Slower growth; high risks

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World Bank Indonesia
BKPM, December 16, 2013
Overview of recent economic developments

Framing the policy choices for the current account and growth in 2014

2014: outlook and policies
GLOBAL ECONOMY IMPROVING

OECD composite leading indicators

Source: OECD
COMMODITY PRICES STABILIZING

USD price index, 2005=100

Top 10 Indonesian export commodities

Energy prices

Non-Energy prices

Source: World Bank

22 percent fall since Feb 2011
GLOBAL POLICY UNCERTAINTIES STILL HIGH

Sovereign bond yields, percent

- US 10-year (LHS)
- Emerging markets USD bonds (RHS)
- Indonesia USD bonds (RHS)

Source: JP Morgan
5-yr gov. bond yield (RHS)

IDR 000 per USD

Source: CEIC
AND GROWTH MODERATING

GDP growth, percent

Year on year
QoQ saar

Source: BPS; World Bank staff calculations
THE CURRENT ACCOUNT DEFICIT STABILIZING

Source: BI
THE TRADE BALANCE RECOVERY NASCENT

Goods trade balance, USD billion

- Non-oil and gas
- Oil and gas
- Merchandise trade balance

Source: BI
Net trade impacts from the raw mineral export ban are expected to be negative in the near-term.

**Scenario 1:** the export ban is fully enforced and 100% of proposed smelters in the pipeline are built and operate to full capacity.

**Scenario 2:** As Scenario 1 except only the proposed additional smelters that are considered realistic by the SEADI (2013) export ban study are built.

**Scenario 3:** The export ban is fully enforced but none of the proposed smelters in the pipeline are built and become operational over 2014-2017.

Under Scenario 2 the projected negative impact on net trade in 2014 is around 0.6 percentage points of GDP, moving the current account deficit projection up to 3.2 percent of GDP.

The longer-term distortionary implications of the export ban could be sizeable.
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MYTH #1: INDONESIA GETS ENOUGH FDI

Foreign direct investment as a share of GDP (2009-2012 average)

- Vietnam*
- China
- Russia
- Brazil
- Malaysia*
- Thailand
- Argentina
- India*
- Indonesia
- Mexico
- Turkey
- South Africa*
- Philippines
- Korea

*Data through 2011
Source: World Bank
FACT: MORE FDI NEEDED, QUITE URGENTLY

Policy options:

- Implementation of August package investment measures
- Implementation of the good “Doing Business” measures announced
- Higher regulatory and policy certainty – e.g. mining

Source: BI
MYTH #2: INDONESIA IMPORTS TOO MUCH

Imports of goods and services as a share of GDP (2009-2012 average)

Vietnam: 85%
Malaysia: 75%
Thailand: 65%
Korea*: 60%
Philippines: 55%
Mexico: 50%
South Africa: 45%
Turkey: 40%
India: 35%
China*: 30%
Indonesia: 25%
Russia: 20%
Argentina: 15%
Brazil: 10%

*Data through 2011
Source: World Bank
FACT: IMPORT COMPRESSION HURTS GROWTH...

Destinations of imports by sector, percent

Manufacturing industries
Construction
Services
Transport & com.
Trade, hotel & restaurant
Agriculture
Financial & bus. Services
Mining & quarrying
Utilities

Source: World Input-Output database 2011
...AND IT IS HAPPENING ALREADY

Import growth, year-on-year change in 3-month moving average, percent

Source: BPS; World bank staff calculations
MYTH #3: A LARGE BASE OF CONSUMPTION ASSURES STRONG GROWTH

FACT: THE CURRENT RISKS ARE REAL

Household final consumption expenditure, percent of GDP
Real GDP growth, percent

Source: World Bank
## SLOWER GROWTH IN 2014 THAN 2013

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<td><strong>Real GDP</strong></td>
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<td>(% change)</td>
<td>6.5</td>
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<td>5.6</td>
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<td><strong>Consumer price index</strong></td>
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<tr>
<td>(% change)</td>
<td>5.4</td>
<td>4.3</td>
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<td>6.7</td>
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<td><strong>Current account balance</strong></td>
<td>0.2</td>
<td>-2.8</td>
<td>-3.5</td>
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<td>(% GDP)</td>
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<td><strong>Major trading partner GDP</strong></td>
<td>3.6</td>
<td>3.4</td>
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<td>3.9</td>
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<td>(% change)</td>
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Source: World Bank
...WITH GROWTH RISKS TO THE DOWNSIDE

Material risk of growth falling below 5 percent, due to:

- External financing constraints bite harder
- More marked deceleration in domestic demand than expected in the base case as private consumption and investment are affected by:
  - Higher interest rates
  - Higher import prices
  - Wealth and sentiment effects
SLOWER PACE OF POVERTY REDUCTION...

MORE ENTRENCHED POOR

2013 average per capita household consumption by percentile, as a ratio of the national poverty line

Source: BPS; World Bank staff calculations
SUPPORTING GROWTH AND MINIMIZING RISKS IN 2014

Maintaining macroeconomic stability
- Currency flexibility
- Monetary and fiscal policy coordination
- Building policy buffers and contingency planning

Supporting investment, including inward direct investment
- Pro-investment DNI revision
- Implementation of "doing business" measures
- Improving policy and regulatory certainty: process and implementation

Supporting exports
- "Quick wins" in trade facilitation and logistics
- Plugging infrastructure and skills gaps for longer-term competitiveness
ALSO IN THIS DECEMBER 2013 IEQ EDITION

- Analysis of the 2014 Budget
- An update on poverty trends
- An update on labor market trends
- New survey results on local governance capacity

On the web: