

# How to steer Indonesia's rising path toward its golden age

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Indonesia is rising.

With a population of 275 million, it is the fourth largest country in the world, has 17,000 islands and is known for its incredible natural diversity. A rising star in Southeast Asia,<sup>3</sup> Indonesia is often referred to as a “tiger” because of its young population, demographic dividend and tech-savvy citizens. A title it has earned in more ways than one.

In the past ten years alone, Indonesia has strengthened its growth engine through strengthened macro-fiscal and public sector management that has ensured greater economic stability and investment. These have in turn helped improve the quality of human capital and deliver more infrastructure. Indonesia made significant progress in achieving income convergence, reaching Upper-Middle Income Country (UMIC) status in 2023.<sup>4</sup> And Indonesia's growth has been inclusive, with the proportion of people living in poverty dropping from 12 percent in 2012 to 9.36 percent<sup>5</sup> in March 2023.

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<sup>3</sup> <https://www.forbes.com/sites/eladnatanson/2019/05/14/indonesia-the-new-tiger-of-southeast-asia/?sh=6bf1ee2476ce>

<sup>4</sup> <https://www.worldbank.org/en/country/indonesia/overview>

<sup>5</sup> <https://www.bps.go.id/en/pressrelease/2023/07/17/2016/indonesia-poverty-profile-in-march-2023.html>

## **Indonesia today.**

**Sound fiscal management spurs economic growth.** Indonesia has demonstrated exceptional fiscal stewardship, maintaining an impressively low average budget deficit of 2.3 percent of GDP since 2014 and achieving a historic low of 1.65 percent in 2023. This disciplined approach kept public debt at a manageable 39 percent of GDP, significantly below the UMICs average of over 50 percent<sup>6</sup>. As a result, Indonesia has attained an investment-grade rating for its sovereign credit. Landmark reforms in taxation, subsidies, and national services have yielded promising outcomes. For instance, the proportion of individual tax filers surged from 29 to 43 percent of the labor force during 2016-2021, driving steady increases in tax revenues. At the same time, districts' own resource revenues have more than doubled from around 8 to 15 percent of total district revenues between 2010 and 2020. Also, fuel subsidies have been reduced substantially from 2.3 percent of GDP in 2014 to just 0.6 percent in 2022.<sup>7</sup> The overall data and facts described in this opinion based on the World Development Indicators database of the World Bank.

**Bold legislative reforms drive efficiency and investment.** The landmark 2022 Law on Intergovernmental Fiscal Relations has bolstered the regulatory framework, enhancing equity and quality in subnational spending. Similarly, regulatory quality has seen improvements through the 2020 Jobs Creation Omnibus Law, which streamlined business startup processes and liberalized private investment, fostering economic growth. The introduction of the government's One Single Submission system has streamlined bureaucratic procedures, resulting in the registration of 5.9 million firms within just two years.<sup>8</sup>

**Government-led efforts are improving healthcare and health outcomes<sup>9</sup>.** The stunting rate has plummeted from 37.2 percent in 2018 to 21.6 percent in 2022, thanks to the government's flagship anti-stunting program, Investing in Nutrition and Early Years. National Health Insurance coverage has become nearly universal, reaching 91.8 percent in 2022 compared to 66.5 percent

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<sup>6</sup> World Development Indicators Database, WB fiscal space database.

<sup>7</sup> World Development Indicators Database, Op. Cit.

<sup>8</sup> World Governance Indicators.

<sup>9</sup> Indonesia using Rifaskes 2013, 2018 and National Nutrition Status Survey (SSGI) year 2019, 2021, 2022, Stunting data by income level using WHO-UNICEF-WB joint modeled estimates, Global Health Observatory Database, WHO (2023).

in 2016. In addition, out-of-pocket spending on health has decreased from 45 percent of total health expenditure in 2014 to 31.8 percent in 2020. During the pandemic, Indonesia not only rolled out free national COVID-19 vaccines programs, but also expanded testing labs from 49 to 1,100+ between March 2020 and June 2023, and more than doubled hospital capacity for isolation and critical care beds.

**Push for infrastructure development spurs road expansion, digital access, and better basic services with improved land use leading to reduced emissions over time<sup>10</sup>.** Indonesia has expanded its road network by over 30 percent since 2015, while digital access tripled in the same period. Ninety-nine percent of Indonesians have access to electricity, with 21 million new customers connected during 2015-2022. Initiatives like the Water Supply and Sanitation for Low-income Communities project have increased access to sustainable water and sanitation services in thousands of villages across the country. Similarly, the Indonesia National Slum Upgrading project has improved infrastructure and services for 8.6 million beneficiaries in urban areas. The Indonesia Infrastructure Financing Facility has notably leveraged its capital 22.5 times over to support 56 infrastructure projects. Land use policies implemented over the past decade are resulting in reduced emissions from land use, with strong decreases in deforestation now evident.

### **Indonesia tomorrow.**

Indonesia is rising from a strong foundation of economic stability and natural wealth, winged by the strength of its resilient people. As it navigates towards its high-income goal, the World Bank is proud to continue partnering with Indonesia.

To ensure a steady rise toward its ambitious goal, Indonesia cannot afford complacency but will need to continue to reform its economy. In particular, structural reforms that boost growth by removing bottlenecks to functioning of markets and create more and better jobs will be important. Our list of top five is the following:

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<sup>10</sup> World Development Indicators database.

*First*, Indonesia will need to maintain and further enhance its excellent track record of economic stability and performance, thanks to very credible economic team, as this is crucial for sustainable development. Political stability is a must and set back policy is not an option.

*Second*, Indonesia will need to further simplify laws and regulations to attract further investment and allow the private sector to flourish. While private investment was liberalized, there are still significant constraints to investment and private sector activity that would need to be addressed for economic growth to accelerate. While Indonesia's tariffs are consistent with international standards, non-tariff barriers have proliferated and constrained trade. Some of these measures impose significant costs, equivalent to up to a 30 percent tariff. As a result, Indonesia is today trading well below its neighboring countries and will fall further behind unless action is taken.

*Third*, despite commendable progress, Indonesia's infrastructure sector faces significant challenges. The roads in major cities are congested, while inter-urban and rural roads quality needs improvement. Telecommunications infrastructure lags neighboring countries. Indonesia will need to persist in its efforts for more and better infrastructure to serve its citizens.

*Fourth*, Indonesia, like all other middle-income countries, faces challenges in protecting the environment, conserving resources, and limiting emissions. By 2030, the energy sector is projected to become the largest contributor to GHG emissions. However, Indonesia has committed to achieving net-zero emissions in the power sector by 2050, underscoring its strong dedication to environmental sustainability. The establishment of the "Energy Transition Mechanism Country Platform" demonstrates Indonesia's intent to transition. To build on these positive steps, ongoing efforts to advance the energy transition agenda are imperative. These efforts include phasing down coal in timely manner, enhancing the revenue model for the state-owned electricity company, reallocating subsidies, bolstering the grid network, and fostering a more favorable investment climate for renewable energy.

Further ecosystem restoration and sustainable forest management techniques can also contribute to climate change mitigation and adaptation. Indonesia aims to reach net zero emissions in Forestry and Other Land Use (FOLU) by 2030, which will make a major contribution to Indonesia's enhanced NDC target.

Finally, Indonesia will need to maintain its momentum to improve access to basic public services, such as healthcare and education. Major initiatives to transform the health sector are already underway. A similar transformation would greatly benefit the education sector. Implemented well, these efforts will ensure that Indonesia's most valuable assets — its people — are prepared to steer Indonesia into its golden age.