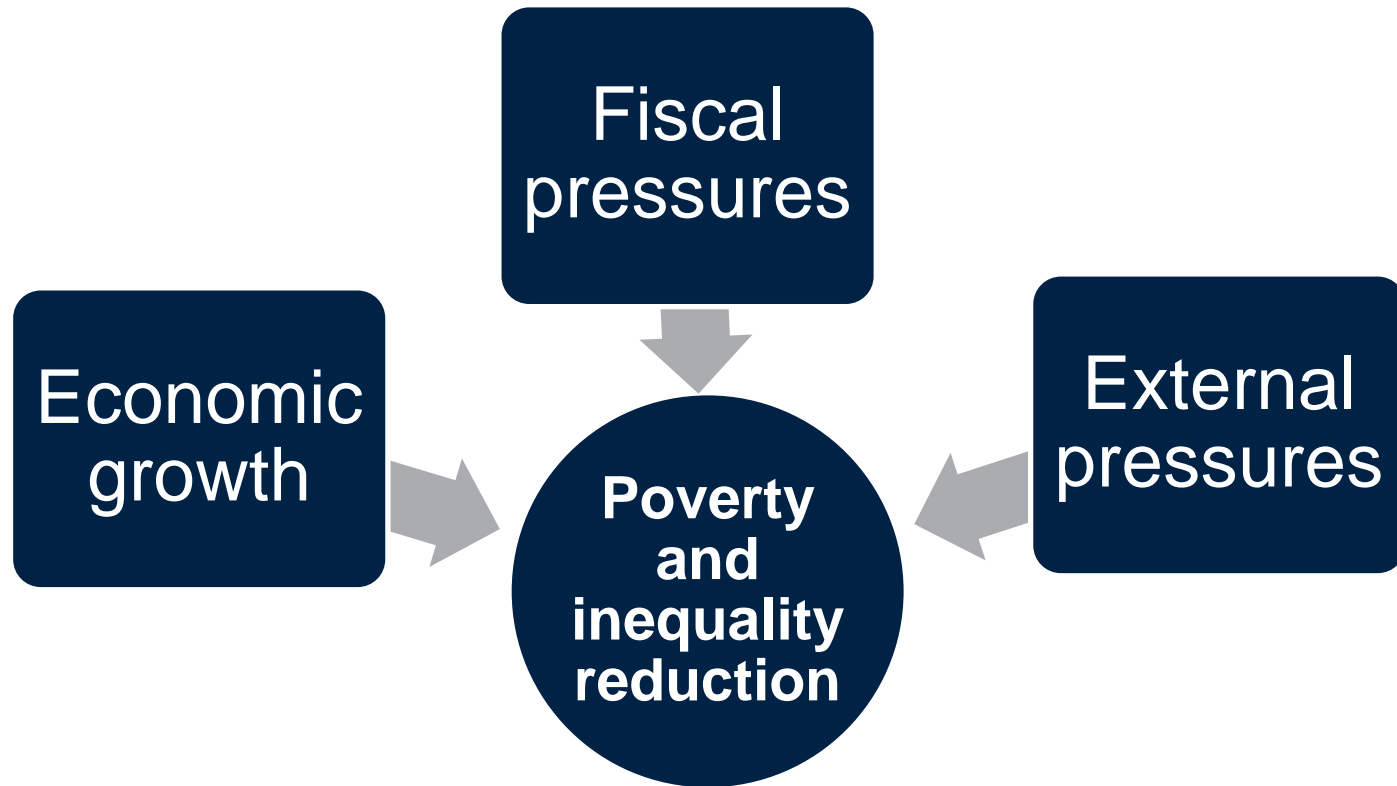


Indonesia Economic Quarterly, July 2014 *Hard choices*

Ndiamé Diop
Lead Economist



The new administration will face major near-term challenges



Ending extreme poverty and achieving shared prosperity?

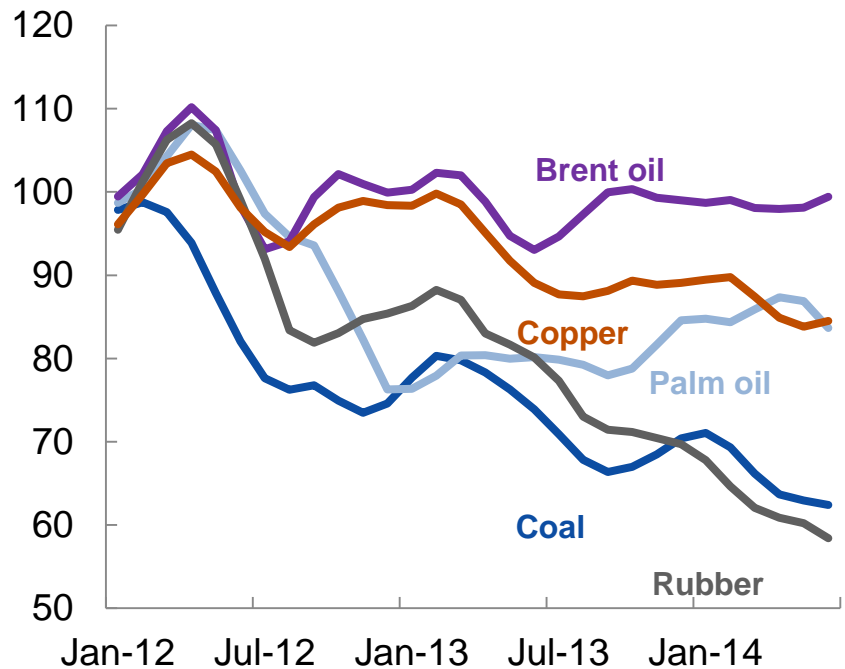
OR

Persistent pockets of extreme poverty and many Indonesians left behind?

International backdrop

High-income economy growth is strengthening...

...but most global commodity prices, except oil, continue to decline
(index, January 2012 = 100, 3mma)

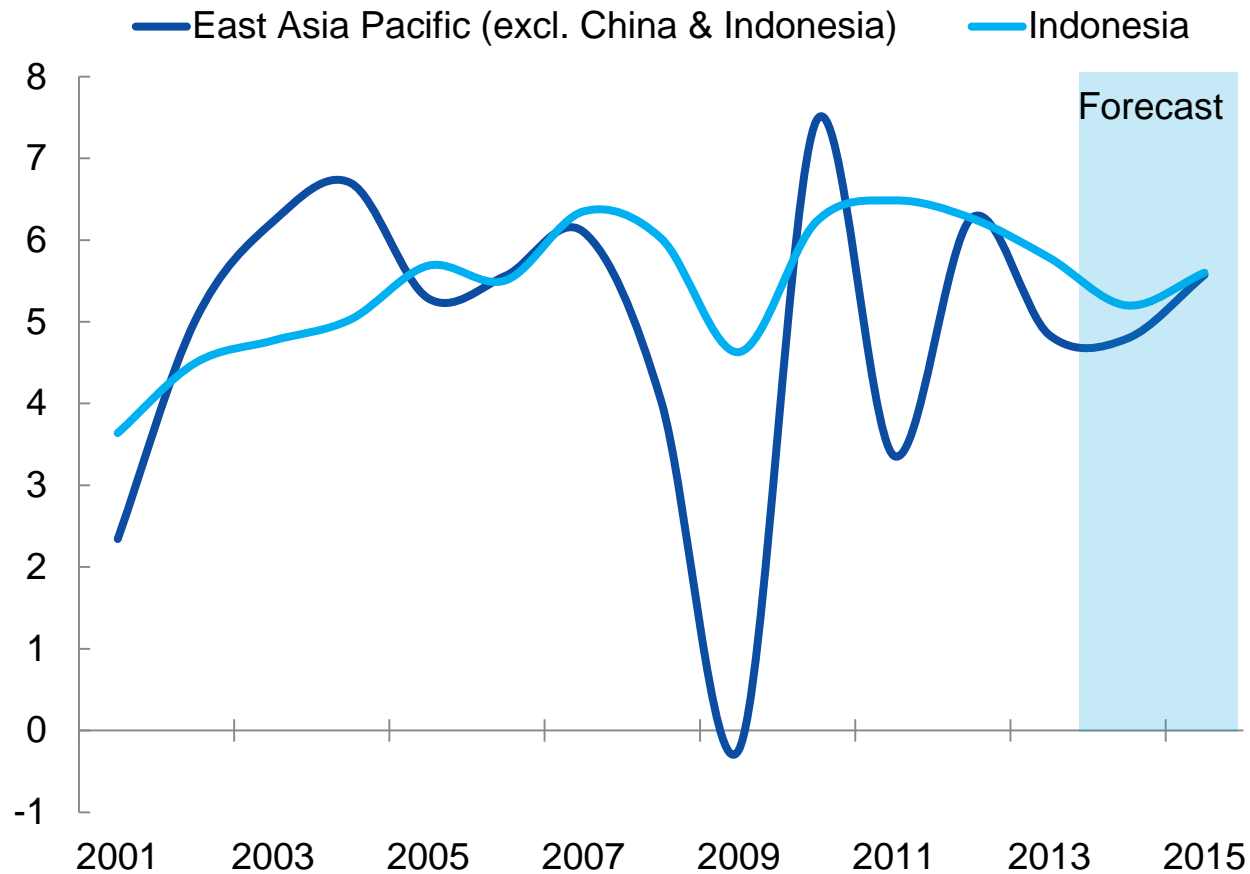


Source: World Bank



Economic growth - Will Indonesia return to 6% growth?

(annual growth, percent)

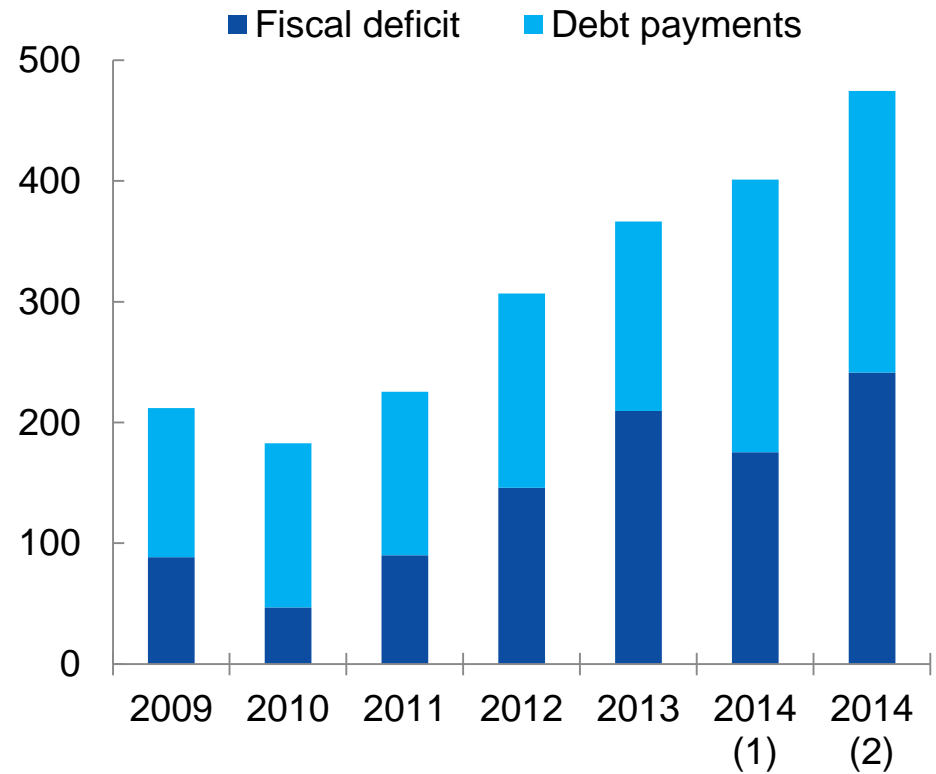
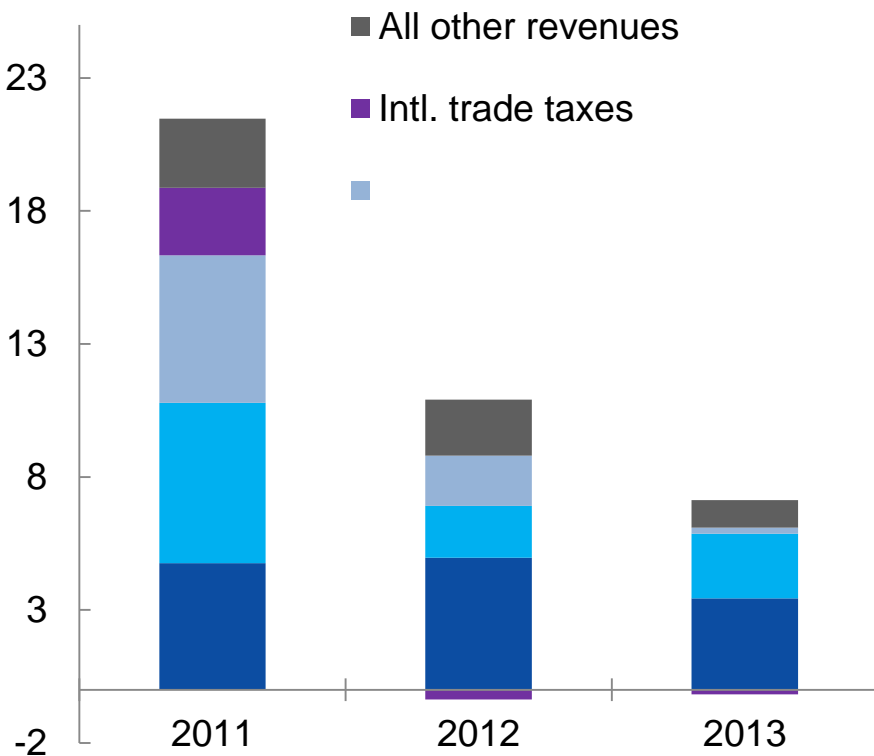


Source: BPS; World Bank staff calculations



Fiscal risks are building up steeply

... and contributed to a substantial rise in government financing needs



Note: 2014 (1) is initial Budget (APBN), (2) is revised Budget (RAPBN-P)

Source: Ministry of Finance; World Bank staff calculations



Hard choices

External balance still in focus despite macro stabilizing measures

After successful macro stabilization,
focus now on weak exports...
*(export and import USD values, yoy
growth, 3mma)*

...which have been hit by ongoing
commodity sector challenges
*(contributions to export value growth
yoy, percentage points)*

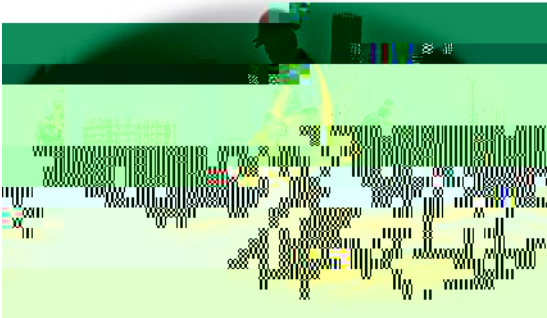
Source: CEIC; World Bank staff calculations

Moderate pace of growth expected to continue

			July IEQ		Previous (March IEQ)		
			2014p	2015p	2014p	2015p	
		2012	2013	2014p	2015p	2014p	2015p
Real GDP	(% change)	6.2	5.8	5.2	5.6	5.3	5.6
Consumer price index	(% change)	4.3	6.9	5.8	4.9	6.2	5.2
Current account balance	(% of GDP)	-2.8	-3.3	-2.9	-2.4	-2.9	-2.1
Budget balance	(% of GDP)	-1.9	-2.2	-2.8	n.a.	-2.6	n.a.

Source: BI; BPS; Ministry of Finance; World Bank staff projections

Assessing the hard policy choices ahead



Addressing near-term macro challenges

Reinvigorating growth
Fiscal pressures
External pressures

...AFFECTS THE CAPACITY TO DELIVER ON KEY STRUCTURAL REFORMS:

- SUPPLY-SIDE REFORMS

Infrastructure

Skills

Functioning of markets

- REFORMS TO ENSURE SHARED PROSPERITY

Local access to services

Social protection

Management of disaster risks & resilience



FISCAL REFORMS

Redirecting spending
Mobilizing revenue

...and achieve key development outcomes

Faster poverty reduction

Reduced inequality



Why does inequality matter for Indonesia?

- **Inequality can slow down economic growth**

Preliminary research comparing districts in Indonesia indicates that high levels of inequality hurt growth.

- **Inequality slows down poverty reduction**

If all households received growth equally, poverty would have fallen from 17.4 percent in 2003 to 0 percent by 2010.

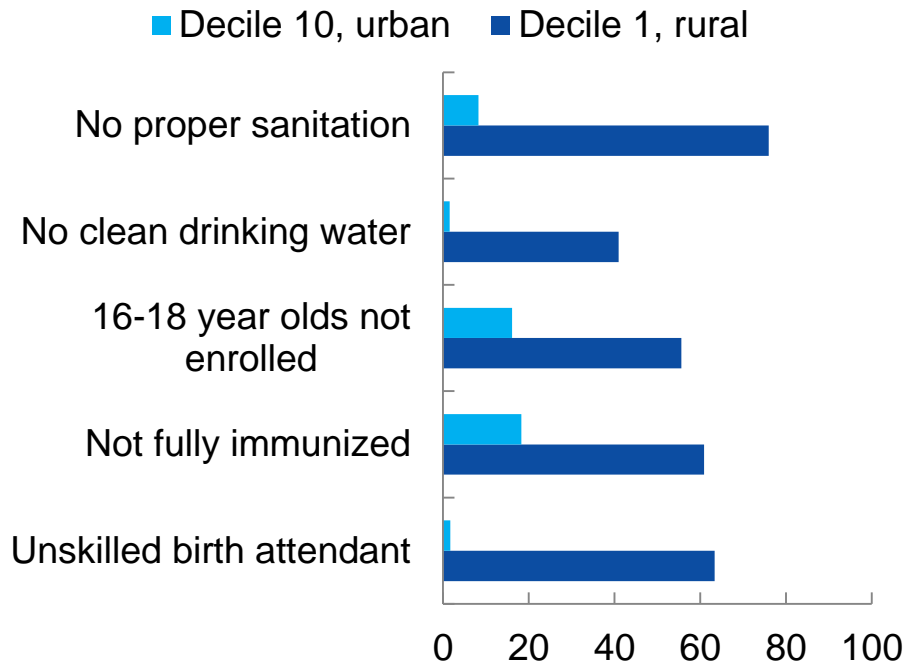
- **Inequality can trigger conflict and social tension**

Districts with Gini coefficients of 40 experienced 60 percent more conflict than districts with Gini coefficients of 20.

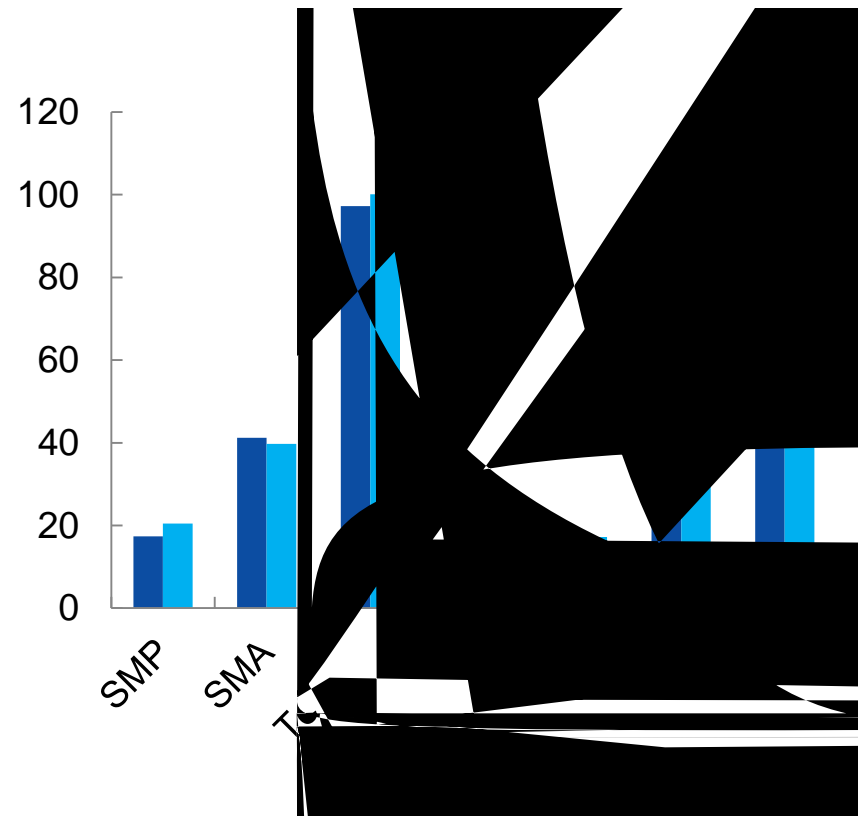
- **The majority of Indonesians believe that the country is more unequal than they'd like it to be**

What is causing the rise in inequality?

Children are born with unequal opportunities



Returns from jobs favor the rich and well-educated



Source: Susenas; DHS; World Bank staff calculations



What is causing the rise in inequality?

The poor are more vulnerable to shocks to their income

- All households face risks, for example health, cost of living shocks, and natural disasters, that can affect their income
- The rich have access to more efficient coping mechanisms to respond to shocks (savings, insurance, good jobs, etc.); the poor often do not

What can be done to address rising inequality?

83% of Indonesians believe **it is “urgent” for the new government to tackle inequality**

- **Distribution:** improve spending and taxation policies (for example, eliminate regressive fuel subsidies, enhance tax compliance)
- **Opportunities:** increase poor households’ access to high quality education and health
- **Mobility:** support labor mobility for high-quality job creation
- **Safety nets:** adequate and well-targeted, to reduce the vulnerability of the poor to shocks

Thank you

July 2014 IEQ Contents:

- Regular update on economic developments and the outlook
- New purchasing power parity-adjusted estimates of Indonesia's economy
- |

