



PART IV

CHALLENGES, POLICY DIRECTION, AND OUTLOOK OF INDONESIA ECONOMY

Image Caption:

One of the key challenges in the Indonesian economy is the quality of infrastructure. Bridges are part of the connectivity infrastructure so urgently needed for achieving equitable distribution of economic growth throughout the Indonesian archipelago.

INFOGRAPHICS: PART IV

CHALLENGES, POLICY DIRECTION, AND OUTLOOK OF INDONESIA ECONOMY

UPCOMING GLOBAL CHALLENGES

- Sluggish economic growth
- Potentially protective trade policy
- Policy which increases capital reversal.
- Increased in global inflation trends.

UPCOMING DOMESTIC CHALLENGES



Short Term Domestic Challenges

- Capability to increase tax revenue
- Completion of corporates and banks consolidation process
- Policy transmission effectiveness
- Risk of increasing inflation pressure



Medium Term Domestic Challenges

- Improving export's composition
- Enhance the role of industrial sector
- Promote market competition and sound trade.
- Strengthened domestic financing structure



POLICY MIX RESPONSE



GOVERNMENT



BANK INDONESIA



FINANCIAL SERVICES AUTHORITY

COORDINATION AND SYNERGY



FISCAL



MONETARY



MACRO PRUDENTIAL



MICRO PRUDENTIAL



PAYMENT SYSTEM



STRUCTURAL REFORM

ECONOMIC OUTLOOK

GDP Growth

5.0-5.4%

Inflation

4.0±1%

Current Account Deficit

<2.5%

Credit Growth

10-12%

Deposit Growth

9-11%



Current Account Deficit
<2.5% of GDP



Inflation expected to be at 3±1%



Higher and more sustained economic growth

MEDIUM TERM OUTLOOK

PART IV

Challenges, Policy Direction, and Outlook of Indonesia Economy

The outlook for Indonesia is an increasingly robust economy, but this economy will require astute management going forward due to some challenges are still emerging and can lower the economic outlook ahead. These challenges have arisen from both global and domestic risks that, if not immediately mitigated, are at risk not only to make economic growth unsuitable, but also to put pressure on economic stability. Once stability is disrupted and this condition persists, it will generate pressures that in turn will weigh down on economic growth both in the short term and in the medium-long term.

The economic challenge has been triggered by four interconnected global risks. First, there is the risk that the recovery in global economic growth and trade volume will underperform forecasts, which in turn may cause commodity prices to fall short of projected levels. Second, international trade policies in advanced economies will become more protective. This second risk may bring further reduction in the world trade volume, global economic growth, and commodity prices. Third, the combination of US macroeconomic policy, especially expansive fiscal policy and tighter monetary policy may heighten the risk of capital reversal to the US and the uncertainty of world financial markets. Fourth, global inflation is rising again when world commodity prices continue to rise.

Economic challenges need even greater attention because the completion of various domestic issues will also be the key to the acceleration of economic recovery. First, it is related to the ability to increase tax revenue as a basis for creating greater space for a fiscal stimulus in stimulating economic growth. Second, it deals with the speed of completion of the corporate and banking consolidation process. Third, concerning efforts to reinvigorate the effectiveness of monetary policy transmission, which had previously stalled due to the consolidation of the banks and corporations. Finally, on efforts to optimize the strategy for controlling the risk of mounting inflation.

In the medium and long term, economic challenges are related to strengthening the structure of the economy for greater resilience. These efforts are aimed at preventing Indonesia from the trap of middle-income economies.

These challenges relate to the drive for structural reinforcement of the economy in the real sector and the financial sector. The structural challenges in the real sector relate to expand the diversity of export product composition so as to complement the role of resource-based exports. Challenges in the real sector also link to expand the manufacturing role in the economy and strengthening the market structure and trading system in support of greater efficiency. The challenges in the financial sector relate to strengthening domestic financing structures for greater diversity, increasing the structure of bank funds to become more balanced, and deepening financial markets so as to support economic financing and improve the effectiveness of monetary policy.

Macroeconomic policy in 2017 will seek to mitigate an array of risks and their effect on the Indonesian economy. The policy direction will be implemented through policy synergy among the Government, Bank Indonesia, and the Financial Services Authority. The policy synergy will be implemented through fiscal, monetary, macroprudential, microprudential, and structural policy mixes. Policy synergies are aimed at mitigating short-term cyclical risks in order to sustain the momentum for economic recovery. In addition, policy synergy is also directed to continue to strengthen the structure of the economy for greater resilience and competitiveness.

In 2017, Bank Indonesia will stay the course in safeguarding economic stability, which will serve as a basis for accelerating economic recovery. In this context, Bank Indonesia will pursue a mix of monetary, macroprudential, payment system and rupiah currency management (SP-PUR) policies. Monetary policy will be focused on maintaining macroeconomic stability and synergizing with macroprudential policies directed at maintaining financial system stability. Meanwhile, the policy of payment system and rupiah currency management will be aimed to support structural improvements through increasing transaction efficiency in the economy so as to support the operation of monetary and macroprudential policy transmission, as well as maintaining financial system stability.

Bank Indonesia will consistently take monetary policy to control inflation in line with the target and keep the current account deficit at a healthy level. Consistent with the monetary policy direction, policy rate will still be directed to keep inflation in line with the target. Exchange rate policy will be focused on maintaining the stability of the rupiah exchange rate in line with its fundamental value. The monetary policy direction will also be supported by the strengthening of monetary policy operations, such as the implementation of an averaging statutory reserve requirement in mid-2017 and optimizing the use of Government Securities as a monetary operation instrument replacing Bank Indonesia Certificates in stages.

Bank Indonesia will also optimize macroprudential policy and payment system to ensure financial system stability with low systemic risk and support economic activities efficiency. In this regard, macroprudential policies will remain directed to mitigate the accumulation of risks arising from the behaviour of systemic procyclicalities and risks in the financial system. Bank Indonesia will also embark on a number of initiatives to accelerate financial market deepening to support both the stability and financial system resilience. Under this policy direction, Bank Indonesia will continue to develop financial markets through an ecosystem approach. In addition, Bank Indonesia will support the acceleration of sharia economic and financial development as a complement to conventional finance. Regarding the payment system, policy will focus on strengthening institutions and infrastructure, and encouraging financial inclusion.

The Bank Indonesia policy mix in 2017 will also be synergized with the policies of the Government and the Financial Services Authority to strengthen policy effectiveness in maintaining macroeconomic and financial system stability and promoting economic recovery. These synergies include coordination with the Government in controlling inflation targeted. In addition, Bank Indonesia will continue to support the Government's efforts to accelerate and sharpen various structural policies that are believed to also contribute significantly to boosting the quality of economic growth.

It is expected that continued support Indonesia's economic recovery in 2017 will come from policy consistency in responding to various challenges. In 2017, Indonesia's economic growth is projected to increase in the range of 5.0-5.4%. This growth will be driven to a large extent by domestic demand, such as consumption and investment, although export performance is expected to improve. Private consumption is expected to continue strong underpinned by good household convictions and a growing middle class economy. Investments will also rise as a result of the continued development of government infrastructure and a resurgence in private investment in line with the positive impact of rising commodity prices. Meanwhile, exports are also expected to increase driven by higher world economic growth and increases in global commodity prices.

Economic stability is predicted to remain under control and accompanied by improved banking intermediation. Inflation is forecasted to rise in 2017, but still manageable within the target range of $4.0 \pm 1\%$. Rising inflation in 2017 will be mainly driven by the impact of rising energy prices and the effect of higher administered prices inflation, while core inflation will remain under control. Alongside the prudently-managed economic stability, the current account deficit is predicted to remain well below the 2.5% level of GDP. Concerning bank intermediation, the outlook for higher economic growth, reduction in credit risk, and potentially declining lending rates may stimulate increases in bank lending during 2017 in the range of 10-12%. A rise in loan growth may yield multiplier effects for depositor funds, which are projected to grow in the range of 9-11% in 2017.

The outlook for improvement of Indonesia's economic growth in the medium term is expected to continue. This outlook is supported by positive impacts of structural reforms pursued by the Government, including various infrastructure improvements. Structural reform will be a foothold for building more robust economic structures in order to improve economic efficiency and productivity and ultimately economic competitiveness. The implementation of the Economic Policy Packages by the Government is expected to improve the investment climate in Indonesia. In addition, household consumption will steadily increase in

tandem with more vibrant economic growth and expanding the number of the middle class. Interregional connectivity will also improve, which not only reinforces production and distribution structures, but also lowers costs of production. These various improvements are expected to strengthen economic stability with inflation predicted to be within the range of $3\pm 1\%$ by 2021.



CHAPTER 15

Economic Challenges and Policy Direction

In 2016, the Indonesian economy held its ground to lay down positive foundations for the future sustainability of economic recovery. However, global and domestic risks that have both a short-term and long-term dimension may pose challenges for management of the economic outlook. In 2017, the direction of macroeconomic policy will focus on mitigating these risks to keep macroeconomic stability well in hand, sustaining the process of economic recovery, and continuation of structural reinforcement of the economy in the medium to long term. Policies will be implemented within a single synergy of policy involving the Government, Bank Indonesia, the Financial Services Authority (OJK), and various stakeholders at the national and sub-national levels.

Image Caption:

Every effort for advancement and progress will also face challenges. The Indonesian economy needs appropriate strategies and policy responses to mitigate risks arising from the global and domestic economic environment.

The Indonesian economy remained competitive and resilience in 2016, which laid down foundations for the future sustainability of economic recovery. In addition to improved cyclical conditions of global and domestic economy in 2017, robust economic recovery will also be supported by prudent management over economic and financial system stability. The potential for further improvement in the economy is even greater, due to the more solid policy synergy established among the different authorities. In addition, the prospect for sustained confidence on the part of economic actors in the corporate and banking sectors, which already started to lift up in the fourth quarter of 2016, is also expected to bolster the outlook for economic recovery in 2017.

On the other hand, various global and domestic risks still persist, which could pose challenges for these efforts to maintain the outlook for economic improvement. The risks may not only cause economic growth to fall short of targeted projections, but may also bring pressure to bear on economic and financial system stability. Inflation may rise, the rupiah exchange rate could become susceptible to downward pressure and financial system stability may suffer. When economic and financial system stability is derailed, this in turn can heighten the risks to economic growth in the short term and also the medium to long term dimension.

At the global level, the risks stemming from mainly four issues that may impact the domestic economy if not addressed properly. The first risk is related to fragile recovery in global economic growth and trade volume, which may again underperform forecasts as was the case in 2016. This may lead to the similarly disappoint expectations over rising commodity prices phenomenon. The second risk is in conjunction with the international trade policies in advanced countries that have turned towards protectionism, along with the development of populist political platforms. The third risk concerns the direction of US macroeconomic policy, in particular expansionary fiscal policy and tight monetary policy that runs the risk of triggering a reversal of US capital from emerging markets and fuelling increased uncertainty on world financial markets. The latter risk is related to the possibility of resurgence in global inflation, particularly if world prices for commodities, including energy, continue to climb.

In the domestic economy, those risks pose challenges that have both short term and long term implications. The challenges are primarily four-fold in the short term. The first challenge concerns with the efforts to increase tax revenues

as a pre-condition for supporting sound and sustainable expansion of fiscal space. The second challenge is related to how fast the corporate and banking consolidation process can reach completion. The third challenge focuses on the efforts for further strengthening of the effectiveness of monetary policy transmission. The last challenge is about the risk of rising inflation if triggered by increased inflation in the administered prices category. In the medium to long term, the challenges to the economy are related to consistency for steady reinforcement of the economic structure for greater resilience while simultaneously ensuring that Indonesia does not become caught in the middle-income trap (See Box 15.1.).

The direction of macroeconomic policy in 2017 will focus on measures for safeguarding macroeconomic and financial system stability to ensure the continuity of economic recovery. In this regard, macroeconomic policy will be directed towards mitigating short-term cyclical risk in order to sustain the momentum for economic recovery and the strengthening of financial system stability. This will be achieved through the ongoing structural reinforcement of the economy for greater resilience and competitiveness. Consistent with this policy direction, the policy synergy involving the Government, Bank Indonesia, and the Financial Services Authority will be strengthened further by a mix of fiscal policy, monetary policy, macroprudential policies, and policies for structural reform.

In line with direction of macroeconomic policy, Bank Indonesia will stay the course in safeguarding macroeconomic stability by employing a policy mix that combines monetary policy, macroeconomic policy, and payment system policy. The focus of monetary policy will be consistently directed towards curbing inflation in line with the target and maintain a prudent level in the current account deficit. Monetary policy will also be supported by a policy for managing the exchange rate in line with fundamentals and the strengthening of policy for monetary operations. In addition, Bank Indonesia will promote financial market deepening through several approaches aimed at supporting financial system stability and resilience, as well as development of sharia-compliant economics and finance. Macroprudential policy will focus on maintaining financial system stability with low systemic risk while continuing to provide space for actions to promote economic recovery. Payment system policy will focus on strengthening of institutions and infrastructure and on promoting financial inclusion. Bank Indonesia will continue to strengthen policy coordination and communication with

various stakeholders in order to boost the effectiveness of the policies in place.

15.1. ECONOMIC CHALLENGES

Global Economic Risks

The predicted upturn in outlook for the Indonesian economy in 2017 will be influenced by the assumption that the global economy is on a sustained upward cycle. World economic growth is forecast to keep arising, bolstered by the progress of economic reforms in many advanced countries. Furthermore, it is assumed that higher world economic growth will spur increases in commodity prices, including the prices for Indonesia's main export commodities. Aside from this, the uncertainties on global financial markets are also assumed to ease in keeping with the outlook for improvement in the global economy.

However, there is also the risk that global economic outlook will disappoint expectations, which may then bear down on the outlook for the Indonesian economy. There are four risks stemming from the global economy that demand attention, as they could derail the economic recovery in Indonesia. These global risks include the following: (i) weaker than expected global economic recovery and trade volume, which in turn will lower the outlook for further improvement in global commodity prices, (ii) adoption of more protectionist international trade policies in advanced countries that may subsequently dampen global economic growth, (iii) capital reversal from emerging markets in line with mounting uncertainty on global financial markets, affected by the risks of a tightened US monetary policy and geopolitical risks in many countries of the world; and (iv) increase in global inflation spurred by upward movement in global commodity prices including oil prices and non-oil and gas commodity prices.

The first risk at the global level is related to the potential lack of improvement in economic growth given that the economic consolidation process in advanced countries has not reached completion, including in China. The slower than predicted recovery in global economic growth will weigh down on global trade volume and in turn ensure that increases in commodity prices fail to meet earlier expectation.

The second risk is related to the protectionist policy stance in international trade by the US and other advanced economies and the risk of greater populism in geopolitics. Initially, this policy direction could lead to contraction in the volume of world trade and in turn have broader impact by

depressing global economic growth and commodity prices. The issues of trade protectionism and populist policies could then spread further afield, thus increasing uncertainty on global financial markets.

The third global risk is related to the risk of capital reversal from emerging markets to the US, triggered by the macroeconomic policy direction adopted by the US. The risk of capital reversal has been triggered by the direction of US fiscal expansion aimed at stimulating US economic growth. The risk of capital reversal will escalate even further when more rapid economic growth then stokes inflationary pressure in the US, and meets with a more aggressive monetary policy tightening response from the Fed. If capital reversal takes place simultaneously with geopolitical risk events in some countries, this could heighten the uncertainty on global financial markets.

The latter risk stems from the tendency towards higher global inflation spurred by increases in energy and non-energy global commodity prices. The risk of escalating global inflation calls for vigilance, given that it will lead to increased domestic inflationary pressure and affect other economic variables.

Challenges for Domestic Economy

In domestic economy, a number of emerging risks will simultaneously pose challenges for managing the positive outlook for the economy. The challenges facing the domestic economy have both a short term and medium to long term dimension. In the short term, the challenges are related to the efforts to increase tax revenues, accelerated completion of the corporate and banking consolidation process, improved effectiveness of monetary policy transmission and risks that may stoke inflationary pressure. In the medium to long -term, the challenges to the economy are directed toward the actions to rectify structural issues in order to build greater resilience into the Indonesian economy. A number of medium to long term challenges are related to efforts for strengthening the various elements that support sustainable economic development.

The first challenge for the domestic economy in the short term is related to the efforts to generate higher tax revenues as a platform for expanding fiscal space for an economic growth stimulus. The drive to increase tax revenues is crucially important as this can create greater fiscal space without detriment to the outlook for fiscal resilience. Developments in recent years show that the tax ratio (tax revenues to GDP) remain relatively unchanged at around 11%, below the levels achieved by other countries

in the region. The tax amnesty program launched by the Government in 2016 could become an initial step in tax reform for achieving this increase in tax revenues.

The second challenge is related to how long the corporate and banking consolidation process can reach completion. This challenge is also influenced by the fiscal capacity to deliver an economic stimulus. Recent developments in the fourth quarter of 2016 point to improved performance in the private sector, and especially in non-construction investment. This is a heartening condition indeed, as it may reflect the onset of improvement in corporate confidence for embarking on business expansion. In the fourth quarter of 2016, indicators pointed to improvement in bank confidence reflected in more robust credit growth. The positive developments among corporate entities and in the banking system are predicted to carry over into 2017 and support national economic recovery.

The third challenge concerns the measures taken to strengthen the effectiveness of monetary policy transmission, which was less than optimal due to the ongoing consolidation process in the banking and corporate sectors. During 2016, the lack of optimum monetary policy transmission was visible in both the interest rate channel and the credit channel. This adverse development was closely tied to the influence of a modest increase in credit risk that acted to restrain credit growth through both supply and demand. Lending rates also did not decline to the same extent as the policy rate.

The effectiveness of monetary policy transmission is expected to improve in 2017 as the corporate and banking consolidation process winds down. On one hand, the banking system is expected to start channelling credit and reduce interest rates in keeping with the trend for monetary policy relaxation previously pursued by Bank Indonesia in 2016. On the other hand, corporate entities are also expected to generate increased demand for credit commensurate with the improved economic outlook.

The final challenge revolves around the risk of higher inflation triggered by price increases for goods in the strategic administered prices category. The risk of increases in administered prices is related to the prospect for sustained growth in global commodity prices, including energy prices. Initially, this inflationary risk may have a direct impact through increases in administered prices category such as for fuels and electricity tariffs. In the subsequent stage, however, attention will be given to dampen the secondary impact of higher inflation in administered prices, as this could spread to volatile food and core inflation.

In the medium to long term, these challenges relate to the drive for reinforcement of the economic structure particularly in the real and financial sectors. The structural challenges in the real sector are related to diversification of export products so that they will complement the role of resource-based exports. The challenges in the real sector are also linked to the motivation to expand the manufacturing role in the economy and to strengthen market and trading structures in support of greater efficiency. The challenges in the financial sector are about efforts to bolster domestic financing structures for greater diversity, improve the funding structure of the banking system for greater equilibrium, and to deepen financial markets so that they will have greater capacity to support financing for the economy and strengthen monetary policy effectiveness.

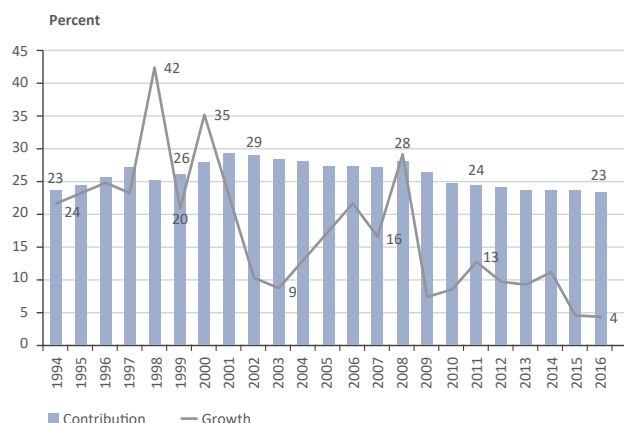
The structural challenges for greater export diversification in the real sector are also influenced by the need for further strengthening of the current real sector conditions. In this regard, the majority of exports still consist of resource-based products and this composition needs to be diversified in favor of high-value manufactured products. Export data shows a growing concentration of exports in resource-based products occurred since 2004 (Chart 15.1). The second challenge in the real sector is related to more rapid strengthening of the manufacturing sector role to establish a basis for increasing added value in the economy. The urgency to strengthen strategic industries based on the downward trend of the manufacturing sector contribution to GDP (Chart 15.2). Aside from revamping the composition of exports and strengthening the manufacturing sector, a further challenge in the real sector is related to the efforts to create and promote healthier market competition and trading, including improvements market structures and trading schemes for staple food commodities.

Chart 15.1. Export and Import Goods Diversity



Source: UN Comtrade, calculated

Chart 15.2. Manufacturing Sector Growth and Contribution to GDP



Source: BPS-Statistics Indonesia, calculated

In the financial sector, the challenges are related to efforts to build more robust domestic financing structures for optimum support of financing for the economy. At this point, considerable opportunity remains to expand the role of domestic sources of financing. So far, foreign funds, and in particular short-term inflows of foreign funds, have been sufficient to cover the gap in domestic sources of financing. Although these foreign funds can bridge gaps in financing the economy, the large proportion of short-term foreign funds could give rise to other complexities related to the management of exchange rate and inflation, and may also render the economy more susceptible to turmoil during times of global uncertainty.

The economic structural reform in the financial sector is also related to disparities in the composition of funds and lending in the banking industry. On the funding side, the disparities have resulted from the substantial proportion of short-term funds placed by large depositors. This means that for banks, the cost of funds is high and may not be feasible because of the sensitivity of funding sources to changes in interest rates. An imbalanced composition of funds will in turn cause banks to reduce optimum capacity for extending credit.

A further challenge in the financial sector is also related to the imbalanced composition of financing on the domestic financial market. At this time, financing of economic activity continues to rely heavily on bank credit rather than other sources of financing, such as the stock market and bonds. In addition, the financial market also lacks in depth, due to the limited variety of available market instruments and narrow domestic investor base. This condition runs the risk of triggering increased volatility on the domestic market at a

time of price fluctuations on financial markets, even though the source of the turmoil is not particularly large.

15.2. POLICY DIRECTION IN 2017

In responding to these multifaceted challenges in 2017, it will be important for the direction of macroeconomic policy to be focused on maintenance of macroeconomic and financial system stability for sustaining economic recovery. The policy direction needs to take into account of the various short-term risks and uncertainties that could impair economic stability, and in turn hinder the economic recovery process. The safeguarding of macroeconomic stability is of considerable importance, given that economic stability forms the foundation for promoting economic growth. At the same time, the policy for ensuring sustainable economic growth and actions for strengthening the economic structure in the medium term will also be taken forward.

The direction of macroeconomic policy is also intended to improve the quality of economic growth. To this end, economic growth needs to be directed in support of measures to alleviate poverty and income disparities. Therefore, it is necessary to place an inclusive economic development strategy first and foremost as this can serve as a bridge for efforts to achieve more equitable income distribution, expand access to basic needs, and afford equal opportunity to all members of society to obtain decent employment.

This policy direction will be implemented through policy synergy, bringing together the Government, Bank Indonesia, and the Financial Services Authority (OJK) and executed in a mix of fiscal policy, monetary policy, macroprudential policies, and policies for structural reform. The various policies in place are not only aimed at mitigating short-term cyclical risks, but also at sustaining the momentum for economic recovery. This synergy will also be directed towards continued structural reinforcement of the economy for greater resilience and competitiveness.

Bank Indonesia Policy Direction

Bank Indonesia will consistently aim its macroeconomic policy on maintaining economic stability in 2017. Within this context, Bank Indonesia will employ a mix of monetary and macroprudential policies, along with payment system and rupiah currency management policies. Monetary policy will focus on maintaining macroeconomic stability and will be synergized with macroprudential policies aimed

at safeguarding financial system stability. Meanwhile, payment system and rupiah currency management policies will aim to improve transaction efficiency within the economy that in turn will support the operation of monetary and macroprudential policy transmission. The various policies that have been pursued up until 2016 and going forward are part of Bank Indonesia's transformation process that was launched in 2014.

Regarding monetary policy, Bank Indonesia consistently pursues a policy of managing inflation in line with the target and maintaining the current account deficit at a prudent level. In line with this monetary policy direction, the policy rate will be managed for curbing inflation within its target. The monetary policy stance will also be reinforced by an exchange rate policy aimed at maintaining stability in the rupiah according to its fundamental value. Exchange rate policy will also be supported by management of domestic forex supply and demand, as well as promoting the deepening of the forex market. Furthermore, Bank Indonesia also strengthens bilateral cooperation, particularly with other countries in the region, in order to reduce dependency on the US dollar. The aim of the bilateral cooperation is to promote local currency settlement on domestic financial markets in international trade and investment transactions.

The monetary policy direction will be reinforced by the operational strategy of monetary policy. First, Bank Indonesia will implement the Averaging Reserve Requirement in mid-2017. The aim of the Averaging Reserve Requirement policy is to provide flexibility to banks in managing liquidity more efficient that in turn will strengthen monetary policy transmission. Second, Bank Indonesia will optimize the use of government securities as monetary policy instruments in a phased replacement of Bank Indonesia Certificates (SBIs). The objectives of this strategy are to promote financial market deepening and implement the mandates of the Bank Indonesia Act and the State Treasury Act. Third, Bank Indonesia will reintroduce the Variable Rate Tender mechanism in monetary operations, replacing the Fixed Rate Tender mechanism.

Bank Indonesia also pursues several initiatives to accelerate financial market deepening. Under this policy direction, Bank Indonesia will continue working for development and expansion of the financial market under an ecosystem approach. This development and expansion will be conducted with the seven pillars of instruments, users/providers of funds, intermediation institutions, infrastructure, regulatory framework, the benchmark rate, and coordination/education. To support this initiative, Bank Indonesia continues to forge closer coordination with

the relevant authorities in accelerating financial market deepening.

Macroprudential policies will remain focused on maintaining financial system stability to lower systemic risk, while continuing to create space for boosting economic recovery. Furthermore, macroprudential policies will target the mitigation of accumulated risk arising from procyclical behaviour and systemic risks in the financial system. In this regard, Bank Indonesia will strengthen and expand the scope of macroprudential surveillance of households, corporations, and non-financial corporate groups. Monitoring of risks outside the banking system has taken on greater importance in line with advancements in financial technology (fintech). Bank Indonesia continues to study in depth the potential and risks of fintech as input for assessment of macroprudential policies.

Bank Indonesia will make further improvements for more robust macroprudential assessments under a national and regional balance sheet approach to strengthen the assessment of systemic risk and identification of imbalances in the financial system. This approach is expected to provide more robust risk measurement in each element and the interconnection risks among the different elements of the financial system and to strengthen mapping of vulnerabilities and sources of disruption to regional financial systems.

Bank Indonesia will also support the accelerated development of the sharia-compliant economy and finance as a complement to conventional finance. To this end, Bank Indonesia will prepare and launch a blue-print for development of the sharia-compliant economy and finance covering both the commercial side and Islamic social finance. To support the deepening of the sharia-compliant financial market, Bank Indonesia will promote sharia money market instruments by using Sharia Government Securities as underlying transactions and implementing the Waqaf-linked Sukuk bonds. In regard to sharia social finance, Bank Indonesia promotes various efforts to expand the role of zakat (obligatory contribution) and waqaf (endowment) and move forward with initiatives for establishment of a regulatory standardisation institution and policy formulation at the international level.

Bank Indonesia also devotes attention to the development of Micro, Small, and Medium Enterprises (MSMEs). To maintain control over volatile food prices, Bank Indonesia will promote the expansion and development of inflation control clusters based on MSMEs in a downstream development approach. These inflation control clusters will also become one of the instruments at the disposal of the

Regional Inflation Control Teams (TPIDs). In addition, Bank Indonesia will carry forward the program for expansion and deepening of MSME infrastructure credit to mitigate the obstacle of asymmetric information that has resulted from the gap between the capacity of MSMEs and bank financing. Bank Indonesia will boost the implementation of programs for creation of new economic activities in the regions and in rural areas through development of prime MSMEs under a Local Economic Development (LED) approach.

Regarding the payment system, policy will be carried out through actions designed to reinforce institutional components and the infrastructure of the domestic payment system and to promote financial inclusion. Implementation of the policy direction will build on the mission for creating a secure, efficient, smoothly operating, and reliable payment system with consideration for expansion of access and consumer protection in support of monetary and financial system stability.

Bank Indonesia will pursue several initiatives within the context of building stronger institutions and infrastructure in the payment system. First is to implement the rules on Payment Transaction Processing (PTP) which apply to all payment system service providers, including fintech operators. Second, Bank Indonesia ensures the effectiveness and productiveness of the Fintech Office established on 14 November 2016 and the regulatory sandbox function in order to promote the sound development of fintech. Third, Bank Indonesia will accelerate the formation of an agency to operate the management functions for the National Standard of Indonesian Chip Card Specification (NSICCS), targeted to be established by 30 June 2017. Fourth, Bank Indonesia will accelerate the National Payment Gateway (NPG). Fifth, Bank Indonesia requires payment system service providers to conduct the processing of financial transactions inside Indonesia, hold data within Indonesia, keep funds in the national banking system, use central bank money, and comply with mandatory use of the rupiah within the territory of the Republic of Indonesia.

In regard to the efforts to support financial inclusion, Bank Indonesia will take further actions to expand financial access and improve efficiency by integrating the electronic non-cash ecosystem into Government programs and public services. The policy strategy will be directed towards expansion of the Government to People scheme, which consists of non-cash social assistance distributed through a Digital Financial Services (DFS) agency system, and development of People to Government, namely a smart city program that includes payment of official user charges and for public services used by members of the public.

On rupiah currency management, Bank Indonesia will promote the clean money policy by extending coverage to remote and outermost regions under a master plan set out in the Centralized Cash Network Plan (CCNP). For this purpose, Bank Indonesia initiates the issuance of the new rupiah emission simultaneously in all denominations.

The various policy directions to be pursued by Bank Indonesia will always be in coordination with the Government and various other stakeholders at the national and sub-national levels. The coordination that has been managed well so far will be improved further in various media for coordination, including the Round Table Policy Dialogue (RTPD), Bank Indonesia - National/Regional Government Coordination Meetings, the Inflation Monitoring and Control Team (TPI), the Regional Inflation Control Teams (TPIDs), the Financial System Stability Committee (FSSK), and the Indonesia Payment System Forum (FSPI). Bank Indonesia will also continue to forge closer coordination for financial market deepening in the Coordinating Forum for Development Financing on the Capital Market (FK-PPPK), the Indonesia Foreign Exchange Market Committee (IFEMC), and the Association Cambiste Internationale (ACI).

As for coordination in the area of financial system stability, the coordination with the Financial Services Authority (OJK) within the context of implementing the Act concerning Financial System Crisis Prevention and Resolution will focus on determination of Systemically Important Banks (SIBs) and the coordinating mechanism for provision of short-term liquidity loans. Meanwhile, coordination with the Indonesia Deposit Insurance Corporation (IDIC) will focus on resolving problems with bank solvency related to the sale of IDIC-held government securities to Bank Indonesia.

At the international level, Bank Indonesia will bolster coordination with the Government to secure the national interest, while expanding Indonesia's role in the international community. Bank Indonesia continues to actively voicing out the importance of synergy for promoting growth and recovery in the global economy, and for strengthening the resilience of the economy and financial system, in the global as well as the regional forums. In an attempt to maintaining favorable market sentiments, Bank Indonesia continues to support Government efforts to ensure the creation of positive perceptions of the Indonesian economy. In that regard, Bank Indonesia will strengthen the role of the Investor Relations Unit (IRU) and coordinate more closely with the Central Government, sub-national governments, and overseas government representatives to ensure the effectiveness of these measures.

As an attempt to expand Indonesia's role at the international level, Bank Indonesia will work in synergy with the Government for successful hosting of the Annual Meetings of the International Monetary Fund (IMF) and World Bank (WB), which will be held in Bali in 2018. The Annual Meetings of the IMF and WB are yearly events attended by governors and officials of central banks, ministers and officials of ministries of finance and development, the private sector, investors, and academics to discuss the key issues of the global economy. With financial sector authorities and practitioners attending from the 189 member countries of the IMF and WB, Indonesia will play a crucial role as the host of the Annual Meetings. First, the estimated number of participants in this series is around 15,000 persons from various countries worldwide. Second, the participants in the meetings are policy makers, corporate leaders and prominent investors, making the event a highly strategic platform for dialogue, promotional activities, and encourage investment decisions. Furthermore, the entire attention of the world economy will be focused on the host country. This will provide opportunity to build positive perceptions of Indonesia and to demonstrate that Indonesia is a safe and hospitable country, with well managed infrastructures and sound macroeconomic stability.

As the host country, Indonesia has prepared a structured and comprehensive working program in preparation for the 2018 Annual IMF and WB Meetings in Bali, which is called "Voyage to Indonesia" (Figure 15.1). The objectives of this program are twofold, namely to successfully organize the IMF-WB 2018 Annual Meeting and to optimize the benefits of such event for Indonesia and the region. The main message to be conveyed is that Indonesia is a reformed, resilient, and progressive nation, which place great importance in the achievement of sustainable and inclusive economic growth.

This program comprises of a wide range of seminar and expo activities aimed at promoting Indonesian economy. Furthermore, the program will also promote the development of sharia-compliant economics and finance as a source of sustainable economic growth, improvements in the investment climate and tourism, and the expanding role of women as a source of economic growth driven by entrepreneurship development and financial access.

Regarding international cooperation, Bank Indonesia consistently participates and supports the Government in fostering collaboration to finance development, including facilitation of international cooperations. This includes the establishment of the Islamic Investment Infrastructure Bank (IIIB) or the World Islamic Investment Bank (WIIB)

Figure 15.1. Framework of Voyage to Indonesia Program



Source: Bank Indonesia

which can be tapped to assist in funding of infrastructure projects in Indonesia. Support for the Government will also be provided in relation to the investment and infrastructure agenda initiatives under G-20 collaboration forum (the Global Infrastructure Connectivity Alliance), which aimed at facilitating connectivity in construction of cross-border infrastructure between the G-20 countries and beyond.

Synergy of Fiscal Policy and Structural Policies

This policy mix of Bank Indonesia will also be synergized with the policies of other institutions, thus bringing together the Government, Bank Indonesia, and the Financial Services Authority (OJK). This policy synergy is aimed to strengthen policy effectiveness in safeguarding macroeconomic and financial system stability and to promote economic recovery.

In the context of synergy with fiscal policy, Bank Indonesia will support a range of Government measures to improve the outlook for fiscal sustainability as part of the undertaking for a more sustainable of economic growth. Bank Indonesia supports Government commitments to maintain the three pillars of fiscal policy reform, namely optimization of state revenues, productive and quality management of state expenditures, and management of financing according to prudential principles.

Regarding the optimization of state revenues, Bank Indonesia supports various efforts for successful tax reforms as a foundation for strengthening the tax revenue structure. The tax amnesty policy launched in 2016 has recorded quite excellent results that can serve as a platform for strengthening performance in taxation to achieve the

tax ratio target of approximately at 13%-14% of GDP in the medium term. In state expenditure management, Bank Indonesia will support Government efforts to improve the quality of state expenditures. These expenditures need to be prioritized and channelled into productive sectors that can generate sizeable multiplier effects on the economy. In this regards, sound expenditure allocations becomes extremely important, namely reallocation of expenditures away from energy subsidies to mandatory activities such as infrastructure development, education, and health. This strategy, in turn, will improve the effectiveness of the fiscal policy role in supporting economic recovery.

In line with the Government fiscal policy commitments, Bank Indonesia will support the strategy under the 2017 State Budget, which focuses on the acceleration of infrastructure development, interregional connectivity, and productive economic activities that can generate sizeable multiplier effects for the economy, while also taking into account the availability of fiscal space and fiscal sustainability in the medium term. The budget target for infrastructure spending in 2017 is targeted at Rp387 trillion, up from Rp225 trillion in the previous year. This increase is attributable to the bump in the share of infrastructure expenditures to total expenditures of 18.6%, larger than the 15.2% share in 2016. Overall, the fiscal policy for 2017 points to a deficit in the 2017 State Budget at 2.4% of GDP (see Table 15.1).

Besides synergy in fiscal policy, Bank Indonesia will also support Government efforts to accelerate and enhance the structural reforms agenda. These structural reform policies are highly important, as they in turn will contribute towards strengthening the resilience and competitiveness of the economy, as well as help the economy to steer clear out of the middle-income trap (see Box 15.1).

In this regard, Bank Indonesia sees at least three policy priorities which require due attention, namely policy for strengthening the resiliency and self-sufficiency of energy, food, and availability of water; policy for strengthening sectoral roles; and policies aimed at accelerating the development of physical and non-physical infrastructure. Some of these policy priorities has already been incorporated into the Economic Policy Packages launched by the Government (see Box 15.2).

The first policy priority pertains to various efforts to improve resilience and self-sufficiency of energy, food, and availability of water. On the energy policy, Bank Indonesia supports Government efforts to refocus its attention toward development of primary energy sources along with new and renewable energy as described in the

national energy framework. On the food self-sufficiency, restructuring the food supply chain and trading schemes along with mitigating issues related to the distribution of staple goods is necessary in the short term. This is crucial to ensure food availability, particularly to prevent shortage when demand soars while production is limited. At the same time, however, it is also necessary to pursue medium to long-term policies aimed to sustain the sufficient level of food supply, namely through modernization of the agriculture sector that will increase productivity. In order to improve agricultural performance in rural areas, supports are directed to developing via cluster programs aimed to support food self-sufficiency. Lastly, to promote environmentally-friendly economic development, policy is directed to improve the provisioning of clean water.

The second policy priority focuses on the key economic sectors, among others are the manufacturing and the maritime sectors. Bank Indonesia supports the government agenda to strengthen upstream industries, such as the basic metals industry and basic chemicals industry, and also policy that supports downstream industries. In term of the utilization of natural resources, policy is aimed to harness the comparative advantage from Indonesia's abundance of natural resources. In this regard, the industrialization policy is to focus on sectors which have the most backward and forward linkages to other sectors. In addition, policy will also be directed toward promoting innovation in creative industries, especially the ones that have the potential to create large numbers of new jobs and generate high value added.

Alongside the policies for industrialization, further strengthening is also needed for policies in the tourism and maritime sectors to obtain optimum benefit from the multifaceted potential of Indonesia's nature. The tourism sector boasts considerable potential for further improvement, granted that this sector can cushion the impact of economic shocks, including the shocks occurring at times of exchange rate turmoil.

In the maritime sector, Bank Indonesia sees enormous potential due to Indonesia's unique position as the largest archipelagic nation in the world. The policy direction for promoting this sector represents a challenge in itself, given that so far, the contribution of the non-oil and gas maritime subsector has been extremely low compared to equivalent contributions in other archipelagic countries (Chart 15.3). The role of the maritime sector is also important considering the contribution of maritime transport services to the deficit in the services and current account. Among various reasons causing the deficit, the two major factors at play

Table 15.1. State Budget (APBN) 2015-2017

Rp trillion

Items	2015		2016			2017
	Revised State Budget (APBN-P)	Realization	State Budget (APBN)	Revised State Budget (APBN-P)	Realization	State Budget (APBN)
A. Total Revenue	1,761.7	1,508.0	1,822.5	1,786.2	1,555.1	1,750.3
Domestic Revenue	1,758.4	1,496.0	1,820.5	1,784.2	1,546.9	1,748.9
1. Tax Revenue	1,489.2	1,240.4	1,546.7	1,539.2	1,285.0	1,498.9
2. Nontax Revenue (PNBP)	269.2	255.6	273.8	245.1	261.9	250.0
i. Natural Resources (SDA) Nontax Revenue	119.0	101.0	124.9	90.5	65.7	87.0
Grants	3.3	12.0	2.0	2.0	8.2	1.4
B. Total Expenditure	1,984.1	1,806.5	2,095.7	2,082.9	1,860.3	2,080.5
I. Central Government Expenditures	1,319.5	1,183.3	1,325.6	1,306.7	1,150.1	1,315.5
Employee Expenditure	2,93.1	281.1	347.5	342.4	305.1	343.3
Goods Expenditure	238.8	233.3	325.0	304.2	259.4	296.6
Capital Expenditure	275.8	215.4	201.6	206.6	166.4	194.3
Debt Interest Payment	155.7	156.0	184.9	191.2	182.8	221.2
Subsidy	212.1	186.0	182.6	177.8	174.2	160.1
Social Assistance	4.6	4.3	4.0	8.5	6.5	2.2
Social Assistance	107.7	97.2	55.3	53.4	49.6	57.0
Others Expenditure	31.7	10.1	24.7	22.5	6.0	41.0
II. Transfer to Regions and Village Funds	664.6	623.1	770.2	776.3	710.3	764.9
1. Transfer to Regions	643.8	602.4	723.3	729.3	663.6	704.9
2. Village Funds	20.8	20.8	47.0	47.0	46.7	60.0
C. Primary Balance	-66.7	-142.5	-88.3	-105.5	-122.5	-109.0
D. Surplus/Deficit	-222.4	-298.5	-273.2	-296.7	-305.2	-330.2
(% GDP)	(1.9)	(2.6)	(2.2)	(2.4)	(2.5)	(2.4)
E. Financing	222.4	323.1	273.2	296.8	331.0	330.2
Unspent/(deficiency) of Budget Financing (SiLPA)		24.6			25.8	

Source: Ministry of Finance

are insufficient port infrastructures slow progress in the development of large scale ship building industries.

Considering the vastness potential of the Indonesia's maritime sector, Bank Indonesia supports Government actions for integrating the shipyard industry and seaport developments. The positive developments of the shipyard industry will generate huge multiplier effects for the economy, beginning with the steel industry that supplies raw material for ship engines and equipment, then the fishing and trawling industries, tourism industry particularly cruise services, and sea transportation industry. The strengthening of the maritime sector will have a compounded value added benefit if the development of shipyard industry and port infrastructure can be integrated into an ecosystem of interconnected economic zones.

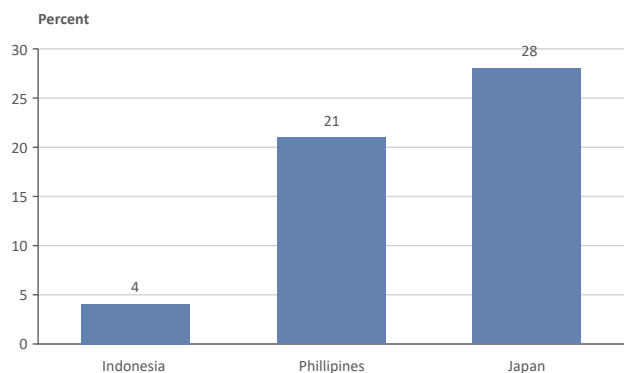
Apart from this sectoral aspect, the industrialization policy also needed to be coupled with efforts for continued development of the digital economy. Indonesia has vast potential as a digital market due to the steady rise in internet penetration. It accounts for 40.5% of the entire

digital market of South East Asia.¹ Furthermore, growth in online trading has reached of 50%. In this regard, Indonesia can be a special market niche for internet-based startups.² Bank Indonesia supports the Government strategy to bolster expansion in start-ups, such as one thousand start-up program and regulations pertaining to funding for start-up companies listed in the e-commerce roadmap.

The third policy priority is to accelerate the development of infrastructure, which include both physical and non-physical infrastructure. Regarding physical infrastructure, Bank Indonesia is providing steadfast support for government work on projects such as toll road, railway construction and revitalization of seaports. Bank Indonesia supports

1 In Indonesia, online sales are climbing by 40% each year (Ernst & Young). Internet penetration has steadily increased in Indonesia and has now reached about 40%, representing 104 million internet users. Online sales were projected to reach USD18 million by the end of 2016 (Association of Indonesian Internet Providers/ APJII).

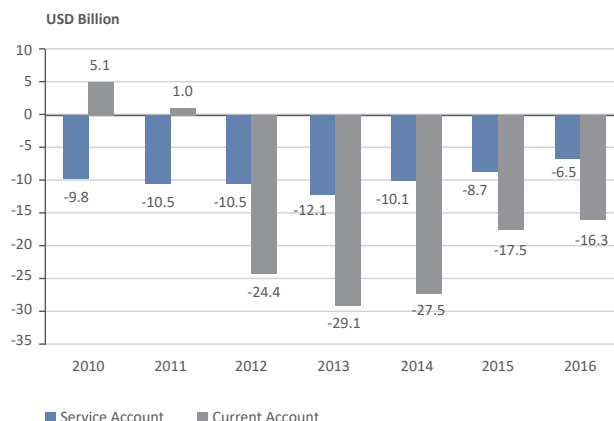
2 A survey conducted by Google Inc. and Temasek Holdings Pte Ltd measured the potential for digital markets in South East Asia and estimated a market opportunity worth USD200 million until 2025 and that about 40.5% or USD80 million originates primarily from Indonesia, a country dominated by e-commerce.

Chart 15.3. Maritime Sector Contribution to GDP

Source: CEIC, calculated

the accelerated construction of power plants due to their vital role in the industrialization process. Bank Indonesia also supports the construction of infrastructure which strengthen food and energy resilience as well as clean water provision, such as water treatment systems at various strategic location.

Serious attention is also required on the development of non-physical infrastructure. There are several key aspects which need to be considered, namely the commitment to continuously improve on the quality of capital, particularly human capital, innovation and technology, as well as sound institutions. Regarding the institutional framework, commitments must be further strengthened to combat corruption and improvement of legal certainty in Indonesia.

Chart 15.4. Service Account Deficit and Current Account Deficit

Source: Bank Indonesia

Bank Indonesia firmly believe that the Government is committed to make steady improvements to the institutional framework which not only will improve the ease of doing business in Indonesia going forward, but will also make the economy more competitive.

Bank Indonesia is confident that increasingly solid policy synergy can be attained if the various economic policies currently present can be harmonised and are supported by regional governments. In this regard, improvement in the economy on a national scale can be achieved if each regional government is able to use the regional balancing fund more effective and efficient. When the economy need a stimulus, the use of Regional Government funds can take up the slack in areas yet utilized by the central Government.

Box 15.1. Middle-Income Trap

As it entered the 21st century, Indonesia had a promising prospect and opportunities. In 2004, Indonesia joined a new class of economies, namely the middle-income countries.¹ This was a moment that brought hopes and simultaneously provided opportunity to move up in the ranks towards a high-income country. Aside from this, Indonesia also entered the period of the demographic bonus (2010-2030) where the dependency ratio is low (Chart 1). The demographics bonus points to opportunity to generate higher economic growth. However, this would not be an easy journey. Various efforts would be required to boost workers' productivity through education. Without these measures, the country would be hard pressed to avoid the middle income trap.

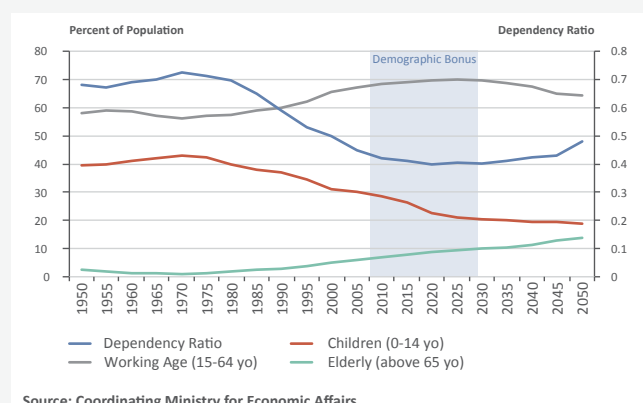
Indonesia's economic growth has been driven to a large extent by manufacturing, but since 2009, the manufacturing growth has maintained a declining trend. Similarly, the proportion of the manufacturing contribution has been steadily shrinking (mainly since 2015) and is far below that of other countries, such as China and South Korea. Indonesia's manufacturing decline is also reflected in the national export profile. The contribution of manufactured goods to exports has steadily diminished, substituted by resource-based export commodities, particularly in comparison to the period before the early 2000s. Indonesia's manufactured export performance is depicted in the Trade Specialization Index which measures the penetration of Asian products on world markets and is used to measure the competitiveness of Indonesia's manufactured products. Since 2001, this index has

maintained steady decline and is in fact the lowest in the ASEAN region (Chart 2).

The issue facing manufacturing in Indonesia is a structural one, where growth in consumption sector has not been matched by growth in production sectors. High-income earners in population are growing at the rate of 5.9%, far higher compared to population in the middle and low-income brackets with growth is only at 1.3%. The transformation of Indonesia's consumers on the Growth Incidence Curve (GIC) to a population with complex lifestyle resembling those of the high-income countries, which is also reflected in lifestyles and high demand for digital technology and other luxury goods (Figure 1).² However, the transformation of Indonesia's consumers has not been matched by transformation in the industry sector, which remains dependent on low-tech industry. This condition is illustrative of a structural imbalance.

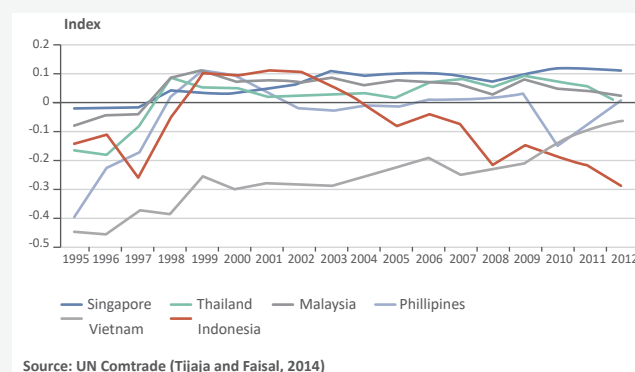
In the longer term, the structural imbalance will have more serious consequences with the risk that the Indonesian economy in a middle-income trap. Simulations with economic growth at 5% per annum will only bring Indonesia to a GDP per capita of USD7,152 (2030).³ Indonesia must maintain a minimum growth rate of 6% per annum to join the ranks of high-income countries, for which the lower limit of GDP per capita is USD12,616. This calls for sustained efforts to bring about high and sustainable economic growth, which will pave the way for achieving the hopes of reaching the level of a high-income country.

Chart 1. Demographic Bonus



1 Indonesia's per capita GDP reached USD1,080 in 2014, placing it between the lower limit of the middle-income countries (USD1,036) and the lower limit of high-income countries (USD12,616) according to classification by the World Bank.

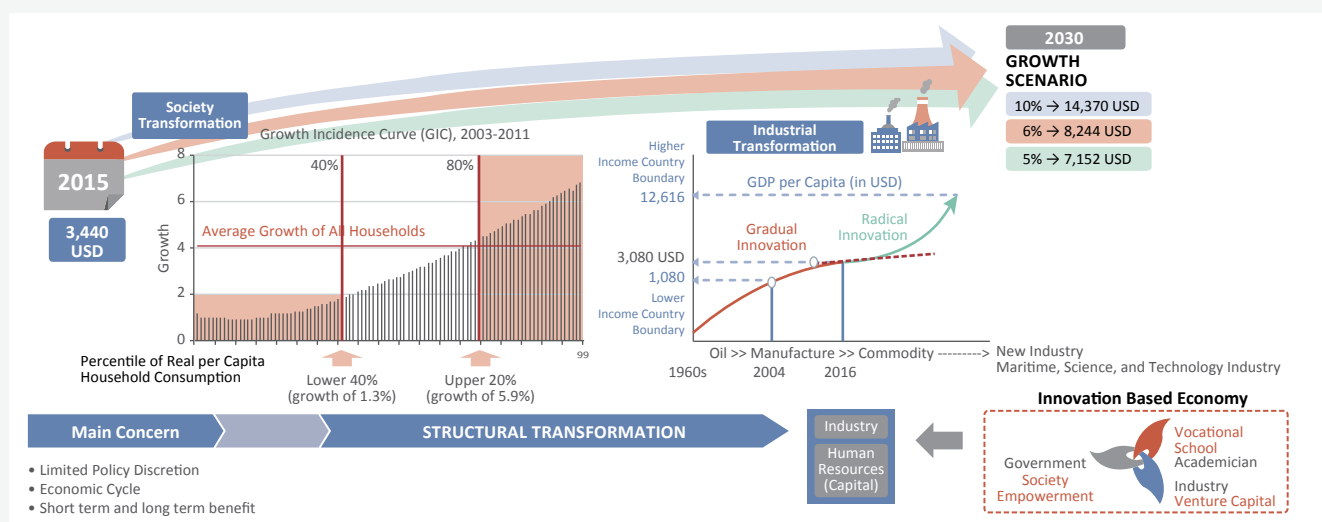
Chart 2. Trade Specialization Index - Manufactured Product



2 The GIC indicates the annual growth rate in consumption between two periods for each percentile of distribution. Accordingly, the GIC portrays how average growth in consumption is distributed across all household distributions.

3 Simulations with growth rates of 5% per annum, 6% per annum, and 10% per annum with GDP per capita in 2015 at USD3,440 per annum.

Figure 1. Structural Reform Framework



Strategy to Achieve High Growth

Eichengreen, Park, and Shin (2013) state that the key to a nation's success in avoiding the middle-income trap is to boost exports of high technology products and raise the quality of its human resources. These two actions will lead to strengthening of the industry sector, where improvement to the level of medium or high technology-based industry is a prerequisite for producing medium or high technology products. The development of a robust industrial base requires quality human resources, large investments, and high technology accompanied by innovations.

Human resources development through improved quality of education or extra schooling years can spur higher economic growth (Mankiw, Romer, and Weil, 1992). Improvements to education will strengthen the skills of the workforce, which in turn will bring higher productivity. The government has pursued various measures for the advancement of education, including measures designed to promote the establishment of vocational schools. It is important not only to boost education in terms of quantity, but also to raise the quality of education.⁴ Studies in Indonesia have discovered a positive correlation between quality of education and economic growth.⁵ Human resources development will not only contribute towards building a more robust industrial

sector, but can also alleviate poverty. Such condition subsequently can achieve the inclusive economic growth.

A Growth Diagnostic study (Bank Indonesia, 2016) found that among the primary obstacles to investment in Indonesia are the lingering inadequacies in energy infrastructure and connectivity infrastructure. The Government is progressing with the development of energy infrastructure, including power plants under the 35,000 MW program, and connectivity infrastructure such as roads, ports, railways, and airports. With more robust infrastructure in place, industry will be able to expand production capacity and lower the costs of transporting raw materials or finished goods, thus becoming productive and efficient. It is expected that these measures will stimulate investor interest, particularly in the industry sector.

In Schumpeter's theory, investment, which is an important part of growth, represents a function of advancements in technology and supply of entrepreneurs.⁶ Furthermore, Schumpeter believed that small-scale companies and industries are more efficient in coming up with innovations. The high proportion of small-scale industry to medium industry, or the missing middle phenomenon, indicates that Indonesia's small-scale industries face difficulty in moving up the ladder to medium-sized industry unless they are able to bring new innovations to the table. Therefore, attention is needed to a strategy for innovation development alongside a strategy for HR development and investment in order to achieve high, sustainable economic growth.

⁴ Hanushek (2013) emphasises the importance of cognitive skills to economic growth, where in the absence of improvement in the quality of schooling, developing countries will have difficulty in improving their economic performance in the long term.

⁵ Affandi, Anugrah, and Bary, "Pembangunan Sumber Daya Manusia di Indonesia", 2016 (unpublished)

⁶ Joseph Schumpeter (1883-1950) developed a well-known theory about innovation in which creative destruction is a process for implementing new innovations to replace outdated methods.

Box 15.2. Survey of Performance and Effectiveness of Structural Reforms Launched in Economic Policy Packages

The issuance of 14 Economic Policy Packages for accelerating structural reforms sought to accelerate growth in Indonesian economy. The Government, formed a task force to conduct an ongoing evaluation of the implementation of these policy packages to optimize their effectiveness and impact. One of the evaluation methods is a survey directed towards the business community and Regional Governments.¹ The purpose of this survey is to ascertain the level of awareness and the impact of some of the Economic Policy Packages released to date.

Most of the business community and regional governments are well informed about some of these Economic Policy Packages. In the business category, 86% (of the 157 who responded) stated that they knew about the 12 Economic Policy Packages launched by the Government, while 14% had no knowledge of these measures. As for regional government respondents, the vast majority are well informed of these 12 Economic Policy Packages (98.1%).

The survey also found that the contents of all Economic Policy Packages are understood, but with variable percentages. Fewer than 50% of business respondents understand the contents of packages V, VI, VII, and XI (Table 1). Similarly, fewer than 50% of regional government respondents understand the content of packages V, VII, and XI (Table 2). This points to the need for more intensive

Table 1. Business Enterprises Comprehension of Economic Policy Packages

Economic Policy Packages	Objective Comprehension	Substance Comprehension	Relevancy with Business Enterprises
Package I	88.9%	58.5%	74.1%
Package II	79.3%	60%	55.6%
Package III	80%	55.6%	63%
Package IV	77.8%	57.8%	67%
Package V	60.7%	43.7%	32.6%
Package VI	65.2%	43.7%	32.6%
Package VII	68.9%	51.1%	40%
Package VIII	45.9%	31.9%	12.6%
Package IX	78.5%	62.2%	65.2%
Package X	82.2%	60%	57.8%
Package XI	65.9%	45.2%	43%
Package XII	69.6%	51.9%	48.9%

Source: Working Group (POKJA) III Survey Result

1 Survey conducted by Working Group III during July 2016 with a scope covering 25 provinces. Respondents consisted of 157 respondents from the business community and 52 respondents from regional governments.

Table 2. Regional Government Comprehension of Economic Policy Packages

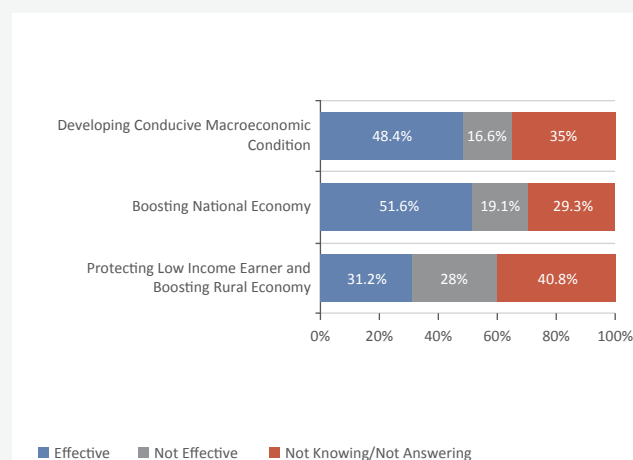
Economic Policy Packages	Objective Comprehension	Substance Comprehension
Package I	96.2%	82.7%
Package II	94.2%	78.8%
Package III	90.4%	65.4%
Package IV	80.8%	53.8%
Package V	65.4%	36.5%
Package VI	84.6%	59.6%
Package VII	84.6%	67.3%
Package VIII	61.5%	30.8%
Package IX	90.4%	73.1%
Package X	92.3%	82.7%
Package XI	73.1%	44.2%
Package XII	78.8%	53.8%

Source: Working Group (POKJA) III Survey Result

dissemination of information to improve understanding of these policy packages.

Business confidence in the effectiveness of the Economic Policy Packages remains limited. Among respondents, 48.4% believe that the Economic Policy Packages will be effective for the first objective of supporting a sound macroeconomic condition while 51.2% consider that the Economic Policy Packages will be effective for second objective of stimulating the national economy (Chart 1). However, only 31.2% of respondents are confident that the Economic Policy Packages will work effectively for the third objective of protecting low-income earners and stimulating

Chart 1. Business Enterprises Confidence Regarding Economic Policy Packages Effectiveness



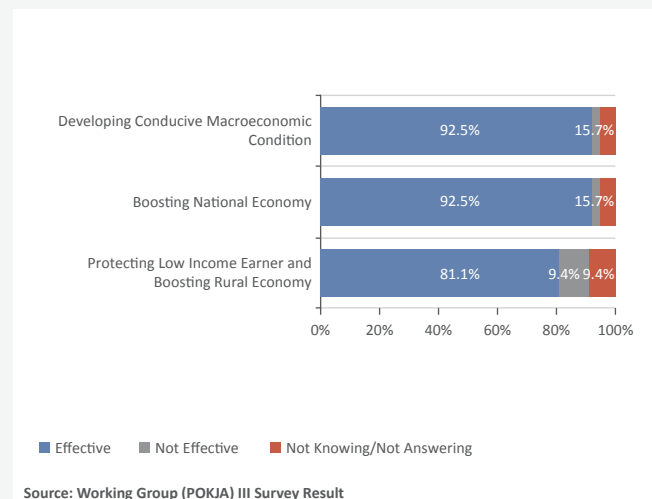
Source: Working Group (POKJA) III Survey Result

activity in the rural economy. As for regional governments, almost all respondents believed that the Economic Policy Packages will be effective for achieving all three objectives. This is reflected from the percentages of respondents who feel confident about the first, second, and third objectives, respectively recorded at 92.5%, 82.5%, and 81.1% (Chart 2).

The survey was also conducted to measure the perceptions about the effectiveness of some Economic Policy Packages released to date. The survey was taken by 300 corporate respondents, mostly from the manufacturing sector. Out of the 41 regulations related to the Policy Packages, the one most familiar to the business community is the Regulation concerning Wages (91.3%), followed by provisions about Revaluation of Fixed Assets for Taxation Purposes (81%) and determination of adjustments to electricity billing rates. Other regulations, however, are not so widely known in the business community (fewer than 50% of respondents), namely the regulation on Construction and Expansion of Domestic Oil Refineries (39.7%), Procedures for Issuance of Special Licences for Mining of Minerals and Coal (41.3%), and Export-Oriented People's Business Credit (45.3%).

The business community viewed that the most relevant and useful regulations govern aspects of business certainty, production or sales, costs of production, investment, and competitiveness. There are 15 regulations which meet these criteria (Table 3). However, a small minority of respondents (about 1%-3%) still held the perception that the regulations on Building Construction Permit (IMBs) for

Chart 2. Regional Government Confidence Regarding Economic Policy Packages Effectiveness



Buildings, Determination of Nuisance Permits in Regions, and Wage Levels have a negative effect on business activity due to unharmonious regulations between the central government and the sub-national regulations, as well as due to financially burdensome wage regulations.

The survey also identified regulations which yield the most positive impact on business. These business activities are grouped into seven main category, namely: (i) production/sales; (ii) production costs; (iii) investment; (iv) labor; (v) financial conditions; (vi) certainty of business, and (vii) competitiveness.



CHAPTER 16

Economic Outlook

Indonesia economic outlook is expected to continue improving, supported by stronger global and domestic economic momentum. In 2017, economic growth is projected to reach in range of 5.0% and 5.4%, accompanied by inflation within $4\pm 1\%$ target. The favorable domestic economic outlook is predicted to persist in the medium term on the various structural reform measures taken to boost economic growth, while maintaining low and manageable inflation together with a sound current account deficit.

Image caption:

Like a boat in the middle of a vast ocean, the Indonesian economy will always be faced with waves of challenge and uncertainty. Nevertheless, perseverance and consistency will bring the boat to the island of its destination.

The Indonesian economy is forecasted to continue gaining traction in 2017, influenced by the promising global and domestic economic outlook. Globally, economic growth is expected to improve on that achieved in 2016 and, thus, potentially contribute to rising global energy and non-energy prices. In the domestic economy, the promising outlook is supported by fewer internal consolidation in the corporate and banking sectors. The corporate sector is expected to continue the nascent business expansion that began in the fourth quarter of 2016, fuelled by corporate confidence on a rebound in commodity prices. In line with the upbeat performance in corporate sector, the banking industry is also expected to increase lending as credit risks wind down. In addition, fiscal policy in 2017 will also be directed to stimulate the economy, particularly through priority spendings and those sectors with a larger multiplier effect on growth.

Applying those assumptions, Indonesia's economy in 2017 will be marked by improved economic growth and maintained economic stability. Indonesian economic growth in 2017 is projected to surge within the range of 5.0% to 5.4%, primarily bolstered by stronger domestic demand particularly from consumption and investment, as well as an upswing in export performance. Meanwhile, inflation in 2017 is predicted to remain within the target corridor of $4\pm 1\%$, albeit accelerating somewhat higher than that of the previous year. Maintained economic stability shall be accompanied by a sound current account deficit at a level below 2.5% of GDP. The prospect of higher economic growth, lower credit risk, and potentially lower lending rates could edge up credit growth in the range of 10% to 12 % and, subsequently, feed through to stronger deposit growth, which is projected to reach 9% to 11%.

The prospect of stronger economic growth is expected to persist in the medium term due to the downward inflation trend and healthy current account deficit. The medium-long-term economic projection is further supported by the positive impact of various structural reforms to boost economic efficiency and productivity, which, in turn, will drive economic growth without triggering excessive pressures on both, inflation or the current account deficit. Inflation is projected to remain inside the target range of $3\pm 1\%$ in 2021, while the current account deficit should remain sound at a level below 2.5% of GDP.

16.1. SHORT-TERM ECONOMIC OUTLOOK

Global Economic Outlook

The global economy is predicted to gain traction in 2017, accelerating from 3.1% to 3.4%, as developing and advanced countries project an uptick in GDP growth (Table 16.1). Economic recovery in developing countries will be driven by stronger growth in net exporter countries of energy and also non-energy commodities. On the other hand, growth in advanced countries will primarily originate from the United States, in contrast to a relatively weaker growth in Europe and Japan. The muted growth prospect in Europe is primarily blamed on geopolitical risks and Brexit fallout, while Japan remains plagued by an aging population that continues to eschew consumption.

Expected US economic gains should contribute to stronger global growth in 2017. Increasingly solid domestic demand, in terms of both household consumption and investment, will boost US growth. Household consumption is expected to increase as labor market conditions improve, reflected by an unemployment rate close to the Non-Accelerating Inflation Rate of Unemployment (NAIRU) of 4.8%, while both labor participation and wages increase. Meanwhile, planned US fiscal expansion is expected to stimulate investment through the various government-led infrastructure projects announced during the presidential election campaign of Donald Trump.

The US economic outlook will be marked by the Fed's response to normalise monetary policy. In line with

Table 16.1. Realization and Outlook of Global Economy

	2015	2016	2017 ^(p)
World	3.2	3.1	3.4
Developed Countries	2.1	1.6	1.9
Japan	1.2	1.0	0.8
USA	2.6	1.6	2.3
Euro Zone	2.0	1.6	1.6
France	1.3	1.2	1.3
Germany	1.5	1.9	1.5
Italy	0.7	0.9	0.7
Spain	3.2	3.2	2.3
Emerging Countries	4.0	4.1	4.5
China	6.9	6.7	6.5
India	7.2*	7.3*	7.2

*Estimates are standardized based on available data from January to December 2016.

Based on fiscal year from March 2015 to March 2016, the Indian GDP for 2015 is recorded at 7.5%.

^(p) Projection

Source: WEO IMF January 2017, calculated

monetary policy normalization, the Fed is expected to raise the Federal Funds Rate (FFR) in 2017, anticipating the inflationary pressures and an excessive spike in wages due to the sharp drop in unemployment. The Fed's policy response could become more aggressive if inflationary pressures intensify due to the expansive fiscal policy of the US Administration under the leadership of President Trump.

China's economy remains beset by consolidation. Growth is therefore expected to moderate slightly in 2017. Nonetheless, deeper consolidation has been avoided due to persistently strong investment, particularly in large-scale government infrastructure projects and through increased foreign direct investment (FDI). FDI is expected to surge after the implementation of policy to relax regulations on foreign investment. Nonetheless, persistently large risks in the financial sector due to overleverage demand vigilance, since it potentially harms China's economic outlook.

In general, the more promising global economic outlook is expected to raise energy and non-energy commodity prices. The upward energy and non-energy commodity price trends in the latter half of 2016 are expected to persist after an agreement to cut production at the beginning of 2017 by OPEC and non-OPEC members. Such agreement will create conditions of net demand on the oil market expected in the third quarter of 2017 and, ultimately, elevate the oil price. Meanwhile, rising non-energy commodity prices will be driven by metals and coal. Metal prices will rise on strong demand from China to develop infrastructure in China and the US. Coal prices are also set to rebound on growing demand from China and supply disruptions.

Domestic Economic Outlook

Economic Growth Outlook

The favorable global economic outlook, coupled with a rebound on commodity prices, will contribute to domestic economic growth in 2017. Furthermore, growth in 2017 will be driven by stronger corporate confidence in the real and financial sectors. Economic growth projection in 2017 is set at a range from 5.0% to 5.4%, supported by solid domestic demand and improving export prospects (Table 16.2). The prospect of strong domestic demand is based on increasing consumption and investment, while export performance will improve on the favorable impact of global economic momentum and rising international commodity prices.

Solid private consumption in 2017, which is a combination of Households and Nonprofit Institutions Serving Households (NPISH) spendings, is expected within the range of 4.9%

Table 16.2. GDP Outlook by Expenditure

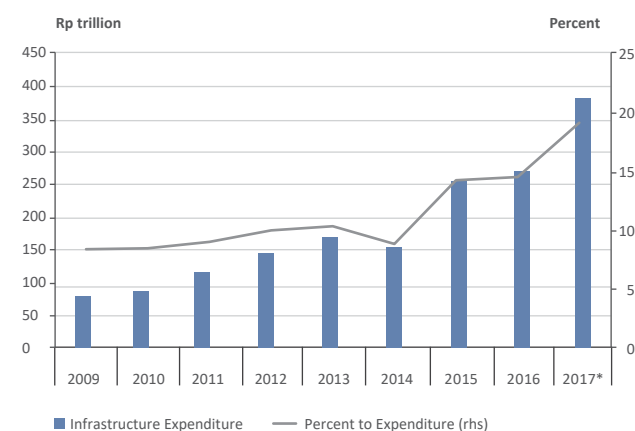
GDP Component	Percent, yoy	
	Realization 2016	Outlook 2017
Household Consumption	5.0	4.9 - 5.3
Government Expenditure	- 0.2	1.7 - 2.1
Gross Fixed Capital Formation	4.5	5.8 - 6.2
Goods and Services Export	-1.7	3.3 - 3.7
Goods and Services Import	-2.3	2.2 - 2.6
Gross Domestic Product	5.0	5.0 - 5.4

Source : BPS-Statistics Indonesia and Bank Indonesia, calculated

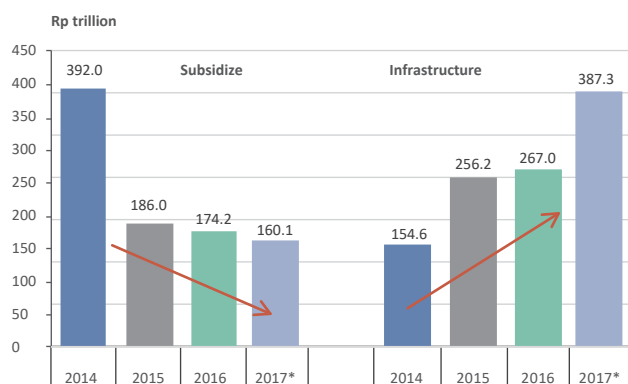
to 5.3%. A manageable inflation will bolster household purchasing power, underpinned the outlook for private consumption. Furthermore, the second-round effect of government expenditure, including infrastructure spending, is also expected to indirectly support higher incomes. The rise in household income is also indirectly influenced by a rebound on international commodity prices. Such rebound will raise export proceeds and subsequently drive household consumption.

Investment growth is also expected to surge in the range of 5.8% and 6.2% on the government's planned infrastructure projects, thus supporting construction investment. The government's plans are reflected in the budget allocation for infrastructure spending, which increased in 2017 (Chart 16.1). The larger allocation for infrastructure expenditure is also inextricably linked to the positive impact of subsidy reallocation policy to spending on productive sectors (Chart 16.2). The promising investment outlook is also propped up by nonbuilding investment. The nonconstruction investment gains recorded in the fourth quarter of 2016, are expected to persist into 2017

Chart 16.1. Government Infrastructure Expenditure



*Budget
Source : Ministry of Finance, calculated

Chart 16.2. Subsidize Expenditure and Infrastructure

*Based on State Budget 2017

Source : Ministry of Finance, calculated

in line with the winding down of internal consolidation in the corporate sector and the rising of global commodity prices. The favorable nonbuilding investment outlook is also the outcome of a number of policies aimed to improve Indonesia's investment climate, primarily through banishing bureaucracy and the introduction of a series of Economic Policy Packages.

Regarding the external sector, export performance is expected to reverse the previous 1.7% contraction in 2016 to post positive growth within a range from 3.3% to 3.7%. Export gains are the result of stronger global economic growth and rising international commodity prices. Furthermore, economic growth in trading partner countries, which is also expected to improve, should have a permanent impact on stronger export growth. On the other hand, however, stronger domestic demand and export gains are expected to edge up imports in 2017 in the range of 2.2% to 2.6%. Based on import categorization, higher imports will stem from capital goods, such as machinery and equipment, in line with the prospect of stronger investment.

By economic sector, domestic demand shall remain the key contributors to economic growth in 2017. Robust expansion is projected in the trade and communication sector, financial sector and construction sector (Table 16.3). The trade and communication sector is expected to continue tracking an upward trend, in the range of 8.7% to 9.1%, in line with the recovery in the manufacturing sector, indicated by a surge of export-import activities. In addition, better quality spendings for infrastructure projects, such as the construction of Terminal 3 of the Soekarno-Hatta Airport and New Tanjung Priok Port, supported an improvement in the construction sector. Meanwhile, the prospects of the communication subsector are predicted to improve in line

Table 16.3. GDP Projection by Industrial Origin

Industrial Origin	Percent, yoy	
	Realization 2016	Outlook 2017
Agriculture	3.3	3.0 - 3.4
Mining	1.1	1.5 - 1.9
Manufacturing	4.3	4.4 - 4.8
Electricity, Gas, Water*	5.3	5.0 - 5.4
Construction	5.2	5.7 - 6.1
Wholesale and Retail Trades, Accommodation, and Food Service Activities**	4.1	4.4 - 4.8
Transport, Storage, Information, and Communication***	8.4	8.7 - 9.1
Financial Service****	7.0	6.3 - 6.7
Other Services Activities*****	4.4	4.7 - 5.1
Gross Domestic Product	5.0	5.0 - 5.4

*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) Accommodation 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

Source : BPS-Statistics Indonesia and Bank Indonesia, calculated

with digital economic advancement through e-commerce and Financial Technology (FinTech).

Improving global economic conditions, including rising global commodity prices, are expected to boost the agricultural and mining sectors, growing respectively in the ranges of 3.0% to 3.4% and 1.5% to 1.9% in 2017. Congruently, the manufacturing sector growth is also predicted to accelerate slightly from 4.4% to 4.8%, supported by stronger domestic demand and the improved investment climate after the Government introduced a series of Economic Policy Packages.

Geographically, the favorable domestic economic outlook is supported by stronger economic growth in a number of regions. Growth in Java is forecasted to range from 5.4% to 5.8%, underpinned by stronger consumption and investments as well as an export surge. Furthermore, consumers' confidence were more upbeat towards the end of 2016, which is expected to linger into 2017. Incomes were expected to maintain through an adjustment to the minimum wage, coupled with local election activity, which drove consumption by Households and Nonprofit Institutions Serving Households (NPISH). Meanwhile, the expected investment gains will still be driven by government infrastructure projects. Externally, optimism surrounding the expected global recovery and planned diversification of export destinations are the salient factors driving export growth.

Economic growth on Sumatra is predicted to reach 4.5% to 5.0%. In terms of spending, increasing household consumption is in line with stronger public purchasing power and investment as the corporate sector rebounds. By sector, sources of economic growth on Sumatra will originate from the agricultural sector, manufacturing sector, and construction sector. Growing demand for agricultural produces and rising commodity prices will improve agricultural sector performance. To some extent, stronger domestic demand and a rebound on commodity prices will also boost manufacturing industry performance. While the construction sector is expected to expand on various infrastructure development projects, including toll roads, dams and preparations for hosting the Asian Games in 2018.

The economic outlook for Kalimantan and Eastern Indonesian Region (KTI) is also expected to improve. Kalimantan will grow as exports pick up on rising commodity prices, including coal, crude palm oil (CPO) and processed minerals. Meanwhile the economy of KTI will be driven by consumption and investment activities. Household consumption should increase as incomes in the primary sector rise, while commitment to accelerate the development of connectivity infrastructure should drive investment.

Inflation Outlook

Headline inflation (CPI) is predicted to remain within the $4\pm 1\%$ target corridor for 2017, despite increasing from the previous year. CPI shall remain below the target range due to relatively stable core inflation, well anchored inflation expectations, manageable exchange rates. In addition, aggregate demand can be relatively met through adequate aggregate supply. Volatile food (VF) inflation is predicted to decelerate slightly due to the fading impact of La Nina, which will help to maintain food security. Moreover, government policy to increase horticultural productivity in order to meet the demand for food through domestic production is also expected to lower VF inflation.

The prospect of higher inflation in 2017 is primarily driven by higher administered prices (AP) that are expected to be higher from the previous period. Meanwhile, AP inflation is influenced by continuing reform of energy subsidies. The prospect of higher global energy prices could push up administered prices (AP), including fuels and electricity rates.

Indonesia Balance of Payments Outlook

Indonesia's balance of payments (BOP) is expected to maintain a surplus in 2017. The BOP surplus is based on the

controlled current account deficit and significant capital and financial account, which is expected to offset the current account deficit. The potential BOP surplus is also predicted to advance the position of FX reserve assets in Indonesia.

The current account deficit is projected to remain at a healthy level of below 2.5% of GDP in 2017. Nevertheless, the current account deficit is expected to widen in 2017 as the larger oil and gas trade deficit outstrips the wider non-oil and gas trade surplus. On one hand, the larger oil and gas trade deficit will be attributable to fewer oil and gas exports as oil and gas lifting is reduced. On the other hand, oil and gas imports will surge to meet domestic demand. In contrast, the non-oil and gas trade balance is expected to record a larger surplus due to potential non-oil and gas export gains on rising commodity prices, although non-oil and gas imports are also expected to increase to fulfill domestic demand.

The capital and financial account is expected to record another surplus in 2017, albeit down slightly on the previous year. An adequate capital and financial account surplus is predicted to offset the current account deficit. Furthermore, the capital and financial account surplus will be influenced by the promising national economic outlook perceived by investors, which will maintain nonresident capital inflows to Indonesia in the form of portfolio investment. Nevertheless, foreign capital inflows will be slightly on conditions recorded in 2016 due to higher uncertainty on global financial markets stemming from the undisclosed fiscal and monetary policy response in the US.

Financial System Stability Outlook

Financial system stability (FSS) is expected to remain sound, supported by stronger banking industry and financial market performance. The prospect of stronger economic growth is expected to bolster banking sector performance. Furthermore, the prospect of stronger economic growth, milder credit risk, and potentially lower lending rates could drive bank lending in 2017, with credit growth is projected in the range of 10% to 12%. Stronger credit growth should also have a multiplier effect on deposit growth, which is projected within the range from 9% to 11%.

The bank intermediation function is also supported by a Capital Adequacy Ratio (CAR) that recorded well above the minimum threshold of 8 percent in the banking industry. Lower credit risk is associated with the promising domestic economic outlook and the prudential principles applied by the banking sector. In addition, the banks are expected to maintain liquidity as repatriated Tax Amnesty funds flow back into the country.

Congruent with the favorable banking sector outlook, bond issuances and Initial Public Offerings (IPO) on the capital market are also expected to increase due to competitive yields on investments in Indonesia compared to average global yields. Economic financing from finance companies is also expected to expand. Institutional investors, such as pension funds, insurance, mutual funds and nonresident investors, are expected to absorb the potential increase of nonbank financing.

16.2. MEDIUM-TERM ECONOMIC OUTLOOK

The promising medium-term economic outlook of Indonesia is expected to endure on the back of lower inflation and a sound current account deficit. Furthermore, the medium-term national economic outlook will also be bolstered by the various ongoing structural reforms to enhance economic efficiency and productivity. The promising medium-term economic outlook will also stem from improvements to inter-regional connectivity, which will expand the production and distribution networks, and also lower production costs. In general, greater efficiency and productivity will, in turn, foster economic growth, without compounding pressures on inflation or the current account deficit.

Medium-term economic growth in Indonesia is expected to track an upward trend, driven by the global economy and potential domestic economic gains. Global economic momentum will not only be propelled by growth in developing countries but also in advanced countries. Notwithstanding, developing countries will continue to function as the main drivers of global growth. Meanwhile, domestic economic potential will rest on the implementation of various structural reforms to enhance economic productivity and, therefore, precipitate sustainable economic growth. Simulations have shown that stronger medium-term economic growth is possible if comprehensive structural reforms can be maximised to prevent Indonesia from becoming embroiled in the middle-income trap.

By component, the medium-term national economic outlook is still supported by household consumption. Solid household consumption will be maintained by an increase in public purchasing power as the emergent middle class continues to expand and inflation is maintained within the medium-term target. In addition, Indonesia is also currently reaping the demographic bonus of a dominant productive age population.

The successful implementation of structural reforms will subsequently nurture economic growth without

exacerbating inflationary pressures. Inflation is predicted to decline within the range of $3\pm 1\%$ by 2021, in line with lower inflation expectations trend due to structural improvements in the economy, combined with closer policy coordination between Bank Indonesia and the Government. The structural improvements include enhanced productivity, improved market structure and trade, as well as advanced distribution and logistics. Such improvements will, in turn, boost economic efficiency and, ultimately, alleviate inflationary pressures.

The current account deficit is expected to remain sound at a level below 2.5% of GDP in 2021 as a result of the positive effect of structural reforms, including infrastructure development, which should increase economic capacity and, therefore, drive highly competitive industries to boost future export performance. Moreover, greater economic productivity should also reduce the dependency of imported goods as the domestic industries begin to successfully produce the substitutes. According to the import-export outlook, the trade surplus is expected to expand. Structural reforms are also expected to benefit capital and financial account performance. The capital and financial account surplus is forecasted to grow as nonresident capital flows are drawn to Indonesia due to the improved investment climate. In general, the current account gains, coupled with the capital and financial account surplus, will expand the overall balance surplus and, ultimately, raise the position of official reserve assets.

16.3. ECONOMIC RISKS AND CHALLENGES

The domestic economic outlook still demands vigilance because of several global and domestic economic risks in the short-medium term that could disrupt the economic prospects. The risk factors are not only related to slow down in the economic growth but also potential pressure on the financial system stability. Economic instability, if left unchecked, could reverse robust economic growth in the short-term as well as medium to long-term.

Globally, there are four salient economic risk factors. First, the global economic recovery and world trade volume (WTV) could undershoot and prices may not rise as expected. Second, international trade policy in advanced countries appears to be consistent with the prevalent protectionist rhetoric and accompanied by populist sentiment. Third, the US macroeconomic policy direction could exacerbate the risk of capital reversal and uncertainty on global financial markets. Fourth, global inflation could increase if world commodity prices, particularly energy prices, continue to climb.

The various global economic risks will challenge Indonesia's economy in terms of maintaining macroeconomic stability and strengthening economic growth. The challenges are linked to four main factors. First, the ability to raise tax revenues as an attempt to expand fiscal space in order to provide a stimulus that will foster economic growth. Second, the ability to expedite the internal consolidation process in the banking and corporate sectors. Third, the ability to strengthen the effectiveness of monetary policy transmission. Finally, the ability to optimise the control mechanism for inflation, which is expected to accelerate. In the medium to long-term, however, the economic challenges stem from efforts to strengthen a more resilient economic structure. The various endeavours will be directed towards strengthening the economy to become more resilient and competitive, thus facilitating more equitable economic growth, while simultaneously preventing Indonesia from falling into the middle-income trap.

