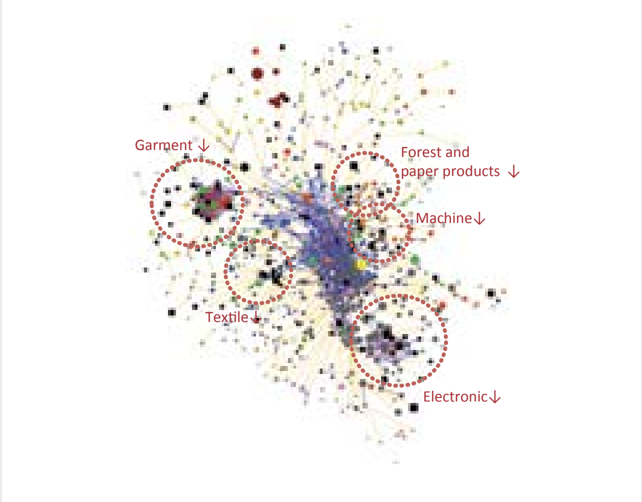


Chart 5. **Indonesia Product Space (2013)**



4 Hausmann, Hwang, and Rodrik (2007).

5 Product space consists of intersection nodes and the lines connecting these nodes. Intersection nodes with different colours represent Leamer product classifications (e.g. natural resources, labor-intensive and metallurgy) while node size represents the international trading value of the product. Coloured lines reflect the degree of closeness among products, with red and dark blue indicating a high degree of closeness and yellow and light blue portray low density linkages. The product space of each country is differentiated by the black points, i.e. export products of that country with RCA>1.

Chart 6. **The Share of Surviving Export Relationships (2003-2013)**

Another dimension, that of sustainability margin, is represented by an indicator of the ability to maintain trading links. During the period of 2003-2013, the share of Indonesia's surviving new export relationships was 61.2% (Chart 6). This export duration was superior only to the Philippines and Malaysia, but came below that of Vietnam, Thailand, China, and India.

Indonesia's trade performance must also be seen from the aspect of competitiveness in global value chains. Global economic developments in the 21st century point to a change in in the pattern of trade from competition in producing certain products to competition to be involved in production processes, i.e. manufacturing, pre-fabrication, or post-fabrication.[6] Indonesia's ability to be involved in any of these production processes will be determined more by competitiveness as a location of choice, according to the characteristics of input factors. Indonesia needs to increase its attractiveness for investment in order to encourage export-oriented investment. A comparative analysis of FDI characteristics among ASEAN countries shows that investment in Indonesia provides employment on a large scale, but is more domestic oriented. Other countries in the region, however, are able to attract higher quality investment. In Thailand, FDI boosts exports; in Vietnam, FDI drives exports and employment; and in Malaysia, FDI strengthens skills-based export products (Table 1).

6 Based on the characteristics of value added and input factors, each stage of this production can be illustrated in the form of a smiley curve.

Furthermore, analysis using a triangular trading scheme approach indicates that the most competitive ASEAN countries in the global value chain are Singapore, Malaysia, and Thailand (Chart 7).[7] This measurement of competitiveness is obtained from the level of import productivity, i.e. the ability to export after importing raw materials and intermediate goods. The measurement of competitiveness also takes account of the scale of exports in global value chains.

The second stage of the competitiveness analysis seeks to analyse the competitiveness of factors contributing

Table 1. **Characteristics of FDI in ASEAN**

Productivity Ratio	FDI / Affiliated Company (USD Million)	Export / Affiliated Company (USD Million)	Labor / Affiliated Companies
Indonesia	$4.85	$69.39	809
Vietnam	$10.80	$107.81	896
Malaysia	$3.48	$122.25	389
Thailand	$6.10	$204.24	709

7 For the concept of the triangular trading scheme, refer to Lejour et al (2013) and Johnson-Noguera (2011). According to this method, trading data that is initially bilateral is reconstructed into trade between three countries, namely the supplier of raw materials (origin), the connecting point (hub) and the final destination. Information obtained from this scheme of trading by three countries includes the following: (1) imports of raw materials that are processed for export (production hub); (2) imports of raw materials that are processed for the domestic market; (3) exports of raw materials to the world; (4) exports of products manufactured with domestically-sourced raw materials; and (5) self-sufficient activities (sourcing, processing, and consumption in-country).

Chart 7. Competitiveness of ASEAN 5 in the Global Value Chain

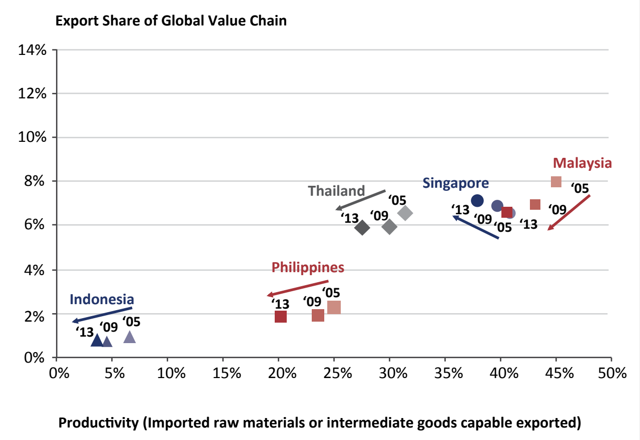
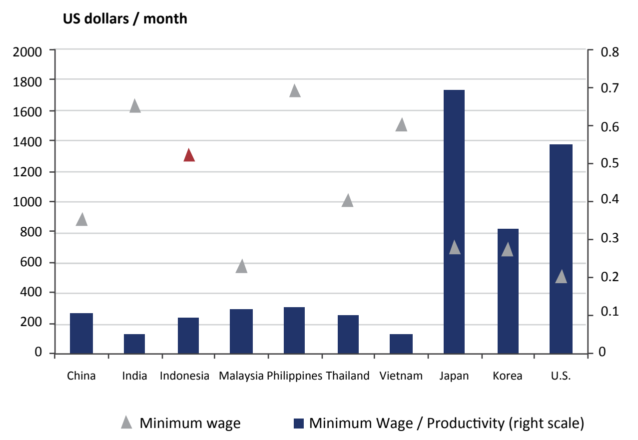


Chart 8. Minimum Wages and Productivity



Source: World Development Indicators, World Bank, processed

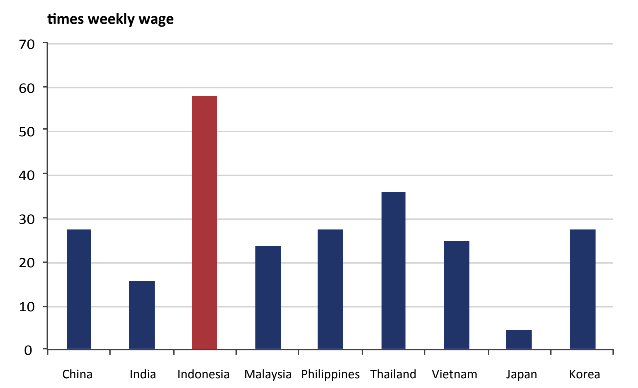
to Indonesia's export performance. Competitiveness is measured by the three dimensions of market access, supply-side factors, and trade promotion support. Each of these dimensions shapes export performance through its influence on companies through the channels of entry costs, cost of factors and transactions that determine the competitiveness of production at the manufacturing level, and the level of technology and efficiency of the sector or company. Results of the analysis show that the challenges facing Indonesia's exports are mainly attributable to poor worker competitiveness (skill set), high costs of production and logistics, lack of a conducive business environment and complex bureaucracy with regard to domestic policy and institutions, and poor market access.

Regarding the dimension of conditions, the costs for labor in Indonesia are high. After factoring in the level of productivity, the minimum wage is higher than that of advanced economies (Chart 8). The high minimum wage is a reason for job losses through mass layoffs and relocation of factories to provinces with a lower minimum wage. The cost of dismissals is also very high compared to peers at about 50 times the weekly wage (Chart 9). Besides this, there are several implicit costs such as the large number of trade unions that complicate negotiation processes, frequent demonstrations, and rising operational risks. As regards skills, more serious issues are at stake. The World Bank (2014) claims that a skills mismatch exists in which 50% of graduates from high school or equivalent education and 15% of university graduates work in unskilled positions. Seventy percent of manufacturers claim it is very difficult to fill skilled positions. At the same time, only 5% of workers have received on-the-job formal training.

The condition of logistics in Indonesia poses serious obstacles to building competitiveness. The Indonesian Logistics and Forwarders Association (2015) claims that the cost of logistics in Indonesia is about 24% of GDP, far higher than the average logistic cost in Asian countries. Although WDI data indicates that Indonesia's Logistic Performance Index has slightly improved (Chart 10), it still ranks lower in comparison to peers. Another issue related to conditions is the lack of international certification and compliance with regard to export products and industrial processes (Chart 11).

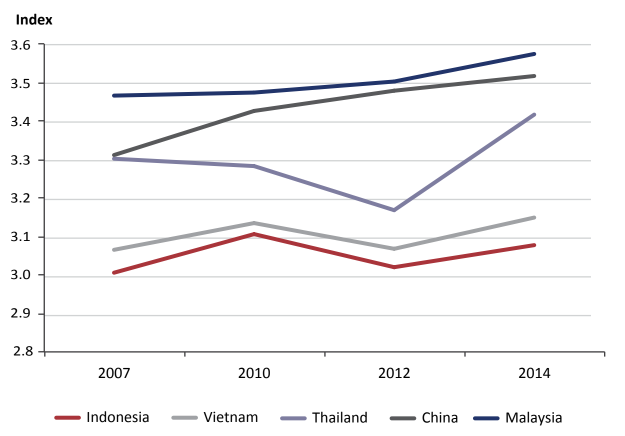
Regarding the framework of business incentives, in Indonesia the policies for streamlining FDI (Chart 12) and improving the ease of doing business (Chart 13) rank the lowest in ASEAN. In several aspects, such as

Chart 9. Dismissal Costs



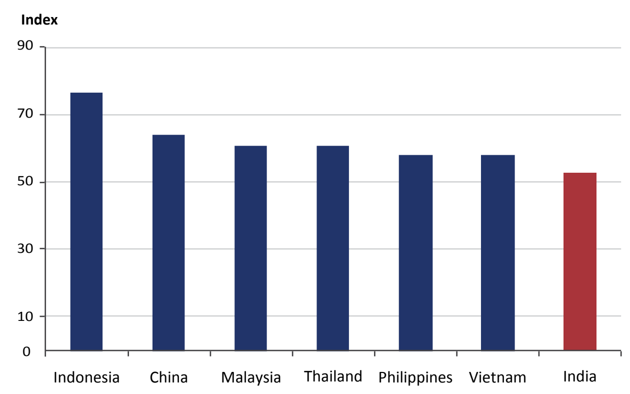
Source: Global Competitiveness Index, WEF

Chart 10. Logistics Performance Index



Source: World Bank

Chart 12. Ease of Establishment Index (2014)

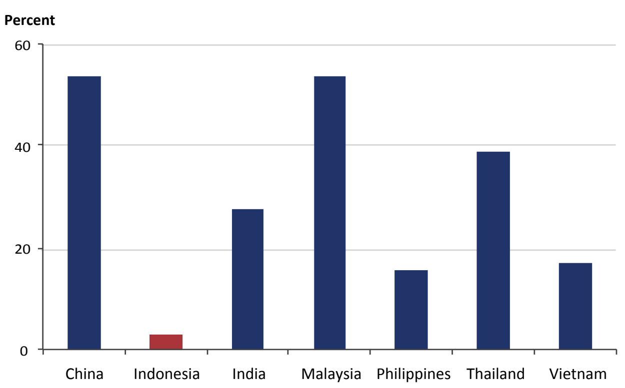


Source: Enterprise Surveys, World Bank

starting a business, processing construction permits, registering property, paying taxes, and enforcing contracts, Indonesia lags far behind its peers. As regards market access under trade agreements, Brunei, Malaysia, Singapore, and Vietnam are in a superior position to Indonesia. Indonesia's FTA has mostly been concluded within the ASEAN regional trading system. In regional block trading, Indonesia is currently negotiating the Regional Comprehensive Economic Partnership (RCEP) with participation from other ASEAN countries. This does not form part of the Trans Pacific Partnership (TPP). Other obstacles faced by Indonesia's export products arise from non-tariff measures such as sanitary and phytosanitary provisions and technical barriers.

Regarding support from promotion of trade, exports, and investment, Indonesia is in a comparatively weak position. Another issue is inadequate use of Special Economic Zones (SEZs). Indonesia has a similar number of SEZs as do peer countries, but when compared to the geographical area of its territory, the number is small (UNIDO, 2015). In addition, SEZs have seen only limited development, as they are not supported by adequate infrastructure such as integration into energy supply and transport links. Some SEZs have been established at considerable distance from supporting infrastructure, such as sea ports. There has also been a lack of effectiveness in the management of industrial zones, with weak promotional support.

Chart 11. Companies with International Certification



Source: Enterprise Surveys, World Bank

Chart 13. Ease of Doing Business in Indonesia (2015)

Source: World Bank

Picture 1. **Improvement Strategy of National Industrial Competitiveness**

NATIONAL INDUSTRIAL STRATEGY

Institutions and Leadership	Trade and Investment incentive scheme	Human Resources and Employment	Infrastructure	Technical and Business Services Efficiency	Financing Access	Market Access
• Coordination (between sectors, the central-local) • Trust and collective action • Management, administration, and governance effectiveness	• Export promotion • Investment facilitation • Industrial area • Fiscal incentives • Macro environment (controlled inflation and a stable exchange rate)	• Completion of the national education system (Link and Match) • Skills and labor productivity • Labor Policy	• Connectivity (roads, logistics, ports, customs) • Energy & utilities • Fiscal policy logistics • Coordination and regulation	• Technological improvement • R&D and innovation • Business services • Intellectual Property Right	• Access to finance (financial inclusion) • Venture capital • Long-term financing sources	• Trade Agreement • Certification / standardization • The information system (repository) • Expanding markets and systems

To respond to these challenges, it is necessary to improve industrial competitiveness by upgrading and deepening the industry sector, creating value added, and developing export-oriented industry. The industries affected by these concerns are all industries in a general sense, whether resource-based, labor-intensive, medium technology or high technology. This calls for a national industry strategy that covers seven essential elements: (i) institutions and leadership; (ii) trade and investment incentive schemes; (iii) human resources and labor; (iv) infrastructure; (v) technical efficiency and business services; (vi) access to finance; and (vii) access to markets (Picture 1).

Box 15.2 Growth Strategy for Supporting Structural Reform in Indonesia

One of the challenges to carrying out structural reforms is to formulate a growth strategy that can have significant impact on the economy of a country. Therefore, it is necessary to formulate a development strategy based on priorities determined by the most important obstacles. Structural reforms also need to take account of regionality, give that each region may have differences in resources and structural constraints.

Within this context, Hausmann, Rodrik, and Velasco (2005) introduced an alternative growth diagnostic approach to identify the major obstacles to promoting investment and economic growth. Analysis of these major obstacles is performed by diagnosing each branch of the decision tree, beginning with the two major factors of high financing and low economic returns (Picture 1). To formulate development priorities on the basis of these major obstacles, a policy simulation process is carried out with the use of the Computable General Equilibrium (CGE)-IndoTERM model.[1] Use of this model is necessary to analyse the impact of structural reforms on regional and national macroeconomic parameters, such as economic growth, exports, and employment. Bank Indonesia (2015) has conducted growth diagnostic studies for 24 provinces in Indonesia in which the decision tree analysis was combined into the CGE model.[2]

As a rule, the most important obstacles in nearly all areas of Indonesia arise from the quantity and quality of human resources and capacity and reliability of electricity supply. Regarding human resources, the average duration of school education in Sumatra, Java, Kalimantan, and Eastern Indonesia is 8.6, 8.1, 8.1, and 7.9 years respectively. Nationwide, this average is still less than 9 years. This is a matter of concern as Indonesia needs large numbers of highly educated technical personnel to manage the transition to an advanced country, particularly in order to reinforce economic structures in the medium and high technology-related sectors of industry. In the regions outside Java, skilled workers are also needed to strengthen the diversification of high value added sectors of the economy. Historically speaking, the phenomenon of shortages of qualified personnel outside Java is evident from the widespread employment of workers from other regions. Furthermore, analysis in some provinces also indicates that in general, the lesser educated workers are found in rural areas, and these workers are mostly active in the agriculture sector. The low quality of the workforce in the agriculture sector may hamper the process of increasing agricultural productivity, particularly in order to attain food self-sufficiency. If self-sufficiency is not achieved or food supplies diminish, prices for food items will increase at a faster rate than for industrial goods. High prices for foodstuffs, which represent an essential need, will drive up the cost of living in cities, which will ultimately stoke the pressure for wage increases demanded by industrial workers. In the end, this will slow employment and affect the pace of Indonesia's transformation into an industrial country. Following this, a policy simulation using the CGE-IndoTERM model confirmed the identification of obstacles in human resources. According to the simulation results, increased productivity achieved through accelerated development of human capital has potential for significant impact across the entire archipelago, particularly in strengthening mainstay manufacturing sectors in individual regions (Chart 2). Implemented nationwide, a policy program for development of human capital would have potential to boost economic growth by 0.25% per annum and employment by 0.50% per annum (deviation from baseline scenario without such policy).[3]

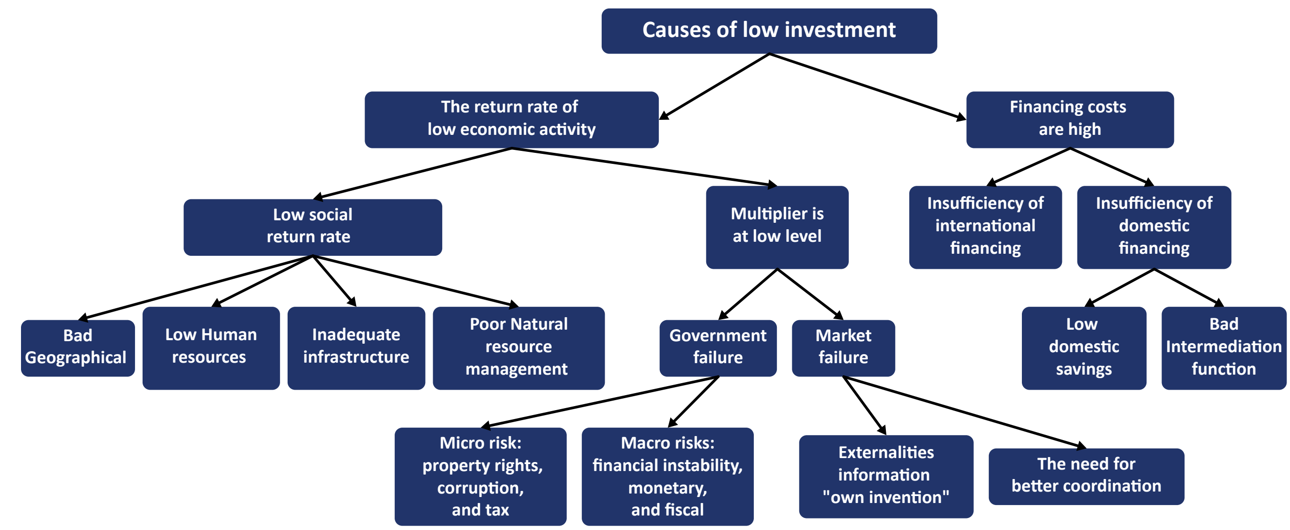
Regarding electricity, there is relatively adequate supply for household needs in Java, but the large industrial population has also created similarly heavy demand for energy, necessitating further increases in electricity capacity. However, outside Java, both business and households suffer electricity shortages. In addition, the persistently high number of companies that attempt to provide their own electricity attests to the inadequate reliability of electrical power. According to the World Bank Enterprise Survey (2009), losses attributable to power cuts in Indonesia could reach as much as 1.6% of the value of production. Results from policy simulation with the CGE-IndoTERM model also confirm the importance

1 IndoTERM is a bottom-up multisectoral, interregion CGE model developed under collaboration by several institutions: the Center for Economics and Development Studies, Padjadjaran University; Center for Policy Studies, Victoria University; Asian Development Bank; AusAID; and the National Development Planning Agency.

2 The 24 provinces selected for the Bank Indonesia Growth Diagnostic study of 2015 are Aceh, North Sumatra, West Sumatra, Riau, the Riau Islands, South Sumatra, Bengkulu, Lampung, Jakarta, Banten, West Java, Yogyakarta, Central Java, East Java, East Kalimantan, Central Kalimantan, West Kalimantan, South Kalimantan, North Sulawesi, South Sulawesi, Maluku, North Maluku, West Nusa Tenggara and Bali.

3 For full details, see: Affandi and Anugrah (2015), Strategi Pertumbuhan di Indonesia: Pendekatan *Growth Diagnostic*.

Picture 1. **Decision Tree Growth Diagnostic**



Source: Hausmann, Rodrik, and Velasco (2005)

of electricity development. Based on these results, a policy for building electricity capacity has potential to boost national economic growth by 0.25% per annum and employment by 0.13% per annum (deviation from baseline scenarios without such policy). Development of electricity capacity also has potential to boost export growth and employment while providing opportunity for each region in Indonesia to develop their mainstay industries (Chart 3). This demonstrates that provision of electricity infrastructure is desperately needed by business for both carrying out expansion and to improve productivity where businesses now face potential losses.

Besides human capital and energy infrastructure, connectivity also poses major obstacles for many regions in Indonesia. In particular, these obstacles are attributable to the capacity and quality of ports, roads, and airports. Dwelling times, turnaround times and port capacity shows that the efficiency of ports in Indonesia lags far behind that of competing ASEAN countries such as Malaysia and Singapore. Regarding roads, for many industries the extent of road damage remains high, added to which is the imposition of illegal levies. This occurs even in Java, where infrastructure is in relatively better condition. In addition, some provinces in Indonesia also face other, quite varied

Chart 2. **Impact of Human Capital Development in 4 Indonesia Regions (Industry with the biggest incremental in each region)**

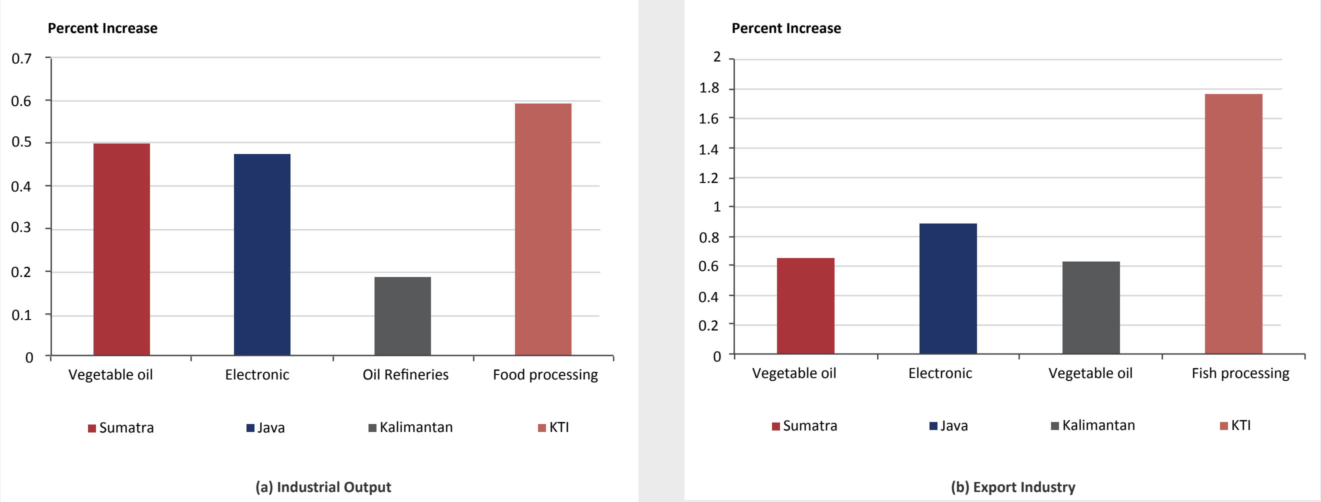
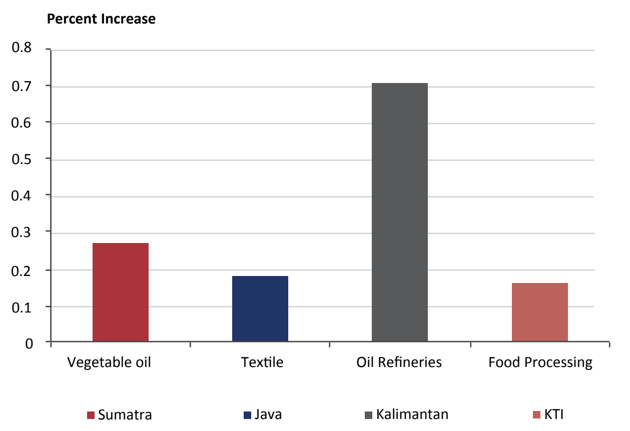
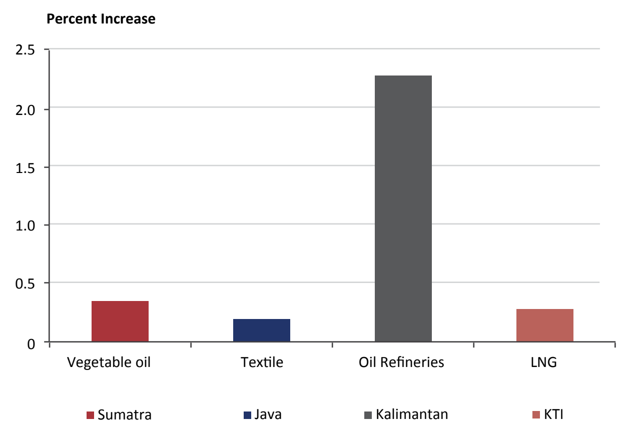


Chart 3. **Impact of Power Development in 4 Indonesia Regions (Industry with the biggest incremental in each region)**



(a) Industrial Output



(b) Export Industry

obstacles, such as problems with bureaucracy and security, as well as problems with the quality of human resources and infrastructure. These problems affect both infrastructure for connectivity (roads, ports, and railways) and electricity infrastructure.

The future is always filled with uncertainty. Nonetheless, the future is also imbued with hope for those who aspire. The Indonesian economy has the potential for stronger growth and more solid fundamentals.

Chapter 16

Outlook

The Indonesian economy is expected to grow stronger, more sustainable and inclusive. The optimism for Indonesian economic growth is to a large extent attributable to commitments and consistency in accelerating the implementation of cross sectoral structural reforms. In the short-term, economic growth will continue to be driven by domestic demand bolstered by investment in infrastructure projects. In the medium-term, economic growth is set to increase as infrastructure projects begin delivering benefits by expanding capacity in the economy. With these developments, macroeconomic and financial system stability will be kept well under control.

Against the backdrop of limited global growth, the upward growth trend for the Indonesian economy is expected to be sustained in line with the implementation of structural reforms. The overall outlook for the global economy is improved from the previous year, albeit a fairly limited growth. The global economy, led by advanced economies, is forecasted to begin showing improvement, particularly in the United States. On the other hand, the economy in China is predicted to slow further with impact that will continue to hold back increases in commodity prices. Against the background of this global economic outlook, the future momentum of the Indonesian economy will be determined to a great extent by the structural reforms implemented by the Government and Bank Indonesia. Bank Indonesia predicts an upbeat economic outlook for 2016 with growth in the range of 5.2-5.6% accompanied by subdued inflation on track with the target of 4±1%. In keeping with rising economic growth, credit expansion is forecasted to reach 12-14%. However, a slightly enlarged current account deficit is predicted in comparison to 2015 due to intensive work on infrastructure projects. Hence, the forecasted current account deficit is still at a safe level, which is below 3% of Gross Domestic Product (GDP).

The medium-term forecast is for steadily improving and more sustainable economic growth that in 2020 is projected to reach 6.3-6.8%. Growth in household consumption will remain stable, buoyed by the expanding proportion of the middle class and more extensive provision of social security. Investment will forge ahead with rising growth momentum as work progresses on infrastructure projects and improvements are made to the business climate. The quality of government expenditures will improve with greater emphasis on capital expenditures in keeping with cutbacks in the portion allocated to subsidies. In addition, state budget allocations for transfers to the regions and Village Funds will be increased over past years to bring about greater equity in development for all regions. Implementation of the structural reform programs will be crucial to increase capacity and capability on the production side that will pave the way for the economy to achieve stronger, more sustainable, and inclusive growth.

16.1. SHORT-TERM ECONOMIC OUTLOOK

Global Economic Outlook

The global economy will show improvement, albeit still relatively limited . The forecast for global economic growth in 2016 is 3.4%, bolstered by the continued recovery in the U.S. economy. The improvement in the U.S. economy will be driven by the rising consumption in response to increase in employment and low oil prices. Despite a fairly solid recovery, the monetary normalization policythrough increases in the Federal Funds Rate (FFR) is predicted to move forward gradually in 2016, although various risks still overshadow the U.S. economy. Meanwhile, improvement in the economy of Europe is becoming visible on the demand side, supported by accommodative monetary policy. Improvement has been driven mainly by increased consumption and labor productivity. In addition, the continuation of the Quantitative Easing (QE) policy by the European Central Bank (ECB) may offset some of the negative impact of the Fed's policies on the global capital flows to Emerging Markets (EM). On the other hand, China's economy is expected to slow further as a result of the ongoing rebalancing process. With recovery in the global economy predicted to progress at an uneven pace, the world trade volume is expected to see only moderate growth in 2016.

The trend in global commodity prices is expected to remain negative. The decline in commodity prices points to the end of the super-cycle era in global commodity prices brought about by weakening economic growth in EM economies and particularly China as the traditional major buyer of global commodities. In addition, world oil prices will stay at a low level due to the limited recovery in the global economy and the continuing glut in world oil supply.

Domestic Economic Outlook

GDP Outlook by Expenditure

Domestic demand will continue to provide the main driver for economic growth in 2016, which is expected to reach 5.2-5.6% amid the limited recovery in external conditions. Overall growth in household consumption in 2016 is forecasted to reach 5.0-5.4% (Table 16.1). Acceleration of structural reforms through construction of infrastructure is expected to promote job creation. Wage increases and payment of the 13th and 14th month salary for civil servants, members of the police and military, and pensioners will also boost household incomes. Public purchasing power will be bolstered not only from higher incomes, but also supported by targeted inflation within the range of 4±1%.

In 2016, investment is projected to grow more robust at 7.2-7.6%, up from the preceding year. Similar to 2015, infrastructure investment will become the leading contribution to future investment growth. This outlook is based mostly on the confidence over improvement of

Table 16.1. GDP Outlook by Expenditure

Variable	Realization 2015	Outlook 2016
GDP Growth (%, yoy)	**4.8**	**5.2-5.6**
Household Consumption*	4.8	5.0-5.4
Government Expenditure	5.4	6.4-6.8
Gross Fixed Capital Formation	5.1	7.2-7.6
Goods and Services Export	-2.0	-5.5 - (-5.1)
Goods and Services Import	-5.8	-5.1 - (-4.7)

Source: BPS-Statistics Indonesia, processed
*Consist of (i) Household Consumption and (ii) Non-profit Institutions Servings Household Consumption

implementation of government infrastructure projects to support economic growth. The government is also pursuing efforts to improve the effectiveness of state spending by increasing allocations for productive expenditures. Productive expenditure allocations will focus on improving the key enablers for development, particularly by building infrastructure in order to boost competitiveness and expand production capacity. Steady improvement is also predicted for private sector investment growth as domestic demand begins to climb and in keeping with forecasts for more robust external demand for Indonesia's exported products. Support for the growing role of the private sector role is also provided by more accommodative monetary and macroprudential policies.

The Government has launched the National Strategic Projects (PSN) to accelerate the development of infrastructure. To expedite progress on the government plan, the Government has designated 225 projects worth over Rp100 billion as National Strategic Projects (Diagram 16.1), for which pre-feasibility studies have been completed. For 30 of the 225 projects, The Government has assigned the Committee for Acceleration of Priority Infrastructure Delivery (KPPIP) to accelerate construction work. In most cases, these 30 infrastructure projects offer potential for funding under the private-public partnership scheme. Of these 30 priority projects, tendering for 13 has been concluded and some projects have entered the construction phase (Diagram 16.2). To support the successful implementation of National Strategic Projects, the Government issued Presidential Regulation No. 3 of 2016 concerning Acceleration of The Implementation of National Strategic Projects, which provides facilities and streamlining of requirements related to licensing, procurement, land acquisition, and guarantees by the Government. Electricity infrastructure benefits from additional facilities besides those stipulated in the PSN Presidential Regulation. These added facilities, which remove some obstacles to the development of electricity infrastructure, are set forth in Presidential Regulation No. 4 of 2016. This Presidential Regulation stipulates definite powers for PLN as the provider for construction of electricity infrastructure, funding assistance from the Ministries of Finance, SOEs, and Energy and Mineral Resources, and freedom for PLN to solicit domestic and foreign funding with the backing of guarantees issued by the Government.

On the external side, exports are forecasted to maintain negative growth in 2016. The flagging performance of exports is consistent with predictions of continued economic slowdown in China, one of Indonesia's major export markets. As a result, export commodity prices are also expected to maintain negative growth in

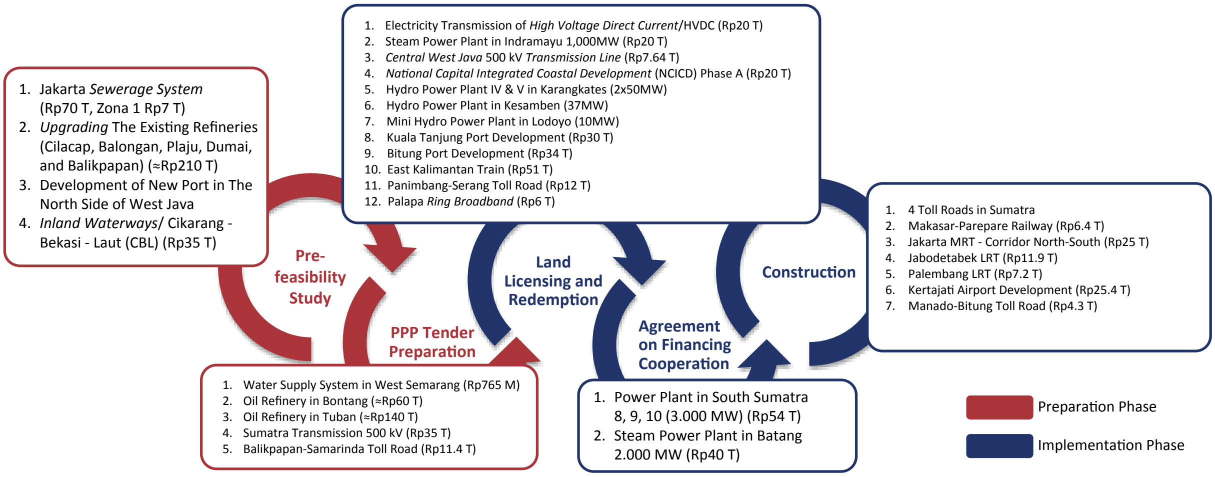
Diagram 16.1. National Strategic Projects

	Road	Railway	Airport	Port	Housing	Energy	Electricity
PSN	52	19	17	13	3	7	402
Priority Projects	4	5	1	4	-	3	9

	Water	Dam	Agriculture and Fishery	PLBN	ICT	SEZ
PSN	10	60	3	7	3	25
Priority Projects	3	-	-	-	1	-

Source: Committee for Acceleration of Priority Infrastructure Delivery

Diagram 16.2. Development of Priority Projects



Source: Committee for Acceleration of Priority Infrastructure Delivery

2016. Although higher growth is forecasted for some of Indonesia's major export destinations, this will not be sufficient to offset the overall fall in demand for Indonesia's export products. Indonesia's real export growth in 2016 is projected at about -5.5 to -5.1%.

Import growth is expected not to differ significantly from the previous year's figure. With a situation of expanding domestic demand, while exports continue to chart negative growth, import growth in 2016 is projected at -5.1% to -4.7%. The lacklustre performance of imports at a time of rising investment is explained by the fact that the largest source of investment growth is investment in construction and infrastructure. Due to the less elastic nature of imports for construction/infrastructure investments compared to investment in machinery/equipment, the impact from higher investment on imports will be relatively limited. In addition, the downward trend in imports of raw materials in early 2016 also resulted from Indonesian manufacturing not yet operating at high capacity.

GDP Outlook by Industrial Origin

In keeping with improvement in domestic demand, the manufacturing sector will remain the leading contributor on the production side, followed by the transportation and communications sector and the construction sector. In 2016, similar to 2015, these three sectors will provide the main driver for the economy, particularly the construction sector driven by the public infrastructure development by the Government. Manufacturing sector growth is forecasted to reach 4.8-5.2% in 2016 as domestic demand begins to regain momentum (Table 16.2). The relatively limited growth in this sector is explained by the downbeat outlook for global commodity prices that can potential become a disincentive for exporters of manufactured goods to increase their production capacity. Furthermore, growth in this sector is also supported by the metal industry, due to the public infrastructure investment.

The transportation and communications sector is expected to maintain the positive trend of past years. In 2016, this sector is predicted to grow by 9.2-9.6%. This growth will be driven by the expected progress on projects for expansion of ports and airports along with provision of transportation

Table 16.2. GDP Projection by Industrial Origin

	Realization	Outlook
	2015	2016
GDP Growth (%, yoy)	4.8	5.2-5.6
Agriculture	4.0	3.4-3.8
Mining	-5.1	-6.6 - (-6.2)
Manufacturing	4.2	4.8-5.2
Electricity, Gas, and Water*	1.6	3.3-3.7
Construction	6.6	8.7-9.1
Wholesale and Retail Trades, Accommodation, and Food Service Activities**	2.8	4.1-4.5
Transport, Storage, Information, and Communication***	8.5	9.2-9.6
Financial Services****	7.0	8.8-9.2
Other Services Activities*****	6.5	7.0-7.4

Source: BPS-Statistic Indonesia, Bank Indonesia calculation
*Consist of 2 industrial origins: (i) Electricity and Gas Supply and (ii) Water Supply
** Consist of 2 industrial origins: (i) Wholesale and Retail Trades, Repair of Motor Vehicles and Motorcycles and (ii) Accomodation and Food Service Activities
*** Consist of 2 industrial origins: (i) Transport and Storage and (ii) Information and Communication
**** Consist of 3 industrial origins: (i) Financial Services. (ii) Real Estate and (iii) Business Services
***** Consist of 4 industrial origins: (i) Public Administration and Defense; Compulsory Social Security, (ii) Education, (iii) Human Health and Social Work Activities, (iv) Other Services

modes undertaken by the government as part of the medium-term infrastructure development plan. Within this context, the Government will undertake procurement of about 1,050 rapid transit buses for 32 provinces, construction of 10 ships for pioneer routes, procurement of 3 ferries for the Merak-Bakauheni crossing, expansion of 34 major and minor airports in 17 provinces, and expansion of 40 ports in 14 provinces. The Soekarno-Hatta Airport Terminal 3 Ultimate is slated to enter operation by the end of 2016. This project will support an increase in air transportation capacity while stimulating growth for other modes of transportation. Meanwhile, under the strategy for improving national connectivity, the Government will also develop mass transit systems including rail-based mass rapid transit and urban rail developments in 10 metropolitan centers.

Growing needs in data and communications will spur growth in the communications subsector. The need for communications networks will lead to steady growth in data and communications traffic in line with technological advancements and the burgeoning growth of the middle class. The government is pressing forward for expansion of broadband coverage in Indonesia by exploring possibilities for collaboration with various parties in the provision of telecommunications networks in areas with difficult access. Besides this, the development of the new 4G technology with high download and upload speeds is expected to bring about increased data use in Indonesia. Accelerated development of information and communications technology (ICT) infrastructure will boost development of the digital economy throughout Indonesia. This advancement of the digital economy will have a positive effect on future economic growth (see Box 16.1).

Higher growth in the construction sector is predicted at 8.7-9.1% in 2016. This sector will benefit mainly from the greater stimulus for acceleration of infrastructure projects following the issuance of Presidential Regulation No. 3 of 2016 concerning Acceleration of The Implementation of National Strategic Projects. After a period of delay in 2015 due to a consolidation process in government administration, the Government renewed efforts in 2016 to expand and speed up tender and procurement processes and embarked on construction for projects spread among eight sectors. These sectors are aviation, telecommunications and informatics, maritime transport, railways, electricity and energy, land and road transportation, housing and urban settlements, and water resources. Meanwhile, several projects are under way, including the construction of Terminal 3 Ultimate at the Soekarno-Hatta Airport, construction of the Kertajati Majalengka Airport, expansion of the Ahmad Yani Airport in Semarang, construction of the Kalibaru Priok terminal, construction of the Teluk Lamong multi-purpose terminal, construction of the Trans-Java toll road (Cikampek-Palimanan, Bawen-Salatiga, and Solo-Ngawi-Kertosono), and construction of the Trans-Sumatra toll road (Bakauheni-Tegineneng, Pekanbaru-Dumai, and Kayuagung-Betung).

Regional GDP Outlook

In 2016, the aggregate growth outlook for various regions, notably Java, Sumatra, and Kalimantan, is brighter in comparison to 2015. In Java, the economy is forecasted to grow in the range of 5.6-6.0% on stronger investment performance driven by expansion in government development of infrastructure for agriculture (reservoirs, retention basins, and irrigation networks) and connectivity (roads, railways, seaports, and airports). In addition, the ongoing improvement in consumption and exports of manufactured goods will contribute to economic expansion in Java in line with improving expectations of private incomes and demand from export markets for Indonesian manufactured products. By comparison, the growth forecast for Sumatra is in the range of 4.2-4.7%. Upbeat economic growth in Sumatra is also expected in relation to the work in progress on large-scale infrastructure projects such as the Trans-Sumatra toll road, power plants, and sport facilities for the 2018 Asian Games. Meanwhile, Kalimantan is predicted to see stronger growth albeit on the lower end of the scale at 2.1-2.5%. The Kalimantan economy are expected to recover on stronger industry performance with the continuing development of downstream industry in some regions (smelters and manufacturing of CPO derivatives). In addition, it is also predicted a more upbeat performance in agriculture and mining sectors. However, further improvement in the Kalimantan economy will be limited in view of the gloomy outlook for mining commodity prices. In other developments, economic growth in Eastern Indonesia is forecasted at 7.1-7.5%, down in comparison to 2015 due to flagging performance in mining exports and private investment.

Inflation Outlook

Inflation in 2016 is forecasted to remain within the inflation target range of 4±1%. Moderate pressure is expected from core inflation. External factors affecting core inflation are kept under control with the prudently managed exchange rate volatility and sustained low international prices for non-oil and gas commodities. On the domestic front, rising domestic demand is expected to meet with supply side response without giving rise to significant inflationary pressure. Inflation expectations are predicted to remain well anchored, in keeping with support from policy and close coordination between Bank Indonesia and the Government. Against this background, demand-side inflationary pressure is expected to remain relatively moderate.

Slightly higher inflation in the volatile foods category is expected for 2016 compared to 2015. This rise in volatile foods inflation is related to the persistent strength of domestic demand and potential for a shift in the planting season. The Indonesian Rice Millers and Rice Traders Association (PERPADI) announced that the most critical shortage of food supply, which normally falls in January-February each year, could stretch to January-March in early 2016 due to the El Nino. The very low rainfall in October 2015 meant that farmers, particularly those working in rain-irrigated cultivation, were unable to plant crops. As a result, the harvest in February 2016 will be less than in previous years due to postponement of the planting season. To ease pressure from volatile foods inflation in future periods, it is necessary to reinforce buffer stocks and increase production to curb price movements in foodstuff commodities.

In 2016, overall administered prices inflation (AP) is predicted to ease compared to the previous year. The forecast for the low AP inflation is bolstered by the implementation of a more flexible scheme for energy prices that are set according to market prices and the forecast for lower world oil prices in 2016 compared to the year before. However, in view of the likelihood of further subsidy reforms, price increases for government-regulated commodities such as electricity and subsidised bottled LPG gas cannot be ruled out in the future.

Balance of Payments Outlook

In 2016, the current account deficit is predicted to remain below 3% of GDP. This forecast for current account deficit is explained by rising non-oil and gas imports driven by domestic economic activities. While global demand is on the rise, the ongoing correction in global commodity prices and stubbornly low oil prices will limit the extent of export growth in 2016. On the other hand, non-oil and gas imports are predicted to climb in keeping with growth of domestic demand, which also linked to the government's accelerated construction of infrastructure.

The outlook for lower global oil prices in 2016 will have an adverse effect on the outlook for oil and gas exports. The slide in world oil prices has potential to diminish investment in the oil and gas industry, which could worsen the existing contraction in oil and gas lifting caused by natural declining in ageing oil wells. This will reduce oil and gas exports, which in turn will bring downward pressure to bear on the oil and gas trade balance. As regards to imports, oil import volume is forecasted to rise in keeping with increasing consumption of fuels, but the value of these imports will decrease in response to low global oil prices. Overall, this will bring about a slight reduction in the oil and gas trade deficit.

The capital and financial account is expected to record an increased surplus on rising inflows of foreign capital through direct investment and a reduced deficit in other investment. The larger foreign direct investment surplus is consistent with the predicted increase in gross fixed capital formation supported by improving economic fundamentals. At the same time, the shrinking deficit in other investment is explained mainly by a fall in private sector fund placements in banks abroad. On the other hand, the impact of increases in the FFR will be to reduce inflows of non-resident capital. The more robust surplus in the capital and financial account is expected to cover the current account deficit, enabling the overall Indonesia balance of payments to stay in surplus.

Outlook for Financial System Stability

In 2016, financial system stability is predicted to hold steady, bolstered by the resilience of the banking system and improving performance on the financial market. In the forecast, the capital adequacy ratio (CAR) will remain high, well above the 8% regulatory minimum. In addition, non-performing loans (NPLs) will stay low and stable. Improvement is predicted in banking liquidity in response to the launching of more expansionary government financial operations. In keeping with the upbeat growth in the economy, stronger growth is forecasted for bank deposits and credit at 13-15% and 12-14%, respectively. Th range of the projected credit expansion is still consistent with Bank Indonesia's efforts to safeguard macroeconomic and financial system stability. Bank Indonesia will continue to promote an active banking role in support of efforts to manage the economy on a more prudent course in coordination with the Financial Services Authority. Meanwhile, upbeat performance is also predicted on the stock market and government bonds market, buoyed by positive investor perceptions of future improvement in the fundamentals and outlook of the Indonesian economy.

16.2. MEDIUM-TERM OUTLOOK FOR THE ECONOMY

In the medium-term forecast to 2020, economic growth will maintain an upward trend. This is supported by an improving outlook for the global economy and the beneficial effects of various structural policies enacted by the Government. Medium-term growth in the economy may reach as much as 6.3-6.8% in 2020 (Chart 16.1). On the domestic side, investment is set to grow in tandem with construction of infrastructure projects, improvement in the business climate, reform of the bureaucracy, and increased FDI. Government spending directed more towards capital expenditures and greater efficiency in allocation of subsidies will also contribute to higher investment. Implementation of structural reform programs and a series of policy packages will pave the way for increased productivity and thus bolster the production side, which in turn will help ease dependence on imports of intermediate and capital goods. These conditions will enable volatility in the rupiah to be curbed more easily and support the achievement of low, stable inflation (Chart 16.2).

Steady growth in household consumption is predicted for the medium-term. This trend is supported by the rising proportion of the working age population, which will increase the total workforce while simultaneously bringing down the dependence ratio (Chart 16.3). The steady downward trend in poverty and growing middle class population will also stimulate growth in household consumption. In other developments, predicted improvement of the contribution from exports will strengthen public purchasing power from export earnings, thus increasing household consumption. Government consumption is projected to record higher growth, buoyed by rising government revenues in tandem with stronger economic growth and the various measures taken by the government to enhance revenues.

In the medium-term, investment growth will be closely linked to the structural reforms now under way. A very important fulfilment of the structural reforms is construction of infrastructure, which represents a major focus in the government development plan. Numerous infrastructure projects which are now under construction in a various parts of Indonesia are expected to strengthen economic growth in the regions, particularly outside Java. Structural reforms will also involve necessary improvements to the investment climate to attract more investment to Indonesia and increase the contribution of MSMEs to economic growth. This is reflected in the various policy packages launched so far to support improvement in the investment climate. Surveys by a number of international institutions show that Indonesia remains a major destination country for investment, an indication that Indonesia is steadily gaining competitiveness. Besides this, Indonesia's large and steadily growing market, particularly among the middle class, is a key driver for investment (Chart 16.4). To meet the growing and increasingly varied demand for goods and services for domestic consumption and export, it is necessary for investment to grow at a level commensurate with economic growth. In addition, there is considerable potential for investment in the MSME sector and outside Java to become a source of future economic growth.

Export growth is forecasted to improve in line with stronger global economic growth. More vibrant economic growth particularly in trading partners, positive growth in

Chart 16.1. GDP Outlook 2016-2020

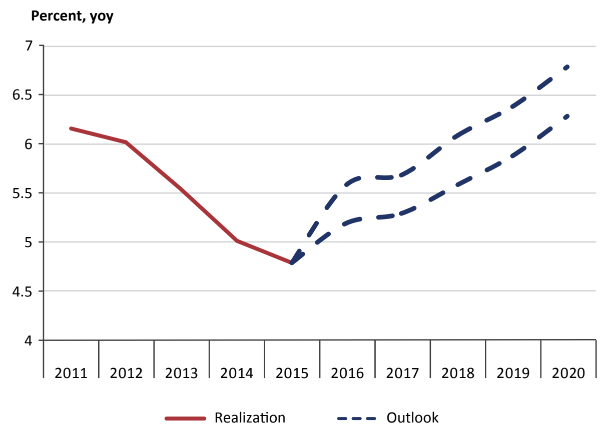


Chart 16.2. Inflation Outlook 2016 – 2020

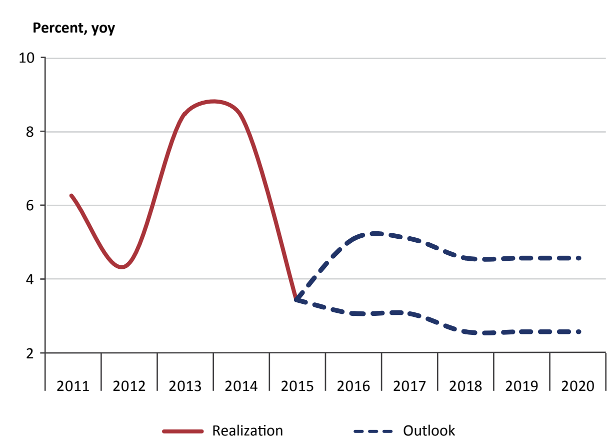
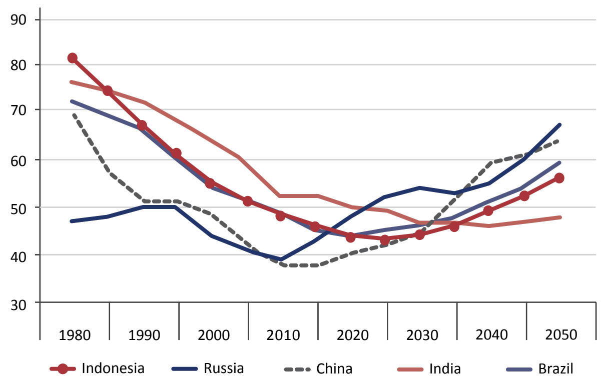


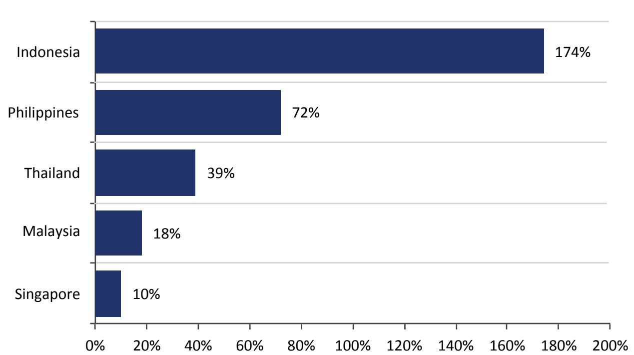
Chart 16.3. **Dependency Ratio in Indonesia and Some Regional Countries**



Source: UN-DESA, processed

commodity prices, and greater capacity for producing a wider variety of export goods are key to the forecast where contribution of exports to economic growth is expected to expand. Although some of Indonesia's major export destinations, such as China and Europe, are forecasted to experience a moderate growth trend, some of the major destination countries and regions for Indonesian exports, such as the U.S., Japan and India, are predicted to maintain an upward growth trend. In addition, the operation of smelters, exports of minerals, and processing of mining products is expected to have a positive impact on exports from increased value added. In the medium-term, export growth is predicted to climb, bolstered by measures to improve competitiveness that include a competitive exchange rate, subdued inflation and diversification of markets and products.

Chart 16.4. **Middle Class Growth**



Source: AC Nielsen

Imports are also forecasted to climb in line with the economic growth trend. In view of the projection for higher investment growth, imports of capital goods in the form of machinery and equipment are also predicted to rise. Added to this, mounting levels of production to meet domestic and foreign demand will also drive demand for imports of raw materials. Imports of consumer goods are expected to grow in line with growth in household consumption.

Inflation in the medium-term is forecasted to be in the range of 3.5$\pm$1% in 2020. Inflationary pressure from external factor will maintain a moderate trend consistent with expectations of only limited improvement in international commodity prices in the medium-term and low volatility in exchange rate movements. From the domestic side, it is expected that rising domestic demand will meet with a more robust supply-side response as structural reforms gain traction in increasing the capacity of the economy. Under these conditions, inflationary pressure from the demand side is predicted to be largely minimal. Inflation expectations will also remain low in line with implementation of monetary policy consistent with the prescribed inflation target, bolstered by strengthened policy coordination by Bank Indonesia and the Government.

In the medium-term, the balance of payments is set to improve with a sound current account deficit maintained at a sustainable level. This improvement will be driven mainly by non-oil and gas exports, where steady improvement is forecasted in line with continuing progress in global economic recovery and assumption of positive growth in non-oil and gas export commodity prices. On the other hand, higher domestic and export demand coupled with development of infrastructure will boost imports of raw materials and capital goods. In the oil and gas sector, the prospect of a gradual rebound in oil prices will affect potential improvement to oil export revenues. However, room for this improvement will become increasingly limited due to the natural decline in output from ageing oil wells. Gas exports are forecasted to maintain growth in line with the increase in assumed gas production, even in spite of the obligation to meet domestic oil and gas needs with 25% of oil and gas production. Meanwhile, oil imports are predicted to keep climbing in line with the growth of the middle class and the associated increase in fossil fuel consumption.

The forecast of steady improvement for the capital and financial account will enable it to finance the current account deficit. The more robust fundamentals of the economy achieved through implementation of the government's structural reform policies will create opportunity to stimulate capital inflows for both foreign direct investment (FDI) and placement in portfolio instruments. Through the increase in foreign capital inflows, it will be possible to meet the growing funding needs of development. Thus in the medium-term, with a prudently managed current account deficit and a surplus in the capital and financial account, Indonesia is predicted to chart a balance of payments surplus.

Risks

Looking forward, there are a number of risk factors that could still have adverse impact on the outlook for the economy. On the external side, the limited and unevenly distributed global economic growth may constrain future growth in the Indonesian economy, particularly in trade. The present composition of exports means that Indonesia's export growth is heavily influenced by demand from emerging market nations and especially China. If growth in these countries declines further than expected, Indonesia's exports may see reduced growth. Lower export growth will not only occur in terms of volume, but also value, given that the dynamics of growth in the world economy also influence international commodity prices.

Weaker international commodity prices may also trigger a reduction in potential output. If commodities remain the dominant component in Indonesia's export structure, this will carry the risk of limited growth in the potential output of Indonesia. The reason for this will be slowing investment growth in response to the depressed prospects for commodity prices. The risk arising from limited growth in potential output will then be significant inflation at the time that economic growth gathers momentum.

Despite predictions of more gradual increases in the FFR, global financial markets still pose risks related to uncertainty of further monetary policy normalization. On one hand, the prolonged lack of clarity about the consistency of economic improvement in the U.S. suggests that increases in the FFR will be gradual. On the other hand, this uncertainty could also exacerbate investor perceptions of risk. The risk of investors engaging in risk on-risk off behavior may in turn exacerbate volatility in capital flows, and fluctuation in foreign capital inflows will then increase volatile movement in the exchange rate. This may lead to postponement of investment, rising domestic inflation, and escalating risks in corporate balance sheets.

The implementation of structural reform policies also carries some risks. When structural reforms are not implemented in accordance with the initial concepts set out in the National Medium-Term Development Plan (RPJMN 2015-2019), this may affect the achievement of economic growth targets. In addition, execution of infrastructure projects with high import content has potential to exacerbate the current account deficit, given the continuing limitations of domestic capacity. This in turn may disrupt macroeconomic stability. A further concern related to the current account and structural reforms is the risk that short-comings in the downstream development of the mining sector could undermine the external balances of the economy if the potential for maximum contribution to exports from refined mining products is not realized. If the various programs and policies announced in the past are not implemented properly and fail to meet their stated targets, this will exacerbate the risk that higher levels of economic growth will not be achieved. In view of these risk factors, the implementation of structural reforms will be crucial for the economy to achieve strong, sustainable and inclusive growth.

Box 16.1. The Digital Economy as a Driver of Economic Growth

In recent times, the digital economy has become an issue of growing interest, both in Indonesia and worldwide. The digital economy itself is defined as "the virtual arena in which business actually is conducted, value is created and exchanged, transactions occur, and one-to-one relationship mature by using any internet initiative as medium of exchange" (Hartman, 2000). Initially, the concept of a digital economy consisted of three main components. First is supporting infrastructure, which includes but is not limited to hardware, software, telecommunications, networks, and so on. Second is e-business, or how the business process takes place, encompassing every process an organisation conducts over computer networks. Third is e-commerce, or how the process of transferring goods and services is also conducted over a computer network (Mesenbourg, 2001).

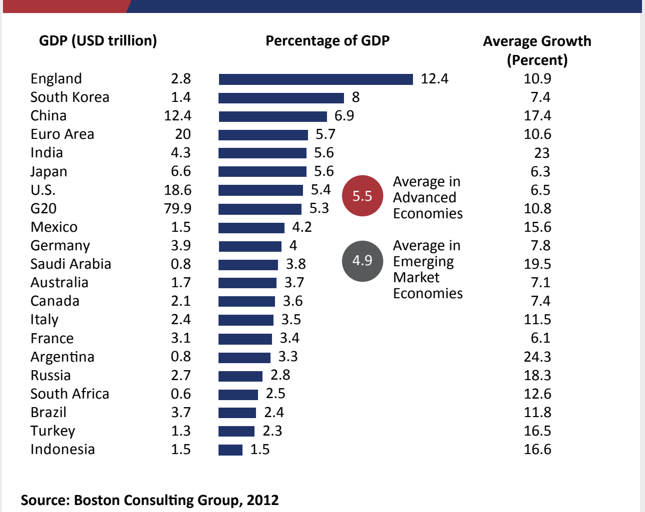
The rapid advancements in concept of the digital economy mean that it now exists in many varied forms and has taken hold in many sectors in the economy. This has implications not only for information and communication technology (ICT), but also other sectors, such as trade, transportation, finance, and health. In the retail sector, the most classical concept is that of e-commerce. In the transportation sector, the digital economy has given birth to the e-ticket concept and even automated vehicles in mass transportation. Even in the education sector, many have adopted the digital economy with open online courses, a concept initiated by Harvard University and MIT. Many books and journals are now bought and sold over the internet and in the form of soft files. In the health sector, the concept of the digital economy has been adopted in numerous forms, such as electronic records or even medical diagnoses presented with numbers and charts on a monitor.

The rapid expansion of the digital economy across the world is illustrated by a number of indicators. Investment in telecommunications is high and on a steady upward trend. The OECD (2015) notes that since 2000, worldwide investment in telecommunications has averaged 200 billion US dollars per year. As a result, the total number of telephone connections, consisting of analogue, digital (IDSN and DSL), modem, fibre optic, and cellular connections, reached about 2.1 billion in 2013. Fixed line telephones have been in decline since 2001, an indication of the growing preference of the world's citizens for mobile telephones. The number of internet users also continues to grow, particularly in Asia (Chart 1). In 2016, the internet-based digital economy is expected to reach 5.5% of GDP in the G20 members with advanced economies and 4.9% of GDP in the developing countries of the G20 (Chart 2).This phenomenal growth in the digital economy has been spurred by the positive impact of its use. The study by OECD (2014) has shown that industries operating in information technology in the OECD nations enjoy higher labor productivity compared to that of the economy as a whole (Chart 3). This demonstrates that the use of digital technology has increased worker productivity. OECD data also points to the resilience of revenues earned by the top 250 ICT corporate players when the global financial crisis struck. While the revenues of these companies

Chart 1. Number of Internet Users

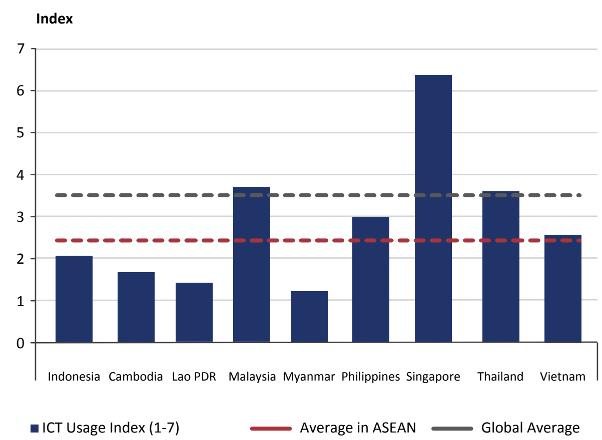
Source: Emarketer

Chart 2. Development of Internet as a Percentage of GDP



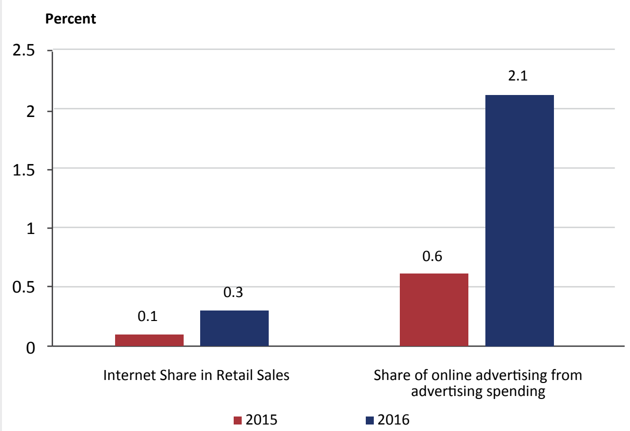
Source: Boston Consulting Group, 2012

Chart 3. **Usage Index of ICT in 2015**



Source: Global Competitiveness Index, World Economic Forum, 2015

Chart 4. **The Impact of e-Commerce in Indonesia**



Source: Boston Consulting Group, 2012

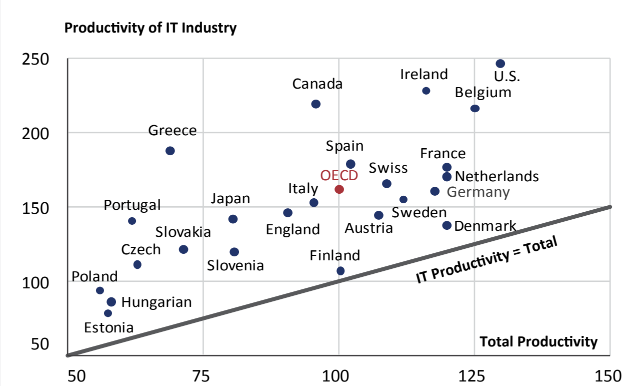
indeed declined, they bounced back quickly. The positive impact of the use of digital technology is also evident in World Bank study showing that each additional 10 mobile telephones per 100 persons will bring about an 0.8% increase in the GDP in developing countries.

The digital economy has not only made economies more efficient, but also has consequences for the process of creative destruction (Schumpeter, 1942). An example is the competition between conventional transportation services and those using digital technology, as well as the competition between conventional shops and online shops. Due to its various advantages, digital technology will gradually displace conventional ways of doing business. During this transition process, there will be potential for adverse impact on the economy. On one hand, the use of digital technology will raise productivity and reduce production costs so that as a rule, customers will be better off. On the other hand, the conventional ways of doing business generally provide more jobs. Use of digital technology has the potential to displace conventional business and thus reduce employment.

In Indonesia, growth in the digital economy is expected to gather pace. At this time, the level of advancement lags somewhat behind, as indicated by the lower index for use of ICT compared to world and ASEAN averages (Chart 4). However, with the accelerated completion of ICT infrastructure projects, the digital economy is expected to gain more rapid momentum in Indonesia in keeping with the vast size of the market. Several studies about Indonesia (BCG, 2012) point to the impact of using the digital economy. In particular, internet use is predicted to climb from 0.1% of total sales in 2010 to 0.3% in 2016. Shopping purchases conducted with the method of Research Online Purchase Offline (ROPO), meaning that the buyer selects goods via online media and purchase offline, average about 16 US dollars per online user. With the growing activity of online shopping, spending on online advertising is also expected to climb from about 0.6% of total shopping advertising in 2010 to 2.1% in 2016 (Chart 5). The latest research also suggests that digital involvement of small and medium enterprises (SMEs) would boost Indonesia's annual economic growth rate by 2% (Deloitte, 2015).

To prepare the way for the development of the digital economy and its significant effects on the economy as

Chart 5. **Productivity of IT Industry, OECD**



Source: OECD

a whole, the Government has prepared an e-commerce road map with emphasis on seven issues of strategic importance: (i) logistics, (ii) funding, (iii) consumer protection, (iv) communication infrastructure, (v) taxes, (vi) education and human resources, and (vii) cyber security. In logistics, preparations involve the use of the National Logistics System (SISLOGNAS) blueprint to increase the speed of e-commerce logistic deliveries and reduce delivery costs. In funding, efforts include the finalisation of the Draft Government Regulation concerning e-commerce and establishment of a Public Services Agency that would be able to extend grants to digital MSMEs. Preparations in consumer protection include the building of consumer confidence through regulation, protection of industry participants and the phased development of the national Payment Gateway that will offer improved electronic retail payment services.

As envisaged in government programs, communications infrastructure will be upgraded and improved as it comprises the backbone to growth in the e-commerce industry. In addition to infrastructure, a further strategy to promote the digital economy is being pursued in taxation. The strategy to be executed includes simplification of taxation obligations and taxation procedures for e-commerce startup and provision of tax incentives for e-commerce investors. In addition, education will be provided for the entire e-commerce ecosystem in an effort to improve the education and qualifications of human resources working in this field. This will be complemented by awareness raising for online retailers and the public about cybercrime and the importance of security in electronic transactions. These government policies are expected to help the growth of the digital economy to generate positive impact for the economy as a whole.

APPENDICES

Bank Indonesia Regulation

No.	Regulation No.	Date	Description
1	PBI No. 17/1/PBI/2015	January 30, 2015	Nominal Amount and Value of Rupiah Removed from Circulation 2014
2	PBI No. 17/2/PBI/2015	March 26, 2015	Interbank Offered Rate
3	PBI No. 17/3/PBI/2015	March 31, 2015	Mandatory Use of Rupiah within the Territory of the Republic of Indonesia
4	PBI No. 17/4/PBI/2015	April 27 2015	Sharia Interbank Money Market
5	PBI No. 17/5/PBI/2015	May 29, 2015	Fourth Amendment of PBI No. 5/13/PBI/2003 concerning the Net Open Position for Commercial Banks
6	PBI No. 17/6/PBI/2015	May 29, 2015	Amendment to Bank Indonesia Regulation Number 16/16/PBI/2014 on Foreign Exchange Transactions against Rupiah between the Bank and the Domestic Party
7	PBI No. 17/7/PBI/2015	May 29, 2015	Amendment to Bank Indonesia Regulation Number 16/17/PBI/2014 on Foreign Exchange Transactions against Rupiah between the Bank and the Foreign Party
8	PBI No. 17/8/PBI/2015	May 29, 2015	Regulation and Monetary Supervision
9	PBI No. 17/9/PBI/2015	May 29, 2015	Implementation of Fund Transfer and Scheduled Clearing by Bank Indonesia
10	PBI No. 17/10/PBI/2015	June 18, 2015	Loan to Value Ratio or Financing to Value Ratio for Loan or Financing Facilities for Property and Advance Payments for Loans or Financing Facilities for Motor Vehicles
11	PBI No. 17/11/PBI/2015	June 25, 2015	Amendment to Bank Indonesia Regulation Number 15/15/PBI/2013 concerning Reserves Requirement for Commercial Banks in Rupiahs and Foreign currency Share Conventional Commercial Bank
12	PBI No. 17/12/PBI/2015	June 25, 2015	Amendment to Bank Indonesia Regulation Number 14/22/PBI/2012 on Lending or financing by commercial banks and technical assistance in Developing Micro, Small, and Medium Enterprises
13	PBI No. 17/13/PBI/2015	August 25, 2015	Second amendment on PBI Number 16/16/PBI/2014 regarding Foreign Exchange Transaction against Rupiah between Bank and Local Parties
14	PBI No. 17/14/PBI/2015	August 25, 2015	Second amendment on PBI Number 16/17/PBI/2014 regarding Foreign Exchange Transaction against Rupiah between Bank and Foreign Parties.
15	PBI No. 17/15/PBI/2015	October 2, 2015	Third Amendment to Bank Indonesia Regulation Number 16/16/PBI/2015 concerning the Foreign Exchange Transactions against Rupiah between Bank and Domestic Parties
16	PBI No. 17/16/PBI/2015	October 2, 2015	Third Amendment to Bank Indonesia Regulation Number 16/17/PBI/2015 concerning the Foreign Exchange Transactions against Rupiah between Bank and Foreign Parties
17	PBI No. 17/17/PBI/2015	November 10, 2015	Bank Indonesia Commercial Papers in Foreign Currency ("SBBI Valas").
18	PBI No. 17/18/PBI/2015	November 12, 2015	Transactions Implementation, Securities Administration, and Instantly Fund Settlement
19	PBI No. 17/19/PBI/2015	November 12, 2015	Second Amendment to Bank Indonesia Regulation Number 10/13/PBI/2008 concerning the Auction and Administration of Government Bond
20	PBI No. 17/20/PBI/2015	November 12, 2015	Third Amendment to Bank Indonesia Regulation Number 12/11/PBI/2010 on Monetary Operations
21	PBI No. 17/21/PBI/2015	November 26, 2015	Second Amendment to Bank Indonesia Regulation Number 15/15/PBI/2013, regarding the Statutory Reserve of Commercial Banks in Rupiah and Foreign Currency for Conventional Commercial Banks
22	PBI No. 17/22/PBI/2015	December 23,2015	Mandatory Countercyclical Buffers
23	PBI No. 17/23/PBI/2015	December 23, 2015	Amendment to Bank Indonesia Regulation Number 16/10/PBI/2014, regarding Foreign-Exchange Revenues from Export Proceeds and the Withdrawal of Foreign-Exchange Debt
24	PBI No. 17/24/PBI/2015	December 30, 2015	Demand Deposit Account at Bank Indonesia

Regulations and Policies in Economic and Finance Area in 2015

Date	Description	Regulation
January		
6	Second Amendment to the Regulation of the Minister of Finance Number 196 / PMK.03 / 2007 on Procedures for Bookkeeping Implementation by Using Foreign Language and Currency Unit Other Than Rupiah As Well As the Liability for Submission of Annual Income Tax Return of Agency Taxpayer	Regulation of the Minister of Finance No. 1/PMK.03/2015
February		
13	Elimination of Tax Administrative Sanctions in the form of interest based on the Article 19 Paragraph (1) of Law No.6 of 1983 on General Provisions and Tax Procedures (KUP) granted taxpayers waiver on penalty for late payment of tax debts	Regulation of the Minister of Finance No. 29/PMK.03/2015
19	Government Food Reserves	Government Regulation No. 17/2015
24	The Types and Tariffs of Non-Tax State Revenue Applicable to the Technology Assessment and Application Body	Government Regulation No. 6/2015
March		
6	Master Plan of national industry Development year 2015-2035	Government Regulation No. 14/2015
12	Treatment of Value Added Tax ("VAT") for the Transfer of Fuel to Foreign Sea Transportation Vessels	Government Regulation No.15/2015
26	Standard Input Fiscal Costs Year 2016	Regulation of the Minister of Finance No.65/PMK.02/2015
April		
6	Income tax facilities for companies which invest in certain business sectors and/or regions	Government Regulation No. 18/2015
29	Amendment to Government Regulation Number 60 Year 2014 On The Village Fund Sourced From Budget Revenue and Expenditure	Government Regulation No. 22/2015
May		
25	Amendment to the Regulation of the Minister of Finance Number 115/PMK.07/2013 on Procedures for Cigarette Tax Withholding and remittance.	Regulation of the Minister of Finance No. 65/PMK.02/2015
25	Amendment to the Minister of Finance Regulation Number 70/PMK.04/2009 regarding the Periodical Excise Payment Facility for Factory Entrepreneurs that Settle Their Excise Payables by Applying the Payment Method	Regulation of the Minister of Finance No. 103/PMK.04/2015
28	Second Amendment to the Regulation of the Minister of Finance Number 125/PMK.06/2011 on the Management of State Property Originating concentration Fund And Tasks Fund Prior Fiscal Year 2011	Regulation of the Minister of Finance No. 104/PMK.06/2015
June		
8	Types of Goods Other than Automobiles Subject to Luxury Sales Tax	Regulation of the Minister of Finance No. 106/PMK.010/2015
8	Fourth Amendment to the Regulation of the Minister of Finance Number 154/PMK.03/2010 concerning the Collection of Article 22 Income Tax in Connection with the Payment of the Delivery of Goods and Activities in the Import Sector or Business Activity in Other Sectors	Regulation of the Minister of Finance No. 107/PMK.010/2015
23	Development of Industrial Resources	Government Regulation No. 41/2015
July		
7	Budget classification	Regulation of the Minister of Finance No. 127/PMK.02/2015
27	Amendment to the Regulation of the Minister of Finance Number 257/PMK.02/2014 concerning Revised Budget Procedures for Fiscal Year 2015	Regulation of the Minister of Finance No. 140/PMK.02/2015
27	Guidelines for Preparation and Review on Ministry Work Plan and Budget (RKA-KL) and Legalization of Budget Execution Document (DIPA)	Regulation of the Minister of Finance No. 143/PMK.02/2015
30	The Implementation of the Subsidy for Interest on People's Business Credit	Regulation of the Minister of Finance No. 146/PMK.05/2015
August		
4	Amendment to Government Regulation Number 77 of 2013 concerning the Reduction of Income Tax Tariffs for Domestic Corporate Taxpayers in the Form of Public Companies	Government Regulation No. 56/2015
4	Quality and Safety Assurance System for Fishery Products and Increasing the Added Value of Fishery Products	Government Regulation No. 57/2015

Regulations and Policies in Economic and Finance Area in 2014 - Continued

Date	Description	Regulation
September		
4	Types and Tariffs of Non-Tax State Revenue that Can Be Applied by the Commission for the Supervision of Business Competition (“KPPU”).	Government Regulation No. 68/2015
17	The Import and Delivery of Certain Transportation Equipment and Delivery of Taxable Services Related to Certain Transportation Equipment Exempted from Value Added Tax	Government Regulation No. 69/2015
October		
27	Amendment to the Minister of Finance Regulation Number 143/PMK.02/2015 on Guidelines for Preparation and Study Work Plan and Ministry / Agency Budget and the Budget Implementation List Approval	Regulation of the Minister of Finance No. 196/PMK.02/2015
November		
9	Second Amendment to Government Regulation Number 29 of 2000 concerning the Implementation of Construction Services	Government Regulation No. 79/2015
9	Import and/or Transfer of Certain Strategic Taxable Goods Exempted from Value Added Tax	Government Regulation No. 81/2015
20	Amendment to MOF Regulation Number 106/PMK.010/2015 concerning Luxury Taxable Goods Other Than Motorized Vehicles that are Subject to Sales Tax on Luxury Goods. This regulation amends the first attachment of the former regulation	Regulation of the Minister of Finance No. 206/PMK.010/2015
December		
22	Filing Procedures for Multiple Year Contract Agreement (Multi- Years Contract) in the Government Goods / Services Procurement to the Minister of Finance	Regulation of the Minister of Finance No. 238/PMK.02/2015

Table 1. **Gross Domestic Product by Expenditures [1)]**

In Billions of IDR

Type of Expenditures	2011	2012	2013	2014*	2015**				
					I	II	III	IV	TOTAL
Constant Prices									
1. Private Consumption Expenditure	**3,977,289**	**4,195,788**	**4,423,417**	**4,651,480**	**1,188,729**	**1,202,797**	**1,245,314**	**1,245,418**	**4,882,259**
a. Food and Beverages, except of Restaurant	1,489,545	1,545,636	1,612,839	1,684,170	433,448	439,621	452,767	450,448	1,776,284
b. Clothing and Services Related	162,350	172,878	182,010	190,255	48,263	48,946	50,365	49,703	197,277
c. Dwelling and Utilities Related	543,181	575,044	608,427	636,100	163,022	164,095	169,335	170,364	666,817
d. Health and Education Services	268,834	284,509	300,791	319,311	81,635	83,627	86,732	86,997	338,991
e. Transportation and Communication	953,674	1,018,099	1,085,322	1,148,242	291,433	295,065	307,404	307,267	1,201,170
f. Restaurant and Hotel	355,868	381,367	403,321	430,865	109,279	109,844	115,659	117,248	452,031
g. Others	203,836	218,255	230,706	242,536	61,648	61,598	63,052	63,390	249,688
2. NPI Serving Household Consumption Expenditure	**76,790**	**81,919**	**88,618**	**99,420**	**23,610**	**24,133**	**25,177**	**25,869**	**98,789**
3. Government Consumption Expenditure	**652,292**	**681,819**	**727,812**	**736,283**	**133,868**	**176,555**	**192,911**	**272,591**	**775,925**
a. Collective Consumption	407,985	420,887	455,890	459,596	81,984	106,696	121,149	167,473	477,302
b. Individual Consumption	244,307	260,931	271,922	276,687	51,884	69,859	71,762	105,118	298,623
4. Gross Fixed Capital Formation	**2,316,359**	**2,527,729**	**2,654,375**	**2,775,734**	**691,587**	**712,666**	**737,706**	**774,642**	**2,916,602**
a. Building	1,675,389	1,811,558	1,933,672	2,040,387	508,742	526,069	549,802	582,906	2,167,519
b. Machineries and Equipment	273,416	306,654	307,782	294,160	72,277	71,411	73,786	75,740	293,214
c. Transportation	143,012	171,259	161,592	147,968	35,759	35,844	39,098	38,116	148,817
d. Other Equipment	34,348	35,908	37,472	40,294	10,160	10,817	11,522	12,013	44,513
e. Cultivated Biological Resources	139,609	146,767	149,080	162,746	43,842	41,550	39,954	45,185	170,532
f. Intellectual Property Product	50,585	55,583	64,776	90,179	20,807	26,975	23,544	20,681	92,006
5. a. Changes in Inventories	**118,207**	**174,183**	**124,454**	**156,720**	**55,061**	**57,015**	**58,385**	**-57,613**	**112,848**
b. Statistical Discrepancies [1)]	1,252	30,882	57,576	88,875	33,687	31,133	338	-8,240	56,918
6. Export of Goods and Services	**1,914,268**	**1,945,064**	**2,026,114**	**2,046,296**	**498,477**	**505,674**	**505,581**	**496,213**	**2,005,945**
a. Goods	1,746,663	1,761,024	1,828,150	1,842,722	451,246	455,293	451,848	442,572	1,800,958
a.1. Non-Oil	1,442,177	1,479,142	1,584,709	1,607,801	389,863	393,836	384,535	373,726	1,541,959
a.2. Oil and Gas	304,486	281,882	243,441	234,921	61,383	61,457	67,314	68,846	258,999
b. Services	167,605	184,039	197,964	203,574	47,231	50,381	53,733	53,641	204,987
7. Less Import of Goods and Services	**1,768,822**	**1,910,300**	**1,945,867**	**1,988,537**	**468,551**	**472,560**	**452,719**	**478,524**	**1,872,353**
a. Goods	1,495,888	1,632,008	1,665,064	1,705,062	403,314	403,524	386,815	407,130	1,600,784
a.1. Non-Oil	1,203,515	1,326,281	1,338,229	1,378,479	326,607	321,856	305,248	326,707	1,280,418
a.2. Oil and Gas	292,373	305,727	326,835	326,583	76,707	81,668	81,567	80,423	320,365
b. Services	272,934	278,291	280,803	283,475	65,236	69,035	65,904	71,394	271,570
8. GROSS DOMESTIC PRODUCT	**7,287,635**	**7,727,083**	**8,156,498**	**8,566,271**	**2,156,469**	**2,237,413**	**2,312,693**	**2,270,357**	**8,976,932**
Current Prices									
1. Private Consumption Expenditure	**4,260,076**	**4,768,745**	**5,321,088**	**5,915,742**	**1,547,657**	**1,582,873**	**1,654,724**	**1,667,952**	**6,453,206**
a. Food and Beverages, except of Restaurant	1,638,644	1,854,629	2,049,782	2,248,519	590,744	606,533	630,764	637,249	2,465,290
b. Clothing and Services Related	175,860	187,041	203,088	222,284	57,733	58,987	61,443	60,709	238,872
c. Dwelling and Utilities Related	569,629	637,060	705,522	780,828	210,222	212,962	220,872	223,505	867,561
d. Health and Education Services	290,850	327,738	359,752	395,785	103,803	106,741	113,164	113,883	437,590
e. Transportation and Communication	993,369	1,085,926	1,246,467	1,416,823	360,273	370,441	388,904	388,948	1,508,566

Table 1.	Gross Domestic Product by Expenditures [1] - Continued

Type of Expenditures	2011	2012	2013	2014*	2015**				
					I	II	III	IV	TOTAL
f. Restaurant and Hotel	385,156	443,100	499,346	565,281	147,813	149,359	158,557	161,445	617,173
g. Others	206,569	233,251	257,131	286,222	77,069	77,849	81,021	82,213	318,153
2. NPI Serving Household Consumption Expenditure	**80,530**	**89,586**	**103,929**	**124,242**	**30,673**	**31,790**	**33,588**	**34,885**	**130,936**
3. Government Consumption Expenditure	**709,451**	**796,848**	**908,574**	**996,197**	**180,350**	**253,906**	**292,930**	**398,356**	**1,125,542**
a. Collective Consumption	444,289	492,963	568,131	622,774	110,529	153,664	183,831	245,283	693,307
b. Individual Consumption	265,162	303,885	340,443	373,423	69,821	100,242	109,100	153,073	432,235
4. Gross Fixed Capital Formation	**2,451,914**	**2,819,026**	**3,051,496**	**3,442,027**	**896,207**	**933,377**	**970,381**	**1,030,013**	**3,829,978**
a. Building	1,791,932	2,053,896	2,242,780	2,569,122	673,690	699,422	732,171	780,795	2,886,078
b. Machineries and Equipment	280,002	329,147	343,132	350,149	86,778	89,449	94,004	97,381	367,612
c. Transportation	146,580	179,039	172,446	159,332	39,401	39,806	44,372	45,869	169,448
d. Other Equipment	35,531	38,480	41,709	48,786	12,954	14,151	15,352	16,086	58,543
e. Cultivated Biological Resources	145,934	159,227	177,280	204,747	57,522	56,328	54,459	63,187	231,497
f. Intellectual Property Product	51,934	59,236	74,149	109,891	25,862	34,220	30,023	26,696	116,800
5. a. Changes in Inventories	**131,329**	**202,638**	**178,091**	**210,407**	**77,779**	**81,947**	**86,431**	**-87,403**	**158,754**
b. Statistical Discrepancies [1]	4,616	-27,181	58,392	-39,387	-19,093	-22,240	-64,749	-79,963	-186,045
6. Export of Goods and Services	**2,061,886**	**2,118,979**	**2,283,777**	**2,497,116**	**599,343**	**620,620**	**620,364**	**593,854**	**2,434,181**
a. Goods	1,890,412	1,918,040	2,044,358	2,223,342	532,066	546,850	539,218	512,815	2,130,950
a.1. Non-Oil	1,528,932	1,572,451	1,703,499	1,869,262	459,445	491,075	478,483	455,598	1,884,601
a.2. Oil and Gas	361,481	345,589	340,859	354,080	72,621	55,775	60,735	57,217	246,349
b. Services	171,474	200,939	239,419	273,774	67,276	73,769	81,146	81,039	303,231
7. Less Import of Goods and Services	**1,868,075**	**2,152,937**	**2,359,212**	**2,580,527**	**584,644**	**613,405**	**595,048**	**612,666**	**2,405,762**
a. Goods	1,596,456	1,850,040	2,012,940	2,177,253	484,873	503,961	486,711	493,826	1,969,371
a.1. Non-Oil	1,230,538	1,439,293	1,523,386	1,652,354	405,478	410,610	398,068	421,036	1,635,191
a.2. Oil and Gas	365,918	410,747	489,554	524,899	79,395	93,351	88,643	72,790	334,180
b. Services	271,619	302,897	346,272	403,274	99,771	109,444	108,337	118,840	436,391
8. GROSS DOMESTIC PRODUCT	**7,831,726**	**8,615,705**	**9,546,134**	**10,565,817**	**2,728,272**	**2,868,867**	**2,998,622**	**2,945,029**	**11,540,790**

Notes:
[1] Since year 2010, GDP figures using 2010=100 as a base year
*) Provisional figures
**) Very Provisional figures

Source: BPS-Statistics Indonesia

Table 2. **Gross Domestic Product by Industrial Origin at Constant Prices [1)]**

In Billions of IDR

Industrial Origin	2011	2012	2013	2014*	2015**				
					I	II	III	IV	TOTAL
Agriculture, Forestry and Fishery	**993,857**	**1,039,441**	**1,083,142**	**1,129,053**	**282,703**	**311,897**	**328,235**	**251,622**	**1,174,457**
Agriculture, Livestock, Hunting, and Agriculture Services	780,581	816,304	847,764	880,390	220,545	245,549	261,700	181,778	909,571
Food crops	250,787	263,076	268,268	268,427	82,730	78,064	78,027	38,952	277,773
Horticultural crops	120,079	117,425	118,208	124,301	30,185	34,450	34,641	28,125	127,401
Plantation crops	281,465	301,020	319,533	338,502	69,862	94,734	109,353	76,541	350,490
Livestock	113,603	119,250	125,302	132,221	33,319	33,695	34,739	34,559	136,313
Agricultural Services and Hunting	14,646	15,534	16,453	16,938	4,448	4,606	4,939	3,601	17,594
Forestry and Logging	58,731	58,872	59,229	59,574	13,390	16,391	15,058	15,127	59,966
Fishery	154,545	164,264	176,149	189,090	48,768	49,957	51,477	54,717	204,920
Mining and Quarrying	**748,956**	**771,562**	**791,054**	**796,712**	**190,253**	**186,558**	**189,930**	**189,499**	**756,239**
Crude Petroleum, Natural Gas, and Geothermal	335,737	323,632	313,328	306,855	75,058	76,314	77,499	78,389	307,259
Coal and Lignite Mining	199,244	230,589	247,595	248,475	55,575	46,763	46,736	47,490	196,564
Iron Ore mining	95,414	91,615	98,609	98,318	21,471	24,597	24,516	24,507	95,092
Other Mining and Quarrying	118,562	125,726	131,523	143,063	38,148	38,885	41,179	39,112	157,324
Manufacturing	**1,607,452**	**1,697,787**	**1,771,962**	**1,853,688**	**468,061**	**484,535**	**488,892**	**490,970**	**1,932,457**
Manufacture of Coal and Refined Petroleum Products	233,052	227,456	221,450	216,182	52,043	52,097	53,761	54,474	212,375
Manufacture of Food Products and Beverages	400,004	441,342	459,283	502,856	126,979	138,564	138,510	136,721	540,774
Manufacture of Tobacco Products	67,097	73,011	72,814	78,879	19,429	20,617	21,519	22,389	83,953
Manufacture of Textiles and Wearing Apparel	102,561	108,754	115,913	117,723	28,395	28,335	27,774	27,575	112,079
Manufacture of Leather and Related Products and Footware	21,852	20,665	21,746	22,968	5,747	5,986	5,858	6,291	23,882
Manufacture of Wood and Products of Wood and Cork, Articles of Straw and Plaiting Materials	55,231	54,787	58,181	61,743	15,338	15,263	14,801	15,208	60,609
Manufacture of Paper and Paper products Printing and Reproduction of Recorded Media	70,632	68,590	68,229	70,670	17,510	17,658	17,920	17,502	70,589
Manufacture of Chemicals and Pharmaceuticals and Botanical Products	124,231	140,102	147,249	153,192	41,905	40,579	41,478	40,503	164,464
Manufacture of Rubber, Rubber Products, and Plastic Products	68,153	73,307	71,946	72,777	18,291	19,750	19,434	18,977	76,452
Manufacture of Other Nonmetallic Mineral Products	54,910	59,252	61,229	62,707	15,831	16,620	16,654	17,477	66,582
Manufacture of Basic Metals	61,860	60,889	67,972	72,059	18,687	19,301	19,107	19,633	76,729
Manufacture of Fabricated Metal Products, Computer, Optical Products, and Electronic Devices	142,245	158,804	173,452	178,544	46,208	48,145	48,081	50,090	192,524
Manufacture of Machinery and Equipment	25,795	25,437	24,164	26,260	6,417	6,868	7,468	7,474	28,227
Manufacture of Transport Equipment	142,815	148,905	171,166	178,023	45,276	44,248	46,138	46,515	182,176
Manufacture of Furniture	22,062	21,589	22,375	23,180	5,947	6,275	6,131	5,985	24,338
Other Manufacturing, Repair and Installation of Machinery and Equipment	14,954	14,897	14,794	15,926	4,059	4,230	4,259	4,157	16,705
Electricity and Gas Supply	**76,678**	**84,393**	**88,805**	**93,756**	**22,721**	**23,728**	**23,526**	**24,920**	**94,895**
Electricity	63,385	70,827	75,051	79,280	19,430	20,440	20,193	21,343	81,407
Gas Supply and Production of Ice	13,294	13,567	13,754	14,476	3,291	3,288	3,333	3,577	13,488
Water Supply, Sewerage, Waste Management and Remediation Activities	**6,125**	**6,330**	**6,540**	**6,924**	**1,788**	**1,850**	**1,888**	**1,893**	**7,420**

Table 2. **Gross Domestic Product by Industrial Origin at Constant Prices [1] - Continued**

Industrial Origin	2011	2012	2013	2014*	2015**				
					I	II	III	IV	TOTAL
Construction	683,422	728,226	772,720	826,616	206,755	213,247	223,650	237,932	881,584
Wholesale and Retail Trades, Repair of Motor Vehicles and Motorcycles	1,013,200	1,067,912	1,119,272	1,177,049	291,614	302,687	308,128	303,647	1,206,075
Wholesale and Retail Trade and Repair of Motor Vehicles and Motorcycles	190,878	203,431	218,291	229,229	57,190	56,306	58,055	58,756	230,307
Wholesale and Retail Trades, except of Motor Vehicles and Motorcycles	822,322	864,481	900,981	947,820	234,423	246,381	250,073	244,891	975,768
Transport and Storage	265,774	284,663	304,506	326,933	82,907	85,848	89,347	90,674	348,776
Railways Transport	2,298	2,202	2,337	2,823	683	719	764	784	2,950
Land Transport	145,019	155,852	167,560	180,367	46,719	47,304	49,434	49,801	193,257
Sea Transport	23,542	25,601	27,372	29,474	7,028	7,474	7,691	7,980	30,174
River, Lake and Ferry Transport	8,813	9,057	9,469	10,118	2,462	2,477	2,646	2,637	10,222
Air Transport	43,917	47,030	49,263	52,255	13,216	14,265	14,703	15,005	57,189
Warehousing and Support Services for Transportation, Postal and Courier	42,185	44,921	48,505	51,896	12,798	13,609	14,110	14,467	54,983
Accommodation and Food Service Activities	214,022	228,233	243,748	257,816	65,513	66,670	67,741	69,130	269,055
Accommodation	39,785	43,567	47,700	51,427	12,906	13,499	13,837	14,400	54,641
Food and Beverages Service Activities	174,237	184,665	196,049	206,389	52,608	53,171	53,904	54,731	214,414
Information and Communication	281,694	316,279	349,150	384,407	102,000	104,193	107,514	109,357	423,064
Financial and Insurance Services	256,443	280,896	305,515	319,826	84,212	82,667	88,522	91,695	347,096
Financial Intermediary Services	158,504	175,168	192,098	197,712	52,308	50,261	55,623	58,439	216,631
Insurance and Pension Fund	55,802	60,045	64,661	69,795	18,174	18,454	18,725	19,046	74,398
Other Financial Services	35,860	38,868	41,372	44,465	11,683	11,888	12,101	12,130	47,801
Financial Supporting Services	6,277	6,815	7,384	7,854	2,048	2,065	2,073	2,080	8,266
Real Estate Activities	213,441	229,254	244,238	256,440	66,142	66,853	67,661	68,155	268,811
Business Services	108,239	116,293	125,491	137,795	36,062	36,703	37,491	38,139	148,396
Public Administration and Defence; Compulsory Social Security	276,337	282,235	289,449	296,330	74,361	74,777	76,471	84,785	310,394
Education	215,029	232,704	250,016	263,890	65,421	69,616	70,901	77,602	283,540
Human Health and Social Work Activities	72,592	78,380	84,621	91,357	23,012	23,753	24,644	26,433	97,841
Other Services Activities	109,372	115,675	123,083	134,070	35,139	35,842	36,597	37,324	144,902
Gross Value Added At Basic Price	7,142,634	7,560,263	7,953,312	8,352,660	2,098,663	2,171,425	2,231,136	2,193,777	8,695,000
Taxes less Subsides on Products	145,001	166,821	203,186	213,612	57,806	65,988	81,557	76,580	281,931
Gross Domestic Product	7,287,635	7,727,083	8,156,498	8,566,271	2,156,469	2,237,413	2,312,693	2,270,357	8,976,932

Notes:
[1] Since year 2010, GDP figures using 2010=100 as a base year
*) Provisional figures
**) Very Provisional figures

Source: BPS-Statistics Indonesia

Table 3. **Gross Domestic Product by Industrial Origin at Current Prices [1)]**

In Billions of IDR

Industrial Origin	Constant Prices				
	2011	2012	2013	2014*	2015**
Agriculture, Forestry and Fishery	**1,058,245**	**1,152,262**	**1,275,048**	**1,409,656**	**1,560,399**
Agriculture, Livestock, Hunting, and Agriculture Services	832,514	902,126	994,778	1,089,550	1,186,521
Food crops	270,977	305,671	332,112	343,252	393,372
Horticultural crops	125,286	125,108	137,369	160,569	175,165
Plantation crops	303,403	323,362	358,172	398,261	411,863
Livestock	117,257	130,614	147,982	167,008	183,444
Agricultural Services and Hunting	15,591	17,372	19,143	20,460	22,677
Forestry and Logging	62,248	65,882	69,599	74,618	81,743
Fishery	163,484	184,254	210,671	245,488	292,136
Mining and Quarrying	**924,813**	**1,000,308**	**1,050,746**	**1,042,901**	**879,400**
Crude Petroleum, Natural Gas, and Geothermal	444,068	492,894	520,088	508,911	382,681
Coal and Lignite Mining	253,026	270,519	282,193	257,236	198,882
Iron Ore mining	104,284	100,845	98,468	93,898	80,286
Other Mining and Quarrying	123,436	136,050	149,996	182,856	217,551
Manufacturing	**1,704,251**	**1,848,151**	**2,007,427**	**2,219,441**	**2,405,409**
Manufacture of Coal and Refined Petroleum Products	284,099	298,403	314,216	329,058	307,704
Manufacture of Food Products and Beverages	410,387	457,773	491,142	562,017	647,002
Manufacture of Tobacco Products	71,735	79,340	82,684	95,668	108,860
Manufacture of Textiles and Wearing Apparel	108,192	116,558	129,912	139,032	139,394
Manufacture of Leather and Related Products and Footware	22,045	21,687	24,810	28,600	31,445
Manufacture of Wood and Products of Wood and Cork, Articles of Straw and Plaiting Materials	59,501	60,629	66,958	76,072	77,821
Manufacture of Paper and Paper products, Printing and Reproduction of Recorded Media	75,308	73,665	74,319	84,373	87,801
Manufacture of Chemicals and Pharmaceuticals; and Botanical Products	124,717	143,460	157,042	180,037	209,288
Manufacture of Rubber, Rubber Products and Plastic Products	72,006	76,425	76,466	80,263	85,962
Manufacture of Other Nonmetallic Mineral Products	55,606	63,028	69,401	76,852	83,492
Manufacture of Basic Metals	62,846	64,557	74,495	82,119	90,389
Manufacture of Fabricated Metal Products, Computer, Optical Products and Electronic Devices	142,059	162,970	186,195	198,081	226,662
Manufacture of Machinery and Equipment	23,376	24,832	25,504	33,079	37,255
Manufacture of Transport Equipment	154,864	166,391	192,768	207,401	220,360
Manufacture of Furniture	21,985	22,487	24,931	28,118	31,281
Other Manufacturing, Repair and Installation of Machinery and Equipment	15,523	15,947	16,584	18,673	20,693
Electricity and Gas Supply	**91,722**	**95,638**	**98,687**	**114,618**	**131,264**
Electricity	72,816	73,350	74,358	83,842	102,083
Gas Supply and Production of Ice	18,906	22,288	24,329	30,776	29,181
Water Supply, Sewerage, Waste Management and Remediation Activities	**6,209**	**6,604**	**7,209**	**7,887**	**8,606**
Construction	**712,184**	**805,208**	**905,991**	**1,041,950**	**1,193,346**

Table 3. **Gross Domestic Product by Industrial Origin at Current Prices [1) - Continued**

Industrial Origin	Constant Prices				
	2011	2012	2013	2014*	2015**
Wholesale and Retail Trades, Repair of Motor Vehicles and Motorcycles	**1,066,092**	**1,138,484**	**1,261,146**	**1,420,054**	**1,534,067**
Wholesale and Retail Trade and Repair of Motor Vehicles and Motorcycles	208,944	228,667	258,942	292,839	312,069
Wholesale and Retail Trades, except of Motor Vehicles and Motorcycles	857,148	909,818	1,002,203	1,127,215	1,221,998
Transport and Storage	**276,122**	**313,156**	**375,306**	**466,969**	**578,964**
Railways Transport	2,408	2,783	3,143	4,228	6,262
Land Transport	148,062	159,226	190,201	225,882	283,222
Sea Transport	24,083	26,615	30,062	36,075	39,307
River, Lake and Ferry Transport	9,202	9,780	11,165	13,137	14,267
Air Transport	47,029	62,201	77,722	108,792	142,536
Warehousing and Support Services for Transportation, Postal and Courier	45,338	52,552	63,014	78,855	93,370
Accommodation and Food Service Activities	**224,215**	**252,612**	**289,498**	**321,062**	**341,790**
Accommodation	41,102	51,052	63,489	74,255	81,238
Food and Beverages Service Activities	183,113	201,560	226,009	246,807	260,553
Information and Communication	**281,778**	**311,362**	**341,009**	**369,415**	**406,888**
Financial and Insurance Services	**270,586**	**320,534**	**370,132**	**408,439**	**464,735**
Financial Intermediary Services	167,456	204,479	237,170	256,029	291,510
Insurance and Pension Fund	58,759	65,882	76,005	87,337	99,041
Other Financial Services	37,761	42,688	48,279	55,245	63,180
Financial Supporting Services	6,610	7,485	8,679	9,829	11,003
Real Estate Activities	**218,797**	**237,914**	**264,275**	**294,573**	**329,797**
Business Services	**113,975**	**127,724**	**144,604**	**165,991**	**190,268**
Public Administration and Defence; Compulsory Social Security	**304,756**	**340,568**	**372,195**	**404,630**	**450,733**
Education	**232,727**	**270,372**	**307,862**	**342,063**	**388,683**
Human Health and Social Work Activities	**76,405**	**86,235**	**96,881**	**109,147**	**123,410**
Other Services Activities	**113,022**	**122,566**	**140,316**	**163,549**	**190,580**
GROSS DOMESTIC PRODUCT	**7,831,726**	**8,615,705**	**9,546,134**	**10,565,817**	**11,540,790**

[1)] Since year 2010, GDP figures using 2010=100 as a base year
*) Provisional figures
**) Very Provisional figures

Source: BPS-Statistics Indonesia

Table 4. **Monthly Minimum Wages/Earnings by Province**

Rp

Province	2009	2010	2011	2012	2013	2014
Nanggroe Aceh Darussalam	1,200,000	1,300,000	1,350,000	1,400,000	1,550,000	1,750,000
North Sumatra	905,000	965,000	1,035,500	1,200,000	1,305,000	1,505,850
West Sumatra	880,000	940,000	1,055,000	1,150,000	1,350,000	1,490,000
Riau	901,650	1,016,000	1,120,000	1,238,000	1,400,000	1,700,000
Riau Islands	892,000	925,000	975,000	1,015,000	1,365,087	1,665,000
Jambi	800,000	900,000	1,028,000	1,142,000	1,300,000	1,502,300
South Sumatra	824,730	927,825	1,048,440	1,195,220	1,630,000	1,825,000
Bangka Belitung	850,000	910,000	1,024,000	1,110,000	1,265,000	1,640,000
Bengkulu	727,950	780,000	815,000	930,000	1,200,000	1,350,000
Lampung	691,000	767,500	855,000	975,000	1,150,000	n.a.
Banten	917,500	955,300	1,000,000	1,042,000	1,170,000	1,325,000
DKI Jakarta	1,069,865	1,118,009	1,290,000	1,529,150	2,200,000	2,441,301
West Java	628,191	671,500	732,000	780,000	850,000 1)	n.a.
Central Java	575,000	660,000	675,000	720,000	830,000 2)	n.a.
D.I. Yogyakarta	700,000	745,694	808,000	892,660	947,114 3)	n.a.
East Java	570,000	630,000	705,000	745,000 3)	866,250 4)	n.a.
Bali	760,000	829,316	890,000	967,500	1,181,000	n.a.
West Nusa Tenggara	832,500	890,775	950,000	1,000,000	1,100,000	1,210,000
East Nusa Tenggara	725,000	800,000	850,000	925,000	1,010,000	n.a.
West Kalimantan	705,000	741,000	802,500	900,000	1,060,000	1,380,000
Central Kalimantan	873,089	986,500	1,134,580	1,327,459	1,553,127	1,723,970
South Kalimantan	930,000	1,024,500	1,126,000	1,225,000	1,337,500	1,620,000
East Kalimantan	955,000	1,002,000	1,084,000	1,177,000	1,752,073	1,886,315
North Sulawesi	929,500	1,000,000	1,080,000	1,250,000	1,550,000	1,900,000
Central Sulawesi	720,000	777,500	827,500	885,000	995,000	1,250,000
South Sulawesi	905,000	1,000,000	1,100,000	1,200,000	1,440,000	1,800,000
South East Sulawesi	770,000	860,000	930,000	1,032,300	1,125,207	1,400,000
West Sulawesi	909,400	944,200	1,006,000	1,127,000	1,165,000	n.a.
Maluku	775,000	840,000	900,000	975,000	1,275,000	1,415,000
North Maluku	770,000	n.a	889,350	960,498	1,200,622	n.a.
Gorontalo	675,000	710,000	762,500	837,500	1,175,000	1,325,000
Papua	1,216,100	1,316,500	1,403,000	1,515,000 4)	1,710,000	1,900,000
West Papua	1,180,000	1,210,000	1,410,000	1,450,000	1,720,000	1,870,000

Keterangan:
- By the decree of Manpower Minister of the Republic of Indonesia No.PER-01/MEN/1999 tahun 1999, at the beginning of each year, the regional minimum wages or Provincial minimum wages stipulated by the Governor of the said province, base on information from each Regional Wage Board of the province
- "n.a" data, consists of: new Province and the abstinence of minimum wages on North Maluku

1) By the decree of its Governor No. 561/Kep.1405-Bangsos/2012, West Java Province' minimum wages refers to Majalengka regency' minimum wages amounted to Rp850,000
2) By the decree of its Governor No.561.4/58/2012, Central Java Province' minimum wages refers to Wonogiri regency' minimum wages amounted to Rp830,000
3) By the decree of its Governor No. 370/KEP/2012, Special Region of Yogyakarta' minimum wages refers to Gunungkidul regency' minimum wages amounted to Rp974,114
4) By the decree of its Governor No. 72 year 2012 regarding Minimum Wages on East Java and its surrounding region on 2012, refers to Magetan regency' minimum wages amounted to Rp866,250

Source: Ministry of Manpower of the Republic of Indonesia, *Direktorat Pengupahan & Jamsostek - Ditjen PHI* (Directorate of Wage & Social Security - Directorate General of Industrial Relations and Social Security Workers)

Table 5. Indonesia's Consumer Price Index

Period [1]	Food Stuff	Prepared Food, Beverage, Cigarette and Tobacco	Housing, Water, Electricity, Gas and Fuel	Clothing	Medical Care	Education, Recreation and Sports	Transportation, Communication and Financial Services	CPI	CPI Inflation
2001	**290.74**	**278.75**	**208.57**	**277.90**	**262.99**	**224.12**	**221.47**	**249.15**	**12.55**
2002	**317.29**	**304.35**	**235.08**	**285.38**	**277.79**	**248.43**	**255.85**	**274.13**	**10.03**
2003	**311.84**	**323.35**	**256.74**	**305.60**	**293.54**	**277.52**	**266.34**	**287.99**	**5.06**
2004 [2]	**111.10**	**115.70**	**124.19**	**113.36**	**113.06**	**126.20**	**114.25**	**116.86**	**6.40**
2005	**126.55**	**131.56**	**141.50**	**121.21**	**119.99**	**136.60**	**165.38**	**136.86**	**17.11**
2006	**142.92**	**139.93**	**148.34**	**129.50**	**127.03**	**147.70**	**167.06**	**145.89**	**6.60**
2007	**159.01**	**148.90**	**155.58**	**140.41**	**132.51**	**160.74**	**169.15**	**155.50**	**6.59**
2008 [3]	**122.70**	**114.98**	**113.02**	**112.27**	**109.13**	**109.84**	**107.26**	**113.86**	**11.06**
2009	**127.46**	**123.96**	**115.09**	**119.01**	**113.38**	**114.11**	**103.32**	**117.03**	**0.33**
2010	**147.39**	**132.59**	**119.79**	**126.76**	**115.86**	**117.86**	**106.10**	**125.17**	**0.92**
2011									**3.79**
January	150.64	133.24	120.37	126.95	116.41	118.36	106.43	126.29	0.89
February	150.14	133.86	120.85	126.85	117.21	118.51	106.59	126.46	0.13
March	147.22	134.29	121.20	127.33	117.65	118.71	106.68	126.05	-0.32
April	144.42	134.56	121.46	128.28	118.10	118.80	106.75	125.66	-0.31
May	144.01	134.86	121.76	129.10	118.69	118.83	106.90	125.81	0.12
June	145.84	135.41	122.13	129.84	119.18	119.04	107.06	126.50	0.55
July	148.52	135.98	122.36	130.65	119.50	120.20	107.24	127.35	0.67
August	150.11	136.60	122.76	134.66	119.81	122.77	108.10	128.54	0.93
September	149.97	137.25	123.08	135.96	120.07	123.43	108.29	128.89	0.27
October	149.45	137.61	123.33	134.25	120.38	123.80	107.85	128.74	-0.12
November	150.33	137.88	123.60	136.08	120.58	123.85	107.99	129.18	0.34
December	152.76	138.57	123.95	136.35	120.79	123.94	108.14	129.91	0.57
2012									**4.30**
January	155.59	139.47	124.62	136.24	121.40	124.12	108.39	130.90	0.76
February	154.45	139.95	124.96	137.90	121.58	124.22	108.46	130.96	0.05
March	153.94	140.59	125.21	138.11	121.77	124.31	108.57	131.05	0.07
April	154.13	141.46	125.51	137.48	122.05	124.39	108.80	131.32	0.21
May	153.90	142.03	125.74	137.18	122.27	124.41	108.88	131.41	0.07
June	156.32	142.71	126.19	137.71	122.53	124.55	108.91	132.23	0.62
July	158.94	143.98	126.39	137.96	123.04	125.25	109.25	133.16	0.70
August	161.29	144.94	126.72	139.14	123.34	127.38	110.89	134.43	0.95
September	159.80	145.76	127.16	141.19	123.51	128.74	110.00	134.45	0.01
October	159.12	146.32	127.69	142.52	123.82	129.01	109.98	134.67	0.16
November	158.91	146.61	127.88	142.38	124.08	129.09	110.23	134.76	0.07
December	161.44	147.04	128.10	142.72	124.30	129.16	110.52	135.49	0.54
2013									**8.38**
January	166.91	147.71	128.82	143.07	124.66	129.22	110.21	136.88	1.03
February	170.39	148.41	129.87	142.23	125.36	129.47	110.30	137.91	0.75
March	173.87	149.00	130.14	141.23	125.66	129.62	110.51	138.78	0.63
April	172.48	149.45	130.68	139.63	125.94	129.82	110.62	138.64	-0.10
May	171.04	149.98	131.66	137.92	126.23	129.90	110.67	138.60	-0.03
June	173.04	150.98	131.93	137.52	126.52	129.95	114.88	140.03	1.03
July	182.48	153.32	132.51	137.39	127.02	130.85	125.91	144.63	3.29
August	185.67	154.37	133.39	139.88	127.49	132.63	127.10	146.25	1.12
September	180.32	155.57	134.20	144.06	127.83	133.57	126.09	145.74	-0.35
October	179.20	156.42	134.55	143.26	128.25	133.98	126.76	145.87	0.09
November	178.36	156.85	135.47	143.22	128.69	134.13	126.79	146.04	0.12
December	179.77	157.99	136.07	143.46	128.90	134.21	127.50	146.84	0.55

Table 5. **Indonesia's Consumer Price Index - Continued**

Period [1]	Food Stuff	Prepared Food, Beverage, Cigarette and Tobacco	Housing, Water, Electricity, Gas and Fuel	Clothing	Medical Care	Education, Recreation and Sports	Transportation, Communication and Financial Services	CPI	CPI Inflation
2014 [4]									**8.36**
January	117.81	110.71	108.72	103.88	105.76	105.98	113.72	110.99	1.07
February	118.23	111.19	108.90	104.47	106.06	106.16	113.89	111.28	0.26
March	117.71	111.67	109.07	104.55	106.50	106.31	114.16	111.37	0.08
April	116.43	112.17	109.34	104.29	107.15	106.56	114.39	111.35	-0.02
May	116.26	112.56	109.59	104.42	107.59	106.63	114.63	111.53	0.16
June	117.41	112.92	110.01	104.73	107.98	106.72	114.85	112.01	0.43
July	119.69	114.05	110.50	105.62	108.40	107.20	115.86	113.05	0.93
August	120.12	114.64	111.31	105.86	108.76	108.89	115.72	113.58	0.47
September	119.92	115.23	112.17	105.68	109.07	109.63	115.44	113.89	0.27
October	120.22	115.73	113.34	105.90	109.72	109.88	115.62	114.42	0.47
November	122.80	116.55	113.90	105.81	110.19	109.97	120.58	116.14	1.50
December	126.76	118.84	115.55	106.49	111.00	110.37	127.27	119.00	2.46
2015									**3.35**
January	127.52	119.61	116.48	107.39	111.73	110.66	122.10	118.71	-0.24
February	125.65	120.15	116.96	107.95	112.17	110.81	120.26	118.28	-0.36
March	124.73	120.88	117.30	107.86	112.89	110.92	121.19	118.48	0.17
April	123.75	121.48	117.56	108.12	113.32	110.98	123.40	118.91	0.36
May	125.47	122.09	117.80	108.37	113.70	111.05	123.60	119.50	0.50
June	127.48	122.76	118.07	108.67	114.06	111.13	123.80	120.14	0.54
July	130.06	123.39	118.22	109.09	114.47	111.51	125.90	121.26	0.93
August	131.24	124.26	118.41	109.10	115.27	113.43	125.20	121.73	0.39
September	129.83	124.75	118.65	110.01	115.78	114.44	124.67	121.67	-0.05
October	128.46	125.25	118.76	110.29	116.11	114.62	124.70	121.57	-0.08
November	128.89	125.84	118.94	110.04	116.62	114.68	124.80	121.82	0.21
December	133.01	126.47	119.41	110.14	116.90	114.75	125.30	122.99	0.96

[1] Annual/Quarterly data is figures at the end of the reference period
[2] CPI has been calculated from 45 cities using 2002 = 100 as a base year, and classified into 7 groups
[3] CPI has been calculated from 66 cities using 2007 = 100 as a base year, and classified into 7 groups, as of June 2008
[4] CPI has been calculated from 82 cities using 2012=100 as a base year, and classified into 7 groups, as of January 2014

Source: BPS-Statistics Indonesia

Table 6. Consumer Price Index from 82 cities

Percent, yoy

City	2011	2012	2013	2014 [1]	2015 [1]
Meulaboh	n.a.	n.a.	n.a.	8.20	0.58
Banda Aceh	3.32	0.06	6.39	7.83	1.27
Lhokseumawe	3.55	0.39	8.27	8.53	2.44
Sibolga	3.71	3.30	10.08	8.36	3.34
Pematang Siantar	4.25	4.73	12.02	7.94	3.36
Medan	3.54	3.79	10.09	8.24	3.32
Padang Sidempuan	4.66	3.54	7.82	7.38	1.66
Padang	5.37	4.16	10.87	11.90	0.85
Bukit Tinggi	n.a.	n.a.	n.a.	9.24	2.79
Tembilahan	n.a.	n.a.	n.a.	10.06	2.06
Pekanbaru	5.09	3.35	8.83	8.53	2.71
Dumai	3.09	3.21	8.60	8.53	2.63
Bungo	n.a.	n.a.	n.a.	8.99	1.29
Jambi	2.76	4.22	8.74	8.72	1.37
Palembang	3.78	2.72	7.04	8.38	3.05
Lubuk Linggau	n.a.	n.a.	n.a.	9.34	3.47
Bengkulu	3.96	4.61	9.94	10.85	3.25
Bandar Lampung	4.24	4.30	7.56	8.36	4.65
Metro	n.a.	n.a.	n.a.	6.50	2.67
Tanjung Pandan	n.a.	n.a.	n.a.	13.15	0.88
Pangkal Pinang	5.00	6.57	8.71	6.81	4.66
Batam	3.76	2.02	7.81	7.61	4.73
Tanjung Pinang	3.32	3.92	10.09	7.49	2.46
Jakarta	3.97	4.52	8.00	8.95	3.30
Bogor	2.85	4.06	8.55	6.83	2.70
Sukabumi	4.26	3.98	8.03	8.38	2.20
Bandung	2.75	4.02	7.97	7.75	3.93
Cirebon	3.20	3.36	7.86	7.08	1.56
Bekasi	3.45	3.46	9.46	7.68	2.22
Depok	2.94	4.11	10.97	7.49	1.87
Tasikmalaya	4.17	3.87	6.89	8.09	3.53
Cilacap	n.a.	n.a.	n.a.	8.18	2.63
Purwokerto	3.40	4.73	8.50	7.09	2.52
Kudus	n.a.	n.a.	n.a.	8.59	3.28
Surakarta	1.93	2.87	8.32	8.01	2.56
Semarang	2.87	4.85	8.19	8.52	2.56
Tegal	2.58	3.10	5.80	7.40	3.95
Yogyakarta	3.88	4.31	7.32	6.59	3.09
Jember	2.43	4.49	7.21	7.53	2.31
Banyuwangi	n.a.	n.a.	n.a.	6.59	2.15
Sumenep	4.18	5.05	6.62	8.04	2.62
Kediri	3.62	4.63	8.05	7.49	1.71
Malang	4.05	4.60	7.92	8.14	3.32
Probolinggo	3.78	5.88	7.98	6.79	2.11
Madiun	3.49	3.51	7.52	7.39	2.75
Surabaya	4.72	4.39	7.52	7.90	3.43
Serang	2.78	4.41	9.16	10.07	3.20
Tangerang	3.78	4.44	10.02	9.81	7.64
Cilegon	2.35	3.91	7.98	11.37	2.13
Singaraja	n.a.	n.a.	n.a.	10.32	2.97
Denpasar	3.75	4.71	7.35	8.03	2.70
Mataram	6.38	4.10	9.27	7.18	3.25
Bima	7.19	3.61	10.42	7.37	4.11
Maumere	6.59	6.49	6.24	4.00	3.89
Kupang	4.32	5.10	8.84	8.32	5.07
Pontianak	4.91	6.62	9.48	9.38	6.17
Singkawang	6.72	4.21	6.15	9.65	4.00
Sampit	3.60	4.69	7.25	7.90	5.72
Palangkaraya	5.28	6.73	6.45	6.63	4.20
Tanjung	n.a.	n.a.	n.a.	8.80	6.69
Banjarmasin	3.98	5.96	6.98	7.16	5.03
Balikpapan	6.45	6.41	8.56	7.43	6.26
Samarinda	6.23	4.81	10.37	6.74	4.24
Tarakan	6.43	5.99	10.35	11.91	3.42
Manado	0.67	6.04	8.12	9.67	5.56
Palu	4.47	5.87	7.57	8.85	4.17
Bulukumba	n.a.	n.a.	n.a.	9.45	2.17
Watampone	3.94	3.65	6.86	8.22	0.97
Makassar	2.87	4.57	6.24	8.51	5.18
Pare-pare	1.60	3.49	6.31	9.38	1.58
Palopo	3.35	4.11	5.25	8.95	3.38
Kendari	5.09	5.25	5.92	7.40	1.64
Bau-bau	n.a.	n.a.	n.a.	11.37	3.95
Gorontalo	4.08	5.31	5.84	6.14	4.30
Mamuju	4.91	3.28	5.91	7.88	5.07
Ambon	2.85	6.73	8.81	6.81	5.92
Tual	n.a.	n.a.	n.a.	11.48	8.58
Ternate	4.52	3.29	9.78	9.34	4.52
Manokwari	3.64	4.88	4.63	5.70	2.77
Sorong	0.90	5.12	7.93	6.84	6.17
Merauke	n.a.	n.a.	n.a.	12.31	5.76
Jayapura	3.40	4.52	8.27	7.98	2.79
National CPI	**3.79**	**4.30**	**8.38**	**8.36**	**3.35**

Notes
[1] Calculated using 2012=100 as a base year, taken from 82 cities

Source: BPS-Statistics Indonesia

Table 7. Indonesia's Wholesale Price Indices

Items	2010 1)	2011 2)	2012	2013	2014	2015	Annual Percentage Changes -2015 to 2014 (%)
Agriculture	231.43	248.78	263.25	264.48	175.05	240.68	37.49
Mining and Quarrying	212.31	221.50	231.20	217.33	117.22	119.87	2.26
Manufacturing	172.01	180.32	187.48	181.29	122.89	128.89	4.88
Import	160.90	177.37	189.17	188.20	137.37	134.19	-2.32
Export	137.80	154.11	163.15	164.64	138.73	130.47	-5.96
Oil and Gas	142.05	173.11	194.28	168.58	168.10	110.65	-34.18
Non-Oil and Gas	124.52	148.00	153.16	153.03	129.07	136.98	6.13
General Index	**170.59**	**183.31**	**192.69**	**189.60**	**132.44**	**138.26**	**4.39**

1) As of January 2009, WPI calculated using 2005=100 as a base year
2) As of year 2011, WPI calculated using 2010=100 as a base year
Since November-December 2013, Statistics Indonesia no longer disseminated WPI figures for Oil and Gas Exports

Source: BPS-Statistics Indonesia

Table 8. **Indonesia's Balance of Payments**

USD million

Items	2011	2012	2013	2014	2015				
					I*	II*	III*	IV**	2015
I. Current Account	**1,685.08**	**-24,418.12**	**-29,114.92**	**-27,499.21**	**-4,159.16**	**-4,296.34**	**-4,190.40**	**-5,114.71**	**-17,760.61**
A. Goods	33,825.00	8,679.52	5,833.23	6,982.57	3,062.50	4,124.78	4,140.85	1,952.89	13,281.02
- Exports, fob	191,108.71	187,346.48	182,089.23	175,292.79	37,826.76	39,685.42	36,085.57	34,742.87	148,340.62
- Imports, fob	-157,283.71	-178,666.96	-176,255.99	-168,310.22	-34,764.25	-35,560.64	-31,944.72	-32,789.99	-135,059.60
1. General Merchandise	32,215.37	6,710.91	4,068.67	5,474.03	2,690.38	3,809.66	4,047.23	2,004.23	12,551.49
- Exports	189,432.27	185,337.19	180,293.99	173,759.96	37,450.31	39,366.32	35,727.63	34,396.53	146,940.79
- Imports	-157,216.90	-178,626.28	-176,225.32	-168,285.94	-34,759.94	-35,556.66	-31,680.40	-32,392.30	-134,389.29
a. Non-Oil and Gas	32,865.50	11,949.85	13,777.23	17,303.64	3,946.84	5,932.07	6,157.85	2,987.13	19,023.88
- Exports	151,365.60	149,765.76	146,705.57	145,007.89	33,068.44	34,721.90	32,037.54	30,698.16	130,526.04
- Imports	-118,500.10	-137,815.90	-132,928.34	-127,704.25	-29,121.60	-28,789.83	-25,879.69	-27,711.04	-111,502.16
b. Oil and Gas	-650.13	-5,238.94	-9,708.56	-11,829.61	-1,256.46	-2,122.41	-2,110.62	-982.90	-6,472.39
- Exports	38,066.67	35,571.43	33,588.42	28,752.07	4,381.87	4,644.42	3,690.09	3,698.36	16,414.74
- Imports	-38,716.80	-40,810.38	-43,296.98	-40,581.68	-5,638.33	-6,766.83	-5,800.71	-4,681.26	-22,887.14
2. Other Goods	1,609.64	1,968.61	1,764.56	1,508.54	372.13	315.12	93.62	-51.34	729.53
- Exports	1,676.44	2,009.29	1,795.23	1,532.83	376.44	319.11	357.94	346.35	1,399.84
- Imports	-66.80	-40.67	-30.67	-24.29	-4.32	-3.98	-264.32	-397.69	-670.30
B. Services	-9,803.27	-10,564.20	-12,071.65	-10,009.69	-1,844.84	-2,651.44	-2,151.16	-1,845.92	-8,493.36
- Exports	21,888.15	23,660.23	22,944.08	23,530.93	5,525.70	5,084.62	5,445.70	5,834.83	21,890.86
- Imports	-31,691.42	-34,224.43	-35,015.73	-33,540.62	-7,370.55	-7,736.06	-7,596.86	-7,680.75	-30,384.22
C. Primary Income	-26,547.17	-26,627.83	-27,054.65	-29,691.96	-6,804.54	-7,195.34	-7,452.26	-6,575.62	-28,027.76
- Receipts	2,581.12	2,649.63	2,602.36	2,129.61	467.77	722.47	705.34	930.39	2,825.97
- Payments	-29,128.28	-29,277.45	-29,657.01	-31,821.57	-7,272.32	-7,917.81	-8,157.59	-7,506.01	-30,853.73
D. Secondary Income	4,210.51	4,094.38	4,178.15	5,219.87	1,427.72	1,425.66	1,272.17	1,353.94	5,479.48
- Receipts	7,635.63	8,066.75	8,508.30	9,373.54	2,521.23	2,645.39	2,538.72	2,627.19	10,332.53
- Payments	-3,425.12	-3,972.37	-4,330.15	-4,153.67	-1,093.50	-1,219.73	-1,266.56	-1,273.25	-4,853.04
II. Capital Account	**32.89**	**50.57**	**45.29**	**26.57**	**0.93**	**0.29**	**1.67**	**13.75**	**16.63**
- Receipts	32.89	50.57	45.29	26.57	0.93	0.29	1.67	13.75	16.63
- Payments	-	-	-	-	-	-	-	-	-
III. Financial Account [2]	**13,603.33**	**24,858.06**	**21,964.42**	**44,962.07**	**5,085.92**	**2,241.05**	**277.14**	**9,515.69**	**17,119.80**
- Assets	-16,453.46	-17,971.27	-15,467.05	-10,785.81	-8,302.32	-8,524.29	-3,786.87	340.20	-20,273.27
- Liabilities	30,056.80	42,829.33	37,431.47	55,747.88	13,388.24	10,765.33	4,064.01	9,175.48	37,393.07
1. Direct Investment	11,528.39	13,716.23	12,295.44	14,788.34	1,694.73	3,466.62	1,781.81	2,315.38	9,258.54
a. Assets	-9,036.54	-7,484.55	-11,111.69	-10,387.53	-3,451.13	-3,393.66	-1,344.99	-1,237.43	-9,427.22
b. Liabilities	20,564.94	21,200.78	23,407.13	25,175.87	5,145.86	6,860.29	3,126.80	3,552.80	18,685.76
2. Portfolio Investment	3,806.37	9,206.43	10,874.79	26,067.40	8,508.53	5,592.02	-2,218.37	4,824.69	16,706.88
a. Assets	-1,189.45	-5,467.02	-1,272.76	2,586.74	24.32	-737.21	-682.99	393.35	-1,002.53
b. Liabilities	4,995.82	14,673.45	12,147.55	23,480.66	8,484.21	6,329.23	-1,535.38	4,431.34	17,709.41
- Public Sector	826.50	9,251.20	10,257.27	15,379.83	6,942.00	3,808.36	890.56	5,727.76	17,368.68
- Private Sector	4,169.31	5,422.25	1,890.28	8,100.83	1,542.21	2,520.88	-2,425.94	-1,296.42	340.73
3. Financial Derivatives	69.35	12.99	-334.36	-155.55	92.88	-2.87	230.87	-300.92	19.96
4. Other Investment	-1,800.78	1,922.42	-871.45	4,261.88	-5,210.22	-6,814.73	482.83	2,676.54	-8,865.58
a. Assets	-6,754.48	-5,352.99	-3,427.38	-3,426.43	-5,080.38	-4,622.37	-1,954.94	1,147.59	-10,510.09
b. Liabilities	4,953.69	7,275.42	2,555.93	7,688.31	-129.84	-2,192.36	2,437.77	1,528.95	1,644.52
- Public Sector	-2,258.17	2,453.31	-1,375.64	-4,208.60	-1,143.89	-1,366.46	1,664.59	376.85	-468.91
- Private Sector	7,211.87	4,822.11	3,931.58	11,896.91	1,014.05	-825.90	773.19	1,152.10	2,113.42
IV. Total (I + II + III)	**15,321.30**	**490.50**	**-7,105.20**	**17,489.43**	**927.69**	**-2,055.00**	**-3,911.59**	**4,414.72**	**-624.18**
V. Net Error and Omissions	**-3,464.68**	**-275.38**	**-219.52**	**-2,240.84**	**375.45**	**-870.18**	**-653.76**	**674.62**	**-473.87**
VI. Overall Balance (IV + V)	**11,856.61**	**215.12**	**-7,324.73**	**15,248.59**	**1,303.14**	**-2,925.18**	**-4,565.35**	**5,089.34**	**-1,098.05**

Table 8. Indonesia's Balance of Payments - Continued

Items	2011	2012	2013	2014	2015				
					I*	II*	III*	IV**	2015
VII. Reserves and Related Items ³	**-11,856.61**	**-215.12**	**7,324.73**	**-15,248.59**	**-1,303.14**	**2,925.18**	**4,565.35**	**-5,089.34**	**1,098.05**
A. Reserve Asset Transactions	-11,856.61	-215.12	7,324.73	-15,248.59	-1,303.14	2,925.18	4,565.35	-5,089.34	1,098.05
B. Credit and Loans with IMF	-	-	-	-	-	-	-	-	-
C. Exceptional Financing	-	-	-	-	-	-	-	-	-
Memorandum:									
- Reserve Assets Position	110,123.00	112,781.03	99,386.71	111,861.60	111,553.65	108,029.62	101,719.53	105,931.02	105,931.02
In Months of Imports & Official Debt Repayment	6.74	6.15	5.47	6.45	6.64	6.78	6.77	7.45	6.45
- Current Account (% GDP)	0.20	-2.78	-3.19	-3.09	-1.95	-1.97	-1.94	-2.39	-2.06
- Debt Payments Ratio (%)	-	-	-	-					
Government Debt Payments & Monetary Authority ratio (%)	-	-	-	-					

Catatan:
1) Excludes reserves and related items
2) Negative represents surplus and positive represents deficit

*) Provisional figures
**) Very provisional figures

Table 9. **Value of Non-Oil and Gas Export By Commodities [1)]**

USD thousand

Commodities	2011		2012		2013		2014		2015*	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
Agricultural Products	**5,077,862**	**3.32**	**5,584,278**	**3.68**	**5,787,688**	**3.90**	**5,927,312**	**4.04**	**5,764,008**	**4.37**
Cocoa bean	616,202	0.40	388,326	0.26	443,372	0.30	201,407	0.14	118,047	0.09
Shrimp	1,064,620	0.70	1,111,388	0.73	1,467,208	0.99	1,786,335	1.22	1,331,320	1.01
Coffee bean	1,030,338	0.67	1,241,922	0.82	1,166,406	0.79	1,030,826	0.70	1,210,617	0.92
Fish and other related	970,195	0.63	1,106,691	0.73	1,003,940	0.68	987,893	0.67	966,832	0.73
Spices	430,320	0.28	631,746	0.42	554,137	0.37	577,627	0.39	780,981	0.59
Tea	136,366	0.09	126,754	0.08	131,112	0.09	108,843	0.07	89,969	0.07
Vegetable materials	159,926	0.10	134,133	0.09	165,132	0.11	228,122	0.16	160,884	0.12
Fruits	172,746	0.11	181,322	0.12	184,506	0.12	299,853	0.20	363,396	0.28
Tobacco	61,037	0.04	60,791	0.04	93,458	0.06	82,397	0.06	58,878	0.04
Vegetables	57,605	0.04	83,943	0.06	67,687	0.05	82,958	0.06	109,083	0.08
Resin and resin gums	87,903	0.06	94,134	0.06	105,591	0.07	107,564	0.07	111,456	0.08
Natural rubber	28,493	0.02	19,481	0.01	14,178	0.01	11,675	0.01	11,017	0.01
Other agricultural products	262,111	0.17	403,647	0.27	390,962	0.26	421,812	0.29	451,528	0.34
Manufacturing Products	**111,461,020**	**72.83**	**112,171,467**	**73.91**	**109,321,211**	**73.62**	**115,437,931**	**78.78**	**104,807,597**	**79.44**
Palm oils	16,709,854	10.92	17,685,127	11.65	16,518,525	11.12	17,461,545	11.92	15,402,551	11.68
Textile and textile products	13,172,828	8.61	12,510,222	8.24	12,770,966	8.60	12,847,055	8.77	12,338,815	9.35
Electrical apparatus, measuring instruments and optical	8,592,466	5.61	11,157,423	7.35	10,716,148	7.22	10,108,187	6.90	8,778,287	6.65
Base metal products	10,774,417	7.04	9,303,974	6.13	8,614,179	5.80	9,085,294	6.20	7,610,957	5.77
Processed rubber	14,083,724	9.20	10,368,180	6.83	9,306,376	6.27	7,022,184	4.79	5,843,690	4.43
Paper and paper products	4,144,400	2.71	3,938,382	2.59	3,732,138	2.51	3,779,966	2.58	3,599,155	2.73
Processed food	4,582,987	2.99	5,089,625	3.35	5,369,071	3.62	6,325,797	4.32	6,284,730	4.76
Chemicals	4,579,567	2.99	3,634,536	2.39	3,498,625	2.36	3,851,429	2.63	2,805,673	2.13
Processed wood products	3,244,615	2.12	3,338,150	2.20	3,510,392	2.36	3,906,760	2.67	3,815,167	2.89
Footwear	3,254,189	2.13	3,518,257	2.32	3,859,520	2.60	4,109,724	2.80	4,507,506	3.42
Artificial resin, plastic materials	2,402,329	1.57	2,475,062	1.63	2,608,021	1.76	2,760,476	1.88	2,320,365	1.76
Furniture	1,722,845	1.13	1,728,879	1.14	1,693,575	1.14	1,728,798	1.18	1,684,510	1.28
Ships and other vessels	328,274	0.21	397,701	0.26	683,239	0.46	746,924	0.51	373,775	0.28
Paper materials	1,537,801	1.00	1,540,093	1.01	1,816,694	1.22	1,713,636	1.17	1,725,688	1.31
Parts of vehicles	1,213,935	0.79	1,961,842	1.29	1,814,455	1.22	2,096,510	1.43	2,240,557	1.70
Motor vehicle 4 wheels and more	1,541,550	1.01	2,491,899	1.64	2,492,773	1.68	2,919,493	1.99	2,668,989	2.02
Parts of machines	457,288	0.30	854,526	0.56	684,059	0.46	763,367	0.52	730,405	0.55
Fatty acid	1,334,065	0.87	1,878,791	1.24	1,718,603	1.16	2,367,180	1.62	1,835,927	1.39
Computer and parts	279,570	0.18	699,832	0.46	575,740	0.39	579,213	0.40	542,119	0.41
Soap and detergent	740,114	0.48	866,562	0.57	895,776	0.60	906,194	0.62	801,862	0.61
Essential oils	527,167	0.34	546,023	0.36	566,619	0.38	593,827	0.41	548,931	0.42
Glass and glassware	432,356	0.28	498,666	0.33	452,941	0.31	432,535	0.30	405,962	0.31
Fertilizer	415,196	0.27	548,257	0.36	631,035	0.42	508,675	0.35	302,134	0.23
Sports requisites	323,236	0.21	453,825	0.30	545,887	0.37	514,885	0.35	468,007	0.35
Products of ceramic	375,447	0.25	342,240	0.23	342,339	0.23	365,290	0.25	348,555	0.26
Cattle fodder	510,353	0.33	599,077	0.39	733,112	0.49	775,918	0.53	568,753	0.43
Margarine and other fats	922,707	0.60	811,401	0.53	618,983	0.42	777,803	0.53	620,029	0.47
Products of pharmacy	428,328	0.28	441,752	0.29	449,277	0.30	519,046	0.35	574,188	0.44
Articles of gold	1,053,125	0.69	170,300	0.11	183,584	0.12	2,122,861	1.45	3,292,902	2.50
Leather and leather products	223,765	0.15	211,209	0.14	230,055	0.15	218,039	0.15	193,115	0.15
Disinfectant preparation	236,899	0.15	247,671	0.16	318,040	0.21	302,762	0.21	277,200	0.21
Aircraft and parts	160,270	0.10	105,480	0.07	102,608	0.07	97,571	0.07	87,749	0.07

Table 9. **Value of Non-Oil and Gas Export By Commodities [1] - Continued**

Commodities	2011		2012		2013		2014		2015*	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
Synthetic organic dyes	133,908	0.09	140,127	0.09	164,488	0.11	182,768	0.12	188,510	0.14
Cement	57,724	0.04	20,050	0.01	49,657	0.03	37,365	0.03	62,559	0.05
Motor vehicle 2 and 3 wheels	109,138	0.07	197,914	0.13	105,918	0.07	143,786	0.10	406,731	0.31
Wickerwork	56,680	0.04	85,021	0.06	81,805	0.06	77,596	0.05	76,891	0.06
Processed rattan	42,098	0.03	1,586	0.00	877	0.00	504	0.00	1,207	0.00
Container	7,556	0.00	9,865	0.01	12,727	0.01	5,833	0.00	3,430	0.00
Glicerol and lye	22,959	0.02	47,161	0.03	75,656	0.05	76,636	0.05	34,465	0.03
Other manufacture products	10,725,291	7.01	11,254,781	7.42	10,776,727	7.26	12,604,496	8.60	10,435,549	7.91
Mining Products	**34,270,797**	**22.39**	**31,365,925**	**20.67**	**30,946,415**	**20.84**	**22,838,643**	**15.59**	**19,416,688**	**14.72**
Coal	26,924,584	17.59	26,248,270	17.29	24,359,167	16.40	20,818,030	14.21	15,955,978	12.09
Copper ore	4,706,934	3.08	2,565,990	1.69	2,999,560	2.02	1,673,548	1.14	3,277,196	2.48
Nickel ore	1,333,171	0.87	1,458,409	0.96	1,677,366	1.13	85,913	0.06	0	0.00
Bauxite	767,138	0.50	637,597	0.42	1,318,775	0.89	47,742	0.03	744	0.00
Granite	35,792	0.02	15,598	0.01	131	0.00	0	0.00	1	0.00
Other mining products	503,179	0.33	440,061	0.29	591,415	0.40	213,410	0.15	182,769	0.14
Other Sector Products [2]	555,909	0.36	644,161	0.42	650,255	0.44	803,892	0.55	537,751	0.41
Unclassified Exports [3]	**1,676,441**	**1.10**	**2,009,286**	**1.32**	**1,795,235**	**1.21**	**1,532,832**	**1.05**	**1,399,835**	**1.06**
Total, fob	**153,042,030**	**100.00**	**151,775,118**	**100.00**	**148,500,805**	**100.00**	**146,540,609**	**100.00**	**131,925,879**	**100.00**

Notes:
[1] Commodity classification based on The Harmonized System (HS) disseminated by Bank Indonesia as supporting figures for Indonesia' Balance of Payments data
[2] Consist of art goods, goods not elsewhere specified, and goods procurred in ports by carriers
[3] Consist of nonmonetary gold and merchanting goods

*) Provisional figures

Table 10. Volume of Non-Oil and Gas Export By Commodities [1)]

Ton thousand

Items	2011		2012		2013		2014		2015*	
	Volume	Share (%)	Volume	Share (%)	Volume	Share (%)	Volume	Share (%)	Volume	Share (%)
Agricultural Products	**2695.96**	**0.52**	**3,005**	**0.54**	**3,103**	**0.48**	**3,215**	**0.63**	**3,772**	**0.81**
Cocoa bean	211	0.04	172	0.03	198	0.03	77	0.02	54	0.01
Shrimp	119	0.02	133	0.02	145	0.02	160	0.03	148	0.03
Coffee bean	344	0.07	446	0.08	532	0.08	384	0.08	513	0.11
Fish and other related	550	0.11	644	0.12	649	0.10	623	0.12	420	0.09
Spices	96	0.02	111	0.02	119	0.02	156	0.03	151	0.03
Tea	68	0.01	62	0.01	65	0.01	61	0.01	51	0.01
Vegetable materials	230	0.04	169	0.03	192	0.03	203	0.04	207	0.04
Fruits	209	0.04	243	0.04	245	0.04	300	0.06	352	0.08
Tobacco	20	0.00	16	0.00	20	0.00	17	0.00	12	0.00
Vegetables	88	0.02	147	0.03	104	0.02	111	0.02	196	0.04
Resin and resin gums	38	0.01	71	0.01	73	0.01	50	0.01	69	0.01
Natural rubber	9	0.00	9	0.00	7	0.00	6	0.00	8	0.00
Other agricultural products	713	0.14	780	0.14	755	0.12	1,068	0.21	1,591	0.34
Manufacturing Products	**62,703**	**12.20**	**64,782**	**11.73**	**70,819**	**10.88**	**75,443**	**14.85**	**78,323**	**16.91**
Palm oils	15,823	3.08	18,967	3.43	21,517	3.31	22,889	4.51	26,496	5.72
Textile and textile products	1,934	0.38	1,951	0.35	2,109	0.32	2,213	0.44	2,264	0.49
Electrical apparatus, measuring instruments and optical	573	0.11	623	0.11	588	0.09	536	0.11	517	0.11
Base metal products	2,256	0.44	2,361	0.43	2,019	0.31	3,059	0.60	3,672	0.79
Processed rubber	3,080	0.60	3,030	0.55	3,324	0.51	3,248	0.64	3,258	0.70
Paper and paper products	4,216	0.82	4,227	0.77	4,263	0.66	4,343	0.86	4,552	0.98
Processed food	2,499	0.49	2,315	0.42	2,538	0.39	3,351	0.66	2,988	0.65
Chemicals	4,843	0.94	4,088	0.74	3,863	0.59	4,185	0.82	3,943	0.85
Processed wood products	3,986	0.78	4,202	0.76	4,900	0.75	5,972	1.18	5,423	1.17
Footwear	193	0.04	199	0.04	213	0.03	214	0.04	235	0.05
Artificial resin, plastic materials	1,201	0.23	1,279	0.23	1,350	0.21	1,483	0.29	1,417	0.31
Furniture	588	0.11	599	0.11	551	0.08	552	0.11	505	0.11
Ships and other vessels	128	0.02	165	0.03	107	0.02	134	0.03	159	0.03
Paper materials	2,902	0.56	3,185	0.58	3,671	0.56	3,494	0.69	3,400	0.73
Parts of vehicles	156	0.03	231	0.04	230	0.04	259	0.05	286	0.06
Motor vehicle 4 wheels and more	178	0.03	260	0.05	268	0.04	322	0.06	314	0.07
Fatty Acid	1,200	0.23	1,855	0.34	2,150	0.33	2,589	0.51	2,700	0.58
Computer and parts	15	0.00	25	0.00	22	0.00	21	0.00	20	0.00
Soap and detergent	621	0.12	745	0.13	839	0.13	863	0.17	839	0.18
Essential oils	106	0.02	100	0.02	101	0.02	100	0.02	90	0.02
Cattle fodder	3,660	0.71	4,236	0.77	4,613	0.71	4,822	0.95	5,144	1.11
Margarine and other fats	796	0.15	766	0.14	681	0.10	805	0.16	802	0.17
Products of pharmacy	19	0.00	21	0.00	26	0.00	24	0.00	21	0.00
Articles of gold	0	0.00	0	0.00	0	0.00	-	0.00	-	0.00
Leather and leather products	12	0.00	10	0.00	11	0.00	8	0.00	7	0.00
Disinfectant preparation	79	0.02	72	0.01	82	0.01	95	0.02	82	0.02
Aircraft and parts	1	0.00	0	0.00	1	0.00	2	0.00	1	0.00
Syntetic organic dyes	25	0.00	30	0.01	34	0.01	34	0.01	32	0.01
Cement	1,318	0.26	275	0.05	946	0.15	571	0.11	1,216	0.26
Motor vehicle 2 and 3 wheels	11	0.00	20	0.00	11	0.00	15	0.00	37	0.01
Wickerwork	22	0.00	23	0.00	22	0.00	22	0.00	21	0.00

Table 10. **Volume of Non-Oil and Gas Export By Commodities [1] - Continued**

Items	2011		2012		2013		2014		2015*	
	Volume	Share (%)	Volume	Share (%)	Volume	Share (%)	Volume	Share (%)	Volume	Share (%)
Processed rattan	40	0.01	1	0.00	0	0.00	-	0.00	-	0.00
Container	3	0.00	3	0.00	4	0.00	3	0.00	2	0.00
Glicerol and lye	96	0.02	164	0.03	248	0.04	318	0.06	168	0.04
Other manufacture products	7,871	1.53	6,219	1.13	6,688	1.03	6,238	1.23	5,548	1.20
Mining Products	**448,449**	**87.27**	**484,713**	**87.73**	**576,742**	**88.64**	**429,253**	**84.51**	**380,970**	**82.27**
Coal	348,056	67.74	385,421	69.76	422,637	64.95	408,345	80.40	366,002	79.04
Copper ore	1,480	0.29	1,109	0.20	1,455	0.22	715	0.14	1,712	0.37
Nickel ore	37,474	7.29	46,901	8.49	64,232	9.87	4,284	0.84	-	0.00
Bauxite	39,634	7.71	29,799	5.39	55,557	8.54	2,087	0.41	3	0.00
Granite	4,468	0.87	2,002	0.36	19	0.00	-	0.00	-	0.00
Other mining products	17,337	3.37	19,480	3.53	32,842	5.05	13,822	2.72	13,254	2.86
Other Sector Products [2]	0	0.00	0	0.00	0	0.00	-	0.00	-	0.00
Total	**513,849**	**100.00**	**552,502**	**100.00**	**650,666**	**100.00**	**507,914**	**100.00**	**463,068**	**100.00**

Notes:
[1] Commodity classification based on The Harmonized System (HS) and not include goods procured in ports by carriers, repair on goods, and adjustment for coverage of Batam industrial exports. Data disseminated by Bank Indonesia as supporting figures for Indonesia' Balance of Payments data.
[2] Consist of arts goods and other goods not elsewhere specified

* Provisional figures

Table 11. **Value of Non-Oil and Gas Export By Country of Destination (fob) 1)**

USD thousand

	2011		2012		2013		2014		2015*	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
America	**19,749,881**	**12.90**	**18,824,693**	**12.40**	**19,401,683**	**13.07**	**20,327,656**	**13.87**	**19,271,765**	**14.61**
North America	15,967,415	10.43	15,286,203	10.07	15,795,051	10.64	16,607,330	11.33	16,021,732	12.14
United States of America	15,019,944	9.81	14,497,394	9.55	15,017,442	10.11	15,851,790	10.82	15,296,049	11.59
Canada	946,635	0.62	787,624	0.52	775,984	0.52	754,366	0.51	724,445	0.55
Other North American Countries	836	0.00	1,185	0.00	1,626	0.00	1,174	0.00	1,238	0.00
Central and South America	3,782,466	2.47	3,538,490	2.33	3,606,631	2.43	3,720,326	2.54	3,250,033	2.46
Argentina	352,449	0.23	310,359	0.20	336,956	0.23	237,166	0.16	238,132	0.18
Brazil	1,665,021	1.09	1,479,334	0.97	1,517,190	1.02	1,503,465	1.03	1,164,516	0.88
Mexico	597,834	0.39	594,865	0.39	625,022	0.42	814,494	0.56	802,893	0.61
Other Central and South American Countries	1,167,162	0.76	1,153,932	0.76	1,127,463	0.76	1,165,201	0.80	1,044,491	0.79
Europe	**22,381,070**	**14.62**	**20,827,697**	**13.72**	**19,998,354**	**13.47**	**20,044,107**	**13.68**	**18,474,267**	**14.00**
European Union	19,204,575	12.55	17,780,102	11.71	16,613,817	11.19	16,846,951	11.50	14,769,293	11.20
Netherlands	4,728,965	3.09	4,473,179	2.95	4,009,880	2.70	3,909,794	2.67	3,407,574	2.58
Belgium	1,341,888	0.88	1,293,102	0.85	1,254,708	0.84	1,217,226	0.83	1,103,886	0.84
United Kingdom	1,627,847	1.06	1,679,815	1.11	1,618,871	1.09	1,659,576	1.13	1,521,994	1.15
Italy	2,995,989	1.96	2,279,791	1.50	2,121,981	1.43	2,287,691	1.56	1,871,943	1.42
Germany	3,201,299	2.09	3,064,411	2.02	2,860,998	1.93	2,819,491	1.92	2,652,171	2.01
France	1,049,478	0.69	1,116,351	0.74	1,053,698	0.71	1,018,400	0.69	971,332	0.74
Spain	2,231,984	1.46	2,059,230	1.36	1,806,692	1.22	1,938,255	1.32	1,476,585	1.12
Other European Union 2)	2,027,124	1.32	1,814,223	1.20	1,886,988	1.27	1,996,519	1.36	1,763,807	1.34
Russia	852,039	0.56	866,396	0.57	934,132	0.63	1,056,775	0.72	993,581	0.75
Turkey	1,423,668	0.93	1,361,964	0.90	1,537,295	1.04	1,447,167	0.99	1,159,227	0.88
Other European Countries	900,788	0.59	819,235	0.54	913,110	0.61	693,214	0.47	1,552,167	1.18
Asia and Middle East	**103,157,274**	**67.40**	**102,731,460**	**67.69**	**99,945,259**	**67.30**	**95,974,111**	**65.49**	**86,415,801**	**65.50**
ASEAN	26,971,924	17.62	30,797,388	20.29	29,359,595	19.77	28,840,547	19.68	27,176,857	20.60
Brunei Darussalam	65,327	0.04	116,854	0.08	88,496	0.06	98,866	0.07	85,588	0.06
Philippines	3,642,588	2.38	3,651,969	2.41	3,757,698	2.53	3,886,987	2.65	3,916,971	2.97
Cambodia	266,448	0.17	290,188	0.19	316,755	0.21	416,539	0.28	429,189	0.33
Lao PDR	10,613	0.01	23,736	0.02	5,087	0.00	6,212	0.00	7,135	0.01
Malaysia	8,779,155	5.74	8,445,424	5.56	7,161,960	4.82	6,400,296	4.37	6,183,373	4.69
Myanmar	321,484	0.21	412,643	0.27	576,497	0.39	587,256	0.40	610,521	0.46
Singapore	7,142,675	4.67	10,136,569	6.68	9,687,013	6.52	10,012,470	6.83	8,639,863	6.55
Thailand	4,547,436	2.97	5,469,613	3.60	5,209,797	3.51	4,990,703	3.41	4,590,229	3.48
Vietnam	2,196,200	1.44	2,250,393	1.48	2,556,292	1.72	2,441,218	1.67	2,713,988	2.06
Hong Kong SAR	3,078,247	2.01	2,644,935	1.74	2,646,008	1.78	2,760,064	1.88	2,040,839	1.55
India	13,158,360	8.60	12,454,827	8.21	12,948,553	8.72	12,220,101	8.34	11,590,643	8.79
Iraq	148,874	0.10	44,886	0.03	171,973	0.12	70,480	0.05	94,987	0.07
Japan	18,135,364	11.85	17,165,696	11.31	16,025,840	10.79	14,636,828	9.99	13,016,824	9.87
South Korea	7,283,875	4.76	6,657,016	4.39	5,999,024	4.04	5,725,271	3.91	5,398,399	4.09
Pakistan	910,807	0.60	1,375,854	0.91	1,412,034	0.95	2,048,083	1.40	1,988,049	1.51
People Republic of China	21,414,082	13.99	20,783,070	13.69	21,156,450	14.25	16,465,326	11.24	13,250,434	10.04
Saudi Arabia	1,372,845	0.90	1,764,557	1.16	1,728,591	1.16	2,155,287	1.47	2,064,769	1.57
Taiwan, Province of China	4,154,619	2.71	4,084,297	2.69	3,714,616	2.50	3,891,682	2.66	3,636,068	2.76
Other Asian and Middle East Countries	6,528,277	4.27	4,958,934	3.27	4,782,574	3.22	7,160,441	4.89	6,157,932	4.67
Australia and Oceania	**3,235,990**	**2.11**	**4,026,451**	**2.65**	**3,922,662**	**2.64**	**4,519,496**	**3.08**	**3,730,377**	**2.83**
Australia	2,445,147	1.60	3,296,172	2.17	2,989,647	2.01	3,697,363	2.52	2,991,168	2.27
New Zealand	388,844	0.25	356,826	0.24	444,951	0.30	460,164	0.31	396,674	0.30

Table 11. **Value of Non-Oil and Gas Export By Country of Destination (fob) [1] - Continued**

	2011		2012		2013		2014		2015*	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
Other Australia and Oceania Countries	401,999	0.26	373,454	0.25	488,064	0.33	361,970	0.25	342,536	0.26
Africa	**3,961,906**	**2.59**	**4,552,974**	**3.00**	**4,400,184**	**2.96**	**4,857,604**	**3.31**	**3,503,548**	**2.66**
South Africa	1,409,167	0.92	1,642,411	1.08	1,245,443	0.84	1,378,907	0.94	665,661	0.50
Other African Countries	2,552,739	1.67	2,910,563	1.92	3,154,740	2.12	3,478,697	2.37	2,837,887	2.15
Unclassified destinations exports [3]	**555,909**	**0.36**	**811,843**	**0.53**	**832,663**	**0.56**	**817,635**	**0.56**	**530,122**	**0.40**
Total, fob	**153,042,030**	**100.00**	**151,775,118**	**100.00**	**148,500,805**	**100.00**	**146,540,609**	**100.00**	**131,925,879**	**100.00**

Notes:
1) Data disseminated by Bank Indonesia as supporting figures for Indonesia' Balance of Payments data
2) Enlargements become 27 states since Bulgaria and Romania integrates in European Union on January 2007
3) Consist of goods procured in ports by carriers, repair on goods, and adjustment for coverage of Batam industrial exports

*) Provisional figures

Table 12. **Value of Import By Broad Economic Categories [1]**

USD thousand

Items	2011		2012		2013		2014		2015*	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
Consumption Goods	**22,611,945**	**14.38**	**25,532,632**	**14.29**	**26,879,699**	**15.25**	**25,907,577**	**15.39**	**18,460,886**	**13.67**
Food and beverages, primary, mainly for household	1,832,692	1.17	1,537,179	0.86	1,394,325	0.79	1,541,254	0.92	1,320,174	0.98
Food and beverages, processed, mainly for household	3,533,437	2.25	2,759,331	1.54	2,812,575	1.60	2,750,512	1.63	2,332,902	1.73
Passenger motor cars	872,628	0.55	1,498,307	0.84	1,171,510	0.66	784,431	0.47	583,152	0.43
Transport equipment, non-industrial	555,433	0.35	367,729	0.21	383,485	0.22	268,909	0.16	243,875	0.18
Durable consumer goods	1,192,777	0.76	1,592,871	0.89	1,624,973	0.92	1,415,739	0.84	1,073,677	0.79
Semi durable consumer goods	1,501,594	0.95	1,921,446	1.08	2,150,785	1.22	1,952,560	1.16	1,965,869	1.46
Non durable consumer goods	1,490,297	0.95	1,910,634	1.07	2,154,691	1.22	2,158,041	1.28	2,023,313	1.50
Fuels and lubricants, processed, oil products [2]	11,465,941	7.29	13,720,367	7.68	14,736,636	8.36	14,504,300	8.62	8,181,422	6.06
Goods not specified elsewhere	167,147	0.11	224,769	0.13	450,718	0.26	531,831	0.32	736,501	0.55
Raw Materials and Auxilliary Goods	**113,151,281**	**71.94**	**126,732,417**	**70.93**	**127,649,765**	**72.42**	**121,677,775**	**72.29**	**97,933,125**	**72.51**
Food and beverages, primary, mainly for industry	4,112,931	2.61	4,005,713	2.24	4,348,635	2.47	4,934,923	2.93	4,100,987	3.04
Food and beverages, processed, mainly for industry	3,261,887	2.07	3,317,376	1.86	3,294,925	1.87	3,247,084	1.93	2,725,053	2.02
Industrial supplies, primary	6,679,561	4.25	5,480,589	3.07	6,180,739	3.51	5,967,884	3.55	4,616,230	3.42
Industrial supplies, processed	49,204,480	31.28	58,236,091	32.59	56,624,346	32.13	56,247,051	33.42	49,419,113	36.59
Parts and accessories for capital goods	13,831,250	8.79	18,011,245	10.08	17,191,495	9.75	15,552,758	9.24	14,628,275	10.83
Parts and accessories for transport equipments	6,617,550	4.21	8,267,873	4.63	8,980,793	5.10	7,128,761	4.24	6,139,476	4.55
Fuels and lubricants, primary	10,923,734	6.95	11,008,146	6.16	13,322,222	7.56	12,896,531	7.66	8,011,548	5.93
o/w crude oil [2]	10,905,440	6.93	10,987,073	6.15	13,236,094	7.51	12,600,220	7.49	7,725,385	5.72
Fuels and lubricants, processed	18,519,887	11.77	18,405,384	10.30	17,706,610	10.05	15,702,783	9.33	8,292,444	6.14
o/w oil products [2]	16,590,030	10.55	15,540,944	8.70	14,408,358	8.17	12,442,784	7.39	6,057,936	4.49
o/w Liquified Petroleum Gas [3]	1,708,094	1.09	2,626,816	1.47	3,094,502	1.76	3,039,246	1.81	2,061,615	1.53
Capital Goods	**30,490,023**	**19.39**	**36,086,323**	**20.20**	**30,909,621**	**17.54**	**29,448,344**	**17.50**	**24,842,044**	**18.39**
Capital goods (except transport equipment)	22,301,038	14.18	26,642,473	14.91	25,541,302	14.49	25,570,739	15.19	22,411,496	16.59
Passenger motor cars	872,628	0.55	1,498,307	0.84	1,171,510	0.66	784,431	0.47	583,152	0.43
Other transport equipment, industrial	7,316,357	4.65	7,945,543	4.45	4,196,809	2.38	3,093,174	1.84	1,847,396	1.37
Other capital goods [4]	724,016	0.46	743,455	0.42	714,679	0.41	753,791	0.45	419,475	0.31
Unclassified imports [5]	71,097	0.05	43,071	0.02	32,398	0.02	25,620	0.02	706,232	0.52
Total, cif	**167,048,361**	**106.21**	**189,137,898**	**105.86**	**186,186,162**	**105.63**	**177,813,107**	**105.65**	**142,361,763**	**105.41**
Insurance and Freight	**9,764,655**	**6.21**	**10,470,943**	**5.86**	**9,930,168**	**5.63**	**9,502,882**	**5.65**	**7,302,073**	**5.41**
Total, fob	**157,283,706**	**100.00**	**178,666,955**	**100.00**	**176,255,994**	**100.00**	**168,310,225**	**100.00**	**135,059,690**	**100.00**

Notes:
[1] Commodity classified by Broad Economic Category (BEC). Data disseminated by Bank Indonesia as supporting figures for Indonesia's Balance of Payments data
[2] A component of oil imports
[3] A component of gas imports
[4] Consist of goods procured in ports by carriers, and repair on goods
[5] Consist of nonmonetary gold

*) Provisional figures

Table 13. Value of Non-Oil and Gas Import By Commodities (cif) [1)]

USD thousand

Commodities	2011		2012		2013		2014		2015*	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
Agricultural Products	**9,277,539**	**7.82**	**8,129,294**	**5.90**	**8,650,023**	**6.51**	**9,340,745**	**7.31**	**7,683,489**	**6.85**
Cocoa bean	62,895	0.05	62,719	0.05	77,422	0.06	342,015	0.27	169,735	0.15
Shrimp	49,459	0.04	51,709	0.04	63,173	0.05	60,399	0.05	49,054	0.04
Coffee bean	39,092	0.03	109,399	0.08	29,424	0.02	39,856	0.03	27,492	0.02
Fish and other related	172,917	0.15	129,259	0.09	139,702	0.11	139,614	0.11	142,605	0.13
Spices	396,509	0.33	153,669	0.11	30,082	0.02	71,275	0.06	35,429	0.03
Tea	24,749	0.02	28,732	0.02	24,199	0.02	19,568	0.02	19,914	0.02
Vegetable materials	1,896	0.00	1,748	0.00	1,834	0.00	1,422	0.00	4,129	0.00
Fruits	792,567	0.67	834,467	0.61	653,001	0.49	781,392	0.61	656,088	0.58
Tobacco	134,434	0.11	258,929	0.19	224,698	0.17	205,018	0.16	82,833	0.07
Vegetables	557,773	0.47	470,697	0.34	612,965	0.46	612,117	0.48	530,410	0.47
Resin and resin gums	4,131	0.00	2,174	0.00	2,163	0.00	7,671	0.01	4,723	0.00
Natural rubber	27,408	0.02	39,576	0.03	36,709	0.03	31,477	0.02	30,798	0.03
Other agricultural products	7,013,708	5.92	5,986,217	4.34	6,754,652	5.08	7,028,921	5.50	5,930,280	5.29
Manufacturing Products	**115,099,993**	**97.08**	**136,202,320**	**98.80**	**129,985,389**	**97.76**	**123,554,860**	**96.73**	**108,034,613**	**96.31**
Palm oils	24,992	0.02	509	0.00	46,251	0.03	489	0.00	4,624	0.00
Textile and textile products	6,529,501	5.51	6,788,245	4.92	7,061,634	5.31	7,178,665	5.62	6,871,579	6.13
Electrical apparatus, measuring instruments and optical	15,462,441	13.04	19,690,154	14.28	19,581,953	14.73	17,966,458	14.07	16,304,871	14.54
Base metal products	14,687,575	12.39	20,917,890	15.17	19,191,815	14.43	17,403,341	13.63	14,232,799	12.69
Processed rubber	1,260,895	1.06	1,624,157	1.18	1,423,535	1.07	1,303,276	1.02	1,094,345	0.98
Paper and paper products	1,941,297	1.64	1,931,670	1.40	1,914,713	1.44	2,026,246	1.59	1,730,914	1.54
Processed food	5,203,802	4.39	4,572,444	3.32	4,471,081	3.36	4,392,198	3.44	3,937,824	3.51
Chemicals	8,642,410	7.29	9,284,444	6.73	9,219,775	6.93	9,169,681	7.18	7,544,441	6.73
Processed wood products	366,068	0.31	378,610	0.27	367,416	0.28	349,575	0.27	316,110	0.28
Footwear	314,536	0.27	367,657	0.27	412,326	0.31	389,560	0.30	411,544	0.37
Artificial resin, plastic materials	6,270,210	5.29	7,139,882	5.18	7,827,678	5.89	7,913,122	6.20	6,974,388	6.22
Furniture	261,448	0.22	365,781	0.27	371,420	0.28	340,918	0.27	325,454	0.29
Ships and other vessels	2,134,241	1.80	2,006,036	1.46	1,411,337	1.06	1,452,848	1.14	1,110,284	0.99
Paper materials	1,180,856	1.00	1,043,749	0.76	1,259,124	0.95	1,274,317	1.00	961,080	0.86
Parts of vehicles	3,013,552	2.54	3,890,143	2.82	3,995,442	3.01	3,527,161	2.76	2,987,859	2.66
Motor vehicle 4 wheels and more	5,842,187	4.93	7,580,873	5.50	4,627,083	3.48	3,266,401	2.56	2,202,850	1.96
Gold bar		n.a.		n.a.		n.a.		0.00		n.a.
Parts of machines	1,630,158	1.37	2,615,726	1.90	2,066,901	1.55	2,167,452	1.70	1,901,927	1.70
Fatty Acid	66,289	0.06	65,820	0.05	68,853	0.05	62,857	0.05	53,913	0.05
Computer and parts	2,707,714	2.28	2,641,069	1.92	2,758,276	2.07	2,465,939	1.93	2,312,213	2.06
Soap and detergent	263,520	0.22	325,142	0.24	329,083	0.25	348,722	0.27	305,795	0.27
Essential oils	683,025	0.58	849,363	0.62	1,098,519	0.83	1,014,065	0.79	952,312	0.85
Glass and goods from glass	320,015	0.27	398,987	0.29	395,404	0.30	374,295	0.29	307,386	0.27
Fertilizer	2,587,220	2.18	2,617,943	1.90	1,744,110	1.31	1,822,385	1.43	2,014,494	1.80
Sports requisites	185,708	0.16	248,572	0.18	233,121	0.18	160,270	0.13	157,148	0.14
Products of ceramic	259,801	0.22	425,998	0.31	320,347	0.24	369,382	0.29	326,183	0.29
Cattle fodder	2,208,054	1.86	2,783,272	2.02	3,044,755	2.29	3,274,681	2.56	2,736,151	2.44
Margarine and other fats	27,930	0.02	41,562	0.03	39,595	0.03	33,930	0.03	33,816	0.03
Products of pharmacy	513,397	0.43	560,115	0.41	612,677	0.46	685,807	0.54	717,287	0.64
Articles of gold	11,364	0.01	29,145	0.02	22,971	0.02	20,092	0.02	16,350	0.01
Leather and leather products	473,948	0.40	445,709	0.32	460,467	0.35	549,072	0.43	511,157	0.46
Disinfectant preparation	277,063	0.23	289,489	0.21	407,411	0.31	392,330	0.31	380,978	0.34
Aircraft and parts	2,014,855	1.70	2,320,848	1.68	1,495,957	1.13	675,982	0.53	797,216	0.71
Synthetic organic dyes	349,173	0.29	378,996	0.27	441,577	0.33	486,373	0.38	432,458	0.39

Table 13. Value of Non-Oil and Gas Import By Commodities (cif) 1) - Continued

Commodities	2011		2012		2013		2014		2015*	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
Cement	65,850	0.06	206,954	0.15	240,513	0.18	249,431	0.20	191,235	0.17
Motor vehicle 2 and 3 wheels	139,190	0.12	165,928	0.12	207,286	0.16	145,336	0.11	127,339	0.11
Wickerwork	3,740	0.00	1,751	0.00	1,354	0.00	2,387	0.00	2,804	0.00
Processed rattan	81	0.00	5	0.00	73	0.00	44	0.00	40	0.00
Container	16,253	0.01	14,359	0.01	21,626	0.02	21,487	0.02	13,207	0.01
Glicerol and lye	2,622	0.00	959	0.00	272	0.00	206	0.00	81	0.00
Other manufacture products	27,157,012	22.90	31,192,368	22.63	30,791,657	23.16	30,278,076	23.71	26,732,157	23.83
Mining Products and Other Sector Products	**1,197,691**	**1.01**	**1,130,859**	**0.82**	**1,302,202**	**0.98**	**1,521,494**	**1.19**	**1,469,492**	**1.31**
Coal	12,860	0.01	18,699	0.01	82,752	0.06	296,310	0.23	286,080	0.26
Copper ore	103,809	0.09	102,762	0.07	148,665	0.11	42,830	0.03	107,472	0.10
Nickel ore	0	0.00	11	0.00	6	0.00	0	0.00	0	0.00
Bauxite	421	0.00	716	0.00	811	0.00	280	0.00	734	0.00
Granite	8,853	0.01	9,883	0.01	6,971	0.01	8,205	0.01	6,799	0.01
Other mining products	1,071,747	0.90	998,788	0.72	1,062,997	0.80	1,173,870	0.92	1,068,406	0.95
Other Sector Products 2)	458,608	0.39	474,557	0.34	429,382	0.32	457,091	0.36	265,359	0.24
Unclassified Import 3)	**71,097**	**0.06**	**43,071**	**0.03**	**32,398**	**0.02**	**25,620**	**0.02**	**706,232**	**0.63**
Total, cif	**126,104,929**	**106.36**	**145,980,103**	**105.89**	**140,399,394**	**105.60**	**134,899,810**	**105.61**	**118,159,185**	**105.34**
Insurance and Freight	**7,538,026**	**6.36**	**8,123,524**	**5.89**	**7,440,379**	**5.60**	**7,171,269**	**5.61**	**5,986,630**	**5.34**
Total, fob	**118,566,903**	**100.00**	**137,856,579**	**100.00**	**132,959,014**	**100.00**	**127,728,541**	**100.00**	**112,172,555**	**100.00**

Catatan:
1) Commodity classification based on The Harmonized System (HS) and not include goods procured in ports by carriers, repair on goods, and adjustment for coverage of Batam industrial exports. Data disseminated by Bank Indonesia as supporting figures for Indonesia's Balance of Payments data.
2) Consist of arts goods and other goods not elsewhere specified
3) Consists of nonmonetary gold
* Provisional figures

Table 14. Volume of Non-Oil and Gas Import By Commodity [1)]

Ton Thousand

Commodities	2010		2011		2012		2013		2014		2015*	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
Agricultural products	**11,092**	**15.77**	**13,900**	**16.43**	**12,787**	**13.98**	**14,902**	**15.54**	**15,982**	**16.23**	**16,054**	**16.23**
Cocoa bean	27	0.04	19	0.02	24	0.03	31	0.03	109	0.11	53	0.05
Shrimp	3	0.00	6	0.01	7	0.01	8	0.01	7	0.01	6	0.01
Coffee bean	18	0.03	14	0.02	51	0.06	13	0.01	18	0.02	12	0.01
Fish and other related	178	0.25	213	0.25	141	0.15	138	0.14	127	0.13	122	0.12
Spices	25	0.04	72	0.08	57	0.06	31	0.03	32	0.03	29	0.03
Tea	11	0.01	19	0.02	23	0.03	20	0.02	14	0.01	14	0.01
Vegetable materials	1	0.00	1	0.00	0	0.00	0	0.00	0	0.00	1	0.00
Fruits	650	0.92	781	0.92	781	0.85	505	0.53	548	0.56	434	0.44
Tobacco	15	0.02	36	0.04	63	0.07	56	0.06	39	0.04	22	0.02
Vegetables	643	0.91	896	1.06	791	0.86	784	0.82	853	0.87	711	0.72
Resin and resin gums	3	0.00	1	0.00	1	0.00	1	0.00	2	0.00	2	0.00
Natural rubber	14	0.02	9	0.01	18	0.02	19	0.02	21	0.02	27	0.03
Other agricultural products	9,505	13.51	11,830	13.98	10,831	11.84	13,296	13.86	14,213	14.43	14,621	14.78
Manufacture products	**52,306**	**74.37**	**63,747**	**75.35**	**71,648**	**78.31**	**72,661**	**75.76**	**69,652**	**70.73**	**67,625**	**68.38**
Palm oils	43	0.06	23	0.03	0	0.00	65	0.07	0	0.00	8	0.01
Textile and textile products	984	1.40	1,075	1.27	1,252	1.37	1,317	1.37	1,358	1.38	1,316	1.33
Electrical apparatus, measuring instruments and optical	865	1.23	2,380	2.81	1,207	1.32	1,080	1.13	1,022	1.04	1,014	1.03
Base metal products	10,215	14.52	11,551	13.65	17,652	19.29	20,758	21.64	15,476	15.72	14,700	14.86
Processed rubber	241	0.34	329	0.39	304	0.33	426	0.44	290	0.29	274	0.28
Paper and paper products	2,995	4.26	3,143	3.72	3,066	3.35	3,053	3.18	3,016	3.06	2,417	2.44
Processed food	3,743	5.32	5,993	7.08	5,443	5.95	4,894	5.10	4,952	5.03	5,324	5.38
Chemicals	7,404	10.53	7,560	8.94	8,770	9.58	8,603	8.97	8,720	8.86	8,469	8.56
Processed wood products	511	0.73	703	0.83	735	0.80	776	0.81	657	0.67	547	0.55
Footwear	42	0.06	52	0.06	58	0.06	57	0.06	50	0.05	49	0.05
Artificial resin, plastic materials	2,266	3.22	3,455	4.08	3,401	3.72	3,709	3.87	3,718	3.78	3,817	3.86
Furniture	124	0.18	142	0.17	140	0.15	142	0.15	131	0.13	140	0.14
Ships and other vessels	1,063	1.51	1,380	1.63	1,225	1.34	550	0.57	679	0.69	477	0.48
Paper materials	1,250	1.78	1,310	1.55	1,349	1.47	1,629	1.70	1,605	1.63	1,310	1.32
Parts of vehicles	375	0.53	463	0.55	537	0.59	550	0.57	533	0.54	451	0.46
Motor vehicle 4 wheels and more	453	0.64	532	0.63	663	0.72	458	0.48	337	0.34	247	0.25
Gold bar		0.00		0.00		0.00		0.00		0.00		0.00
Parts of machines	153	0.22	204	0.24	262	0.29	187	0.20	177	0.18	168	0.17

Table 14. Volume of Non-Oil and Gas Import By Commodity [1] - Continued

Commodities	2010		2011		2012		2013		2014		2015*	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
Fatty Acid	24	0.03	31	0.04	36	0.04	59	0.06	40	0.04	42	0.04
Computer and parts	64	0.09	60	0.07	51	0.06	49	0.05	45	0.05	47	0.05
Soap and detergent	96	0.14	97	0.12	124	0.14	139	0.14	145	0.15	141	0.14
Essential oils	76	0.11	83	0.10	93	0.10	113	0.12	107	0.11	101	0.10
Glass and glassware	302	0.43	363	0.43	403	0.44	413	0.43	386	0.39	333	0.34
Fertilizer	4,936	7.02	6,457	7.63	6,285	6.87	5,483	5.72	6,679	6.78	7,376	7.46
Sports requisites	55	0.08	73	0.09	69	0.08	62	0.06	42	0.04	41	0.04
Products of ceramic	357	0.51	520	0.61	872	0.95	734	0.76	966	0.98	992	1.00
Cattle fodder	4,082	5.80	4,362	5.16	4,890	5.34	5,017	5.23	5,355	5.44	5,502	5.56
Margarine and other fats	4	0.01	7	0.01	10	0.01	12	0.01	13	0.01	14	0.01
Products of pharmacy	20	0.03	20	0.02	26	0.03	31	0.03	25	0.03	29	0.03
Articles of gold	0	0.00	0	0.00	0	0.00	0	0.00	0	0.00	0	0.00
Leather and leather products	57	0.08	56	0.07	53	0.06	57	0.06	60	0.06	53	0.05
Disinfectant preparation	55	0.08	53	0.06	53	0.06	69	0.07	71	0.07	72	0.07
Aircraft and parts	8	0.01	8	0.01	37	0.04	2	0.00	2	0.00	1	0.00
Synthetic organic dyes	67	0.10	63	0.07	70	0.08	78	0.08	77	0.08	70	0.07
Cement	1,533	2.18	1,391	1.64	3,370	3.68	3,685	3.84	4,066	4.13	3,373	3.41
Motor vehicle 2 and 3 wheels	7	0.01	12	0.01	13	0.01	17	0.02	13	0.01	9	0.01
Wickerwork	0	0.00	1	0.00	1	0.00	1	0.00	1	0.00	3	0.00
Processed rattan	0	0.00	0	0.00	0	0.00	0	0.00	0	0.00	0	0.00
Container	2	0.00	2	0.00	3	0.00	5	0.01	4	0.00	4	0.00
Glicerol and lye	8	0.01	8	0.01	2	0.00	0	0.00	0	0.00	0	0.00
Other manufacture products	7,825	11.13	9,782	11.56	9,125	9.97	8,382	8.74	8,833	8.97	8,694	8.79
Mining Products and Other Sector Products	**6,930**	**9.85**	**6,950**	**8.22**	**7,061**	**7.72**	**8,342**	**8.70**	**12,839**	**13.04**	**15,223**	**15.39**
Coal	56	0.08	48	0.06	65	0.07	496	0.52	2,260	2.30	2,814	2.85
Copper ore	0	0.00	33	0.04	39	0.04	73	0.08	23	0.02	63	0.06
Nickel ore	0	0.00	0	0.00	0	0.00	0	0.00	0	0.00	0	0.00
Bauxite	1	0.00	1	0.00	1	0.00	1	0.00	0	0.00	1	0.00
Granite	24	0.03	29	0.03	42	0.05	27	0.03	26	0.03	19	0.02
Other mining products	6,848	9.74	6,839	8.08	6,914	7.56	7,744	8.07	10,529	10.69	12,326	12.46
Other Sector Products [2]	1	0.00	1	0.00	1	0.00	1	0.00	1	0.00	0	0.00
Total	**70,330**	**100.00**	**84,598**	**100.00**	**91,498**	**100.00**	**95,907**	**100.00**	**98,474**	**100.00**	**98,903**	**100.00**

Notes:
[1] Commodity classification based on The Harmonized System (HS) and not include goods procured in ports by carriers, repair on goods, and adjustment for coverage of Batam industrial exports. Data disseminated by Bank Indonesia as supporting figures for Indonesia's Balance of Payments data
[2] Consist of arts goods and other goods not elsewhere specified
* Provisional figures

Table 15. Value of Non-Oil and Gas Import By Country of Origin (CIF) 1)

USD thousand

End of Period	2010		2011		2012		2013		2014		2015*	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
America	**12,047,861**	**12.21**	**15,688,248**	**12.44**	**16,193,572**	**11.09**	**15,874,282**	**11.31**	**14,697,090**	**10.89**	**13,502,861**	**11.43**
North America	8,687,002	8.80	11,068,663	8.78	11,382,731	7.80	10,871,756	7.74	9,982,751	7.40	9,190,892	7.78
United States of America	7,450,054	7.55	9,064,606	7.19	9,556,941	6.55	8,766,560	6.24	8,073,713	5.98	7,568,469	6.41
Canada	1,236,948	1.25	1,998,298	1.58	1,809,859	1.24	2,104,103	1.50	1,907,658	1.41	1,620,667	1.37
Other North American Countries	0	-	5,759	0.00	15,931	0.01	1,094	0.00	1,380	0.00	1,756	0.00
Central and South America	3,360,859	3.41	4,619,585	3.66	4,810,841	3.30	5,002,526	3.56	4,714,339	3.49	4,311,968	3.65
Argentina	936,672	0.95	1,577,916	1.25	1,749,601	1.20	1,683,663	1.20	1,460,787	1.08	1,298,541	1.10
Brazil	1,682,622	1.71	1,789,636	1.42	1,934,842	1.33	2,205,400	1.57	2,548,100	1.89	2,425,589	2.05
Mexico	203,240	0.21	394,537	0.31	566,649	0.39	516,890	0.37	186,888	0.14	197,406	0.17
Other Central and South American Countries	538,326	0.55	857,496	0.68	559,748	0.38	596,573	0.42	518,563	0.38	390,432	0.33
Europe	**11,463,569**	**11.62**	**14,176,998**	**11.24**	**17,366,142**	**11.90**	**17,387,563**	**12.38**	**15,509,072**	**11.50**	**13,767,419**	**11.65**
European Union	8,745,835	8.86	11,045,709	8.76	13,533,662	9.27	13,374,868	9.53	12,665,808	9.39	11,278,442	9.55
Netherlands	597,250	0.61	808,102	0.64	843,705	0.58	865,846	0.62	908,390	0.67	792,296	0.67
Belgium	533,788	0.54	570,577	0.45	614,244	0.42	649,753	0.46	581,431	0.43	556,595	0.47
United Kingdom	809,153	0.82	1,030,182	0.82	1,280,271	0.88	1,063,312	0.76	898,540	0.67	816,292	0.69
Italy	839,860	0.85	1,089,934	0.86	1,506,481	1.03	1,680,403	1.20	1,720,335	1.28	1,417,318	1.20
Germany	2,654,621	2.69	3,085,809	2.45	4,039,148	2.77	4,377,945	3.12	4,095,067	3.04	3,440,767	2.91
France	1,128,030	1.14	1,544,263	1.22	1,607,593	1.10	1,525,163	1.09	1,292,626	0.96	1,315,149	1.11
Spain	305,056	0.31	390,512	0.31	521,227	0.36	573,305	0.41	553,596	0.41	472,661	0.40
Other European Union 2)	1,878,076	1.90	2,526,330	2.00	3,120,994	2.14	2,639,142	1.88	2,615,822	1.94	2,467,364	2.09
Russia	1,051,174	1.07	1,255,824	1.00	1,743,576	1.19	2,038,204	1.45	1,184,540	0.88	904,150	0.77
Turkey	286,002	0.29	334,116	0.26	409,520	0.28	257,638	0.18	259,152	0.19	248,968	0.21
Other European Countries	1,380,558	1.40	1,541,349	1.22	1,679,384	1.15	1,716,853	1.22	1,399,572	1.04	1,335,859	1.13
Asia and Middle East	**68,553,280**	**69.47**	**88,138,518**	**69.89**	**104,529,392**	**71.61**	**99,498,165**	**70.87**	**96,425,276**	**71.48**	**84,340,679**	**71.38**
ASEAN	18,551,532	18.80	25,074,815	19.88	31,711,907	21.72	30,210,287	21.52	29,605,452	21.95	25,989,378	22.00
Brunei Darussalam	5,878	0.01	8,941	0.01	14,703	0.01	6,406	0.00	26,161	0.02	26,744	0.02
Philippines	585,439	0.59	751,789	0.60	795,015	0.54	770,294	0.55	693,242	0.51	681,157	0.58
Cambodia	3,995	0.00	7,324	0.01	11,053	0.01	17,752	0.01	18,722	0.01	21,133	0.02
Lao PDR	615	0.00	1,292	0.00	3,278	0.00	7,543	0.01	51,265	0.04	1,027	0.00
Malaysia	4,035,334	4.09	5,218,598	4.14	6,339,805	4.34	5,913,357	4.21	5,752,177	4.26	4,990,782	4.22
Myanmar	31,617	0.03	69,558	0.06	63,359	0.04	72,997	0.05	122,243	0.09	159,685	0.14
Singapore	5,460,689	5.53	6,548,829	5.19	10,745,357	7.36	10,117,172	7.21	10,050,010	7.45	8,952,779	7.58
Thailand	7,325,871	7.42	10,135,104	8.04	11,221,263	7.69	10,624,689	7.57	9,685,779	7.18	8,009,840	6.78
Vietnam	1,102,095	1.12	2,333,380	1.85	2,518,074	1.72	2,680,076	1.91	3,205,853	2.38	3,146,230	2.66
Hong Kong SAR	1,759,224	1.78	2,338,465	1.85	1,897,323	1.30	1,956,494	1.39	1,892,903	1.40	1,807,478	1.53
India	2,690,908	2.73	3,856,988	3.06	3,991,576	2.73	3,756,065	2.68	3,559,370	2.64	2,666,966	2.26
Iraq	1,176	0.00	703	0.00	200	0.00	49	0.00	342	0.00	243	0.00
Japan	15,867,587	16.08	18,461,913	14.64	22,624,472	15.50	18,934,319	13.49	16,805,848	12.46	13,226,019	11.19
South Korea	5,457,507	5.53	7,243,088	5.74	8,276,805	5.67	8,787,367	6.26	7,749,581	5.74	6,277,854	5.31
Pakistan	70,303	0.07	190,042	0.15	271,276	0.19	162,555	0.12	158,655	0.12	173,453	0.15

Table 15. Value of Non-Oil and Gas Import By Country of Origin (CIF) [1] - Continued

End of Period	2010		2011		2012		2013		2014		2015*	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
People Republic of China	19,052,020	19.31	24,222,690	19.21	29,030,885	19.89	29,488,605	21.00	30,473,168	22.59	29,178,518	24.69
Saudi Arabia	742,071	0.75	948,559	0.75	1,021,447	0.70	973,749	0.69	967,809	0.72	673,083	0.57
Taiwan, Province of China	2,794,787	2.83	3,681,422	2.92	4,198,366	2.88	4,142,844	2.95	3,628,231	2.69	3,106,748	2.63
Other Asian and Middle East Countries	1,566,165	1.59	2,119,833	1.68	1,505,136	1.03	1,085,831	0.77	1,583,918	1.17	1,240,940	1.05
Australia and Oceania	**4,925,665**	**4.99**	**5,756,139**	**4.56**	**5,767,039**	**3.95**	**5,761,917**	**4.10**	**6,365,424**	**4.72**	**5,333,685**	**4.51**
Australia	4,147,752	4.20	4,985,847	3.95	5,004,988	3.43	4,879,329	3.48	5,485,538	4.07	4,675,877	3.96
New Zealand	722,892	0.73	726,069	0.58	692,249	0.47	796,396	0.57	837,699	0.62	628,441	0.53
Other Australia and Oseania Countries	55,020	0.06	44,223	0.04	69,803	0.05	86,192	0.06	42,187	0.03	29,367	0.02
Africa	**1,158,485**	**1.17**	**1,895,420**	**1.50**	**1,663,061**	**1.14**	**1,473,965**	**1.05**	**1,475,904**	**1.09**	**971,285**	**0.82**
South Africa	520,756	0.53	687,657	0.55	649,171	0.44	622,865	0.44	475,771	0.35	230,613	0.20
Other African Countries	637,729	0.65	1,207,764	0.96	1,013,890	0.69	851,101	0.61	1,000,133	0.74	740,672	0.63
Unclassified imports [3]	**537,468**	**0.54**	**449,606**	**0.36**	**460,896**	**0.32**	**403,501**	**0.29**	**427,043**	**0.32**	**243,255**	**0.21**
Total, cif	**98,686,329**	**100.00**	**126,104,929**	**100.00**	**145,980,103**	**100.00**	**140,399,394**	**100.00**	**134,899,810**	**100.00**	**118,159,185**	**100.00**

Notes:
[1] Data disseminated by Bank Indonesia as supporting figures for Indonesia's Balance of Payments data
[2] Enlargements become 27 states since Bulgaria and Romania integrates in European Union on January 2007
[3] Consist of goods procured in ports by carriers, and repair on goods
* Provisional figures

Table 16. **Value of Oil and Gas Export (fob)**

Items	2010	2011	2012	2013	2014*	2015**
Export Value (in Millions of USD)						
Oil and its product	11,635	14,821	14,648	17,889	13,806	7,823
Gas	12,840	17,663	17,860	15,700	14,946	8,592
- LNG	11,708	15,204	12,448	10,568	10,294	6,135
- LPG	8	74	9	11	4	7
- Natural Gas	900	2,164	5,402	5,121	4,648	2,444
- Other Gas	224	220	0	0	0	6
Total	24,475	32,484	32,507	33,588	28,752	16,415
Export Volume						
Oil and its product (in millions of Barrel)	156	149	132	170	143	156
Gas	1,896	1,711	1,411	1,253	1,186	1,169
- LNG (in millions of MMBTU)	1,506	1,264	931	888	834	841
- LPG (in thousands of MT)	11	81	8	10	4	10
- Natural Gas (in millions of MMBTU)	123	207	472	355	347	317
- Other Gas	256	158	0	0	0	0
Total	2,051	1,860	1,543	1,422	1,329	1,324

MMBTU: *Million British Thermal Unit*
MT: Metric Ton

* Provisional figures
** Very provisional figures

Table 17. Money Supply

In Billions of IDR

End of Period	M1[1)] Outstanding	M1 Share (%)	Quasi Money[2)] Outstanding	Quasi Money Share (%)	M2[3)] Outstanding	M2 Changes (%) Annual	M2 Changes (%) Quarterly
2009	**515,824**	**24.09**	**1,622,055**	**75.75**	**2,141,384**	**12.95**	**6.09**
2010	**605,411**	**24.52**	**1,856,720**	**75.12**	**2,471,206**	**15.32**	**8.55**
2011	**722,991**	**25.13**	**2,139,840**	**74.37**	**2,877,220**	**16.43**	**8.85**
2012	**841,652**	**25.45**	**2,455,435**	**74.24**	**3,307,508**	**14.95**	**5.73**
2013	**887,084**	**23.78**	**2,820,521**	**75.61**	**3,730,409**	**12.79**	**4.08**
January	787,860	24.10	2,470,101	75.57	3,268,789	14.41	
February	786,549	23.98	2,483,011	75.69	3,280,420	15.02	
March	810,055	24.38	2,500,342	75.25	3,322,529	14.01	0.45
April	832,213	24.76	2,515,813	74.85	3,360,928	14.72	
May	822,876	24.02	2,588,094	75.54	3,426,305	14.42	
June	858,499	25.15	2,543,285	74.51	3,413,379	11.81	2.73
July	879,986	25.10	2,608,175	74.38	3,506,574	14.69	
August	855,783	24.43	2,625,946	74.98	3,502,420	13.29	
September	867,715	24.21	2,691,972	75.11	3,584,081	14.57	5.00
October	856,171	23.94	2,697,734	75.42	3,576,869	13.03	
November	870,412	24.07	2,720,945	75.25	3,616,049	12.72	
December	887,084	23.78	2,820,521	75.61	3,730,409	12.79	4.08
2014							
January	842,678	23.07	2,787,449	76.32	3,652,349	11.73	
February	834,532	22.96	2,787,035	76.67	3,635,060	10.81	
March	853,502	23.37	2,785,176	76.25	3,652,531	9.93	-2.09
April	880,470	23.66	2,828,686	76.00	3,721,882	10.74	
May	906,727	23.98	2,860,135	75.65	3,780,955	10.35	
June	945,718	24.51	2,903,415	75.26	3,857,962	13.02	5.62
July	918,566	23.63	2,959,732	76.14	3,887,407	10.86	
August	895,827	23.05	2,982,674	76.74	3,886,520	10.97	
September	949,168	23.67	3,044,842	75.93	4,010,147	11.89	3.94
October	940,349	23.37	3,066,421	76.19	4,024,489	12.51	
November	955,535	23.44	3,099,350	76.03	4,076,670	12.74	
December	942,221	22.58	3,209,475	76.90	4,173,327	11.87	4.07
2015							
January	918,079	21.99	3,233,881	77.46	4,174,826	14.31	
February	927,848	22.00	3,278,945	77.73	4,218,123	16.04	
March	957,580	22.55	3,275,499	77.14	4,246,361	16.26	1.75
April	959,376	22.44	3,302,204	77.23	4,275,711	14.88	
May	980,915	22.87	3,293,147	76.79	4,288,369	13.42	
June	1,039,518	23.85	3,305,641	75.84	4,358,802	12.98	2.65
July	1,031,906	23.60	3,325,908	76.05	4,373,208	12.50	
August	1,026,323	23.30	3,362,148	76.34	4,404,085	13.32	
September	1,063,039	23.58	3,426,343	76.00	4,508,603	12.43	3.44
October	1,036,311	23.32	3,391,260	76.33	4,443,078	10.40	
November	1,051,191	23.61	3,386,209	76.05	4,452,325	9.21	
December	1,055,440	23.20	3,479,961	76.50	4,548,800	9.00	0.88

[1)] Consists of Currency and Demand deposits
[2)] Consists of Time deposits and Savings, both in Rupiah and foreign currency, and Demand deposits in foreign currency held by Residents
[3)] Consists of Narrow money (M1), Quasi money, and Securities other than Stock with up-to-1 year maturity

Table 18. **Changes in Money Supply and its Affecting Factors**

In Billions of IDR

Items	2010	2011	2012	2013	2014	2015			
						I	II	III	IV
Money Supply									
M2	2,471,206	2,877,220	3,307,508	3,730,409	4,173,327	4,246,361	4,358,802	4,508,603	4,548,800
M1	605,411	722,991	841,652	887,084	942,221	957,580	1,039,518	1,063,039	1,055,440
Currency	260,227	307,760	361,897	399,609	419,262	382,005	409,713	428,860	469,534
Demand Deposits	345,184	415,231	479,755	487,475	522,960	575,576	629,805	634,178	585,906
Quasi Money	1,856,720	2,139,840	2,455,435	2,820,521	3,209,475	3,275,499	3,305,641	3,426,343	3,479,961
Affecting Factors	**2,471,206**	**2,877,220**	**3,307,508**	**3,730,409**	**4,173,327**	**4,246,361**	**4,358,802**	**4,508,603**	**4,548,800**
Net Foreign Assets	865,121	912,174	965,442	1,011,361	1,105,783	1,189,181	1,190,279	1,232,071	1,176,638
Net Claims on Central Government	368,717	351,177	389,827	406,611	416,608	426,449	408,232	482,396	491,127
Claims on Other Sectors	1,910,022	2,383,823	2,917,452	3,526,612	3,961,583	3,981,351	4,157,396	4,270,057	4,318,126
Claims on Regional Government	1,594	1,410	2,790	4,727	6,635	6,271	5,889	5,999	6,516
Claims on Private Sectors	1,684,207	2,118,376	2,581,327	3,098,305	3,488,677	3,509,105	3,651,282	3,759,846	3,822,128
Net Other Assets	-121,460	-29,895	17,778	34,146	49,733	32,309	25,783	34,972	57,313

Table 19. **Interest Rate on Time Deposits in Rupiah and Foreign Currency by Group of Banks[1)]**

Percent

Maturity	December 2010		December 2011		December 2012		December 2013		December 2014		December 2015	
	Rupiah	Foreign Currency	Rupiah	Foreign Currency	Rupiah	Foreign Currency	Rupiah	Foreign Currency	Rupiah	Foreign Currency	Rupiah	Foreign Currency
State Banks												
1 month	6.48	2.08	6.04	1.32	5.22	0.95	7.15	1.11	8.12	1.81	7.14	0.73
3 months	6.73	2.07	6.62	2.11	5.54	1.11	7.60	1.38	8.73	1.61	7.25	0.73
6 months	6.55	2.05	6.54	2.05	5.58	1.98	6.84	1.37	8.83	1.99	7.56	1.21
12 months	6.93	2.78	6.94	1.47	5.91	1.66	6.88	1.69	8.80	1.75	7.87	1.43
24 months	7.66	2.62	6.40	1.25	5.87	1.23	8.19	0.94	9.34	0.65	9.09	1.85
Private National Banks												
1 month	6.94	1.91	6.62	1.81	5.96	2.06	8.53	2.48	9.04	2.34	7.89	1.23
3 months	7.06	1.85	6.91	2.03	5.81	2.14	7.53	2.51	9.11	2.53	8.36	1.36
6 months	7.06	1.81	7.28	2.41	6.18	2.40	7.61	2.64	9.54	2.59	8.84	1.68
12 months	6.83	2.24	7.05	1.93	5.82	2.47	6.79	2.39	8.58	2.52	8.36	1.64
24 months	9.19	2.28	5.83	0.41	4.23	2.63	7.43	3.28	7.33	2.67	9.09	2.52
Regional Government Banks												
1 month	8.07	1.98	7.39	2.09	5.92	2.03	7.55	2.60	8.05	2.76	7.81	1.42
3 months	8.59	2.00	8.04	6.29	6.69	2.48	8.41	2.82	9.03	2.64	8.26	1.11
6 months	9.99	1.49	8.24	1.00	6.60	1.55	7.81	1.45	9.35	1.09	8.42	1.10
12 months	12.07	1.30	8.41	1.28	7.08	1.04	7.32	1.80	9.10	1.52	9.21	0.62
24 months	7.73	-	7.63	-	6.65	1.20	7.44	1.15	7.70	1.04	7.68	0.53
Foreign and Joint Banks												
1 month	7.69	2.64	5.00	1.19	4.61	1.51	7.51	1.67	7.51	1.37	7.36	0.60
3 months	7.16	1.79	5.74	1.62	5.54	1.90	7.98	1.52	8.57	1.41	8.11	0.78
6 months	6.97	2.59	6.47	1.74	6.04	2.04	8.17	2.02	9.23	1.52	8.71	0.96
12 months	6.81	2.19	6.64	1.51	6.19	1.86	6.90	2.42	9.50	2.40	8.86	1.37
24 months	4.04	2.50	6.64	1.17	6.20	0.92	9.18	1.46	10.01	1.40	9.62	1.74
Commercial Banks												
1 month	6.83	2.05	6.35	1.53	5.58	1.48	7.92	1.80	8.58	2.00	7.60	1.00
3 months	7.06	1.93	6.81	1.90	5.76	1.86	7.61	2.07	8.94	2.18	7.99	1.13
6 months	7.20	2.03	7.19	2.11	6.05	2.20	7.49	2.10	9.30	2.23	8.54	1.38
12 months	7.88	2.56	7.06	1.69	6.09	2.09	6.89	2.14	8.79	2.25	8.47	1.54
24 months	8.11	2.43	6.33	0.80	5.47	1.63	8.17	2.01	9.26	1.96	9.07	2.22

[1)] Weighted average at the end of the reference period

Table 20. Issuance, Repayment, and Outstanding of Bank Indonesia Certificates (SBI)

In Billions of IDR

End of Period	Issuance	Repayment	Outstanding
January - December 2004	1,194,384	1,197,054	102,732
January - December 2005	1,119,549	1,100,922	70,047
January - December 2006	2,145,485	2,010,322	207,800
January - December 2007	3,204,778	3,163,851	248,727
January - December 2008	2,113,381	2,181,379	2,348,711
2009			
January	156,141	161,903	206,450
February	134,384	125,951	235,224
March	107,870	109,849	233,754
April	141,864	141,112	230,285
May	85,000	94,850	232,073
June	97,942	88,814	231,392
July	150,318	147,013	235,519
August	113,259	125,519	234,585
September	187,680	177,035	217,287
October	198,801	180,199	240,631
November	184,877	173,205	243,719
December	247,555	238,642	253,756
2010			
January	232,791	192,349	295,965
February	221,447	213,564	303,847
March	183,931	189,868	297,910
April	150,270	104,374	343,806
May	78,287	123,120	298,973
June	91,466	120,781	269,658
July	61,048	95,981	234,724
August	73,625	38,100	270,249
September	64,161	82,625	251,785
October	36,449	63,227	225,006
November	59,999	71,445	213,561
December	55,000	68,448	200,113
2011			
January	25,000	29,799	195,314
February	14,000	14,680	194,635
March	45,525	10,012	230,148
April	23,422	23,499	230,071
May	12,281	44,481	197,871
June	15,000	26,925	185,946
July	4,000	7,950	181,996
August	7,000	17,768	171,228
September	8,000	30,000	149,228
October	13,841	20,000	143,069
November	8,941	14,000	138,010
December	27,292	45,525	119,777
2012			
January	10,000	23,422	106,355
February	5,000	12,281	99,074
March	10,423	15,000	94,497
April	5,000	4,000	95,497
May	7,167	7,000	95,664
June	2,070	8,000	89,734
July	6,285	13,841	82,178
August	8,240	8,941	81,477
September	14,003	27,292	68,188
October	11,372	10,000	69,560
November	11,245	5,000	75,805
December	13,491	10,423	78,873
2013			
January	10,399	5,000	84,272
February	10,965	7,167	88,070
March	6,000	2,070	91,999
April	9,665	6,285	95,379
May	7,590	8,240	94,729
June	1,194	14,003	81,920
July	3,553	11,372	74,101
August	3,223	11,245	66,079
September	12,386	13,491	64,974
October	34,685	10,399	89,260
November	11,000	10,965	89,295
December	8,097	6,000	91,392
2014			
January	9,720	9,665	91,447
February	8,000	7,590	91,857
March	12,846	1,194	103,510
April	10,609	3,553	110,566
May	7,000	3,223	114,342
June	8,000	12,386	109,957
July	10,000	34,685	85,272
August	8,000	11,000	82,272
September	5,000	8,097	79,175
October	12,275	9,720	81,730
November	8,875	8,000	82,605
December	19,140	12,846	88,899
2015			
January			88,290
February			87,290
March			87,290
April			77,290
May			69,290
June			64,290
July			52,015
August			55,155
September			42,631
October			39,016
November			37,510
December			32,300

Notes:
SBI was introduced in February 1984, and since July 1998 the selling of SBI was executed by Step Out Rate (SOR) auction system

Table 21. Interest Rates of Credit on Rupiah (IDR) by Group of Banks [1]

Percent

End of Period	State Banks		Regional Government Banks		Private National Banks		Foreign and Joint Banks		Commercial Banks	
	Working Capital	Investment	Working Capital	Investment	Working Capital	Investment	Working Capital	Investment	Working Capital	Investment
2010	13.06	10.81	13.57	12.44	13.02	13.20	10.23	11.82	12.83	12.28
2011	12.37	10.39	13.52	12.40	12.34	12.64	8.71	14.89	12.16	12.04
2012										
March	12.19	10.12	13.62	12.40	12.27	12.42	8.25	9.44	12.01	11.62
June	12.00	9.98	13.63	12.33	12.02	12.23	7.98	9.54	11.79	11.46
September	11.91	9.94	13.76	12.29	11.95	12.10	7.96	9.58	11.70	11.36
December	11.70	10.08	13.66	12.25	11.68	11.88	7.90	9.47	11.49	11.27
2013										
January	11.75	10.13	13.60	12.18	11.68	11.88	8.00	9.55	11.49	11.29
February	11.67	10.09	13.71	12.20	11.64	11.87	8.03	9.55	11.45	11.27
March	11.72	10.07	13.44	12.20	11.58	11.82	8.04	9.44	11.44	11.24
April	11.75	10.07	13.66	12.25	11.53	11.77	8.05	9.45	11.44	11.21
May	11.78	10.04	13.63	12.27	11.55	11.72	8.03	9.43	11.46	11.17
June	11.79	10.35	13.60	12.24	11.46	11.67	8.11	9.49	11.41	11.14
July	11.89	10.46	13.59	12.23	11.85	11.86	8.46	9.66	11.66	11.29
August	11.69	10.54	13.62	12.26	11.90	11.93	8.74	9.90	11.63	11.37
September	11.71	10.53	13.61	12.27	12.15	12.16	9.23	10.24	11.80	11.50
October	11.86	10.72	13.46	12.23	12.26	12.28	9.47	10.46	11.93	11.65
November	11.94	10.79	13.46	12.20	12.42	12.39	9.69	10.55	12.06	11.73
December	11.94	10.84	13.37	12.23	12.55	12.51	9.84	10.71	12.12	11.82
2014										
January	12.05	10.91	13.34	12.21	12.68	12.63	9.96	10.87	12.23	11.92
February	12.06	10.96	13.34	12.27	12.86	12.69	10.09	11.04	12.33	11.98
March	12.09	10.98	13.36	12.23	12.87	12.72	10.20	10.97	12.37	12.00
April	12.23	11.04	13.30	12.34	12.79	12.77	10.19	10.99	12.38	12.06
May	12.38	11.13	13.19	12.18	13.19	12.96	10.25	11.04	12.63	12.18
June	12.26	11.20	13.24	12.21	13.29	13.02	10.27	11.00	12.63	12.24
July	12.34	11.40	13.27	12.22	13.36	13.06	10.41	10.78	12.70	12.32
August	12.42	11.43	13.21	12.22	13.43	13.07	10.44	10.91	12.76	12.34
September	12.44	11.44	13.24	12.23	13.43	13.08	10.44	10.94	12.78	12.34
October	12.52	11.48	13.72	12.51	13.39	13.13	10.49	10.94	12.82	12.39
November	12.53	11.48	13.84	12.40	13.41	13.13	10.41	10.90	12.84	12.38
December	12.50	11.47	13.63	12.38	13.36	13.11	10.49	10.93	12.79	12.36
2015										
January	12.52	11.47	13.56	12.25	13.31	13.02	10.39	10.59	12.76	12.29
February	12.55	11.45	13.38	12.13	13.29	13.03	10.26	10.51	12.74	12.27
March	12.65	11.49	13.71	12.37	13.36	13.06	10.26	10.47	12.82	12.32
April	12.64	11.45	13.71	12.36	13.25	13.06	10.23	10.77	12.75	12.32
May	12.61	11.45	13.72	12.38	13.20	13.02	10.21	10.75	12.72	12.30
June	12.60	11.46	13.74	12.39	13.17	13.02	10.18	10.60	12.70	12.29
July	12.54	11.46	13.56	12.18	13.14	12.98	10.28	10.68	12.65	12.26
August	12.59	11.45	13.47	12.45	13.03	12.87	10.30	10.67	12.63	12.21
September	12.48	11.44	13.47	12.52	13.00	12.83	10.51	10.78	12.58	12.19
October	12.43	11.42	13.45	12.25	12.98	12.85	10.72	10.95	12.58	12.19
November	12.36	11.40	13.66	12.44	12.92	12.77	10.79	11.13	12.55	12.14
December	12.30	11.35	13.50	12.19	12.82	12.77	10.79	11.25	12.46	12.12

[1] Weighted average

Table 22.	**Flow of Bank Notes within Bank Indonesia Head Office and Regional Offices**

In Billions of IDR

Offices	2010		2011		2012		2013		2014		2015	
	In	Out	In	Out	In	Out	In	Out	In	Out	In	Out
Sumatra Region												
Nanggroe Aceh Darussalam	1,163.6	4,569.7	2,308.0	6,338.1	2,619.6	6,378.0	4,035.8	8,242.4	4,567.0	8,632.4	4,709.8	9,636.6
North Sumatra	16,598.4	16,370.3	23,237.8	22,176.5	25,980.6	22,494.6	26,674.6	22,284.0	30,499.9	26,389.3	30,253.6	27,877.1
West Sumatra	6,896.3	5,458.4	9,384.5	5,299.7	11,192.1	6,434.3	13,151.6	7,204.7	14,102.9	7,060.0	13,308.8	7,470.7
Riau	1,383.3	9,939.0	3,012.5	12,434.1	4,447.3	13,013.8	6,286.8	15,974.0	6,356.3	15,157.5	7,156.5	15,788.6
Riau Islands	650.4	4,789.3	1,426.3	5,818.6	2,236.0	6,965.6	2,295.2	9,257.9	2,563.0	10,231.5	3,217.7	9,802.5
Jambi	874.0	4,686.6	1,867.6	5,216.7	2,138.5	5,013.2	3,864.9	8,018.7	5,169.1	8,379.3	4,978.1	8,324.5
South Sumatra	9,985.9	14,927.9	7,820.3	14,523.6	9,126.0	15,600.1	8,056.5	14,350.6	10,039.8	13,262.9	10,797.2	13,483.7
Bengkulu	672.4	2,241.8	1,153.1	2,560.5	1,201.3	2,959.3	2,642.0	4,262.8	3,261.5	4,561.9	2,791.3	4,851.5
Lampung	5,053.3	4,855.1	7,690.1	5,724.4	6,969.2	6,375.6	7,274.3	8,251.6	9,450.1	8,341.1	8,107.5	9,945.2
Bangka Belitung									13.7	322.1	1,176.6	2,004.8
Special Capital Region - Jakarta	**52,064.5**	**69,187.7**	**62,958.0**	**101,604.4**	**76,664.9**	**136,466.6**	**84,525.8**	**149,240.8**	**92,103.0**	**152,275.9**	**100,424.8**	**163,749.4**
Java' Region (excluding Jakarta)	**83,684.9**	**49,642.1**	**123,916.7**	**83,511.4**	**160,482.3**	**111,362.6**	**200,722.0**	**137,567.4**	**217,301.9**	**147,069.0**	**230,140.4**	**171,567.5**
West Java	26,044.3	11,352.7	43,774.9	20,781.8	60,629.0	28,894.9	72,420.8	35,821.4	78,660.2	40,856.6	81,302.7	47,062.7
Central Java	25,451.4	11,256.7	35,136.8	19,975.1	43,298.1	28,492.9	57,317.7	37,673.4	60,475.4	39,110.2	65,198.1	46,840.5
Special Region - Yogyakarta	3,374.8	3,775.1	6,489.8	7,537.8	9,172.7	9,486.0	13,984.1	12,072.6	13,890.7	13,171.1	14,831.2	14,079.7
East Java	28,814.4	23,257.6	38,515.2	35,216.7	47,382.5	44,488.8	56,999.4	52,000.1	64,275.6	53,931.2	68,808.4	63,584.7
Eastern Indonesia' Region												
Bali	3,208.1	5,004.2	6,394.3	8,911.8	8,202.5	10,781.8	10,433.2	13,145.0	11,599.9	13,103.6	13,071.7	14,470.6
West Nusa Tenggara	1,160.9	2,491.0	1,802.6	3,818.7	3,675.7	4,379.1	4,516.4	5,179.4	5,694.4	5,619.5	6,285.0	6,727.9
East Nusa Tenggara	1,826.0	2,987.9	2,125.2	3,693.1	2,735.0	4,259.6	3,168.8	4,708.7	3,512.4	4,663.1	3,651.2	5,529.6
West Kalimantan	1,159.3	4,271.0	2,830.8	5,221.4	3,385.7	5,698.1	4,029.1	6,011.1	5,942.5	6,735.8	6,675.5	8,485.6
Central Kalimantan	828.5	5,343.5	778.8	6,849.9	1,134.8	7,740.6	1,896.7	8,031.5	1,887.4	8,309.8	3,546.9	10,190.2
South Kalimantan	4,324.5	3,989.2	5,369.1	5,125.7	7,311.0	5,579.8	8,471.1	6,419.1	9,613.8	6,264.8	9,558.4	6,754.6
East Kalimantan	2,127.5	9,392.0	4,293.3	12,337.5	5,743.2	14,425.7	7,542.2	17,550.8	8,935.6	17,425.6	9,646.0	16,514.4
North Sulawesi	4,763.2	5,354.5	5,671.0	6,606.3	6,634.6	6,375.0	7,436.4	4,738.8	7,374.5	7,207.1	6,286.3	7,202.2
Central Sulawesi	1,149.7	3,384.8	1,562.9	4,017.5	1,884.8	4,457.9	2,585.6	5,045.5	3,000.1	5,731.1	2,593.3	5,309.8
South Sulawesi	4,942.3	4,412.4	10,593.5	8,967.2	13,701.5	11,872.6	16,805.3	14,149.9	19,384.3	15,645.6	19,583.1	16,235.7
South East Sulawesi	603.7	2,132.8	659.4	2,888.8	963.6	2,950.2	1,392.7	3,511.4	2,255.7	3,537.5	2,384.8	4,715.8
North Maluku	357.5	1,295.3	586.2	1,631.0	632.6	1,677.2	895.9	2,016.6	1,005.8	1,815.6	1,006.5	2,397.0
Maluku	968.0	1,892.7	1,272.8	2,352.4	1,147.1	2,689.7	1,388.7	2,716.3	1,781.0	2,865.8	1,789.5	3,123.3
Papua	4,561.7	8,699.5	4,710.1	9,986.1	6,046.8	13,600.2	6,785.9	12,128.3	6,793.7	11,298.5	6,099.0	11,623.5
West Papua									11.7	170.1	517.5	1,898.6
Total	**210,919**	**246,909**	**293,317**	**346,849**	**366,171**	**428,836**	**436,806**	**489,177**	**484,161**	**511,300**		

Notes: Bangka Belitung and West Papua Offices begin its activity on year 2014.

Table 23. **World Economic Growth**

Percent, yoy

Countries	2010	2011	2012	2013	2014	2015e
World	**5.4**	**4.2**	**3.4**	**3.3**	**3.4**	**3.1**
Advanced Economy Countries	3.1	1.7	1.2	1.1	1.8	1.9
United States of America	2.5	1.6	2.2	1.5	2.4	2.4
Euro Area	2.0	1.6	-0.8	-0.3	0.9	1.6
Germany	3.9	3.7	0.6	0.4	1.6	1.3
France	2.0	2.1	0.2	0.7	0.2	1.4
Italy	1.7	0.6	-2.8	-1.7	-0.4	1.0
Japan	4.7	-0.5	1.7	1.6	0.0	0.6
United Kingdom	1.9	1.6	0.7	1.7	2.9	2.2
Canada	3.4	3.0	1.9	2.0	2.5	1.2
Developing Countries and Emerging Markets	7.5	6.3	5.2	5.0	4.6	4.0
Africa Sub-Sahara	6.6	5.0	4.3	5.2	5.0	3.5
Latin America and Caribbean	6.1	4.9	3.1	2.9	1.3	-0.3
Developing Countries and Emerging Asian	9.6	7.9	6.8	7.0	6.8	6.6
China	10.6	9.5	7.7	7.7	7.3	6.9
Developing Countries and Emerging Europe	4.8	5.4	1.3	2.9	2.8	3.4
Commonwealth of Independent States	4.6	4.8	3.4	2.2	1.0	-2.8
Russia	4.5	4.3	3.4	1.3	0.6	-3.7
Middle East and North Africa	5.2	4.6	5.0	2.1	2.8	2.5

Sources: IMF-World Economic Outlook Database January 2016 and Bloomberg.

Table 24. **World Inflation Rate**

Annual average, percent

Countries	2008	2009	2010	2011	2012	2013	2014	2015
World	**6.4**	**2.8**	**3.8**	**5.2**	**4.2**	**3.9**	**3.5**	**3.3**
Advanced Economy Countries	3.6	0.4	1.7	2.7	2.1	1.5	1.6	0.4
United States of America	3.8	-0.3	1.6	3.1	2.1	1.5	1.6	0.1
Euro Area	3.3	0.3	1.6	2.7	2.5	1.4	0.4	0.0
Germany	2.7	0.2	1.1	2.5	2.1	1.6	0.8	0.1
France	3.2	0.1	1.7	2.3	2.2	1.0	0.6	0.1
Italy	3.5	0.8	1.6	2.9	3.3	1.2	0.2	0.1
Japan	1.4	-1.3	-0.7	-0.3	0.0	0.3	2.7	0.8
United Kingdom	3.6	2.2	3.3	4.5	2.8	2.6	1.5	0.0
Canada	2.4	0.3	1.8	2.9	1.5	2.0	2.4	1.3
Emerging Economies	8.9	4.5	5.7	6.6	4.7	4.9	4.4	4.5
Africa	10.8	8.8	8.3	7.9	8.5	7.1	6.9	7.2
Latin America	9.1	6.5	6.8	7.8	6.6	7.2	8.2	11.2
Asian (excluding Japan)	6.4	1.9	4.7	5.6	3.6	3.7	2.8	2.1
China	5.9	-0.7	3.3	5.4	2.7	2.6	2.0	1.4
Malaysia	5.4	0.6	1.7	3.2	1.7	2.1	3.2	2.1
Thailand	5.5	-0.8	3.3	3.8	3.0	2.2	1.9	-0.9
Philippines	8.2	4.3	3.8	4.7	3.2	2.9	4.2	1.4
Vietnam	23.1	6.5	11.8	18.1	6.8	6.0	1.8	0.6
Russia	14.1	11.7	6.9	8.5	5.1	6.8	7.8	15.6
Middle East	8.7	4.4	3.7	4.0	3.1	3.1	3.2	3.7

Source: Bloomberg

Table 25. **Interest Rates and Exchange Rates**

End of Periode, percent

Items	2009	2010	2011	2012	2013	2014	2015
Government Bond Yield (10 year), %							
Unites States of America	3.84	3.29	1.88	1.76	3.03	2.17	2.27
Japan	1.30	1.13	0.98	0.79	0.74	0.33	0.27
Euro Area	3.39	2.96	1.83	1.32	1.93	0.54	0.63
6 months LIBOR, %							
USD	0.43	0.46	0.81	0.51	0.35	0.36	0.85
Yen	0.48	0.35	0.34	0.28	0.21	0.14	0.14
Euro	0.97	1.18	1.57	0.22	0.35	0.15	-0.04
Exchange Rates							
USD/Yen	93.03	81.12	76.91	86.75	105.31	119.78	120.22
USD/EUR	1.43	1.34	1.30	1.32	1.37	1.21	0.92
USD/GBP	1.62	1.56	1.55	1.63	1.66	1.56	1.47

Source: Bloomberg

Glossary

Term	Description
Administered prices	Inflation predominantly influenced by shocks from government policy and prices, for example prices of subsidised fuels, electricity billing rates, and transport fares
Austerity program	Economic policy program aimed at reducing the budget deficit significantly either by raising taxes or cutting government spending
Bailout	Loan injection to a company or country that having serious financial difficulty or bankruptcy
Barrel	Unit of volume, normally used in international oil trading
Basel III	A global regulatory standard on bank soundness based on bank capital adequacy, stress testing, and market liquidity. The members of the Basel Committee on Banking Supervision agreed this regulations will be implemented in 2013-2018
BI Rate	The policy rate reflecting the monetary policy stance adopted by Bank Indonesia
Bid to Cover Ratio	A ratio to describe the level of demand for certain securities during the bidding process by comparing total bids with the amount won
Capital Flows	The movement of money for the purpose of investment, trade or business production can be either inflow or outflow
Capital Reversal	Sudden reversal on the direction of capital inflows
Clean Money Policy	Policy for replacement of damaged or soiled currency with currency fit for circulation in order to improve the quality standard of currency in circulation
Consensus Forecast	Future predictions made by combining several separate forecasts made with the use of different methodologies
Cost Push Inflation	Inflation arising from pressure from the supply side. The factors driving cost push inflation may arise from depreciation in the exchange rate, impact of imported inflation, particularly in trading partner nations, increases in administered prices and the occurrence of negative shocks due to natural disasters and disruption to distribution
Countercyclical Buffer	A policy aimed at preventing the occurrence of systemic risk due to periods of excessive channeling of loans through the establishment of additional capital for bank
Credit Limit	Maximum limit of credit that may be extended
Credit Rating	An assessment of the creditworthiness of an individual or corporation
Crisis Management Protocol	Procedure for crisis management that establishes the protocol for deploying a management team and defines the roles and responsibilities of the members of the team
Deflation	General decline in prices of goods and services
Deleveraging	the reduction of the leverage ratio, or the percentage of debt in the balance sheet of a single economic entity, such as a household or a firm
Dependency Ratio	Ratio of the dependence of population of nonproductive age to the productive population
Deposit Facility	Placement of rupiah funds by banks at Bank Indonesia
Deposit Rate	Rate of interest on a bank deposit
Time Deposit	A certain amount of funds placed at bank for a fixed term before it may be withdrawn without incurring a penalty
Rupiah Depreciation	Decline in the rupiah exchange rate against foreign currencies
Devisa	Foreign exchange: All goods that may be used as international payment instruments
Disposable Income	Amount of the personal income of an individual that may be used for purchases and saving, after deduction for taxes and other costs
Down Payment	Initial payment before completing payment on a purchase
Dropshot	Redistribution policy of rupiah currency fit for circulation (ULE) deposited by a bank in which Bank Indonesia does not need to perform a detailed count and sort of that currency before recirculating them to the same bank (depositing bank) or any other bank. Payment by Bank Indonesia to the bank is made using one unbroken, sealed transparent plastic package (10 bundles) bearing the label of the depositing bank.
Durables	Goods with long-lasting use
Fiscal Expansion	Policy for increasing fiscal operations by expanding government expenditures
Emerging Markets	Group of nations with rapidly growing economies, reflected among others in their financial markets development and industrialisation
E-Money	Electronic money, i.e. a payment instrument with the following features: (1) issued on the basis of the value of money paid in advance to the issuer; (2) monetary value is stored electronically on a medium such as server or chip; (3) used as an instrument for payments to merchants who are not issues of the electronic money; and (4) the value of the electronic money paid in by the holder and managed by the issuer does not constitute a deposit as referred to in the laws governing banking.
Euro	Currency of the countries in the Eurozone

Term	Description
Exchange Rate Pass Through	Percentage of change in the local currency attributable to movement in the exchange rate between the exporting and importing countries. Exchange rate pass through occurs when the change in currency value influences changes in prices and also inflation
Export	Sale of goods or commodities from one country to another.
Enabling Factor	Factor that is supportive
External Imbalance	The presence of current account deficit and/or capital outflow
Financial sophistication	The act of creating and popularizing new financial instruments as well as new financial technologies, institutions, and markets
Financial Inclusion	The right of every individual to have full access to quality financial services on a timely, convenient and clearly defined basis at affordable cost
Fiscal Drag	Tight fiscal policy imposed by a government that leads to low aggregate demand to the extent of generating deflationary pressure, normally because of inadequate state expenditures or excessive taxes
Fiscal Space	Space for fiscal policy expansion
Flight to Quality	Term used to describe the phenomenon on financial markets when investors sell what they consider to be risky investments and buy safer investments
Fiscal Sustainability	Ability to finance or support government programmes over the long-term
Fixed Subsidy	Subsidy provided in a fixed amount
Foreign Exchange Swap/ FX Swap	Transaction/contract for the purchase or sale of a foreign currency against another (foreign) currency on a specified date together with an agreement to sell or repurchase at a different date in the future at a price stipulated at the contract date. The two transactions are conducted simultaneously and with the same counterparty
Forward Guidance	Instrument used by central banks to carry out monetary policy for influencing market expectations about interest rate levels in the future
Demand Deposit	Deposits at banks in which withdrawal may be made on demand using a cheque or other payment order or by book-keeping transfer
Global Value Chain	Global network containing all parties involved in the production of a good or service
Hedging	Techniques of mitigating risks arising from price fluctuations on the financial market
Idle Money	Money that does not earn any income hence may gradually lose its value due to inflation
Import	Activity of purchasing goods from overseas
Imported Inflation	Inflation caused by price increases for imported goods
Poverty Gap Index	Average measure of gap between individual spending by the poor and the poverty line. The greater the index, the lower the average spending per person compared to the poverty line, or the deeper the level of poverty
Poverty Severity Index	Measurement of the distribution of spending among the poor. The higher the index, the greater the disparity among the poor themselves
Industrial Upgrading	A process of improving the ability of a firm or an economy to move to more profitable and/or technologically sophisticated capital and skill-intensive economic niches
Inflation	General increase in prices of goods and services
Core Inflation	Persistent component in inflation movements, influenced by fundamentals such as demand-supply interaction, exchange rate, international commodity prices, trading partner inflation and inflation expectations
Traded Core Inflation	Core inflation reflecting external pressures
Interbank Lending	Loans extended by banks to one another for a specific term. The loans usually are short-term loans.
Intercompany Loans	Loans made by a department to another department within the organizational structure
Interoperability	Capability of a system to interact and function with other systems without limitation of access
Intra-regional Trade	Trade in goods and services between countries of the same region or economic zone.
Investment	Accumulation of a form of assets with the expectation of earning profit in the future. At times, investment is also referred to as capital investment
Portfolio Investment	Investment in securities traded on the financial market
Investment Grade	Rating as suitable for investment
Leading Indicator	A measurable economic factor that changes before the economy starts to follow a particular trend
Lending Facility	Provision of rupiah funds by Bank Indonesia to banks
Less Cash Society	Society accustomed to using non-cash instruments of payment

Term	Description
Lifting	Volume of oil taken from stock, transported by tanker or pipeline and sold to buyers. In other words, lifting is oil production that is ready for sale
Long-Term Financing Operation	A very low interest rate long-term loan scheme for European banks that was offered by ECB to help ease the European financial crisis
Low Income Country	Country with low level of incomes
Lower Middle Income Country	Country with lower-middle level of incomes
M1	Narrow measure of money (currency outside banks and demand deposits)
M2	Broad measure of money (currency outside banks, demand deposits, quasi-money and securities other than stocks)
Macroprudential	Approach to financial regulation with the aim of mitigating risks in the overall financial system
Margin	Difference
Medium/High Technology	Type of technology used in the production of exported goods
Middle Income	Segment of population with middle level incomes
Middle Income Trap	A situation where a country's economic growth slows after reaching middle income levels. The growth is not enough to bring the country into high-income levels
Microprudential	Prudential approach related to the management of an individual financial institution so that its survival in ensured
Minimum Holding Period	Minimum times for holding assets
Mismatch	The difference in maturities between assets and liabilities side of a financial institution
Current Account	Part of balance of payments that records a nation's flow of goods and services
Negative Interest Rate	A negative return on deposits charged by the central bank or commercial bank. This scheme was implemented in some countries, e.g. Euro and Japan, to boost their domestic economy
Net Demand	More demand than what is produced
Net Interest Margin	Ratio of net interest income to average earning assets
Net Supply	More produced than there is demand
Net Worth	Total assets minus total liabilities for an individual or company
New Order	communication of an intention to buy for immediate or future delivery
Nontradables Sector	Sector not generating outputs that can be traded overseas
Nondurables Goods	goods that are immediately consumed in one use or ones that have a lifespan of less than 3 years
Offshore	Foreign exchange transactions conducted outside the territory of the country that issues the currency
Online Banking	Financial transactions conducted with the use of an internet connection
Onshore	Foreign exchange transactions conducted within the territory of the country that issues the currency
Monetary Authority	An entity that has the authority to control the money supply in a country and have the right to set interest rates and other parameters that determine the cost and supply of money
Bond Market	Place for trading bonds
Monetary Loosening	Monetary policy for boosting economic performance judged to be moving too slowly. Example: lowering interest rates
Monetary Tightening	Monetary policy for restraining economic performance judged to be moving too fast. Example: raising interest rates
Periphery	A group of less developed countries (areas) that connected to an advanced center country within a certain economic zone
Push factor	Common factors that drive the movement of capital flows to certain countries
Quantitative Easing	Policy for monetary loosening or augmenting the monetary stimulus by the central bank by purchasing financial assets in a certain volume from commercial banks or other private institutions
Gini Ratio	A measure of income inequality
Reinvestment Earning	Part of foreign income that does not transferred abroad but it spent for investment in the domestic economy (Balance of Payment context)
Repo	See "Repurchase Agreement"
Repurchase Agreement	Transaction for the sale of a securities instrument between two parties followed by an agreement in which repurchase of the same securities will be executed at an agreed price at a future date
Levy	Local charges for a payment of services or special permits provided and/or granted by the local government for the benefit of individuals or bodies

Term	Description
Return	Yield or profit, i.e. one factor motivating investors to invest and also rewarding an investor's courage in assuming the risks of his investment
Reverse Repo	Transaction for purchase of securities with a commitment to resell at an agreed term and price
Right Issue	Rights to subscribe/purchase new shares issued by a company
Risk Appetite	Limit of acceptable risk
Risk Aversion	Investor tendency to avoid risk
Risk Free	the minimum return an investor expects for any investment because he will not accept additional risk unless the potential rate of return is greater than the risk-free rate.
Safe Heaven Asset	Assets with low risk
Samurai Bonds	Yen-denominated bond issued in Japan by non-Japanese company
Second Round Effect	The knock-on effects of a policy
Payment System	System related to transfer of an amount of money from one party to another party
Smelter	Facility for processing mined ore with the function of increasing metal content to a level that meets a standard as raw material for end products
Solvability	The ability of a company to meet its short-term and long-term liabilities
Fiscal Stimulus	Fiscal policy of a government aimed at influencing aggregate demand that in turn (is expected) will exert influence on activity in the economy in the short-term
Subsidy	Form of financial assistance paid by the government to producers, distributors, consumers and the public in defined areas
Sukuk	Long-term created securities based on sharia principles
Super Cycle	A period in which the world economy experiences rapid growth as a result of a combination of factors, among other are technological progress and natural resources
Supervisory Action	Action undertaken in the course of bank supervision to strengthen the resilience of a bank
Surveillance	Observation or monitoring of activities, behaviour or other changes in information of a target
Tenor	Term for repayment of a loan, stated in days, months or years
Term Deposit	An amount of funds placed at a bank or other financial institution for a minimum term before it may be withdrawn without incurring a penalty. Also referred to as time deposit
Terms of trade	Ratio of export prices to import prices
The Fed	The central bank of the United States, comprising an independent entity within government administration
Unbanked	Individuals or business that do not have access to financial services typically offered by financial institutional
Upper Middle Income	Segment of population with middle to high incomes
Velocity of Money	Concept that indicates how many times money circulates within an economy over the course of a year
Volatile Food	Inflation predominantly influenced by shocks in the food category, such as harvests, adverse natural elements or factors in the movement of domestic food commodity prices or movement in international food commodity prices
Yield	Income or profit or return that will be obtained from investment

Abbreviations

No.	Abbreviation	Description
1	ABIF	ASEAN Banking Integration Framework
2	ABS	Asset Backed Securities
3	ABSPP	Asset-Backed Securities Purchase Program
4	ACI	Cambiste Association Internationale
5	ADB	Asian Development Bank
6	AEC	ASEAN Economic Community
7	AFAS	Framework Agreement on Services
8	AFI	Alliance for Financial Inclusion
9	AFSBI	Bank Indonesia's Strategic Functions
10	AIIB	Asian Infrastructure Investment Bank
11	AMRO	ASEAN + 3 Macroeconomic Research Office
12	AP	Administered Prices
13	APBD	Local government budget
14	APBN	State budget
15	APBN-P	Revised State budget
16	ARAM	Rate Forecast
17	ASA	ASEAN Swap Arrangement
18	ASEAN	Association of Southeast Asian Nations
19	ASEAN 5	Malaysia, Indonesia, Singapore, Thailand, Philippines
20	ASEAN+3	ASEAN + China, Japan and South Korea
21	ATIGA	ASEAN Trade in Goods Agreement
22	ATM	Automated Teller Machine
23	Bansos	Social Assistance
24	Bappenas	National Development Planning Agency
25	Bareskrim	Criminal Investigation Unit of the National Police
26	BCBS	Basel Committee on Banking Supervision
27	BCSA	Bilateral Currency Swap Arrangement
28	BI	Bank Indonesia
29	BI-CAC	Bank Indonesia-Counterfeit Analysis Center
30	BIG-eB	Bank Indonesia Government Electronic Banking
31	BIS	Bank for International Settlements
32	BKPM	Investment Coordinating Board
33	BLU	Public Service Agency
34	BNP2TKI	National Agency for the Placement and Protection of Indonesian Migrant Workers
35	BoE	Bank of England
36	BoJ	Bank of Japan
37	BOK	Bank of Korea
38	BOP	Balance of Payment
39	BOPO	Operating Expenses to Operating Income
40	Botasupal	Coordinating Agency for Eradication of Counterfeit Money
41	BPD	Regional Development Banks
42	BPK	Audit Board of the Republic of Indonesia
43	BPM6	Balance of Payments and International Investment Position Manual, 6th edition

No.	Abbreviation	Description
44	BPN	National Land Management Agency
45	BPR	Rural Banks
46	BPS	Statistics Indonesia
47	BSA	Bilateral Swap Arrangement
48	BSM	Help Poor Students
49	BU	Commercial Banks
50	BUK	Conventional Commercial Banks
51	BUKU	Commercial Banks by Group of Operations
52	BULOG	National Logistics Agency
53	BUMN	State-Owned Enterprises
54	BUSN	Private Banks
55	CAR	Capital Adequacy Ratio
56	CBCA	Cross Border Collateral Arrangement
57	CBP	Government Rice Buffer Stock
58	CBPP	Covered Bond Purchase Program
59	CBR	Central Bank of Russia
60	CBRT	Central Bank of the Republic of Turkey
61	CBU	Completely Build Up
62	CCB	Countercyclical Buffer
63	CDS	Credit Default Swap
64	CeBM	Central Bank Money
65	CF	Consensus Forecast
66	CGE	Computable General Eqiilibrium
67	CGS	Comprehensive Growth Strategy
68	CIP	Covered Interest Parity
69	CIV	Cash In Vault
70	CMIM	Chiang Mai Initiative Multilateralization
71	COB	Currency Outside Banks
72	CPI	Consumer Price Index
73	CPO	Crude Palm Oil
74	DAK	Special Allocation Funds
75	DB	Doing Business
76	DBH	Revenue Sharing Funds
77	DF	Deposit Facility
78	DFS	Digital Financial Services
79	DHE	Export Proceeds
80	DJPK	The Directorate General of Fiscal Balance
81	DJPL	The Directorate General of Sea Transportation
82	DNI	Negative Investment List
83	DPAU	Department of Financial Access and MSMEs Development
84	DPK	Bank Deposits
85	DPM	Department of Monetary Management
86	DPR	Board Representatives of Indonesia
87	DSR	Debt Service Ratio
88	ECB	European Central Bank

Abbreviations - Continued

No.	Abbreviation	Description
89	EDC	Electronic Data Capture
90	EM	Emerging Markets
91	EMBIG	Emerging Market Bond Index Global
92	EMEAP	Executives' Meeting of East Asia Pacific Central banks
93	E-payment	Electronic payment
94	ESDM	Energy and Mineral Resources
95	FASBIS	BI Sharia Deposit Facility
96	FDI	Foreign Direct Investment
97	FDR	Financing to Deposit Ratio
98	FFR	Federal Funds Rate
99	FIN	Financial Identity Number
100	FKMM	Forum for Macro/Micro-prudential Coordination
101	FKSSK	Coordination of Financial System Stability
102	FMIs	Financial Market Infrastructures
103	FOMC	Federal Open Market Committee
104	FSAP	Financial Sector Assessment Program
105	FSB	Financial Stability Board
106	FTV	Financing to Value Ratio
107	FX	Foreign Exchange
108	G20	Group of Twenty
109	Gapoktan	Farmers Group
110	GBI	Governor of Bank Indonesia
111	GDP	Gross Domestic Product
112	GFSN	Global Financial Safety Net
113	GIH	Global Infrastructure Hub
114	GII	Global Infrastructure Initiative
115	GMRA	General Master Repurchase Agreement
116	GNNT	National Non-Cash Movement
117	GPA	Global Policy Agenda
118	GPFI	Global Partnership on Financial Inclusion
119	GSIBs	Global Systemically Important Banks
120	GTCK	Chili Planting Movement in Dry Season
121	GVCs	Global Value Chains
122	GWM	Reserve Requirement
123	HCS	Perfectly Printed Rupiah
124	HLM	High Level Meeting
125	ICP	Indonesia Crude Price
126	IKNB	Nonbank Financial Institutions
127	IMF	International Monetary Fund
128	Inpres	Presidential Instruction
129	IOSCO	International Organization of Security Commissions
130	IPE	Retail Sales Index
131	IPO	Initial Public Offerings
132	IPTEK	Science and Technology

No.	Abbreviation	Description
133	ISSK	Financial System Stability Index
134	ITF	Inflation Targeting Framework
135	Jabodetabek	Jakarta, Bogor, Depok, Tangerang, Bekasi
136	JCI	Jakarta Composite Index
137	JGB	Japanese Government Bonds
138	JIBOR	Jakarta Interbank Offered Rate
139	JISDOR	Jakarta Interbank Spot Dollar Rate
140	JKD	Data Communication Network
141	JPKI	International Financial Safety Net
142	JPSK	Financial System Safety Net
143	K/L	Ministry / Agency
144	KAD	Inter-Regional Collaboration
145	KADIN	Indonesian Chamber of Commerce and Industry
146	KCJ	Railway Commuter Jabodetabek
147	KEA	ASEAN Economic Community
148	KI	Investment Loan
149	KIP	Smart Indonesia Card
150	KIS	Health Indonesian Card
151	KK	Consumer Loan
152	KKP	Ministry of Maritime Affairs and Fisheries
153	KKS	Prosperous Family Card
154	KMK	Working Capital Loan
155	KPK	Corruption Eradication Commission
156	KPR	Housing Loan
157	KPwDN-BI	Bank Indonesia Regional Representative Office
158	KSEI	Indonesian Central Securities Depository
159	KSK	Study of Stability of the Financial System
160	KSKS	Family Prosperity Saving Card
161	KSM	Very Poor Families
162	KTI	East Indonesia Region
163	KUPVA	Non-Bank Foreign Exchange Business Activities
164	KUR	Small Business Loans
165	LCR	Liquidity Coverage Ratio
166	LCS	Less Cash Society
167	LDR	Loan to Deposit Ratio
168	LF	Lending Facility
169	LKK	Conventional Financial Institutions
170	LKPP	Central Goverment's Financial Report
171	LKS	Sharia Financial Institutions
172	LLD	Foreign Exchange Flow
173	LPG	Liquefied Petroleum Gas
174	LPS	Deposits Insurance Corporation
175	LTRO	Long-Term Refinancing Operation
176	LTV	Loan to Value
177	LU	Business Sector

No.	Abbreviation	Description
178	MHP	Minimum Holding Period
179	MOPS	Mean of Platts Singapore
180	MoU	Memorandum of Understanding
181	MP3EI	Masterplan for the Acceleration and Expansion of Indonesia's Economic Development
182	MRA	Master Repurchase Agreement
183	MRA	Master Repurchase Agreement
184	MSMEs	Micro, Small, and Medium Enterprises
185	MTM	Month to Month
186	NAV	Net Asset Value
187	NDA	Net Domestic Assets
188	NDF	Non Deliverable Forward
189	NFA	Net Foreign Assets
190	NFP	Nonfarm Payrolls
191	NIM	Net Interest Margin
192	NKRI	Republic of Indonesia
193	Nonmigas	Non Oil and Gas
194	NPF	Non Performing Financing
195	NPG	National Payment Gateway
196	NPISH	Nonprofits Institution Serving Household
197	NPLs	Non-Performing Loans
198	NTB	West Nusa Tenggara
199	O/N	Overnight
200	OECD	Organisation for Economic Co-operation and Development
201	OJK	Financial Services Authority
202	OM	Monetary Operation
203	OMO	Open Market Operations
204	OPEC	Organisation of the Petroleum Exporting Countries
205	OTC	Over The Counter
206	P2P	Person to Person
207	PAD	Regionally Generated Revenues
208	PBB	Land and Property Tax
209	PBI	Bank Indonesia Regulation
210	PBoC	People's Bank of China
211	PDRB	Regional Gross Domestic Product
212	Pelni	National Shipping Company of Indonesia
213	Pemda	Local Government
214	Pemilu	General Election
215	Pemprov	Provincial Government
216	PerMen	Minister Regulation
217	Perpres	Presidential decree
218	Perum Peruri	The Indonesia Government Security Printing and Minting Corporation
219	PFMIs	Principles for Financial Market Infrastructures
220	PII	International Investment Position

No.	Abbreviation	Description
221	PIN	Personal Identification Number
222	PKH	Family Hope Program
223	PLJP	Short-Term Liquidity Loans
224	PLL	Precautionary and Liquidity Line
225	PLN	State Electricity Company
226	PMA	Foreign Investment
227	PMK	Finance Minister Regulation
228	PNBP	Non Tax Revenue
229	PNPM	National Program for the Empowerment of the People
230	PNS	Civil Servants
231	Pokjanas	National Working Group
232	Poktan	Farmers group
233	PP	Finance Companies
234	PPh	Income Tax
235	PPnBM	Sales Tax on Luxury Goods
236	PPP	Purchasing Power Parity
237	PSE	Electronic Service System
238	PSKS	Family Welfare Deposit Programme
239	PTK	Financial Transactions Programme
240	PTP	Point to Point
241	PUAB	Interbank Money Market
242	PUR	Currency management
243	QAB	Qualified ASEAN Banks
244	QE	Quantitative Easing
245	Rakornas	TPID National Coordination Meeting
246	RBA	Reserve Bank of Australia
247	RBI	Reserve Bank of India
248	RCAP	Regulatory Consistency Assessment Program
249	RCEP	Regional Comprehensive Economic Partnership
250	RCU	Money Printing Plan
251	RDG	The Board of Governors' Meeting
252	REMBI	Regional Macroeconomic Model
253	RFA	Regional Financial Arrangements
254	RKP	Government Work Plan
255	RKPD	Regional Working Program Plan
256	RKT	Sustainability Plan Task
257	RMB	Renminbi
258	ROA	Return on Assets
259	ROE	Return on Equity
260	RR	Reverse Repo
261	RT	Households
262	RTGS	Real Time Gross Settlement
263	SAK-ETAP	Financial Accounting Standards module for Entities
264	SAP	Strategic Action Plan

No.	Abbreviation	Description
265	SARB	South African Reserve Bank
266	SBI	Bank Indonesia Certificates
267	SBN	Government Securities
268	SBS	Sharia Repo Securities Transactions
269	SBSN	Sharia Based Government Bonds
270	SDA	Natural Resources
271	SDBI	Bank Indonesia Certificates of Deposit
272	SDHI	Indonesian Haj Funds Sukuk
273	SDM	Human Resources
274	SDR	Special Drawing Rights
275	SE	Circular letter
276	SIB	Systemically Important Banks
277	SiLPA	Budget Financing Surplus
278	SITC	Standard International Trade Classification
279	SK	Decree
280	SKDU	Business Survey
281	SKNBI	Bank Indonesia National Clearing System
282	SMEs	Small and Medium Sized Enterprises
283	SNRT	Survey of Household Balance Sheet
284	SOP	Standard Operational Procedure
285	SP	Payment System
286	SPN	Government Treasury Bills
287	SPPUR	Payment System and Rupiah Currency Management
288	SPT	Notice
289	SSK	Financial System Stability
290	SSSS	Securities Settlement System
291	SUN	Government Bonds
292	TA	Technical Assistance
293	TD	Term Deposit
294	TKI	Indonesian Migrant Workers
295	TLAC	Total Loss absorbing Capacity

No.	Abbreviation	Description
296	TMF	Capital and Financial Account
297	TNI	Indonesian National Army
298	TNI-AL	Indonesian Army-Navy
299	TNP2K	Team for the Acceleration of Poverty Reduction
300	ToB	Training of Beneficiaries
301	ToT	Training of Trainers
302	TPI	Inflation Monitoring and Controling Team
303	TPID	Regional Inflation Monitoring and Controling Team
304	TTL	Electricity Tariffs
305	TUKAB	Interbank Cash Transactions
306	U.S.	United States
307	UKA	Foreign Exchange Bank Notes
308	ULE	Fit Notes and Coins
309	ULN	Foreign Debt
310	UMP	Provincial Minimum Wages
311	Upsus	Special Improvement Efforts
312	UTLE	Currency Unfit for Circulation
313	UU	Legislation
314	UUS	Sharia Business Units
315	Valas	Foreign Currency
316	VAT	Value Added Tax
317	VCF	Value Chain Financing
318	VF	Volatile Foods
319	WCPSS	Working Committee on Payment and Settlement Systems
320	WEO	World Economic Outlook
321	WIIB	World Islamic Investment Bank
322	Wisman	Foreign Tourists
323	WTO	World Trade Organization
324	YoY	Year on Year
325	ZIS	*Zakat, Infak, Dole*

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