INTERNATIONAL MONETARY FUND

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INDONESIA

August 2024

2024 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR INDONESIA

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2024 Article IV consultation with Indonesia, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its July 22, 2024 consideration of the staff report that concluded the Article IV consultation with Indonesia.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on July 22, 2024, following discussions that ended on June 7, 2024, with the officials of Indonesia on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 2, 2024.
- An **Informational Annex** prepared by the IMF staff.
- A **Statement by the Executive Director** for Indonesia.

The documents listed below have been or will be separately released.

Selected Issues
Financial Stability System Assessment

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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PRESS RELEASE

PR24/303

IMF Executive Board Concludes 2024 Article IV Consultation with Indonesia

FOR IMMEDIATE RELEASE

Washington, DC – **August 7, 2024**: On July 22, the Executive Board of the International Monetary Fund (IMF) concluded the 2024 Article IV consultation[1] with Indonesia and the 2024 Financial System Stability Assessment.

Indonesia's prudent fiscal, monetary, and financial policy frameworks have provided the foundations for macro-stability and social gains. Decisive policy actions facilitated a robust recovery from consecutive global shocks since 2020. Indonesia's growth remains strong despite external headwinds, inflation is low and well-contained, the financial sector is resilient, and policies are generally prudent and geared towards preserving buffers.

The outlook remains positive despite a challenging global context. Growth would reach 5.0 and 5.1 percent in 2024 and 2025 respectively, with dynamic domestic demand offsetting the drag from softer commodity prices. Inflation is projected to converge to the mid-point of the target range over time. Real exports would expand at a slower pace while import growth would recover in line with domestic demand, leading to moderate current account deficits in 2024-25. The balance of payments surplus will continue to strengthen over time, reflecting a pickup of FDI and portfolio inflows, supporting a further buildup of reserve buffers.

Risks are broadly balanced. Commodity price volatility (e.g., from geopolitical shocks), a slowdown in Indonesia's key trading partners, or spillovers from high-for-longer policy rates in advanced economies (AEs) are important external downside risks. On the domestic side, a weakening of long-standing sound macro-fiscal frameworks could hamper policy credibility. On the upside, stronger-than-anticipated growth in trading partners, or an earlier-than-expected monetary policy easing could strengthen growth; deeper-than-envisaged structural reforms could raise growth over the medium term.

Executive Board Assessment[2]

Executive Directors welcomed Indonesia's strong economic performance, substantial buffers, and track record of prudent policies. They concurred that risks are broadly balanced in the near term, while noting significant uncertainties from tighter global financial conditions, geopolitical tensions, and commodity price volatility.

Directors welcomed the authorities' commitment to fiscal discipline. They considered that slightly narrower deficits in 2024 and 2025 would support growth while preserving fiscal space to help respond to downside risks. They saw scope for strengthening the fiscal framework to

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.IMF.org/external/np/sec/misc/qualifiers.htm.

allow more countercyclical policies within the budget cap. Directors supported efforts to strengthen revenue mobilization and streamline energy subsidies to create room for development spending needs within the fiscal rule.

Directors welcomed the reduction of inflation to the target range and agreed that the monetary policy stance should remain data dependent, with a flexible exchange rate acting as a shock absorber. They concurred that foreign exchange market interventions should be judiciously deployed under certain shocks and circumstances, mindful of preserving reserve buffers. A few Directors encouraged the authorities to provide foreign exchange intervention data. Directors supported efforts to deepen financial markets and strengthen the effectiveness of monetary policy transmission.

Directors welcomed the 2024 FSAP's assessment that the financial system is broadly resilient and well-capitalized. They encouraged continued progress in strengthening financial sector supervisory and regulatory frameworks, the financial safety net, and crisis management, as well as close monitoring of pockets of potential vulnerabilities. Directors welcomed efforts to enhance the macroprudential policy framework and saw merit in clarifying the primacy of financial system resilience as the objective of macroprudential policy. They encouraged a gradual tightening of the macroprudential stance as the credit gap closes. Further strengthening the AML/CFT framework remains important.

Directors welcomed the authorities' goal of reaching high-income status by 2045. They noted that achieving this in an inclusive manner will require ambitious structural reforms, including on governance and anti-corruption, leveling up learning outcomes, logistics and infrastructure, fostering trade openness, and enhancing social protection. Directors agreed that transitioning away from non-tariff trade measures would be critical to support inclusive growth and global economic integration, while industrial policies should target market failures, minimizing trade and investment distortions.

Directors welcomed the authorities' commitments to achieve net-zero emissions by 2060 and the steps taken to limit greenhouse gas emissions and deforestation. A plan for off-grid power generation, energy subsidy reforms and carbon pricing, and phasing out related non-tariff measures would be key to achieving climate goals.

Table 1. Indonesia: Selected Economic Indicators, 2022–27

Nominal GDP (2023): Rp 20,892 trillion or US$1,371 billion
Population (2023): 277 million
Main exports (percent of total, 2023): coal (16.5), base metal (15.6), palm oil (8.7), oil and gas (6.2), electrical apparatus (5.5), textile and products (4.5)
GDP per capita (2023): US$4,942
Unemployment rate (September 2023): 5.3 percent
Poverty headcount ratio at national poverty line (March 2022): 9.5 percent of population

	2022	2023	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.
Real GDP (percent change)	**5.3**	**5.0**	**5.0**	**5.1**	**5.1**	**5.1**
Domestic demand	3.8	5.1	5.0	5.2	5.1	5.1
Of which:						
Private consumption 1/	5.0	4.9	5.1	5.1	5.1	5.1
Government consumption	-4.5	2.9	5.5	4.2	3.0	3.0
Gross fixed investment	3.9	4.4	5.0	5.7	5.7	5.7
Change in stocks	0.1	0.5	0.0	0.0	0.0	0.0
Net exports 2/	0.8	0.7	0.2	0.2	0.3	0.3
Statistical discrepancy 2/	0.9	-0.4	0.0	0.0	0.0	0.0
Output gap (in percent)	**-1.1**	**-0.3**	**-0.2**	**-0.1**	**0.0**	**0.0**
Saving and investment (in percent of GDP)						
Gross investment 3/	29.7	30.5	30.5	30.6	30.7	30.8
Gross national saving	30.7	30.4	29.6	29.3	29.3	29.4
Prices (12-month percent change)						
Consumer prices (end period)	5.4	2.8	2.8	2.7	2.6	2.5
Consumer prices (period average)	4.1	3.7	2.9	2.8	2.6	2.6
Public finances (in percent of GDP)						
General government revenue	15.2	15.0	14.8	14.9	15.0	15.0
General government expenditure	17.4	16.6	17.1	17.6	17.5	17.4
Of which: Energy subsidies	0.9	0.8	0.8	0.6	0.5	0.4
General government balance	-2.2	-1.6	-2.3	-2.6	-2.5	-2.4
Primary balance	-0.2	0.5	-0.3	-0.6	-0.3	-0.1
General government debt	40.1	39.6	39.5	39.4	39.3	39.1
Money and credit (12-month percent change; end of period)						
Rupiah M2	8.4	3.5	9.9	10.0	9.8	9.8
Base money	23.9	-1.5	4.0	6.0	7.0	7.4
Claims on private sector	10.1	9.2	10.5	11.3	9.5	9.6
One-month interbank rate (period average)	4.2	6.4	...	...	...	...
Balance of payments (in billions of U.S. dollars, unless otherwise indicated)						
Current account balance	13.2	-1.9	-12.3	-20.5	-24.2	-25.5
In percent of GDP	1.0	-0.1	-0.9	-1.3	-1.4	-1.4
Trade balance	62.7	46.5	34.8	30.1	29.4	32.8
Of which: Oil and gas (net)	-24.8	-19.7	-20.9	-18.3	-13.8	-14.2
Inward direct investment	25.4	21.8	26.0	29.6	33.5	36.1
Overall balance	4.0	6.3	0.8	6.7	9.6	13.7
Terms of trade, percent change (excluding oil)	22.9	-12.4	0.8	1.0	-3.4	-0.2
Gross reserves						
In billions of U.S. dollars (end period)	137.2	146.4	147.2	153.9	163.5	177.3
In months of prospective imports of goods and services	6.2	6.1	5.5	5.2	5.1	5.2
As a percent of short-term debt 4/	206	209	198	192	190	193
Total external debt 5/						
In billions of U.S. dollars	396.5	408.5	419.0	439.4	461.6	482.8
In percent of GDP	30.1	29.8	29.4	28.3	27.5	26.6
Exchange rate						
Rupiah per U.S. dollar (period average)	14,850	15,237	...	...	...	...
Rupiah per U.S. dollar (end of period)	15,573	15,399	...	...	...	...
Memorandum items:						
Jakarta Stock Exchange (12-month percentage change, composite index)	4.1	6.2	...	...	...	...
Oil production (thousands of barrels per day)	800	797	794	791	788	785
Nominal GDP (in trillions of rupiah)	19,588	20,892	22,555	24,367	26,274	28,313

Sources: Data provided by the Indonesian authorities; Bloomberg L.P.; and IMF staff estimates and projections.

1/ Includes NPISH consumption.
2/ Contribution to GDP growth (percentage points).
3/ Includes changes in stocks.
4/ Short-term debt on a remaining maturity basis.
5/ Public and private external debt.

INTERNATIONAL MONETARY FUND

INDONESIA

STAFF REPORT FOR THE 2024 ARTICLE IV CONSULTATION

July 2, 2024

KEY ISSUES

Outlook and Risks. Indonesia's growth remains strong despite external headwinds. Inflation is firmly in the target range and the financial sector is resilient. The authorities have been pursuing an ambitious growth agenda to reach high-income status by 2045. This comprises public spending, institutional reforms, and Industrial Policy (IP). Risks are broadly balanced. Key downside risks include persistent commodity price volatility (e.g., from geopolitical shocks), an abrupt slowdown in Indonesia's key trading partners, or adverse spillovers from tighter-for-longer global financial conditions. On the domestic side, a weakening of long-standing sound macro-fiscal frameworks could hamper policy credibility. On the upside, stronger-than-anticipated growth in trading partners or faster disinflation in AEs could prop up growth while deep structural reforms would raise growth over the medium term.

Main Policy Recommendations

- ***Indonesia's longstanding fiscal prudence should be preserved***. A slightly narrower deficit would support both growth and a more balanced policy mix. The fiscal rule's budget cap of 3 percent of GDP has served Indonesia well. An enhanced medium-term fiscal framework (MTFF), with well-defined operational targets, would help ensure that fiscal policy can act counter-cyclically within the fiscal rule more systematically. Prioritizing revenue mobilization—through ambitious reforms encompassing tax administration and policy—would strengthen fiscal space to significantly boost needed development spending while still meeting the fiscal rule. Closely monitoring fiscal risks and avoiding the buildup of contingent liabilities will also be key.

- ***The monetary policy stance is appropriate***. The policy rate is above neutral; with financial risks contained, accommodative macroprudential policy has supported credit growth while liquidity remains comfortable. Monetary policy should remain data-driven, based on the evolution of domestic conditions, and the exchange rate serving as a shock absorber. Foreign Exchange Intervention (FXI) would be appropriate under certain shocks and circumstances, particularly when shocks trigger

spikes in market premia given shallow FX markets, though its use will need to be mindful of preserving reserve buffers. Market development and policy effectiveness would be bolstered by greater price discovery and an increasingly market-determined interest rate term structure.

- ***Further financial sector reform would protect resilience and enable sound financial market deepening***. Clarifying that financial system resilience takes priority amongst objectives as the macroprudential toolkit is calibrated would enhance communication and effectiveness. Bolstering financial sector regulation and supervision, the financial safety net, crisis management, and systemic liquidity and resolution frameworks are key aspects of the agenda. Developing the credit infrastructure to foster sound financial access—including of digital financial services—and continuing to address remaining gaps in the Anti-Money Laundering and Combating Financing of Terrorism (AML/CFT) framework would also be important.

- ***Bridging structural gaps will be needed to achieve higher and inclusive potential growth and reach high income status, as envisaged in the country's national development strategy—the Golden Vision 2045***. Horizontal structural reforms, including strengthening governance and anti-corruption, leveling up education and skills, enhancing health and social protection, investing in logistics and infrastructure, fostering openness, and bolstering the business environment will be essential to boost broad-based growth. Carefully designing IP to target market failures and avoid trade and investment distortions should help strengthen its benefits and reduce costs, helping prevent risks of hindering potential growth. Transitioning away from non-tariff barriers will also be critical to sustain strong and inclusive growth while supporting global economic integration.

Approved By
Rupa Duttagupta (APD) and Anna Ilyina (SPR)

Discussions took place in Jakarta during May 27-June 7, 2024. The mission comprised Maria Gonzalez (Head), Ashique Habib, Raju Huidrom, Choonsung Lim, Anne-Charlotte Paret and Dennis Botman (Resident Representative) (all APD), and Bruno Albuquerque (SPR). Mses. Fadilah, Handayani, Kusumawardani, Tresnatri, and Messrs. Dachlan and Pasha (all Resident Representative Office) supported the mission. Yati Kurniati, Executive Director, Irfan Hendrayadi, Advisor (all OED) joined the meetings. Amr Hosny (FAD) provided significant inputs ahead of the mission. Agnes Isnawangsih and Patricia Tanseco (both APD) contributed to the preparation of this report.

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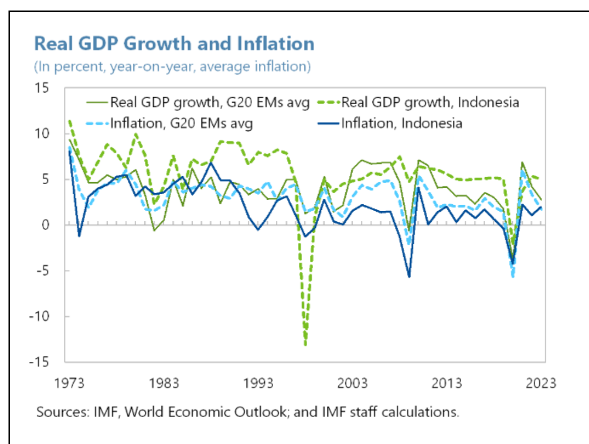
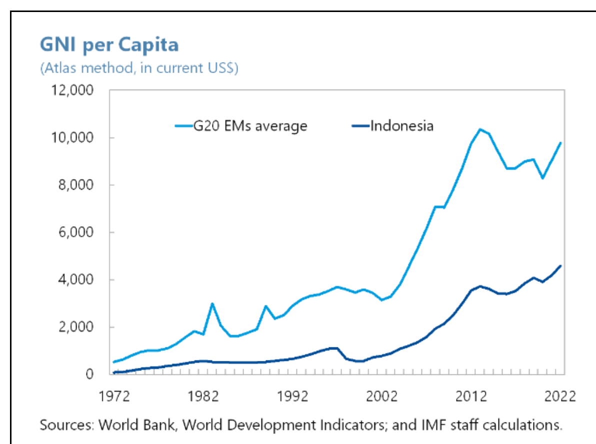
CONTEXT: BALANCING GROWTH AND STABILITY

1. Indonesia's longstanding strong economic performance owes much to its prudent macroeconomic policies, yet more is needed to sustainably lift inclusive growth. The country has enjoyed over two decades of high growth and macroeconomic stability while making steady progress in poverty reduction and increasing social and economic inclusion. Prudent fiscal, monetary, and financial policy frameworks provided the foundation for such sustained gains. Decisive policy actions facilitated a robust recovery from consecutive global shocks since 2020, while policy pivots since then have underlined commitments to sound frameworks and to rebuilding and sustaining buffers. The economy ranks among the twenty largest in the world, thanks to support from steady growth, natural resources, a strategic geographical location, and a large young population. Yet income per capita is relatively low, underscoring the importance of closing remaining human, physical, and institutional capital gaps to strengthen medium-term growth.





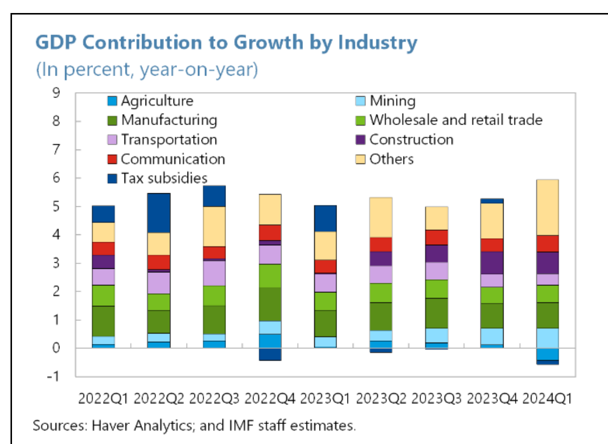
2. Indonesia's ambition is to achieve high-income status by 2045. The country's national development strategy—the *Golden Vision 2045*—aims to transform Indonesia into a high-income country by the centennial of its Independence. The aspiration is to increase value added by moving through the value chain from raw commodities, build a skilled population ready for the digital age, and accelerate infrastructure development and institutional reform to support balanced, green, and equitable growth. A new administration headed by President-elect Prabowo Subianto, set to take power in October 2024 for a five-year term, has pledged to continue this agenda. Achieving this vision will require broad and sustained structural reforms,[1] while safeguarding hard-earned gains on macroeconomic stability.

[1] Indonesia also officially received its OECD Accession Roadmap in May 2024, after inquiring about joining the OECD in July 2023 and becoming the first country in Southeast Asia to start accession talks with the OECD in February 2024.

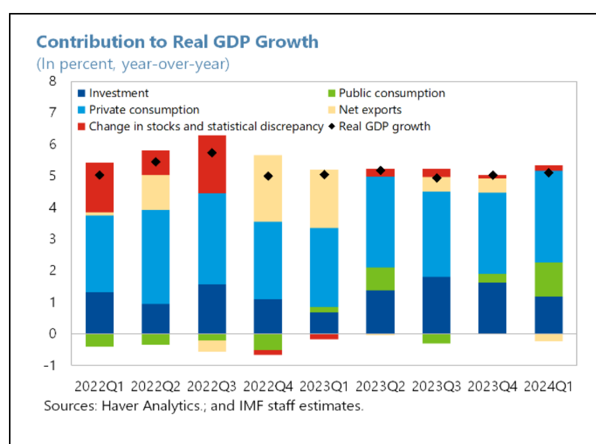
RECENT DEVELOPMENTS: RESILIENT GROWTH AND PRUDENT POLICIES AMID GLOBAL UNCERTAINTIES

Growth has proven resilient and inflation is within the central bank's target range. Policies have remained generally prudent and geared towards preserving buffers, in line with past Fund recommendations.

3. Economic growth was strong in 2023 despite external headwinds. Real GDP growth reached 5.0 percent, led by resilient private consumption and investment. Net exports lost momentum driven by falling commodity prices and trading partner demand. Economic activity indicators were robust in 2024Q1 as spending toward the February Presidential election and *Ramadan* fostered domestic demand (Figure 1). Growth was broad-based, with the mining, transportation, communication, and accommodation and food services sectors performing above historical average; however, agricultural production weakened due to *El Niño* droughts.



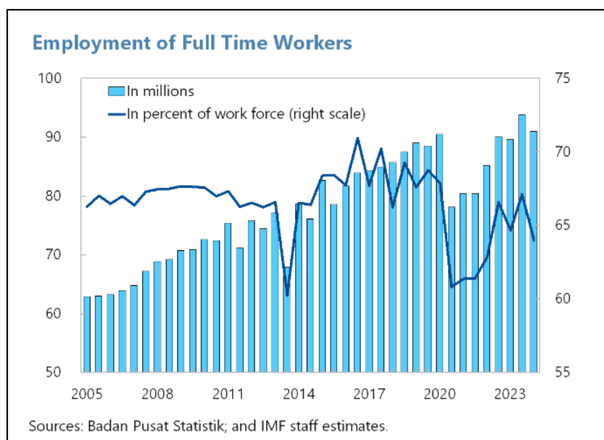
Sources: Haver Analytics; and IMF staff estimates.

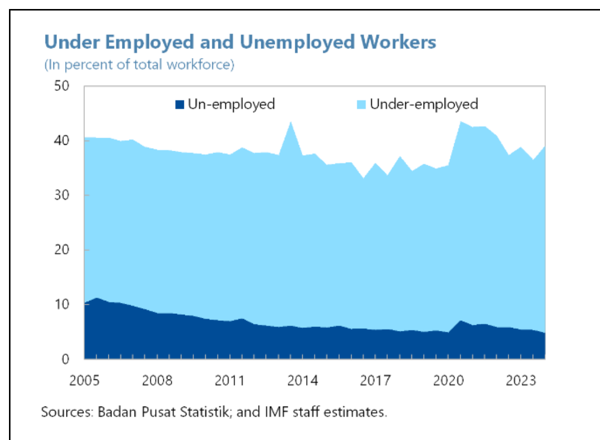


Sources: Haver Analytics.; and IMF staff estimates.

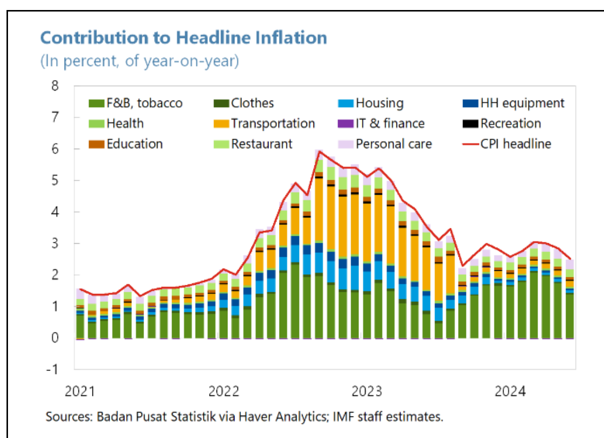
4. Economic indicators point to the persistence of some slack. The output gap is estimated to have been -0.3 percent of potential GDP in 2023, albeit with high uncertainty on the size and speed at which it is closing. Capacity utilization is yet to pick up firmly to pre-pandemic levels (73.9 percent in 2023 vs. 75.6 percent in 2019, Figures 1-2). Unemployment stood at 5.3 percent by end-2023, nearing the pre-pandemic rate (5.2 percent in late 2019). However, other measures of labor market conditions suggest some persistent, albeit declining, slack: the share of workers in full-time or formal employment is lower than pre-pandemic, the rate of under-employed workers remains higher and core inflation, while having inched up slightly (to 1.9 percent yoy in May and June, relative to 1.8 percent in April) remains below the mid-point of the inflation target range. Vulnerable employment has steadily increased since 2015.[2] Real and nominal wages have continued to recover, and most wages now exceed their 2019 levels.

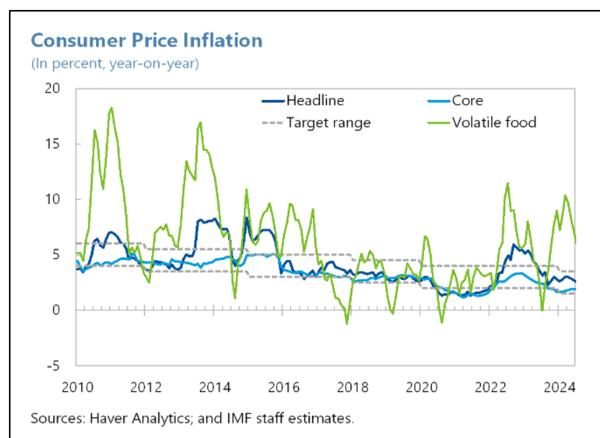
[2] The vulnerable employment estimate by the International Labor Organization (ILO) refers to the sum of (i) own-account workers (i.e., without employees) and (ii) contributing family workers (i.e., unpaid family workers).





5. Inflation is well within its target band. Appropriately tightening monetary policy settings, alongside administrative measures[3] helped bring inflation down from its 2022 surge. December 2023 core and headline inflation were at 1.7 percent and 2.8 percent respectively, within Bank Indonesia's (BI) target band (3±1 percent). Inflation indicators remain within the updated 2024 target range (2.5±1 percent),[4] with readings of 2.5 percent and 1.9 percent of headline and core inflation in June, respectively. Recent pressures stemmed from volatile components—food, beverages, and tobacco—including due to *El Niño* shock, though volatile food inflation softened in May-June. Inflation expectations remain well-anchored.

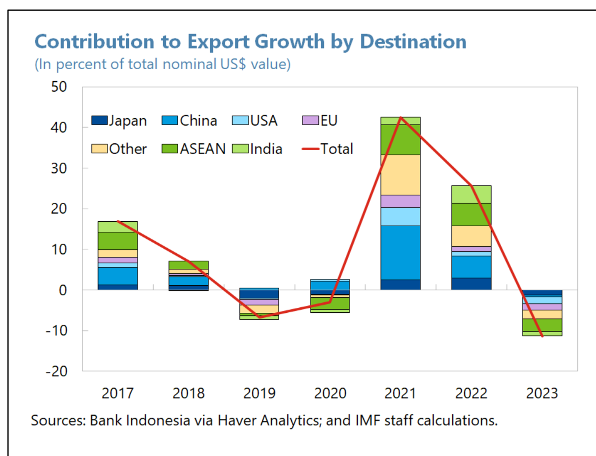




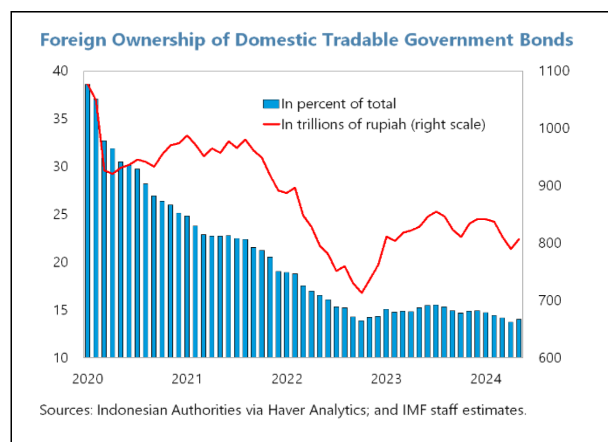
[3] The government stabilizes food prices by coordinating with ministries, the state logistics agency (BULOG), BI and trade associations. This involves: (i) monitoring of food prices, (ii) signed and monitored agreements on ceiling prices for key foodstuffs; (iii) improvement and subsidy support of ports and ship routes to relieve bottlenecks.

[4] BI's target range is defined periodically under a Cooperation Agreement between BI and the Ministry of Finance. This establishes targets for a specific period, consistent with a gradually lower inflation target over time.

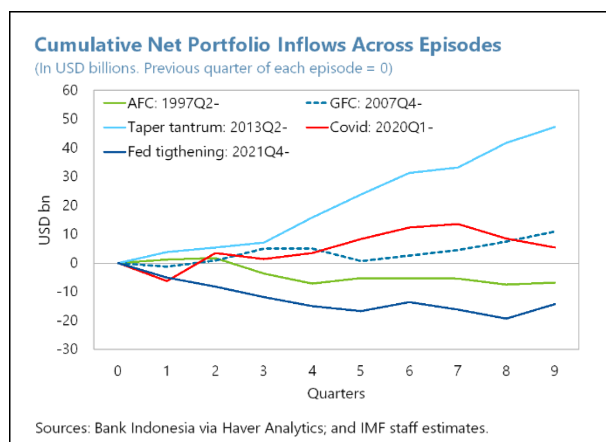
6. Indonesia's external position in 2023 was broadly in line with the level implied by medium-term fundamentals and desirable policies (Annex I). The current account (CA) balance moved from a surplus of 1 percent of GDP in 2022 to a narrow deficit (0.1 percent of GDP) in 2023, led by a broad-based decline in commodity prices (particularly affecting coal, palm oil, and mining-related exports). This was partially offset by lower import values of oil, gas, and raw materials. The services account improved slightly, as foreign tourist arrivals nearly doubled relative to 2022. Following net outflows in 2022, portfolio investment flows initiated a recovery towards end-2023,[5] which more than offset a decline in net FDI inflows, leading to a surplus in the capital and financial account in 2023 (0.7 percent of GDP), and to an overall balance of payments (BoP) surplus. However, portfolio outflows reemerged in early-2024, reflecting the heightened volatility in global financial markets.



Sources: Bank Indonesia via Haver Analytics; and IMF staff calculations.



Sources: Indonesian Authorities via Haver Analytics; and IMF staff estimates.



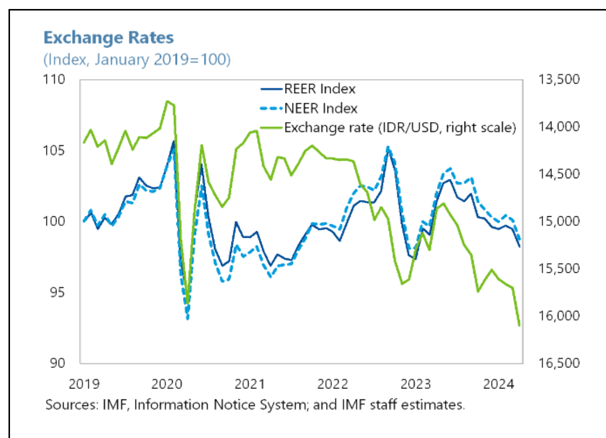
Sources: Bank Indonesia via Haver Analytics; and IMF staff estimates.

7. Foreign reserves remain adequate. Gross International Reserves (GIR) rose from US$137 billion in 2022 to US$146 billion (10.7 percent of GDP) in 2023 and are at 123 percent of the Assessing Reserve Adequacy (ARA) metric. Through 2023 and in early 2024, the rupiah has faced episodes of high volatility, largely in reaction to market uncertainties about the future path of U.S. monetary policy (including given increasingly compressed interest rate differentials with the U.S. throughout the yield curve) and the rising tensions in the Middle East. BI has responded with a mix of tools; these have included policy rate hikes of 25 bps in both October 2023 and April 2024 (with the stated objective of pre-emptively taming inflation passthrough), and foreign exchange intervention (FXI) in the spot and derivatives markets to address heightened exchange rate (ER) volatility.[6] The issuance of new BI short-term securities (in local and foreign currency) since Fall 2023 has sought to

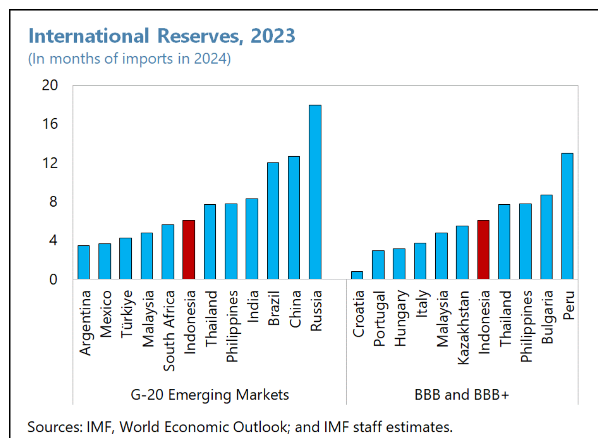
[5] The share of foreign holdings of tradable domestic government securities rose from 14.4 in 2022 to 14.9 percent at the end of 2023 but remains considerably below pre-pandemic levels (around 39 percent at end-2019).

[6] GIR declined to US$139 billion by end-May 2024, remaining within the adequacy range.

dampen pressures by deepening the market and attracting foreign investors. The authorities also made changes to the existing export repatriation requirements for commodity producers.[7] Net international reserves (NIR) strengthened by US$4.8 billion year-on-year in 2023, even as BI's short positions on FX derivatives nearly doubled through to a still moderate US$14.3 billion by end-year.[8] Indonesia's *de facto* ER arrangement is classified as floating.



Sources: IMF, Information Notice System; and IMF staff estimates.



Sources: IMF, World Economic Outlook; and IMF staff estimates.

8. Overall financial conditions remain accommodative. Standard indicators point to an accommodative financial stance amid a still open credit gap (Figure 7). Bank lending interest rates and equity prices were broadly unchanged since 2023, while house prices declined in real terms. Sovereign and corporate spreads gradually narrowed. Private sector credit by banks expanded by 10.4 percent y/y in 2023, and by 13.1 percent y/y in April 2024. This reflected a broad-based increase across types of loans, and borrowers. The authorities phased out the last remaining pandemic-forbearance measures end-March 2024.[9]

ROBUST OUTLOOK AMID BALANCED RISKS

The baseline forecasts entail a broadly positive outlook with balanced risks; medium-term prospects are solid but could be further strengthened by tackling structural priorities.

9. Growth is projected to remain high, and inflation well-anchored. Real GDP growth in 2024 is projected at 5.0 percent, supported by an increase in public consumption and investment growth offsetting the continued drag on net exports due to external headwinds (including lower commodity prices and weaker trading partner growth); the output gap would remain negative, and fully close by 2026. Growth would pick up slightly to 5.1 percent in 2025, on the back of a fiscal

[7] Government Regulation No.36 of 2023 (effective 1 August 2023), mandates that natural resource exports proceeds valued more than US$250,000 or the equivalent (fob) be repatriated and at least 30 percent (net of the exporter's FX obligations) of the repatriated funds be retained within the Indonesian financial system for at least three months; there are no currency conversion requirements; exporters may use the repatriated funds for FX swap transaction with banks or as a collateral to get IDR loans from banks if there are needs for rupiah for their domestic business activities; there are no limitations on how the exporter could use such IDR loans.

[8] A common NIR measure subtracts predetermined short-term net drains from a country's foreign currency assets; see Guidance Note (B2) of the Update of the Balance of Payments Manual 6 (BPM6).

[9] See OJK Policy Statement, March 31, 2024.

expansion. Headline inflation would stabilize around the midpoint of its updated target range. Real exports would expand at a slower pace while import growth would recover (in line with domestic demand), leading to moderate CA deficits in 2024-25. Overall, the BoP surplus would continue to increase gradually, reflecting a pickup in FDI and portfolio inflows, and supporting a further buildup of reserve buffers (Tables 1-10).

10. Near-term risks to the outlook appear broadly balanced (Annex II). They imply two-sided risks both to growth (Annex IV) and inflation.

- **Downside risks** include persistent commodity price volatility due to supply and/or demand disruptions (e.g., linked to conflicts or trade restrictions) or an abrupt global slowdown or recession in Indonesia's key trading partners (China, the U.S.). Slower-than-envisaged AE disinflation momentum resulting in higher-for-longer global interest rates, or a systemic financial instability episode (causing spikes in interest rates, risk premia, and asset repricing) could trigger capital outflows and disorderly market conditions. On the domestic side, a weakening of long-standing sound macro-fiscal frameworks could hamper policy credibility.

- **Upside risks** include stronger-than-anticipated growth in China and other trading partners or faster-than-expected disinflation in AEs leading to more frontloaded policy rate cuts by central banks, which would reinforce the growth momentum.[10] A faster and/or deeper implementation of needed horizontal structural reforms could also strengthen growth (see Section E and Structural Reform SIP).

11. Medium term growth prospects remain strong relative to regional peers, though contained by prevailing structural gaps. Medium-term growth is estimated at about 5 percent, driven by strong private consumption and investment (supported by contained inflation and the authorities' Golden Vision that foresees strong public investment in connectiveness, in particular). Lifting medium term growth beyond this, in a sustainable and durable way, would require a broad-based expansion across sectors (Section E), and a comprehensive structural reform strategy that increases productivity growth, bolsters production factors (i.e., infrastructure and a skilled workforce), tackles institutional weaknesses (including on governance and corruption), and continues strengthening global trade and financial integration. Such reforms would also reduce or overcome pandemic-related scarring,[11] and enhance resilience against structural global risks—such as those linked to the global energy transition and climate change,[12] the deepening of geoeconomic fragmentation (GEF) and the deployment of AI-based technologies.

Authorities' Views

12. The authorities broadly shared staff's views on the overall outlook and assessment of risks. In the near term, they consider growth could be stronger under the baseline, expecting a range

[10] See, for example, the World Economic Outlook WEO of January and April 2024.

[11] See 2023 Article IV Consultation, IMF Country Report No. 23/221.

[12] Such risks include natural disasters, heat stress, agricultural losses due to climate shocks as well as risks on the green transition (see the World Bank's Indonesia Country Climate and Development Report, CCDR).

between 4.7-5.5 percent in 2024 and 4.8-5.6 percent in 2025.[13] This would be driven by domestic consumption and investment. The output gap is still open and expected to close by end-2025. Over the medium term, they expect growth to gradually rise further towards the objective of 6-7 percent as a result of their transformation strategy under the 2045 Golden Indonesia Vision. Inflation remains well-anchored, reflecting BI's pro-stability monetary policy and the government's prudent fiscal stance, administered prices and supply policies, including coordinated efforts between central and local governments. The authorities remain vigilant of the risks posed by the future path of U.S. Federal Funds rate, and global geopolitical tensions that could have potential spillovers on the domestic economy, especially on the exchange rate, inflation and economic growth. The authorities, however, have reservations about domestic policy actions being a downside risk. They have consistently applied a sound macroeconomic framework and remain committed to doing so, thereby maintaining policy credibility.

POLICIES: SAFE TRANSIT TO THE GOLDEN VISION

Preserving a sound and prudent macro-fiscal framework in the near and medium term will be critical for Indonesia to achieve its long-term ambition. Development spending priorities for 2025 and beyond should be anchored by an ambitious revenue mobilization reform and accommodated well within the guardrails set by Indonesia's longstanding fiscal rule. The monetary policy stance is appropriate and should remain data-driven, based on the evolution of domestic conditions, with the exchange rate serving as a shock absorber. While Indonesia has ample policy space, this should be carefully managed to preserve buffers in a global shock-prone environment; use of FXI would be appropriate under certain shocks and conditions. Bridging structural gaps will be key to achieve higher and inclusive potential growth and reach high income status.

A. Fiscal Policy: Lifting Potential Growth while Protecting Credibility

13. Following a decisive post-pandemic consolidation, Indonesia's fiscal position further strengthened in 2023, while remaining growth friendly. In line with the country's post-pandemic fiscal consolidation path, the overall deficit narrowed from 2.4 percent of GDP in 2022 to 1.61 percent of GDP in 2023, anchored by the first primary surplus (0.5 percent of GDP) in about a decade. The outturn was below the original budget and the fiscal rule deficit cap (2.9 and 3 percent of GDP, respectively). Revenue overperformance more than offset a slight spending overrun.[14] Total spending was moderately above budget (0.2 percent of GDP), including from higher capital spending and transfers to subnational governments (SNGs). Social assistance stabilized at 0.8 percent of GDP,

[13] This incorporates overlapping ranges for the Ministry of Finance (5.0-5.3 percent in 2024 and 5.1-5.5 percent in 2025) and Bank Indonesia (4.7-5.5 percent in 2024 and 4.8-5.6 percent in 2025).

[14] As of end-2023, tax revenues from trade and manufacturing were about 50 percent of total tax revenues, while the contribution of mining activities was around 11 percent.

and the energy subsidy bill fell slightly relative to 2022. The public debt-to-GDP ratio continued its decline, reaching 39.6 percent of GDP by end-year—comfortably within the fiscal rule's public debt ceiling (60 percent of GDP).

Central Government Operations, 2022-24
(In percent of GDP, unless otherwise indicated)

	2022	2023			2024	
		Budget	MoF outlook*	Final	Budget	Proj.
Revenues and grants	13.5	11.7	12.5	13.3	12.3	13.1
Oil and gas revenues	1.2	0.9	0.8	0.9	0.8	0.8
Non-oil and gas revenues	12.3	10.8	11.7	12.4	11.5	12.2
of which VAT	3.5	3.5	3.5	3.7	3.6	3.7
Expenditure and net lending	15.8	14.7	14.9	14.9	14.7	15.4
Current expenditure	9.6	9.0	9.1	8.5	9.1	9.3
of which energy subsidies	0.9	1.0	0.9	0.8	0.8	0.8
Development expenditure	2.1	1.7	1.9	2.2	1.8	2.1
Capital spending	1.2	1.0	1.2	1.5	1.1	1.4
Social assistance spending	0.8	0.7	0.7	0.8	0.7	0.7
Transfers to local governments	4.2	3.9	3.9	4.2	3.8	4.1
Overall balance	-2.4	-2.9	-2.3	-1.6	-2.3	-2.3
Memorandum items:						
Primary balance	-0.4	-0.8	-0.2	0.5	-0.1	-0.3
Cyclically-adjusted primary balance	-0.2			0.5		-0.3
General government debt	40.1			39.6		39.5

* MoF outlook for 2023, based on draft budget (RAPBN) 2024.
Sources: Indonesian authorities; and IMF staff estimates.

14. The fiscal stance is projected to become expansionary in 2024. Following three years of consolidation, the 2024 deficit would expand to 2.3 percent of GDP, still within the fiscal rule guardrail.[15] The resulting fiscal impulse (estimated at 0.8 percentage points of GDP) implies an expansionary fiscal stance. A slightly narrower deficit would continue to support growth and protect the vulnerable while also helping preserve fiscal space to respond to downside risks. Given staff's projected revenues, containing spending to around budgeted levels for 2024 would be consistent with a somewhat less expansionary stance; efforts to enhance the targeting of energy subsidies would not only help achieve the recommended stance, while enhancing price incentives in the use of energy and protect vulnerable groups.

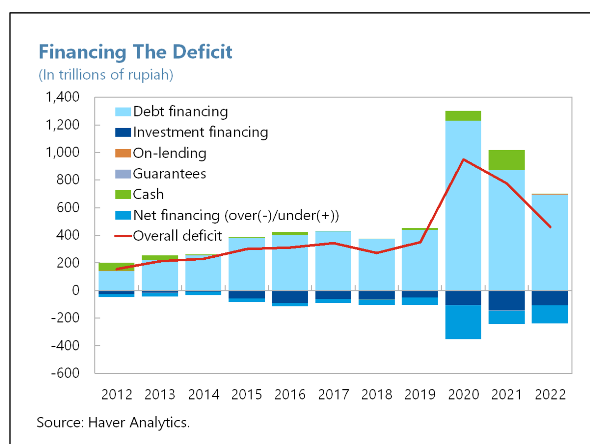
15. The fiscal stance would remain moderately expansionary in 2025, gradually consolidating thereafter—and support a stable debt-to-GDP ratio over the medium-term. The draft 2025 Government Work Plan[16] underpinning the 2025 Budget proposes a deficit of 2.45-2.8 percent of GDP, which could come close to the 3 percent ceiling. Staff projects a deficit of 2.6 percent of GDP, implying a moderately expansionary fiscal impulse (0.3 percentage points of GDP). A slightly narrower fiscal stance would be more appropriate as the output gap closes and given the need to preserve fiscal space in a shock-prone global environment. The 2025 deficit is expected to accommodate key campaign pledges by the elected administration, which would be partially offset by revenue mobilization and spending reallocation. Revenue mobilization efforts could rely on the implementation of measures (including those identified by Fund technical assistance) that would bring yields in the near and medium term (text table). This could be complemented with some spending reallocation, including from streamlined and better targeted energy subsidies. The authorities envisage the deficit to narrow from 2026 onwards to maintain public debt stable at under 40 percent of GDP. They expect a broadened tax base thanks to improved compliance enforcement to deliver revenue gains; further outlining concrete tax measures to anchor a strengthened revenue path would be important. Ongoing consideration to gradually roll

[15] Given that revenues tend to overperform, staff projects higher revenues in 2024 relative to the budget. The higher revenues, in turn, are expected to accommodate higher spending than budgeted.

[16] This is based on the "Policy Settings" for the 2025 Budget published on May 20, 2024. The final measures recommended will be defined based on this document.

in new emerging priority spending—including the "Nutritious Meal for Kids" program—and ensuring it is well-targeted and effective is welcome, as this approach would foster effectiveness while helping preserve fiscal prudence. As the authorities focus on lifting potential growth, fiscal policy should aim to provide structural support; relying on pro-cyclical support for this purpose could lead to overheating in the economy and pose a burden for monetary and external policies.

16. Fiscal and debt risks remain contained. The Sovereign Risk and Debt Sustainability Framework (SRDSF) points to an overall "low" risk of sovereign stress (Annex III); staff assess Indonesia to have some fiscal space. Aside from a generally prudent deficit path, public debt sustainability is supported by a favorable interest rate-growth differential, highlighting the importance of preserving Indonesia's good standing in global financial markets. Beyond broad fiscal prudence, strong domestic revenue mobilization efforts would help limit the debt service-to-tax ratio over the medium term. Budget financing is largely domestic, with external loans and FX-denominated government securities meeting about a quarter of the public gross financing needs (GFNs), which are moderate at around 5 percent of GDP. The share of local currency public debt held by domestic entities (excluding BI) was at 67 percent as of end-January; this limits rollover risks, but exposes banks and Non-Bank Financial Institutions (NBFIs) to sovereign debt repricing shocks, although banks appear broadly resilient (¶27). Public-Private Partnerships (PPPs), as well as below-the-line operations with state-owned enterprises are expected to rise, including to finance infrastructure (e.g., the construction of the new capital city, Nusantara). Preventing the buildup of actual and contingent liabilities related to these operations will be key to keep fiscal risks at bay.[17]



Source: Haver Analytics.

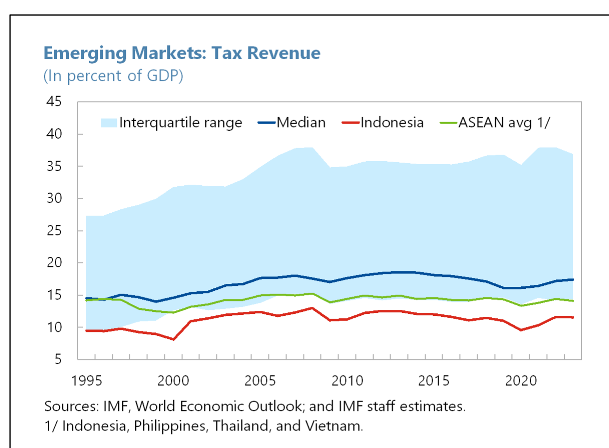
17. Indonesia's current fiscal rules are well-suited to support its ambition, especially if complemented with further fiscal structural reforms to open further fiscal space. The rules provide an appropriate, well-understood and credible framework, which can help accommodate evolving spending priorities; however, evidence on the cyclicality of Indonesia's fiscal policy is mixed (Annex VI). The deficit rule provides a sound guardrail, which should be complemented with an enhanced Medium-Term Fiscal Framework (MTFF), articulated with the annual budget and long-term fiscal plans, supporting a well-calibrated medium-term objective (MTO) set up on a (multi-year) rolling basis to help support more systematic counter-cyclical policymaking that is also compliant with the rule. Further rationalization of current spending—including energy subsidies—and measures to prioritize domestic revenue mobilization would release substantial fiscal space to support the evolving development needs within the rule, particularly given Indonesia's low tax-to-GDP ratio

[17] The government reported US$22 billion (1.6 percent of GDP) in outstanding public guarantees on infrastructure programs, including US$6.5 billion in guarantees for PPPs as of 2023Q3 (BI, Feb 2024). This compares to outstanding guarantees of US$23 billion including PPPs for US$6.4 billion as of 2022Q3 (BI, Feb 2023). The actual stock of PPPs is estimated at US$22 billion (1.3 percent of GDP).

(below). While the debt cap (60 percent of GDP) is also broadly appropriate and Indonesia's debt-to-GDP ratio is low, its debt-service is high (at about 2 percent of GDP), and the share relative to public revenues is higher than peers (Figure 5). Bringing the fiscal deficit close to its ceiling on a protracted basis could erode fiscal space through rising debt service payments; this highlights the importance of securing upfront tax revenue mobilization.

18. A comprehensive medium-term fiscal structural strategy would be critical to help achieve Indonesia's ambition, both to secure fiscal resources to boost spending while keeping a sound macro-fiscal stance, and to deploy them in an effective, transparent, and targeted manner.

- ***Revenue Mobilization***. Indonesia's tax-to-GDP ratio has been persistently low and lags that of EM peers. The elected administration has pledged to raise total revenue by 10 ppts from 13 percent of GDP, although detailed measures and timelines are yet to be specified. Proposals include establishing a new National Revenue Agency (NRA) and improving collection processes through digitalization.[18] Plans to establish NRA should be carefully designed, as such restructuring may prove costly; achieving net gains in tax collections will require tackling the fundamental tax administration gaps. International experience shows that enhancing key aspects of revenue administration—including compliance risk management (CRM), the use of third-party data, digitalization, broadening taxpayer bases, and securing appropriate staffing—would be important (Annex VII). Revenue efforts should also encompass an ambitious tax policy reform; besides fully implementing the 2021 Tax Harmonization Law, it would be critical to update the Medium-Term Revenue Strategy (MTRS)—including by further strengthening direct and indirect taxes, and minimizing leakages from tax incentives.[19] Revisiting existing tax expenditures (currently estimated at 1.7 percent of GDP) and ensuring that tax holidays and incentives remain limited will be critical to prevent the erosion of the tax base and secure improved tax revenues over the medium term.[20]



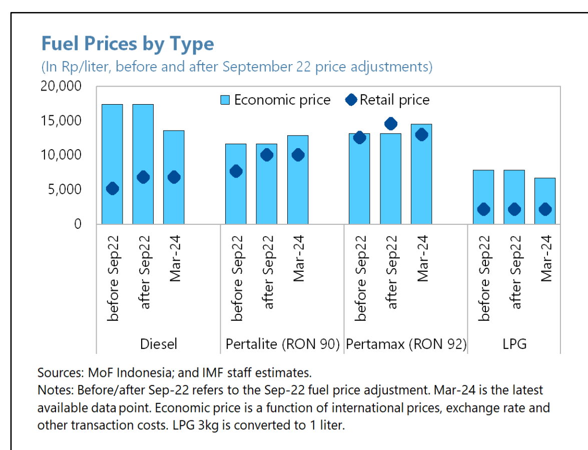
Sources: IMF, World Economic Outlook; and IMF staff estimates.
1/ Indonesia, Philippines, Thailand, and Vietnam.

[18] The authorities plan to expand the tax base by strengthening compliance and improving tax administration. They are also assessing a range of tax policy measures based on their distributional and economic impact.

[19] The IMF previously advised on a MTRS which has been partially implemented; more recent technical assistance is providing further options. See Appendix V of the 2022 AIV Staff Report (Country Report No. 2022/084) and Appendix IV of the 2020 AIV Staff Report (Country Report No. 2021/046).

[20] Tax expenditures are linked mostly to VAT (by tax type), households (by beneficiary), and the processing industry (by sector) (MoF Tax Expenditure Report 2022). The mining sector accounts for only 1 percent of total tax incentives on average, while the processing sector (including downstreaming activities) accounts for 24 percent of total incentives on average (~0.4 percent of GDP annually).

- ***Expenditure policy***. Efforts to help achieve the Golden Vision could include broadening the coverage and adequacy of social protection programs (which are low compared to peers); and moving from commodity- to people-based assistance (see 2023 Article IV Consultation). Boosting the quality of health and education spending and addressing infrastructure gaps are also important (section E). An energy subsidy reform, including via a more automatic alignment of retail fuel prices with international prices, would open space to attend these needs.[21] Stated plans by the elected administration to enhance efficiency via better targeting of subsidies are welcome.



Tax Reform Measures

	2017 MTRS	2021 Tax Reform[1]	2024 Fund TA (forthcoming)	Potential Revenue Gains[2]
Tax Policy	**3.5**			
VAT	**1.8**			
Remove certain exemptions	0.2	done		-
Reduce registration threshold	0.2	pending		0.2
Replace STLG with VAT and vehicle excise	0.6	pending		0.6
Increase in the standard rate by 2 percentage points	0.8	+1ppt in 2022		0.4
Excises	**0.5**			
Introduce new excises on fuel	0.5	pending		0.5
Add excises on plastic	-	some progress		-
Reform of tobacco taxation			0.7	0.7
Non-tobacco reforms (excluding fuels)[3]			0.8	0.8
CIT	**0.4**			
Reduce SME threshold	0.1	pending		0.1
Introduce alternative mimimum tax	0.3	pending		0.3
Reform small business regime and incentives[4]			1.4	1.4
PIT	**0.4**			
Broaden base (include middle class, increase progressivity)	0.4	new PIT bracket		0.4
Reduce basic allowance; reduce top income tax bracket.[5]			0.4	0.4
Property tax	**0.3**			
Reduce transaction tax and increase property tax	0.3	pending		0.3
Carbon tax	-	IDR 30 or higher/kgCO2		
Tax Administration	**1.5**	some progress		-
Compliance improvement programs (VAT, high income individuals)				
Institutional reforms (organization, IT)				
Total Revenue Gains from Pending Tax Policy				**6.1**

Source: IMF staff estimates based on previous country reports (CR 22/84, CR 21/46, CR 19/251), 2017 MTRS Fund TA, and Fund TA (forthcoming).
1/ Tracks implementation of measures from 2017 MTRS.
2/ Potential revenue gains over the medium term in percent of GDP. Estimated as sum of pending tax policy measures from the 2017 MTRS (i.e. not implemented yet in the 2021 Tax Reform) and measures from the 2024 Fund TA (forthcoming).
3/ Revenue potential through comparison with international peers.
4/ Rough estimate based on average CIT productivity in comparator counntries.
5/ This entails a reduction in the threshold above which the highest rate of 35 percent applies.

[21] A semi-automatic pricing formula was introduced in 2015, based on an international oil price index, exchange rate and other tax and distribution costs. Adjustments ceased in 2017-18. Energy subsidy reform is discussed in Chapter 7 of *Indonesia: Selected Issues* for the 2020 AIV Staff Report (Country Report No. 2021/047).

- ***Fiscal and Debt Risk Management***. Given the gradually rising portfolio of PPP and public guarantees to support infrastructure development, fiscal risk management should be enhanced in line with recent Fund TA advice. In the short-term, PPPs may create relief in terms of government budget outlays but have long-term fiscal implications and can affect fiscal and debt sustainability. Enhancing the currently fragmented process to evaluate PPPs and issue fiscal guarantees by providing the MOF a stronger 'gatekeeping' role is needed. Continuing to strengthen the fiscal accounts to ensure they provide a comprehensive view of fiscal activities of the general government (GG) activities and of implicit liabilities will be key to keep fiscal risks at bay.[22, 23]

- ***Decentralization***. Indonesia's fiscal decentralization has steadily gained momentum, with important mandates devolved to SNGs since 2000. Recent 2022 legislation seeks to strengthen SNG taxation and spending outcomes, minimize vertical and horizontal fiscal imbalances, and optimize public service delivery. PFM weaknesses remain, including execution gaps (e.g., SNGs often carry forward unspent resources from inter-governmental transfers). SNG tax bases are narrow, and limit the scope to raise local revenues. Tackling these gaps will be critical for SNG's to support the achievement of Indonesia's goals soundly and effectively.

Authorities' Views

19. The authorities underscored that fiscal policy would remain prudent in the near term. They broadly shared staff's baseline assessment on the fiscal stance in 2024-25. They indicated that they have flexibility for adjustment, thanks to built-in automatic spending adjustment mechanisms that can be used to release fiscal space, as well as budget contingencies deployed if near-term downside risks materialize. The preliminary underpinnings for the draft 2025 budget prioritize capital expenditure to support durable growth. Potential new spending priorities—including the "Nutritious Meal for Kids" program—would be decided by the new administration but the authorities expect these to be rolled out gradually and accommodated well within the 3 percent deficit limit via expenditure reprioritization—this may include enhancements in the targeting of energy subsidies. They agreed that strengthening tax revenues is crucial for bolstering fiscal space and are analyzing a menu of tax measures based on their economic and distributional impact, as well as enhancements to the revenue administration. They considered that their financing and debt management strategy has served them well, while noting that it remains flexible, including to opportunistically tap into cheaper foreign financing.

20. The authorities remained committed to preserving fiscal policy credibility over the medium term. They saw the 3 percent deficit ceiling as an important policy anchor that has contributed to macro-stability. They saw merit in complementing the rule with an enhanced

[22] Investments to SOEs in the form of equity injections to accelerate infrastructure development should be recorded as below-the-line financing. Transfers to SOEs to cover losses, however, should be classified above the line as capital transfers if the receiving SOE is a market entity, or as capital grants if it is a government unit (i.e., non-market SOE) under the Government Finance Statistics Manual (GFSM) 2014, and reflected in the deficit and debt levels.

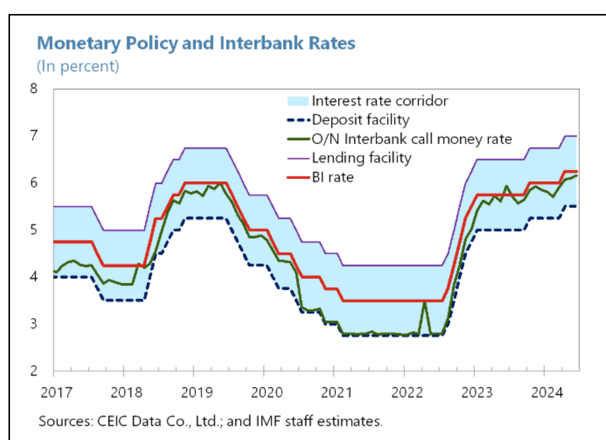
[23] If a statutory body or SOE is determined to be a non-market unit then it needs to be consolidated it as part of the GG (as an extrabudgetary unit) according to the GFSM 2014.

medium-term fiscal framework. They broadly concurred with staff's assessment of fiscal risks and debt sustainability and agreed that boosting fiscal revenues will be key to accommodate development spending within the guardrails of the fiscal rule. The authorities argued that tax incentives provide important support to the development of higher value-added activity under the growth agenda. They agreed that developing a credible roadmap for identifying and addressing tax administration gaps should be a priority for the new administration. They remained committed to keeping fiscal risks contained through enhanced management, including in the context of PPPs and below-the-line equity injections to compensate SOEs for quasi-fiscal operations.

B. Monetary Policy: Securing Price Stability

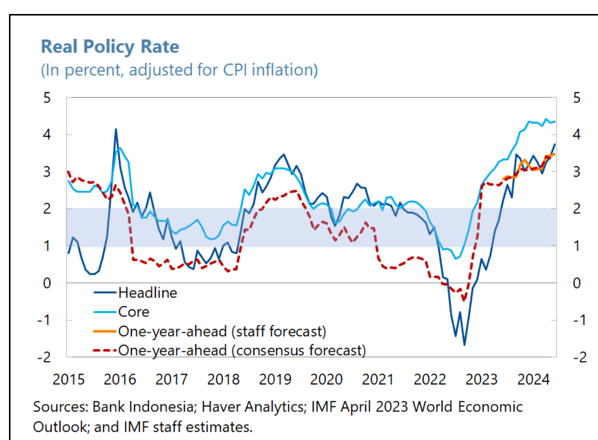
21. The monetary policy (MP) stance remains broadly adequate. Bank Indonesia (BI) hiked the policy rate by 25 bps in April 2024 to 6.25 percent—following a 25 bps off-cycle hike in October 2023. The two rate hikes were intended to fend-off possible imported inflation pressures from rupiah depreciation in the context of geopolitical tensions (including in the Middle East) and heightened external monetary policy uncertainty, including from higher-for-longer policies in AEs contributing to increasingly narrow interest rate differentials and the global US dollar appreciation. The real policy rate is above its estimated neutral level of 1-2 percent. With financial risks contained, macroprudential policy (MPPs) has been kept accommodative to support credit growth, and liquidity remains comfortable. The authorities have noted that their policy path would remain cautious given external risks. Given persistent uncertainties, the MP path should remain data-driven and supported by a flexible ER serving as a shock absorber. With inflation further softening in May and June, and absent significant shocks that raise inflationary pressures, gradually easing the monetary policy stance would seem appropriate. A tighter-than-baseline monetary policy path may be warranted if upside inflation risks begin to materialize, including because of a more expansionary fiscal policy stance than currently expected. If inflation falls faster than envisaged—e.g., due to a larger or more protracted than estimated output gap—a faster pace of interest cuts may be warranted. Continued clear communication of the outlook for monetary policy and the overall policy mix will help markets navigate uncertainties and would further anchor inflation expectations.

Monetary Policy and Interbank Rates
(In percent)



Sources: CEIC Data Co., Ltd.; and IMF staff estimates.

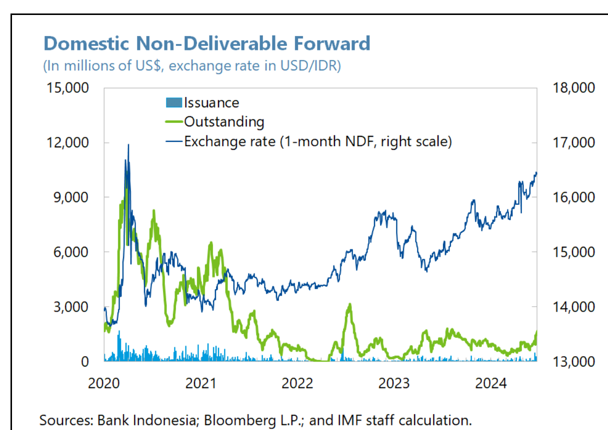
Real Policy Rate
(In percent, adjusted for CPI inflation)

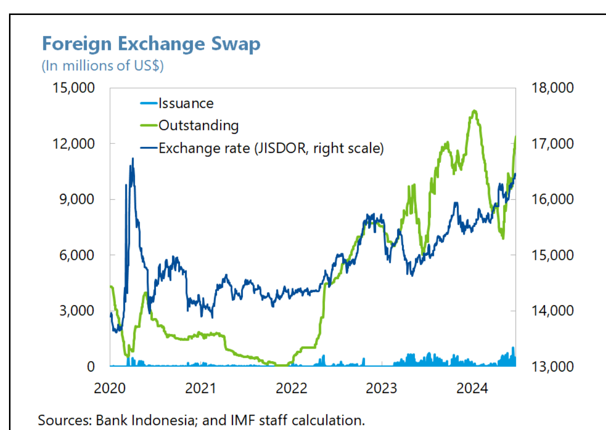


Sources: Bank Indonesia; Haver Analytics; IMF April 2023 World Economic Outlook; and IMF staff estimates.

22. The ER should continue to play its role as a shock absorber. With Indonesia's inflation expectations well-anchored and low FX balance sheet mismatches, the shallow FX markets remain

the most relevant friction under the Fund's Integrated Policy Framework, IPF (2023 Article IV Consultation, and Section D and Annex X below). Continued ER flexibility would help deepen domestic markets (¶23). FXI is a warranted component of the policy response under certain shocks and circumstances. BI indicated its decision to use FXI in the spot and derivatives markets in the external stress episodes of October 2023 and April 2024. These episodes took place in the context of rising UIP premia. While FXI data is not public, significant movements of the ER during both episodes, along with monetary policy rate hikes, point to the authorities pursuing multiple channels of adjustment. Indonesia's reserves are within the ARA range, and while NIR has declined somewhat since end-2023, BI has appropriately unwound FX derivatives following strain episodes. Exploiting risk-on episodes to further replenish reserve buffers is welcome. The 2023 change to the export repatriation regulation is assessed as a Capital Flow Measure (CFM) under the Fund's Institutional View on the liberalization and management of capital flows. The macroeconomic impact has been modest (at around ½ percent of GDP in GIR); data thus far point to exporters holding marginally more than strictly required, likely reflecting the convenience of new instruments with attractive returns and fiscal incentives. Staff recommends that the authorities gradually phase out this measure, with due regard to market conditions.





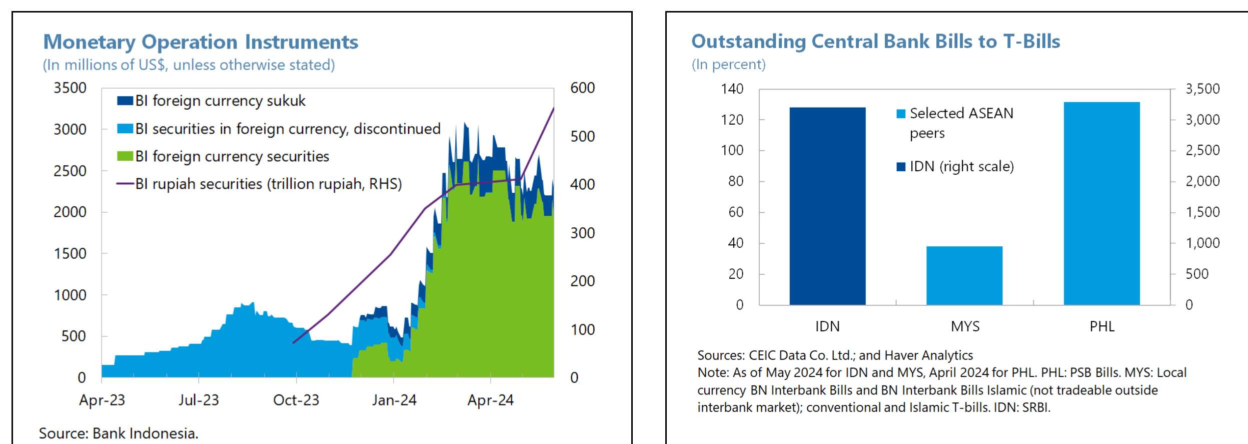
23. BI's efforts to foster market development and enhance reserve buffers could be bolstered to enhance policy effectiveness. In 2023, BI introduced a short-term local currency instrument (SRBI) and mirroring FX-denominated open market instruments to facilitate money market development and attract capital flows into the short-end of the curve. The outstanding stock of the SRBI—which BI utilizes to pursue its "pro-market" open market operation strategy to affect yields (Figure 6)—stands at about IDR 558 trillion (US$34 billion), of which some 73 percent was held domestically, as of end-May 2024.[24, 25] The outstanding stock of SRBI has grown significantly larger than the stock of T-Bills (about IDR 17 trillion).[26] The domestic money, government securities, and FX

[24] BI phased out in September 2023 its "Operation Twist", which involved selling short-term and purchasing long-term government bonds, with tenors of five years and above. This was explicitly designed to raise yields in the front sector of the curve to make it more attractive to non-resident investors. The SRBI is intended to influence government bond yields at the short-end in a market-based manner.

[25] The outstanding stock of the new FX instruments is moderate.

[26] The ratio of SRBI to T-Bills is large when compared to similar ratios for regional peers where both the central bank and government issue at the short end of the curve, though the stock of T-Bills has been declining since 2018.

markets still present some segmentation, calling for BI's relatively frequent and broad presence. Further developing markets while preserving stability will require allowing for strengthened price discovery and an increasingly market-determined term structure of rupiah interest rates. While any FXI use will need to balance multiple considerations, an important benefit of a restrained approach to FXI would be to further raise incentives for private sector hedging and FX market deepening.



Source: Bank Indonesia.

Sources: CEIC Data Co. Ltd.; and Haver Analytics
Note: As of May 2024 for IDN and MYS, April 2024 for PHL. PHL: PSB Bills. MYS: Local currency BN Interbank Bills and BN Interbank Bills Islamic (not tradeable outside interbank market); conventional and Islamic T-bills. IDN: SRBI.

24. Clarifying BI's role in crisis situations would continue to safeguard MP independence and predictability. BI has phased out its pandemic-era primary market purchases of government securities. The framework for future such purchases has been clearly restricted by the Financial Sector Omnibus Law (FSOL) to crisis episodes. Looking forward, ensuring that implementing regulations are in line with international best practices to maintain central bank independence and price stability would be key. Safeguards include ensuring any such purchases are made voluntarily at the initiative of the central bank.[27] With part of the stock of pandemic bonds starting to fall due, careful management would help avoid market disruptions as it unwinds.

Authorities' Views

25. The authorities view the monetary policy stance as broadly neutral. It maintained inflation and Rupiah exchange rate stability. They underscored that, in line with BI's Policy Mix framework, the monetary policy stance is not determined only by the policy rate, but also by the policy settings to maintain adequate liquidity—including MPP. In conjunction with BI's policy stance, the monetary liquidity conditions are loose as reflected in ample liquidity, thus supporting conducive lending rates and accelerating intermediation in various sectors. The MPP stance, in the context of a negative credit gap and contained financial risks, has supported intermediation to high-priority sectors. The authorities intend to maintain the data-driven approach in monetary policy to guard Rupiah stability. BI is pursuing a pro-market strategy for deepening of liquidity in both rupiah and FX markets, further portfolio inflows, and strengthen policy transmission effectiveness. This strategy includes the introduction of the SRBI, and is aligned with the Blueprint for Money Market Development (BPPU) 2025. The authorities view the FSOL as building adequate safeguards to limit

[27] Tobias Adrian; Christopher J. Erceg; Simon T Gray; Ratna Sahay "Asset Purchases and Direct Financing: Guiding Principles for Emerging Markets and Developing Economies during COVID-19 and Beyond," IMF, October 2021.

primary market purchases by BI to handling financial system instability caused by crisis conditions. The implementing regulations will be prepared under the principle of 3T (targeted, temporary, and transparent) to further ensure central bank independence. Regarding the maturing bonds purchased during the pandemic, the authorities will ensure that the unwinding process is conducted in a gradual and orderly manner to avoid market disruptions.

26. The authorities disagreed with the classification of the export repatriation regulation as an outflow capital flow measure (CFM). The regulation change is not aimed at managing cyclical capital flows, but at addressing structural issues by ensuring the earnings from Indonesia's natural resource exports are available as part of the FX liquidity in the banking system to support the country's economic resilience, economic growth and welfare. The regulation has been designed to avoid disruptions to exporters' activities, as it applies to FX earnings net of FX obligations. The authorities have also introduced several financial instruments, alongside fiscal incentives, to make repatriating funds attractive. They view the repatriation requirement as instrumental in shifting exporters' perspectives and incentives to place the FX export proceeds onshore, thereby contributing to the deepening of the domestic financial market. They have underlined that the measure will be periodically assessed and refined as needed.

C. Financial Sector Policies: Preserving Stability and Supporting Growth

27. The financial system is broadly resilient; systemic risk is assessed as moderate and broadly unchanged from last year (2024 FSAP). Banks dominate the financial system, are profitable, and their capital buffers and liquidity coverage ratios remain well above regulatory minima. Credit growth has recovered to pre-pandemic rates. A tightened "bank-sovereign nexus"—due to holdings of sovereign bonds and SOE lending—poses risks, but banks appear resilient. There has been progress in implementing the 2017 FSAP recommendations (Table 12). The financial system is broadly resilient to solvency risks from contagion and to system-wide liquidity stress. The authorities should expand data coverage of key interlinkages to enhance monitoring as the financial system develops. These include banks' cross-border exposures, institution-level NBFI-bank exposures, and bank-NFC linkages.

- ***Banking sector***. Overall resilience rests on strong capital and liquidity buffers; though there are pockets of vulnerability for small banks in adverse scenarios. Liquidity Coverage Ratios (LCRs) should be made mandatory for all banks, and FX risk monitoring further enhanced. Non-Performing Loans (NPLs) are low at 2.3 percent of total loans (April 2024); further strengthening guidance and supervision should help ensure NPLs are recognized on a timely and full basis, including following the phasing out of the pandemic forbearance, which will also help contain the risks of zombification (Annex VIII).

- ***NFCs***. NFCs appear resilient and overall vulnerability indicators have strengthened (Annex VIII). Weaknesses remain in sectors hard-hit by the pandemic and amongst smaller publicly listed firms. The persistence of unproductive and unviable (zombie) firms, however, may delay a necessary creative destruction and negatively affect the prospects for long-term productivity growth. Although the share of listed zombie firms seems to have declined recently, it remains

above pre-pandemic levels, while also standing somewhat above other regional peers. More generally, NFCs' external debt exposures have fallen from 16.8 in 2015Q3 to 8.5 percent of GDP at end-2023—a notable improvement relative to peers. The authorities' prudential FX and liquidity policies have helped contain FX exposures, which are closely monitored.[28] Expanding granular data coverage of large firms (listed and non-listed) as well as small and medium enterprises (SMEs) will support monitoring and risk assessment.

- ***Households***. Household leverage is low, with debt-to-GDP at 16.3 percent (2023Q3). About 30 percent of bank lending is to households, about 2 percent of which are NPLs. Given the sector's ongoing expansion—including via mortgages—further strengthening the monitoring of loans to households by expanding indicators (e.g., LTV and DSTI for origination and outstanding stocks of household debt) and assessing risks across the income distribution would support the identification of emerging vulnerabilities.

- ***NBFIs***. The sector is small (about 24 percent of the financial system's assets in 2023), with limited interconnectedness. However, risks are rising for the insurance sector due to inadequate premium management and risk transfer practices. As the NBFI sector and its interconnections could grow rapidly with financial deepening efforts, it would be prudent to develop a framework to understand and reduce future systemic risks.

28. Recent financial sector reform has entailed substantial progress; some areas could be further strengthened. Enhancing independence of the financial supervisor (OJK) and the resolution authority and deposit insurer (LPS), and providing clarity on OJK's primary supervisory objectives is important. Further enhancing supervisory effectiveness, for example by continuing to improve the risk assessment methodology, better integrating certain supervisory activities, and intensifying scrutiny in assessing corporate governance and risk management practices, would be welcome. Bolstering the financial safety net, crisis management, and systemic liquidity frameworks is needed; the resolution framework should be further aligned with the Financial Stability Board's (FSB) Key Attributes.

29. BI actively relies on a broadly defined MPP toolkit, which could be shifted to a more neutral stance as the credit gap closes. BI's toolkit reflects a three-pronged strategy for MPP: financial system resilience, balanced and sustainable intermediation, and financial inclusion. Clarifying that financial system resilience is prioritized as BI calibrates the broad toolkit, including whenever the three objectives may compete with each other, would be important. Separating the elements of the current toolkit which do not have financial resilience as their main focus (e.g., into a *sustainable and balanced-growth* toolkit), would strengthen effectiveness and foster clear

[28] There are prudential regulations that limit banks' net open FX positions and corporates are subject to a minimum hedging requirement of 25 percent that applies to their short-term net foreign currency liabilities with a maturity up to 3 months and between 3-6 months, and a minimum FX liquidity ratio of 70 percent that applies to their liquid foreign currency assets as share of short-term foreign currency liabilities (with maturities less than three months). The hedging and liquidity requirements on non-financial corporates have been assessed as both capital flow management measures as well as macroprudential policy measures (i.e., CFM/MPMs) under the Fund's Institutional View. The authorities have advised that this measure is not a CFM, and moreover, that the classification of this measure as an MPM does not correspond to the definitions within their own MPP toolkit.

communication. BI's current accommodative MPP stance is intended to foster sustainable credit and economic growth in the context of contained financial risks, and help counterbalance a monetary policy rate setting geared towards safeguarding rupiah stability. Looking forward, with potential downside macro-financial risks on the horizon (Annex IV), gradually shifting MPPs towards a more neutral stance as the credit gap closes would help contain the build-up of risks, further supporting the banking system's strong capital and liquidity positions. This, alongside the recommended narrower-than-projected fiscal deficits and gradual reductions to the monetary policy rate, would support an appropriate rebalancing of the overall policy mix.

30. Financial digitalization has grown fast since the pandemic, assisted by the authorities' development efforts. BI established the Indonesia Payment System Blueprint (BSPI) 2025 to support the digitalization agenda, which includes the introduction of standardized QR codes (QRIS) in 2019 and modernized real-time payment system (BI-FAST) in 2021. The expansion of financial digitalization has been broad (e-money, mobile banking, fintech P2P lending and digital investment), albeit from a small scale. Continued efforts to narrow digitalization and financial literacy gaps would support P2P lending growth (Annex IX). OJK should continue strengthening the regulatory and supervisory approach to new financing models to ensure business resilience and consumer/investor protection. The authorities should develop adequate cooperation arrangements for the regulation and supervision of information technology-based financial services, consistent with the FSOL.

31. The authorities should continue addressing the outstanding gaps in their Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) framework. The 2023 Mutual Evaluation Report by the Financial Action Task Force (FATF) of Indonesia's AML/CFT regime found the legal framework is strong and broadly effective. Key areas for further progress include improving risk-based supervision for non-financial sectors, imposing effective and dissuasive sanctions in all sectors, and applying targeted financial sanctions for terrorist financing-related activities. It will also be important to ensure that accurate information on ultimate beneficial owners of legal persons is available to law enforcement.

Authorities' Views

32. The authorities agreed with staff that systemic risks are well contained. They continue to carefully monitor risks to the banking sector and undertake regular stress tests. As per regulations, banks continue timely and complete reporting each month of their financial positions, including NPLs, which has helped ensure asset quality is accurately reflected as the forbearance measures were removed. The authorities agreed with staff that the risks from cross-sectoral and cross-border exposures are contained, and agreed that BI's and OJK's ongoing collaborative efforts to strengthen the monitoring of such interlinkages will ensure resilience as the financial system further develops. OJK has taken steps to resolve risk management practices in the insurance sector. The authorities underlined the importance of continuing to strengthen the AML/CFT regime. They also stressed their efforts in enhancing financial literacy and inclusion, including by closing the digital divide and enhancing the regulatory and supervisory framework.

33. The authorities emphasized that safeguarding financial stability is the ultimate objective of macroprudential policy (MPP). They noted that BI's three-pronged MPP strategies

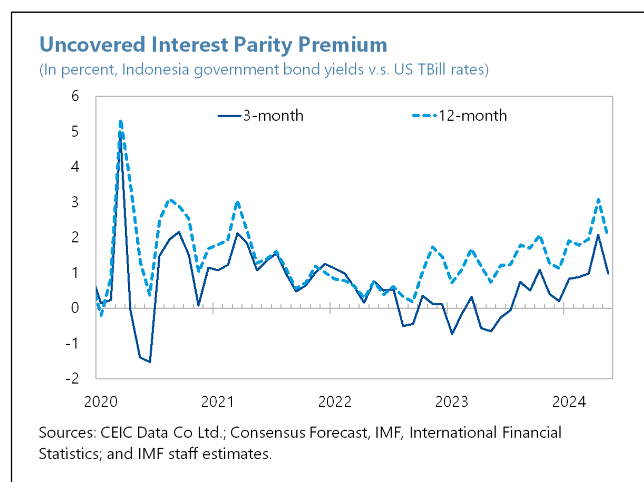
complement each other in maintaining financial stability as outlined by Warjiyo and Juhro (2019), namely through: (i) the *balanced intermediation* strategy, which addresses procyclicality that reflects time varying and countercyclical dimensions; (ii) the *financial resilience* strategy, which mitigates systemic risks associated cross sectional dimension that is associated with interconnectedness, potential spillovers and contagion, as well as common risk factors within the financial system; and (iii) the *financial inclusion* strategy, which supports financial stability by diversifying economic participation of broader economic segments, thereby reducing concentration risk and strengthening financial system structure.

34. The authorities see this framework as particularly relevant in the domestic context. This is evidenced by its support of the financial sector's stability during the pandemic, aligning more closely with the broader context of emerging markets than the narrower definition provided by the IMF. Furthermore, these policy strategies are mandated by the FSOL, which represents a milestone in financial sector reform initiated consensually by financial sector authorities. The robust framework embodies important lessons learned from concerted efforts during the pandemic to strengthen financial stability and mitigate future financial crisis.

D. Policies to Manage Near- and Medium-Term Risks

Indonesia will need to navigate a more shock-prone world. Potential adverse shocks, including those emanating from the two largest economies—China and the U.S.—could have significant spillovers through trade, commodity prices, and financial markets. Identifying the appropriate policy mix to address emerging shocks would depend on the specific nature of the shock, the economy's structural characteristics and frictions, and the need to preserve buffers.

35. Indonesia has strong fiscal and financial buffers—as well as robust policy frameworks—to respond to adverse shocks. If downside risks materialize, the available fiscal space can be used in a targeted way to preserve priority development spending, including to support the vulnerable. Inflation is well-anchored and financial sector risks contained, leaving scope for monetary policy to balance risks to inflation, output, and financial stability. In the context of an integrated policy framework (IPF), appropriately adjusting the standard macroeconomic policy settings and allowing the ER to play a shock absorbing role will be key (Annex II).



Sources: CEIC Data Co Ltd.; Consensus Forecast, IMF, International Financial Statistics; and IMF staff estimates.

36. The assessment of Indonesia's key frictions remains unchanged from that in 2023—centering on the persistence of shallow FX markets.[29] These may warrant the use of FXI in response to shocks triggered by

[29] Indonesia does not appear to face significant frictions related to unhedged FX balance sheet exposures and has well anchored inflation expectations (see 2023 Article IV, Appendix V).

sudden changes in investor risk appetite that could lead to capital outflows and large ER depreciation, exemplified by a sharp increase in the country's uncovered interest parity (UIP) premium. UIP premia have risen in Indonesia through 2023 and early 2024, reflecting the impact of global uncertainties in the domestic market.

37. A model-based analysis is used to help gauge the appropriate policy mix that could help Indonesia tackle possible downside scenarios (Annex X). The analysis focuses on a subset of risks—adverse growth shocks in China or policy shocks in the U.S., which may impact Indonesia through worsening terms of trade (including lower prices for Indonesia's commodity exports), and potentially trigger risk-off shocks. The appropriate policy response will need to be calibrated to the nature and duration of the shock, supported by enhanced communication, with FXI appropriate in the context of risk-off episodes. While inflation expectations are well-anchored and currency mismatches on private sector balance sheets contained, FXI may also be warranted in the face of large shocks that trigger severe depreciation, which if not moderated, could set off non-linear responses for inflation and threaten financial stability.[30]

38. The use of fiscal and reserve buffers will need to keep future needs in mind. Preserving buffers and keeping some powder dry will be particularly important in a world where GEF is likely to lead to a prolonged period of more frequent and volatile external shocks, including to capital flows and commodity prices.

Authorities' Views

39. The authorities agreed with staff's assessment on the need for carefully designed policy responses in the face of external volatility. They also underscored Indonesia's well-established track record of prudently navigating shocks and strong policy buffers. BI's policy mix, combined with fiscal efforts if needed, has the necessary instruments to address external stress while protecting domestic stability. The authorities appreciate staff's continuing engagement on the IPF. Alongside the conditions described in staff's simulations, they view FXI as also warranted based on early pressures on the FX market given substantial uncertainties faced by policymakers in determining the nature and duration of the shocks in real time, and the risks of non-linearities that could affect expectations. Integrating MPPs as an important part of the toolkit to sustain optimal intermediation while safeguarding financial stability, should be considered in staff's analysis as well.

E. Achieving High Income: A Structural Reform Program

40. Achieving the Golden Vision and reaching the high-income status by 2045 will require growing high, for long. Estimates suggest that reaching this goal will require an annual nominal GNI growth rate of 8 to 9 percent, roughly equivalent to 6-7 percent real annual growth (assuming annual inflation around 2 percent), sustained over two decades (see text chart for details).

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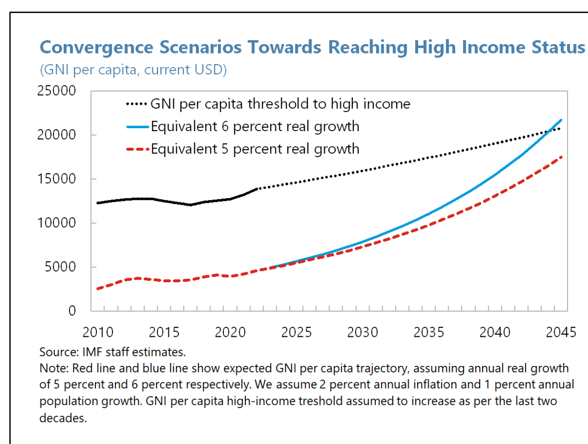
[30] For example, Caselli and Roitman (2019) find that the rate of exchange rate passthrough becomes non-linear when the exchange rate depreciates by more than 24 percent in a sample of EMs.

41. Comprehensive horizontal structural reforms are essential to bridge important gaps and help meet Indonesia's ambitions for strong and broadly shared growth (see Structural Reform SIP).



Convergence Scenarios Towards Reaching High Income Status
(GNI per capita, current USD)

Source: IMF staff estimates.
Note: Red line and blue line show expected GNI per capita trajectory, assuming annual real growth of 5 percent and 6 percent respectively. We assume 2 percent annual inflation and 1 percent annual population growth. GNI per capita high-income treshold assumed to increase as per the last two decades.

- ***Strong and sustained growth episodes have typically been accompanied by broad improvements in structural areas***. Historical evidence indicates that prolonged high-growth and fast income convergence episodes were underpinned by: (i) sound and robust structural initial conditions, and (ii) improvement in horizontal structural areas along the convergence process. Analysis reveals Indonesia's structural gaps in areas such as governance, infrastructure, human capital, labor resilience, export complexity, and economic openness, compared to both its current peers and where these historical success growth cases started (SIP and Box 1).

- ***Horizontal structural reform can have a positive, significant effect on output***. Regression analysis provides further evidence that packaging reforms yields better output outcomes, human development aspects are key to boost growth (for EMs and AEs), and a major "first-generation" structural reform package[31] could raise output levels by around 1.5-2 percent after two years, relative to baseline (i.e., would help to bring annual growth up to around 6 percent from the current 5 percent). These results point to key reform priorities and a possible sequencing of structural reforms in Indonesia (Box 1, Table).

42. Facilitating private sector activity will be essential to lifting potential output growth. Supporting Indonesia's attractiveness to FDI would help mitigate GEF risks: securing transparent, simple, and predictable investment and business frameworks could build resilience against reshoring pressures and attract new investment flows. In addition, there is a critical role for the domestic private sector to support inclusive, broad-based growth. More agile and productive NFCs could further contribute to raising growth. In addition, micro, small, and medium enterprises (MSMEs) are estimated to contribute over 60 percent of Indonesia's GDP, and absorb 97 percent of Indonesia's workforce; boosting their performance and productivity is essential to achieve the Golden Vision (see SIP on MSMEs).

- ***Indonesian firms face operational constraints***. There is room to enhance business, labor market, as well as credit market regulations and credit infrastructure that currently hamper private sector activity and competitiveness. Indonesia's MSMEs are confronted with infrastructure deficits, and face credit barriers[32] (especially younger firms) which impacts their performance.

[31] This would include reforms on external sector regulation, governance, and business regulation reforms, to which human development reforms are added.
[32] For instance, only 76 percent of small firms have a checking or saving account, in contrast to 91 percent of large firms that have one (see SIP on MSMEs).

Trade barriers, particularly non-tariff measures (NTMs), impose a burden on Indonesian businesses and discourage FDI (Annex XI). [33]

- ***The reform agenda should lift these barriers to ensure the private sector can help boost growth sustainably***. Bolstering logistics performance and infrastructure should be a key aspect of the reform agenda,[34] There is a need to foster greater economic openness, improving the regulatory frameworks (such as on product market regulation and trade facilitation), and lowering NTMs. Improving insolvency frameworks would contribute decisively to stimulating private investment from healthy firms, therefore lifting productivity and potential growth in Indonesia (Annex VIII). Continuing to strengthen governance (through an improvement of the rule of law, such as enhancing contract enforcement and the protection of property rights) and anti-corruption frameworks (including institutional effectiveness of the anti-corruption agency, the judiciary, and the asset declaration system) would support accountability and business certainty.

43. Indonesia's growth acceleration strategy rests on enhancing the value-added down the chain from raw commodities through Industrial Policy (IP). IP was first deployed on nickel ore—where Indonesia has a commanding global market share. The strategy was supported, inter alia, by fiscal incentives and NTMs, and has helped increase exports of refined nickel and FDI into the e-battery/e-vehicle value chain. The authorities plan on extending the strategy to a further range of commodities.[35,36] Given Indonesia's diversified economic structure, expanding IP to other commodities and relying only on a group of sectors to drive real GDP growth to 6-7 percent could prove challenging. Further risks stem from global uncertainty and the challenges of mitigating potential IP related distortions. Simulations suggest that reaching a real GDP growth rate of 7 percent in the next five years will require leading sectors to grow consistently well above their five-year moving average growth, while the rest of the economy would need to continue growing at some 5 percent in real terms throughout the period.[37] Durably lifting growth will require a significant and sustained broad-based expansion of the economy, supported by comprehensive horizontal reforms. These reforms would have important complementarities with IP (to creating a competitive

[33] NTMs comprise a broad set of measures, including import and export restrictions, import licensing, and local content requirements. NTMs add up to an average tariff equivalent that is relatively higher than peers in the region; also trade facilitation in Indonesia is below OECD country median (see World Bank, Indonesia Economic Prospects, 2022).

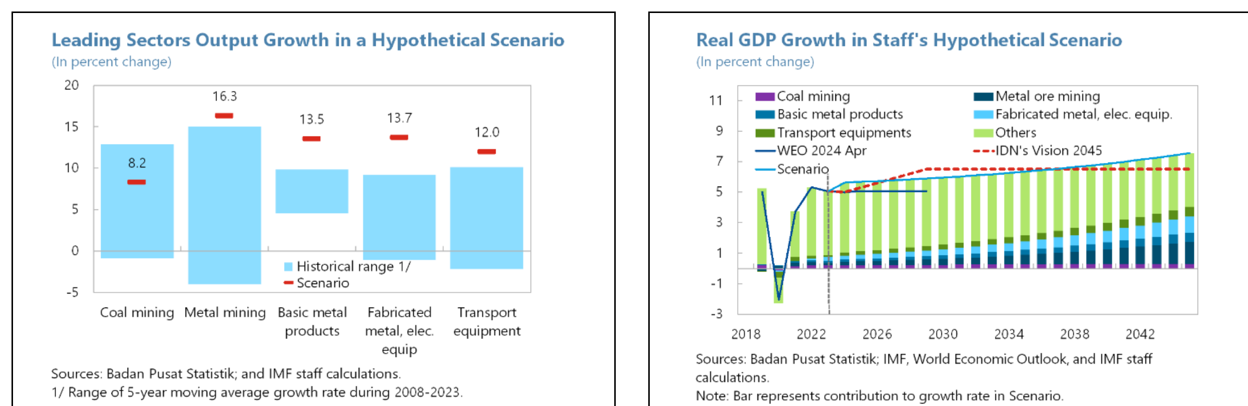
[34] This could help reduce resource misallocation towards productive firms, particularly MSMEs; see Hsieh and Klenow (2009).

[35] See 2023 Article IV. Aside from restrictions on exports of nickel ore, barriers were extended to other commodities (e.g., bauxite and copper) in mid-2023. There is no evidence that this extension has attracted FDI, given Indonesia's relatively more limited position as a global producer/exporter, and as key producing/exporting firms were granted exemptions on such restrictions.

[36] The authorities have discussed up to 21 commodities in total, although specific plans (and toolkits) are yet to be detailed. Aside from metals, commodities include crude palm oil and fisheries.

[37] Anchoring higher long-term growth on specific technology-dependent value chains will also need to contend with emerging new technologies and competitors, and with risks of commodity stock depletion.

business environment that is critical for IP success, and improving human capital, which will be needed to upgrade value added and attract FDI).



44. As IP is deployed, it will be important to use careful design to minimize risks to growth. While IP can be beneficial if targeting well-identified market failures in a time-bound and cost-effective way, it also comes with potentially high fiscal costs, as well as risks of rent-seeking and resource misallocation that can best be mitigated with strong governance frameworks. These trade-offs should be carefully assessed, also to protect competition and innovation, and avoid distortions and adverse cross-border spillovers. Transitioning away from the use of NTMs will be critical to supporting global economic integration, and avoid limiting growth opportunities for firms and reducing the private sector's nimbleness, which could ultimately hamper both trade and growth.[38]

45. The recently published Comprehensive Investment and Policy Plan (CIPP) for on-grid power generation is an important step in the right direction, and further reforms will support the green transition. The overall national climate mitigation strategy is appropriately focused on forestry and land use (FOLU), where abatement costs are low (see 2023 Article IV Consultation). Strong enforcement and monitoring will be critical to ensuring that the mitigation efforts in FOLU are credible, given risks of illegal deforestation and enforcement gaps. At the same time, off-grid power generation is heavily reliant on coal and is currently under expansion to meet the IP deployment needs in remote locations. While the power generation transition may take time and entail some costs, complementing the CIPP with a plan to transition off-grid power generation under the Just Energy Transition Partnership (JETP)—as the authorities intend to do by the end of the year—would help set a path to meet Indonesia's climate goals. An energy subsidy reform, carbon pricing[39] and gradually phasing out related NTMs would be key to achieving Indonesia's Nationally Determined Contribution (NDC) to reduce GHG emissions in 2030 by 32 percent, and the goal of achieving Net

[38] Cali, M. et al, 2024, "*Trade Policy and Exporters' Resilience: Evidence from Indonesia*" show that Indonesian firms facing NTMs may be unable to respond to (or benefit from) external shocks that require flexibly adjusting imported inputs.

[39] The mandatory emission trading system (ETS) is currently limited to the energy sector, and expected to further expand.

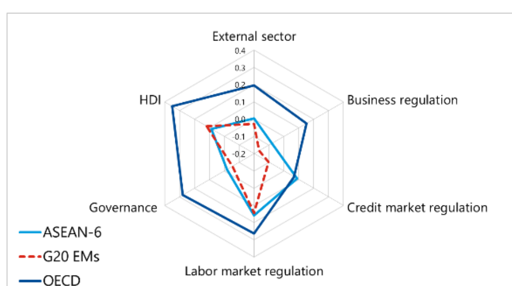
Zero emissions by 2060. These would be best accompanied with measures to support those most vulnerable during the transition and efforts to boost generation and access to renewable energy.

Box 1. Structural Reforms

- **A granular benchmarking exercise shows that Indonesia has significant structural gaps to bridge vis-à-vis peers** (see SIP). Indonesia is relatively less open to trade and has the least sophisticated exports within ASEAN, consistent with lower labor productivity and human capital. To foster converge, it would be important to further strengthen governance and anti-corruption frameworks, as well as the legal system to support accountability and business certainty. The quality of Indonesia's infrastructure and logistics should be enhanced. Finally, bridging structural gaps towards these peers will require enhancing education and health, reducing labor vulnerability, informality, and gender gaps, and leveling up living conditions in a broadly shared way.[1]

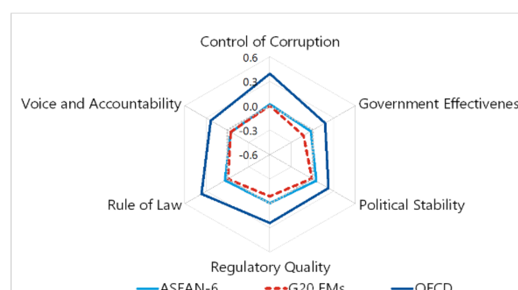
Indonesia Structural Gaps to Comparator Groups

Structural Gaps in Indonesia



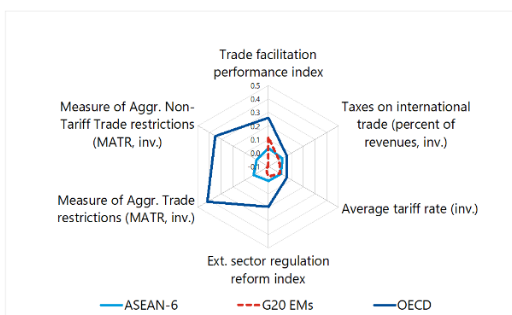
Sources: UNDP; Fraser Institute; and IMF staff calculations, replicating structural reform indices in *Structural Reforms to accelerate Growth, Ease Policy Trade-offs, and Support the Green Transition in EMDEs, IMF SDN/2023/007.*

WGI Governance Indicators



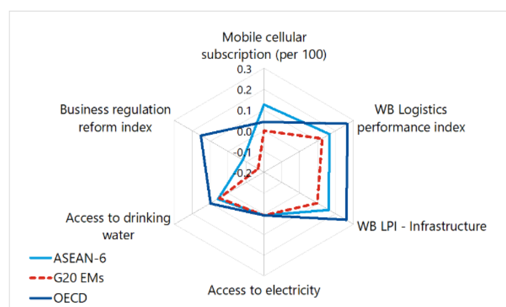
Source: Worldwide Governance Indicators.
Note: Use of these indicators should be considered carefully, given degree of uncertainty, and as they are derived from perceptions-based data.

Trade Regulations and Barriers



Sources: World Bank, World Development Indicators; and IMF staff estimates.

Business Regulation and Infrastructure



Sources: World Bank, World Development Indicators; and IMF staff calculations.

Note: The spider charts show Indonesia's gaps relative to peer group's median. All variables are normalized (0 to 1) for the entire sample of AEs and EMs (with higher values denoting better outcomes) prior to computing gaps. A positive gap indicates a worse outcome relative to comparator group.

[1] Higher levels of human capital—including increasing flexibility to upskill—would be critical to enhance AI-readiness.

Box 1. Structural Reforms (Concluded)

- **Structural reforms can have an important effect on output and be mutually reinforcing**. Cross-country analysis (following Budina et al., 2022) focusing on EMs and AEs, suggests that reforms in governance, external sector regulation, credit market regulation, and human development (health, education) all have a positive, significant effect on output; the effect is stronger if reforms are implemented simultaneously; and mutually reinforcing packages have significant effects, independently of whether countries have already implemented strong reforms in the past or not.
- **Results help guide a possible sequencing of structural reforms in Indonesia (see Text Table 1)**. Reforms in the areas with wider gaps should be prioritized and introduced in tandem, to provide a self-reinforcing boost to growth. Among these, governance and anti-corruption are foundational, and could be combined in a first set of reforms in the near term with business regulation efforts to make it easier for firms to operate and expand, and external sector reforms supporting competitiveness—which should all support FDI as well. Some reforms (e.g., education, social services, infrastructure) may require structural (as opposed to cyclical) public spending and should be supported by upfront efforts to expand the fiscal space, particularly via revenue mobilization (increase the VAT rate and excises, in a first wave of tax reforms, for example). Reforms in other areas, such as credit market regulation reforms, can deliver stronger output effects if preceded by the first set of reforms.[2]

[2] The comprehensive Job Creation Omnibus Law, enacted during the pandemic with the objective of improving the investment climate and generate new job opportunities, was a first step in that direction. The improvement in the IMD World Competitiveness ranking in 2024, relative to the previous year (in particular in the areas of government and business efficiency) might reflect this. Going forward, more is needed to finalize implementation regulations and streamline regulations further, improve business certainty, ease trade and logistics processes, level up learning outcomes, and enhance social protection.

Authorities' Views

46. To achieve their 2045 Golden Indonesia Vision, the authorities are implementing transformational reforms to enhance social protection, improve productivity, and foster new sources of growth. The first stage of their long-term development plan targets strengthening transformational foundations for an inclusive and sustainable economy and focuses on increasing the quality of education, health and social protection, and infrastructure. This would be achieved through measures covering human capital (e.g., longer compulsory education, wider delivery of secondary education, nutrition programs to reduce stunting) and investment (e.g., the new Capital, new sea and air hubs, stronger digital infrastructure, and energy transition infrastructure). The authorities also aim to implement a governance transformation, including strengthening the regulatory framework and enhancements in the business climate.

47. The authorities see their IP strategy as consistent with the needed insertion of Indonesia into the global value chains (GVCs). They expect industrial performance and economic competitiveness to benefit from their IP, initially focused on the mining sector, but to be extended to other commodities, including agricultural products. They underscored the strong results achieved from the implementation of IP on nickel ore, which has delivered strong FDI for the construction of smelters; this will be expanded to copper by end-2024. They see IP as needed to make the most of their rich natural resources, enable the increase in value-addition in their economy and attract investment flows, especially in the face of geopolitical fragmentation trends which create an uneven playing field as significant distortions are imposed by the largest economies.

48. The authorities are committed to achieving Net-Zero Emission by 2060 or sooner, which has been incorporated in the National Long-Term Development Plan for 2024-2025. In coordination with international partners, the authorities expect to release the 2024 CIPP— which should showcase different transition pathways for the off-grid power plant network—around end-2024.[40] Their overall green transition strategy focuses on five areas, namely the development of sustainable energy and the green industry, sustainable land restoration, waste management, and preservation of the coastal and marine environment. Discussions are ongoing on a possible carbon tax on carbon-intensive activities, expanding the emission trading system and carbon exchange market, the use of local content requirements on renewables, and enhancing the targeting of energy subsidies.[41,42] These measures are expected to be addressed by the incoming administration starting end-2024.

Text Table 1. Reform Priorities

	Short-term	Medium-term
A. Fiscal Policy	1. Increase domestic tax revenue to bolster fiscal space. This should also endure beyond the short-term. 2. Prioritize high-quality spending supportive of Indonesia's development and closely monitor fiscal risks 3. Increase coverage and adequacy of the social safety net, improve targeting of subsidies.	4. Better align retail fuel prices with international prices. 5. Enhance the strategic direction of MTFF, and its articulation with the annual budget and long-term plans; ensure the General Government accounts comprehensively reflects fiscal activities. 6. Strengthen SNG's own-revenue sources and PFM, including current and investment spending execution and service delivery capacities
B. Inclusion and Development	1. Boost size and quality of health spending and social protection, for a broadly shared growth. 2. Boost education spending, improve learning time and quality to reduce skill mismatch and increase productivity and knowledge capabilities/economic sophistication.	3. Tackle gender inequality, to further increase the labor force and potential growth.
C. Governance	Strengthen governance and anti-corruption framework, improve legal system to support accountability and business certainty.	
D. Trade and Foreign Investment Policy	1. Avoid intensifying restrictive trade policies (including in the IP context) and transition away from NTMs that distort trade and investment decisions and risk international spillovers.	2. Foster openness in trade and FDI, and increase trade facilitation (e.g. to reduce time, cost and uncertainty of crossborder transactions)
E. Business climate	1. Reduce regulatory uncertainty, bureaucracy costs and administrative hurdles.	
	2. Strengthen infrastructure and logistics	

[40] Grants and TA programs under the JETP initiative have been launched, for a total of US$215 million and around US$800 million loans already signed or approved, with additional US$2 billion undergoing negotiations.

[41] The emissions trading system involves 99 power plants as of 2023 and covers around 86 percent of the total national coal-fired power plant capacity, with 7 million tons of CO2e allowances having been traded so far (for a value of around US$5 million).

[42] Around 570.000 tons of CO2e carbon units amounting to US$2.2 million have been sold in this Carbon Exchange market (IDX Carbon) as of end-April 2024, most of it to banking companies.

Text Table 1. Reform Priorities (Concluded)

F. Credit Market 1/	1. Develop regulation to strengthen the development of credit scores; establish an oversight framework for the Credit Reporting Systems	5. Expand (direct) access to the fast payment system (BI-FAST) and build on the National Standard for Payment Open API (SNAP) to develop a comprehensive approach to open banking/finance
	2. Reforms to enhance capital market development (e.g., repo market, development of interest rate and forex derivatives).	6. Foster the presence of institutional investors in the domestic market
	3. Strengthen regulatory approach to alternative financing models (DFS)	7. Enhance financial literacy and reduce the digitalization gap across Indonesian provinces
	4. Introduce a regulatory green taxonomy and update reporting requirements for firms and financial institutions	8. Explore ways to scale and utilize the domestic banking system to mobilize climate finance.
G. Labor market	1. Enhance the hiring and firing regulation, assess the extent to which wage determination encourages informality.	2. Tackle labor informality and duality, while ensuring the protection of workers.

1/ See 2024 FSAP Recommendations, Annexes VII and VIII, and Selected Issues Paper on Access to Finance by SMEs.

STAFF APPRAISAL

49. Indonesia's growth remains strong despite external headwinds, and the output gap is expected to fully close in 2026. Policies have been broadly prudent in the post-pandemic period. The fiscal deficit has stayed well within the fiscal rule limit, anchoring a declining public debt. Monetary policy has appropriately focused on bringing down inflation into the target range. The 2023 external position was broadly in line with the level implied by medium-term fundamentals and desirable policies (Annex I), and the financial sector is resilient. The authorities have been pursuing an ambitious growth agenda to reach high-income status by 2045, comprising public spending, institutional reforms, and Industrial Policy (IP). Risks to the near-term outlook are broadly balanced.

50. While broadly prudent, the near-term fiscal deficit could be narrowed slightly to support the policy mix. The fiscal position is projected to become expansionary in 2024 and 2025, amid a negative (albeit gradually closing) output gap. This can be managed given well-contained inflation and relatively low public debt; yet, slightly narrower deficits would continue to support growth while allowing for a more balanced policy mix, and preserving policy space to respond to downside risks in a shock-prone global environment.

51. Indonesia's longstanding fiscal prudence should be preserved to protect fiscal space and credibility. The fiscal rule—the 3 percent of GDP deficit cap—remains well-suited to support the Golden Vision, especially if complemented with an enhanced medium-term fiscal framework (MTFF) that ensures more systematic counter-cyclical fiscal policy within the cap. The authorities' ambitious high-level revenue mobilization goals are welcome; a forceful tax reform, keeping tax incentives well-contained, and bolstering revenue administration would be essential to this end. Prioritizing high-quality spending and gradually reducing energy subsidies would help support Indonesia's development goals, while staying within the cap. With fiscal operations by SOEs, PPPs and public guarantees gradually on the rise, closely monitoring fiscal risks and avoiding the buildup of

contingent liabilities should help preserve Indonesia's long-standing track record of prudent policies and debt sustainability.

52. The monetary policy stance remains broadly adequate and should remain data dependent. Absent significant shocks that raise inflationary pressures, a gradual reduction of the policy rate would be appropriate. Given persistent uncertainties, the monetary policy path should remain data driven and ready to act if inflation surprises on either side, with well-communicated moves. With the overarching framework for crisis resolution well established in the FSOL, aligning the implementing regulations for future primary market purchases of government bonds by BI to international best practices will further safeguard central bank independence. Careful management should allow the unwinding of pandemic bonds as they fall due, while helping avoid market disruptions.

53. The macroprudential framework could be refined further. Continuing financial sector reform would protect resilience and support financial deepening. Clarifying that safeguarding financial system resilience is prioritized as BI calibrates the broad toolkit, and explicitly distinguishing the tools for financial system resilience would enhance effectiveness and communication. Gradually shifting the macroprudential stance towards a more neutral stance as the credit gap closes would be appropriate. Recent financial sector reform has entailed substantial progress; yet some areas could be further strengthened, as found in the 2024 FSAP. Key elements of further financial sector reforms include bolstering the financial safety net, crisis management, resolution, and systemic liquidity frameworks, and developing the credit infrastructure to foster sound access and addressing remaining gaps in the Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT) framework.

54. In line with the Integrated Policy Framework (IPF), the exchange rate should continue to play its shock absorbing role. Foreign exchange intervention (FXI) would be an appropriate response under certain shocks and conditions, particularly when shocks trigger spikes in market premia in the context of shallow FX markets. Preserving buffers will be particularly important for future eventual urgencies in a shock-prone global environment. Judicious use of FXI and an emphasis on ER flexibility as a shock absorber would also support greater market development.

55. Reaching high-income status by 2045 will require bridging gaps in key areas via horizontal structural reforms to lift potential growth in an inclusive manner. To this end, strengthening governance and anti-corruption, leveling up learning outcomes, investing in logistics and infrastructure, reducing restrictions to trade, and enhancing social protection will be key to support a more attractive business environment and secure a base capable of absorbing and supporting stronger economic activity and generate new job opportunities—so output can be lifted sustainably, and growth gains can be evenly shared.

56. Transitioning away from the use of Non-tariff Measures (NTMs) and carefully designing Industrial Policy (IP) to minimize trade and investment distortions would support potential growth. Plans to expand IP to new sectors should be preceded by cost-benefit analyses, and if implemented, accompanied by regular reassessments of trade-offs. Sound IP design must target well-identified market failures, be time-bound and cost-effective, and anchored by strong

governance; it should avoid hindering competition and innovation and minimize adverse cross-border spillovers. Transitioning away from the use of non-tariff measures will be critical to sustain strong and inclusive growth while supporting global economic integration.

57. Further reforms would support the green transition. The recently published Comprehensive Investment and Policy Plan (CIPP) for on-grid power generation is an important step in the right direction. The national climate mitigation strategy is appropriately focused on forestry and land use (FOLU), where abatement costs are low. Finalizing plans to transition coal-based off-grid power generation under the Just Energy Transition Partnership (JETP) would help set a path to meet Indonesia's climate goals. An energy subsidy reform, carbon pricing and gradually phasing out related NTMs would support achieving Indonesia's Nationally Determined Contribution (NDC) by 2030, and the goal of achieving Net Zero emissions by 2060.

58. It is recommended that the next Article IV consultation take place on a standard 12-month cycle.

Figure 1. Indonesia: Recent Economic Developments

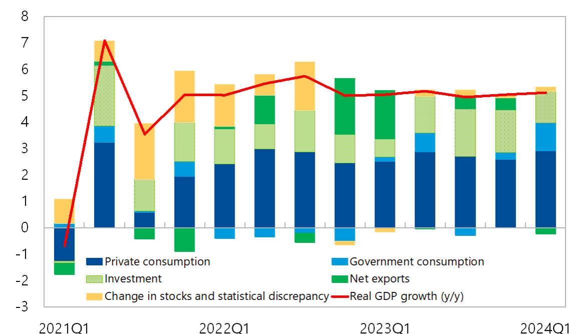
Real GDP growth remained strong in 2023 and 2024Q1…

Real GDP Growth
(In percent)

Sources: Badan Pusat Statistik via Haver Analytics; and IMF staff estimates.

…supported by robust domestic demand.

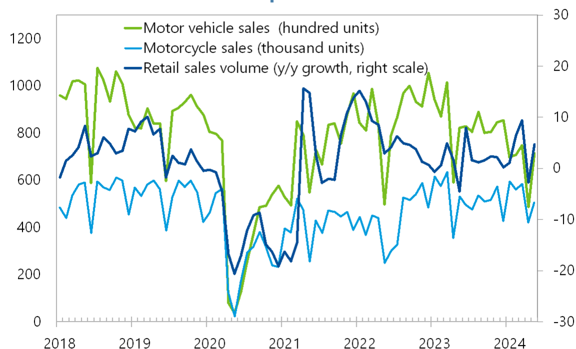
Contribution to Real GDP Growth
(In percent, year-over-year)



Sources: Haver Analytics.; and IMF staff estimates.

Private consumption has been resilient after the post-pandemic recovery…

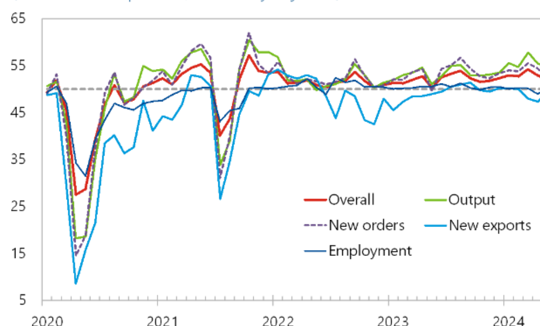
Indicators of Private Consumption Activities



Sources: Haver Analytics; and IMF staff estimates.

… and manufacturing sentiment has remained expansionary.

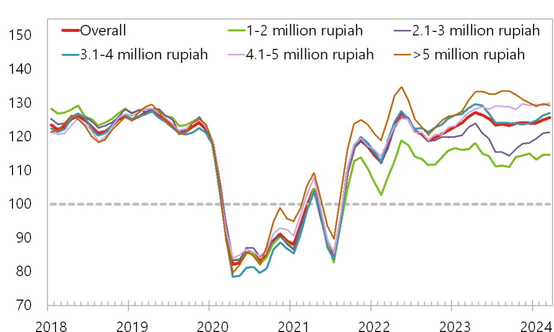
Manufacturing Purchasing Managers' Index
(Index >50 = expansion, seasonally adjusted)



Source: Haver Analytics.

Consumer sentiment has been strong throughout 2023 and into 2024, albeit with income disparities…

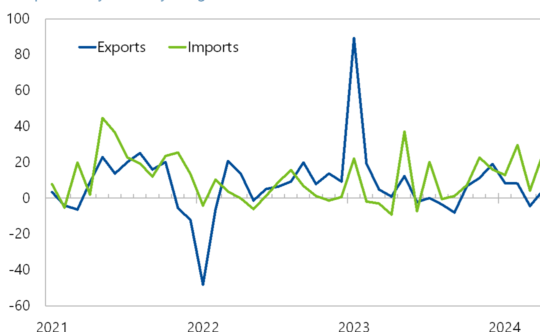
Consumer Confidence Index by Respondents Expenditure
(Index >100= increase, 3mma)



Sources: Bank Indonesia via Haver Analytics; and IMF staff calculations.

… while the volume of merchandise exports has normalized after gaining momentum as of end-2023.

Merchandise Trade Volume
(In percent, year-on-year growth of metric tons)

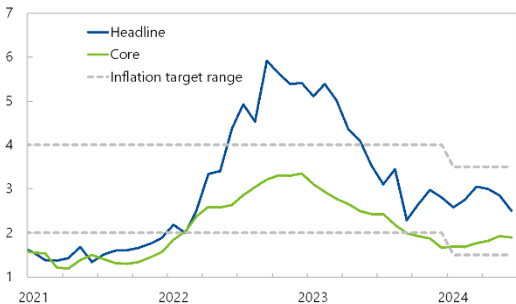


Sources: BPS via CEIC Data Co. Ltd.; and IMF staff estimates.

Figure 2. Indonesia: Inflation Dynamics

Inflation came down since early 2023, to well within BI's target band...

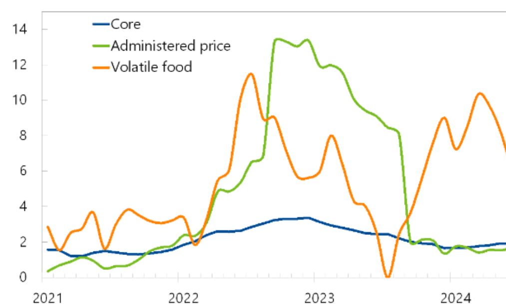
Inflation Developments
(In percent, year-on-year)



Sources: Haver Analytics; and IMF staff estimates.

...reflecting a decline in core and administered price goods, and despite spikes in volatile food inflation in early 2024.

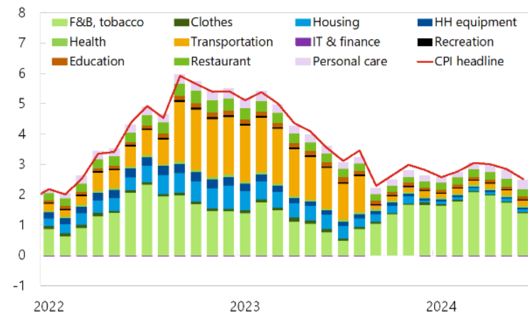
Categories of Price Inflation
(In percent, year-on-year)



Source: Badan Pusat Statistik via Haver Analytics.

Transportation and housing inflation has declined, with remaining inflation driven by food prices.

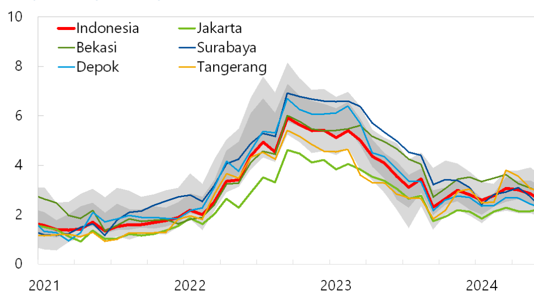
Contribution to Headline Inflation
(In percent, of year-on-year)



Sources: Badan Pusat Statistik via Haver Analytics; IMF staff estimates.

The decline in inflation was observed in all regions.

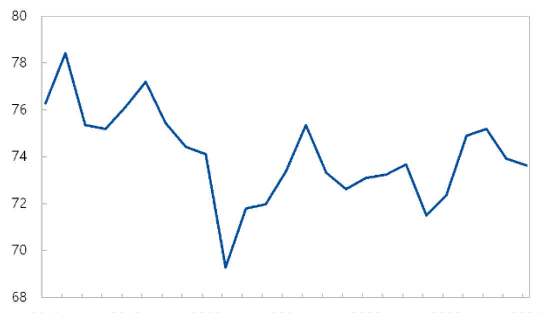
Consumer Price Inflation in 90 Cities 1/
(In percent, year-on-year)



Sources: Badan Pusat Statistik; CEIC Data Co. Ltd.; and IMF staff estimates.
1/ Darker shade indicates 25th to 75th percentiles, lighter shade indicates 10th to 25th and 75th to 90th percentiles.

Capacity utilization has increased but is still well below pre-pandemic levels.

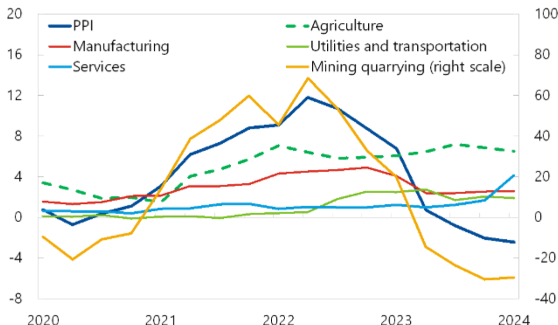
Capacity Utilization
(In percent)



Source: Bank Indonesia via Haver Analytics.

PPI inflation also saw a broad-based decline since early 2023.

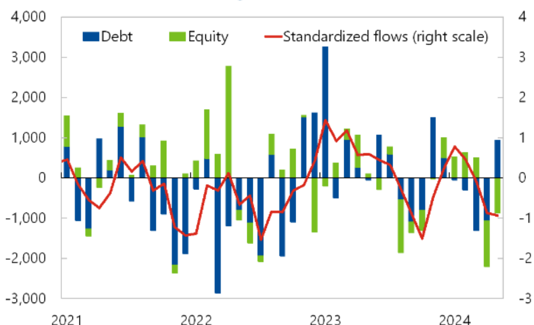
Components of Producer Price Inflation
(In percent, year-on-year)



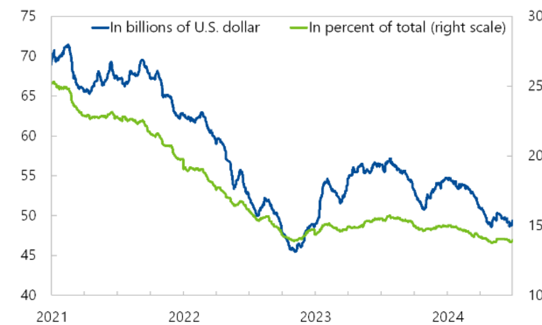
Sources: Badan Pusat Statistik via Haver Analytics; and IMF staff estimates.

Figure 3. Indonesia: Capital Flows and Market Developments

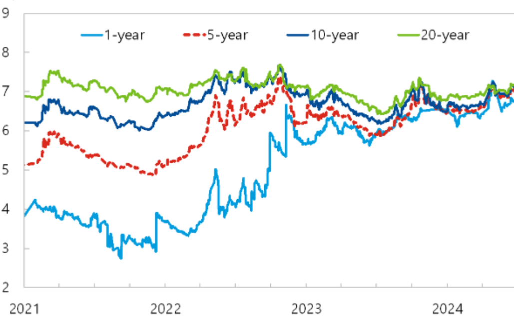
Portfolio investment recorded positive debt inflows in 2023, concentrated at end-year, partly offset by equity outflows.



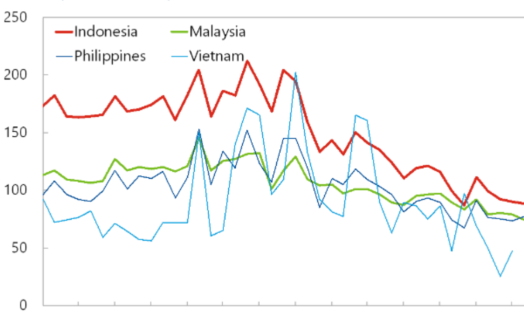
Rupiah government bonds held by foreign investors edged up slightly in 2023, in US$ and as a percent of the debt stock.



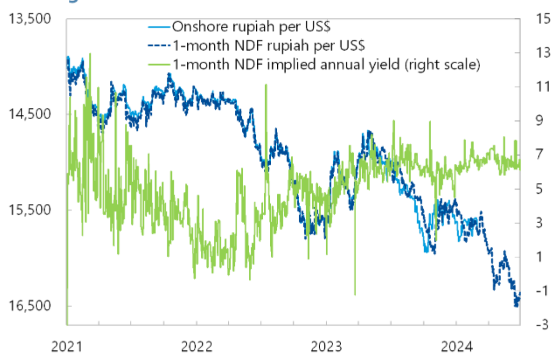
Market interest rates have stayed broadly flat since 2023...



...with an overall decline in volatility in the sovereign premium...



...despite exchange rate depreciation pressures.



Stock market indices have lost some ground over 2024.

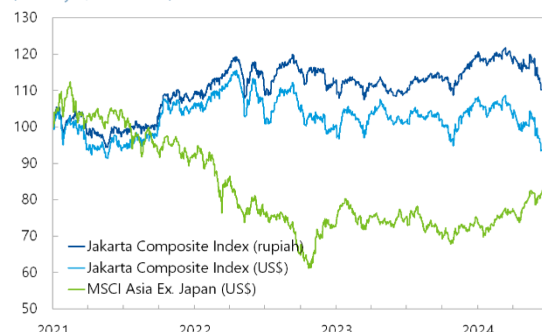
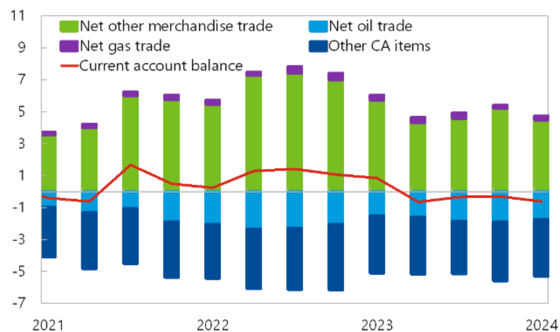


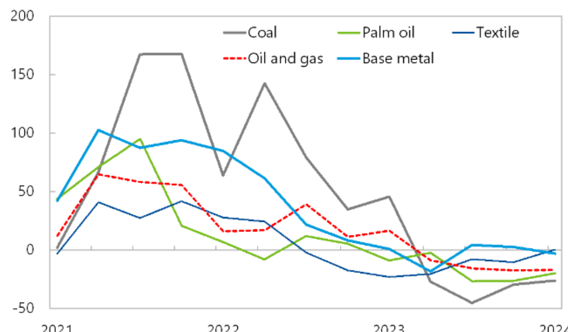
Figure 4. Indonesia: External Sector

The current account recorded a small deficit in 2023 and early 2024, driven mainly by a lower surplus in the non-oil and gas balance



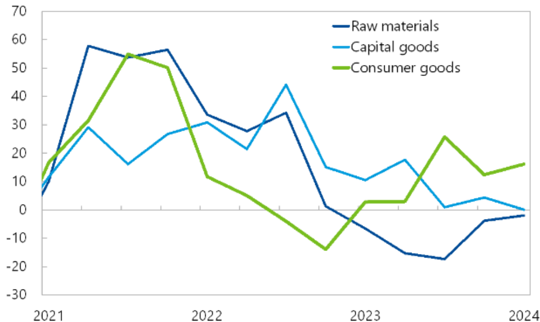
Sources: Bank Indonesia via CEIC Data Co. Ltd.; and IMF staff estimates.

Lower commodity prices led to a broad-based decline in export growth in 2023, particularly coal.



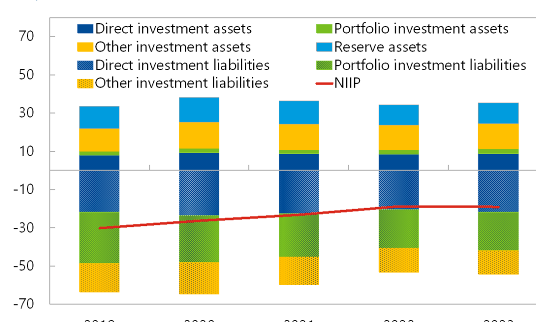
Sources: Haver Analytics; and IMF staff estimates.

Import growth moderated somewhat, mainly reflecting weaker imports of raw materials.



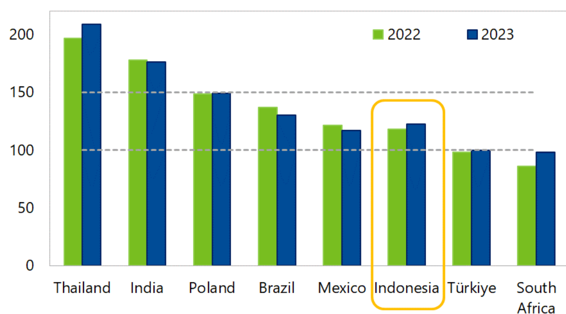
Sources: CEIC Data Co. Ltd; and IMF staff calculations.

The NIIP remained relatively stable in 2023, as the increase in assets was offset by higher direct investment liabilities.



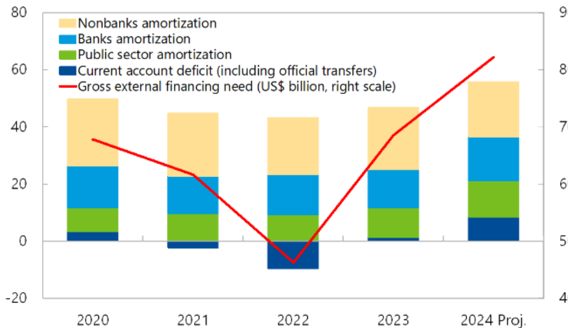
Sources: CEIC Data Co. Ltd.; and IMF staff estimates.

Indonesia's foreign reserves increased in 2023 (US$146 billion), remaining adequate.



Sources: IMF, International Financial Statistics; and IMF staff estimates.
Note: ARA data as of April 2024, except for Indonesia (latest).

External financing needs are projected to increase in 2024 mainly due to the widening in the current account deficit.

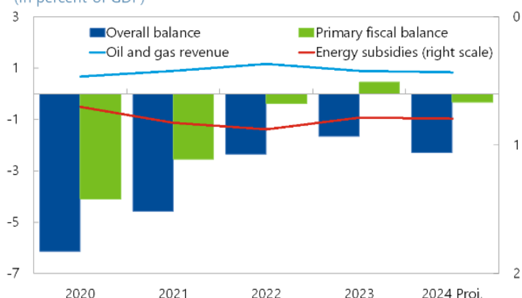


Source: IMF staff estimates.

Figure 5. Indonesia: Fiscal Sector

The primary balance turned into a surplus in 2023, reflecting mostly stronger-than-expected revenue performance …

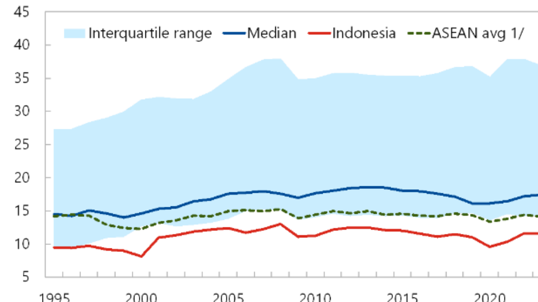
Central Government Indicators
(In percent of GDP)



Sources: Indonesian authorities; and IMF staff estimates and projections.

… yet Indonesia's tax-to-GDP ratio lags behind EM peers.

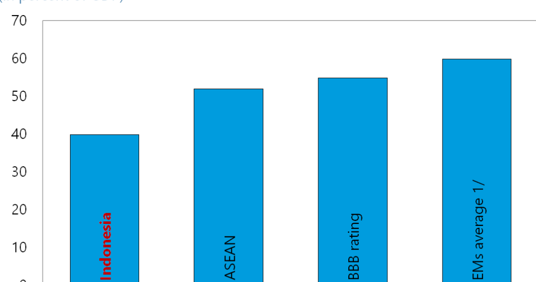
Emerging Markets: Tax Revenue
(In percent of GDP)



Sources: IMF, World Economic Outlook; and IMF staff estimates.
1/ Indonesia, Philippines, Thailand, and Vietnam.

Public debt-to-GDP ratio is lower than peers …

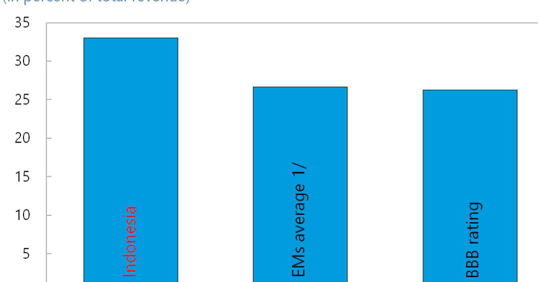
General Government Gross Debt, 2023
(In percent of GDP)



Source: IMF, World Economic Outlook.
1/ Includes: Indonesia, Türkiye, South Africa, Argentina, Brazil, Chile, Colombia, Mexico, Peru, Bangladesh, Sri Lanka, India, Malaysia, Pakistan, Philippines, Thailand, Vietnam, Russia, China, Hungary, Poland, and Romania.

… but the debt service to revenue ratio is higher.

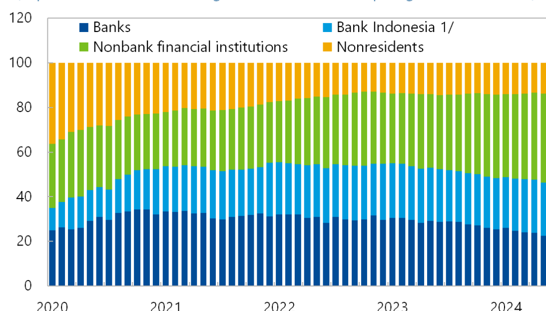
General Government Debt Service Ratio, 2023
(In percent of total revenue)



Sources: IMF, World Economic Outlook; and IMF staff estimates.
1/ Includes: Indonesia, Türkiye, South Africa, Argentina, Brazil, Chile, Colombia, Mexico, Peru, Bangladesh, Sri Lanka, India, Malaysia, Pakistan, Philippines, Thailand, Vietnam, Russia, China, Hungary, Poland, and Romania.

The share of non-resident holdings of rupiah government securities has stabilized at a lower level compared to pre-pandemic.

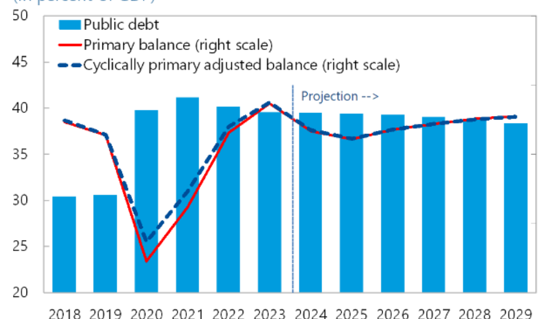
Ownership Share of Indonesian Rupiah Government Bonds 1/
(In percent of total outstanding tradable Indonesian rupiah government bonds)



Sources: Indonesian authorities via Haver Analytics; and IMF staff estimates.
1/ Including government bonds held by Bank Indonesia for monetary operations.

General government debt as share of GDP is expected to decrease gradually over the medium term.

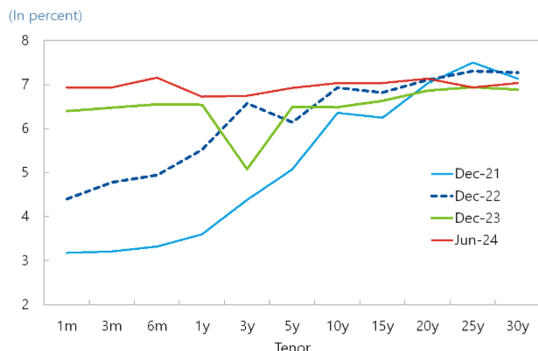
Public Debt, Primary, and Cyclically Adjusted Balance
(In percent of GDP)



Sources: Indonesian authorities; and IMF staff estimates and projections.

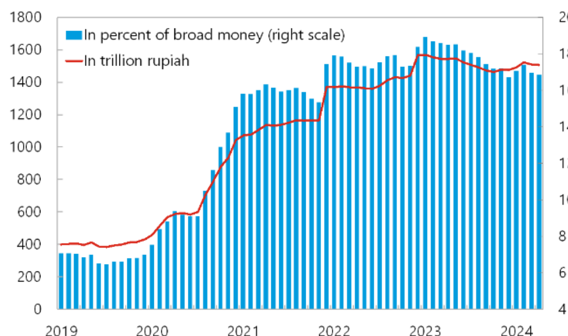
Figure 6. Indonesia: Monetary Sector

Monetary policy tightening since August 2022, along with Operation Twist and subsequently BI's introduction of new short-term instruments, have flattened the yield curve.



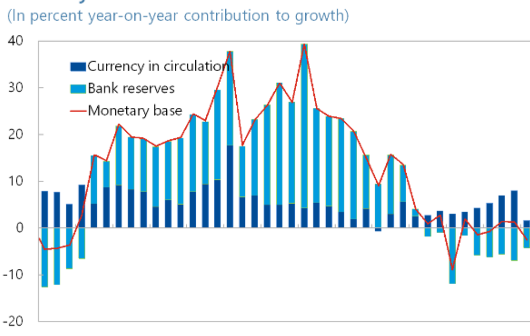
Source: Haver Analytics.

BI ended its pandemic-era primary market government bond purchases in 2022, and total holdings of government bonds stabilized in 2024.



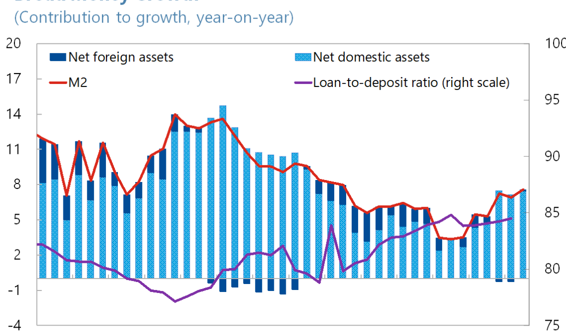
Sources: IMF, International Financial Statistics; Haver Analytics; and IMF staff estimates.

Monetary base growth stalled, driven by bank reserves...



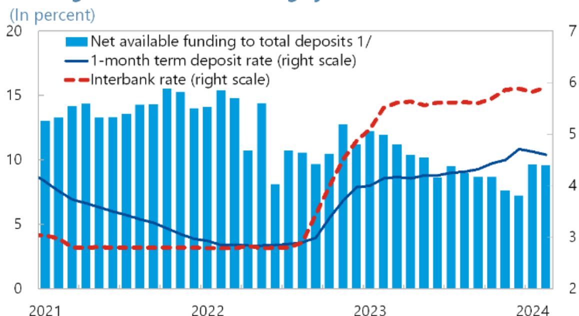
Sources: IMF, International Financial Statistics; and IMF staff estimates.

...while broad money growth, which had moderated, is picking up.



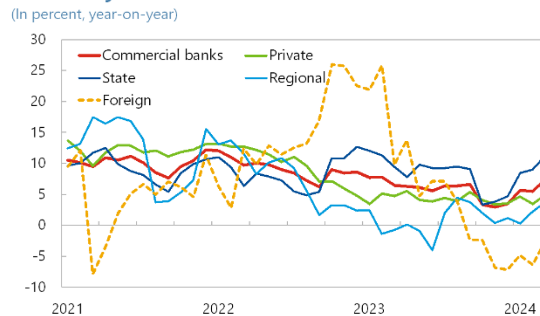
Sources: CEIC Data Co. Ltd; and IMF staff estimates.

Banking system liquidity remains comfortable, though declining somewhat as loan growth normalizes to pre-pandemic rates.



Sources: Bank Indonesia; and IMF staff estimates.
1/ Net available funding is defined as third-party funding less third-party credit and statutory reserves.

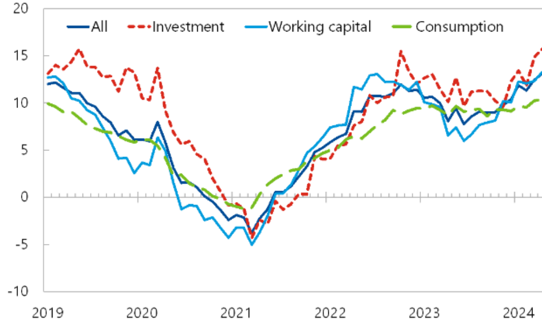
Deposit growth rates picked up in early 2024, particularly at state-owned banks, after decelerating in 2023.



Sources: Otoritas Jasa Keuangan via CEIC Data Co. Ltd.; and IMF staff estimates.
1/ Savings and deposits.

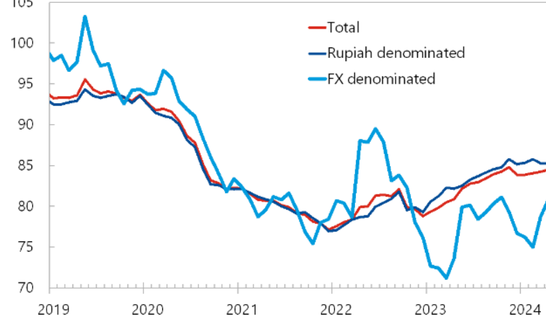
Figure 7. Indonesia: Macrofinancial Developments

Credit growth has returned to pre-pandemic rates, and has continued to pick up in 2024…



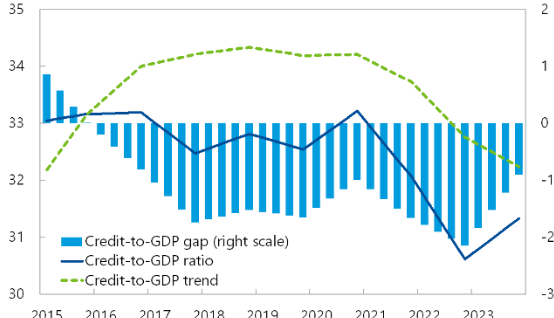
Sources: Indonesia Financial Service Authority; and IMF staff estimates.

… though commercial banks' loan-to-deposit ratios have only partly bounced back.



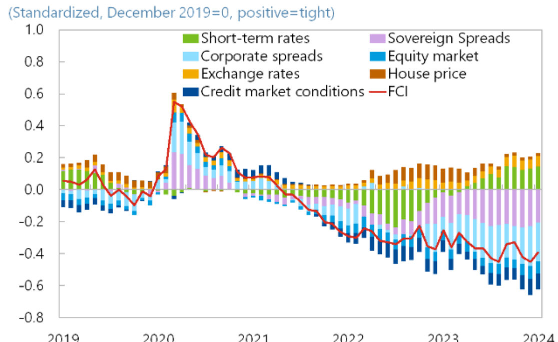
Sources: CEIC Data Co., Ltd.; and IMF staff estimates.

The credit gap remains negative, but has been narrowing since 2023.



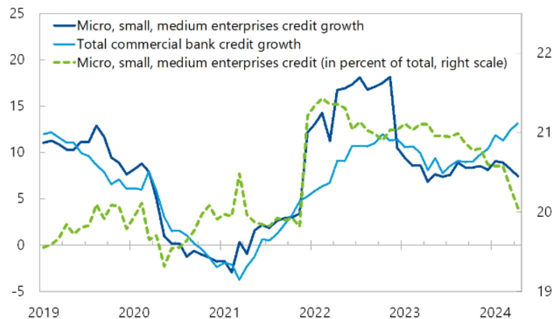
Sources: CEIC Co. Ltd.; and IMF staff estimates.

Financial conditions eased since end-2022 despite the increase in interest rates, amid lower sovereign and corporate spreads.



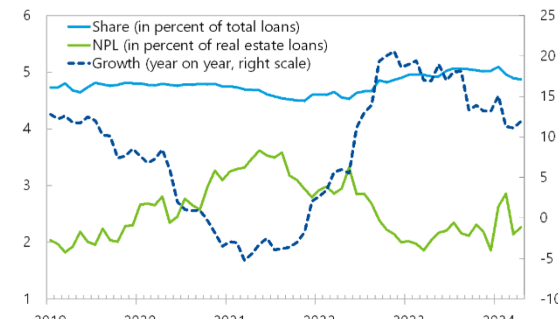
Source: IMF staff estimates.

Recovery in credit growth to MSMEs has been moderating.



Sources: CEIC Data Co. Ltd.; and IMF staff estimates.

Real estate loan growth is also moderating, and non-performing loans ratio has ticked up in 2024.

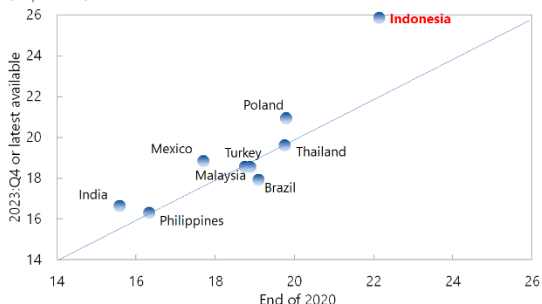


Sources: CEIC Data Co. Ltd.; and IMF staff estimates.

Figure 8. Indonesia: Selected Emerging Market Economies: Financial Soundness Indicators

Indonesia's banking system capital remains adequate and above peers.

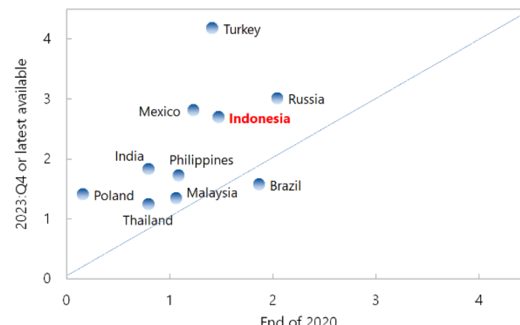
Regulatory Capital to Risk Weighted Assets 1/
(In percent)



Source: IMF, Financial Soundness Indicators.
1/ Includes capital impact of the transition to IFRS9 in January 2020.

Profitability remains at a high level in comparison to peers reflecting large interest margins.

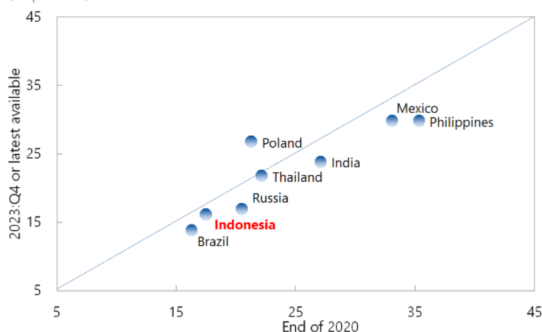
Return on Assets
(In percent)



Source: IMF, Financial Soundness Indicators.

System-wide bank liquidity remains comfortable.

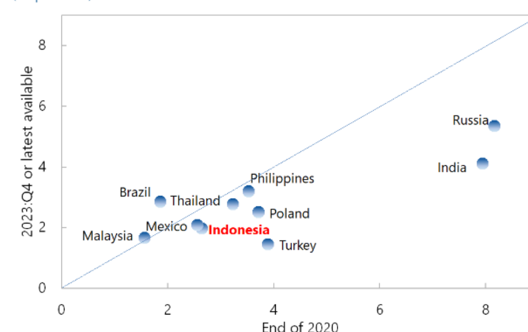
Liquid Assets to Total Assets
(In percent)



Source: IMF, Financial Soundness Indicators.

Nonperforming loans have returned to pre-pandemic levels, partly due to regulatory forbearance measures.

Nonperforming Loans to Total Loans
(In percent)



Source: IMF, Financial Soundness Indicators.

Table 1. Indonesia: Selected Economic Indicators, 2022–27

Nominal GDP (2023): Rp 20,892 trillion or US$1,371 billion
Population (2023): 277 million
Main exports (percent of total, 2023): coal (16.5), base metal (15.6), palm oil (8.7), oil and gas (6.2), electrical apparatus (5.5), textile and products (4.5)
GDP per capita (2023): US$4,942
Unemployment rate (September 2023): 5.3 percent
Poverty headcount ratio at national poverty line (March 2022): 9.5 percent of population

	2022	2023	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.
Real GDP (percent change)	**5.3**	**5.0**	**5.0**	**5.1**	**5.1**	**5.1**
Domestic demand	3.8	5.1	5.0	5.2	5.1	5.1
Of which:						
Private consumption 1/	5.0	4.9	5.1	5.1	5.1	5.1
Government consumption	-4.5	2.9	5.5	4.2	3.0	3.0
Gross fixed investment	3.9	4.4	5.0	5.7	5.7	5.7
Change in stocks	0.1	0.5	0.0	0.0	0.0	0.0
Net exports 2/	0.8	0.7	0.2	0.2	0.3	0.3
Statistical discrepancy 2/	0.9	-0.4	0.0	0.0	0.0	0.0
Output gap (in percent)	**-1.1**	**-0.3**	**-0.2**	**-0.1**	**0.0**	**0.0**
Saving and investment (in percent of GDP)						
Gross investment 3/	29.7	30.5	30.5	30.6	30.7	30.8
Gross national saving	30.7	30.4	29.6	29.3	29.3	29.4
Prices (12-month percent change)						
Consumer prices (end period)	5.4	2.8	2.8	2.7	2.6	2.5
Consumer prices (period average)	4.1	3.7	2.9	2.8	2.6	2.6
Public finances (in percent of GDP)						
General government revenue	15.2	15.0	14.8	14.9	15.0	15.0
General government expenditure	17.4	16.6	17.1	17.6	17.5	17.4
Of which : Energy subsidies	0.9	0.8	0.8	0.6	0.5	0.4
General government balance	-2.2	-1.6	-2.3	-2.6	-2.5	-2.4
Primary balance	-0.2	0.5	-0.3	-0.6	-0.3	-0.1
General government debt	40.1	39.6	39.5	39.4	39.3	39.1
Money and credit (12-month percent change; end of period)						
Rupiah M2	8.4	3.5	9.9	10.0	9.8	9.8
Base money	23.9	-1.5	4.0	6.0	7.0	7.4
Claims on private sector	10.1	9.2	10.5	11.3	9.5	9.6
One-month interbank rate (period average)	4.2	6.4	...	...	...	...
Balance of payments (in billions of U.S. dollars, unless otherwise indicated)						
Current account balance	13.2	-1.9	-12.3	-20.5	-24.2	-25.5
In percent of GDP	1.0	-0.1	-0.9	-1.3	-1.4	-1.4
Trade balance	62.7	46.5	34.8	30.1	29.4	32.8
Of which : Oil and gas (net)	-24.8	-19.7	-20.9	-18.3	-13.8	-14.2
Inward direct investment	25.4	21.8	26.0	29.6	33.5	36.1
Overall balance	4.0	6.3	0.8	6.7	9.6	13.7
Terms of trade, percent change (excluding oil)	22.9	-12.4	0.8	1.0	-3.4	-0.2
Gross reserves						
In billions of U.S. dollars (end period)	137.2	146.4	147.2	153.9	163.5	177.3
In months of prospective imports of goods and services	6.2	6.1	5.5	5.2	5.1	5.2
As a percent of short-term debt 4/	206	209	198	192	190	193
Total external debt 5/						
In billions of U.S. dollars	396.5	408.5	419.0	439.4	461.6	482.8
In percent of GDP	30.1	29.8	29.4	28.3	27.5	26.6
Exchange rate						
Rupiah per U.S. dollar (period average)	14,850	15,237	...	...	...	...
Rupiah per U.S. dollar (end of period)	15,573	15,399	...	...	...	...
Memorandum items:						
Jakarta Stock Exchange (12-month percentage change, composite index)	4.1	6.2	...	...	...	...
Oil production (thousands of barrels per day)	800	797	794	791	788	785
Nominal GDP (in trillions of rupiah)	19,588	20,892	22,555	24,367	26,274	28,313

Sources: Data provided by the Indonesian authorities; Bloomberg L.P.; and IMF staff estimates and projections.

1/ Includes NPISH consumption.
2/ Contribution to GDP growth (percentage points).
3/ Includes changes in stocks.
4/ Short-term debt on a remaining maturity basis.
5/ Public and private external debt.

Table 2. Indonesia: Selected Vulnerability Indicators, 2020–24

	2020	2021	2022	2023	2024	Data as of
Key economic and market indicators						
Real GDP growth (in percent)	-2.1	3.7	5.3	5.0	5.0	Proj.
CPI inflation (in percent, e.o.p)	1.7	1.9	5.4	2.8	2.8	Proj.
Short-term (ST) interest rate (in percent, e.o.p.) 1/	3.8	3.6	6.2	6.6	6.9	June
Ten-year government bond yield (in percent, e.o.p.)	5.9	6.4	6.9	6.5	7.1	June
Indonesia EMBI spread (basis points (bps), e.o.p.)	186	161	133	87	92	June
Exchange rate (rupiah per U.S. dollar, e.o.p.)	14,050	14,253	15,573	15,399	16,375	June
External sector						
Current account balance (in percent of GDP)	-0.4	0.3	1.0	-0.1	-0.9	Proj.
Net FDI inflows (in percent of GDP)	1.3	1.5	1.4	1.1	1.2	Proj.
Exports of goods and nonfactor services (GNFS) (percentage change, in US$ terms)	-10.8	38.3	27.9	-7.3	4.7	Proj.
Real effective exchange rate (average; 2010=100)	71.6	71.2	73.8	73.7	…	
Gross international reserves (in US$ billion)	135.9	144.9	137.2	146.4	147.2	Proj.
In percent of ST debt at remaining maturity (RM)	208.8	243.8	205.9	209.3	198.4	Proj.
Total gross external debt (in percent of exports of GNFS)	233.7	167.7	125.6	139.5	136.7	Proj.
Gross external financing requirement (in US$ billion) 2/	69.5	55.9	53.4	71.8	86.5	Proj.
Public sector (PS) 3/						
Overall balance (in percent of GDP)	-6.1	-4.6	-2.4	-1.6	-2.3	Proj.
Primary balance (in percent of GDP)	-4.1	-2.5	-0.4	0.5	-0.3	Proj.
Gross PS financing requirement (in percent of GDP) 4/	8.8	6.4	4.4	4.5	5.3	Proj.
Public sector gross debt (PSGD) (in percent of GDP)	36.6	41.4	42.8	42.9	42.7	Proj.
Exposed to exchange rate risk (in percent of total PSGD) 5/	33.3	29.7	29.3	28.4	28.9	Proj.
Exposed to interest rate risk (in percent of total PSGD) 6/	7.0	5.8	4.9	4.5	3.9	Proj.
Financial sector (FS)						
Capital to risk-weighted assets, commercial banks (in percent) 7/	23.9	25.7	25.6	27.8	26.0	Apr.
Nonperforming loans, commercial banks (in percent of total loans)	3.1	3.0	2.4	2.2	2.3	Apr.
Foreign currency deposits at commercial banks (in percent of total deposits)	13.2	13.5	15.0	15.3	15.4	Apr.
Foreign currency loans at commercial banks (in percent of total loans)	12.0	12.0	12.5	12.1	13.6	Apr.
Government debt held by financial system (percent of total financial system assets)	14.6	16.5	15.3	14.6	13.6	Apr.
Claims on private sector (annual percentage change)	-0.4	6.1	10.1	9.2	10.5	Proj.

Sources: Data provided by the Indonesian authorities; and IMF staff estimates and projections.

1/ One-month Jakarta Interbank offered rate.

2/ Defined as current account deficit, plus amortization on medium- and long-term debt and short-term debt at end of previous period.

3/ Public sector covers central government only.

4/ Overall balance plus debt amortization.

5/ Debt in foreign currency or linked to the exchange rate.

6/ Government securities at variable interest rates.

7/ Includes capital charge for operational risk.

Table 3. Indonesia: Balance of Payments, 2022–27

(In percent of GDP)

	2022	2023	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.
Current account	**1.0**	**-0.1**	**-0.9**	**-1.3**	**-1.4**	**-1.4**
Goods, net (trade balance)	4.8	3.4	2.4	1.9	1.8	1.8
Exports, f.o.b.	22.2	18.9	18.9	18.9	18.9	19.0
Oil and gas	1.3	1.2	1.1	1.2	1.3	1.2
Non-oil and gas	20.8	17.6	17.7	17.7	17.6	17.7
Agriculture	0.6	0.5	0.5	0.4	0.4	0.4
Manufacturing	15.2	13.3	13.1	13.6	14.5	14.8
Palm oil	2.1	1.7	1.9	1.8	1.9	1.9
Rubber products	0.5	0.3	0.5	0.4	0.4	0.4
Other manufacturing	12.7	11.3	10.7	11.3	12.2	12.5
Mining	4.9	3.8	4.1	3.6	2.7	2.5
Other exports	0.1	0.1	0.1	0.1	0.1	0.1
Imports, f.o.b.	-17.4	-15.5	-16.4	-17.0	-17.2	-17.2
Oil and gas	-3.2	-2.7	-2.6	-2.4	-2.1	-2.0
Non-oil and gas	-14.3	-12.9	-13.9	-14.6	-15.1	-15.1
Consumption	-1.4	-1.5	-1.7	-1.8	-1.6	-1.6
Raw materials	-9.7	-8.3	-9.3	-9.7	-10.1	-10.1
Capital goods	-2.8	-2.9	-2.7	-2.8	-3.1	-3.2
Other	-0.3	-0.2	-0.2	-0.2	-0.2	-0.2
Services, net	-1.5	-1.3	-1.1	-1.1	-1.0	-1.0
Services exports	1.8	2.4	2.6	2.8	2.9	2.9
Services imports	-3.3	-3.7	-3.8	-3.8	-3.9	-3.9
Primary income, net	-2.7	-2.6	-2.6	-2.6	-2.6	-2.6
Secondary income, net	0.4	0.4	0.4	0.4	0.4	0.3
Capital and financial account	**-0.7**	**0.7**	**0.9**	**1.8**	**2.0**	**2.2**
Capital account	0.0	0.0	0.0	0.0	0.0	0.0
Financial account	-0.7	0.7	0.9	1.7	2.0	2.2
Direct investment, net	1.4	1.1	1.2	1.3	1.3	1.3
Abroad, net	-0.6	-0.5	-0.6	-0.6	-0.7	-0.7
In Indonesia (FDI), net	1.9	1.6	1.8	1.9	2.0	2.0
Portfolio investment, net	-0.9	0.2	0.7	1.4	1.7	1.8
Equity, net	-0.1	-0.1	-0.1	-0.2	0.0	0.2
Portfolio debt, net	-0.8	0.3	0.9	1.7	1.7	1.7
Other investment, net	-1.2	-0.5	-1.1	-1.0	-1.0	-1.0
Assets, net	-1.2	-0.7	-0.9	-0.9	-0.8	-0.8
Liabilities, net	0.0	0.2	-0.2	-0.2	-0.2	-0.2
Errors and omissions	**0.0**	**-0.1**	**0.0**	**0.0**	**0.0**	**0.0**
Overall balance	**0.3**	**0.5**	**0.1**	**0.4**	**0.6**	**0.8**
Reserves and related items (- =increase)	**0.6**	**-0.7**	**-0.1**	**-0.4**	**-0.6**	**-0.8**
of which: valuation adjustment	0.9	-0.2	0.0	0.0	0.0	0.0
Memorandum items:						
Reserves assets (US$ billions)	137	146	147	154	164	177
Reserve assets (in percent of ARA)	118	123	119	117	119	123
Reserve assets (in percent of GDP)	10.4	10.7	10.3	9.9	9.7	9.8
Nominal GDP (in billions of U.S. dollars)	1,319	1,371	1,427	1,553	1,680	1,814

Sources: Data provided by Bank Indonesia; and IMF staff estimates.

Table 4. Indonesia: Medium-Term Macroeconomic Framework, 2022–29

	2022	2023	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.	2028 Proj.	2029 Proj.
Real GDP (percent change)	**5.3**	**5.0**	**5.0**	**5.1**	**5.1**	**5.1**	**5.1**	**5.1**
Domestic demand	3.8	5.1	5.0	5.2	5.1	5.1	5.1	5.1
Of which:								
Private consumption 1/	5.0	4.9	5.1	5.1	5.1	5.1	5.1	5.1
Government Consumption	-4.5	2.9	5.5	4.2	3.0	3.0	3.0	3.0
Gross fixed investment	3.9	4.4	5.0	5.7	5.7	5.7	5.6	5.6
Net exports 2/	0.8	0.7	0.2	0.2	0.3	0.3	0.3	0.3
Statistical discrepancy 2/	0.9	-0.4	0.0	0.0	0.0	0.0	0.0	0.0
Output gap (in percent)	**-1.1**	**-0.3**	**-0.2**	**-0.1**	**0.0**	**0.0**	**0.0**	**0.0**
Saving and investment (in percent of GDP)								
Gross investment 3/	29.7	30.5	30.5	30.6	30.7	30.8	30.9	31.0
Gross national saving	30.7	30.4	29.6	29.3	29.3	29.4	29.5	29.6
Prices (12-month percent change)								
Consumer prices (end period)	5.4	2.8	2.8	2.7	2.6	2.5	2.5	2.5
Consumer prices (period average)	4.1	3.7	2.9	2.8	2.6	2.6	2.5	2.5
Public finances (percent of GDP)								
General government revenue	15.2	15.0	14.8	14.9	15.0	15.0	15.0	15.1
General government expenditure	17.4	16.6	17.1	17.6	17.5	17.4	17.3	17.2
General government balance	-2.2	-1.6	-2.3	-2.6	-2.5	-2.4	-2.3	-2.2
General government primary balance	-0.2	0.5	-0.3	-0.6	-0.3	-0.1	0.0	0.1
General government debt	40.1	39.6	39.5	39.4	39.3	39.1	38.8	38.3
Balance of payments (billions of U.S. dollars)								
Current account balance	13.2	-1.9	-12.3	-20.5	-24.2	-25.5	-27.3	-30.3
In percent of GDP	1.0	-0.1	-0.9	-1.3	-1.4	-1.4	-1.4	-1.4
Trade balance	62.7	46.5	34.8	30.1	29.4	32.8	34.9	39.6
In percent of GDP	4.8	3.4	2.4	1.9	1.8	1.8	1.8	1.9
Oil and gas	-24.8	-19.7	-20.9	-18.3	-13.8	-14.2	-14.3	-15.8
Overall balance	4.0	6.3	0.8	6.7	9.6	13.7	14.9	14.2
Gross reserves								
In billions of U.S. dollars (end period)	137.2	146.4	147.2	153.9	163.5	177.3	192.1	206.3
In months of prospective imports	6.2	6.1	5.5	5.2	5.1	5.2	5.2	5.2
As a percent of short-term debt 4/	205.9	209.3	198.4	192.4	189.6	192.7	193.5	190.9
Total external debt								
In billions of U.S. dollars	396.5	408.5	419.0	439.4	461.6	482.8	509.9	540.0
In percent of GDP	30.1	29.8	29.4	28.3	27.5	26.6	26.0	25.6
Credit								
Private sector credit growth (percent)	10.1	9.2	10.5	11.3	9.5	9.6	9.5	9.5
Credit-to-GDP gap (percent) 5/	-2.1	-0.9	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:								
Oil production (thousands of barrels per day)	800	797	794	791	788	785	782	779
Indonesian oil price (period average, in U.S. dollars per barrel)	92.4	76.9	77.0	72.6	69.4	67.1	65.5	64.4
Nominal GDP (trillions of rupiah)	19,588	20,892	22,555	24,367	26,274	28,313	30,499	32,851
Nominal GDP (billions of U.S. dollars)	1,319	1,371	1,427	1,553	1,680	1,814	1,959	2,111

Sources: Data provided by the Indonesian authorities; and IMF staff estimates and projections.

1/ Includes NPISH consumption.

2/ Contribution to GDP growth.

3/ Includes changes in stock.

4/ Short-term debt on a remaining maturity basis.

5/ Follows the guidance of the Basel Committee on Banking Supervision.

Table 5. Indonesia: Summary of Central Government Operations, 2022–27
(In trillions of rupiah)

	2022	2023	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.
Revenues and grants	**2,636**	**2,784**	**2,956**	**3,224**	**3,478**	**3,755**
Of which: tax revenues	2,035	2,154	2,325	2,561	2,776	3,009
Oil and gas revenues	226	186	187	189	179	176
Tax revenues	78	69	61	63	55	54
Nontax revenues	149	117	125	126	123	122
Non-oil and gas revenues	2,404	2,585	2,762	3,026	3,290	3,569
Tax revenues	1,957	2,098	2,263	2,498	2,720	2,955
Income tax	920	993	1,073	1,171	1,276	1,388
VAT	688	764	831	935	1,018	1,105
Other	349	340	359	392	426	463
Nontax revenues	447	488	498	528	570	614
Grants	6	13	8	9	9	10
Expenditure and net lending	**3,096**	**3,121**	**3,474**	**3,867**	**4,140**	**4,441**
Current expenditure	1,872	1,780	2,089	2,271	2,430	2,578
Personnel	402	412	504	550	599	652
Material goods	426	430	487	526	557	586
Subsidies	253	270	276	252	236	235
Of which : energy subsidies	172	164	179	148	123	113
Fuel	116	96	107	111	96	85
Electricity	56	69	72	37	26	28
Interest	386	440	443	503	585	648
Other current expenditure	404	228	378	438	453	458
Development expenditure	402	464	465	567	641	711
Capital spending	241	307	307	397	458	514
Social assistance spending 1/	162	157	157	170	183	197
Transfers to local governments	816	877	921	1,030	1,069	1,152
Of which : transfers for infrastructure 2/	242	254	277	313	319	344
Overall balance	**-460**	**-337**	**-518**	**-644**	**-663**	**-686**
Financing	460	337	518	644	663	686
Net issuance of government securities	504	446	554	674	693	716
Program and project loans (net)	27	-24	29	35	36	38
SOE recapitalization and land acquisition	-64	-63	-62	-61	-60	-59
Other	-7	-22	-3	-5	-6	-8

Sources: Data provided by the Indonesian authorities; and IMF staff estimates and projections.

1/ Some social assistance spending was reclassified to other expenditure in 2016.
2/ Special purpose transfers (DAK) for physical infrastructure and Village Fund transfers. Starting 2017, 25 percent of general transfer and revenue sharing is included.

Table 6. Indonesia: Summary of Central Government Operations, 2022–27

(In percent of GDP, unless otherwise indicated)

	2022	2023	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.
Revenues and grants	**13.5**	**13.3**	**13.1**	**13.2**	**13.2**	**13.3**
Of which: tax revenues	10.4	10.3	10.3	10.5	10.6	10.6
Oil and gas revenues	1.2	0.9	0.8	0.8	0.7	0.6
Tax revenues	0.4	0.3	0.3	0.3	0.2	0.2
Nontax revenues	0.8	0.6	0.6	0.5	0.5	0.4
Non-oil and gas revenues	12.3	12.4	12.2	12.4	12.5	12.6
Tax revenues	10.0	10.0	10.0	10.3	10.4	10.4
Income tax	4.7	4.8	4.8	4.8	4.9	4.9
VAT	3.5	3.7	3.7	3.8	3.9	3.9
Other	1.8	1.6	1.6	1.6	1.6	1.6
Nontax revenues	2.3	2.3	2.2	2.2	2.2	2.2
Grants	0.0	0.1	0.0	0.0	0.0	0.0
Expenditure and net lending	**15.8**	**14.9**	**15.4**	**15.9**	**15.8**	**15.7**
Current expenditure	9.6	8.5	9.3	9.3	9.2	9.1
Personnel	2.1	2.0	2.2	2.3	2.3	2.3
Material goods	2.2	2.1	2.2	2.2	2.1	2.1
Subsidies	1.3	1.3	1.2	1.0	0.9	0.8
Of which : energy subsidies	0.9	0.8	0.8	0.6	0.5	0.4
Fuel	0.6	0.5	0.5	0.5	0.4	0.3
Electricity	0.3	0.3	0.3	0.2	0.1	0.1
Interest	2.0	2.1	2.0	2.1	2.2	2.3
Other current expenditure	2.1	**1.1**	1.7	1.8	1.7	1.6
Development expenditure	2.1	2.2	2.1	2.3	2.4	2.5
Capital spending	1.2	1.5	1.4	1.6	1.7	1.8
Social assistance spending 1/	0.8	0.8	0.7	0.7	0.7	0.7
Transfers to local governments	4.2	4.2	4.1	4.2	4.1	4.1
Of which : transfers for infrastructure 2/	1.2	1.2	1.2	1.3	1.2	1.2
Overall balance	**-2.4**	**-1.6**	**-2.3**	**-2.6**	**-2.5**	**-2.4**
Memorandum items:						
Net issuance of government securities	2.6	2.1	2.5	2.8	2.6	2.5
SOE recapitalization and land acquisition	0.3	0.3	0.3	0.3	0.2	0.2
Primary balance (percent of GDP)	-0.4	0.5	-0.3	-0.6	-0.3	-0.1
Cyclically-adjusted primary balance (percent of GDP)	-0.2	0.5	-0.3	-0.6	-0.3	-0.1
Capital spending and transfers (percent of GDP) 3/	2.5	2.7	2.6	2.9	3.0	3.0
General government debt (percent of GDP)	40.1	39.6	39.5	39.4	39.3	39.1
Indonesian crude oil price (US$ per barrel)	92.4	76.9	77.0	72.6	69.4	67.1
Oil production (thousands of barrels per day)	800	797	794	791	788	785
Nominal GDP (in trillions of rupiah)	19,588	20,892	22,555	24,367	26,274	28,313

Sources: Data provided by the Indonesian authorities; and IMF staff estimates and projections.

1/ Some social assistance spending was reclassified to other expenditure in 2016.

2/ Special purpose transfers (DAK) for physical infrastructure and Village Fund transfers. Starting 2017, 25 percent of general transfer and revenue sharing is included.

3/ Sum of capital spending and transfers for infrastructure.

Table 7. Indonesia: Summary of General Government Operations, 2022–27

	2022	2023	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.
			(In trillions of rupiah)			
Total revenue and grants	**2,972**	**3,131**	**3,343**	**3,641**	**3,928**	**4,241**
Taxes	2,269	2,406	2,595	2,853	3,091	3,349
Taxes on income, profits, and capital gains	998	1,062	1,135	1,234	1,331	1,442
Taxes on goods and services	915	986	1,077	1,203	1,311	1,423
VAT and luxury taxes	688	764	831	935	1,018	1,105
Excise	227	222	246	269	292	318
Taxes on international trade and transactions	91	64	75	83	90	97
Taxes not elsewhere classified	266	294	308	333	359	387
Grants	6	13	8	9	9	10
Other revenue	696	712	740	780	828	882
Total expenditure	**3,401**	**3,476**	**3,861**	**4,285**	**4,591**	**4,927**
Expense	2,647	2,605	2,927	3,191	3,358	3,553
Of which :						
Compensation of employees	996	1,045	1,188	1,289	1,395	1,510
Purchases/use of goods and services	426	430	487	526	557	586
Interest	386	440	443	503	585	648
Energy subsidies	172	164	179	148	123	113
Social benefit	217	221	234	261	291	326
Net acquisition of nonfinancial assets	754	871	934	1,095	1,233	1,373
Net lending/borrowing	**-429**	**-345**	**-518**	**-644**	**-663**	**-686**
Net acquisition of financial assets	102	-177	65	66	66	67
Of which : policy lending	2	0	0	0	0	0
Net incurrence of liabilities	531	167	583	710	729	753
			(In percent of GDP)			
Total revenue and grants	**15.2**	**15.0**	**14.8**	**14.9**	**15.0**	**15.0**
Taxes	11.6	11.5	11.5	11.7	11.8	11.8
Taxes on income, profits, and capital gains	5.1	5.1	5.0	5.1	5.1	5.1
Taxes on goods and services	4.7	4.7	4.8	4.9	5.0	5.0
VAT and luxury taxes	3.5	3.7	3.7	3.8	3.9	3.9
Excise	1.2	1.1	1.1	1.1	1.1	1.1
Taxes on international trade and transactions	0.5	0.3	0.3	0.3	0.3	0.3
Taxes not elsewhere classified	1.4	1.4	1.4	1.4	1.4	1.4
Grants	0.0	0.1	0.0	0.0	0.0	0.0
Other revenue	3.6	3.4	3.3	3.2	3.2	3.1
Total expenditure	**17.4**	**16.6**	**17.1**	**17.6**	**17.5**	**17.4**
Expense	13.5	12.5	13.0	13.1	12.8	12.6
Of which :						
Compensation of employees	5.1	5.0	5.3	5.3	5.3	5.3
Purchases/use of goods and services	2.2	2.1	2.2	2.2	2.1	2.1
Interest	2.0	2.1	2.0	2.1	2.2	2.3
Energy subsidies	0.9	0.8	0.8	0.6	0.5	0.4
Social benefit	1.1	1.1	1.0	1.1	1.1	1.1
Net acquisition of nonfinancial assets	3.8	4.2	4.1	4.5	4.7	4.9
Net lending/borrowing	**-2.2**	**-1.6**	**-2.3**	**-2.6**	**-2.5**	**-2.4**
Net acquisition of financial assets	0.5	-0.8	0.3	0.3	0.3	0.2
Of which : policy lending	0.0	0.0	0.0	0.0	0.0	0.0
Net incurrence of liabilities	2.7	0.8	2.6	2.9	2.8	2.7
Memorandum items:						
General government debt (In percent of GDP)	40.1	39.6	39.5	39.4	39.3	39.1
Nominal GDP (In trillions of rupiah)	19,588	20,892	22,555	24,367	26,274	28,313

Sources: Data provided by the Indonesian authorities; and IMF staff estimates and projections.

Table 8. Indonesia: Monetary Survey, 2022–27

	2022	2023	2024 Proj.	2025 Proj.	2026 Proj.	2027 Proj.
			(In trillions of rupiah)			
Net foreign assets	**1,898.2**	**1,967.3**	**1,998.8**	**2,091.6**	**2,233.1**	**2,439.7**
Claims on nonresidents	2,555.0	2,658.5	2,716.8	2,809.6	2,951.0	3,157.7
Central bank	2,152.2	2,277.3	2,335.6	2,428.4	2,569.8	2,776.5
Other depository corporations	402.8	381.2	381.2	381.2	381.2	381.2
Liabilities to nonresidents	-656.8	-691.2	-718.0	-718.0	-718.0	-718.0
Central bank	-152.7	-219.1	-245.8	-245.8	-245.8	-245.8
Other depository corporations	-504.1	-472.2	-472.2	-472.2	-472.2	-472.2
Net domestic assets	**6,629.8**	**6,859.2**	**7,705.8**	**8,587.7**	**9,490.8**	**10,430.3**
Net claims on central government	2,369.4	2,217.5	2,118.5	1,991.5	1,896.1	1,896.1
of which: held by Bank Indonesia	1,133.4	1,012.5	851.7	822.7	793.8	804.7
Claims on state and local government	3.3	2.3	2.5	2.7	2.9	3.2
Claims on public nonfinancial corporations	443.4	425.4	459.3	496.2	535.0	576.5
Claims on NBFIs	474.5	551.2	595.1	642.9	693.2	746.9
Claims on private sector	5,996.0	6,545.8	7,232.7	8,047.0	8,808.8	9,652.0
Corporates	2,799.8	3,074.1	...	...	...	...
Households	3,196.2	3,471.7	...	...	...	...
Capital and Reserves (-)	2,122.0	2,310.2	2,467.9	2,651.0	2,848.1	3,047.3
Other items, net (-, including discrepancy)	534.8	572.8	234.4	-58.4	-402.9	-602.8
Broad money	**8,528.0**	**8,826.5**	**9,704.7**	**10,679.3**	**11,723.9**	**12,870.0**
Currency in circulation	897.8	975.9	1,073.0	1,180.8	1,296.3	1,423.0
Transferable deposits	4,598.8	4,690.2	5,156.8	5,674.7	6,229.8	6,838.8
Other deposits	3,006.9	3,132.0	3,443.6	3,789.4	4,160.1	4,566.7
Securities	24.6	28.4	31.3	34.4	37.8	41.5
Other liabilities	**410.7**	**498.0**	**234.4**	**-58.4**	**-402.9**	**-602.8**
			(Annual percentage change)			
Net foreign assets	**4.9**	**3.6**	**1.6**	**4.6**	**6.8**	**9.3**
Net domestic assets	**9.4**	**3.5**	**12.3**	**11.4**	**10.5**	**9.9**
Claims on private sector	10.1	9.2	10.5	11.3	9.5	9.6
Corporates	11.7	9.8	...	...	...	...
Households	8.8	8.6	...	...	...	...
Broad money	8.4	3.5	9.9	10.0	9.8	9.8
			(In percent of GDP, end of period)			
Net foreign assets	**9.7**	**9.4**	**8.9**	**8.6**	**8.5**	**8.6**
Net domestic assets	**33.8**	**32.8**	**34.2**	**35.2**	**36.1**	**36.8**
Claims on private sector	30.6	31.3	32.1	33.0	33.5	34.1
Corporates	14.3	14.7	...	...	...	...
Households	16.3	16.6	...	...	...	...
Broad money	**43.5**	**42.2**	**43.0**	**43.8**	**44.6**	**45.5**
Memorandum items:						
Base money (annual percentage change)	23.9	-1.5	4.0	6.0	7.0	7.4
Velocity (nominal GDP/broad money)	2.3	2.4	2.3	2.3	2.2	2.2
Nominal GDP (in trillions of rupiah)	19,588	20,892	22,555	24,367	26,274	28,313

Sources: IMF, International Financial Statistics; and IMF staff estimates.

Table 9. Indonesia: Financial Soundness Indicators, 2020–24

(In percent, unless otherwise indicated)

	2020	2021	2022	2023	2024	
					Latest observation	
Depository institutions						
Capital adequacy						
Regulatory capital to risk-weighted assets	22.1	24.0	24.1	25.8	24.3	Q1
Core Tier-1 capital to risk-weighted assets	20.5	22.4	22.6	24.2	22.7	Q1
Capital to assets	12.6	13.2	13.3	13.4	12.8	Q1
Large exposures to capital	79.9	59.8	62.3	76.8	83.5	Q1
Asset quality						
Nonperforming loans to total gross loans	2.6	2.6	2.1	2.0	2.0	Q1
Nonperforming loans, net of provisions to capital	4.3	3.6	2.9	3.0	3.5	Q1
Specific provisions to nonperforming loans	68.3	71.0	71.2	67.6	66.0	Q1
Earning and profitability						
Return on assets	1.5	1.8	2.4	2.7	2.6	Q1
Return on equity	7.1	9.0	12.4	14.4	15.3	Q1
Interest margin to gross income	61.0	60.5	66.5	64.6	62.8	Q1
Trading income to gross income	6.6	4.9	2.6	2.9	2.5	Q1
Noninterest expenses to gross income	47.0	43.4	45.3	44.6	42.2	Q1
Personnel expenses to noninterest expenses	40.5	42.9	40.9	38.6	41.1	Q1
Liquidity and funding						
Liquid assets to total assets	17.5	20.0	18.3	16.1	14.9	Q1
Liquid assets to short-term liabilities	25.6	29.6	26.6	24.0	22.2	Q1
Customer deposits to total (non-interbank) loans	103.2	110.6	110.0	106.2	105.9	Q1
Sensitivity to market risk						
Net open position in foreign exchange to capital	7.1	6.7	2.9	4.6	5.6	Q1
Foreign currency denominated loans to total loans	12.2	12.5	13.2	13.1	13.7	Q1
Foreign currency denominated liabilities to total liabilities	18.3	18.2	19.4	20.2	20.8	Q1
Gross asset position in financial derivatives to capital	2.5	1.3	1.8	1.2	1.5	Q1
Gross liability position in financial derivatives to capital	1.9	0.9	1.8	1.3	1.6	Q1
Nonfinancial corporates						
Corporate debt (in percent of GDP) 1/	41.9	39.5	37.9	37.8	38.1	Q1
Leverage						
Total liabilities to total assets	48.9	46.4	46.9	45.4	41.9	Q1
Profitability 2/						
Return on assets	8.2	10.7	19.7	11.4	10.7	Q1
Liquidity 2/						
Current assets to current liabilities	194.3	204.4	203.3	198.1	223.2	Q1
Liquid assets to current liabilities	124.1	141.9	141.5	123.1	129.2	Q1
Debt servicing capacity						
Companies with negative equity (in percent of total assets)	4.1	3.4	3.1	3.0	2.9	Q1
Companies with negative equity (in percent of total firms)	8.0	8.6	8.1	7.1	6.8	Q1
Households						
Household debt (in percent of GDP)	17.7	17.3	16.1	16.5	15.4	Q1
Real estate markets						
Residential real estate prices (year-on-year percentage change, average)	1.3	1.2	2.0	1.7	1.9	Q1
Residential real estate loans to total loans	11.4	11.5	13.0	13.5	13.5	Q1
Commercial real estate loans to total loans	13.6	13.0	15.0	14.7	14.6	Q1

Sources: Authorities data; Bloomberg L.P.; IMF, *Financial Soundness Indicators* ; Bank for International Settlements; Haver Analytics; CEIC Data Co. Ltd.; and IMF staff estimates.

1/ Includes domestic and foreign bonds issuance data from BIS.
2/ Based on capitalization-weighted average of listed companies.

Table 10. Indonesia: Key Poverty and Social Indicators

Population	278.7	millions	(2023)
Life expectancy at birth, total	68.3	years	(2022)
Mortality rate, under 5	21.3	per 1,000 live births	(2022)
Secondary school enrollment:			
Total	99.0	percent	(2022)
Female	99.4	percent	(2022)
Male	98.6	percent	(2022)
GINI index	38.8		(2023)
Income share held by highest 20%	46.3	percent	(2023)
Income share held by lowest 20%	7.3	percent	(2023)
Poverty rate	9.4	percent	(2023)
CO2 emissions	2.1	metric tons per capita	(2020)
Population with basic drinking water	94.1	percent	(2022)
Population with basic sanitation	88.2	percent	(2022)
Human development index	0.71		(2022)
Rank	112		
Gender inequality index	0.44		(2022)

Sources: World Bank; Badan Pusat Statistik; and United Nations Development Programme.

Table 11. Indonesia: Implementation of Past Fund Advice		
Policies	**2023 Article IV Consultation Recommendations**	**Actions Since 2023 Article IV Consultation**
Fiscal Policy	Maintaining a broadly neutral fiscal stance below the 3 percent deficit ceiling.	The overall deficit narrowed to 1.7 percent of GDP in 2023.
	Concrete medium-term fiscal framework, including revenue mobilization, energy subsidy reform, expanded social protection, and greater transparency.	The authorities have stated plans to enhance efficiency in energy subsidy via better targeting.
Monetary Policy	BI should maintain a tightening bias in its monetary policy stance and act decisively if inflation surprises on the upside.	BI hiked the policy rate by 25 bps in October 2023, to 6 percent, and further to 6.25 percent in April 2024 to stabilize the currency given external economic uncertainty and possible imported inflation pressures and has stayed on hold since then.
	The exchange rate should continue to play its role as a shock absorber.	The rupiah depreciated against the US dollar by an average of 2.6 percent in 2023. Indonesia's de facto exchange rate regime is classified as floating. The external position in 2023 was broadly in line with the level implied by medium-term fundamentals and desirable policies.
Financial Sector Policies	Keeping the macroprudential policy stance broadly unchanged, with the aim of moving toward a more neutral stance in 2024 as the credit gap narrows.	BI has kept its macroprudential policies (MPPs) loose to avoid a drag on growth.
	Regulatory forbearance measures and incentives should be tightened, including the expiration of the relaxation of loan classification rules.	Regulatory forbearance measures were discontinued in March 2024 as envisaged.
	Continued strengthening of the regulatory and institutional framework will be important.	The authorities have largely implemented the 2017 FSAP Recommendations
Structural Policies and Climate Change	The authorities should consider domestic policies that achieve their objectives of increasing value added in production, while phasing out export restrictions and not extending the restrictions to other commodities.	For 2024, the authorities allocated increased spending budgets in the education, social protection, infrastructure, and health areas, which are considered key to support growth, which is a step in the right direction. Existing restrictions have been maintained, with extensions to some new commodities.
	Broader reforms would be needed to reach net zero, including the gradual reduction of energy subsidies and carbon pricing.	The authorities published a Comprehensive Investment and Policy Plan (CIPP) including the phase out of the on-grid coal-fired power plants, under the JETP. A plan to transition off-grid power generation is also needed.
	Broad-based structural reforms, with priorities on reducing labor market restrictions, improving the investment climate, human capital development, infrastructure investment, and financial deepening.	The incoming Prabowo administration has yet to detail its agenda.

Table 12. Indonesia: Status of Key 2017 FSAP Recommendations[1]	
Key Recommendations	**Authorities' Actions**
Institutional and Legal Arrangements	
Revise OJK Law to give primacy to objective of safeguarding stability, BI Law to include a financial stability and macroprudential policy mandate focused on systemic risk of the financial system, with access to data; and LPS Law to focus objectives on the maintenance of financial stability, continuity of critical functions, protection of insured deposits, and minimization of resolution costs.	**Partially implemented**. There has been structural reform in the Indonesian financial sector through the issuance of an Omnibus law (FSOL) on 12 January 2023 which revises 17 laws related to the financial sector, including OJK Law, BI Law, and LPS Law. The Law 4/2023 aims to strengthen institutional authorities and governance in the financial sector, which includes BI, OJK, LPS, and MoF. Furthermore, the Law focuses on the objectives, duties, and authority of the three institutions (BI, OJK and LPS) to bolster financial system stability, while still prioritizing their independence. The FSOL included the objective of the OJK on financial stability ("actively maintain financial system stability") but has not established the hierarchy of the OJK multiple objectives, giving primacy to the objective of safeguarding stability.
Amend the Insurance Law to specify policyholder protection as principal objective of OJK.	**Partially implemented**. Article 4 letter c of the OJK Law stipulates the purpose of OJK, that all activities in the financial services sector should be able to provide protection of the consumers and public interest. Furthermore, in article 1 number 15 of the OJK Law stipulates that the scope of consumers includes policy holders in Insurance. Thus, the OJK Law has stated that the protection of policyholders in insurance is one of OJK's objectives.
Strengthen legal protection of supervisors and officials of all agencies involved in financial oversight and crisis management in line with global standards.	**Pending**. In addition to being regulated under Article 45 of BI Law and Article 48 of PPKSK Law (Law Number 9 of 2016), the legal protection of supervisors and officials of all agencies (MoF, BI, OJK, LPS) has been further strengthened by Article 27 section 2 of Law Number 2 Year 2020 (Government Regulation in Lieu of Law No. 1 Year 2020 on State Financial Policy and Financial System Stability for Handling COVID-19 Pandemic and/or Encounter the Threat to National Economy and/or Stability of Financial Systems). The law provides legal protection to KSSK members, secretariat and members of Secretariat, as well as officials or employees of MOF, BI, OJK, LPS who carry out their functions in good faith and according to prevailing laws and regulations. In 2023, the FSOL introduced legal protection for OJK and its staff against lawsuits arising from actions or omissions made in good faith. However, the OJK Law does not explicitly provide for the supervisor and their staff to be adequately protected against the costs of defending their actions or omissions.
Financial Sector Oversight	
Introduce a foreign currency liquidity coverage ratio.	**Pending**. Indonesia has complied with the Basel standards by supervising banks' foreign exchange liquidity position using an additional monitoring tool based on the significance of such foreign exchange to the bank's financial position. OJK has been imposing LCR based on significant currencies as a monitoring tool as stipulated in regulation No.42/POJK.03/2015 concerning Liquidity Coverage Ratio Requirement for Commercial Banks. Article 51 and its elucidation of such regulation requires banks to monitor LCR based on significant currencies.
Strengthen BI's capacity for systemic risk analysis and macroprudential stress tests, and OJK's capacity for regulatory stress tests; OJK should do bottom-up stress tests for D-SIBs regularly.	**Implemented**. BI and OJK have been implementing Joint Stress Test (JST) regularly once a year since 2017. BI is responsible for designing macroeconomic scenarios, namely baseline, adverse I (for severe), and adverse II (for moderate), based on potential medium-term global and domestic economic risks, and performing Top-Down Stress Test (TDST) and Granular Stress Test (GST) by using those scenarios. Meanwhile, OJK is responsible for coordinating Bottom-Up Stress Test (BUST) for systemic banks (D-SIB) and other large banks. The results of TDST, GST and BUST are compared and discussed to generate a final report that will be reported to the Board Meeting of BI and OJK.
Reduce OJK's silo structure, including by revising the OJK Law to remove the responsibilities of individual Commissioners for the supervision of specific sectors.	**Partially implemented**. Currently several steps have been taken to reduce silo structures at the OJK, including implementing the RKPT forum for cross-sectoral supervision. Further, OJK has issued and implemented various integrated regulation as joint commitment from OJK to develop and strengthen integrated supervision of financial service sector. The FSOL introduced the requirement that the OJK Charmain leads and conducts systemic assessment of the integrated supervision of financial conglomerates. While there has been some progress in reducing OJK's silo structure, further efforts are required to fully implement this recommendation. FSAP 2024 has not conducted a comprehensive review of its implementation.
Governance of Financial Conglomerates (FCs)	
Strengthen the banking supervisory approach and continue enhancing supervisory practices for financial conglomerates (FCs).	**Partially implemented**. OJK's Committee of Integrated Supervision (RKPT) decided on February 5, 2021 that 14 FCs meet the definition criteria according to OJK Regulation No.45/POJK.03/2020 on FCs (POJK 45). The FCs, through its Lead Entities, have also prepared and submitted their Corporate Charters to OJK as stipulated in Article 5 of POJK 45. 2017 FSAP noted that the OJK has identified 49 FCs in Indonesia at that time, and as mentioned above, the OJK has identified only 14 FCs under the new regulation. FSAP 2024 has not conducted a full review of this recommendation's implementation (this area was reviewed only from consolidated supervision perspective).

Table 12. Indonesia: Status of Key 2017 FSAP Recommendations (Continued)

Key Recommendations	Authorities' Actions
Strengthen corporate governance practices within the financial system, including the boards of commissioners' (BoC) oversight roles and responsibilities.	**Partially implemented**. OJK has stipulated regulations No.55/POJK.03/2016 and 17/POJK.03/2023on Good Corporate Governance for Commercial Banks and No. 18/POJK.03/2016 on the Implementation of Risk Management for Commercial Banks. The regulations require BoC to conduct active. oversight over the bank's activities and to provide advice to the board of directors to improve corporate governance and risk management practice. FSAP 2024 has not conducted a full review of this recommendation's implementation. For banking supervision, FSAP 2024 recommended that the OJK should continue playing a proactive role in strengthening the BoC's role and responsibilities.
Introduce legal provisions for licensed non-operating financial holding companies.	**Implemented**. OJK established its Regulation Number 45/POJK.03/2020 concerning FCs that defines FC as Financial group of company which has combining assets equal to or larger than IDR100,000,000,000,000 (one hundred trillion Rupiah) and consists of more than 1 (one) type of business activities. The regulation requires the FC to appoint or establish a financial company to be the holder of the financial conglomeration. The type of businesses that can be included in financial conglomerates are banks, insurance, multi-finance companies, and securities. In addition, the discussion of financial sector reform has also included the strengthening of OJK function in supervising financial holding companies, including the appointment of financial entity or establishment of new entity as the controller of the FC. FSOL introduced requirements for licensing of financial holding company (it requires the controlling party of financial conglomerates to form financial holding company) and mandated the OJK to issue regulations regarding financial conglomerates, including the licensing of financial holding company, the fit and proper test of the board members of the financial holding company, and other necessary prudential aspects within two years after the promulgation of the law (by January 2025). The implementation of these FSOL requirements remains a high priority. FSAP 2024 has not conducted a full review of this recommendation's implementation.
Crisis Management and Resolution, and Safety Nets	
Revise the PPKSK Law to clarify the role of the KSSK as solely a coordination body; limit the involvement of the President to approving public funding.	**Partially Implemented**. Law No. 4 of 2023 regulates the role of KSSK as a coordination body as reflected in the duties and powers of KSSK. KSSK is in charge of coordinating in handling the problem of Systemically Important Banks and coordinating the steps to be taken by the members of the Financial System Stability Committee to support the implementation of the problems handling of Systemically Important Banks by the Indonesia Deposit Insurance Corporation. Under the constitution, it is the President who can declare a crisis or state of emergency situation as it was last done during the COVID-19 pandemic (Art. 12 of the 1945 Constitution). In addition, he can declare a system wide Bank Restructuring Program.
Adjust the emergency liquidity assistance (ELA) framework to ensure it is effective.	**Implemented**. In response to the COVID-19 pandemic, the Government enacted Law No. 2 of 2020 concerning State Financial Policy and Financial System Stability for Handling COVID-19 Pandemic, which included enhancement of BI's mandate and power in crisis conditions. As a follow up, BI amended its crisis management and resolution framework, particularly regarding BI crisis management protocol and provision of PLJP/PLJPS.
Amend the relevant laws to ensure that resolution powers can be exercised over FCs.	**Pending**. Resolution power over FCs is amongst the topics to be discussed and considered in the amendment of LPS Law under the discussion of financial sector reform.
Develop resolution options and implementation guidelines for banks, and resolvability assessment and resolution planning frameworks for D-SIBs.	**Implemented**. Indonesian authorities have regulated the recovery plan under the Law Number 9 of 2016 concerning Prevention and Mitigation of Financial System Crisis, which was complemented by issuance of OJK Regulation (POJK) No. 14/POJK.03/2017 concerning Recovery Plan for Systemic Banks require Domestically Systemic Important Bank to have recovery plan. On the resolution plan, the Indonesia Deposit Insurance Corporation (IDIC) promulgated IDIC Regulation Number 1/2021 on Resolution Plan in March 2021. Under the regulation, DSIBs and selected non-DSIBs must prepare resolution plan starting in 2022. The regulation also stipulates the resolvability assessment requirement.
Financial Integrity	
Integrate key money laundering or terrorist financing (ML/TF) risks in the priorities and operations of relevant agencies.	**Implemented**. OJK has implemented FATFs' recommendations regarding risk-based AML/CFT, which were adopted as the National Committee of Prevention and Eradication of the Criminal Act of Money Laundering (NCC)s' commitment as stipulated in the National Strategy. This includes risk-based regulation and supervision, and cooperation with related institutions/ministries in the context of information exchange on money laundering offenses. Financial institutions and supervisors have been equipped with National Risk Assessment (NRA) and Sectoral Risk Assessment (SRA) guidelines for the financial services sector as compiled by OJK.
Finalize and implement risk-based AML/CFT supervisory tools.	**Implemented**. In accordance with the FATF Recommendation, OJK has carried out AML/CFT risk-based supervision. Based on the results of the MER FATF 2023, OJK is considered to have a good understanding of ML/TF risks through the establishment of effective regulations and the implementation of effective risk-based AML/CFT supervision.

Table 12. Indonesia: Status of Key 2017 FSAP Recommendations (Concluded)

Key Recommendations	Authorities' Actions
Financial Deepening and Inclusion	
Develop an integrated roadmap for promoting financial deepening and inclusion.	**Implemented**. Financial Deepening. The National Financial Market Development and Deepening Strategy (SN-PPPK) has been reviewed and revi sed in light of the pandemic and changing global and domestic economic and financial market conditions. The financial market deepening is a part of Pillar II "Development of the Financial Services Ecosystem" in The OJK Financial Services Sector Master Plan 2021-2025. In line with the SN-PPPK, OJK and all members of FK-PPPK undertake financial market deepening initiatives. OJK supports the development of the primary and secondary bond and Sukuk market infrastructure. In November 2020, the Indonesian Stock Exchange launched an electronic trading platform phase 2 (Alternative Market Operator System). In addition, in 2019, KPEI as CCP in the stock exchange market also developed a third-party Repo system to support Repo transactions in the market in the absence of standardized services to support the implementation of Repo transactions in accordance with existing regulations. Financial Inclusion. The Government of Indonesia issued Presidential Regulation No. 114 of 2020 on National Strategy for Financial Inclusion (SNKI) that has provided an impetus to accelerate Indonesia's financial inclusion. BI has developed a new approach to enhance financial inclusion focusing on integrating economic activities and financial inclusion.
Enhance bond yield curve by consolidating debt issuance and improving secondary markets.	**Implemented**. IDX has launched IGBF (Indonesia Government Bond Futures) products to improve the secondary market as derivative instruments. As of November 2020, IGBF offered two new series available for market players via the Indonesia Stock Exchange Platform. However, the participation of market players and the demand for the above instruments still need to be further improved. Regarding consolidating debt issuance to enhance the government bond yield curve, the government is actively undertaking prudent portfolio management such as issuing benchmark series in the primary market to maintain the bond yield curve. The government also conducts debt switching transactions to smooth out the maturity profile and reduce non-liquid series in the secondary market. A private placement is also available as an option to increase the volume of specific series to create a more active secondary market. In terms of debt switch in 2021, the government has conducted an auction to buy back bonds in the domestic market on June 17, 2021, which obtained bids amount submitted by bidders of IDR 11.5 trillion with the nominal won by the government amounting to IDR 4.98 trillion. The second auction was held on September 23, 2021. The nominal bids submitted by bidders was IDR 11.24 trillion, while the nominal amount won by the government was IDR 7.07 trillion. In the global market, the government announced the successful completion of its inaugural Tender Offer/Liability Management (LM) Exercise launched on eight series of Notes (the Old Bonds) on September 20, 2021. The LM Exercise was well-received by global investors, and the total amount of tender instructions received across all series of Notes reached USD 2.68 Bio. However, the government decided to repurchase a total nominal amount of USD 1.16 bio as part of our general cash management program and a broader plan to manage our external liabilities. To enhance trading activity, the government, in cooperation with Indonesia Stock Exchange, has been developing an electronic trading platform for government bonds to provide more transparency on price discovery under the over-the-counter market. Currently, the Government and IDX have introduced the system and continue to improve infrastructure with the cooperation of government bond primary dealers. It is expected that the program will be launched formally in the first quarter of 2022.
Further strengthen the enforcement of credit and risk management regulations.	**Partially implemented**. OJK has issued a number of regulations to strengthen banks' credit and risk management practices. OJK is in the process of issuing an updated regulation on Risk-Weighted Assets for Credit Risk and Market Risk which will be implemented by 2023 in line with the target agreed by the Basel Committee on Banking Supervision.
Revise the insurance supervisory framework (three strikes-approach) to allow prompt actions.	**Implemented**. FSAP recommendation has been implemented through issuance of OJK Regulation Number 17/POJK.05/2017 concerning the imposition of administrative sanctions in the form of revocation of business license without prior imposition of other administrative sanctions in cases where there is a drastic deterioration of financial conditions, shareholders are not cooperative and no way of solving the problems that endanger the interests of policyholders, the insured, or the participants.

[1] The updates presented in this table on FSAP recommendations are based on the authorities' inputs. IMF staff's assessment are summarized in bold.

Table 13. Indonesia: Integrating Fund Surveillance and Capacity Development

Area	Surveillance Recommendations	Capacity Development Recent Actions/Plans
Monetary policy and central bank communication	Clear and focused communication on monetary and financial policy is critical, especially during times of financial stress.	The Fund provided technical assistance covering communication on monetary policy and financial stability, as well as monetary and exchange rate modeling and the development of repo market and interest rate benchmark reform.
Statistics	Use of big data for timely economic monitoring could support prompt policy decision making.	The Fund provided technical assistance on the use of big data to develop an enhanced residential property price index, on developing the integrated sectoral accounts and balance sheets statistics, and on compiling Financial Soundness Indicators. The Fund also provided virtual assistance on expanding the coverage of the producer price index to include additional service activities. In July 2023, the Fund provided TA and a workshop on compiling macro-relevant climate change statistics. In February 2024, there was a TA mission on Government Finance Statistics.
Fiscal framework, tax policy and administration	Implement a medium—term revenue strategy (MTRS) to raise revenue by at least 3 percent of GDP over five years to finance spending on infrastructure, education, and health.	The Fund provided technical assistance in August 2017 to set a strategy, which includes specific recommendations on tax policy and administration reforms. The Fund organized a workshop with the authorities on fiscal rules in November 2023. In April 2024, technical assistance was provided on tax diagnostics.
Public financial management	Improve fiscal governance, including infrastructure governance and public investment management.	The Fund conducted Indonesia's PIMA in February 2019, which lists priority actions to improve public investment management, and a Public Sector Balance Sheet Analysis in October 2019. The Fund also provided technical assistance and workshops on budget analysis and costing methodologies. During 2022-23, the Fund provided technical assistance and held workshops on fiscal risks and transparency, cash management and budget execution, fiscal decentralization and local government endowment funds, and internal control. In January 2024, technical assistance on public private partnerships and government guarantees was provided,
Financial sector	Improve financial oversight, crisis management framework, and the monitoring of corporate vulnerabilities.	The Fund provided technical assistance on financial conglomerate supervision, risk-based supervision, financial crisis management, and on strengthening bank and corporate stress testing frameworks, systemic risk analysis and household risk analysis. The Fund also provided a virtual workshop on fintech regulation and supervision, drawing on global practices to identify opportunities to strengthen domestic frameworks.
Financial sector supervision during COVID-19	Preparation and timely implementation of financial regulatory and supervisory response to the pandemic.	The Fund provided virtual workshops on financial supervision, IFRS9 implementation and supervisory treatment under COVID-19.

Annex I. External Sector Assessment

<table>
<tr><td colspan="7"> Overall Assessment: The external position in 2023 was broadly in line with the level implied by medium-term fundamentals and desirable policies. In the medium term, exchange rate flexibility and structural policies are expected to contain the CA deficit. Although external financing needs appear sustainable, Indonesia's reliance on foreign portfolio investment exposes the economy to sharp swings in market sentiment and risk premia, and to fluctuations in global financial conditions. Potential Policy Responses: Maintaining external balance will require structural reforms to enhance productivity and facilitate post-COVID-19 sectoral adjustments. Reforms should include (i) higher infrastructure investment, higher social spending to foster human capital development and strengthen the social safety net, (ii) a reduction of restrictions on inward FDI and external trade, including by moving away from non-tariff barriers, (as discussed in the 2023 Article IV consultation), and (iii) promotion of greater labor market flexibility. Flexibility of the exchange rate should continue to support external stability with the ongoing structural transformation of the Indonesian economy. </td></tr>
<tr><td>Foreign Asset and Liability Position and Trajectory</td><td colspan="6"> Background. Indonesia's NIIP remained unchanged at –19.0 percent of GDP at the end of 2023, reflecting an increase of 1.1 percentage points in gross external assets and liabilities, respectively to 35.3 and 54.3 percent of GDP. The increase in gross external assets was supported by higher FDI abroad, portfolio investment, and reserve assets. In turn, the increase in gross external liabilities reflected fully the increase in FDI inflows. Indonesia's gross external debt remained moderate at 29.8 percent of GDP at end-2023, declining marginally from 30.1 percent of GDP in 2022. External rollover risks in the short-term are contained as reflected in the large share of long-term debt. Assessment. The level and composition of the NIIP and gross external debt indicate that Indonesia's external position is sustainable and subject to limited rollover risk. But the relatively high dependence on foreign portfolio investment (20.1 percent of GDP in 2023) makes Indonesia highly vulnerable to swings in global financial market sentiment. The NIIP as a percent of GDP is projected to stabilize at current levels in the medium term, as robust nominal GDP growth offsets the projected small CA deficits. </td></tr>
<tr><td>2023 (% GDP)</td><td colspan="2">NIIP: –19.0</td><td>Gross Assets: 35.3</td><td>Res. Assets: 10.7</td><td>Gross Liab.: 54.3</td><td>Debt Liab.: 29.8</td></tr>
<tr><td>Current Account</td><td colspan="6"> Background. The CA balance posted a small deficit of 0.1 percent of GDP in 2023, after two consecutive years of surpluses (1.0 percent in 2022). The deficit in 2023 was primarily driven by the non-oil and gas trade balance, reflecting weaker growth in major trading partners, and a broad-based decline in commodity prices. The resilience in domestic demand translated into a smaller decline in imports relative to exports. On the savings-investment side, higher government revenue was broadly offset by lower private savings and higher private investment. The CA deficit is expected to widen moderately in 2024 due to lower commodity prices, while robust domestic demand will support import growth. The CA deficit is expected to remain close to the norm throughout the projection horizon. Assessment. Staff estimates a CA gap of 0.8 percent of GDP for 2023, consistent with an estimated cyclically adjusted CA deficit of −0.3 percent of GDP, a staff assessed norm of −0.8 percent of GDP, and an adjustor of 0.3 percentage points for demographics.[1] Considering the uncertainty in the estimation of the norm, the CA gap for 2023 is in the range of 0.3 to 1.3 percent of GDP. EBA-identified policy gaps are estimated at 1.7 percent of GDP, driven by a tighter fiscal stance than in other countries (1.3) and underspending on healthcare (0.6). </td></tr>
<tr><td>2023 (% GDP)</td><td>CA: –0.1</td><td>Cycl. Adj. CA: –0.3</td><td>EBA Norm: –0.8</td><td>EBA Gap: 0.5</td><td>Staff Adj.: 0.3</td><td>Staff Gap: 0.8</td></tr>
<tr><td>Real Exchange Rate</td><td colspan="6"> Background. The average REER depreciated by 3.7 percent in 2023 compared to the average level in 2022 (or 3.2 percent relative to the pre-COVID 2016-19 average). The depreciation materialized on the back of the rapid tightening in global monetary policy and high volatility in global financial markets. The rupiah managed to recover some of the losses against major currencies toward the end of 2023, as a result of easier global financial conditions, and BI's policy responses (including a one-off interest rate hike). As of end-April 2024, the REER was 2.4 percent below its 2023 average. Assessment. The staff CA gap estimate of 0.8 percent of GDP implies a REER gap of –5.0 percent (applying an estimated elasticity of 0.16). The REER index and level models point to REER gaps of 0.8 percent and – </td></tr>
</table>

	15.9 percent, respectively. Consistent with the staff CA gap, staff assesses the REER gap in the range of –7.9 to –2.1 percent, with a midpoint of –5.0 percent.
Capital and Financial Accounts: Flows and Policy Measures	**Background**. Net capital and financial flows returned to positive territory in 2023 (0.7 percent of GDP), after negative net flows of -0.7 percent of GDP in 2022. The recovery in financial inflows was driven by portfolio investment, particularly concentrated in the last quarter of 2023, reflecting the introduction of several open market instruments by BI to attract capital flows to support international reserves. Net FDI inflows continued to decline, to 1.1 percent of GDP in 2023 (1.4 percent in 2022 and 1.5 percent in 2021). The share of nonresident holdings of rupiah-denominated government bonds ticked up by 0.6 percentage points to 14.9 percent in 2023, but remain considerably below the 39 percent share in 2019. **Assessment**. The recovery in portfolio investment flows in 2023 helped support the small negative CA deficit in 2023. Continued strong policies, focused on safeguarding the fiscal position, advancing financial deepening, and easing broad-based structural reforms that promote an enabling business environment should help sustain capital inflows in the medium term, particularly in periods of high market volatility.
FX Intervention and Reserves Level	**Background**. Since mid-2013, Indonesia has had a more flexible exchange rate policy framework. Official foreign reserves increased to US$146 billion in 2023, from US$137 billion in 2022, reflecting the increase in deposits abroad and the withdrawal of government's foreign loans during the year, which more than offset the decline in securities from FX intervention. **Assessment**. The current level of reserves (10.7 percent of GDP, 123 percent of the IMF's reserve adequacy metric, and 6.1 months of prospective imports) should provide a sufficient buffer against external shocks. Predetermined drains also seem manageable, although they have increased related to short positions on financial derivatives. In line with the IPF, the use of FXI remains appropriate under certain shocks and circumstances, particularly when shocks trigger spikes in market premia given shallow FX markets, while remaining mindful of preserving reserve buffers.

[1] Indonesia is among a few countries with low life expectancy at prime age and demographic indicators are adjusted to account for this. As a result, the model-estimated CA norm is adjusted by subtracting 0.3 percentage points.

Annex II. Risk Assessment Matrix[1]

	Source of Risks	Likelihood	Expected Impact	Policy Recommendation
Global	**Conjunctural. Intensification of regional conflicts.** Escalation or spread of the conflict in Gaza and Israel, Russia's war in Ukraine, and/or other regional conflicts or terrorism disrupt trade (e.g., energy, food, tourism, supply chains), remittances, FDI and financial flows, payment systems, and increase refugee flows.	**High**	**Medium.** Commodity prices, financial flows, and supply chains would be the key transmission channels. For commodities, a deterioration in the terms of trade would lead to lower growth and worsen the external balance. A sharp increase in energy or food prices may strain the fiscal position to the extent these prices remain subject to administrative measures; price adjustments would impact inflation. Supply chain disruptions could affect production and trade, and raise inflation. Capital outflows could tighten financial conditions and create exchange rate volatility.	Use monetary policy to stabilize inflation. If fiscal space is available, well-targeted and temporary support measures could be considered to protect the vulnerable, but should be calibrated to protect fiscal space and limit further pressure on inflation. The exchange rate should remain flexible and market determined. FXI could be used to address disorderly market conditions or the impact of shocks under frictions (e.g., a sharp pickup in the UIP premium in shallow financial markets) while preserving strong buffers.
	Conjunctural. Commodity price volatility. A succession of supply disruptions (e.g., due to conflicts, export restrictions, and OPEC+ decisions) and demand fluctuations causes recurrent commodity price volatility, external and fiscal pressures in EMDEs, cross-border spillovers, and social and economic instability.	**High**	**Medium.** Impact will depend on whether (and which) commodity prices rise or decline, given Indonesia's net commodity exporter status on various key commodities. A rise in the price of oil, of which Indonesia is a net importer, and/or a decline in price of commodities for which Indonesia is a net exporter (e.g., nickel, crude palm oil) would lead to lower growth and worsen the external balance. A sharp increase in energy prices would reverse the moderation in inflation.	Use available policy space (fiscal and monetary policy) countercyclically to stabilize output and inflation. Seek to make progress on reforming energy subsidies. The exchange rate should remain flexible and determined by market forces.
	Structural. Deepening geo-economic fragmentation. Broader conflicts, inward-oriented policies, and weakened international cooperation result in a less efficient configuration of trade and FDI, supply disruptions, protectionism, policy uncertainty, technological and payments system fragmentation, rising shipping and input costs, financial stability, a fracturing of international monetary system, and lower growth.	**High**	**Medium/High.** A weaker global economy would reduce export demand and capital flows, including FDI. Higher uncertainty could weigh on investment and capital flows. Supply chain disruptions could push up inflation. In the long-term, lower productivity gains from the transfer of knowledge and technology embedded in trade and investments from frontier economies could hinder the pace of economic convergence.	Carefully use policy space (fiscal and monetary policy) to stabilize inflation and output, calibrating the response to a long-lasting shock (or protracted series of shocks) to maintain margin for maneuver. Accelerate horizontal structural reforms to support the transition to an economy that is more productive, greener, open and integrated to be more resilient to global geo-economic fragmentation.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Nonmutually exclusive risks may interact and materialize jointly.

Source of Risks	Likelihood	Expected Impact	Policy Recommendation
Conjunctural. Abrupt global slowdown. Global and idiosyncratic risk factors cause a synchronized sharp growth downturn, with recessions in some countries, adverse spillovers through trade and financial channels, and market fragmentation triggering sudden stops in EMDEs. • **China**: Sharper-than-expected contraction in the property sector weighs on private demand, further amplifies local government fiscal strains, and results in disinflationary pressures and adverse macro-financial feedback loops. • **Europe**: Intensifying fallout from Russia's war in Ukraine, supply disruptions, tight financial conditions, and real estate market corrections exacerbate economic downturn. • **U.S.**: Amid tight labor markets, inflation remains elevated, prompting the Fed to keep rates higher for longer and resulting in more abrupt financial, housing, and commercial real estate market correction.	Medium	**Medium/High.** Lower GDP growth, due to weaker investment, export demand and commodity prices; robust domestic demand may offer some offset depending on the size of the shock. The shock could trigger a weakening or reversal in capital flows, leading to currency volatility and tighter domestic credit conditions; possible impact on vulnerable sectors of the population.	Use available fiscal space countercyclically to provide targeted support, while allowing the exchange rate to act as a shock absorber. FXI could be used to address disorderly market conditions or the impact of shocks under frictions (e.g., a sharp pickup in the UIP premium in shallow financial markets) while preserving strong buffers.
Conjunctural. Monetary policy miscalibration. Amid high economic uncertainty, major central banks loosen policy stance prematurely, hindering disinflation, or keep it tight for longer than warranted, causing abrupt adjustments in financial markets and weakening the credibility of central banks.	Medium	**Medium.** Reduced interest rate differentials vis-à-vis the U.S. and major financial centers could lead to capital outflows and put downward pressure on the Rupiah, which may be amplified by disruptive market conditions.	Ensure monetary policy settings remain in line with inflation target objectives. Allow the exchange rate to act as a shock absorber. FXI could be used to address disorderly market conditions (e.g., a sharp pickup in the UIP premium) while keeping strong buffers.
Conjunctural. Systemic financial instability. High interest rates and risk premia and asset repricing amid economic slowdowns and political uncertainty (e.g., from elections) trigger market dislocations, with cross-border spillovers and an adverse macro-financial feedback loop affecting weak banks and NBFIs.	Medium	**Medium**. Direct transmission of instability to the domestic financial sector is likely to be contained amidst strong bank balance sheets and limited interlinkages. However, risk-off sentiment in global financial markets would tighten external financing conditions. Impact on economic activity in major trading partners and/or on commodity prices, if significant, could worsen the external balance, and could create exchange rate volatility.	Monitor spillovers to the domestic financial sector and stand ready to intervene if severe strains begin to emerge. With inflation within BI's target range, monetary policy could be eased to limit the impact on output—which will be enabled further if monetary policy begins to normalize in major economies. Allow the exchange rate to act as a shock absorber. FXI could be used to address disorderly market conditions or the impact of shocks under frictions (e.g., a sharp pickup in the UIP premium in shallow financial markets) while keeping strong buffers.

	Source of Risks	Likelihood	Expected Impact	Policy Recommendation
	Structural. Disorderly energy transition. A disorderly shift to net-zero emissions (e.g., owing to shortages in critical metals) and climate policy uncertainty cause supply disruptions, stranded assets, market volatility, and subdued investment and growth.	**Medium**	**Medium.** Impact will depend on nature of transition, due to Indonesia's position as a major producer/exporter of fossil fuels (e.g., coal) and critical minerals. An unanticipated acceleration in the pace of transition could raise credit and market risks, and generate stranded assets, weighing on financial sector balance sheets given exposures to carbon-intensive firms. However, a sharp increase in prices of critical minerals of which Indonesia is a major producer (e.g., nickel) could boost export values and corporate profits, providing a buffer, at least temporarily.	Continue enhancing domestic transition plan, including to manage and decommission coal-fired power plants to reduce risks of stranded assets. Strengthen climate risk assessment for the financial sector, monitoring of transition risk exposures, as well as disclosure and availability of data. Deploy broad horizontal structural reforms to support diversification, value-addition, and green growth.
	Structural. Extreme climate events. Extreme climate events driven by rising temperatures cause loss of human lives, severe damage to infrastructure, supply disruptions, low growth, and financial stability.	**Medium**	**Low.** Disruptions to economic activity are likely to be localized; becoming macro-critical only if they were to hit major production and/or population centers (including Jakarta) or in case of repeated events or compounding events (multiple shocks occurring simultaneously).	Prioritize targeted support to affected households and businesses, and reconstruction. Preemptively monitor financial sector risks that have geographical and/or sector concentrations that may be impaired in key areas particularly vulnerable to climate shocks (e.g., fisheries, or mining complexes in vulnerable locations). Continue disaster risk management preparedness, in line with already adopted disaster risk financing and insurance strategy in 2018, adaptive social protection roadmap in 2023, and current operationalization of the national "Pooling Fund Bencana – PFB" to manage disaster related financing needs.
Domestic	**Conjunctural. Acceleration of domestic demand.** Rising domestic economic confidence, which could arise, inter alia, from a more rapid and/or deeper than expected implementation of horizontal structural reforms.	**Medium**	**Medium.** Stronger private sector investment as economic prospects improve, contributing to a faster-than-projected closing of the output gap; the recovery in bank credit accelerates.	Fiscal and monetary policies should remain broadly neutral with a tightening bias; a tight monetary policy stance could be warranted if inflation picks up. MPPs should be tightened if credit growth accelerates, closing the credit gap earlier.

Annex III. Public and External Debt Sustainability Analysis[1]

Public Debt Sustainability

1. **Indonesia's public sector debt remains low**. General government debt reached 39.6 percent of GDP in 2023 from 30.6 percent in 2019, owing to the exceptional fiscal measures deployed in 2020-22 to fight the pandemic, during which the fiscal rule was temporarily suspended. Public debt is projected to gradually decline to around 38.3 percent of GDP over the medium-term, mainly driven by a negative cumulative interest rate-growth differential. Gross financing needs are expected to remain moderate, at about 5 percent of GDP over the medium-term. Debt coverage is adequate, and realism tools suggest projections of key debt drivers are within norms.

2. **The SRDSA suggests an overall low risk of sovereign stress**. Medium-term risks are assessed as low (in line with the mechanical signal from the SRDSF). The Debt Fan chart Module indicates an adequate balance of risks around the projected debt baseline. For the GFN Financeability Module, a combination of low GFNs and an initial high bank exposure to the government, result in moderate risks under a macro-fiscal and debt holder shock. Mitigating factors include a declining share of foreign holdings of local-currency debt, and relatively large cash buffers. Taken together, the aggregate MTI produces a mechanical "low" signal (Figure 1).

External Debt Sustainability

3. **Indonesia's external debt has been on a downward path after a temporary increase during the pandemic**. External debt stood at 30.1 percent of GDP in 2022, down from 34.9 percent of GDP at the end of 2021. Indonesia's external debt declined across all sectors, with the general government accounting for more than half of that decline, standing at 14.1 percent of GDP. External debt fell further to 29.8 percent of GDP by end-2023 (Figure 1 and Table 1), driven mainly by a decline in debt of other nonbanking sectors.

4. **External debt is projected to continue to gradually decline to 26 percent of GDP in the medium term**. In the baseline scenario, strong projected growth in nominal GDP more than offsets rising external financing needs as the current account widens somewhat, leading to a small decline in external debt as a share of GDP.

5. **External debt sustainability is robust to interest rate, current account and growth shocks, but is sensitive to exchange rate shocks** (Figure 2). A widening of the current account from projected levels would cause external debt to rise moderately (a one-standard deviation shock would increase external debt to 29 percent of GDP by 2029). Exchange rate depreciation would have the largest impact—a 30 percent depreciation in 2024 would raise external debt to 41 percent of GDP in 2025, and it would decline only slightly at the end of the forecasting horizon.

[1] Prepared by Raju Huidrom (APD), Amr Hosny (FAD) and Bruno Albuquerque (SPR).

Figure 1. Indonesia: Risk of Sovereign Stress

Horizon	Mechanical signal	Final assessment	Comments
Overall	...	**Low**	The overall risk of sovereign stress is assessed as "low", reflecting debt stabilization under the baseline and low levels of vulnerability in both the near and medium-term modules.
Near term 1/			
Medium term	**Low**	**Low**	Medium-term risks are assessed as "low" (in line with the aggregate medium-term mechanical signal) on the basis of balanced risks around the debt baseline, and manageable gross financing needs.
Fanchart	**Moderate**	...	
GFN	**Moderate**	...	
Stress test		...	
Long term	...	na	There are long-term risks from climate change adaptation needs. Adaptation costs are estimated at about 0.8 percent of GDP per year over the long-term. Fiscal reforms to create fiscal space to finance adaptation needs are critical over the longer run.
Sustainability assessment 2/	Not required for surveillance countries	na	na
Debt stabilization in the baseline			Yes

DSA summary assessment

Commentary: Indonesia is at a "low" overall risk of sovereign stress and debt is sustainable. Most indicators have started to normalize as the recovery from the COVID-19 shock has proceeded. Public debt is expected to gradually decline over the medium-term, driven mostly by a favorable interest-growth differential. Debt coverage is adequate, and realism tools sugget projections of key debt drivers are within norms. Medium-term solvency and liquidity risks are manageable. Over the longer run, reforms should continue to tackle risks from climate change.

Source: Fund staff.
Note: The risk of sovereign stress is a broader concept than debt sustainability. Unsustainable debt can only be resolved through exceptional measures (such as debt restructuring). In contrast, a sovereign can face stress without its debt necessarily being unsustainable, and there can be various measures—that do not involve a debt restructuring—to remedy such a situation, such as fiscal adjustment and new financing.
1/ The near-term assessment is not applicable in cases where there is a disbursing IMF arrangement. In surveillance-only cases or in cases with precautionary IMF arrangements, the near-term assessment is performed but not published.
2/ A debt sustainability assessment is optional for surveillance-only cases and mandatory in cases where there is a Fund arrangement. The mechanical signal of the debt sustainability assessment is deleted before publication. In surveillance-only cases or cases with IMF arrangements with normal access, the qualifier indicating probability of sustainable debt ("with high probability" or "but not with high probability") is deleted before publication.

Figure 2. Indonesia: Debt Coverage and Disclosures

	CG	GG	NFPS	CPS	Other	Comments
1. Debt coverage in the DSA: 1/	CG	GG (chosen)	NFPS	CPS	Other	
1a. If central government, are non-central government entities insignificant?					n.a.	

2. Subsectors included in the chosen coverage in (1) above:

Sector		Subsectors captured in the baseline	Inclusion
CPS / NFPS / GG: expected / CG	1	Budgetary central government	Yes
CPS / NFPS / GG: expected / CG	2	Extra budgetary funds (EBFs)	No
CPS / NFPS / GG: expected / CG	3	Social security funds (SSFs)	No
CPS / NFPS / GG: expected	4	State governments	Yes
CPS / NFPS / GG: expected	5	Local governments	Yes
CPS / NFPS	6	Public nonfinancial corporations	No
CPS	7	Central bank	No
CPS	8	Other public financial corporations	No

3. Instrument coverage:

Currency & deposits	Loans	Debt securities	Oth acct. payable 2/	IPSGSs 3/
chosen	chosen	chosen	chosen	chosen

4. Accounting principles:

Basis of recording		Valuation of debt stock		
Non-cash basis 4/ (chosen)	Cash basis	Nominal value 5/ (chosen)	Face value 6/	Market value 7/

5. Debt consolidation across sectors:

Consolidated	Non-consolidated
	chosen

Color code: chosen coverage; Missing from recommended coverage; Not applicable

Reporting on intra-government debt holdings

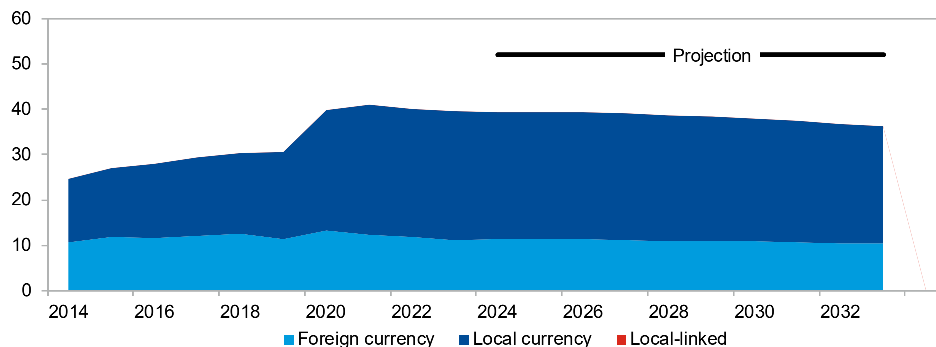
Issuer \ Holder		Budget. central govt	Extra-budget. funds (EBFs)	Social security funds (SSFs)	State govt.	Local govt.	Nonfin. pub. corp.	Central bank	Oth. pub. fin corp	Total
1	Budget. central govt									0
2	Extra-budget. funds									0
3	Social security funds									0
4	State govt.									0
5	Local govt.									0
6	Nonfin pub. corp.									0
7	Central bank									0
8	Oth. pub. fin. corp									0
	Total	0	0	0	0	0	0	0	0	0

1/ CG=Central government; GG=General government; NFPS=Nonfinancial public sector; PS=Public sector.
2/ Stock of arrears could be used as a proxy in the absence of accrual data on other accounts payable.
3/ Insurance, Pension, and Standardized Guarantee Schemes, typically including government employee pension liabilities.
4/ Includes accrual recording, commitment basis, due for payment, etc.
5/ Nominal value at any moment in time is the amount the debtor owes to the creditor. It reflects the value of the instrument at creation and subsequent economic flows (such as transactions, exchange rate, and other valuation changes other than market price changes, and other volume changes).
6/ The face value of a debt instrument is the undiscounted amount of principal to be paid at (or before) maturity.
7/ Market value of debt instruments is the value as if they were acquired in market transactions on the balance sheet reporting date (reference date). Only traded debt securities have observed market values.

Commentary: Coverage in this SRDSA is consolidated General Government debt, consistent with the Government Finance Statistics Manual, 2014. PPPs and public guarantees are not included.

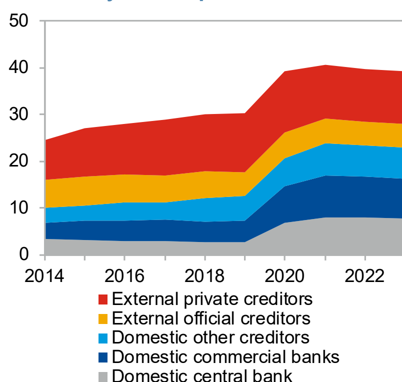
Figure 3. Indonesia: Public Debt Structure Indicators

Debt by Currency (percent GDP)



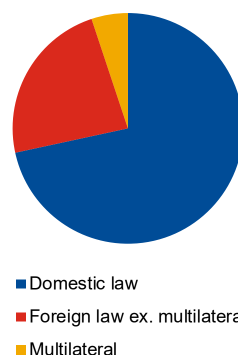
Note: The perimeter shown is general government.

Public Debt by Holder (percent of GDP)



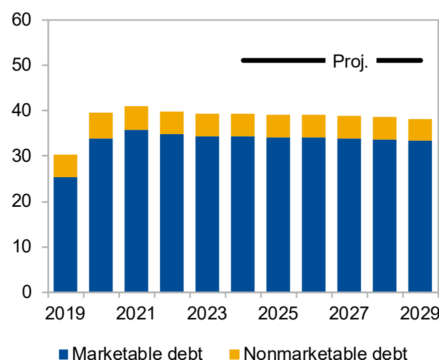
Note: The perimeter shown is general government.

Public Debt by Governing Law, 2023 (percent)



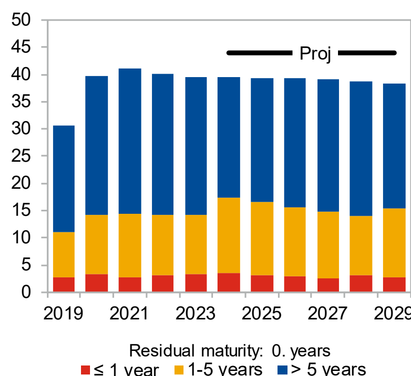
Note: The perimeter shown is general government.

Debt by Instruments (percent of GDP)



Note: The perimeter shown is general government.

Public Debt by Maturity (percent of GDP)



Note: The perimeter shown is general government.

Commentary: The currency composition and maturity profile of public debt are expected to remain about the same over the projection horizon. Domestic banks and the Central Bank (BI) increased their share of public debt holdings during the COVID years.

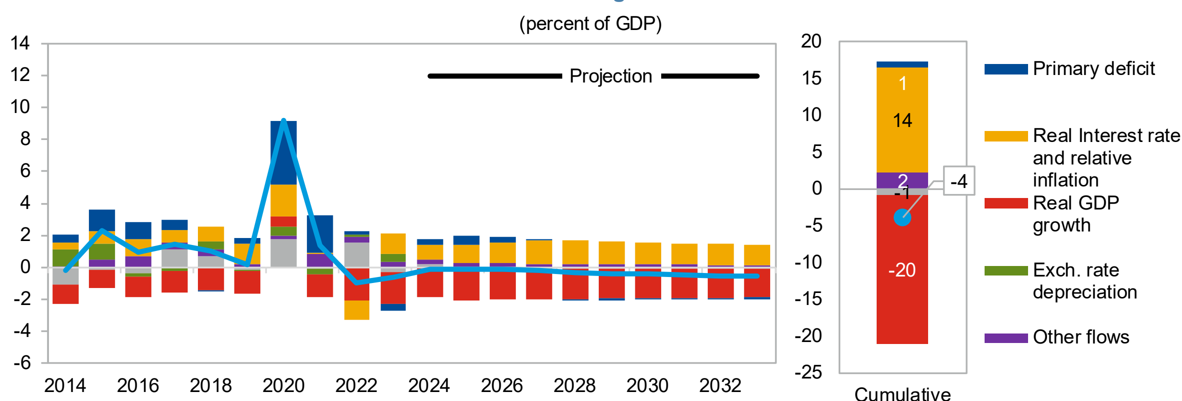
Figure 4. Indonesia: Baseline Scenario

(In percent of GDP, unless indicated otherwise)

	Actual	Medium-Term Projection						Extended Projection			
	2023	2024	2025	2026	2027	2028	2029	2030	2031	2032	2033
Public debt	39.6	39.5	39.4	39.3	39.1	38.8	38.3	37.9	37.4	36.9	36.3
Change in public debt	-0.6	-0.1	-0.1	-0.1	-0.2	-0.3	-0.4	-0.4	-0.5	-0.5	-0.6
Contribution of identified flows	-0.3	-0.3	0.1	0.0	-0.1	-0.2	-0.3	-0.4	-0.4	-0.4	-0.4
Primary deficit	-0.5	0.3	0.6	0.3	0.1	0.0	-0.1	-0.1	-0.1	-0.1	-0.1
Noninterest revenues	15.0	14.8	14.9	15.0	15.0	15.0	15.1	15.1	15.1	15.1	15.1
Noninterest expenditures	14.5	15.2	15.5	15.2	15.1	15.0	15.0	15.0	15.0	15.0	15.0
Automatic debt dynamics	-0.1	-0.9	-0.8	-0.6	-0.5	-0.4	-0.4	-0.5	-0.5	-0.5	-0.5
Real interest rate and relative inflation	1.3	1.0	1.1	1.3	1.4	1.5	1.4	1.4	1.3	1.3	1.3
Real interest rate	1.5	0.9	1.0	1.3	1.4	1.4	1.4	1.3	1.3	1.2	1.2
Relative inflation	-0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.0
Real growth rate	-1.9	-1.9	-1.9	-1.9	-1.9	-1.9	-1.9	-1.8	-1.8	-1.8	-1.8
Real exchange rate	0.5	…	…	…	…	…	…	…	…	…	…
Other identified flows	0.3	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.1
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
(minus) Interest Revenues	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other transactions	0.3	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.1
Contribution of residual	-0.3	0.2	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Gross financing needs	4.5	5.3	5.9	5.5	5.2	4.7	5.0	4.6	4.3	4.1	3.8
of which: debt service	5.0	4.9	5.4	5.2	5.0	4.7	5.1	4.7	4.4	4.2	3.9
Local currency	3.3	3.7	4.0	4.0	3.7	3.4	4.0	3.6	3.4	3.2	3.0
Foreign currency	1.7	1.2	1.3	1.2	1.3	1.2	1.1	1.1	1.0	1.0	0.9
Memo:											
Real GDP growth (percent)	5.0	5.0	5.1	5.1	5.1	5.1	5.1	5.1	5.1	5.1	5.1
Inflation (GDP deflator; percent)	1.5	2.9	2.8	2.6	2.6	2.5	2.5	2.5	2.5	2.4	2.3
Nominal GDP growth (percent)	6.7	8.0	8.0	7.8	7.8	7.7	7.7	7.7	7.7	7.7	7.7
Effective interest rate (percent)	5.6	5.4	5.7	6.1	6.3	6.4	6.3	6.2	6.1	6.0	5.9

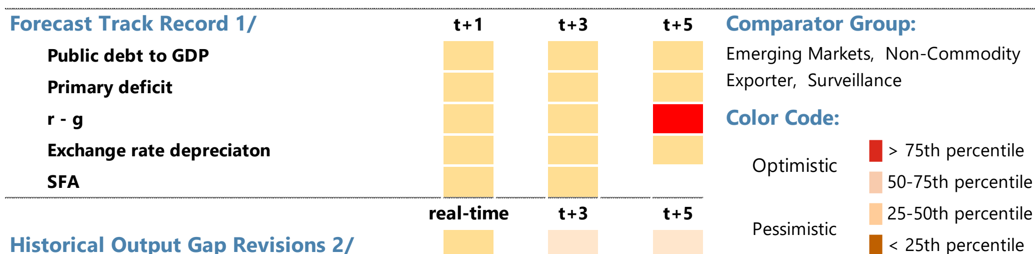
Contribution to Change in Public Debt

(percent of GDP)

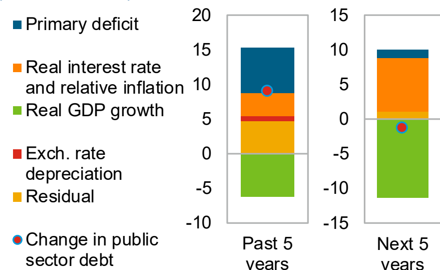


Commentary: Public debt is expected to decrease gradually from 39.6 percent of GDP in 2023 to 38.4 percent of GDP over the medium-term, mostly due to a favorable interest-growth differential. Gross financing needs are expected to remain manageable at around 5 percent of GDP over the medium-term.

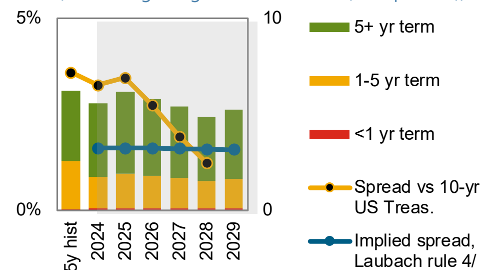
Figure 5. Indonesia: Realism of Baseline Assumptions



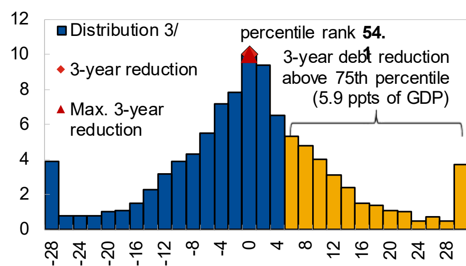
Public Debt Creating Flows
(Percent of GDP)



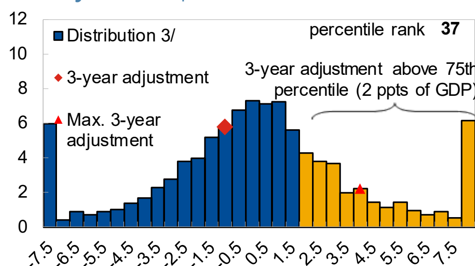
Bond Issuances (bars, debt issuances (RHS, %GDP); lines, avg marginal interest rates (LHS, percent))



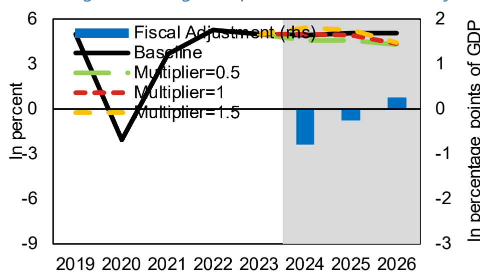
3-Year Debt Reduction
(Percent of GDP)



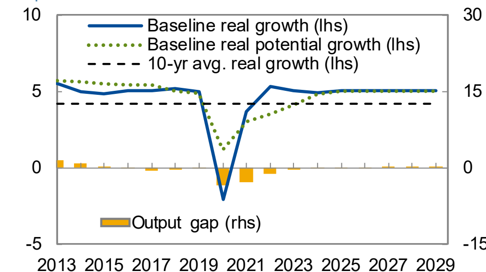
3-Year Adjustment in Cyclically-Adjusted Primary Balance (percent of GDP)



Fiscal Adjustment and Possible Growth Paths
(lines, real growth using multiplier (LHS); bars, fiscal adj. (RHS))



Real GDP Growth
(in percent)

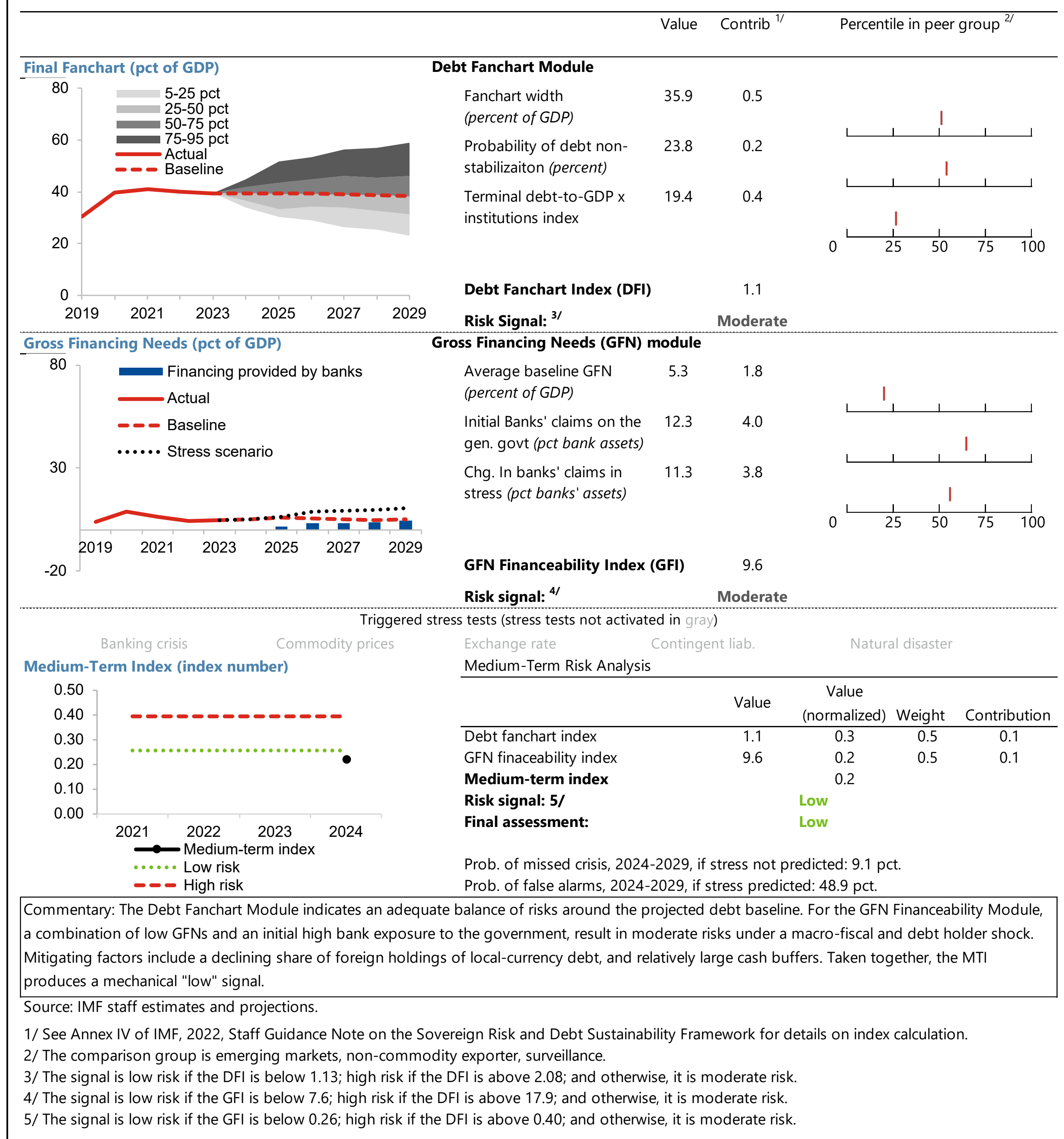


Commentary: Realism analysis does not point to major concerns. Forecast errors show some signs of past optimism in the underlying debt creating flows, but this is largely influenced by unexpectd outcomes during the COVID years. The projected 3-year fiscal adjustment and 3-year debt reduction are well within norms, and the real GDP growth path is in line with the assumed fiscal adjustment and potential growth.

Source : IMF Staff.

1/ Projections made in the October and April WEO vintage.
2/ Calculated as the percentile rank of the country's output gap revisions (defined as the difference between real time/period
3/ Data cover annual obervations from 1990 to 2019 for MAC advanced and emerging economies. Percent of sample on vertical ax
4/ The Laubach (2009) rule is a linear rule assuming bond spreads increase by about 4 bps in response to a 1 ppt increase in the projected debt-to-GDP ratio.

Figure 6. Indonesia: Medium-Term Assessment



Commentary: The Debt Fanchart Module indicates an adequate balance of risks around the projected debt baseline. For the GFN Financeability Module, a combination of low GFNs and an initial high bank exposure to the government, result in moderate risks under a macro-fiscal and debt holder shock. Mitigating factors include a declining share of foreign holdings of local-currency debt, and relatively large cash buffers. Taken together, the MTI produces a mechanical "low" signal.

Source: IMF staff estimates and projections.

1/ See Annex IV of IMF, 2022, Staff Guidance Note on the Sovereign Risk and Debt Sustainability Framework for details on index calculation.
2/ The comparison group is emerging markets, non-commodity exporter, surveillance.
3/ The signal is low risk if the DFI is below 1.13; high risk if the DFI is above 2.08; and otherwise, it is moderate risk.
4/ The signal is low risk if the GFI is below 7.6; high risk if the DFI is above 17.9; and otherwise, it is moderate risk.
5/ The signal is low risk if the GFI is below 0.26; high risk if the DFI is above 0.40; and otherwise, it is moderate risk.

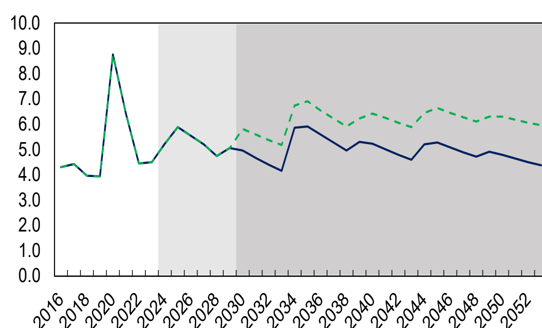
Figure 7. Indonesia: Long-Term Risk Analysis

Relevancy of long-term factors

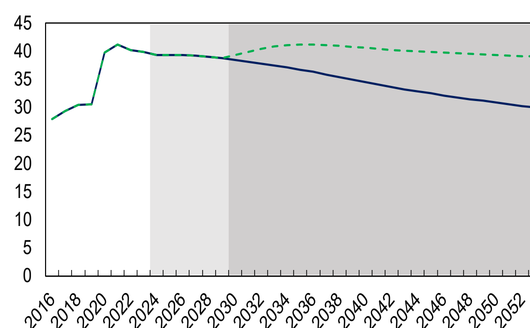
Topic	Vulnerability factors
Climate change	Sizeable adaptation needs over the long-term.
Demographics	n.a.
Long-term amortization	n.a.
Natural resource production	n.a.

Climate Change: Adaptation

GFN-to-GDP ratio



Total public debt-to-GDP ratio

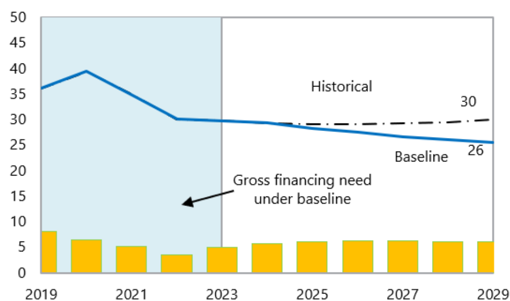


Commentary: The adaptation cost estimates are taken from Aligishiev, Bellon and Massetti (2022) and ESCAP (2019), and focus on two types of adaptation investments: strengthening physical assets and investing in coastal protection. In the case of Indonesia, these amount to about 0.8 percent of GDP per year over the long-term. Fiscal reforms to create fiscal space to finance adaptation needs will be critical over the longer run for Indonesia.

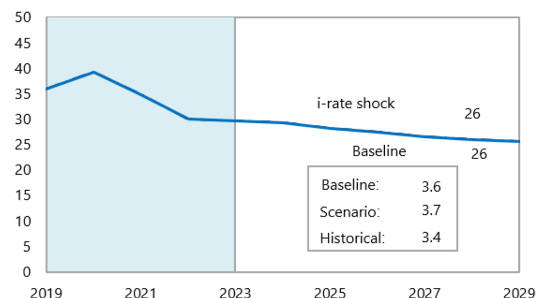
Figure 8. Indonesia: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)

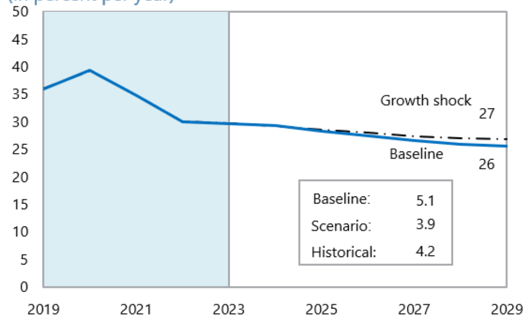
Baseline and Historical Scenarios



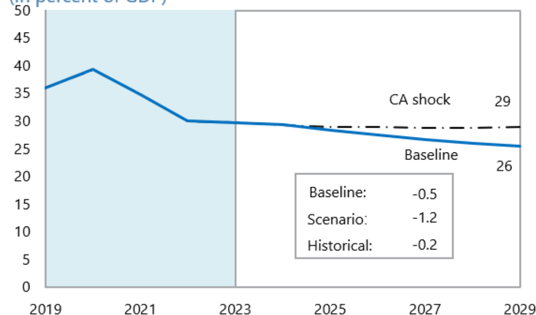
Interest Rate Shock
(In percent)



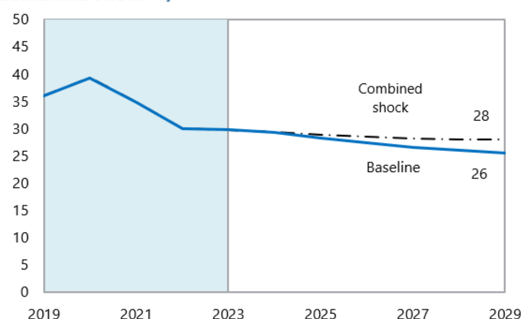
Growth Shock
(In percent per year)



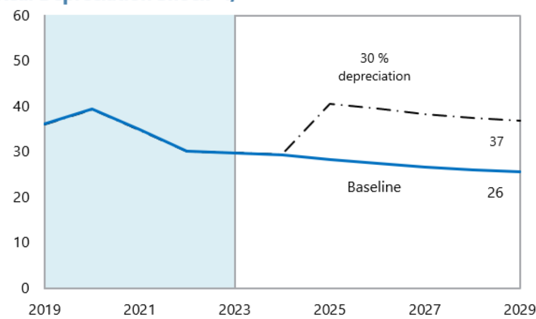
Noninterest Current Account Shock
(In percent of GDP)



Combined Shock 3/



Real Depreciation Shock 4/



Sources: International Monetary Fund, Country desk data; and staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2024.

Table 1. Indonesia: External Debt Sustainability Framework, 2019-2029

(In percent of GDP, unless otherwise indicated)

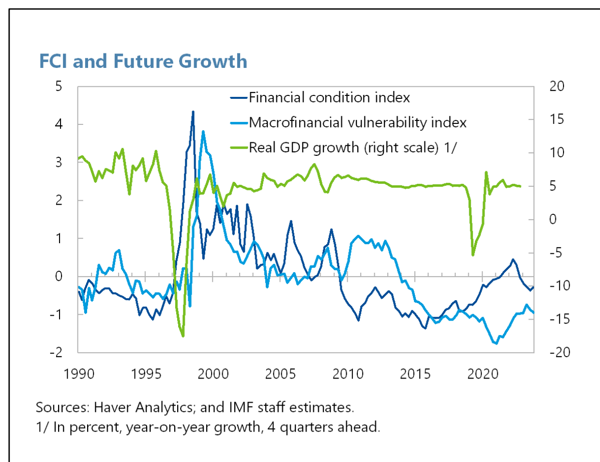
	Actual							Projections						
	2019	2020	2021	2022	2023			2024	2025	2026	2027	2028	2029	Debt-stabilizing non-interest current account 6/
Baseline: External debt	36.1	39.4	34.9	30.1	29.8			29.4	28.3	27.5	26.6	26.0	25.6	-2.6
Change in external debt	0.0	3.3	-4.5	-4.8	-0.3			-0.4	-1.0	-0.8	-0.9	-0.6	-0.5	
Identified external debt-creating flows (4+8+9)	-1.5	1.3	-6.1	-6.1	-2.2			-1.8	-1.3	-1.3	-1.5	-1.4	-1.4	
Current account deficit, excluding interest payments	1.6	-1.0	-1.6	-2.1	-0.9			-0.2	0.3	0.5	0.5	0.5	0.6	
Deficit in balance of goods and services	-0.4	1.8	2.5	3.2	2.1			1.3	0.9	0.8	0.8	0.9	0.9	
Exports	17.9	16.8	20.8	23.9	21.4			21.5	21.7	21.8	21.9	21.8	21.7	
Imports	-18.2	-15.1	-18.3	-20.7	-19.3			-20.2	-20.8	-21.0	-21.0	-20.9	-20.8	
Net nondebt creating capital inflows (negative)	-1.8	-0.9	-1.7	-1.4	-1.1			-1.3	-1.2	-1.4	-1.6	-1.6	-1.6	
Automatic debt dynamics 1/	-1.3	3.2	-2.8	-2.6	-0.2			-0.4	-0.4	-0.4	-0.4	-0.4	-0.4	
Contribution from nominal interest rate	1.1	1.4	1.3	1.1	1.0			1.0	1.0	0.9	0.9	0.9	0.9	
Contribution from real GDP growth	-1.7	0.8	-1.3	-1.7	-1.5			-1.4	-1.4	-1.3	-1.3	-1.2	-1.2	
Contribution from price and exchange rate changes 2/	-0.8	1.0	-2.8	-2.0	0.2			...	...	...	...	...	...	
Residual, including change in gross foreign assets (2-3) 3/	1.6	2.0	1.7	1.3	1.9			1.4	0.2	0.5	0.6	0.8	0.9	
External debt-to-exports ratio (in percent)	201.7	233.7	167.7	125.6	139.5			136.7	130.4	125.9	121.7	119.3	117.6	
Gross external financing need (in billions of U.S. dollars) 4/	90.5	67.7	61.6	46.2	68.5			82.2	94.7	104.2	111.7	119.3	129.5	
In percent of GDP	8.1	6.4	5.2	3.5	5.0			5.8	6.1	6.2	6.2	6.1	6.1	
Scenario with key variables at their historical averages 5/								29.4	29.2	29.1	29.2	29.5	30.0	-1.7
Key Macroeconomic Assumptions Underlying Baseline						10-Year Historical Average	10-Year Standard Deviation							
Real GDP growth (in percent)	5.0	-2.1	3.7	5.3	5.0	4.2	2.3	5.0	5.1	5.1	5.1	5.1	5.1	
GDP deflator in U.S. dollars (change in percent)	2.2	-3.4	8.0	5.6	-1.0	0.1	5.3	-0.8	3.5	3.0	2.8	2.8	2.6	
Nominal external interest rate (in percent)	3.4	3.6	3.6	3.6	3.6	3.4	0.3	3.6	3.6	3.6	3.6	3.6	3.6	
Growth of exports (U.S. dollar terms, in percent)	-5.6	-10.8	38.3	27.9	-7.3	4.9	17.5	4.7	10.0	8.8	8.2	7.7	7.4	
Growth of imports (U.S. dollar terms, in percent)	-6.6	-21.7	36.1	25.5	-3.2	3.8	19.1	8.8	12.4	9.3	7.9	7.5	7.3	
Current account balance, excluding interest payments	-1.6	1.0	1.6	2.1	0.9	-0.2	1.5	0.2	-0.3	-0.5	-0.5	-0.5	-0.6	
Net nondebt creating capital inflows	1.8	0.9	1.7	1.4	1.1	1.4	0.4	1.3	1.2	1.4	1.6	1.6	1.6	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in U.S. dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.
2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).
3/ For projection, line includes the impact of price and exchange rate changes.
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.
5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.
6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Annex IV. Growth at Risk[1]

The Growth at Risk (GaR) framework is used to assess the impact of macro-financial conditions on the probability distribution of future real GDP growth for Indonesia. Indonesia's near-term growth is most vulnerable to financial conditions. Downside risks have declined, but a severe slowdown event in China could jeopardize the outlook.

1. **We apply the Growth at Risk (GaR) framework to Indonesia**.[2] GaR analysis quantifies the impact of macro-financial conditions on the probability distribution of future real GDP growth. A large set of variables is aggregated into three main regressors—called partitions, using principal component analysis. Quarterly data coverage runs from q1:1990-q4:2023. For this exercise, variables under the *financial conditions* partition include various measures of domestic and external financial market returns, bond spreads, the real long-term interest rate, the VIX, the exchange rate and foreign reserves. *Macro-financial vulnerabilities* include credit conditions, debt metrics, house price growth, the current account balance, and bank indicators (liquid-assets, capital adequacy, and equity-to-assets ratio). *Other factors* include trading-partner growth, commodity prices, and consumer confidence. Despite some recent accommodation, financial conditions have tightened since 2015, while macro-financial vulnerabilities have recently started to creep up from a low base.

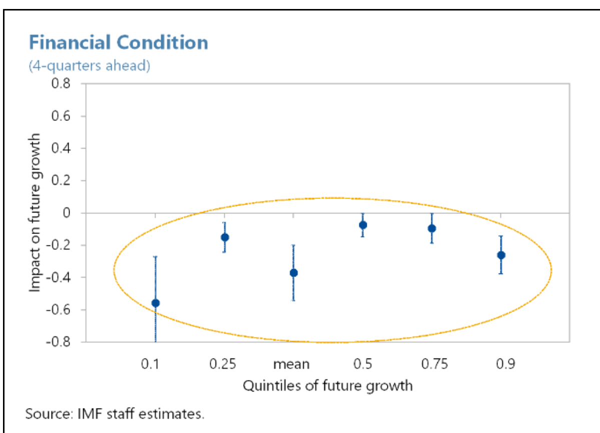


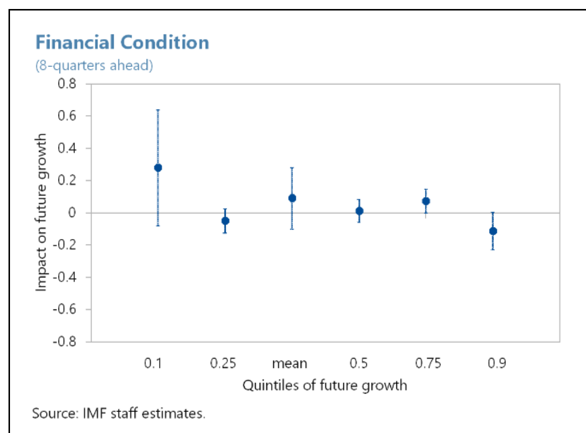
Sources: Haver Analytics; and IMF staff estimates.
1/ In percent, year-on-year growth, 4 quarters ahead.

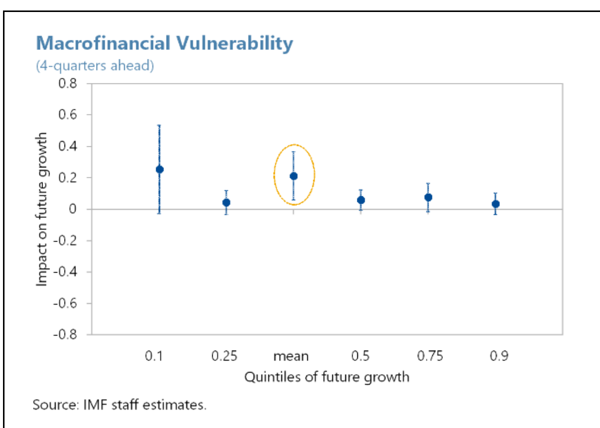
2. **Indonesia's near-term growth is most vulnerable to financial conditions**. Tighter financial conditions weaken growth 4-quarters ahead especially if initial growth is weak, but the impact is not statistically significant over a two-year horizon. Looser macro-financial conditions support activity, but only if initial growth is at average (4-quarters) or relatively strong (8-quarters ahead).

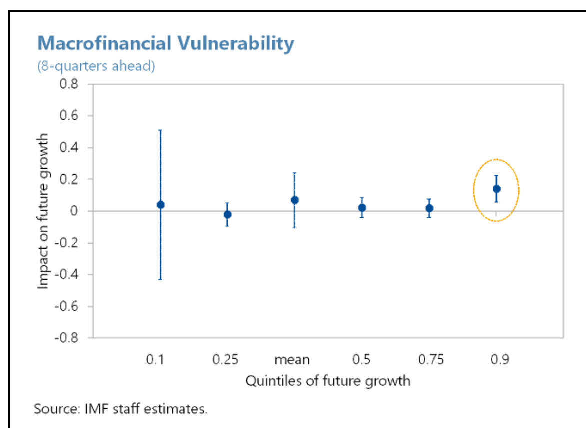
[1] Prepared by Akbar Dachlan, Putri Fadilah, Dessy Kusumawardani, Wantrijan Naibaho, Florischa Tresnatri, and Rifat Pasha (RRO).

[2] See Adrian and others (2018) and Prasad and others (2019) for a description of the GaR methodology. The GaR specification used here is similar to the one used for the 2024 FSAP.

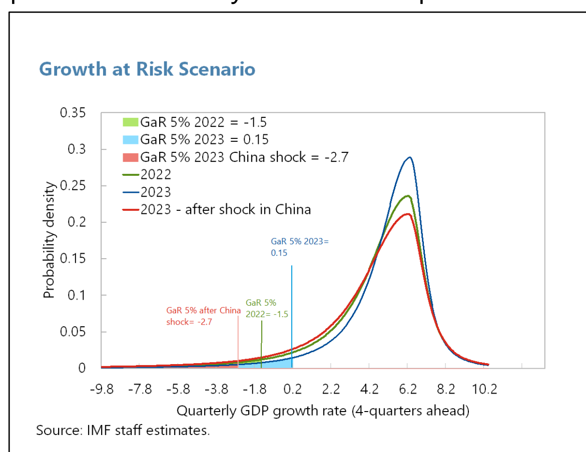








3. While downside risks to growth have declined, a severe slowdown event in China could jeopardize the outlook. In q4:2022, the post-pandemic recovery indicated a 5 percent chance of real GDP contracting by at least 1.5 percent in the following year. A year later, this risk declined as the improvement in macro-financial vulnerabilities and the improvement in financial conditions more than offset the weakening of external factors. However, simulations also reveal Indonesia's sensitivity to China's growth—with a 5 percent probability that growth falls to -2.7 percent over the next year in the event of a severe downturn (two-standard deviations growth shock) in China's economy.



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Annex V. Exposures to Geo-Economic Fragmentation (GEF) Risks[1]

Geoeconomic fragmentation (GEF) poses risks to Indonesia through several channels—including disruptions to commodity markets, reduced capital flows and trade, and weaker global demand and knowledge diffusion. Fragmentation in commodities markets—while potentially improving terms-of-trade in some scenarios—could lead to more price volatility and lower access to supplies and export markets. Indonesia faces similar profiles of vulnerabilities to FDI fragmentation as other major EM and regional peers. However, data so far point to ongoing FDI inflows from major sources. Domestic efforts on structural reforms that enhance Indonesia's attractiveness as a production base, along with the maintenance of policy buffers, will enhance resilience against GEF.

1. **GEF poses risks for Indonesia through several channels**. These include commodity market disruptions, and reduced capital flows and trade (Aiyar and others, 2023). Long-term reductions of global activity, and lower technological development and diffusion would also add headwinds to Indonesia's pursuit of faster potential growth.

2. **Fragmentation of key commodities markets could prove disruptive given Indonesia's economic structure (**IMF, 2023b**)**. As a major commodity exporter, geopolitical supply disruptions may improve Indonesia's terms of trade, but trigger adverse price movements if GEF reduce market access. As a commodity importer, risks are clear: given supply concentration, geopolitical shocks may lead to import price spikes. Prices would be more volatile, reflecting lower capacity in smaller fragmented markets to absorb shocks (e.g., a bad harvest). Finally, commodities fragmentation could pose challenges to Indonesia's pursuit of placing itself in strategic value chains, for instance, if it raises hurdles to accessing key minerals from geopolitically distant economies.

3. **Like its peers, Indonesia faces vulnerabilities to FDI fragmentation**. FDI plays an important role in connecting EMs to global value chains, and as a conduit for the transfer of productivity-enhancing technologies. GEF-induced FDI relocation would then pose challenges to growth. A recently developed IMF *country-level multi-dimensional index of vulnerability* is used to assess re-shoring risks to existing FDI stocks, finding risk levels for Indonesia comparable to other EM and regional peers, based on three dimensions (IMF, 2023a):

- ***Geopolitical***. This captures the idea that reshoring risk rises with the share of investments sourced from more geopolitically distant economies. Indonesia's measure of risk in this dimension is above the median for all countries, which is typical of EMs in Asia and the G20. The relatively elevated risk reflects looser geopolitical ties to the major FDI sources (AEs).

- ***Market Power***. This can help offset geopolitical risk, if a country's dominant position in many markets makes it difficult to find alternate places to relocate production. Indonesia's position in several industries (e.g., mining) offers some protection, as per its below-median score. However,

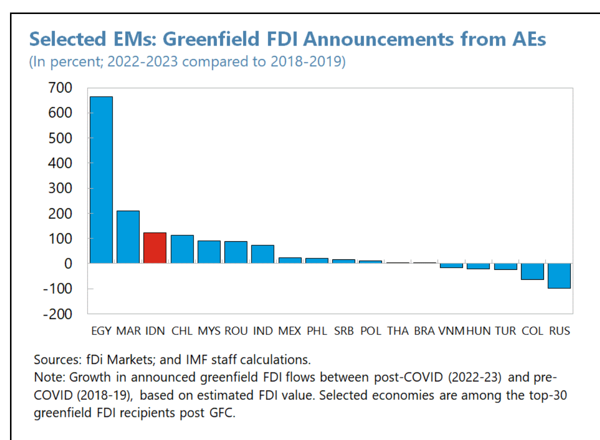
[1] Prepared by Ashique Habib (APD), with inputs from Emmanouil Kitsios (APD).

Indonesia is a relatively small player in most industries in which it hosts FDI, leaving it vulnerable if reshoring pressures were to arise.

- ***Strategic***. Indonesia—like most G20 economies—hosts a variety of investments in strategic sectors which may be targeted by reshoring policies of the source economy, increasing Indonesia's vulnerability.

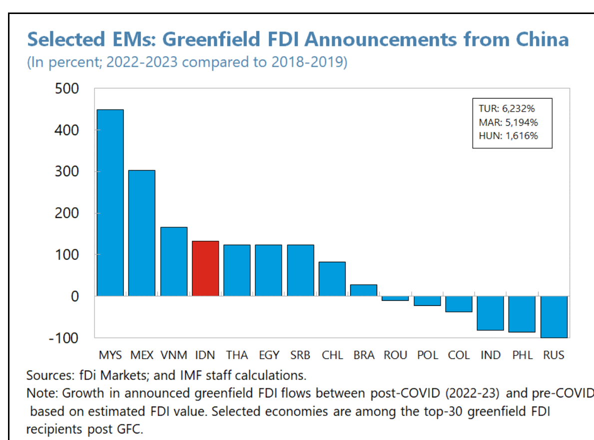
4. **While trade and investment reallocation has risen globally, recent investment flows do not point to shifts away from Indonesia**. Amid heightened tensions between China and some AEs, a comparison of recent announcements for inward greenfield FDI points to continuing flows from both source groups thus far. Further, reallocated trade and investment could create opportunities for both closely aligned economies, and for some non-aligned economies which could emerge as connector countries, serving as a conduit for trade between opposing blocs (Gopinath and others, 2024). Unlike some regional and EM peers (e.g., Vietnam, Mexico), signs of Indonesia playing such a connector role are not yet apparent.

Selected EMs: Greenfield FDI Announcements from AEs
(In percent; 2022-2023 compared to 2018-2019)



Sources: fDi Markets; and IMF staff calculations.
Note: Growth in announced greenfield FDI flows between post-COVID (2022-23) and pre-COVID (2018-19), based on estimated FDI value. Selected economies are among the top-30 greenfield FDI recipients post GFC.

Selected EMs: Greenfield FDI Announcements from China
(In percent; 2022-2023 compared to 2018-2019)



Sources: fDi Markets; and IMF staff calculations.
Note: Growth in announced greenfield FDI flows between post-COVID (2022-23) and pre-COVID based on estimated FDI value. Selected economies are among the top-30 greenfield FDI recipients post GFC.

5. **GEF may leave the economy worse off**. IMF analysis suggests that while non-aligned economies that remain open to all may suffer the least from fragmentation, the reduction in long-term external demand due to an overall smaller global economy may outweigh any gains from trade and investment diversion (IMF, 2023c). Further, non-alignment vis-à-vis blocs may lead to policy uncertainty regarding future alignment, thereby potentially deterring FDI.

6. **Multilateral and domestic efforts are needed to reduce GEF risks and build resilience**. Multilateral efforts are key to dampen geopolitical tensions and set guardrails against GEF disruptions. Domestically, horizontal structural reforms that make Indonesia a more attractive destination for investment and production—including through transparent, simple, and predictable frameworks—would not only build resilience against reshoring pressures but help attract investment flows. These could include, inter alia, upgrading the competition framework, bolstering logistics performance and infrastructure, fostering economic openness, and strengthening governance (see Section E). In a more shock-prone world, maintaining policy buffers will be critical for resilience.

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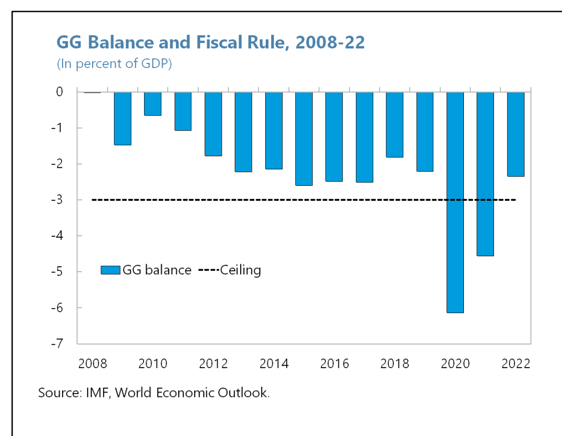
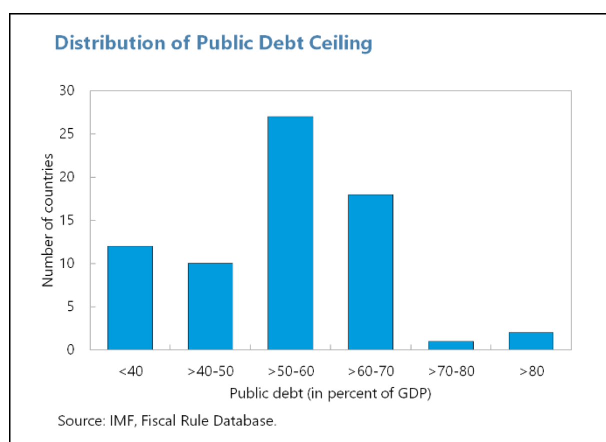
Annex VI. Fiscal Framework[1]

The current fiscal rule has served Indonesia well as a pillar of macroeconomic stability. While there may be some room for enhancements, it should not come at the expense of the framework's credibility, simplicity, and enforceability. Reforms to improve flexibility within the rule, coupled with stronger domestic revenue mobilization and public financial management would go a long way in supporting the needed pro-growth spending, while preserving fiscal prudence and sustainability.

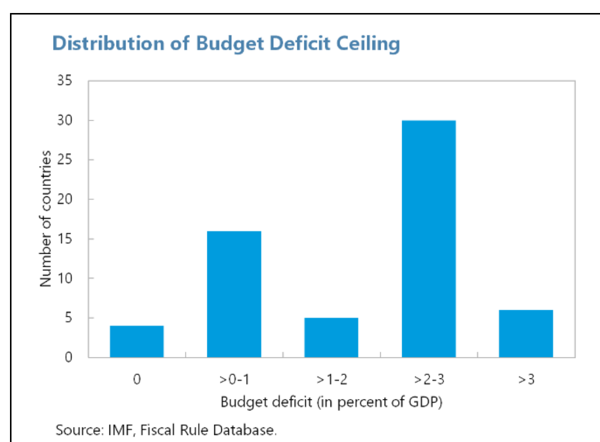
1. **Indonesia's current fiscal rule has served well as a pillar of macroeconomic stability**. Since 1967, Indonesia has had a fiscal rule in place, composed of a deficit ceiling of 3 percent of GDP, and since 2004 a debt ceiling of 60 percent of GDP, both covering the consolidated central and local government (charts). This approach to designing a fiscal rule is broadly aligned with international practice (Lledó and others, 2017; IMF 2018).[2] Deficits have been well-within the ceiling, except when these rules were temporary lifted via a presidential decree during the pandemic (chart).



Source: IMF, World Economic Outlook.



Source: IMF, Fiscal Rule Database.



Source: IMF, Fiscal Rule Database.

2. **Regularly evaluating the adequacy of fiscal rules is generally a good practice**. This is reasonable, especially after large shocks such as the pandemic; but should be guided by a clear cost-benefit analysis, to preserve fiscal credibility and discipline (IMF 2009). In addition, the rules should not be viewed as operational targets (these should be set up through annual and medium-term budgeting), rather they constitute guardrails beyond which macro-fiscal sustainability could be put at risk. Given this purpose, it is not optimal to task fiscal rules with the specific

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[1] Prepared by Amr Hosny (FAD).

[2] Recent surveys on fiscal rules suggest that about 70 countries worldwide had a fiscal framework with an explicit cap on public debt. About 80 percent of those countries also have additional operational rules on the expenditure or budget balance (IMF 2018; Eyraud and others 2018).

objective of enabling growth, which is best addressed through structural reforms and adequate fiscal policy design (e.g., see below on reforms on revenue and spending composition).

3. Fiscal rules should balance simplicity, enforceability and flexibility. These three principles are difficult to achieve simultaneously (Eyraud and others 2018). The current fiscal rule is an asset to Indonesia, and largely achieves these three main principles. It is simple, complied with, and has a demonstrated degree of needed flexibility.

- **Simplicity**. The rule is inspired by the simplicity embedded in the first generation of fiscal rules, which appeared before the global financial crisis (GFC), including the Maastricht criteria developed in Europe in the early 1990's. It is easy to understand and verifiable.

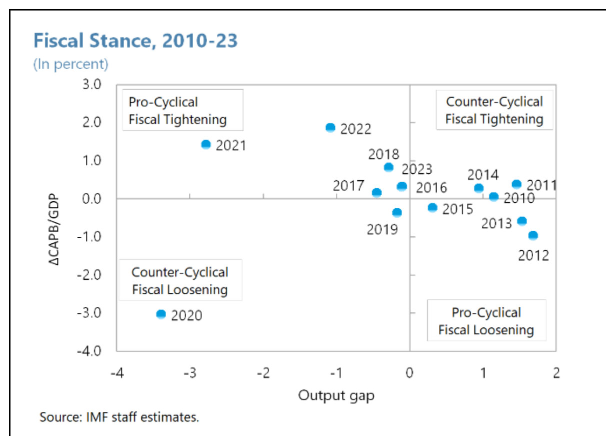
- **Enforceability**. The rule is enforceable by legislation, and a legacy of hard-won fiscal prudence and pragmatism. This is implemented through prudent medium-term fiscal frameworks and annual budgets, and in case of any envisaged higher deficits, then revised budgets are required with parliamentary approval and continued adherence to the deficit ceiling. Other country experiences, especially in the so-called second-generation fiscal rules post-GFC, include introducing independent fiscal councils to monitor compliance.

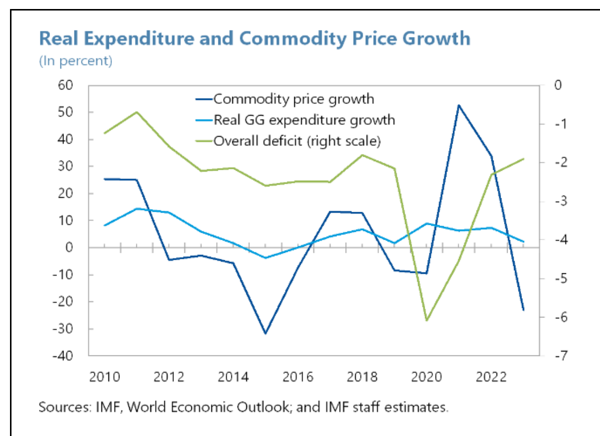
- **Flexibility**. Finally, the temporary suspension of the deficit rule during the pandemic in 2020-22, and the fact that the deficit ceiling was restored a year earlier than planned, show that Indonesia's current system has some built-in flexibility which has not presented a binding constraint in the past. Other countries attempted to increase flexibility by including rules adjusting for the business cycle, like structural balance rules meant to provide more policy room during cyclical downturns. However, experience suggests these are more difficult to operate and implement (Eyraud and others 2018), and may increase complexities (Schaechter and others 2012) that affect the rules' simplicity.

4. Escape clauses and embedded corrective mechanisms can provide additional flexibility within a fiscal rule in dealing with rare events. According to IMF (2009) and Schaechter and others (2012), a well-designed escape clause should include: (i) a limited range of factors (e.g., severe recession or exogenous shocks) that allow such escape clauses to be triggered in legislation, with clear definitions of such events and whether it can be invoked based on a forecast or must await an actual event; (ii) how long the fiscal rule should be suspended for when the escape clause is triggered; and (iii) specification on the path back to the rule and treatment of accumulated deviations.[3] In case of (near) breaches, some countries require corrective mechanisms, for example invoking automatic freezes on aggregate or certain spending items (IMF 2017). It is important to note, however, that while escape clauses may provide some flexibility, they may also jeopardize the rules framework's simplicity and enforceability features and unduly complicate fiscal policy design (Eyraud and others 2018).

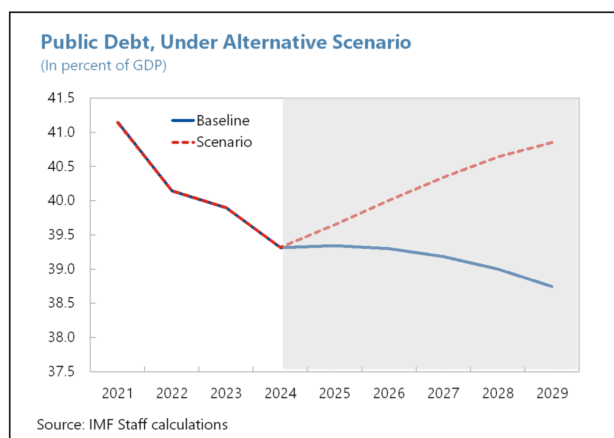
[3] For a more recent discussion in the context of the pandemic, see Gbohoui and Medas (2020).

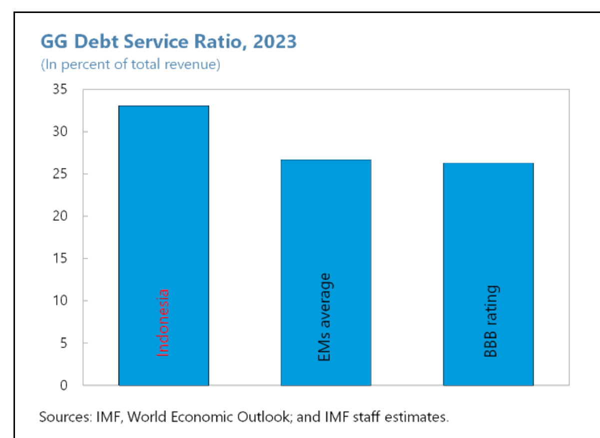
5. The evidence on the cyclicality of Indonesia's fiscal policy is mixed. Over the past decade, fiscal policy in Indonesia was, at different points in time, both pro-cyclical and counter-cyclical, with respect to the business cycle.[4] Fiscal policy tended to be pro-cyclical with respect to commodity prices—for instance, government expenditure exhibited strong correlations (0.5-0.7) with commodity prices over the past decade.





6. An illustrative scenario of sustained deficits would put debt on an upward trend. An illustrative exercise, assuming higher spending leading to sustained fiscal deficits of around 3 percent of GDP over the next 5 years would put public debt on an upward—albeit gradual—trend, reaching 41 percent of GDP by 2029, all else (macro and financing assumptions) equal. While this is below the formal 60 percent of GDP debt ceiling, it carries significant risks of potential breaches of the 3 percent deficit ceiling, along with risks to fiscal space, investor sentiment and thereby cost of new market financing. A worsening of financing terms could erode fiscal space further, given Indonesia's already high debt service-to-revenue ratio; this puts a premium on prioritizing domestic revenue mobilization to finance needed development spending while continuing to treat the deficit cap as a ceiling—rather than a target.

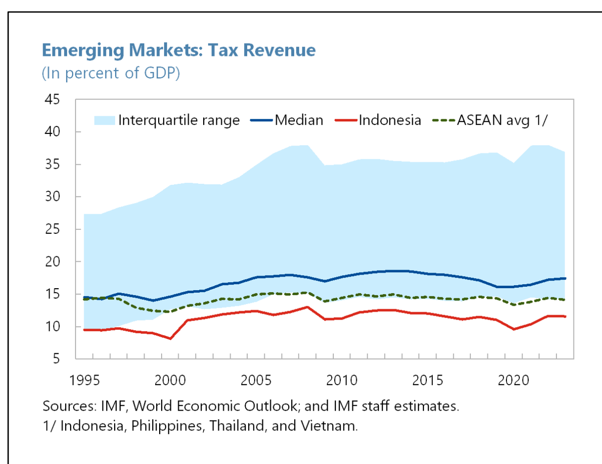




[4] Some studies argue that one should look at the cyclicality of public spending, because tax receipts are endogenous with respect to the business cycle, and expenditure better reflects discretionary fiscal policy (Bova and others 2014; Ilzethki and Vegh 2008; Frankel and others 2013; Kaminsky and others 2004; Dabla-Norris and others 2010). However, we have not seen evidence of procyclicality between real spending and the output gap for 2010-19.

7. Complementary reforms would further enhance fiscal space. Targeted revenue and public financial management (PFM) measures would help the country achieve its objectives without hampering macro-fiscal sustainability.

- **Domestic revenue mobilization** can enhance fiscal space, especially as Indonesia is at the low end of revenue collection compared to peers (chart). Adding 1-3 points to the tax-to-GDP ratio over time, through tax policy and administration measures in line with earlier capacity development work by the Fund (see Appendix V of the 2022 AIV and Appendix IV of the 2020 AIV), would provide room for expanding pro-growth spending while maintaining the current rule and avoiding risks.



- **PFM and spending reforms**. Enhanced macro-policy planning, including by strengthening the medium-term fiscal and budgetary frameworks (MTFF and MTBF, respectively) would help set sustainable targets within the guardrails of the fiscal rule and to serve as forward guidance to annual budgets. An MTFF underpinned by a well-calibrated MTO set up on a (multi-year) rolling basis could also help support more systematic counter-cyclical policymaking.[5] Spending policy reforms could provide for higher quality of spending (e.g., allocation and efficiency of spending as in the WB's 2017 PEFA and the Fund's 2019 PIMA), energy subsidy reform (as discussed in 2020 AIV SIP), and improved execution of decentralized spending by local governments.

- **Coverage**. Limitations in institutional coverage in the rule may open loopholes that circumvent and undermine the credibility of fiscal rules (IMF 2009). Successful fiscal rules generally have a broad institutional and economic coverage (Eyraud and others 2018), as this permits a transparent and comprehensive view of fiscal activities, also allowing to better gauge policy tradeoffs. Fiscal activities, such as off-budget operations by SOEs, while not part of the current institutional coverage of Indonesia's consolidated general government (and thus the coverage of fiscal rules), should be monitored to avoid build-up of fiscal risks in line with recent Fund TA. Ongoing capacity development by the Fund on improving the classification and reporting of Government Finance Statistics (GFS) along the GFS Manual 2014 would also be helpful.

[5] As illustration, the MTO could be defined in terms of an anchor—such as the overall or structural balance—set for the end of the medium term. This could then be complemented with expenditure ceilings defined over a rolling multi-year window: the expenditure ceilings would be such that implied structural balances are consistent with projected cyclical stance (output gaps) over the medium term.

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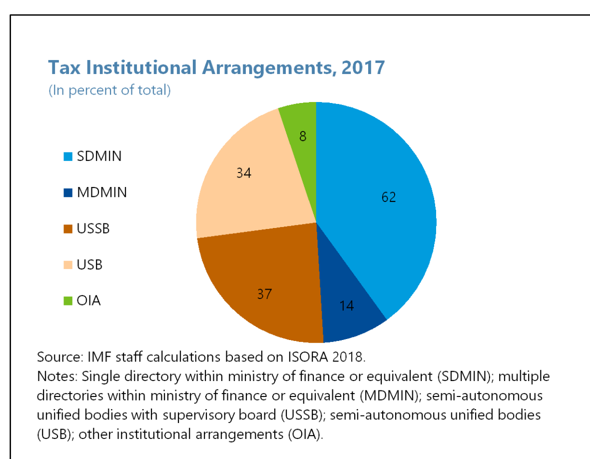
Annex VII. Determinants of Effective Tax Administrations: The International Experience[1]

The elected administration has pledged to raise the total revenue by 10 ppts from 13 percent of GDP, including by establishing a new National Revenue Agency (NRA) and enhancing revenue collection processes. A survey of the literature suggests that raising revenue collection would also require sustained revenue administration reforms and modernization. Key factors to effective revenue administrations include compliance risk management, use of third-party data, digitalization, appropriate staffing, and broader taxpayer bases.

1. **The elected administration has pledged to raise Indonesia's revenue-to-GDP ratio**. To this end, proposals focus on establishing a new National Revenue Agency (NRA) and enhancing revenue collection processes. The focus on domestic revenue mobilization is welcome. Revenue-to-GDP ratio in Indonesia is lower than peers, and raising it–as pledged–by 10 ppts from around 13 percent of GDP is an ambitious goal; achieving it—even partially—would provide significant resources to support Indonesia's priority spending needs while preserving prudent macro-fiscal settings.



Source: IMF staff calculations based on ISORA 2018.
Notes: Single directory within ministry of finance or equivalent (SDMIN); multiple directories within ministry of finance or equivalent (MDMIN); semi-autonomous unified bodies with supervisory board (USSB); semi-autonomous unified bodies (USB); other institutional arrangements (OIA).

2. **Indonesia's tax administration is currently housed as a General Directory within the Ministry of Finance**. The Directorate General of Taxes (DGT) of the MOF focuses mainly on tax collections, similar to peers. Administrations can be classified as follows:

Tax Arrangement by Responsibility

	Semi-autonomous	Within ministry	Other	All
Tax only	32	61	6	99
Tax and customs	39	15	2	56
All	71	76	8	155

Source: ISORA 2018.

- ***By Institutional Arrangement***. Per the International Survey on Revenue Administration (ISORA)[2], tax institutional arrangements are typically grouped into (1) directorate(s) within the Ministry of Finance or its equivalent, or (2) semi-autonomous

[1] Prepared by Amr Hosny (FAD).

[2] ISORA is a joint survey by the IMF, IOTA, OECD, ADB and CIAT. The survey gathers data on collections, institutional structure, budget and human resources, segmentation, taxpayer registration, filing and payment, services and education, collection and enforcement, inspection, audit and investigations, and dispute resolutions. ISORA database is available online here; it covers 155 countries representing around 90 percent of world GDP.

bodies[3] with or without a management board. Semi-autonomous bodies are generally established to provide increased autonomy in human resources and budgeting matters, and to afford some level of insulation from political interference.

- ***By Responsibility Area***. There are two basic types of tax administration in terms of main responsibility: (1) those in which tax and customs administrations are separate organizational entities and (2) those in which tax and customs administrations are co-managed in the same organization (Crandall 2010, OECD 2019, ADB 2020, Crandall et al 2021, ADB 2022).

- ***Indonesia's arrangement***. Indonesia's DGT is a single directory within the Ministry of Finance, covering only tax administration. This is similar to the majority of arrangements worldwide (40 percent) and in ASEAN (above 50 percent). The ADB (2020) provides similar evidence where the semi-autonomous structure is more common in Africa and South America than in Asia. In terms of organizational design, most countries have a hybrid form largely based on functional (e.g. audit, returns and payments, collection, taxpayer services) and taxpayer segment (e.g. large taxpayers office) design criteria (Kidd 2010, WB 2010).

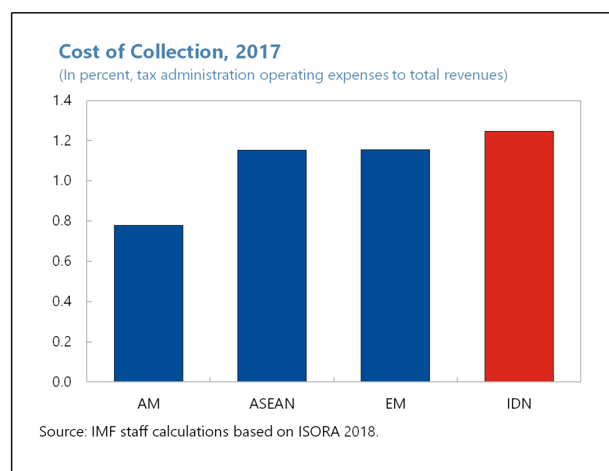
3. Independent revenue systems should not be viewed as a panacea and a diagnostic is advised to determine what features may be most beneficial to achieve the expected benefits. Kidd and Crandall (2006) and Crandall (2010) argue that establishing independent revenue authorities should not be viewed as a panacea and advise countries to consider strategies for reform based on international best practice. Before considering any institutional model, revenue administrations should clearly identify and articulate their key deficiencies and assess the extent to which each model might resolve these. Political commitment is, in any case, vital in sustaining an effective revenue administration. Moreover, an independent agency model alone need not lead to improved effectiveness and/or taxpayer compliance, and its establishment must be coupled with a serious commitment to and plan for reform. In a comparative study of international country experiences of integration of revenue administrations, WB (2010) notes the inability to provide systematic or quantifiable cost-benefit analysis of revenue system integration. This can be due to the difficulty in disentangling cost and/or benefits from integration versus other modernization efforts, as well as macroeconomic and structural factors.

4. Modernizing tax and customs administrations–even if integrated–is a long-term process. The rationale for merging tax and customs administrations is the expected administrative synergy and economies of scale of combining operational functions to improve revenue collection and services (Crandall 2010, WB 2010). That said, the WB (2010) also highlights the importance of understanding that institution building within an integrated revenue authority is a long-term goal and requires persistent effort even after the integration is largely accomplished. Kidd and Crandall

[3] Varying degrees of autonomy are possible; hence "semi-autonomy" reflects a range within the autonomy spectrum (Crandall et al 2021, Crandall 2010). Semi-autonomous bodies also include Revenue Authorities (RA). RAs refers to a governance model for revenue administration where traditional ministry of finance departments (tax and customs administrations) are established as a separate organization with a degree of autonomy from government (Kidd and Crandall 2006, Crandall 2010).

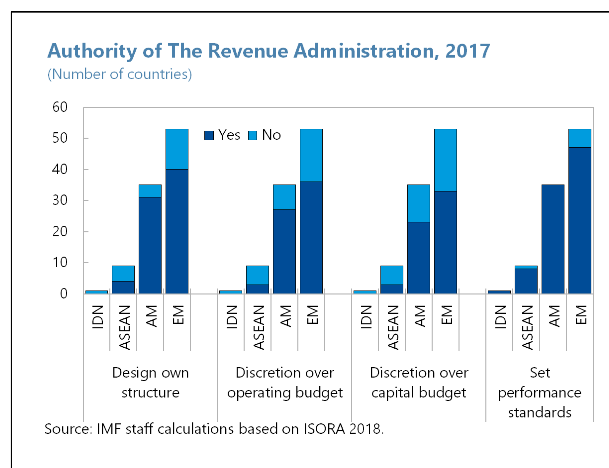
(2006) further argue that modernization of revenue administrations is ultimately the result of improvements in organizational structures, systems, and processes. A move to implement a new governance model for the revenue administration can thus only be, at best, a first step. Along similar lines, Adan et al (2023) report empirical evidence that while tax administration reforms may lead to some initial gains, it could take time for the full results to be realized.

5. **Indonesia could strengthen its revenue administration efficiency further**. The assessment may be based on the "cost of collection" as a proxy measure of a tax administration's efficiency, following OECD (2019). This indicator is computed as the annual operating expenditures of a tax administration as a share of total net revenues collected. The ratio compares inputs (administrative costs) to outputs (revenues), although there are caveats (i.e., other factors that can influence the ratio such as tax policy or macroeconomic changes, differences in tax structures, and/or in range of functions and revenues administered). In Indonesia, this ratio was about 1.2 percent in 2017, somewhat higher than the ASEAN and EM averages, and higher than for advanced markets (AMs).



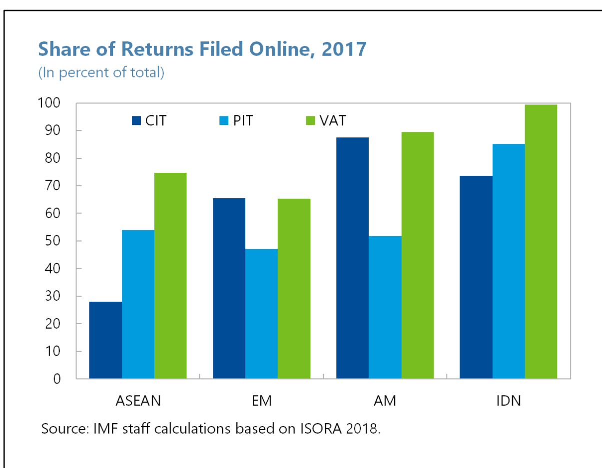
6. **The practices and characteristics of tax administration agencies matter significantly for tax performance; key factors include rigorous compliance risk management, use of third-party data, digitalization, autonomy, and appropriate staffing**. The operational strength of the agency generally comprises compliance risk management (CRM) practices, the use of third-party data (TPD), degree of digitalization of services, service orientation, public accountability, and autonomy. Chang et al (2020) and Adan et al (2023) find empirical evidence that such factors are tightly associated with tax collections. Regardless of the institutional arrangement in place, the literature has identified several factors that are ultimately key to an effective revenue administration. Lessons include:

- **Good practice stipulates that revenue administrations have adequate autonomy over their decisions**. Revenue bodies should have adequate autonomy, particularly in designing their organization, devising plans and objectives, managing budgets, and dealing with important human resource management matters (ADB 2020). Stronger autonomy can reduce management impediments while



maintaining accountability and transparency (Crandall 2010). The ISORA 2018 survey indicates that Indonesia's DGT does not independently design its own structure, operating budget, and capital budget. The DGT, however, does have autonomy to set its performance standards (for example on processing tax returns and refunds, collection, audits, and resolving disputes). The DGT also prepares and publishes an annual report, as in most countries. While this set-up is slightly more common in ASEAN countries, most other countries (including by all income levels) report having relatively more authority on such decisions. This is noticeably the case for countries with semi-autonomous structures (ADB 2020).

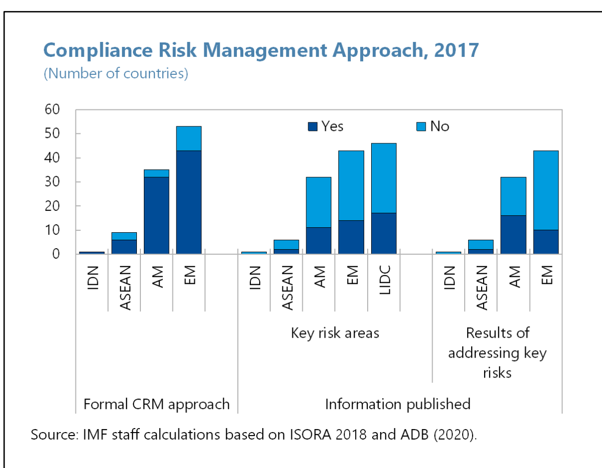
- **Digitalization of tax administration services is especially relevant**. For instance, Nose and Mengistu (2023) find a strong empirical association between digital tax administration operations and improved revenue collection outcomes. They also find that realization of revenue gains is heavily contingent on accompanying policies, legislative and administrative reforms, and the availability of adequate digital connectivity and capable tax administration staff. In Indonesia, according to the ISORA 2018 survey, the share of tax returns filed online (a proxy for digitalization) is quite high, performing notably better than peers. The ADB (2020) reports similar evidence with a focus on Asian countries.



Share of Returns Filed Online, 2017
(In percent of total)

Source: IMF staff calculations based on ISORA 2018.

- **Amongst sound practices of tax administration, CRM and the use of TPD are particularly important**. To enhance tax collection, tax administration reform efforts should prioritize: (i) strengthening CRM including by adopting automated risk profiling and electronic audits; and (ii) utilizing TPD by adopting computer systems for processing the data and prefilling returns (Chang et al 2020). Indonesia, as several peers, has a formal CRM approach, covering return filing, payment processing, collection enforcement, verification/audit and taxpayer services. The DGT does not publish key risk areas or results of addressing them publicly, as in several peers. The ADB (2020) reports similar evidence with a focus on Asian countries.

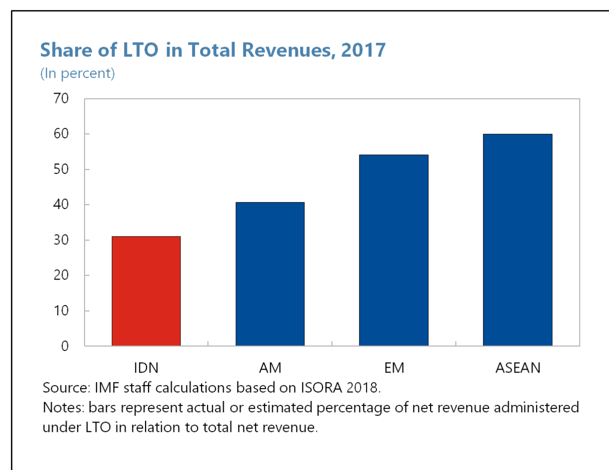


Compliance Risk Management Approach, 2017
(Number of countries)

Source: IMF staff calculations based on ISORA 2018 and ADB (2020).

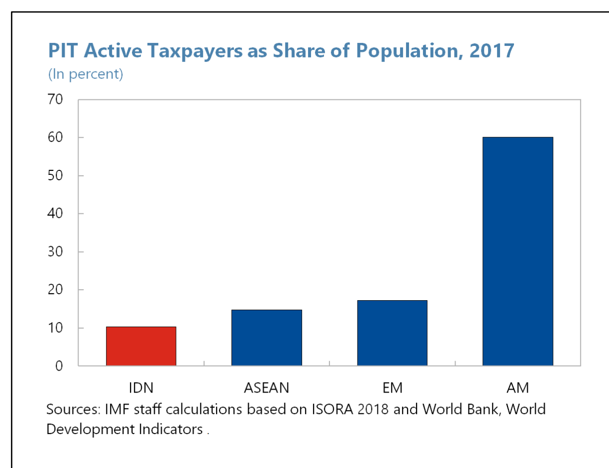
- **Adequately staffing tax administration agencies is important**. For instance, Chang et al (2020) find empirical evidence that increased staffing of a tax agency is associated with improved revenue performance up to a threshold of 0.25 percent of the labor force.

- **The above factors are highly correlated (Chang et al 2020 and Adan et al 2023)**. This aligns with advice to countries that tax administrative reform benefits derive from the strategic integration of multiple components, rather the implementation of individual measures. For example, it is the *effective operation* of an office or program for large taxpayers that matters, rather than the *establishment* of such an office or program (Chang et al 2020). Data from ISORA suggests that most countries (around 85 percent) have a Large Taxpayer Office (LTO), defined based on variables such as annual sales, income, assets, taxes paid and/or type of economic activity. LTOs typically contribute a large share to overall tax revenues. In Indonesia, this share is estimated at around 30 percent, lower than peers.



Source: IMF staff calculations based on ISORA 2018.
Notes: bars represent actual or estimated percentage of net revenue administered under LTO in relation to total net revenue.

7. **Broadening the taxpayer base is also important in economies with relatively high labor and output informality**. The number of active taxpayers (in relation to the labor force or total population) also matters for tax collection, especially in economies with relatively high labor and output informality such as Indonesia's.[4] For example, the share of registered and active taxpayers of personal income taxes (PIT) to total population in Indonesia is around 10 percent. This is relatively lower than the shares in ASEAN and EMs of around 15 and 17 percent, respectively.



Sources: IMF staff calculations based on ISORA 2018 and World Bank, World Development Indicators .

[4] See Hapsari et al (2023) on informality in Indonesia.

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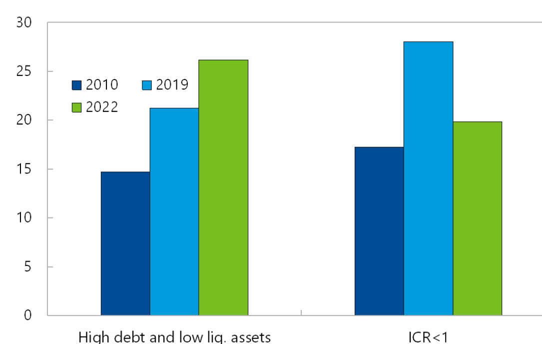
Annex VIII. Non-Financial Corporate Sector Vulnerabilities[1]

Indonesia's nonfinancial corporates (NFCs) have remained relatively resilient during the post-pandemic period, with improving financial risk indicators and profitability metrics. However, pockets of vulnerability remain in some sectors, while being more predominant in smaller publicly-listed firms. In addition, the number of firms with high leverage and limited cash buffers has been increasing, suggesting that firms may have less flexibility to smooth shocks going forward. The persistence of unproductive and unviable (zombie) firms, if unaddressed, may lower overall productivity, investment, and employment in the economy.

1. **The NFC sector in Indonesia has weathered the post-pandemic period relatively well, with financial risk indicators generally improving**. Analysis from a large sample of listed firms in Indonesia shows that NFCs, on average, have managed to decrease leverage and increase interest coverage ratios (ICR) since the pandemic, while also improving profitability indicators (see the 2024 Indonesia FSAP for details).[2] Debt owed by firms with an ICR below one—an indicator of financial distress that measures the ability of a company to service its debt with internal cash flows—has also improved (Figure 1).[3] These trends support the resilience of the corporate sector going forward.

2. **The improvement in firms' balance sheets has, however, been heterogenous across sectors and firm sizes**. Sectors hardest hit by the pandemic, particularly firms operating in consumer discretionary, industrials, information technology, and materials, show a considerable number of firms with ICRs below one (2024 Indonesia FSAP). Debt owed by firms with low coverage ratios seems concentrated in smaller firms, who are typically more financially vulnerable and credit constrained. While several corporates should be able to withstand the materialization of adverse economic and financial shocks, the profitability of smaller firms could decline significantly under stress conditions (2024 FSAP).

Figure 1. Indonesia: Share of Debt Owed by Firms with High Leverage and Low Net Liquid Assets 1/
(In percent)



Source: IMF staff estimates.

1/ Firms with high leverage and low net liquid assets belong to the top quartile of debt-to-assets distribution and to the first quartile of the net liquid asset ratio.

3. **Some prevailing NFC vulnerabilities require, however, close monitoring**. Despite improvements in ICRs since the pandemic, the debt share of firms with high leverage and low liquid assets has trended upwards, standing at 26 percent in 2022, up from 21 percent before the

[1] Prepared by Bruno Albuquerque (SPR).

[2] The analysis in this annex relies on a sample of 640 listed firms from S&P Compustat Global over 2000-2022.

[3] The ICR is computed as the ratio of EBIT to interest expenses.

pandemic (Figure 1).[4] The increase in the number of vulnerable firms has been noticeable among firms in the non-tradable sector and that produce durable goods, including communication services, consumer discretionary, and information technology. Recent studies have found that highly leveraged firms with limited liquid assets typically invest less, are less profitable, face higher financing costs, and are at a higher risk of entering financial distress (Fahlenbrach et al. 2021, Albuquerque 2024). In an adverse scenario, these high-debt firms with limited cash buffers could potentially face more difficulties in accessing external funding to finance their investment spending.

4. The persistence of unproductive and unviable (zombie) firms may delay a necessary creative destruction and negatively affect the prospects for long-term productivity growth. The share of zombie firms rose since the GFC, from a trough of 6.2 percent of all listed firms in 2013 to 10.8 percent in 2022 (Figure 2).[5] This compares with 9.5 percent in 2019, just before the pandemic hit. The share in 2022 is similar when considering the debt owed by zombie firms, although the latter has declined recently. The persistence and increase of zombie firms during the pandemic may reflect, to some extent, the unprecedented policy support and easy financing conditions during the pandemic. Although policy support, including forbearance measures, seemed to have been critical in mitigating the pandemic shock, they may have helped unviable firms stay afloat, delaying a necessary restructuring of firms that were already unviable and unprofitable before the pandemic. While zombification of the Indonesian corporate sector remains at moderate levels, it stands at higher levels relative to several regional peers. In addition, evidence suggests that the presence of zombie firms creates congestion effects on healthy firms competing with zombie firms, leading to lower overall productivity, investment, and employment in the economy (Caballero et al., 2008, McGowan et al., 2018, Acharya et al., 2019, Banerjee and Hofmann, 2022, Albuquerque and Iyer, 2023, Albuquerque and Mao 2023). Moreover, there is heterogeneity across sectors; zombification is assessed to be more prevalent in durable goods industries, such as materials, industrials, and consumer discretionary (Figure 2). Within these sectors, debt owed by zombie firms in construction is particularly high at 33 percent of all the debt in the sector at the end of 2022. These sectors are typically more subject to large swings in demand and were also hardest hit by the pandemic.

5. International evidence shows that the negative spillovers from zombification can be mitigated by limiting lenders' incentives to engage in zombie lending practices and by improving insolvency frameworks. The experience in Japan in the early-90s showed that low-capitalized banks faced incentives to continue lending to zombie firms to prevent them from defaulting, as this would lead these banks to breach regulatory capital requirements (Caballero et al. 2008). More recent evidence on the relationship between low-capitalized banks and zombie lending dates back to the post-GFC period in some European countries (Acharya et al. 2019). The overall finding is that strengthening the banking sector and tightening supervision seemed to have helped

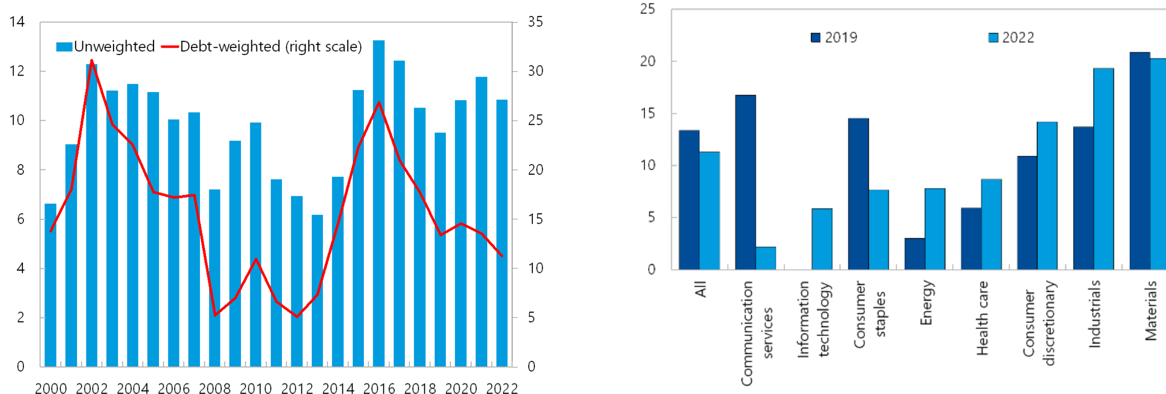
[4] Firms with high leverage and low liquid assets in each year fall in the top quartile of the debt-to-asset distribution *and* in the bottom quartile of the net liquid asset ratio. The latter is computed as current assets net of current liabilities over total assets; it measures how much liquidity firms can immediately use to mitigate shocks.

[5] The definition of zombie firms follows Albuquerque and Iyer (2023), who resort to three balance sheet indicators that aim at capturing firms that are most likely in financial distress and are persistently unprofitable: (i) ICR below one, (ii) leverage ratio above the median firm in the same industry, and (iii) negative real sales growth. These indicators need to persist for at least two consecutive years to minimize misclassification from cyclical fluctuations.

tackled zombification in these areas. On this front, the 2024 Indonesia FSAP stresses that banks are highly capitalized and resilient, which should limit the negative spillovers from zombification in Indonesia. International evidence, however, also shows that strong banks may, however, not be enough to mitigating zombie lending if insolvency frameworks are not well-prepared to deal with the restructuring or insolvency of firms (Andrews and Petroulakis 2019, Becker and Ivashina 2022, Albuquerque et al. 2023). This strand of research underlines that resolving financially distressed firms quickly and at a low-cost can mitigate zombie lending incentives. Using a recent indicator developed by Araujo et al. (2022)—measuring countries' preparedness to handle a large-scale restructuring of corporates—we find that Indonesia ranks considerably lower in crisis preparedness relative to regional peers.[6] By limiting zombie lending incentives, improving insolvency frameworks may therefore yield considerable benefits for economic growth and productivity in Indonesia.

Figure 2. Indonesia: Share of Zombie Firms 1/

(In percent)



Source: IMF staff estimates.

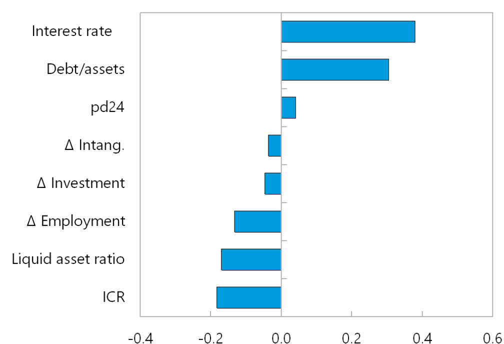
1/ Zombie firms are defined as firms that have for at least two consecutive years an ICR below one, the leverage ratio above the median firm in the respective industry, and negative real sales growth. The figure on the right shows the debt share of zombie firms in each sector.

[6] The crisis preparedness indicator summarizes the legal and institutional status of each country on insolvency frameworks. It includes five dimensions of the insolvency and restructuring regime in the corporate sector: out-of-court restructuring, hybrid restructuring, reorganization, liquidation, and the institutional framework.

6. The overall financial performance of Indonesia's listed NFCs is relatively weaker than in ASEAN peers. Regression analysis that controls for time-varying sectoral shocks indicates that listed Indonesian NFCs tend, on average, to underperform their ASEAN peers on several balance sheet metrics.[7] Firms in Indonesia invest less, both in tangible and intangible assets, have weaker employment growth, and exhibit more signs of financial distress, as indicated by a lower ICR, higher probability of default (in 24 months), higher leverage, and also a higher cost of debt (Figure 3). On the latter, the estimates indicate that the average firm in Indonesia has a cost of debt of around 0.4 standard deviations above the ASEAN firm. While there may be several firm-specific reasons behind the relative financial performance of Indonesian firms, these results underscore the need to continue implementing structural reforms that promote an enabling business environment and create the conditions for healthy firms in Indonesia to prosper.

Figure 3. Indonesia: Characteristic of Indonesia's Non-Financial Firms Relative to ASEAN Firms 1/

(In percentage point difference expressed in standard deviation)



Source: IMF staff estimates.

1/ Each column refers to a regression where the dependent variable is regressed on a dummy variable capturing firms in Indonesia and controlling for sector-time fixed effects.

[7] The regression equation is estimated on quarterly data from 2000Q1 to 2022Q4 on a sample of six ASEAN countries (including Indonesia), representing 3,319 firms. Each dependent variable is regressed on a dummy variable capturing firms in Indonesia, and controlling for sector-time fixed effects. Each variable is standardized to allow all coefficients to be on the same scale.

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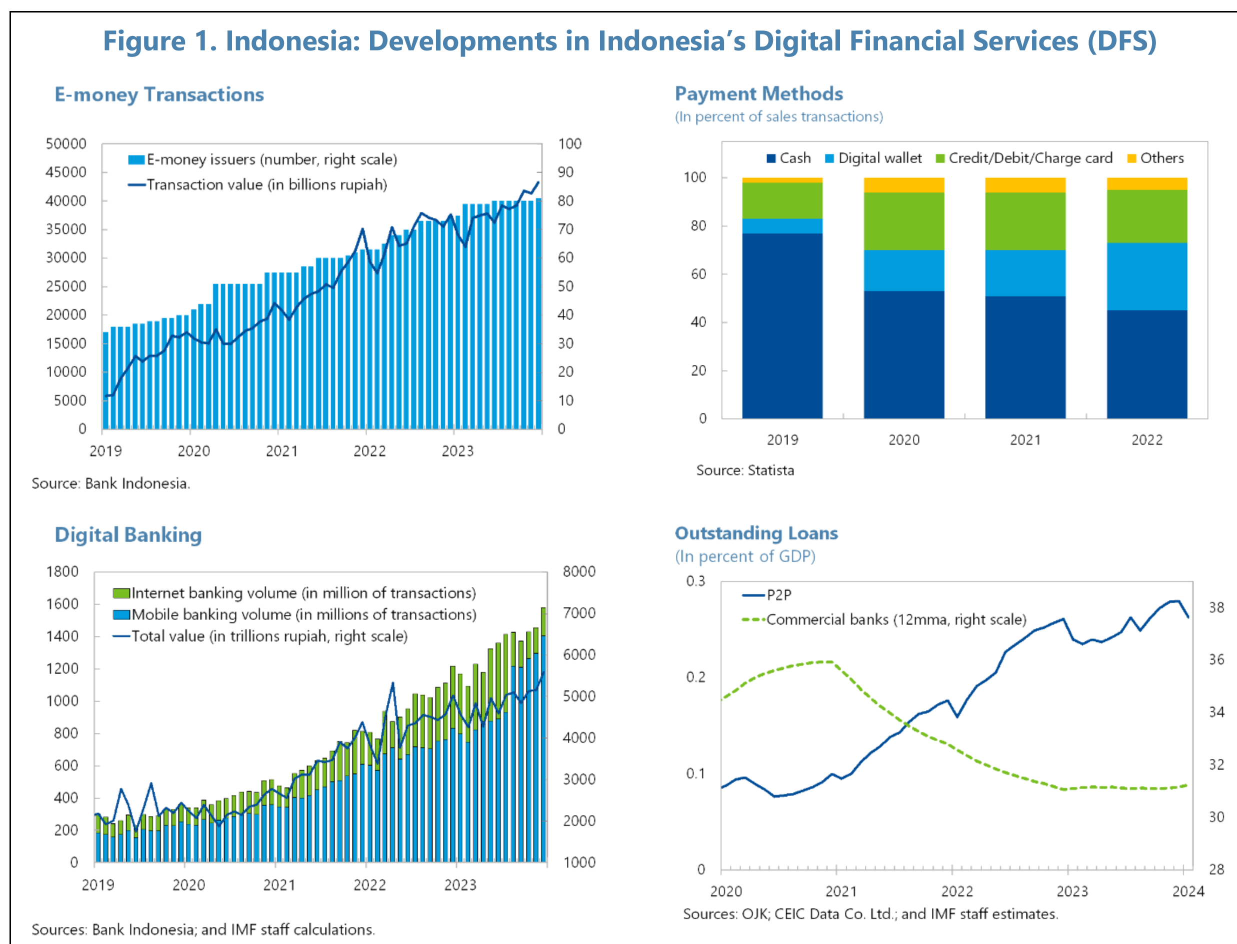
Annex IX. Financial Digitalization[1]

Digital financial services (DFS) have grown rapidly in Indonesia, supported by authorities' initiatives to enhance financial inclusion. A comparative analysis with peers suggests that there is still room for improvement. Analysis on the inter-regional difference and catch-up in Person-to-Person (P2P) lending activities indicates that reducing the digitalization and financial literacy gap is crucial to enhance DFS and financial inclusion. Efforts to strengthen regulation and supervision framework to address potential risks and enhance resilience in the DFS sector should continue, while also fostering innovation.

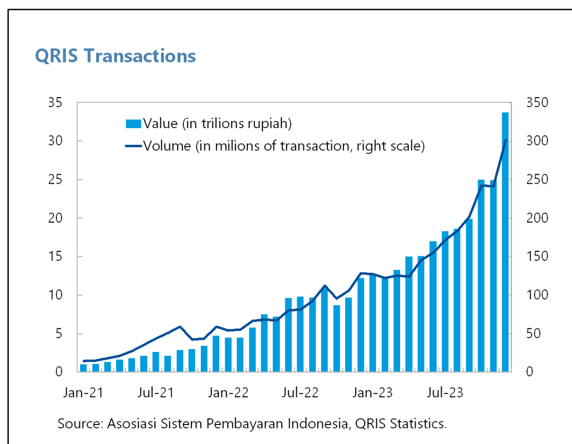
1. Indonesia has made significant strides in the digitalization of its financial sector (Figure 1). The value of e-money transactions increased over 30 percent per year since 2019, reducing the dominance of cash-based payments in the economy. The value and volume of digital banking transactions have also grown fast, especially for mobile banking. Fintech P2P lending and digital investment (e.g., robo-advisor) have expanded rapidly, though the scale is still relatively small.

Figure 1. Indonesia: Developments in Indonesia's Digital Financial Services (DFS)



[1] Prepared by Choonsung Lim (APD).

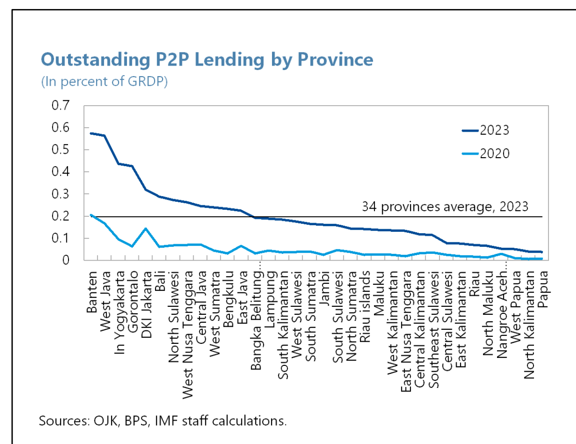
2. **This swift transformation has been enabled by authorities' initiatives**. Bank Indonesia (BI) established the *Indonesia Payment System Blueprint (BSPI) 2025* to support a rapidly growing economic and financial digitalization. This includes the introduction of standardized QR codes (QRIS) to enhance interoperability in 2019. Since inception, QRIS transactions volume and value have exponentially increased. Additionally, as part of BSPI 2025, BI initiated operation of BI-FAST, a modernized real-time payment system, in December 2021. BI-FAST offers faster, safer, scaled 24/7 fund transfer services, compared to existing infrastructure such as Real Time Gross Settlement (RTGS) and National Clearing System (SKNBI). SNAP, the payment API standard, also helps adopting innovative financial services. OJK, the financial supervisor, is rolling out initiatives such as the *Digital Financial Innovation Road Map and Action Plan 2020-2024* and *2020-2025 Indonesian Banking Development Roadmap*, to develop a comprehensive digital financial ecosystem.



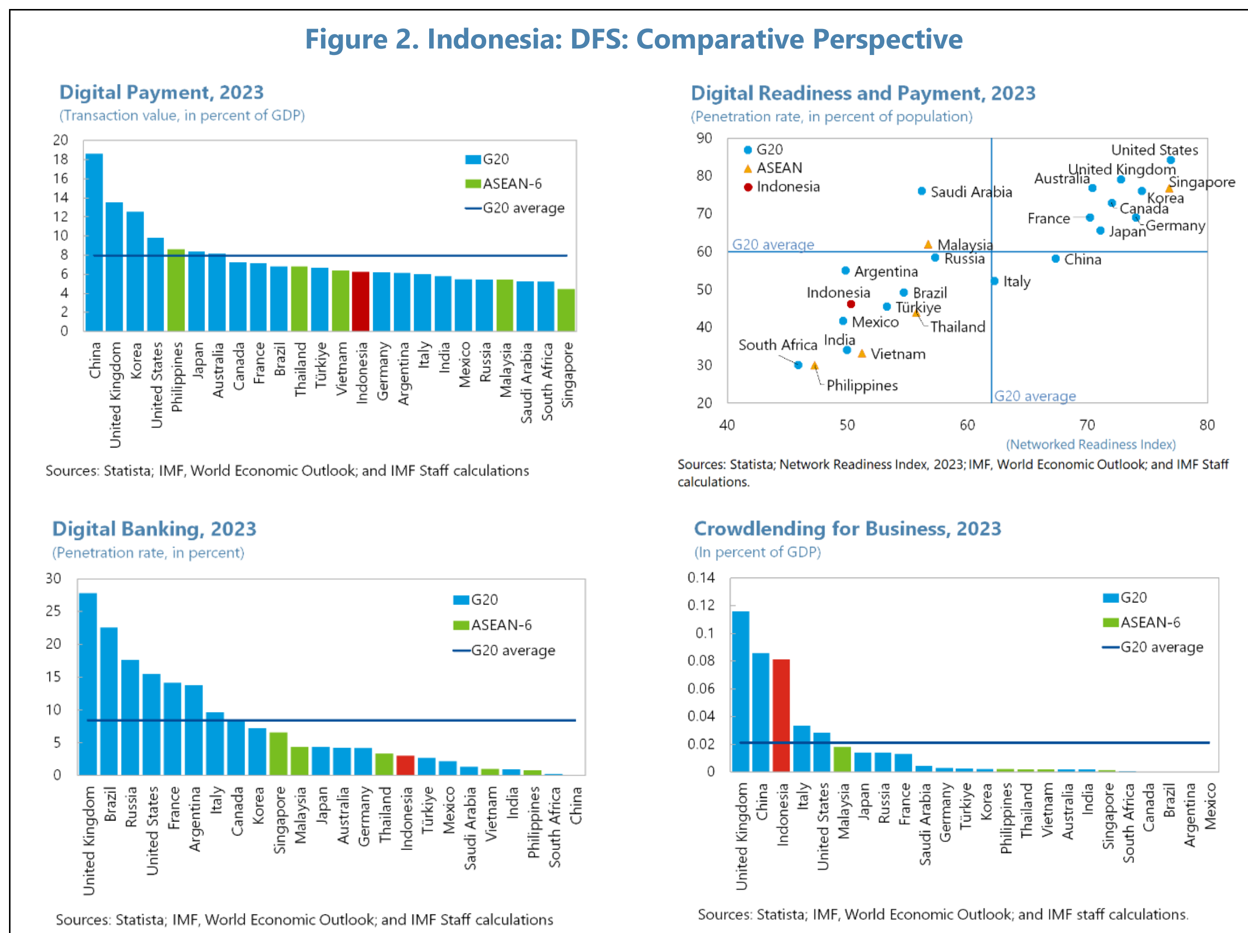
Source: Asosiasi Sistem Pembayaran Indonesia, QRIS Statistics.

3. **However, Indonesia's DFS has scope to deepen further** (Figure 2). Indonesia's digital payment transactions value, compared to its economy size, is below the G20 average and lags those of Philippines, Thailand, and Vietnam among ASEAN-6 countries. The penetration rate seems lower than in G20 peers, reflecting relatively low digital readiness. Likewise, mobile banking penetration significantly lags behind G20 and ASEAN-6 countries. While Indonesia appears to lead digital lending for business, its size is still small, relative to its economy size.

4. **Indonesia's regional disparities pose barriers to advancing DFS**. The inter-regional difference in outstanding values of P2P lending in percent of Gross Regional Domestic Product (GRDP) has widened significantly: the outstanding value of P2P in the bottom five provinces rose on average by 0.04 percentage points of GRDP in the last three years, while the top five provinces increased by 0.32 percentage points. Addressing structural barriers for DFS expansion in provinces with low activities is warranted.



Sources: OJK, BPS, IMF staff calculations.



5. To assess the determinants of DFS (and P2P[2] in particular) across Indonesian provinces, we employ a cross-provincial empirical analysis. The empirical equation is:

$$\boldsymbol{P2P_{i,2023} - P2P_{i,2020} = a + b_1 FinancialLiteracy_{i,2019} + b_2 FinancialInclusion_{i,2019} + b_3 Digitalization_{i,2020} + b_4 GRDPpercapita_{i,2019} + \epsilon_i}$$

where *P2P* is the outstanding value of P2P lending in percent of GRDP for the year of 2023 or 2020, *Financial Literacy* and *Financial Inclusion* are given by the corresponding index surveyed by OJK in 2019, *Digitalization* represents the degree of digitalization in 2020, and *GRDP per capita* controls for income level; *i* is the indicator representing each of the 34 provinces. All values are in logarithms, except for the P2P-to-GRDP ratio.

6. Digitalization data is from the East Ventures' Digitalization Competitiveness Index (DCI) but needs to be adjusted for financial literacy and inclusion. DCI measures the relative distance between provinces in terms of the readiness for digitalization. Specifically, it is an index

[2] Fintech credit can help fill credit gap (IMF WP/20/150).

consisting of three sub-indexes reflecting three aspects: input, output, and support.[3] Financial inclusion is embedded in the support aspect, while financial literacy is likely to be highly correlated with the output aspect. That is, financial literacy and inclusion are both components of DCI as well as individual explanatory variables in the main regression, warranting adjustment: the adjusted digitalization indicator for the main regression is the residual of an auxiliary equation, which is orthogonal to both financial literacy and inclusion,

$$\boldsymbol{DCI_{i,2020} = c + d_1 FinancialLiteracy_{i,2019} + d_2 FinancialInclusion_{i,2019} + u_i}$$

while Financial Literacy and Financial Inclusion can now be used unadjusted in the main equation.

7. The result suggests financial literacy and digitalization have played a significant role in DFS growth. As expected, the degree of digitalization has a positive impact on the growth of P2P lending. The estimation suggests that one-standard-deviation increase in digitalization is associated with the 0.06-percentage point increase in the P2P-to-GRDP ratio. Financial literacy also supports adaptation of new financial services. Financial inclusion's impact turns out to be insignificant to the P2P lending expansion, suggesting that the P2P lending growth did not matter for the larger demand. The negative coefficient of regional income per capita suggests less demand for alternative lending in high-income regions.

Determinants of P2P Lending

Dependent variable:	P2P Lending Growth (2020-2023)
Financial Literacy	0.18*
	(0.10)
Financial Inclusion	0.08
	(0.09)
Digitalization	0.31***
	(0.06)
GRDP per capita	-0.10***
	(0.02)
Observations	34
R-squared	0.539

White standard errors in parentheses.
Constant not reported.
*** p<0.01, ** p<0.05, * p<0.1

8. The result calls for examining the possible existence of *club convergence* dynamics across provinces, as well as the determinants of *club* membership. This would imply that different types of provinces have a different level of convergence point. Classical beta-convergence testing[4] for all provinces indicates that inter-regional gaps in P2P lending activities generally widen over time, with a statistically significant, positive

Beta-Convergence Test

Dependent variable : P2P growth (2020-23, percentage points)	(1) Unconditional convergence	(2) Conditional convergence
Initial P2P level (2020)	1.784***	1.569***
	(0.213)	(0.313)
Observations	34	34

White standard errors in parentheses.
Constant and control variables are not reported.
*** p<0.001

[3] The sub-index for input reflects human resources and expenditure for ICT, and ICT utilization, while the one for output measures of digital economy activities, including DFS. The support sub-index is based on the information on infrastructure, financial inclusion, local government regulation and capacity.

[4] A model for the test is based on the literature (e.g., Sala-i-Martin, 1996) such that $P2P_{i,2023} - P2P_{i,2020} = \alpha + \beta P2P_{i,2020} + \gamma X_i + e_i$, where $P2P$ and X are the P2P-to-GRDP ratio and the determinants included in the regression for P2P lending growth. A (statistically significant) negative coefficient on the initial level ($\beta<0$) suggests a (conditional) convergence. Unconditional convergence test can be done by dropping the control variables (X).

coefficient on the initial level of P2P lending. Given the inter-regional disparity of digital and human capital and their pivotal role evidenced earlier, this finding is not unexpected. However, it remains conceivable that regions with similar levels of capital could converge in P2P lending activities. Understanding whether this is the case—and if so, which determinants determine clustered convergence—can offer policy implications on how to help regions in "low" clubs advance to a club with a higher-level P2P lending, resulting in enhanced financial access and strengthened financial inclusion.

9. To test for club convergence, we follow Philip and Sul (2007, 2009, hereafter PS) and Schnurbus et al. (2017, see Technical Annex). The PS approach identifies four convergence clubs. Group A constitutes 14 provinces, including most Java Island provinces. Club B, C and D include 10, 3 and 7 provinces respectively. The upper panel of Figure 3 shows the group average of P2P lending in percent of GRDP. As of December 2023, group A stands at the highest level of 0.35 percent with a significant distance to the second group B at 0.18 percent, followed by group C and D at merely 0.11 percent and 0.07 percent respectively. Each group appears to converge to a group-specific level, while the convergence rate is larger in group B and D than group A and C (Figure 3 lower panel).

Convergence Club Memberships: P2P Lending

Group A (14 provinces)		Group B (10)	Group C (3)	Group D (7)
Bali	**West Java**	**East Java**	Central Kalimantan	Central Sulawesi
Bangka Belitung Islands	West Nusa Tenggara	East Nusa Tenggara	North Maluku	East Kalimantan
Banten	West Sulawesi	Lampung	Southeast Sulawesi	Nangroe Aceh Darussalam
Bengkulu	West Sumatra	Maluku		North Kalimantan
Central Java		North Sumatra		Papua
DKI Jakarta		Riau islands		Riau
Gorontalo		South Kalimantan		West Papua
In Yogyakarta		South Sulawesi		
Jambi		South Sumatra		
North Sulawesi		West Kalimantan		

Note: In bold for Java island provinces.

10. A logit/probit analysis for the determinants of the club membership confirms the findings in the cross-provincial empirical analysis for the determinants of P2P lending growth. Provinces with higher financial literacy turn out more likely to be in a group with a higher convergence point. The degree of digitalization in a province is also positively associated with the chance to belong in group A. However, financial inclusion remains statistically insignificant. Again, the

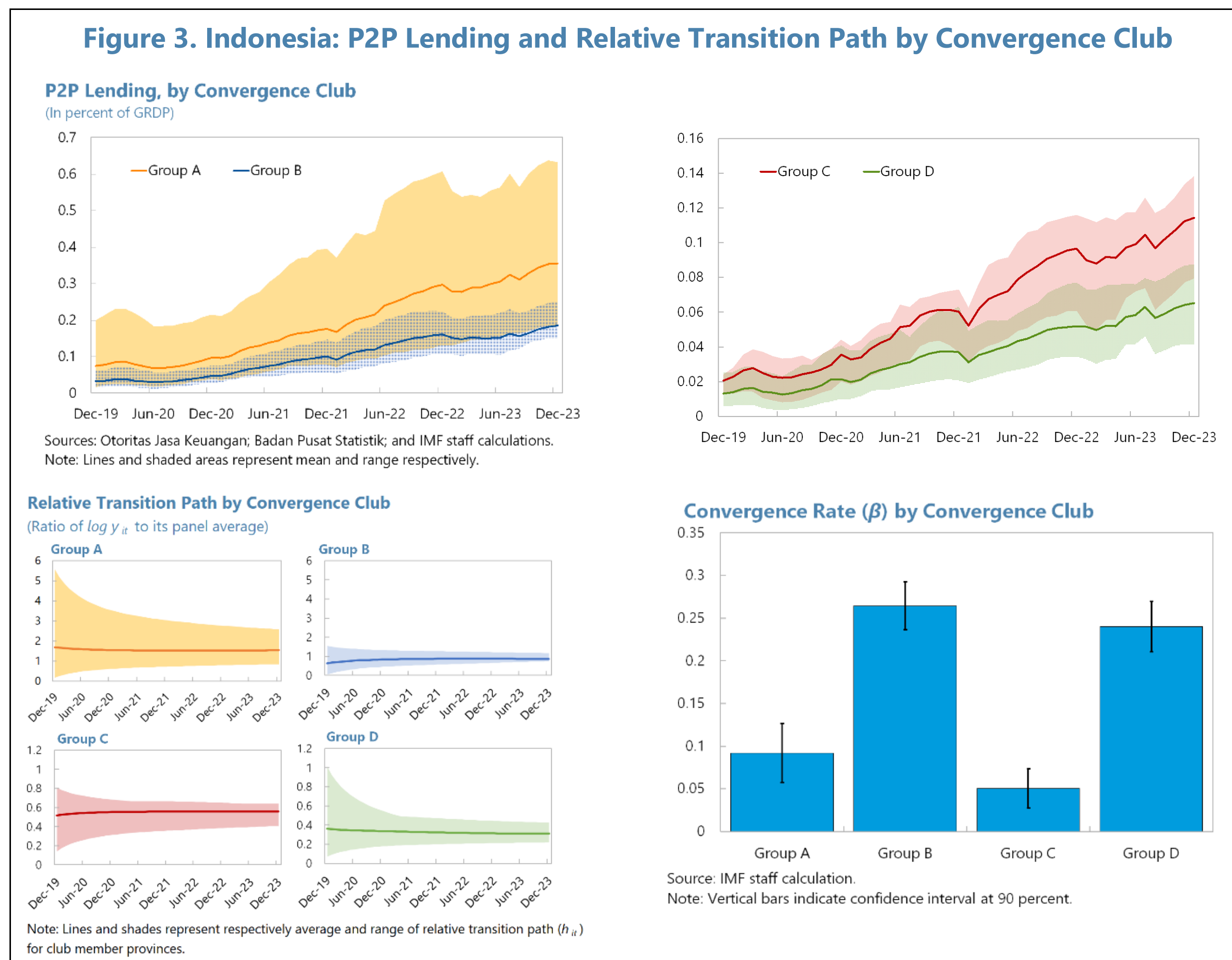
Determinants of Convergence Club Membership

Dependent Variable:	Club Membership, ordinal		Group A (Y/N)	
	(1)	(2)	(3)	(4)
	Ordered Logit	Ordered Probit	Binary Logit	Binary Probit
Financial Literacy	5.989*	3.432**	4.847*	3.009*
	(3.449)	(1.749)	(2.861)	(1.674)
Financial Inclusion	0.779	0.307	-0.991	-0.643
	(2.987)	(1.718)	(3.367)	(1.932)
Digitalization	6.369***	3.967***	4.870**	3.023***
	(1.947)	(1.126)	(1.977)	(1.161)
GRDP per capita	-2.549***	-1.527***	-1.563**	-0.995**
	(0.930)	(0.481)	(0.725)	(0.435)
Observations	34	34	34	34

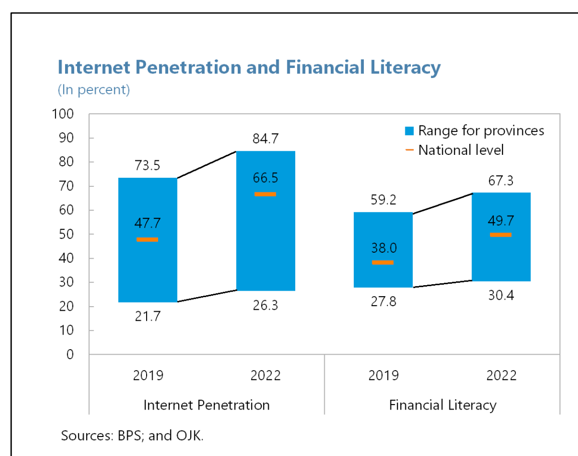
White standard errors in parentheses. Constant not reported.
+ = higher chance to belong to higher group (A>B>C>D).
* p<0.10, ** p<0.05, *** p<0.01

negative sign of the coefficient of the income level is in line with the results in the regression for P2P lending growth, suggesting weaker demand for alternative, innovative lending.

Figure 3. Indonesia: P2P Lending and Relative Transition Path by Convergence Club



11. Findings suggest that reducing digitalization and financial literacy gaps is crucial for fostering DFS. Indonesia's internet penetration improved rapidly from 47.7 percent of population (above 5 years old) in 2019 to 66.5 percent in 2022, but this was led by an acceleration in provinces with already high penetration rate, possibly accentuating divergences. The lowest province-level penetration rate rose from 21.7 percent to 26.3 percent during the same period, while the highest rate increased from 64.9 percent to 74.3 percent, resulting in a widening of the provincial gap between highest and lowest by 6.6 percentage points. Financial literacy marks a same pattern. Thanks to authorities' efforts, national financial literacy strengthened from 38.0 in 2019 to 49.7 in 2022, but regional disparities remained (the lowest level



of subnational financial literacy rose only by 2.6 for 2019-22, while the highest increased by 8.1). Thus, reducing inter-regional gaps is warranted to clearing constraints to DFS.

12. Efforts to strengthen regulation and supervision framework to address potential risks and enhance resilience in DFS should also continue. 2024 FSAP findings indicate a rapid market expansion of P2P lending quickly outpaced regulation, leading to the increasing need for policies preventing fraud and other misconduct; OJK's new guidelines for fintech lending—promoting transparency and sustainability and ensuring the protection of consumer interests—are welcome. Authorities should also strengthen cooperation for regulation and supervision, given the presence of large technology conglomerates and cross-cutting services.

Technical Annex

13. To test the club convergence, we use the approach suggested by Philip and Sul (2007, 2009, hereafter PS) and Schnurbus et al. (2017).

- *Log t convergence test*. The PS model uses a log t regression model for convergence test, assuming a factor model decomposing a panel data y_{it} as

$$\log y_{it} = g_{it} + a_{it}$$

where y_{it} is the P2P-to-GRDP ratio of province i at time t[5]. g_{it} represents systematic components, including permanent common components, and a_{it} represents transitory components. To separate common from idiosyncratic components in this panel, the PS model suggests transforming the factor model to

$$\log y_{it} = \left(\frac{g_{it}+a_{it}}{\mu_t}\right)\mu_t = \delta_{it}\mu_t, \qquad \text{for all } i \text{ and } t,$$

where μ_t is a single common component, and δ_{it} is a time-varying idiosyncratic element, governing the deviation from the common path among the whole panel units. This transformation allows to estimate the relative transition path (h_{it}),

$$h_{it} = \frac{\log y_{it}}{N^{-1}\Sigma_{i=1}^{N} \log y_{it}} = \frac{\delta_{it}}{N^{-1}\Sigma_{i=1}^{N}\delta_{it}}.$$

If convergence holds, h_{it} converges to unity. Then, a quadratic distance measure for transition differential (H_t) can be applied as

$$H_t = N^{-1}\sum_{i=1}^{N}(h_{it}-1)^2.$$

[5] Note that in the log-transformation unity was added, i.e. $y_{it} = P2P_{it} + 1$, to prevent $\log y_{it}$ from being negative for the ease of calculation of relative transition path (h_{it}).

In case of full convergence, H_t converges to zero as $t \to \infty$. Under club convergence, H_t typically converges to a positive constant. Finally, the convergence can be tested, by estimating the log t regression model suggested by PS (2007):

$$\boldsymbol{log\frac{H_1}{H_t} - 2\log(\log t) = \alpha + \beta \log t + u_t}$$

where β can be tested with the null hypothesis of convergence that $\delta_{it} = \delta$ and $\alpha \geq 0$ such that $\beta = 2\alpha$.[6] Alternative hypothesis, implying non-convergence, is either $\delta_{it} \neq \delta$ or $\alpha < 0$. In implementing the test, we use HP-filtered trend of $log\ y_{it}$, as suggested by PS (2007).

- *Clustering algorithm*. PS (2007) proposes an algorithm to identify the convergence clubs with the following steps:

  i. Order provinces in the panel decreasingly according to the last observation.

  ii. Choose a core group G_k of k provinces and compute test statistics $t_k = t(G_k)$ based on the log t regression result. Choose group size k to maximize the test statistic t_k subject to $min\ t_k > -1.65$. Where the minimum test statistic is not met with $k = 2$, drop the first province and proceed to maximize t_k.

  iii. Add a province not in the core group G_k at a time to the core group and run the log t test. Include that province in the club candidate group if the test statistic is greater than the critical value $c = 0$, which is set conservatively given small T.

  iv. Form a new group of the remaining provinces that are not sieved by step iii. Perform the log t test for this group. If the test statistic is greater than -1.65, the algorithm ends with two convergence group. Otherwise, repeat steps i-iii until the algorithm ends. The algorithm can end with provinces not included in any convergence club if the remaining provinces are divergent.

- *Club merging*. Schnurbus et al. (2017) suggests merging clubs iteratively by fulfilling the convergence test jointly with adjacent two clubs until convergence does not hold in a joint test.

[6] PS (2007) defines a relative convergence as $\lim_{t\to\infty} \delta_{it} = \delta$, for all i, and shows that the log t regression model can be applied for the one-sided convergence test with null hypothesis of $\alpha \geq 0$, assuming that for all i, $\delta_{it} = \delta_i + \sigma_{it}\xi_{it}$, where $\sigma_{it} = \frac{\sigma_i}{log(t)t^{\alpha}}$, $t \geq 1$, and $\sigma_i > 0$.

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Annex X. Managing Adverse Shocks: An IPF Application[1]

As Indonesia pursues its ambitious growth agenda, it will need to navigate a more shock-prone and challenging external environment. This annex explores, through the lens of the IMF's Integrated Policy Framework (IPF) and using hypothetical scenarios, the appropriate policy responses to a sharp and prolonged slowdown in China, and to U.S. monetary and fiscal policy shocks. The hypothetical slowdown in China manifests as a negative shock to external demand—with commodities being an important channel. FXI may be an appropriate component of the policy response (along with monetary and fiscal policies) only if the shock triggers a risk-off episode. FXI may also be a warranted element of the policy response to spillovers from U.S. policy shocks if such shocks were to trigger a risk-off sentiment. However, the exchange rate will need to play a large role as a shock absorber. In addition, with substantial uncertainty regarding the nature, magnitude, and duration of such shocks, policymakers will need to be judicious in the use of both FX reserve and fiscal buffers. Preserving buffers will be particularly important in a world where geoeconomic fragmentation is likely to lead to a prolonged period of more frequent and volatile external shocks.

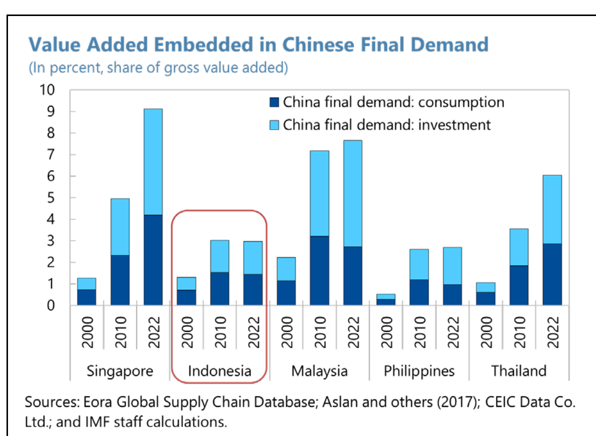
1. **China's importance for the global economy—and for Indonesia—has risen sharply in the past decades**. Along with regional peers, Indonesia's economy has become increasingly linked to China through its central position in global and regional value chains. China's importance as an export market for Indonesia has risen (including for Indonesia's commodities), and China's demand absorbed about 3 percent of Indonesian value added in 2022. Chinese investments flows—including FDI—have also risen in prominence.

2. **An analysis of policy responses to spillovers from China is motivated by the country's systemic role in the global economy, and the current period of heightened risks**. China's medium-term growth rate is projected to moderate with narrowing scope for catch-up growth and other structural constraints, including an ageing population. Besides the ongoing structural slowdown projected in the baseline, China's growth also faces downside risks, including from potentially a longer- or deeper-than-expected contraction in the property sector and rising geo-economic fragmentation. Given China's systemic relevance in the global economy, shocks originating from the country can have large impacts on global commodity prices and on growth in other economies—including Indonesia (IMF, 2024a). Like several Asian currencies, the IDR-USD exchange rate increasingly co-moves with the CNY-USD, with shocks from CNY depreciations spilling over to regional peers through competitive pressures (IMF, 2024b).

3. **At the same time, the U.S. remains the key driver of the global financial cycle, with domestic policy developments implying major spillovers for Indonesia and other EMs**. Over the past decade, several stress periods when the rupiah depreciated sharply against the US dollar were associated with shifts in U.S. policy stances, including the Taper Tantrum and the EM stress period of 2018. Since the beginning of the Fed's latest monetary policy tightening cycle, market uncertainty about its policy path, along with declining interest rate differentials vis-à-vis the U.S., has

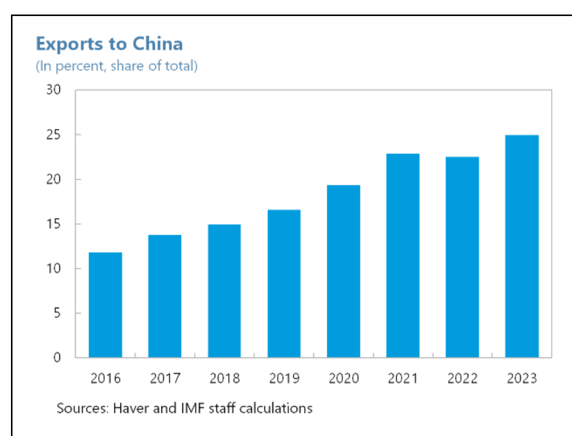
[1] Prepared by Ashique Habib (APD), with valuable inputs from Marcin Kolasa (MCM).

put periodic downward pressure on the rupiah and triggered interventions by BI. Alongside U.S. monetary policy, U.S. fiscal policy stance can also be a source for spillovers to EMs. Expansionary U.S. fiscal policy, by contributing to higher core inflation (as has been the case since 2021), can trigger spillovers by inducing greater monetary policy tightening. Recent IMF analysis suggests sharp increases in U.S. Treasury yields lead to surges in government bond yields and exchange rate turbulence in EMDEs (IMF, 2024c). Though the response of Indonesia's sovereign yields to the 2022-23 surge in the corresponding U.S. yields was relatively muted, recent IMF analysis suggests a 1 percentage-point increase in the U.S. 10-year Treasury yield is associated with, on average, about a 100-bps increase in EM 10-year government bond yields over several quarters. In addition, increases in U.S. fiscal policy uncertainty—such as during episodes in which the debt ceiling is debated, are associated with higher sovereign spreads in EMs. With heightened uncertainty regarding the path of U.S. monetary and fiscal policies, a sharp shock could trigger adverse spillovers for Indonesia.



Value Added Embedded in Chinese Final Demand
(In percent, share of gross value added)

Sources: Eora Global Supply Chain Database; Aslan and others (2017); CEIC Data Co. Ltd.; and IMF staff calculations.



Exports to China
(In percent, share of total)

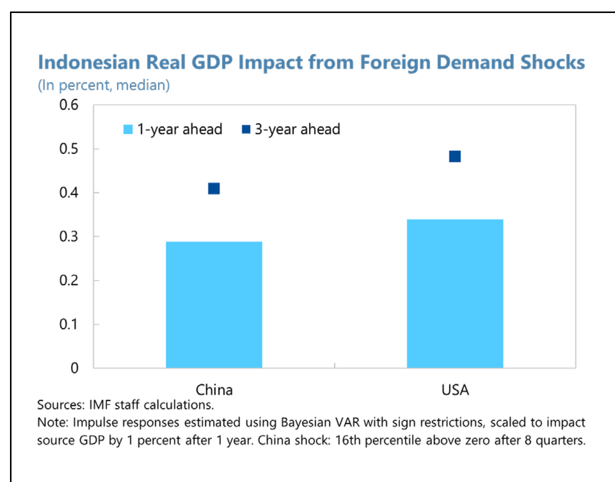
Sources: Haver and IMF staff calculations

4. We assess policy options to address shocks emanating from the U.S. and China through the lens of the IMF's Integrated Policy Framework (IPF). For open economies with flexible exchange rates, the IPF provides a comprehensive basis to assess the joint use of monetary policy, FXI, fiscal, macroprudential, and capital flow measures to address shocks. While exchange rate flexibility retains an essential stabilizing role under the IPF, under certain conditions, FXI may be an appropriate element of an overall policy response.

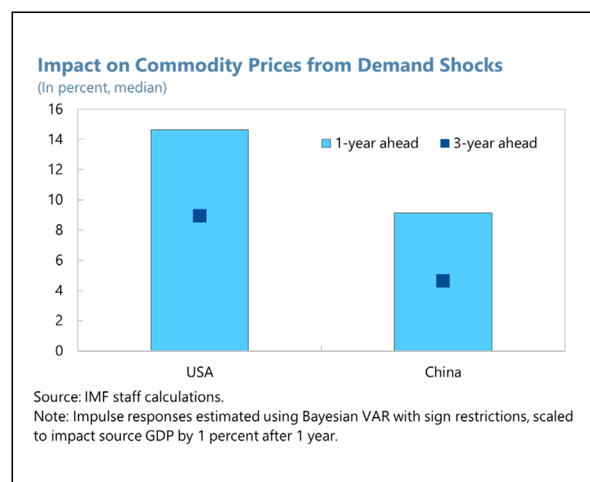
5. FXI may be warranted if country and shock characteristics satisfy one or more of three use cases. First, large capital outflows may trigger sharp and inefficient rise in market premia (e.g., UIP premia) in countries with shallow FX markets. FXI can help to contain large UIP deviations, and thereby avoid excessive tightening of financial conditions. Second, large exchange rate depreciations may trigger stress in economies where corporate sectors have large currency mismatches. The use of FXI to limit exchange rate depreciation can contain financial instability. Third, in economies where large depreciations could de-anchor inflation expectations, containing such depreciations through FXI could support price stability.

6. For Indonesia, shallow FX markets appear to be the key IPF friction. Inflation expectations are well-anchored to BI's target band since adoption of an inflation targeting framework in 2005. Corporates' external FX debt has moderated over the past decade, from about

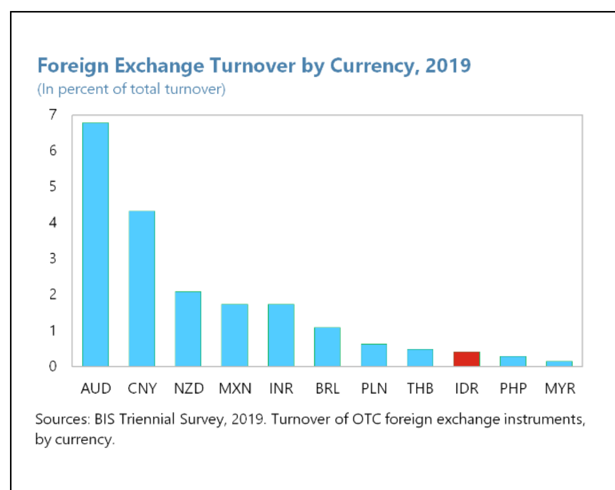
16.8 percent in 2015 to about 8.5 percent in 2023, with BI's prudential hedging and liquidity requirements helping to contain FX risks. However, FX markets in Indonesia are shallow compared to international peers, despite some recent progress in market deepening.



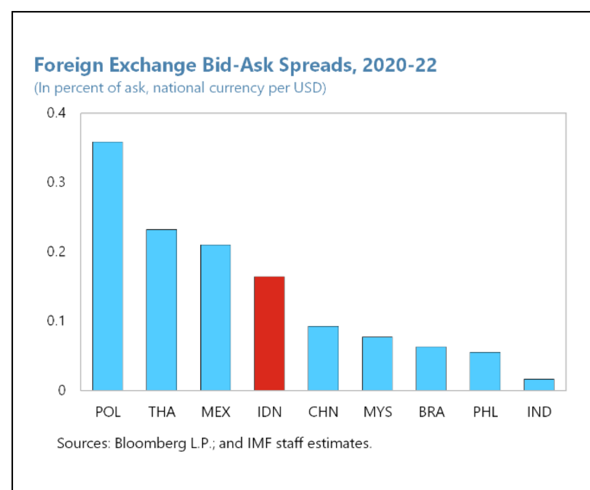
Sources: IMF staff calculations.
Note: Impulse responses estimated using Bayesian VAR with sign restrictions, scaled to impact source GDP by 1 percent after 1 year. China shock: 16th percentile above zero after 8 quarters.



Source: IMF staff calculations.
Note: Impulse responses estimated using Bayesian VAR with sign restrictions, scaled to impact source GDP by 1 percent after 1 year.



Sources: BIS Triennial Survey, 2019. Turnover of OTC foreign exchange instruments, by currency.



Sources: Bloomberg L.P.; and IMF staff estimates.

Model-Based Analysis

7. We use a micro-founded New Keynesian two-economy model to evaluate policy options in response to major external shocks, including the role of FXI. The model is a linearized version of the Adrian and others (2021) IPF model with potentially shallow FX markets, extended to include a supply side, commodities, and a fiscal sector.[2]

8. We consider several hypothetical scenarios centered on two sources of shocks, with scenario variations highlighting key distinctions relevant for the policy mix.

- *A hypothetical slowdown in the representative foreign economy*. The scenario is intended to explore in a stylized setting the impact from a slowdown in China, which may have significant

[2] See Indonesia 2023 Article Staff Report, Annex V (Country Report No. 2023/221) for a description of the model.

real sector implications with possible financial spillovers. Given significant uncertainties regarding the nature of such a shock, several variants are considered. In an acute shock scenario, a sharper than expected slowdown in the foreign economy is followed by a swift recovery. The slowdown in the foreign economy triggers a risk-off sentiment towards EMs and commodities exporters, tightening financial conditions. However, the appropriate policy mix in the absence of a risk-off shock, as well as to a persistent slowdown in the foreign economy (with and without an associated risk-off shock), are also considered.[3]

- *Fiscal and monetary policy shocks in the representative foreign economy*. In this stylized scenario—intended to explore mainly financial spillovers from the US—policy uncertainty increases, with looser-than-expected fiscal policy contributing to higher inflation (but also higher demand for imports), and to sharper-than-expected monetary policy tightening. The foreign economy's bond yields rise, which transmits to higher borrowing costs for EMs. These combined with higher policy uncertainty in the foreign economy triggers a risk-off shock for Indonesia.

Slowdown in the Foreign Economy

9. An acute slowdown in a representative foreign economy accompanied by a risk-off shock is considered. Concretely, the representative foreign economy experiences a demand-driven slowdown, with output 8 quarters after the beginning of the shock about 2 percent lower than baseline. Commodity prices fall, bottoming out after a 16 percent decline. The slowdown raises market concerns about spillovers to other emerging markets and commodity exporters, triggering a risk-off reaction modeled as about a 250-bps increase in the UIP premium.[4] The shock leads to a sharp fall in output below trend, in part due to the fall in commodities exports. The real exchange rate depreciates, contributing to a persistent rise in inflation (which would rise by about 0.7 percent without monetary policy tightening).[5] Three potential policy responses are compared: Monetary policy only; monetary policy and FXI; and monetary and FXI complemented by targeted fiscal transfers to households (Figure 1).

- *Monetary policy only.* The central bank hikes the policy rate by 1.2 percent, which reduces the inflation peak by half, mainly through higher borrowing costs compressing domestic demand. The deviation of output from trend at its trough widens to -1.3 percent after 8 quarters. The compression of domestic demand, along with real exchange rate depreciation, reduces imports

[3] In the hypothetical acute scenario, the deviation in the foreign economy's output from baseline after 2 years is about 2 percent, similar to the downside scenario in the 2023 Article IV Staff Report for China (Country Report No. 2024/038). In the stylized persistent shock scenario, the downward level-shift in the foreign economy's output could reflect a combination of worsening structural headwinds relative to the baseline projections, or a sharper-than-expected realization of China-OECD decoupling, along the lines of the downside risk scenario analysis in IMF (2023b).

[4] For illustrative purposes, similar to levels during the 2018 EM stress period.

[5] In this scenario, the risk-off shock is assumed to trigger a significant exchange rate depreciation, the inflationary impact of which offsets the impact of the output shock. This effect could be softened if inflation expectations remain well-anchored.

of non-commodities. While commodities exports largely recover with the foreign economy, the real exchange rate depreciation helps boost non-commodities exports, and rising non-commodities net exports help return output to trend over time.

- *Monetary policy and FXI*. The central bank uses FXI—about 2 percent of GDP—along with monetary policy. FXI helps to reduce the rise in the UIP premium, and hence limits the exchange rate depreciation. The resulting lower inflationary pressures allow the central bank to achieve a similar path for core inflation with less monetary policy tightening. Shallower monetary policy tightening leads to less domestic demand compression and a smaller fall of output relative to trend. The overall output path is more favorable compared to the monetary policy only scenario, as stronger domestic demand offsets the somewhat weaker external rebalancing, i.e., a smaller rise in net exports. However, the significant use of FXI reduces buffers against future shocks.

- *Monetary policy, FXI, and fiscal stimulus*. In addition to the interventions above, the authorities provide about 0.5 percent of GDP worth of transfers to households during the trough of the shock. The transfers further improve the path of output, by supporting domestic demand, and could also help reduce inequality. Monetary policy needs to be somewhat tighter than in the case without fiscal stimulus to achieve a similar path for core inflation.

- The policy option comprising monetary policy, fiscal stimulus and FXI—along with exchange rate flexibility, appears to best balance needed external adjustment with maintaining price stability and limiting the hit to domestic demand. FXI, by reducing the inefficient rise in UIP premia from the non-fundamental risk-off shock, helps to limit inflationary pressures and potentially disruptive tightening of financial conditions, and thereby improves the trade-off for monetary policy between price and output stabilization.

10. The appropriateness of FXI depends on financial market reactions to the foreign economy growth shock. To illustrate, we consider a scenario where the representative foreign economy experiences the same shocks—with similar impacts on commodity prices, but financial markets remain sanguine about spillovers for Indonesia (Figure 2). In this scenario, financial conditions do not tighten excessively, and with less exchange rate depreciation, inflationary pressures are moderate. Three policy options are presented: monetary policy only; monetary policy combined with fiscal stimulus; and monetary policy combined with FXI. If the starting point for inflation is well-within the target band, the central bank may be able to support domestic demand and reduce the deviation of output from trend by cutting the policy rate while keeping inflation contained. Combining such a monetary policy response with fiscal transfers could further help support domestic activity and protect vulnerable households. In comparison, the use of FXI would not materially change the deviation of output from trend. Rather, FXI would lead to a relatively higher exchange rate, and thereby mainly allow households to maintain imports financed through greater external borrowing. The use of FXI would not be warranted in this case.

11. A second case looks into a persistent slowdown in a representative major economy. Concretely, the representative foreign economy experiences a sharp slowdown in growth, but does not quickly bounce back to the pre-shock path. For Indonesia, while the exact path of the economy

will depend on policy choices (discussed below), the shock tends to lead to a sharp fall of output below trend, in part due to the fall in net exports of commodities, which remains persistently lower due to the drop in foreign demand. Absent countervailing policy interventions, the shock pushes the real exchange rate towards a persistently more depreciated level. Similar to the acute shock, whether FXI is a warranted component of the policy mix depends on whether the slowdown in the foreign economy is accompanied by a non-fundamental risk-off shock.

- *In case of an accompanying risk-off shock, FXI may be appropriate (Figure 3).* As in the acute shock, FXI can help to contain a rise in the UIP premium and excessive tightening of financing conditions. Such an intervention—modeled as an about 2 percent of GDP immediately after the shock—also allows the central bank to impose a shallower MP tightening and achieve a better balance between domestic demand and price stability. However, exchange rate depreciation after the initial FXI plays an important role in allowing the economy to adjust to the persistent nature of the shock, supporting the recovery of output by boosting net exports of non-commodities.

- *Absent the risk-off shock, the use of FXI is likely to delay the necessary adjustment (Figure 4)*. In this case, FXI mainly serves to prop up the exchange rate, facilitating more imports financed by higher external borrowing. The boost to domestic demand is offset by lower net exports, leaving the deviation of output from trend broadly unchanged. In this case, FXI would not be warranted.

- *Similar to FXI, any use of fiscal stimulus will need to be well-targeted, time-bound, and avoid hindering the optimal rebalancing of economic activity.* Since a persistent adverse shock reflects lower permanent incomes, it would be optimal for households to reduce consumption relative to the pre-shock baseline. While targeted fiscal support to vulnerable households and firms may help contain excessive scars in some cases, such interventions should be time-bound and well-targeted to facilitate needed adjustment and protect fiscal space.

Fiscal and Monetary Policy Shocks in the Foreign Economy

12. Hypothetical fiscal and monetary policy shocks in a representative major economy. Amidst higher policy uncertainty, fiscal expenditures surprise on the upside in the representative foreign economy, raising output by about 0.5 percent relative to baseline. Expansionary fiscal policy, combined with supply side shocks, leads to a spike in inflation, which rises by about 1.1 percent even as the foreign central bank tightens monetary policy by 0.6 percent. The expansionary fiscal policy and heightened uncertainty is assumed to cause a persistent rise in the foreign economy's bond yields, which transmits to higher EM borrowing costs of a similar magnitude (i.e., about 100 bps) and persistence. In addition, the shocks trigger a risk-off period, modeled as a further rise in Indonesia's UIP premium, as investors retrench from EM exposures amidst policy shocks and higher policy uncertainty. While the expansionary foreign fiscal policy, along with depreciation pressures on the Rupiah, boosts net exports, core inflation also rises above the central banks' target. Several policy options are considered (Figure 5).

- *Monetary policy only*. The central bank raises the policy rate by about 1.8 percent, which keeps the peak in inflation at about 0.5 percent. Even with the monetary policy tightening, the cumulative impact of the external shocks lead to an abrupt 8 percent decline in the real exchange rate, which then gradually recovers. Domestic demand falls below trend by about 1 percent at its trough due to tighter credit conditions. However, the fall of output below trend is marginal, as higher net exports—reflecting higher foreign demand and further facilitated by the exchange rate depreciation—largely offsets the decline in domestic demand.

- *Monetary policy and fiscal stimulus*. In addition to tightening monetary policy to tackle inflation, the authorities use fiscal stimulus in the form of targeted transfers over eight quarters to households. The fiscal intervention has a cumulative cost of about 0.5 percent of GDP. The boost to domestic demand reduces the deviation of output from trend during the period of intervention, without significantly changing the dynamics of inflation or trade.

- *Monetary policy and FXI*. The central bank uses FXI—about 2 percent of GDP—to reduce the excessive rise in UIP premium, which also reduces the exchange rate depreciation. The associated reduction in inflationary pressures allows the central bank to achieve a similar path for core inflation with less monetary policy tightening. Output actually rises above trend, as lower borrowing costs (and a less depreciated exchange rate) helps to significantly reduce the decline in domestic demand. There is an overall pivot away from external demand relative to the other two options, with net exports of both commodities and non-commodities declining.

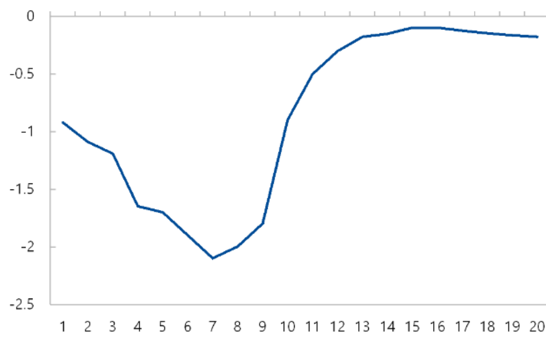
- The third option—using FXI in the face of large non-fundamental and speculative shocks alongside monetary policy, appear to achieve internal and external balance most prudently. Adding fiscal stimulus to the mix would only marginally improve upon the moderate domestic demand shortfall achieved with the combined FXI and monetary policy tightening. It may instead be prudent to preserve fiscal buffers. At the same time, the use of FXI will need to be judicious: a fundamental rise in borrowing costs should be accommodated through exchange rate flexibility, for example if the rising costs reflect a persistent shift in major economies' financing needs.

Concluding Remarks

13. Policymakers will need act under substantial uncertainty and keep future needs in mind. In practice, policymakers are likely to face real-time uncertainty distinguishing between the real and financial shocks, particularly as such shocks are often correlated. In addition, the duration of a shock will likely only be revealed over time. As such, policymakers may need to intervene before a comprehensive assessment of the nature of the shock is feasible. However, interventions should be temporary and targeted to short-term distortions to prices and quantities that may emerge in the context of shallow markets, and will need to keep in mind the available reserves, the cost of rebuilding reserves, and the need to maintain sufficient buffers against future shocks.

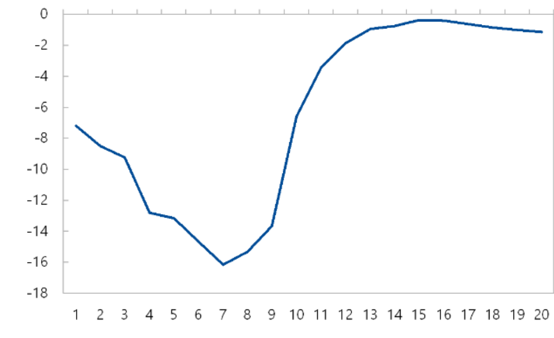
Figure 1. Indonesia: Acute Slowdown in Foreign Economy with Risk Off Shock

Foreign Output
(In percent; relative to baseline)



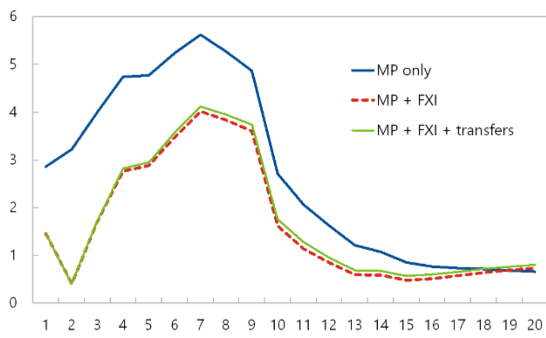
Source: IMF staff estimates

Commodity price
(In percent, relative to baseline)



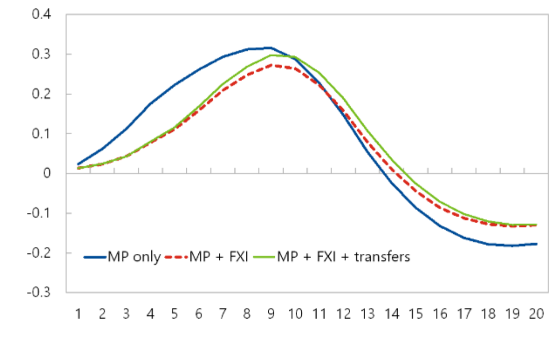
Source: IMF staff estimates.

Real Exchange Rate
(In percent, relative to baseline)



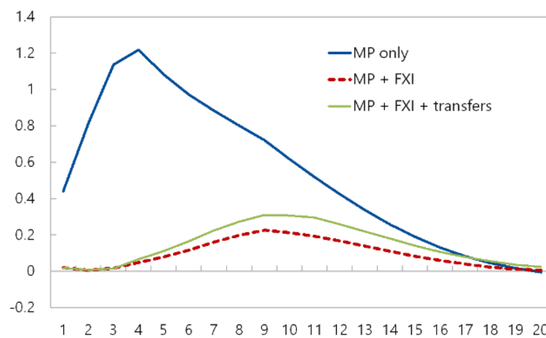
Source: IMF staff estimates.

Core Inflation
(In percent, year-on-year)



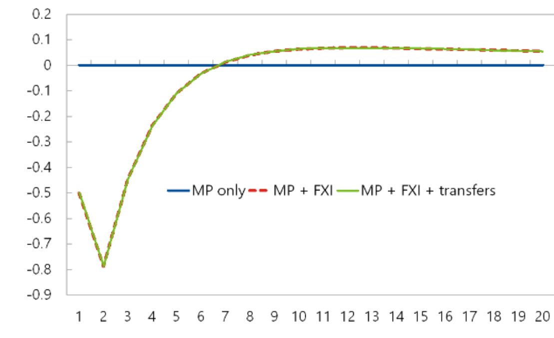
Source: IMF staff estimates.

Policy Rate
(In percent per year)



Source: IMF staff estimates.

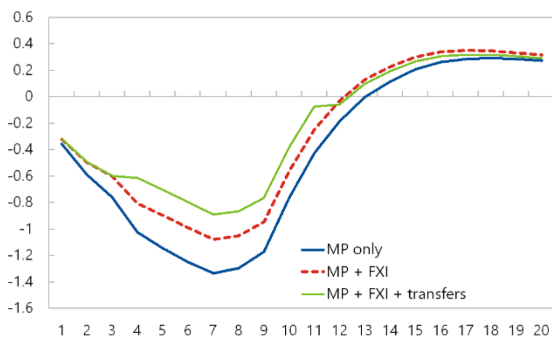
FX Intervention
(In percent, trend GDP)



Source: IMF staff estimates.

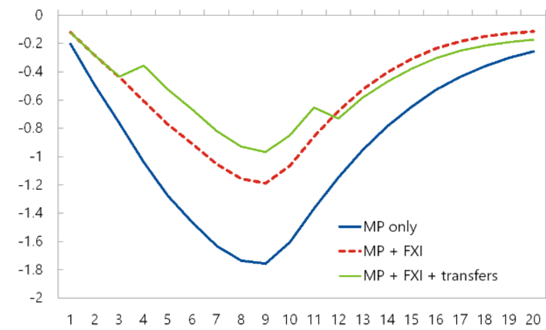
Figure 1. Indonesia: Acute Slowdown in Foreign Economy with Risk Off Shock (Concluded)

Output
(In percent, relative to baseline)



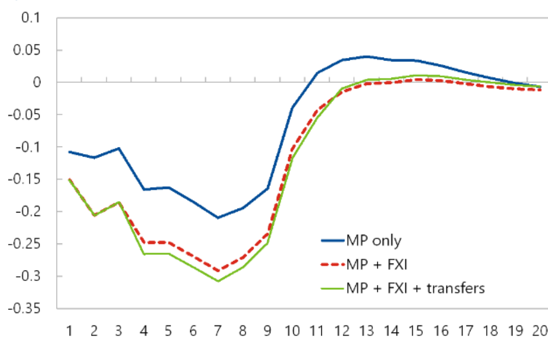
Source: IMF staff estimates.

Domestic Demand
(In percent, relative to baseline)



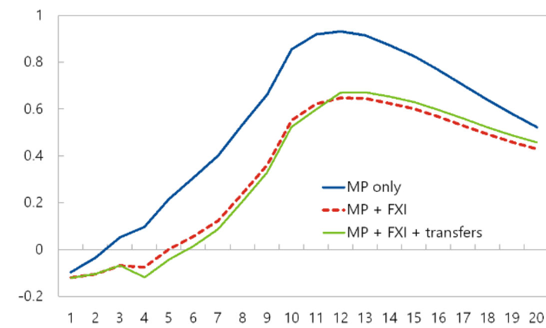
Source: IMF staff estimates.

Real Net Exports, Commodities
(In percent, trend GDP)



Source: IMF, staff estimates.

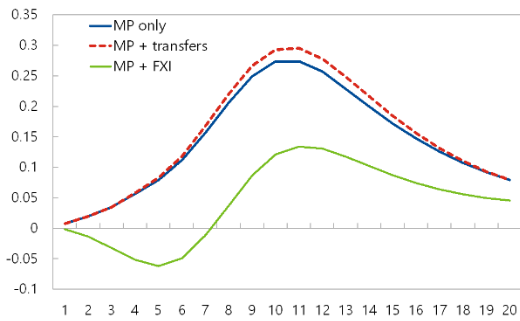
Real Net Exports, Non-Commodities
(In percent, trend GDP)



Source: IMF staff estimates.

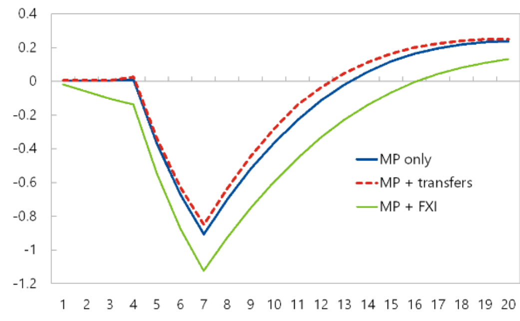
Figure 2. Indonesia: Acute Slowdown in Foreign Economy, No Risk-off Shock

Core Inflation
(In percent, year-on-year)



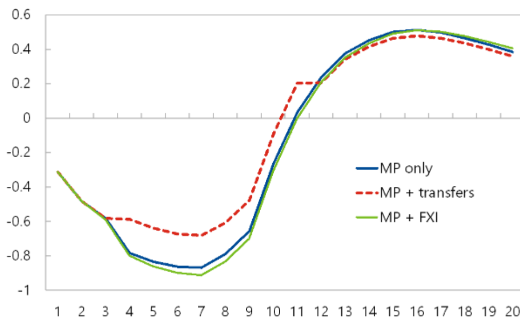
Source: IMF staff estimates.

Policy Rate
(In percent per year)



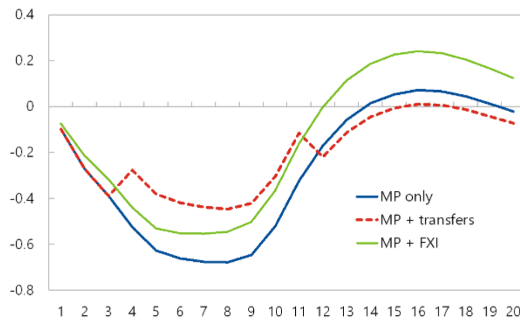
Source: IMF staff estimates.

Output
(In percent, relative to baseline)



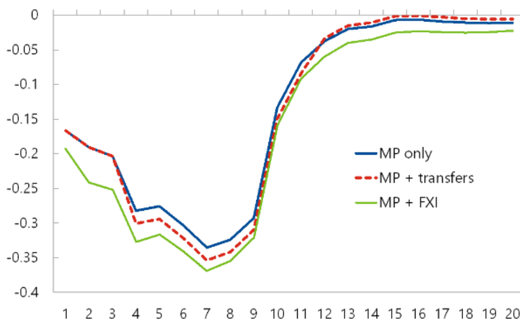
Source: IMF staff estimates.

Domestic Demand
(In percent, relative to baseline)



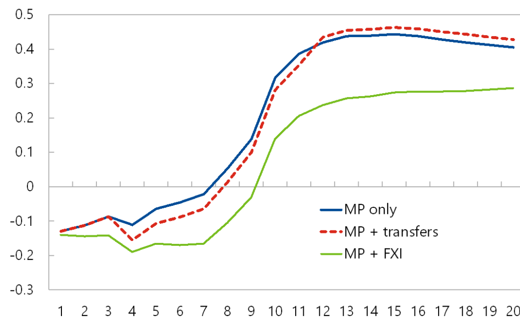
Source: IMF staff estimates.

Real Net Exports, Commodities
(In percent, trend GDP)



Source: IMF staff estimates.

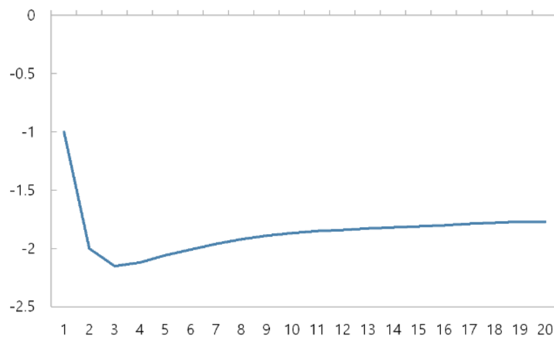
Real Net Exports, Non-Commodities
(In percent, trend GDP)



Source: IMF staff estimates.

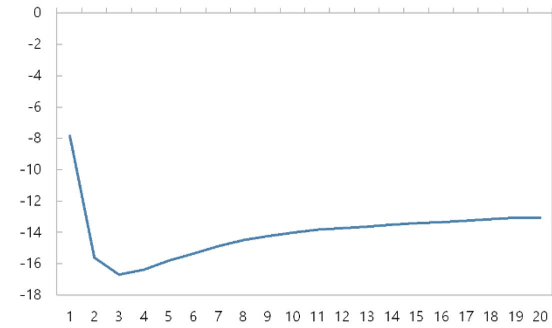
Figure 3. Indonesia: Persistent Slowdown in the Foreign Economy with Risk-Off Shock

Foreign Output
(In percent, relative to baseline)



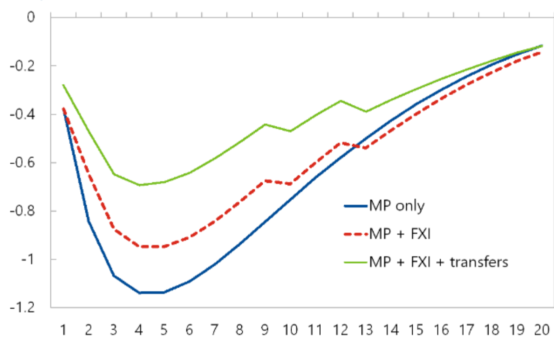
Source: IMF staff estimates.

Commodity price
(In percent, relative to baseline)



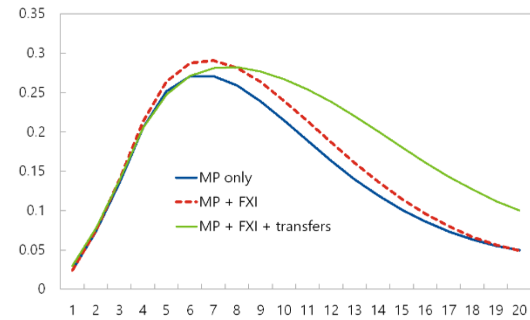
Source: IMF staff estimates.

Output
(In percent, relative to baseline)



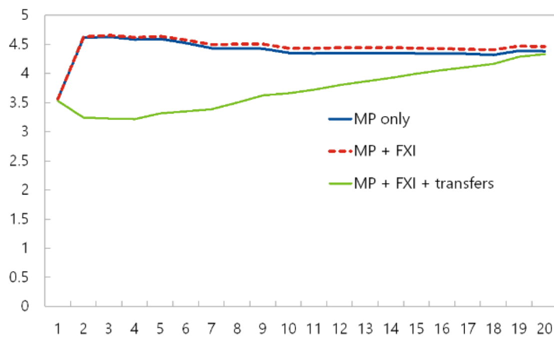
Source: IMF staff estimates.

Core Inflation
(In percent, year-on-year)



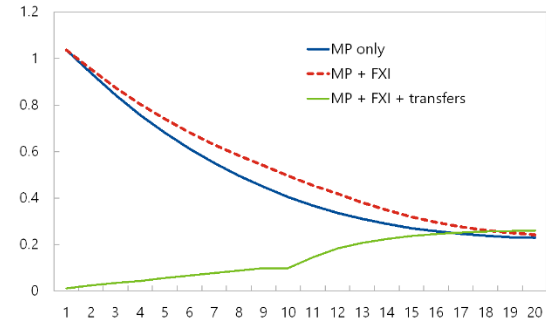
Source: IMF staff estimates.

Real Exchange Rate
(In percent, relative to baseline)



Source: IMF staff estimates.

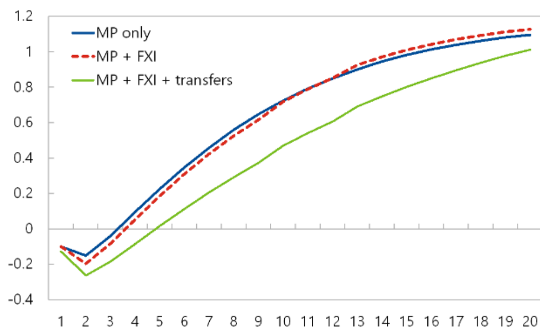
Policy Rate
(In percent per year)



Source: IMF staff estimates.

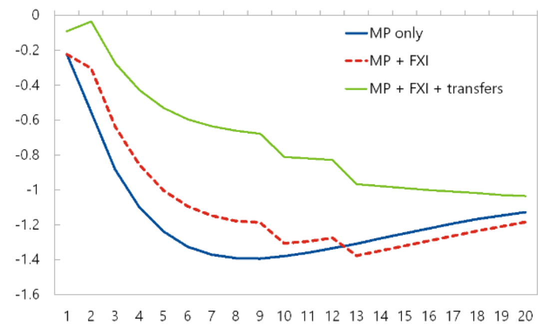
Figure 3. Indonesia: Persistent Slowdown in the Foreign Economy with Risk-Off Shock (Concluded)

Real Net Exports, Non-Commodities
(In percent, trend GDP)



Source: IMF staff estimates.

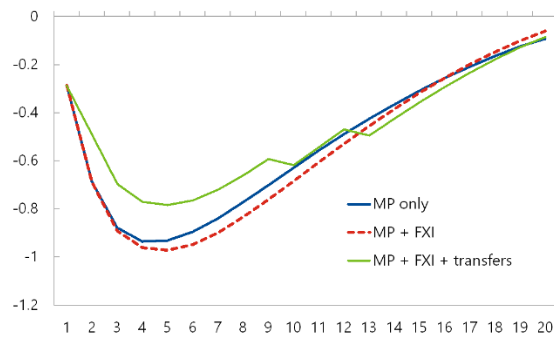
Domestic Demand
(In percent, relative to baseline)



Source: IMF staff estimates.

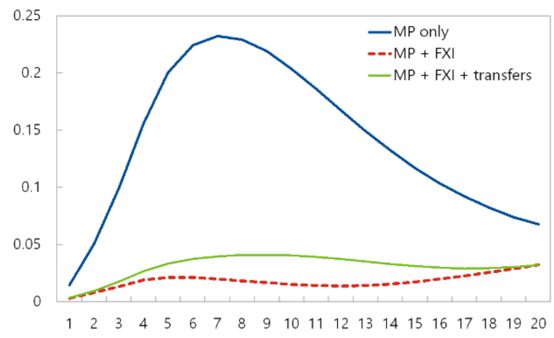
Figure 4. Indonesia: Persistent Slowdown, No Risk-Off Shock

Output
(In percent, relative to baseline)



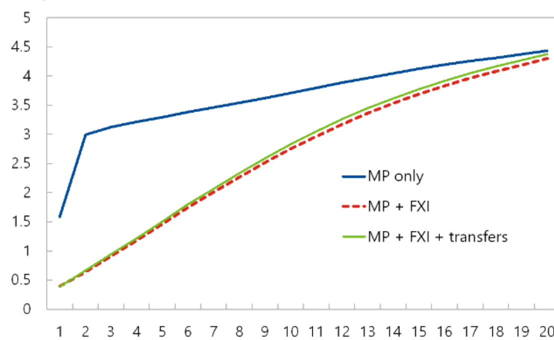
Source: IMF staff estimates.

Core Inflation
(In percent, year-on-year)



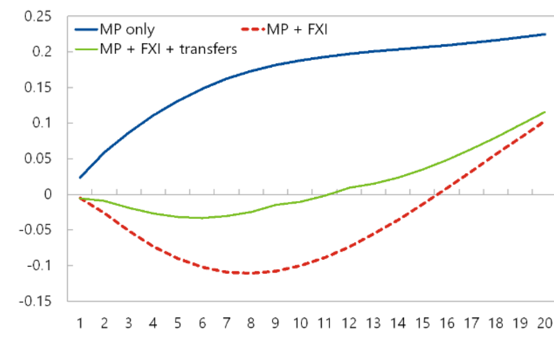
Source: IMF staff estimates.

Real Exchange Rate
(In percent, relative to baseline)



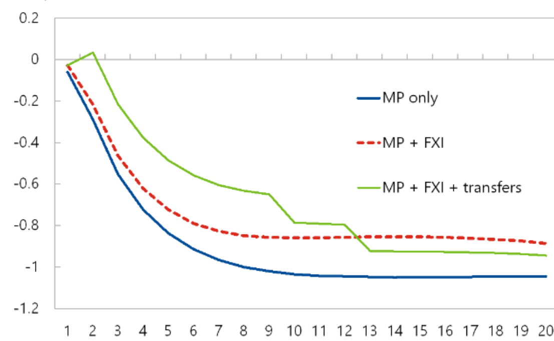
Source: IMF staff estimates.

Policy Rate
(In percent per year)



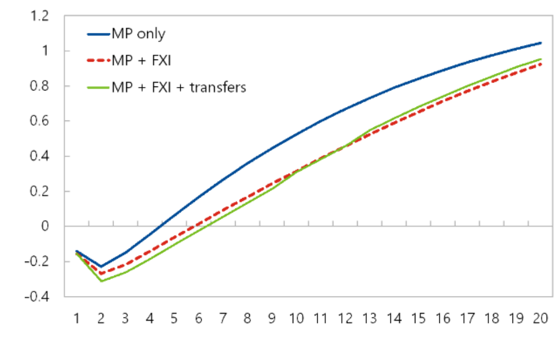
Source: IMF staff estimates.

Domestic Demand
(In percent, relative to baseline)



Source: IMF staff estimates.

Real Net Exports, Non-Commodities
(In percent, trend GDP)

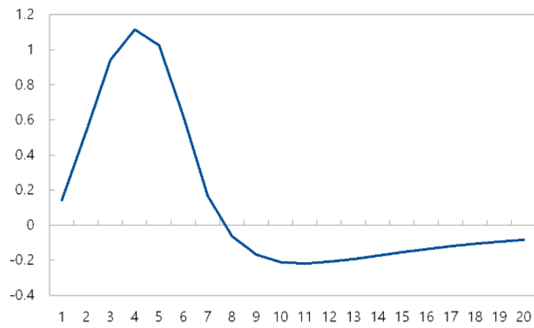


Source: IMF staff estimates.

Figure 5. Indonesia: Fiscal and Monetary Shocks in Foreign Economy

Foreign Core Inflation

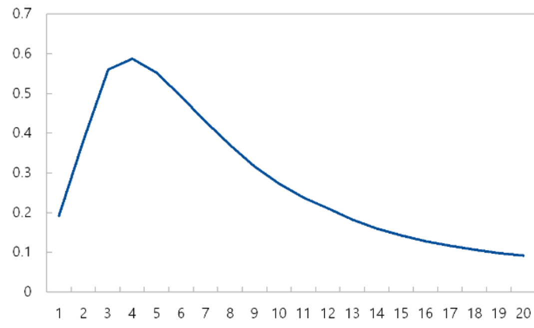
(In percent, year-on-year)



Source: IMF staff estimates.

Foreign Policy Rate

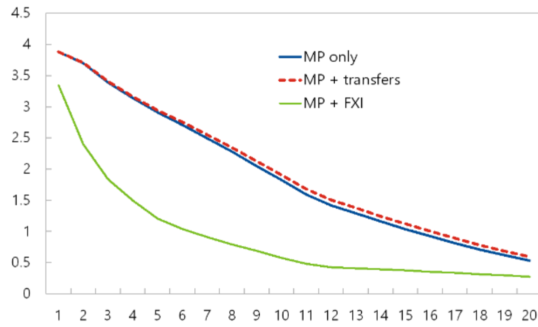
(In percent per year)



Source: IMF staff estimates.

UIP Premium

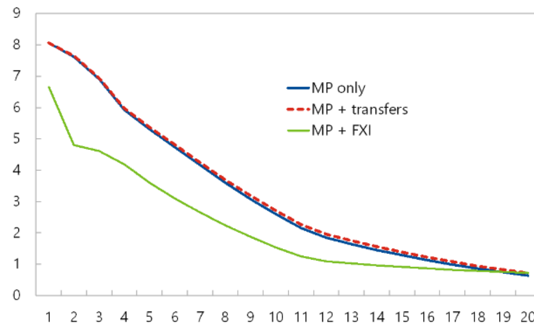
(In percentage point)



Source: IMF staff estimates.

Real Exchange Rate

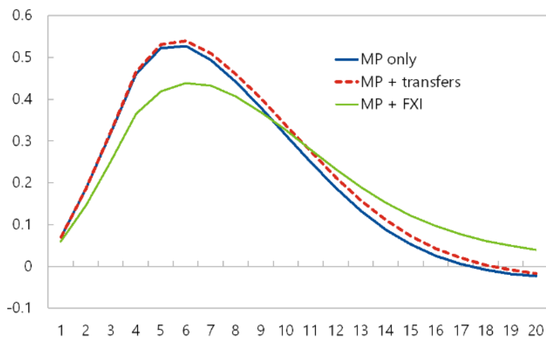
(In percent, relative to baseline)



Source: IMF staff estimates.

Core Inflation

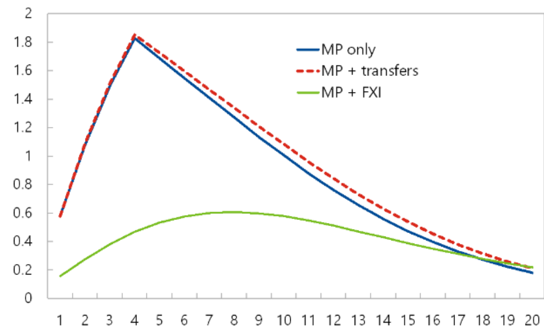
(In percent, year-on-year)



Source: IMF staff estimates.

Policy Rate

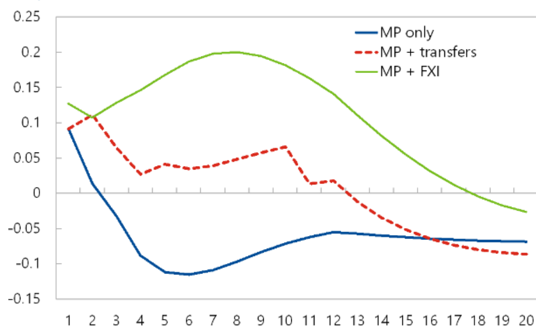
(In percent per year)



Source: IMF staff estimates.

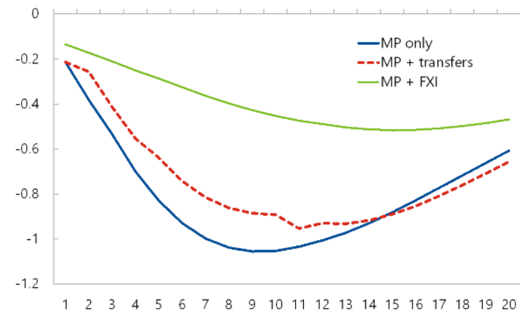
Figure 5. Indonesia: Fiscal and Monetary Shocks in Foreign Economy (Concluded)

Output
(In percent, relative to baseline)



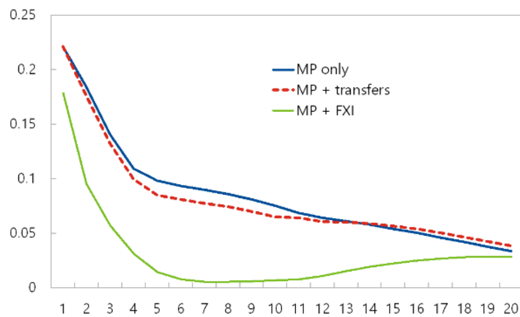
Source: IMF staff estimates.

Domestic Demand
(In percent, relative to baseline)



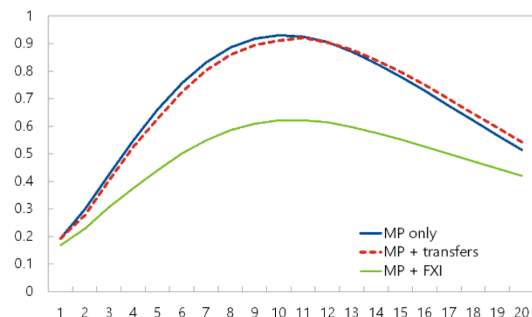
Source: IMF staff estimates.

Real Net Exports, Commodities
(In percent, trend GDP)



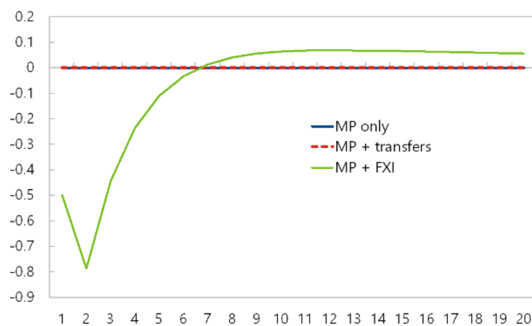
Source: IMF staff estimates.

Real Net Exports, Non-Commodities
(In percent, trend GDP)



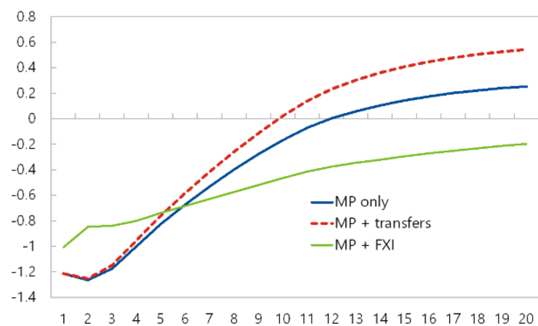
Source: IMF staff estimates.

FX Intervention
(In percent, trend GDP)



Source: IMF staff estimates.

Public Debt
(In percent, relative to baseline)



Source: IMF staff estimates.

References

Adrian, T., C. Erceg, M. Kolasa, J. Linde, and P. Zabczyk (2021) "A Quantitative Microfounded Model for the Integrated Policy Framework", IMF WP 21/292.

International Monetary Fund (2023a) "Indonesia: 2023 Article IV Consultation Staff Report", IMF Country Report No. 2023/221.

International Monetary Fund (2023b) "Regional Economic Outlook Asia and Pacific: Challenges to Sustaining Growth and Disinflation", IMF, October 2023.

International Monetary Fund (2024a) "World Economic Outlook: Steady but Slow", IMF, April 2024.

International Monetary Fund (2024b) "Regional Economic Outlook Asia and Pacific: Steady Growth Amid Diverging Prospects", IMF, April 2024.

International Monetary Fund (2024c) "Fiscal Monitor: Fiscal Policy in the Great Election Year", IMF, April 2024.

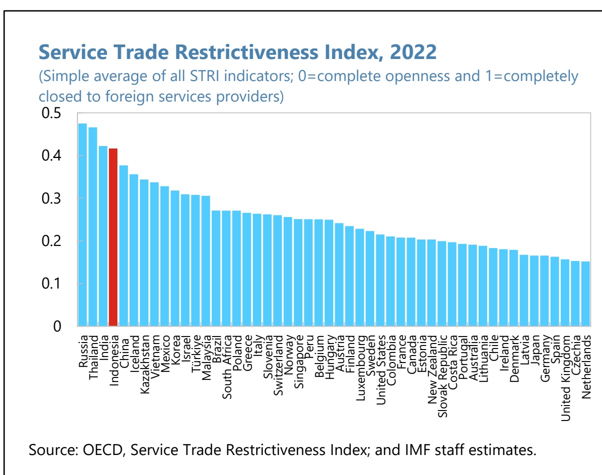
International Monetary Fund (2024d) "People's Republic of China: 2023 Article IV Consultation Staff Report", IMF Country Report No. 2024/038.

Annex XI. Trade Policy

1. Indonesia has a trade policy regime characterized by moderate import tariffs. Its average Most-Favored Nation tariffs amount to 8 percent in 2022 (WTO data). Duties on international trade accounted for around 3 percent of total tax revenue in 2020 according to the WTO Trade Policy Review (2.6 percent from import tariffs, 0.4 percent from export duties). Tariffs are, however, relatively high compared to regional peers.

2. Indonesia has relatively high non-tariff measures (NTMs) on trade, and trade on services is highly restricted. This includes export restrictions on minerals and local content requirements linked to import tariff exemptions, domestic tax reductions, market access and government procurement. In aggregate, Indonesia's NTMs are above global average (see MATR database, Estefania-Flores et al., 2022), whilst Services Trade Restrictiveness is among the highest within countries.

Service Trade Restrictiveness Index, 2022
(Simple average of all STRI indicators; 0=complete openness and 1=completely closed to foreign services providers)



Source: OECD, Service Trade Restrictiveness Index; and IMF staff estimates.

3. Strengthening Indonesia's economic openness would be key to boosting Indonesia's attractiveness. In particular, this would support attracting investment and FDI**.** This calls for gradually phasing out restrictive trade policies, including to support the objective of increasing business certainty and improving Indonesia's attractiveness to foreign investors. Historical evidence suggests that countries that experienced episodes of strong and sustained growth also witnessed an increase in economic openness.

Annex XII. Data Issues[1]

Table 1. Indonesia: Data Adequacy Assessment for Surveillance

Data Adequacy Assessment Rating 1/							
B							
Questionnaire Results 2/							
Assessment	National Accounts	Prices	Government Finance Statistics	External Sector Statistics	Monetary and Financial Statistics	Inter-sectoral Consistency	Median Rating
	B	B	A	B	A	B	B
Detailed Questionnaire Results							
Data Quality Characteristics							
Coverage	B	B	B	B	A		
Granularity 3/	B		A	B	A		
			A		A		
Consistency			B	B		B	
Frequency and Timeliness	A	A	A	A	A		

Note: When the questionnaire does not include a question on a specific dimension of data quality for a sector, the corresponding cell is blank.
1/ The overall data adequacy assessment is based on staff's assessment of the adequacy of the country's data for conducting analysis and formulating policy advice, and takes into consideration country-specific characteristics.
2/ The overall questionnaire assessment and the assessments for individual sectors reported in the heatmap are based on a standardized questionnaire and scoring system (see IMF *Review of the Framework for Data Adequacy Assessment for Surveillance* , January 2024, Appendix I).
3/ The top cell for "Granularity" of Government Finance Statistics shows staff's assessment of the granularity of the reported government operations data, while the bottom cell shows that of public debt statistics. The top cell for "Granularity" of Monetary and Financial Statistics shows staff's assessment of the granularity of the reported Monetary and Financial Statistics data, while the bottom cell shows that of the Financial Soundness indicators.

A	The data provided to the Fund is adequate for surveillance.
B	The data provided to the Fund has some shortcomings but is broadly adequate for surveillance.
C	The data provided to the Fund has some shortcomings that somewhat hamper surveillance.
D	The data provided to the Fund has serious shortcomings that significantly hamper surveillance.

Rationale for staff assessment. Data provision is broadly adequate for surveillance. However, some shortcomings remain on the areas of national accounts, external and fiscal statistics. Staff assessment reflects the absence of a breakdown of investment data in national accounts between public and private. It also reflects the absence of seasonally adjusted quarterly national accounts, the need for an updated base year (currently 2010) and the remaining (albeit declining) inconsistencies between the national accounts and BOP trade data. There is also a presence of small negative net errors and omissions in BOP (averaging -0.1 percnet of GDP in the last 5 years) that suggests a possible under-coverage in the amount of imports in the current account, or the accumulation of assets in the financial account.

Changes since the last Article IV consultation. The inflation expectation survey has been resumed, but remains for internal use of Bank Indonesia. CPI has been rebased to 2022=100, and was first released in early February 2024.

Corrective actions and capacity development priorities. Authorities are working on improving the quality of their statistics, including, for example, to reduce the gap between National Accounts and BoP data, as well as on strengthening the fiscal accounts (GFS). Further work could expand on their efforts on external sector statistics.

Use of data and/or estimates different from official statistics in the Article IV consultation. For nominal and real effective exchange rate (NEER and REER) data staff uses Fund calculated data instead of authorities' as the methodology used is consistent for all member countries.

Other data gaps. Labor data frequency and timeliness could be strengthened. While the granularity of the data is sufficient, the data is published only twice a year. Quarterly or monthly data would allow for an enhanced monitoring of economic conditions (including the output gap) as well as of the impact of structural reforms and long-term scarring of the pandemic across industries.

[1] Prepared by Agnes Isnawangsih (APD).

Table 2. Indonesia: Data Standards Initiatives

Indonesia subscribes to the Special Data Dissemination Standard (SDDS) since September 1996 and publishes the data on its National Summary Data Page. The latest SDDS Annual Observance Report is available on the Dissemination Standards Bulletin Board (https://dsbb.imf.org/).

Table 3. Indonesia: Table of Common Indicators Required for Surveillance

As of July 1, 2024

	Data Provision to the Fund				Publication under the Data Standards Initiatives through the National Summary Data Page			
	Date of Latest Observation	Date Received	Frequency of Data[6]	Frequency of Reporting[6]	Expected Frequency[6,7]	Indonesia[8]	Expected Timeliness[6,7]	Indonesia[8]
Exchange Rates	1-Jul-24	1-Jul-24	D	D	D	D	...	1D
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	May-24	Jun-24	M	M	M	M	1W	NLT 1W
Reserve/Base Money	Apr-24	May-24	W/M	W/M	M	W	2W	1W
Broad Money	Apr-24	May-24	M	M	M	M	1M	NLT 1M
Central Bank Balance Sheet	Apr-24	May-24	M	M	M	W	2W	1W
Consolidated Balance Sheet of the Banking System	Apr-24	May-24	M	M	M	M	1M	NLT 1M
Interest Rates[2]	1-Jul-24	1-Jul-24	D	D	D	D	...	1D
Consumer Price Index	Jun-24	Jul-24	M	M	M	M	1M	1D
Revenue, Expenditure, Balance and Composition of Financing[3]–General Government[4]	2022	Dec-23	A	A	A	A	2Q	10M
Revenue, Expenditure, Balance and Composition of Financing[3]–Central Government	May-24	Jul-24	M	M	M	M	1M	1M
Stocks of Central Government and Central Government-Guaranteed Debt[5]	Mar-24	May-24	Q	Q	Q	Q	1Q	NLT 1Q
External Current Account Balance	Mar-24	May-24	Q	Q	Q	Q	1Q	1Q
Exports and Imports of Goods and Services	Mar-24	May-24	Q	Q	M	M	8W	NLT 33D
GDP/GNP	Mar-24	May-24	Q	Q	Q	Q	1Q	35D
Gross External Debt	Mar-24	May-24	Q	Q	Q	Q	1Q	NLT 1Q
International Investment Position	Mar-24	May-24	Q	Q	Q	Q	1Q	1Q

[1] Includes reserve assets pledged or otherwise encumbered, as well as net derivative positions.

[2] Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

[3] Foreign, domestic bank, and domestic nonbank financing.

[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.

[5] Including currency and maturity composition.

[6] Frequency and timeliness: ("D") daily; ("W") weekly or with a lag of no more than one week after the reference date; ("M") monthly or with lag of no more than one month after the reference date; ("Q") quarterly or with lag of no more than one quarter after the reference date; ("A") annual.; ("SA") semiannual; ("I") irregular; ("NA") not available or not applicable; and ("NLT") not later than.

[7] Encouraged frequency of data and timeliness of reporting under the e-GDDS and required frequency of data and timeliness of reporting under the SDDS and SDDS Plus. Any flexibility options or transition plans used under the SDDS or SDDS Plus are not reflected. For those countries that do not participate in the IMF Data Standards Initiatives, the required frequency and timeliness under the SDDS are shown for New Zealand, and the encouraged frequency and timeliness under the e-GDDS are shown for Eritrea, Nauru, South Sudan, and Turkmenistan.

[8] Based on the information from the Summary of Observance for SDDS and SDDS Plus participants, and the Summary of Dissemination Practices for e-GDDS participants, available from the IMF Dissemination Standards Bulletin Board (https://dsbb.imf.org/). For those countries that do not participate in the Data Standards Initiatives, as well as those that do have a National Data Summary Page, the entries are shown as "..."

INTERNATIONAL MONETARY FUND

INDONESIA

July 2, 2024

STAFF REPORT FOR THE 2024 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By | Asia and Pacific Department

CONTENTS

FUND RELATIONS 2

RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS 4

FUND RELATIONS

(As of May 31, 2024)

Membership Status: Joined February 21, 1967; Article VIII

General Resources Account

	SDR Millions	Percent of Quota
Quota	2,042.90	100.00
IMF's holdings of currency (holding rate)	1,486.02	72.74
Reserve tranche position	557.02	27.27

SDR Department

	SDR Millions	Percent of Allocation
Net cumulative allocation	2,795.99	100.00
Holdings	2,851.27	101.98

Outstanding Purchases and Loans: None

Financial Arrangements

Type	Approval Date	Expiration Date	Amount Approved (SDR Millions)	Amount Drawn (SDR Millions)
EFF	Apr 01, 1998	Dec 31, 2000	1,020.79	783.23
EFF	Jun 24, 1994	Mar 31, 1998	791.20	791.20
Stand by	Feb 20, 1991	Mar 31, 1993	334.20	334.20

Projected Payments to Fund (SDR millions; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2024	2025	2026	2027	2028
Principal					
Charges/Interest		0.02	0.02	0.02	0.02
Total		0.02	0.02	0.02	0.02

Exchange Rate Arrangements

The rupiah has had a *de jure* free floating exchange arrangement since August 14, 1997, and the current *de facto* arrangement is floating. The market exchange rate was Rp 16,321 per U.S. dollar as of July 1, 2024. Indonesia has accepted the obligations of Article VIII, Sections 2, 3, and 4, and maintains an exchange system free of restrictions on payments and transfers for current international transactions and multiple currency practices.

Article IV Consultation

The last Article IV consultation report (IMF Country Report No. 23/221) was discussed by the Executive Board on May 22, 2023.

Resident Representative

Mr. Dennis Botman has been the Resident Representative since August 2023.

RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS

- World Bank: https://www.worldbank.org/en/country/indonesia
- Asian Development Bank: https://www.adb.org/countries/indonesia/main

Statement by Ms. Yati Kurniati, Executive Director for Indonesia,
Mr. Irfan Hendrayadi, Senior Advisor to Executive Director
July 22, 2024

On behalf of the Indonesian authorities, we extend our sincere appreciation to the staff for the productive policy discussions during the Article IV and FSAP missions. The assessments and recommendations presented in the reports offer invaluable insights. The authorities deeply value the engagement with cross-agency representatives and look forward to further strengthening these collaborations going forward.

Outlook

Recent economic performance has demonstrated resilience amid global uncertainties. The momentum of economic growth remained robust, staying above 5%, with an indication of improvement as reflected in the Q1 2024 economic growth rate of 5.11% year-on-year, which is higher compared to 5.04% in Q4 2023. This growth was driven by robust household consumption, significantly benefiting from the general election and substantial investment in infrastructure projects. In the first half of 2024, exports have shown signs of improvement, albeit limited due to continued lower commodity prices.

The BoP remained relatively strong, with a manageable current account deficit of 0.1% GDP in 2023 and 0.6% of GDP in Q1 2024. In 2024, the trade balance continued in surplus, primarily due to non-oil and gas exports, which helped maintain external resilience. The capital and financial account experienced fluctuations due to global financial market uncertainties, resulting in periods of capital outflows in Q1 2024. However, recent developments indicate that the current account deficit will remain low, supported by a continuing trade balance surplus, with capital and financial transactions recording surpluses. BoP performance in 2024 is expected to remain healthy, underscored by a low and manageable current account deficit in the 0.1%-0.9% of GDP range, as well as a capital and financial account surplus. Foreign reserves remain well above the international adequacy standard.

Inflation was maintained within the target range of 2.5%±1%, with the CPI inflation recorded at 2.51% year-on-year in June 2024. This stability was achieved through effective monetary policy measures and coordination between Bank Indonesia (BI) and the government to manage inflationary pressures, particularly in volatile food prices, which has been in a downward trend from its peak of 10.3% in March 2024 to 5.96% in June 2024. Core inflation remained low at 1.90%, and administered prices inflation was contained at 1.68%.

The authorities are more optimistic about growth compared to the staff's projections. They believe that a range of 4.7-5.5% in 2024 and 4.8-5.6% in 2025 is attainable, driven mainly by domestic demand. Solid growth in private consumption is expected in line with maintained public purchasing power and strong consumer confidence. Investment is projected to increase, particularly in building and non-building investment, given the ongoing government infrastructure projects and improving private investment. Improvement in exports is also expected in line with increasing global demand. Furthermore, they highlight the significant impact of digitalization and the increasing adoption of digital payments, which have driven economic activities and supported robust household consumption and investment.

There is optimism that medium-term growth will rise to 6-7%, driven by economic transformation through ambitious structural reforms aimed at achieving the 2045 Golden Indonesia Vision. This includes comprehensive efforts to enhance human capital, continue developing infrastructure, and improve the business and investment climate. Ongoing national strategic projects are expected to drive productivity and economic growth. Notable achievements include the enactment of the Omnibus Law, which has streamlined regulations and improved the business climate. There is a strong commitment to continuous reform, with plans for further enhancements in tax administration, infrastructure development, digitalization, and better integration into global value chains.

The authorities are confident that there is minimal downside risk from domestic policy actions, considering their consistent and strong track record in implementing a sound macroeconomic framework and maintaining

policy credibility. The new administration, which will take office in October 2024, is also committed to continuing structural reform agendas, ensuring the momentum towards sustainable economic growth and the realization of the 2045 vision. The commitment to structural reforms has also been strengthened by the OECD Accession Roadmap that was received in May 2024.

Fiscal Policy

Indonesia's fiscal policy is characterized by prudence, discipline, and a conservative approach in achieving strong, sustainable, and inclusive growth. The authorities believe that strong adherence to fiscal rules, backed by Law 17/2003, will ensure continued fiscal discipline, which has contributed to the country's macroeconomic stability and performance. Indonesia has been among the few countries whose fiscal position shows significant improvement in the aftermath of the pandemic. The fiscal deficit returned to below the 3% level in 2022, a year earlier than initially planned. The fiscal position in 2023 continued to strengthen, with a surplus in the primary balance and a much narrower fiscal deficit at 1.6% of GDP. In 2024, with continued moderation in commodity prices, the fiscal deficit may widen but remain within the statutory threshold. Fiscal policy has been focused not only on tackling cyclical challenges but also on addressing structural challenges. In the last decade, the government has prioritized developing infrastructure, investing in human capital, and continuing institutional reform to enhance long-term potential growth.

Fiscal policy conservatism, prudent and effective financing strategies, as well as automatic adjustment mechanisms, have provided adequate fiscal space in response to recent uncertainties and adverse shocks without compromising fiscal sustainability. New spending priorities by the incoming government, such as the "Nutritious Meal for Kids" program, have also been accommodated in the 2025 Macroeconomic and Fiscal Framework document. The 2025 fiscal deficit target of 2.3%-2.8% of GDP, outlined in the document, has incorporated this new program.

A range of tax measures has been implemented to broaden the tax base and enhance compliance. These measures are part of a broader strategy to increase fiscal space and support development spending. Boosting fiscal revenues is crucial for maintaining fiscal sustainability and accommodating development spending within the fiscal rule's guardrails. Efforts to enhance revenue administration include modernizing tax collection processes and improving taxpayer services. A comprehensive approach to tax reform, which includes both policy and administrative improvements, is expected to yield more substantial revenue gains. Continued fiscal reforms under the new administration are anticipated to further strengthen fiscal position.

Monetary Policy

BI's policy mix aims to maintain macroeconomic stability and support sustainable economic growth. This mix has proven effective in bringing inflation to its target range, maintaining Rupiah stability, ensuring financial system stability, and supporting economic recovery. BI will continue utilizing and calibrating the policy mix to respond to evolving economic conditions and global uncertainties, ensuring that the economy remains resilient and adaptive. The authorities intend to maintain a data-driven approach in monetary policy to safeguard stability.

The exchange rate policy is geared towards ensuring Rupiah stability and economic resilience. The policy aims to stabilize the Rupiah according to its fundamental value, ensuring market mechanisms function effectively, especially during periods of pressure. This is supported by foreign reserves that are well above standard sufficiency and ARA metrics. BI believes their exchange rate policy provides sufficient flexibility to respond to external shocks and maintain economic stability. However, BI cautions against suggestions to increase exchange rate flexibility in the current high-volatility conditions, as it could destabilize the economy and undermine investor confidence in the country's economic fundamentals and prospects. This approach also aligns with the staff assessment regarding the use of Foreign Exchange Intervention (FXI) to address sharp and inefficient rises in market premia. Additionally, it aligns with the assessment related to the Integrated Policy Framework (IPF)

application, where policy options comprising interest rate policy, monetary operation, and FXI result in an overall output path that is more optimal, particularly under the conditions faced by Indonesia.

BI strengthens the pro-market monetary operations strategy to enhance monetary policy effectiveness. BI also reinforces the interest rate structure of the Rupiah money market to maintain attractive yields and portfolio inflows, thereby bolstering Rupiah stability. These include the optimization of BI Rupiah Securities (SRBI), BI Forex Securities (SVBI), and BI Forex Sukuk (SUVBI) to support financial market deepening and attract capital inflow. Strengthening competitive government bond (SBN) term-repo and FX swap transaction strategies continue to be carried out to maintain adequate liquidity in the banking industry. BI views its existing framework as robust and effective in supporting financial market deepening and encouraging capital inflow, hence enhancing monetary policy effectiveness.

The Financial System Omnibus Law (FSOL), launched in 2023, strengthens the central bank's mandate, independence, and accountability. The FSOL provides adequate safeguards for BI's primary market purchases, limiting them to crisis conditions to ensure financial system stability. Implementing regulations will adhere to the principles of being targeted, temporary, and transparent to further ensure central bank independence. Regarding the unwinding of maturing bonds purchased during the pandemic, the authorities ensure that the process follows existing regulations and is conducted in a gradual and orderly manner to avoid market disruptions.

The export repatriation policy improves upon previous regulations, emphasizing stronger implementation and enhanced incentives. The regulation is designed to address structural issues by ensuring earnings from natural resource exports are available within the banking system to support economic resilience and growth. In this regard, the authorities disagree with the classification of the export repatriation regulation as an outflow capital flow measure (CFM). This policy is sensible and well-targeted, applied in a limited manner, specifically to 30% of FX earnings net of FX obligations for natural export proceeds valued more than USD250,000, thus minimizing disruptions to exporters' activities. The expansion of financial instruments and increased fiscal incentives make repatriating funds more attractive, contributing to the deepening of the domestic financial market. The measure will be periodically assessed and refined as needed to maximize its effectiveness.

Financial Sector Policies

Financial sector policies focus on maintaining stability, promoting financial inclusion, and supporting economic growth through various reforms and regulatory measures. The current policy mix, which includes robust regulatory frameworks, digital financial services, and targeted initiatives to enhance financial inclusion, aligns well with Indonesia's economic context and development goals. The authorities greatly value positive results from the FSAP assessment on BCP, FMI assessments, and systemic liquidity management frameworks, as well as the commendatory report on the payment system (BI-RTGS). The authorities have achieved significant advancements in strengthening the regulatory and supervisory framework of the banking sector. In addition, the authorities exhibit a strong adherence to FMI international principles. These achievements underscore the country's commitment as a G20/FSB member to leading by example in complying with international standards. There is also a commitment to continuous improvement and adaptation of financial sector policies in line with international standards and FSOL to ensure long-term stability and growth while addressing emerging challenges and opportunities.

Welcoming the FSAP's comprehensive assessment, the authorities highlighted the resilience of the financial system and the strength of financial policy frameworks. Systemic risks are well-contained through ongoing monitoring of the banking sector and regular stress tests. Monthly reporting of financial positions, including NPLs, ensures asset quality is accurately accounted for. Banks also maintain high loan-loss provisions to mitigate potential cliff effects in credit risk as forbearance measures were removed in March 2024. The sovereign-bank nexus increased during the pandemic but has decreased post-pandemic due to revived credit growth. Furthermore, the performance of Non-Financial Corporations (NFCs) is improving as indicated in the FSAP assessment which

shows median debt-to-equity ratios have decreased from 40 in 2020 to 30 in 2022, median return on assets have increased from 2.5 in 2020 to 3.5 in 2022 and median interest coverage ratios have increased from 2 in 2020 to 4 in 2022. Collaborative efforts between BI and the Financial Services Authority (OJK) to strengthen monitoring of cross-sectoral and cross-border exposures will ensure resilience as the financial system develops.

The ultimate objective of macroprudential policy is to address financial system stability. FSOL clarified and strengthened BI's macroprudential mandate, which focuses on a three-pronged strategy: maintaining financial resilience, managing balanced and sustainable intermediation, and supporting financial inclusion, tailored to Indonesia's needs. Balanced intermediation uses macroprudential policies as countercyclical tools to address systemic risks, ensuring stable credit growth and mitigating economic shocks. Maintaining financial resilience addresses risks from interconnectedness and contagion within the financial system. Supporting financial inclusion diversifies economic participation and reduces concentration risks by broadening access to financial services for underserved populations. These interlinked strategies enhance overall financial stability. Resilient banks manage procyclical tendencies better, providing stable access to financial services, which supports financial inclusion. In turn, financial inclusion contributes to bank resilience by diversifying customer bases and funding sources, especially during economic downturns. These strategies are aligned with domestic financial landscape and the context of emerging markets.

The macroprudential framework is in line with the concept of macroprudential policy to manage systemic risks in the financial sector as referred to by the IMF and other countries. The framework is developed based on potential systemic risks from the perspective of an emerging economy, incorporating the country's crisis experiences and lessons learned from the pandemic, particularly on the macro-financial linkage. It remains relevant as the macroprudential policy framework should be designed to address growing systemic risks in the country and best suit its institutional arrangement, which could further evolve and vary across countries while maintaining the ultimate objective of safeguarding financial stability. Nevertheless, authorities agreed to strengthen their public communication regarding the priority of the three-pronged strategy of the macroprudential policy framework, ensuring clear communication and understanding among stakeholders.

On crisis management, authorities acknowledged international best practices but emphasized that crisis management and resolution frameworks should also consider country-specific circumstances, crisis experiences, and legal regime differences. They now focus on strengthening the implementation of the FSOL to ensure credibility in policy development and governance in exercising authorities' mandates.

Significant strides have been made in ensuring the stability of the banking sector, reflected in robust capital and liquidity resilience and well-managed credit risks. The banking sector remains well-capitalized, with a CAR of 26.14% and gross NPLs at 2.34% in May 2024, demonstrating resilience to economic shocks and the ability to support the broader economy. Meanwhile, bank liquidity remains adequate, as reflected by a high ratio of liquid assets to third-party funds at 25.78% in May 2024. Financial inclusion has been another key focus, with policies aimed at expanding access to financial services for underserved populations. Initiatives such as the expansion of digital banking and electronic payment systems have significantly increased financial inclusion. As of May 2024, the value of digital banking transactions grew by 10.82% year-on-year, and electronic money transactions increased by 35.24%. The promotion of the Quick Response Code Indonesian Standard (QRIS) has seen impressive growth of 213.31%, further supporting financial inclusion and economic activity.

Efforts to improve the regulatory framework for NBFIs and fintech firms continue. The authorities agree with staff on the importance of these sectors in promoting financial inclusion and innovation, but a balanced regulatory approach is necessary to foster growth while ensuring stability. Recent measures to enhance the supervision and regulation of NBFIs and fintech firms aim to achieve this balance, promoting innovation while safeguarding the financial system.

Authorities have put in place a financial sector masterplan and roadmaps that emphasize the gradual approach to reform the financial sector. They believe the current pace of financial sector reforms is considered appropriate and aligns with the domestic macro-financial conditions given the need to balance stability with growth. Financial sector reforms implemented so far, including strengthening macroprudential regulations and promoting digital financial services, have already provided a solid foundation for stability and growth. The growth measures are designed to bolster resilience rather than conflict with the objective of financial stability. Consequently, a continued gradual approach to additional reforms will allow for a stable transition and avoid potential disruptions to the financial system. This preference also applies to recommendations for further consolidation in the banking sector. Furthermore, they aim to enhance the regulatory framework and promote good corporate governance and sound risk management practices across all banks.

On financial integrity, Indonesia became a FATF member in October 2023. The FATF Task Force found that the legal framework is strong. The authorities are working to further enhance its effectiveness based on the mutual evaluation report and have established an action plan.

Structural Reforms

To accomplish the 2045 Golden Indonesia Vision, transformational reforms are being implemented to enhance social protection, improve productivity, and foster new sources of growth. The first stage of the long-term development plan targets strengthening the foundations for an inclusive and sustainable economy. This includes improving the quality of education, health, social protection, and infrastructure. Key measures involve extending compulsory education, broadening secondary education delivery, implementing nutrition programs to reduce stunting, making new capital investments, developing new sea and air hubs, and bolstering digital and energy transition infrastructure. Governance transformation, including regulatory framework enhancement and business climate improvement, is also a priority.

Efforts to streamline regulations and enhance the business climate through the Omnibus Law have reduced regulatory barriers, improved the investment environment, and boosted economic competitiveness. Key milestones include the Omnibus Law on Job Creation, the Harmonized Tax Regulations Law, the Intergovernmental Fiscal Transfer Law, and the FSOL. These integrated reforms aim to build stronger economic fundamentals and enhance long-term growth potential. Implementing the Job Creation Law, which expedites business licensing, accelerates National Strategic Projects, and applies risk-based business analysis to encourage FDI, will enhance economic capacity through increased efficiency and productivity. The positive impact of structural reforms is reflected in the country's improved ranking in the 2024 IMD World Competitiveness Ranking which demonstrates significant strides in economic performance, government efficiency, and business productivity. This improvement highlights the effectiveness of the ongoing policy measures and the commitment to enhancing the overall business environment, which has been instrumental in attracting foreign investments and boosting the nation's competitive edge on a global scale. The FSOL is a crucial step in establishing a deep, innovative, efficient, inclusive, trusted, and stable financial sector.

A well-targeted Industrial Policy (IP), aimed at boosting participation in the global value chains (GVCs) has given positive results. IP is viewed as essential for maximizing the country's rich natural resources, not only for the current generation but also for future generations. This policy is also crucial for increasing value addition in the economy and attracting investment flows, especially amidst geopolitical fragmentation and market distortions. Ultimately, this policy will improve the balance of payments structure, strengthen the external position, and create a more resilient economy, calibrated over time according to market dynamics while prioritizing the benefits for achieving the national vision.

Indonesia has committed to achieving Net-Zero Emission by 2060 or sooner, as incorporated in the National Long-Term Development Plan for 2024-2025. In coordination with international partners, the 2024 Climate Investment and Policy Plan (CIPP) is planned to be released, showcasing different transition pathways for the off-

grid power plant network by the end of 2024. The overall green transition strategy focuses on sustainable energy development, green industry, sustainable land restoration, waste management, and coastal and marine environment preservation. Ongoing discussions include the potential implementation of a carbon tax, expanding the emission trading system and carbon exchange market, using local content requirements for renewables, and enhancing the targeting of energy subsidies, with these measures expected to be addressed by the incoming administration starting end-2024.