



INDONESIA
ECONOMIC
QUARTERLY

October 2013

Continuing adjustment

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Paramadina Public Policy Institute, October 4, 2013**



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OCTOBER 2013 IEQ LAUNCH PRESENTATION

More subdued growth outlook, resulting from two major shocks to the economy and ongoing adjustments

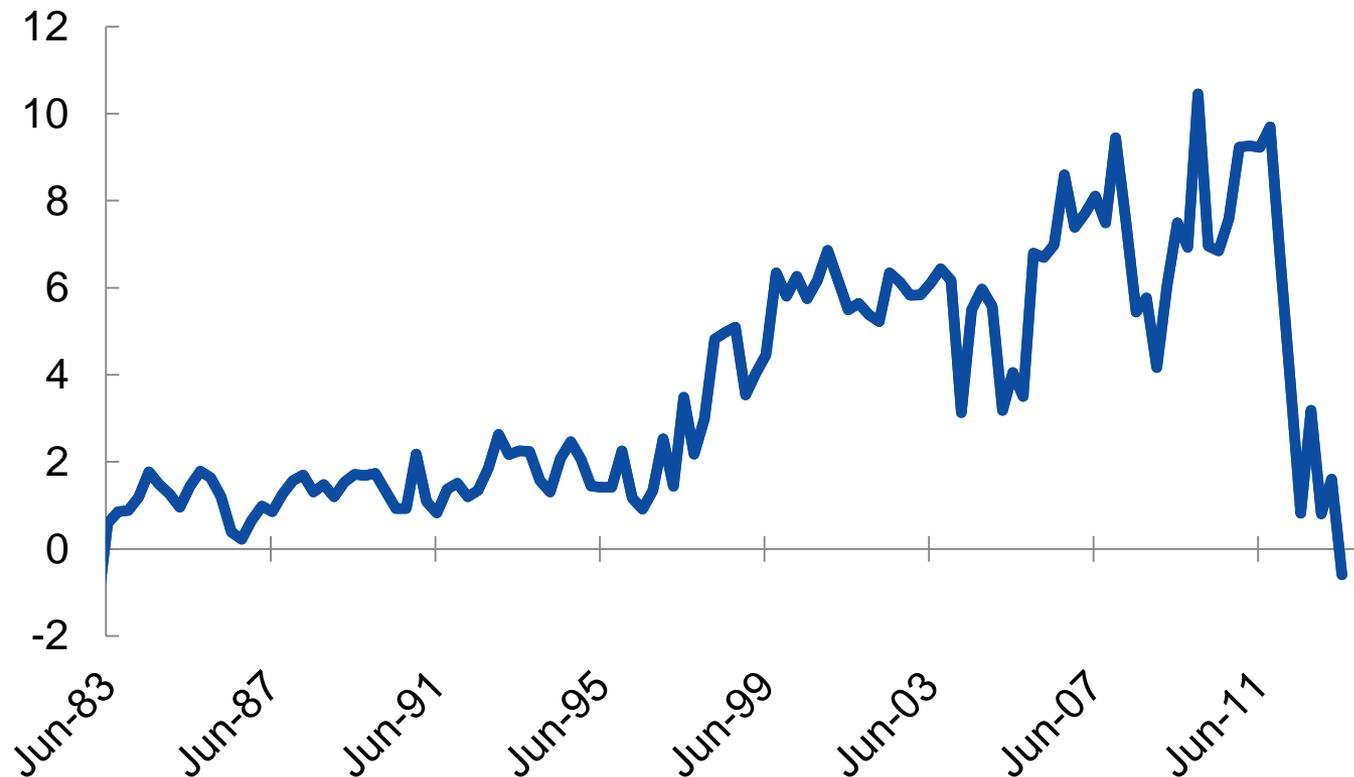
Developments in Q3 show adjustments are well underway but highlight Indonesia's macro vulnerabilities

The role of good policies in this time of *continuing adjustment*



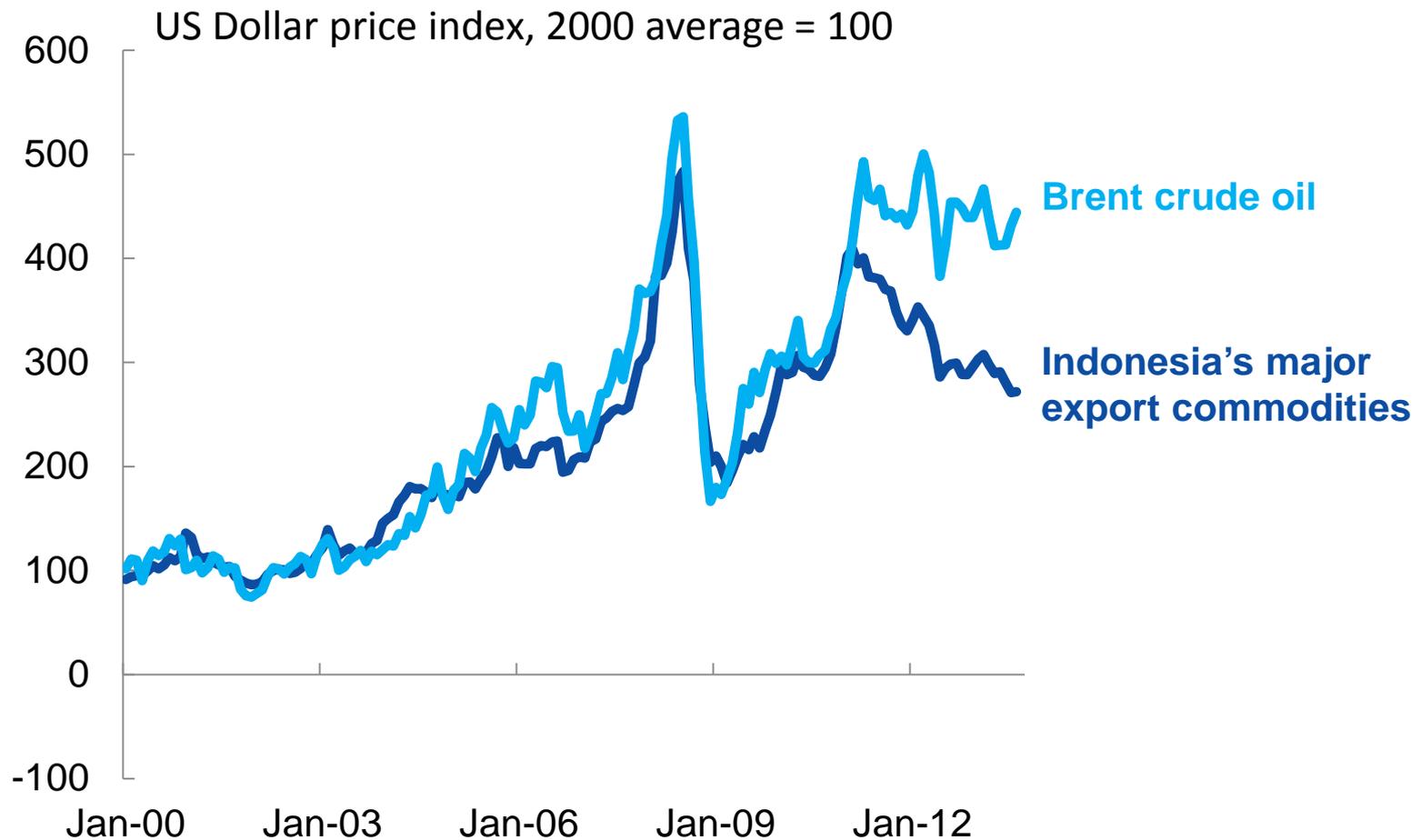
FIRST SHOCK: TRADE SHOCK, SINCE 2011...

Quarterly merchandise trade balance, USD billion



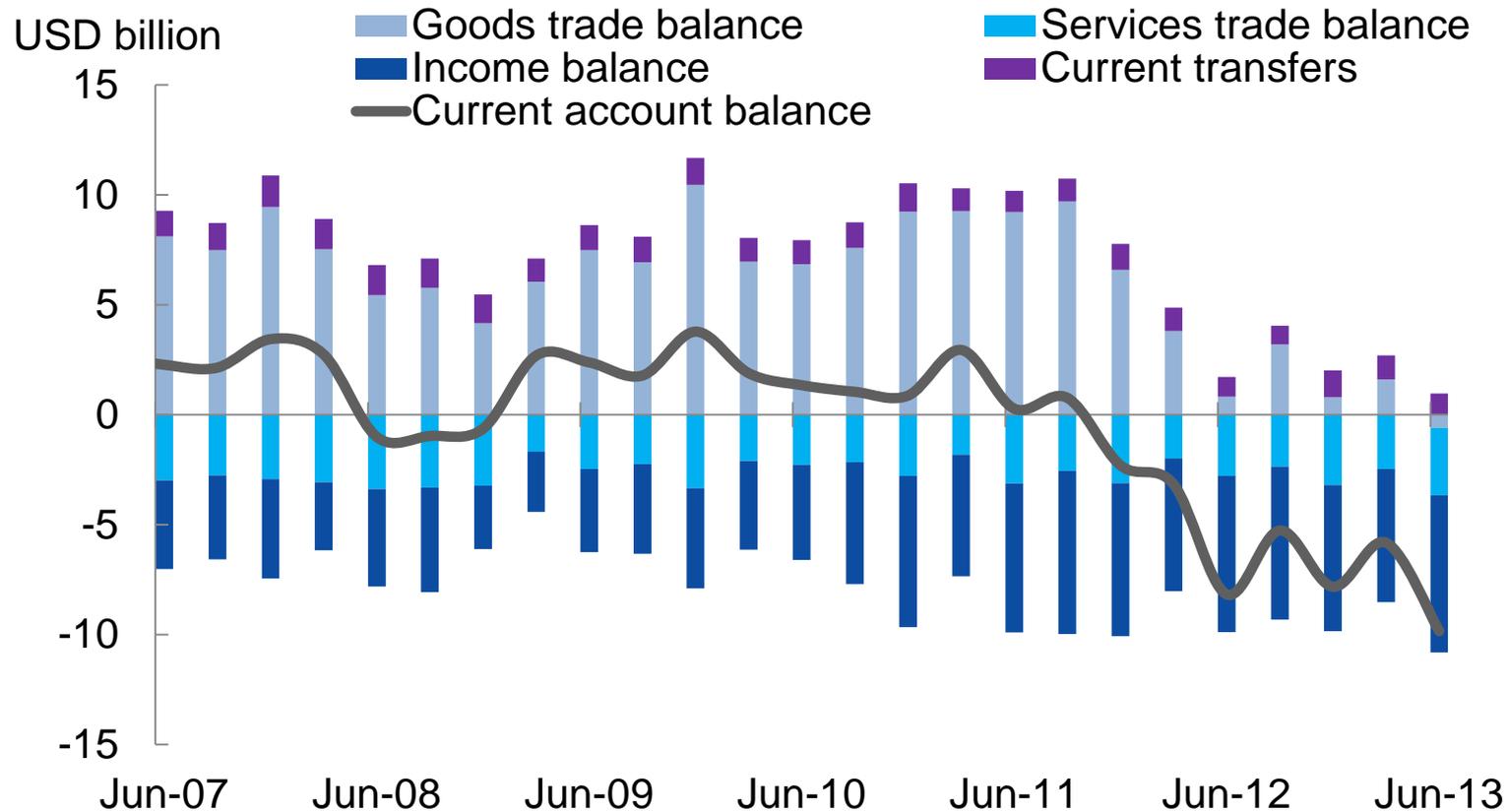
Source: BI

...AS TERMS OF TRADE HAVE WEAKENED



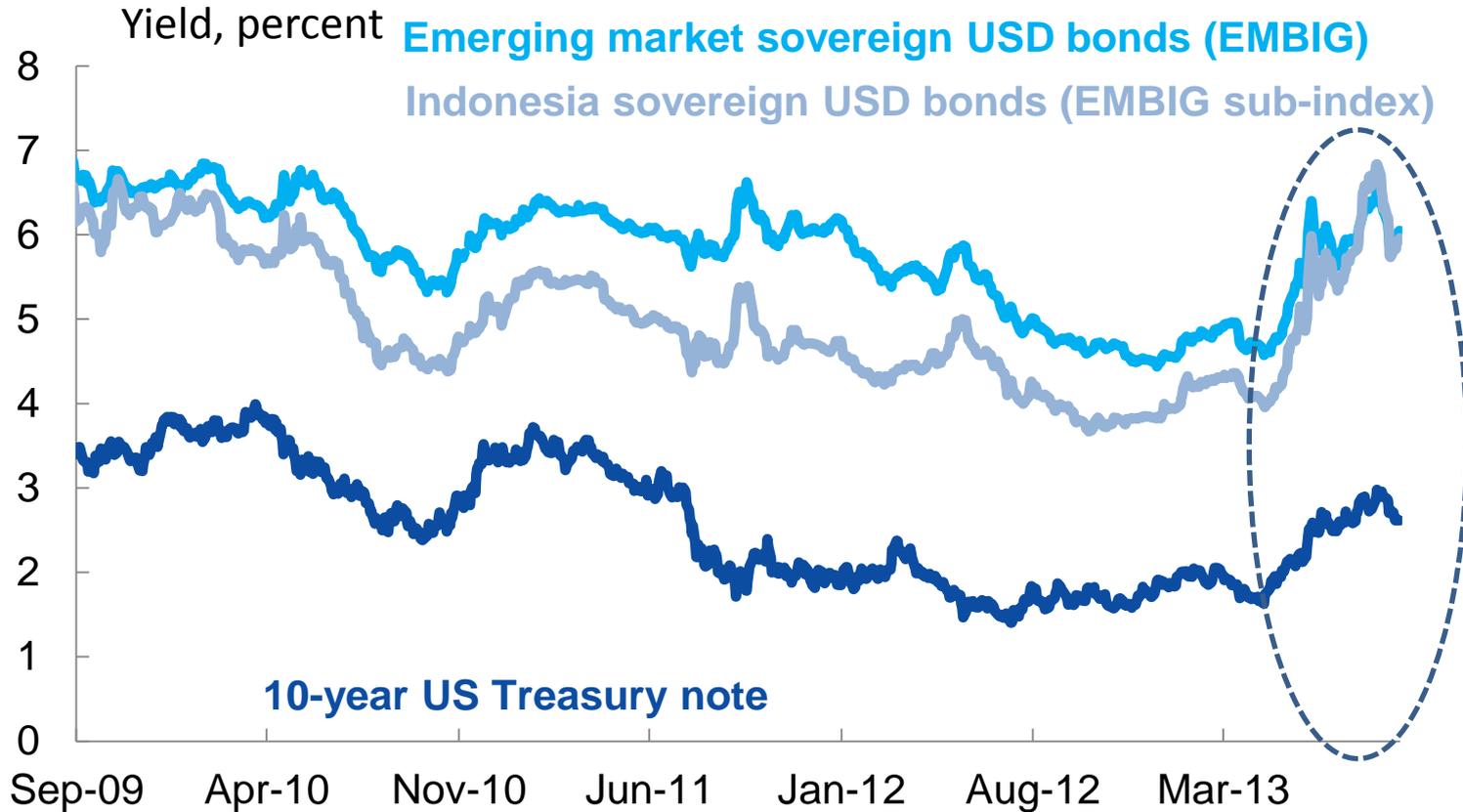
Source: World Bank

PRESSURING THE OVERALL CURRENT ACCOUNT



Source: BI

SECOND SHOCK: FINANCING COSTS



Source: JP Morgan

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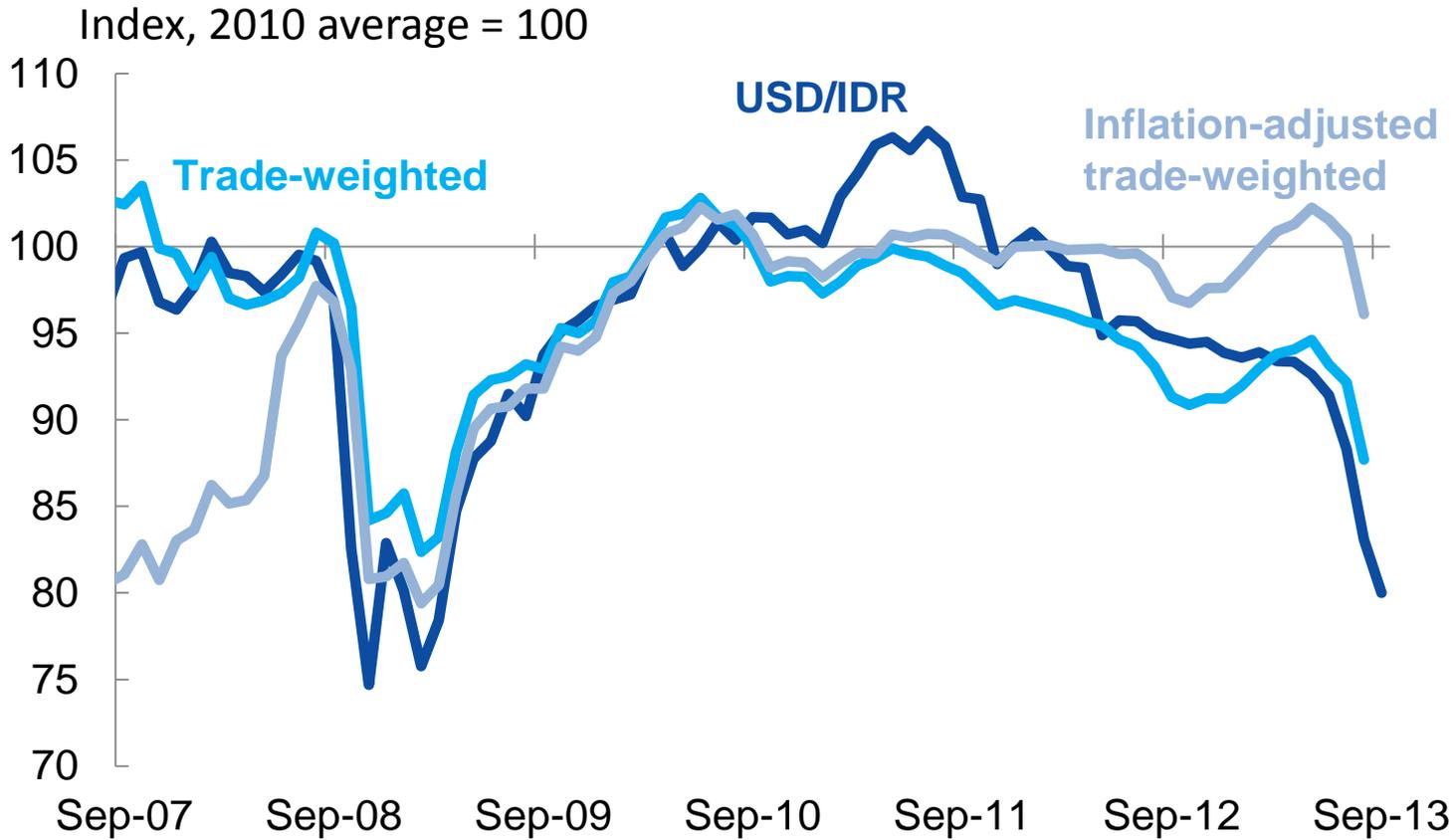
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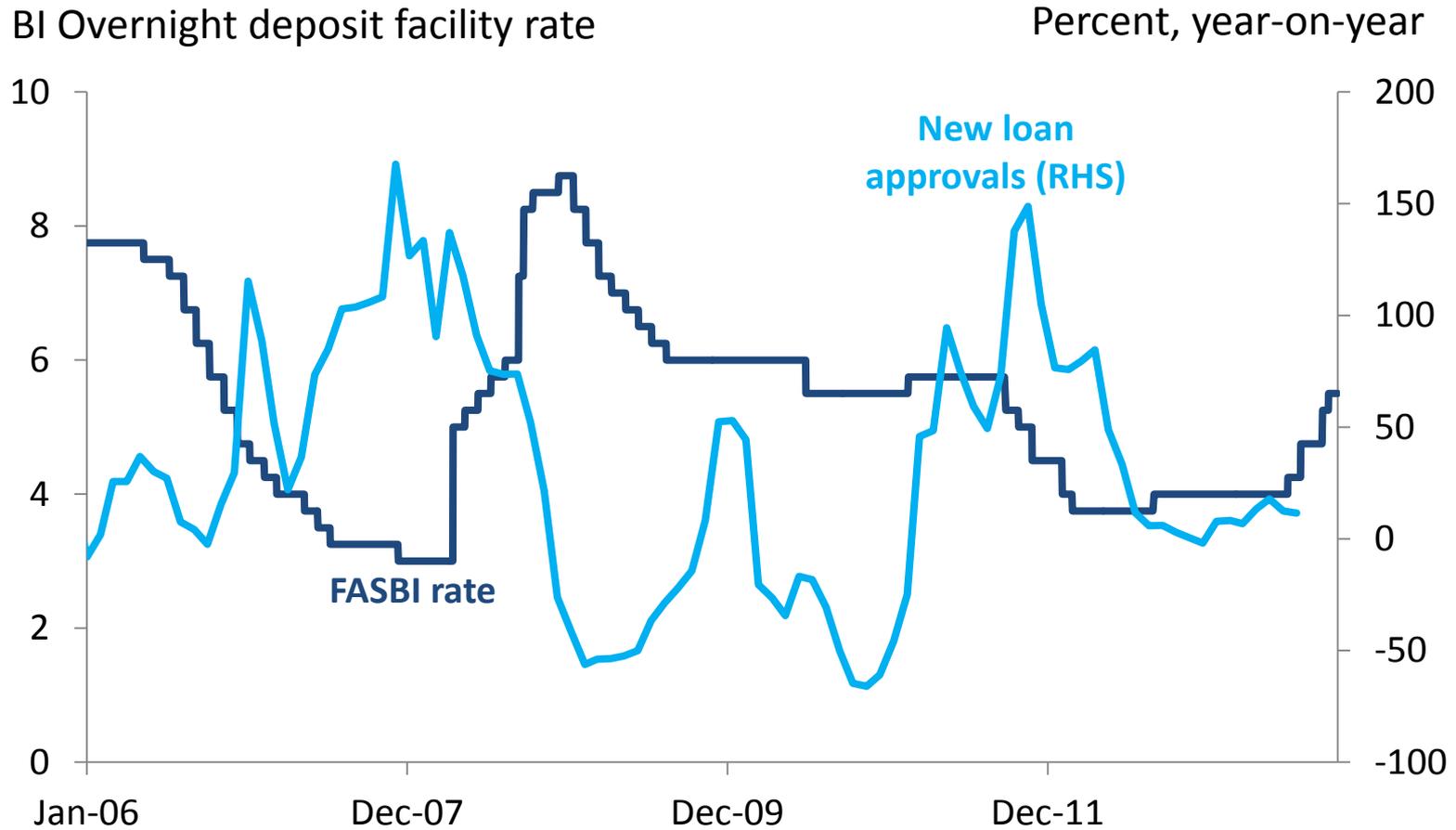


CURRENCY: RUPIAH ADJUSTING



Source: World Bank

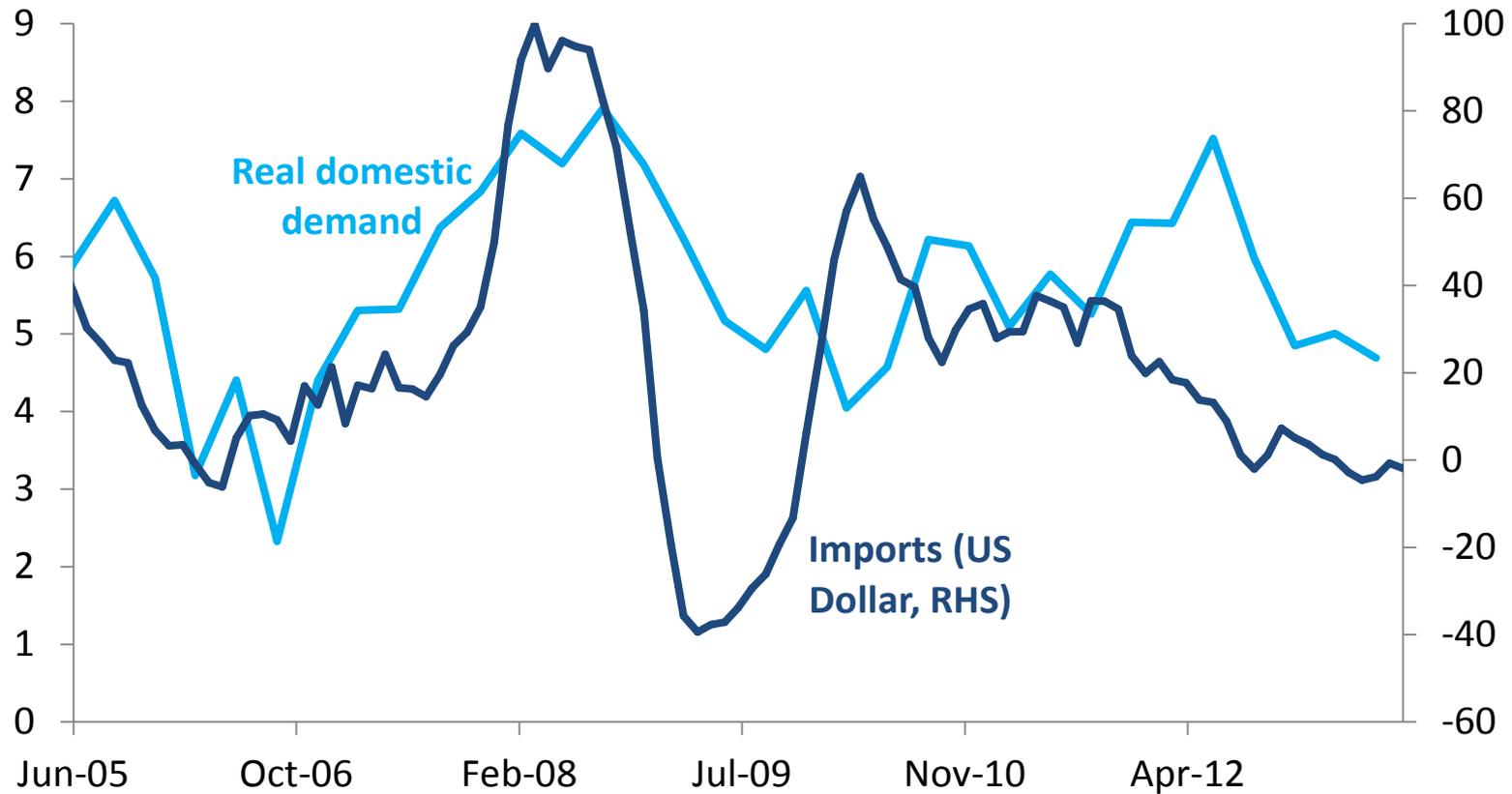
MONETARY CONDITIONS: TIGHTENING



Source: BI

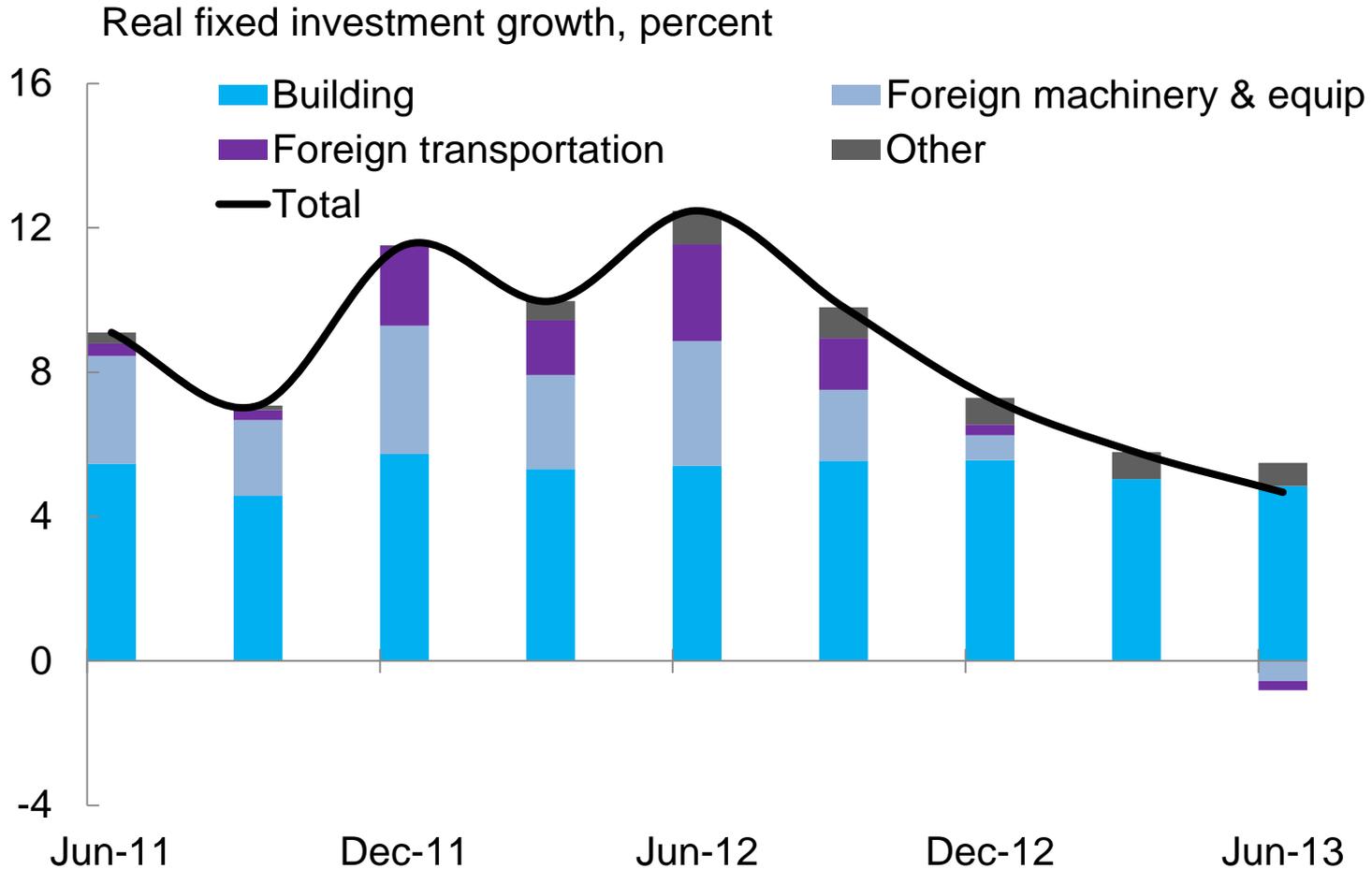
DOMESTIC DEMAND: SOFTENING

Growth yoy, percent



Source: BPS; World Bank staff calculations

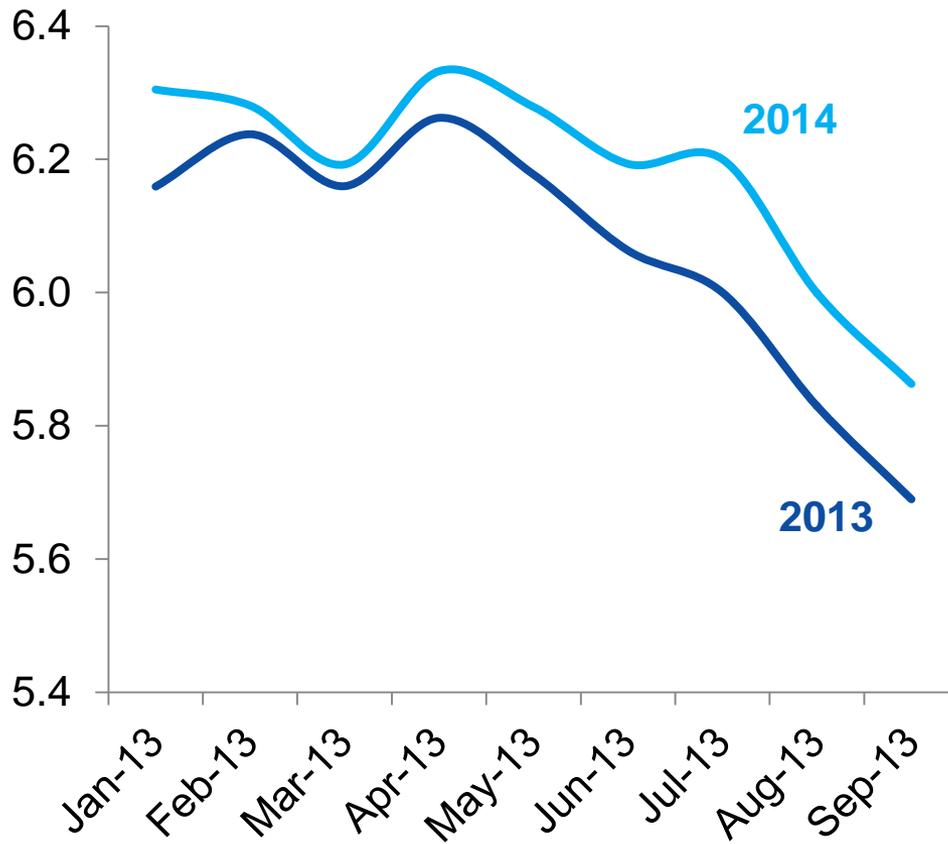
INVESTMENT SLOWING DOWN



Source: World Bank

REPEATED DOWNWARD REVISIONS

Average of analysts' real GDP growth forecasts



Source: Consensus Economics



OUTLOOK: MORE ADJUSTMENT TO COME...

		October IEQ				Previous (July)	
		<u>2011</u>	<u>2012</u>	<u>2013p</u>	<u>2014p</u>	<u>2013p</u>	<u>2014p</u>
Real GDP	(% change)	6.5	6.2	5.6	5.3	5.9	6.2
Consumer price index	(% change)	5.4	4.3	7.3	6.7	7.2	6.7
Current account deficit	(% GDP)	0.2	-2.8	-3.4	-2.6	-2.7	-2.1
Major trading partner GDP	(% change)	3.6	3.4	3.4	3.9	3.4	4.0

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

...BUT PERSPECTIVE, PLEASE



Source: World Bank

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THREE R'S FOR POLICY

➤ **Responding**, to facilitate more near-term adjustment:

- Monetary and fiscal policy coordination
- Exchange rate flexibility

➤ **Reducing uncertainty**:

- Contingency planning
- Communication

➤ **Refocusing policies to lift sustainable growth rate**:

- August package: follow through
- “Quick wins” for competitiveness
- Fiscal sector: energy subsidies, infrastructure spending, social protection



AUGUST PACKAGE: IMPLEMENTATION IS KEY

Relieve external balance pressures

- Exports: tax relief for labor-intensive exporters
- Investment: DNI; “de-bottlenecking”

Reduce inflation pressures

- Food imports: move to price-based restrictions

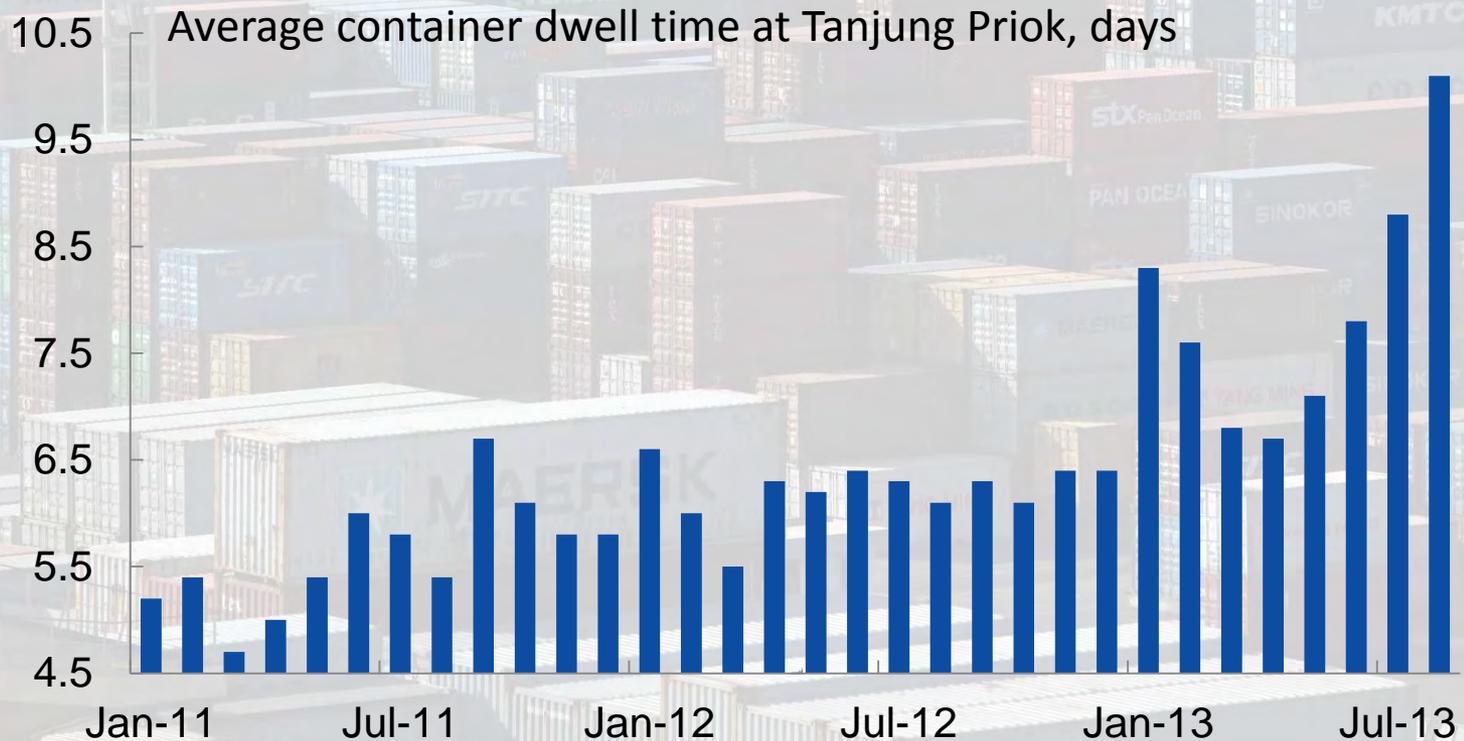
Support employment

- Bounded zones
- Tax relief for qualifying firms in labor-intensive sectors
- Minimum wages



MORE MEASURES TO LIFT COMPETITIVENESS

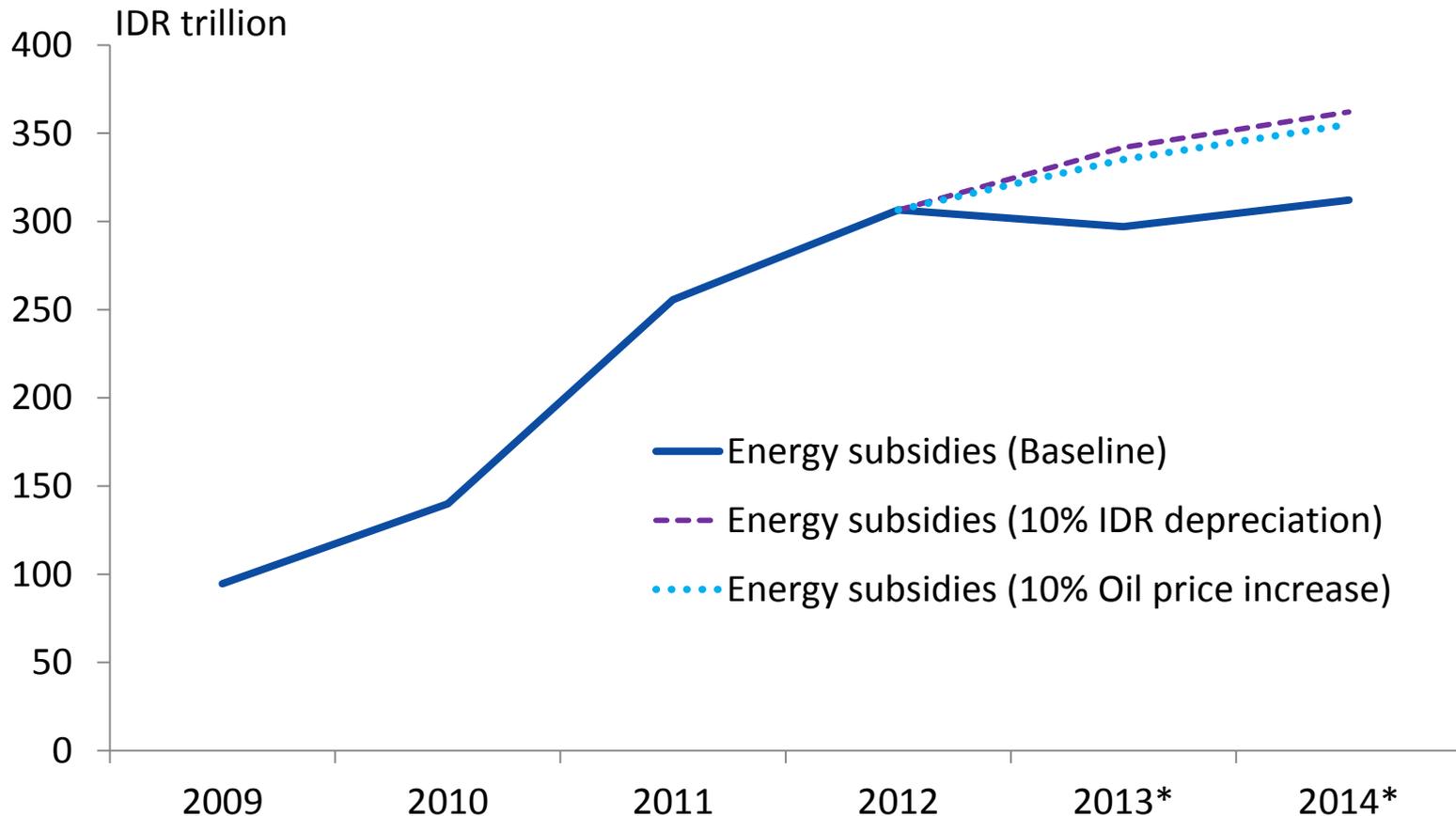
- Boost from weaker Rupiah provides an opportunity...
- ...but will be wasted without a supply response
- “Quick wins” in trade facilitation can help



Source: Jakarta International Container Terminal (JICT)

COSTS AND RISKS FROM ENERGY SUBSIDIES

Energy subsidy costs – baseline and with 10 percent IDR depreciation/oil price increase

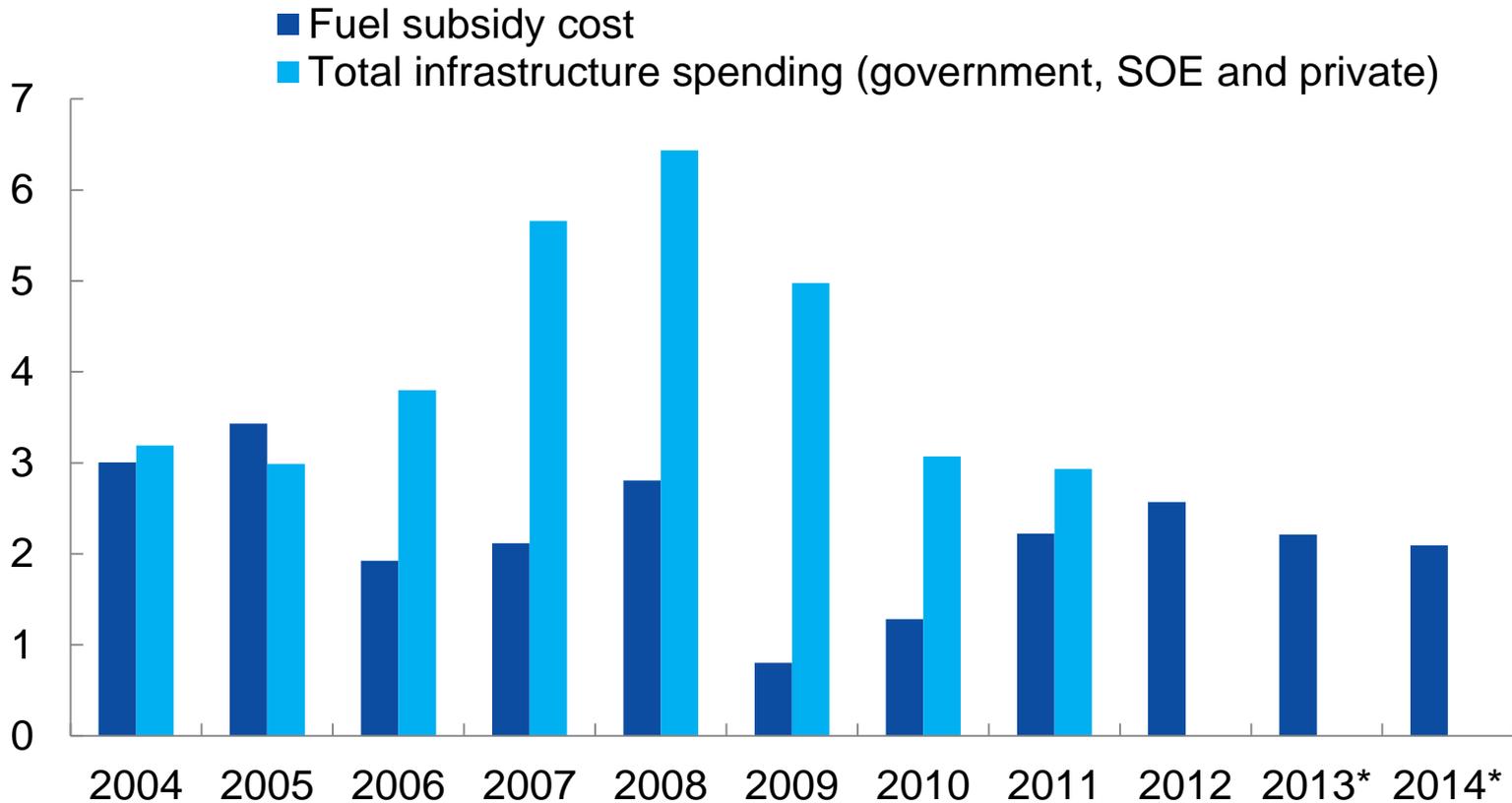


Note: *World Bank projections

Source: World Bank staff calculations

REDIRECTING SPENDING: THE OPPORTUNITY

Spending on fuel subsidies and infrastructure, percent of GDP

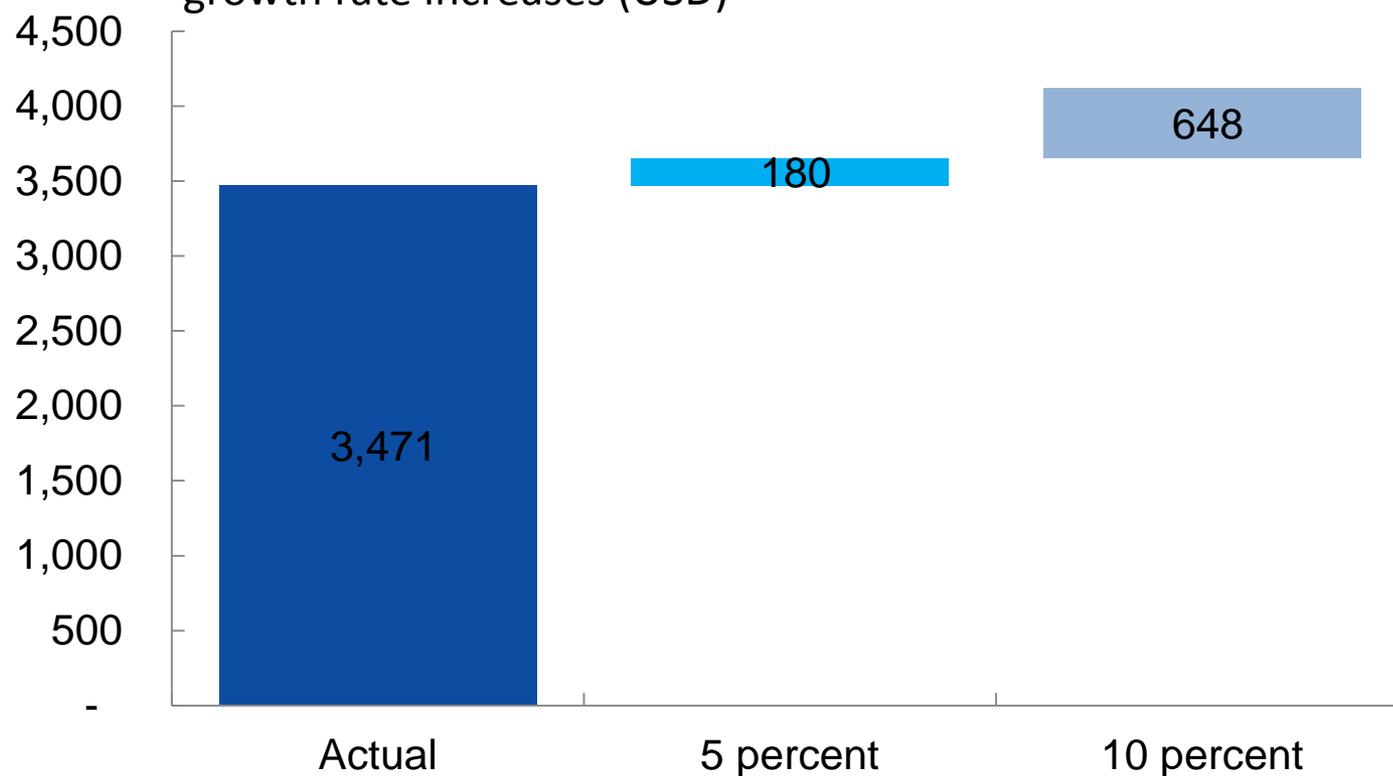


*World Bank projections

Source: Ministry of Finance; World Bank

MORE INFRASTRUCTURE STOCK, HIGHER INCOME

2011 per capita income – actual, and following higher annual infrastructure growth rate increases (USD)



Source: World Bank staff calculations

BREAKING INTO INFRASTRUCTURE CYCLE

**ADDRESS THE
PERSISTENT
INFRASTRUCTURE GAP**

**SUPPORT
EXTERNAL
BALANCES OVER
THE MEDIUM-
TERM**

- Improve domestic and external competitiveness
- Potential to re-orientate import-intensity of spending
- Enhance FDI potential (and provide more stable financing)

**REALLOCATE
SPENDING
TOWARDS
INFRASTRUCTURE**

- Offset the rise in financing costs
- Enhance sustainable growth



MAIN MESSAGES

- **Indonesia faces greater constraints: trade shock, global liquidity**
- **The economy and policy settings are adjusting:**
 - Base case outlook for growth moderation and gradually narrowing current account deficit
 - But external uncertainties still elevated and adjustment phase carries risks
- **Critical continued role for policy – 3 R's:**
 - **Responding**, to facilitate more near-term adjustment
 - **Reducing uncertainty**: contingency planning and communication to support confidence
 - **Refocusing policy efforts** on lifting competitiveness and the sustainable growth rate
 - August policy package implementation
 - Additional “quick wins”, e.g. trade facilitation
 - Continuing progress on fiscal sector reforms

