PwC Indonesia Economic Update

First Quarter 2024

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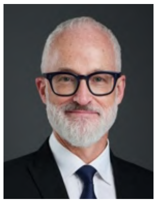
Foreword

As we delve into this Indonesian economic update in Q1 2024, we have observed mixed sentiments on both the global economy and Indonesia’s economy.

Given the anticipated economic instability, geopolitical tensions, and political transitions in several economies, global uncertainty is projected to persist in 2024. The ongoing conflict in the Middle East continues to raise concerns regarding potential disruptions to oil prices due to supply chain disturbances. Adding to the complexity, the upcoming US presidential election will potentially increase uncertainty on the global stage, introducing an element of unpredictability that could potentially reshape geopolitical dynamics and affect economic policies worldwide. In this context, we examine how these global events may influence Indonesia's economic landscape in the coming months.

Domestically, the Indonesian economy grew by 5.05% in 2023, amidst the weakening global economy. This performance, albeit slightly below the previous year's 5.31%, is noteworthy in the context of prevailing global economic challenges. Inflation experienced a significant deceleration, settling at 2.61%, a substantial decrease from 5.51% in the previous year, reflecting the efficacy of the country's monetary policies.

The PwC Indonesia Economic Update is a quarterly publication focusing on Indonesia’s recent economic developments. In this edition, we cover updates in Q1 2024. We hope this report brings significant value to readers and serves as a guide to those interested in Indonesia’s economy.



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Global Economic Update

1. Macroeconomic Update

The global economy is anticipated to decelerate in 2024, with a projected 2.9% growth in the Gross Domestic Product ("GDP") by Purchasing Power Parity ("PPP"), compared to the estimated 3.2% growth in 2023. This anticipated economic downturn is primarily attributed to advanced economies, which are implementing tighter monetary policies and reducing fiscal support. Consequently, a moderate decline is forecasted in advanced economies in 2024, while emerging and developing economies are expected to exhibit relatively more stable growth trajectories.

Table 1.1 Macroeconomic projection by country

Country	Share of 2023 World GDP PPP (%)	Real GDP Growth (%)				Changes in Consumer Price Index ("CPI") (%)				Interest Rate per Mar 24 (%)
		2023	2024	2025	2026-2028	2023	2024	2025	2026-2028	
Global (PPP)		2.8	2.5	2.5	2.5	4.5	3.4	2.7	2.7	
G7	30.0	1.8	1.5	1.5	1.6	4.6	2.6	2.1	2.1	
E7	38.1	5.1	4.4	4.1	4.0	4.1	4.5	3.6	3.7	
United States	15.5	2.5	2.2	1.6	1.9	4.1	2.7	2.2	2.3	5.3
China	18.9	5.2	4.7	4.3	4.1	0.2	1.1	1.7	2.2	3.5
Japan	3.7	1.9	0.8	1.0	0.7	3.3	2.5	1.9	1.6	0.1
United Kingdom	2.2	0.1	0.4	1.2	1.5	7.3	1.8	2.1	2.0	5.3
Eurozone	10.3	0.5	0.7	1.5	1.5	5.1	2.6	2.1	1.9	4.5
Russia	2.9	3.6	2.3	1.4	1.4	6.6	6.2	4.7	4.3	16.0
India	7.5	7.4	6.5	6.4	6.3	5.5	4.8	4.5	4.7	6.5
Indonesia	2.5	5.0	5.0	5.1	4.9	3.7	2.9	2.8	2.1	6.0
South Korea	1.7	1.4	2.2	2.2	2.1	3.6	2.4	2.0	1.9	3.5

Source: PwC Global Economy Watch (2024), various news articles
Note: Data for 2024 onwards are projections from various institutions and compiled by PwC.

Several countries are confronting crises in many forms that strain their economic performance. China faces its own set of challenges, notably a housing crisis characterised by a 6.5% decline in housing sales and a 9.6% reduction in real estate development during 2023. This crisis has been a significant contributor to China's economic downturn, given that real estate comprises approximately a quarter of the nation's economy. Previously, home-buying in China had been seen as a favourable investment instrument due to continuously rising house values, but this led to concerns about a housing bubble. Hence, the Government of China introduced regulations in 2020 to limit excessive borrowing by real estate developers. Consequently, developers now face challenges in repaying loans and completing pre-sold construction projects, which has led to the default of over fifty Chinese property firms since 2021, including two major market leaders. Therefore, the period since 2021 has seen a slowdown in home-buying and there is an expectation that this will further weaken over time. Notably, China's debt-to-GDP ratio in 2023 reached its highest recorded level at 288%.[1]

[1] Time Magazine, 2024, China's Economic Slump Is Here to Stay, https://time.com/6835935/china-debt-housing-bubble/.

Despite predictions of recession by various institutions, the United States (“US”) exhibited favourable economic performance in 2023. This was characterised by robust economic growth of 2.5%, supported by improvements in consumer sentiment and increases in real wages. Moreover, the nation witnessed an unprecedented level of private investment in manufacturing construction, marking the highest peak since 1958.[2] Additionally, the unemployment rate remained stable despite declining inflation, while supply chains showed signs of recovery. Nonetheless, the US is anticipated to experience relatively modest growth in 2024 of 2.2%, attributed to subdued growth in consumer and fiscal spending compared to 2023. These expectations arise from diminishing wage increases and a doubled fiscal deficit from 2023.

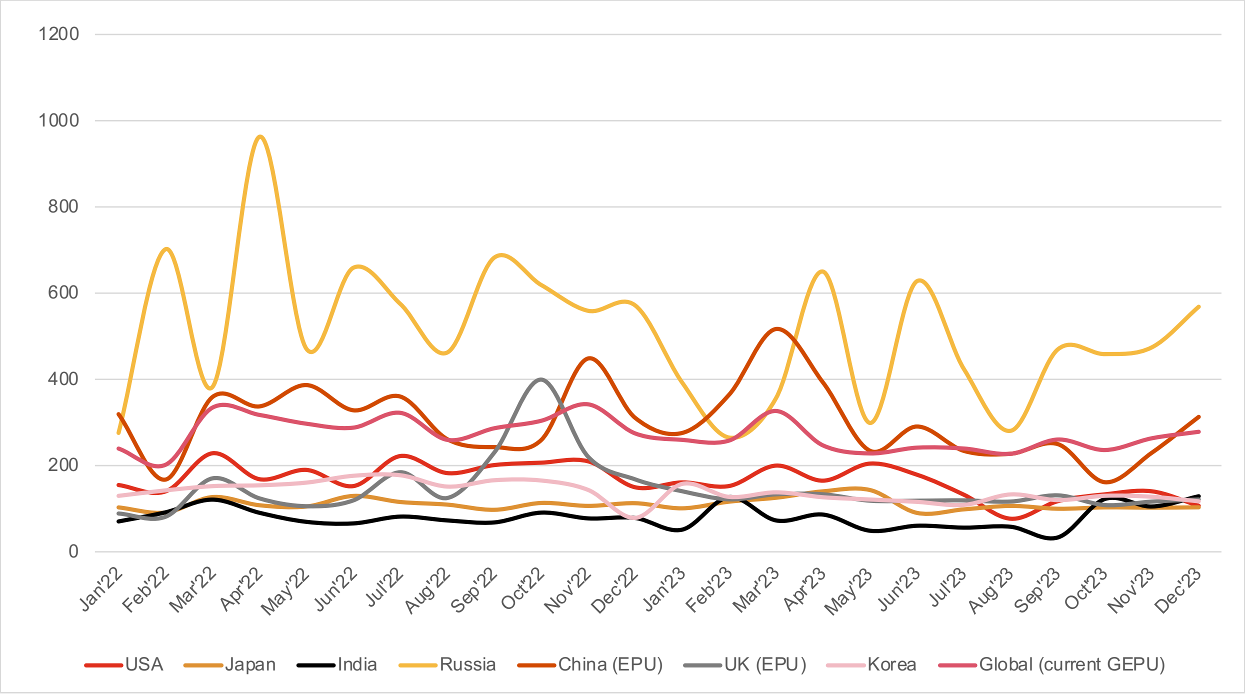
Meanwhile, the United Kingdom (“UK”) anticipates a marginal upturn in its GDP growth for 2024 estimated at 0.4%, attributable to its successful mitigation of inflationary pressures. Notably, the UK has managed to reduce its inflation rate from 7.3% in 2023 to 4% as of early March 2024. This achievement follows a sequence of persistent challenges, including the recovery from the COVID-19 pandemic, the escalation of energy and food costs stemming from Russia's invasion of Ukraine, and labour shortages that prompted wage hikes, all of which contributed to elevated inflation levels during 2023. In response to these circumstances, the Bank of England (“BoE”) continuously raised interest rates from 3.50% at the beginning of 2023 to 5.25% at the end of 2023 in an attempt to achieve its inflation rate target of 2%.[3] A similar initiative was also taken by the European Central Bank (“ECB”) given the similarity of the issues the European Union (“EU”) faces with those faced by the UK.

[2] The White House, 2023, Ten Charts That Explain the U.S. Economy in 2023, https://www.whitehouse.gov/cea/written-materials/2023/12/19/ten-charts-that-explain-the-u-s-economy-in-2023/
[3] Bank of England, 2024, Interest Rates and Bank rates, https://www.bankofengland.co.uk/monetary-policy/the-interest-rate-bank-rate

2. Uncertainty

Geopolitical tension among developed nations was prominent in 2023, amplifying uncertainties surrounding global economic growth. This occurred alongside the anticipated deceleration in economic growth through contracted trade volumes and high inflation across various developed economies, including China and the US, as well as instances of financial instability such as banking crises in the US and Europe.

Figure 2.1 Economic policy uncertainty index by country (2022–2023)



Source: Economic Policy Uncertainty (2024)

Given the anticipated economic instability, geopolitical tensions, and political transitions in several economies, global uncertainty is projected to persist in 2024. The ongoing conflict in the Middle East continues to raise concerns regarding potential disruptions to oil prices due to supply chain disturbances. Mid-October 2023 witnessed an increase of 4.2% to 4.3% in the global prices of the West Texas Intermediate ("WTI") and Brent Crude benchmarks following the conflict, which was reported as the biggest one-day gain since April 3 in 2023.[4] The prices have shown a generally declining trend since then, although a spike was observed during early April of 2024 due to tighter supply following production cuts from Organization of the Petroleum Exporting Countries ("OPEC") countries and higher demand from increased global industrial activities. Further escalation of the conflict poses a potential risk of further price hikes, although to date price rises have been moderate.

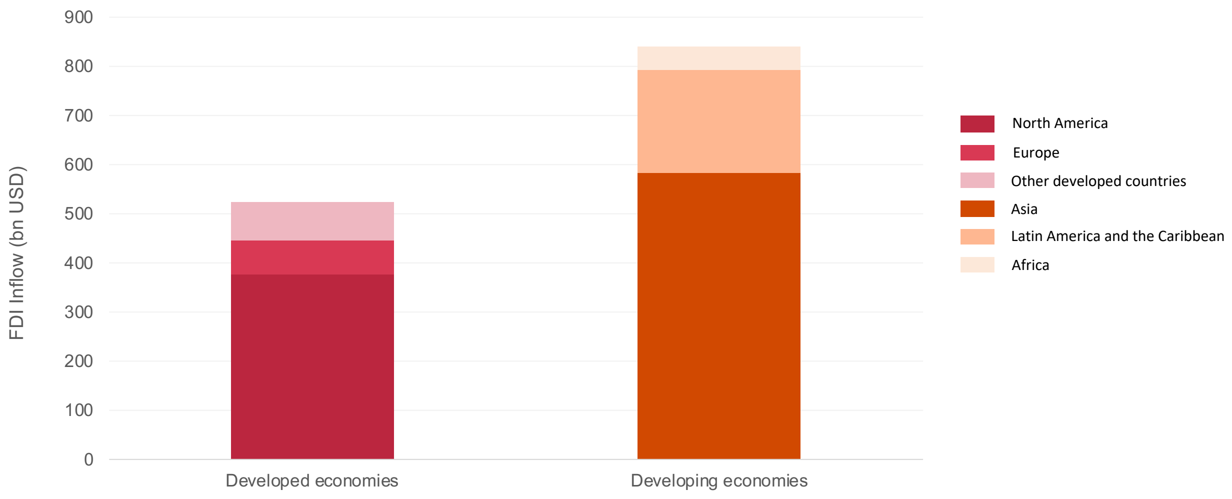
Furthermore, economic instability risks persist in developed economies in 2024, driven by anticipated declines in household savings, high interest rates, and sluggish labour markets, notably observed in the

[4] CNBC, 2024, Oil prices jump more than 4% in the wake of Hamas attack on Israel, https://www.cnbc.com/2023/10/09/brent-wti-prices-jump-after-hamas-attack-on-israel.html

US and Europe. Additionally, political transitions in several nations as they approach significant political events in 2024 such as the US presidential election, the India and UK general elections, the EU Parliament election, the Mexico presidential election and Indonesia's presidential transition add to the prevailing uncertainty.[5]

Consequently, given the substantial apprehensions and uncertain sentiments, the private sector and investors, particularly foreign entities, may adopt a cautious "wait-and-see" approach towards investing in both emerging and developed economies.

Figure 2.2 FDI flows by region (2023)



Source: United Nations Conference on Trade and Development (UNCTAD) (2024)

In 2023, the majority of foreign direct investment ("FDI") inflows continued to be directed towards developing economies, comprising 62% of global FDI. However, certain major developing Asian economies saw notable declines in FDI inflows, despite receiving the largest amount of FDI among developing economies. Asian nations remained preferred destinations for greenfield projects, such as parent companies establishing new operational facilities in foreign countries. The United Nations Conference on Trade and Development ("UNCTAD") reported a 16% decrease in FDI flows to ASEAN member countries in 2023.[6] Nevertheless, these nations remained attractive for manufacturing investments, with a significant 37% increase in greenfield project announcements possibly due to competitive labour cost, abundant labour supply, access to raw materials, government incentives on taxes and subsidies, and trade agreements with key markets such as the US and EU, among many other factors.

Many institutions projected that a decrease in inflation and borrowing costs in global major markets in 2024 would increase global FDI flow, following the increase in investment flow in some European countries during 2023. A decrease in inflation implies a stabilizing economy, which may increase confidence among customers and businesses, hence providing a positive outlook on investments.

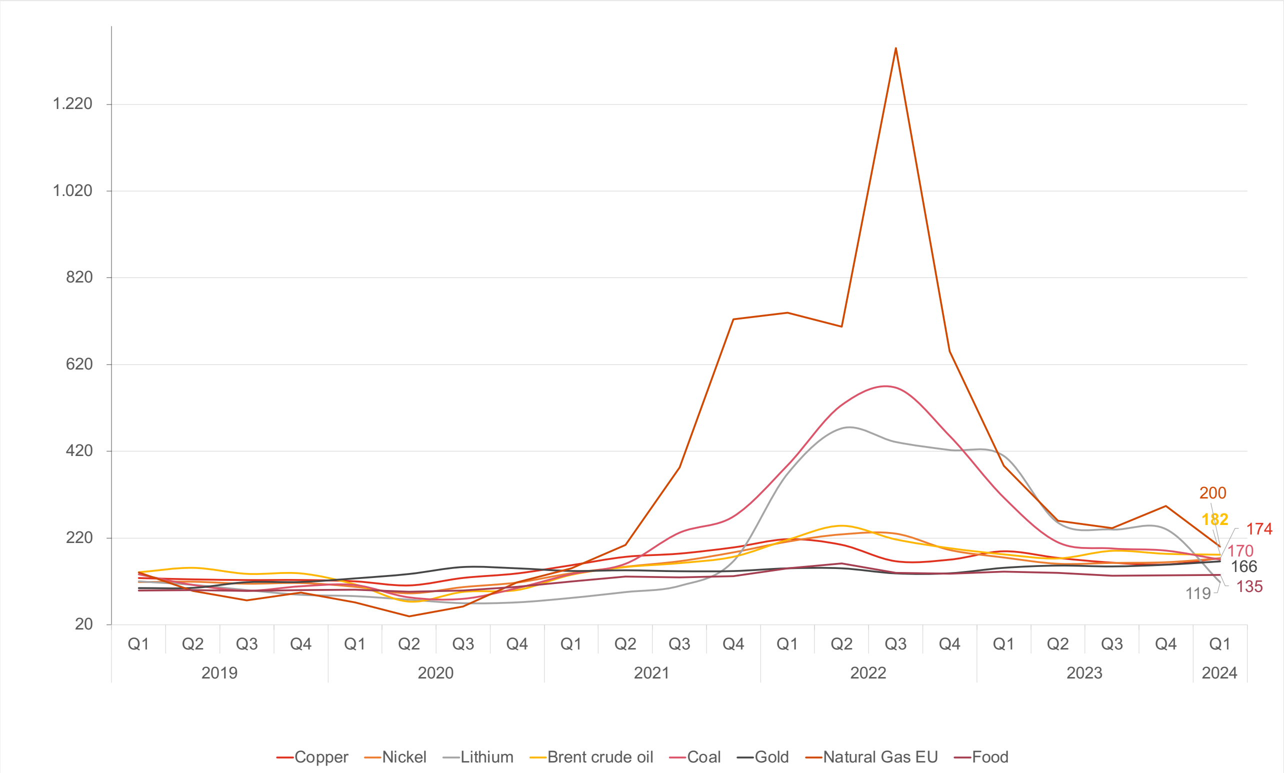
[5] World Economic Forum, 2024 is a record year for elections. Here's what you need to know, https://www.weforum.org/agenda/2023/12/2024-elections-around-world/
[6] UNCTAD, 2024, Foreign direct investment in developing economies fell 9% in 2023, https://unctad.org/news/foreign-direct-investment-developing-economies-fell-9-2023

Additionally, lower borrowing costs would increase the predicted return on investments due to lower costs on loans. Nonetheless, there is caution in light of notable risks, including geopolitical tensions, elevated debt levels across various nations, and the potential for further global economic fragmentation, all of which pose challenges to the overall investment environment.

3. Commodity Prices

The recent conflict in the Middle East has heightened geopolitical risks in commodity markets. While its impact on prices has been limited thus far, historical data indicates that past conflicts in the region have led to increased prices and market volatility. This suggests that if the conflict escalates or draws in more countries in the region, there could be significant disruptions in oil supply, depending on the duration and scale of the escalation.

Figure 3.1 Commodity price index by category (2019– Q1 2024)



Source: International Monetary Fund (IMF) (2024)

Since the latest Middle East conflict began, energy prices have increased although relatively moderately. The World Bank reported that European natural gas prices rose by a further 35% from approximately 31 to 42 Euro per megawatt hour ("MWh")[7] in October 2023 after a price increase due to labour strikes at Australian liquefied natural gas ("LNG") facilities in September 2023.[8] This further spike occurred due a range of other factors, including the closure of a gas field off the Israeli coast, an explosion at an interconnector in the Baltic Sea, and concerns about the Middle East conflict. Factors such as improved global activity and resilient consumption growth despite continued weakness in the real estate sector in China have also supported oil prices. Additionally, the EU has replaced lost

[7] The Brussels Times, 2023, 'The crisis is not over': European gas prices skyrocket 35% in one day, https://www.brusselstimes.com/638315/the-crisis-is-not-over-european-gas-prices-skyrocket-35-in-one-day
[8] World Bank, 2023, Commodity Markets Outlook October 2023, https://openknowledge.worldbank.org/server/api/core/bitstreams/44f54d51-6b06-4ac3-b886-38a46754229f/content

Russian pipeline gas with LNG imports and higher levels of piped gas from Norway and North Africa to avoid supply disruptions. Despite these adjustments, European natural gas prices remain significantly above their 2015–19 average, while coal prices have continued to decline due to improved supply and cleaner fuel substitution.

The World Bank forecasted a 3% decline in global commodity prices in 2024 on the assumption of no further geopolitical disruption.[9] A significant factor contributing to the potentially persistent weakness in commodity prices throughout 2024 is due to the global economic slowdown amid tight monetary policies. Additionally, subdued global trade in goods and vulnerabilities within China's heavily indebted property sector are anticipated to exert downward pressure on energy and industrial metal prices through 2024. However, initiatives aimed at expanding renewable energy infrastructure and electrical vehicles are anticipated to bolster critical mineral commodity prices in 2025 and beyond. Notably, investments in clean energy infrastructure on a global scale have witnessed a substantial rise. This surge is accelerating, leading to heightened demand for critical minerals such as copper, lithium, and nickel.

In 2023, nickel prices started high but experienced a nearly 50% decline during the year due to massive supply growth, notably from Indonesia, and subdued demand from China.[10] Nonetheless, the expanding electric vehicle (“EV”) sector is driving nickel consumption, particularly for batteries. Efforts are underway to find alternatives to nickel and cobalt, driven by environmental concerns, mining activities and cost considerations. While lithium-iron-phosphate batteries are gaining traction, especially in Asia, their limited range poses challenges in regions like North America.

The economic slowdown in China has also led to a declining trend in lithium prices and volatility in copper prices during 2023 and 2024 given China’s significant role in driving demand for lithium and copper.[11] Chinese lithium refining companies are responding by curtailing production. Disruptions in lithium supply and shifts in consumer electronics and EV trends could rapidly impact demand and supply dynamics. However, with the EV market poised for growth, demand for lithium is anticipated to exceed supply in the next few years. Similarly, copper prices are anticipated to surge in the next two years due to mining supply disruptions fueled by political and social unrest regarding the mines in South America and challenges in daily operational mining activities, among many other factors. The rise in prices would also be aggravated by heightened demand for renewable energy.

Meanwhile, food commodities indices dropped in 2023 as compared to the record-high in 2022, despite still being higher than the pre-COVID values. Among other reasons such as adverse climate conditions, the conflict between Ukraine and Russia as major exporters of cereals and vegetable oils resulted in disruptions to their export activities. The war has also affected transportation routes and logistics networks as Russia decided to end the Black Sea Grain Initiative in July 2023, which was previously intended to ensure safe navigation of grain and other food exports that are key to global food security.[12] Furthermore, sanctions imposed upon Russia have led to further pressure on food supply and prices.

[9] World Bank, 2024, Global Commodity Prices Level Off, Hurting Prospects for Lower Inflation, https://www.worldbank.org/en/news/press-release/2024/04/25/commodity-markets-outlook-april-2024-press-release

[10] Investing News Network, 2024, Nickel Price 2023 Year-End Review, https://investingnews.com/daily/resource-investing/base-metals-investing/nickel-investing/nickel-price-update/

[11] Carboncredits.com, 2024, Why Lithium Prices are Plunging and What to Expect, https://carboncredits.com/why-lithium-prices-are-plunging-and-what-to-expect/

[12] International Food Policy Research Institute, 2023, Russia terminates the Black Sea Grain Initiative: What’s next for Ukraine and the world?, https://www.ifpri.org/blog/russia-terminates-black-sea-grain-initiative-whats-next-ukraine-and-world

Nevertheless, 2023 saw a lowering of food commodity prices and a recovery in food security, which occurred due to increased export availability and subdued import demand for meat, improved global supply of cereals, as well as a slowdown in demand and improved weather conditions in Brazil for vegetable oils. However, the prices of several food commodities remained high. Dairy products, for instance, continued to have high prices due to rising demand from Western Europe as it approached the holiday season at the end of 2023.

Note: Food commodities comprise cereal, vegetable oils, meat, seafood, sugar, and other food (apples, bananas, legumes, fishmeal, groundnuts, milk, tomatoes).

Indonesia Economic Update

4. Key Highlights in Indonesia

In 2023, Indonesia showcased resilience and strategic adaptability amidst global economic uncertainties, achieving a GDP growth rate of 5.05%. This performance, albeit slightly below the previous year's 5.31%, is noteworthy in the context of prevailing global economic challenges. Inflation experienced a significant deceleration, settling at 2.61%, a substantial decrease from 5.51% in the previous year, reflecting the efficacy of the country's monetary policies. The manufacturing sector's Purchasing Manager Index ("PMI") also consistently exceeded the 50-point threshold throughout the year, indicating an expectation of sustained industrial expansion. Despite exchange rate fluctuations, the trajectory of Indonesia's economy points towards continued steady growth.

In 2024, Indonesia's economy is targeted to grow at 5.2%, as agreed by the Ministry of Finance and the House of Representatives, or *Dewan Perwakilan Rakyat* ("DPR"). This positive outlook is bolstered by Indonesia's improving appeal as an investment destination, underscored by a 101.3% achievement rate of investment targets in 2023 and stable assessments from international rating agencies. The new capital city (Ibu Kota Nusantara or "IKN") megaproject has attracted heightened interest from both domestic and international investors, reflecting confidence in Indonesia's economic trajectory, though the number of firm investment commitments is still limited.

Domestic consumption, a pivotal driver of Indonesia's economy with a 57% contribution to GDP in 2023, is expected to maintain its significant role in 2024. Government allocations for election-related expenses were set to increase to Rp 15.87 trillion from Rp 11.52 trillion in 2023, alongside projected private and public election spending totalling Rp 294.5 trillion, all of which is expected to catalyse economic activity. Furthermore, in 2024 salaries for civil servants were increased by 8%.[13] The salary increase has impacted approximately 3.7 million individuals who are classified as civil servants.[14] These factors could likely further increase domestic spending, reinforcing its contribution to GDP.

The political landscape has attained a measure of stability following the General Election Commission, or *Komisi Pemilihan Umum* ("KPU")'s confirmation of the victory of Prabowo Subianto in the presidential election. His commitment to continue many of outgoing President Joko Widodo's policies points to a predictable investment climate and policy stability. Such political stability, coupled with sustained increases in government expenditure including civil servant salaries, is anticipated to boost domestic consumption further.

However, the 2024 domestic outlook, while largely optimistic, necessitates caution in light of internal and external challenges. Potential disruptions in global supply chains, uncertainties in the world economy – especially concerning China's economic performance – and domestic political stability issues, notably the upcoming sub-national elections, including for Governor of Jakarta, could pose risks to Indonesia's economic aspirations. Additionally, the global economic landscape may influence Indonesia's growth potential. Despite these challenges, Indonesia's demonstrated resilience to global shocks and an ever more diversified economic base are expected to mitigate adverse impacts, providing a solid foundation for sustained growth.

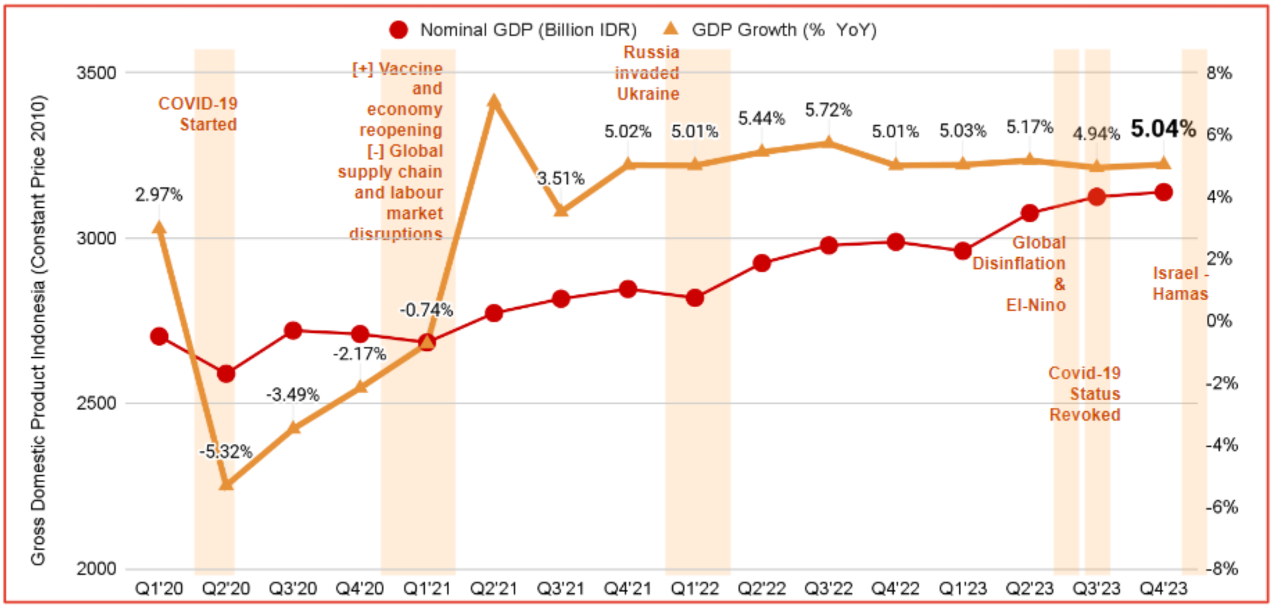
[13] A. Kristianus, 2023, Jakarta Globe, Government Allocates Rp 52 Trillion for Salary Hike of Civil Servants, https://jakartaglobe.id/business/government-allocates-rp-52-trillion-for-salary-hike-of-civil-servants
[14] Central Bureau of Statistics Indonesia (BPS), 2024, Number of Civil Servants by Working Period and Sex, https://www.bps.go.id/en/statistics-table/1/MTE3NyMx/jumlah-pegawai-negeri-sipil-menurut-masa-kerja-dan-jenis-kelamin--2004---2023.html

5. Macroeconomic Update

In summary, Indonesia's economic performance in 2023 has laid a foundation for positive economic growth in 2024. With a strategic emphasis on investment, infrastructure development, downstream processing of minerals and the maximisation of domestic consumption, sustained economic growth is expected, despite global economic uncertainties and domestic challenges.

5.1 Economic growth

Figure 5.1 Indonesia gross domestic product (2020–2023)



Source: Central Bureau of Statistics Indonesia (BPS) (2024)

Indonesia's economic growth in the fourth quarter of 2023 increased to 5.04% (YoY) compared to the previous quarter's rate of 4.94% (YoY). GDP in Q4 2023 is recorded at constant prices at IDR3,139.08 billion and at current prices at IDR5,302.54 billion. In the previous quarter, GDP was recorded at constant prices at IDR3,124.99 billion and at current prices at IDR5,294.98 billion. Even though on an annual basis, GDP growth in 2023, which reached 5.05% (YoY), was lower than the 2022 figure of 5.31% (YoY)[15]. The 2023 figure shows the resilience of the Indonesian economy and was in line with 2023 GDP projections.

In Q4 2023, household consumption and investment were the main contributors of growth. Household consumption, which is the largest component of Indonesia's GDP, grew 4.82% (YoY), partly due to an increase in the minimum wage and government social assistance. Even though there are still global economic challenges and high inflation, the increase in household consumption shows that the purchasing power of the Indonesian people is being maintained[16].

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[15] Central Bureau of Statistics Indonesia (BPS), 2024, Indonesia Economic in Q4 2023 press release, https://www.bps.go.id/id/pressrelease/2024/02/05/2379/ekonomi-indonesia-triwulan-iv-2023-tumbuh-5-04-persen--y-on-y-.html

[16] Republic of Indonesia Cabinet Secretariat, 2024, Dynamics of economic growth in 2023 and projections for 2024, https://setkab.go.id/dinamika-pertumbuhan-ekonomi-indonesia-2023-dan-proyeksi-tantangan-2024/#:~:text=Secara%20kumulatif%20sepanjang%202023%2C%20realisasi,domestik%20yang%20terdampak%20inflasi%20tinggi

Outlook 2024:

The government and DPR have agreed on the basic macro assumptions in the 2024 State Budget ("APBN"), including economic growth of 5.2%.[17] Bank Indonesia predicted economic growth to be in the range of 4.7-5.5%.[18] In Q1 2024, economic growth is recorded at 5.11% YoY.

On the domestic side, household consumption growth in Indonesia is projected to moderate slightly due to a slowdown of economic activity in labour-intensive industries such as manufacturing, agriculture, and trade. This trend is driven by anticipated lower demand from China, Indonesia's largest trading partner.

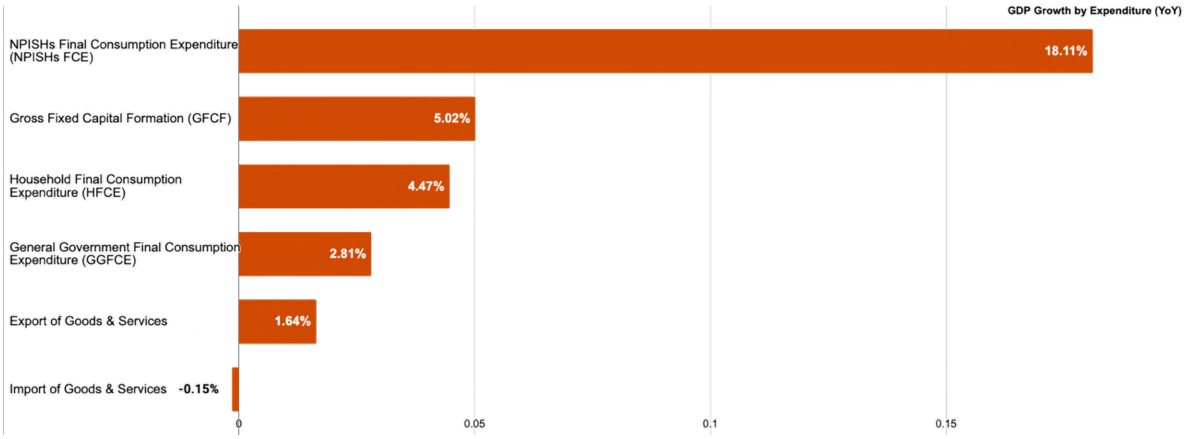
On the external side, the weakening of China's economic growth as Indonesia's main trading partner would have a significant impact on Indonesia's economic growth, especially in terms of both exports and imports. Another important factor is the continued downward trend in prices of Indonesia's mainstay primary commodities in line with the weakening global economy, which has also weakened the contribution of exports to GDP.

On the investment side, the Center of Reform on Economics ("CORE") predicted that investors would postpone strategic decisions until Q3 2024 due to finalisation of presidential election results (which have now completed all possible judicial review processes). However, investment to increase the production capacity of existing businesses, such as in the manufacturing and services sectors, is expected to be relatively unaffected by political uncertainty.

A number of factors are expected to support the Indonesian economy in 2024, such as the elections and the increasing investment in the development of National Strategic Projects, or *Proyek Strategis Nasional* ("PSN"), including the IKN[19]. The downstreaming programm in the mining sector, which has increased the added value of Indonesian exports, is predicted to continue to have a positive impact in the next few years, together with the Government's ambitious plans to leverage its critical minerals resources to develop Indonesia with a battery and EV hub for the region. Additionally, the market diversification strategy and decreased reliance on raw commodity exports are expected to enhance the value added of Indonesian exports and promote greater stability over the long term. The strategy is expected to contribute to stronger economic growth in the future.

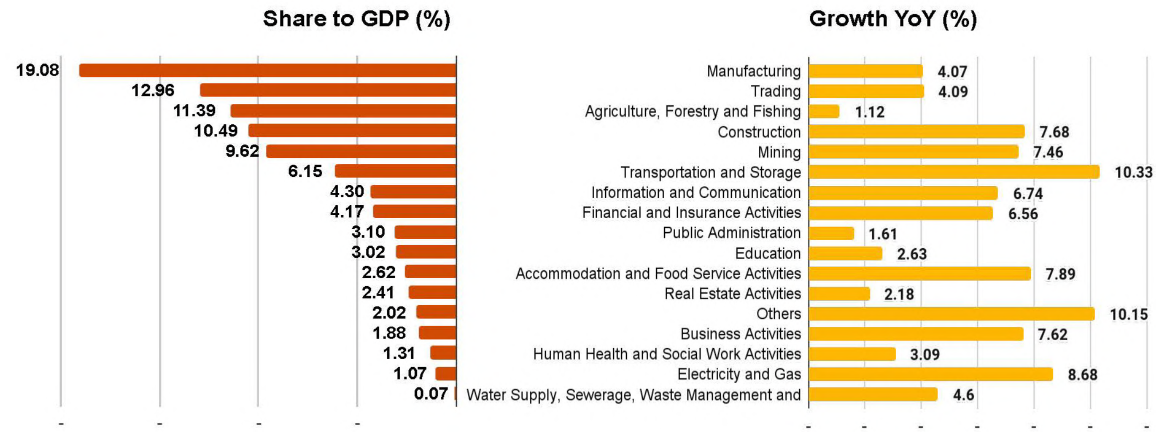
[17] Ministry of Finance, 2024, 2024 APBN Fiscal News, https://fiskal.kemenkeu.go.id/baca/2023/09/21/4463-sah-apbn-2024-resmi-meluncur
[18] Bank Indonesia, 2024, Economic growth Q4 2023 press release, https://www.bi.go.id/id/publikasi/ruang-media/news-release/Pages/sp_262324.aspx
[19] Tech in Asia, 2024, Indonesia Economic 2023 grew 5.05% yoy, https://id.techinasia.com/bps-pertumbuhan-ekonomi-indonesia-2023

Figure 5.2 GDP growth by expenditure Q4 2023 (YoY)



Source: Central Bureau of Statistics Indonesia (BPS) (2024)

Figure 5.3 GDP growth by industry and share to GDP Q4 2023



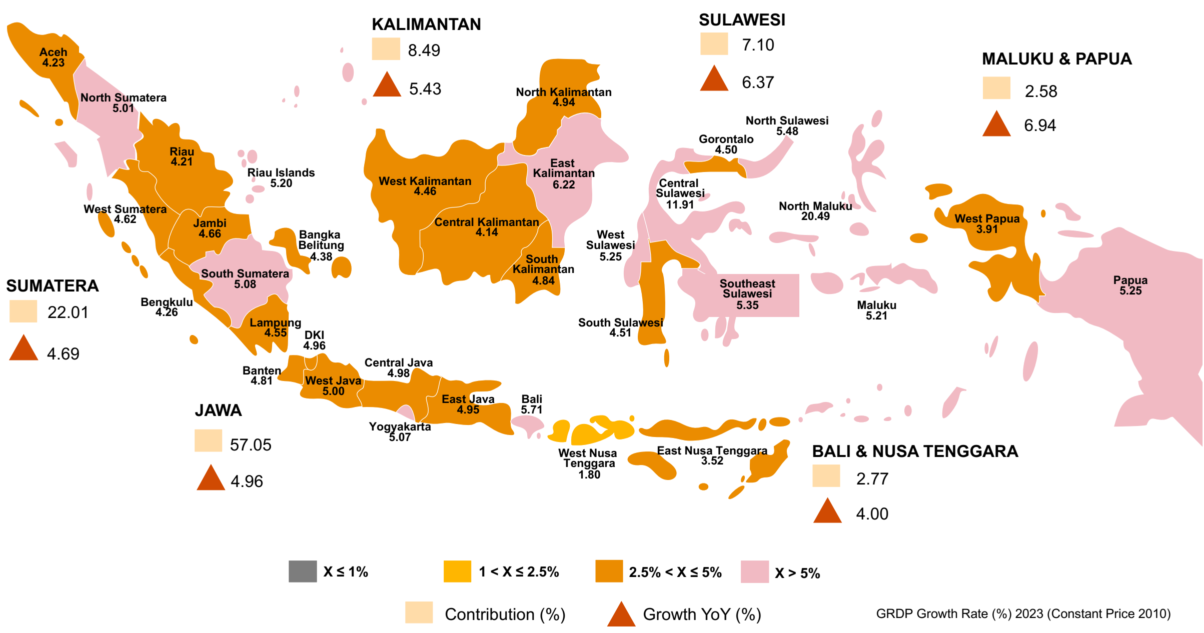
Source: Central Bureau of Statistics Indonesia (BPS) (2024)

Economic growth in the fourth quarter of 2023 was supported by positive achievements in all components of expenditure, except for imports, which contracted slightly, by -0.15% (YoY). Even though the household consumption component was the highest contributor to GDP, the component with the highest growth rate was the final consumption of non-profit institutions serving households (“NPISH”), which grew at 18.11% (YoY), due to increased election preparation activities. The component with the second-highest rate was investment, which grew by 5.02% (YoY), mainly supported by construction investment as infrastructure development continued and investment activity increased. Household consumption grew by 4.47% (YoY) in line with increased mobility, especially during the national religious holidays of Christmas and New Year, stable public purchasing power, and increasing consumer confidence. Government consumption increased by 2.81% (YoY) driven by goods spending and personnel spending. Meanwhile, exports grew by 1.64% (YoY) supported by demand from main trading partners, which continued to grow positively alongside the decline in prices of leading export commodities, as well as improving service exports in line with the increase in the number of foreign tourists.

Economic growth has been strong in all industries. The sector with the highest growth rate was transportation and warehousing at 10.33% (YoY), while the sector with the smallest growth rate was the public administration and defence; compulsory social security industry at 1.61% (YoY). The growth of transportation and warehousing sectors is driven by increased mobility of people and goods following recovery from the effect of the pandemic. Air transport grew by 28.96%, due to an increase in the number of air passengers on both domestic and international routes. Rail transport grew by 23.74% due to an increase in the number of passengers in line with the addition of long-distance train travel schedules and the opening of new DKI Jakarta Light Rapid Transit ("LRT") lines and the Jakarta-Bandung high-speed train.

The second-highest growth rate was the other services activities sector, which grew by 10.52% (YoY). In third position was the electricity and gas procurement sector, which grew at 8.68% (YoY) due to an increase in the state electricity company (PLN)'s electricity sales in 2023 due to an expansion strategy that requires PLN to extend its coverage throughout Indonesia. In fourth position was the accommodation and food and drink provision sector, which achieved growth of 7.89% (YoY), due to the recovery of the tourism and culinary sectors after the COVID-19 pandemic.

Figure 5.4 Gross regional domestic product growth and contribution in 2023



Source: Central Bureau of Statistics Indonesia (BPS) (2024); Simreg Bappenas (2024)
**) other services refer to recreational services, individual services, self-support household activities, and international agencies.*

Spatially, overall, in 2023, economic growth was positive in all provinces. Java Island is still the largest contributor to Indonesia economy at 57.05% with an average growth of 4.96% (YoY). This is because the structure of the Indonesian economy is dominated by a group of provinces on the island of Java, which is the most highly populated Island and the major industrial region.

The province with the highest growth was North Maluku at 20.49% (YoY). From the production side, the highest growth in Maluku occurred in the mining and quarrying sector at 49.07% and from the expenditure side, the highest growth was achieved by the export component at 28.67%.

The province with the second-highest growth rate was Central Sulawesi, which experienced growth of 11.91% (YoY). The production side was supported by the 25.53% YoY growth in the processing industry sector due to the continued increase in nickel processing smelters in this province; this was the sector with the highest growth rate. From the expenditure side, the goods and services export component experienced the highest growth of 18.92%, contributed from nickel, iron and steel commodities.

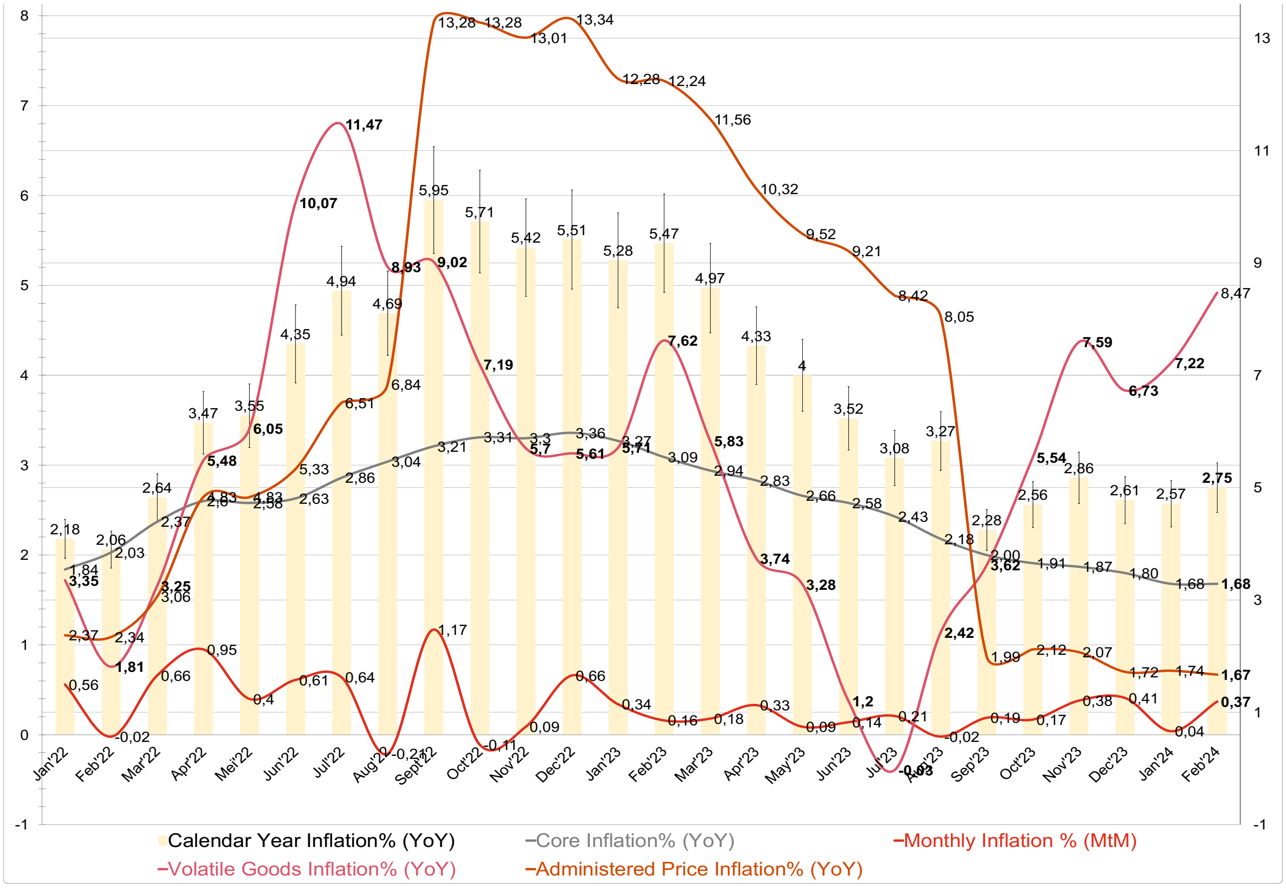
The province with the third-highest growth rate was East Kalimantan, which experienced growth of 6.22% (YoY). The production side was supported by the electricity and gas industry, which grew at 16.05% YoY and the construction industry at 15.82% YoY due to expenditure on IKN; this was the sector with the highest growth rate. In terms of expenditure, the government expenditure component experienced the highest growth of 36.40% YoY since most of the early-stage construction costs of IKN are government funded.

Downstreaming projects, especially those focusing on nickel and the development of the electric car industry from the downstream side, are primarily located in North Maluku and Central Sulawesi. These projects have created employment opportunities for 71,500 workers in Central Sulawesi and 45,600 workers in North Maluku. Despite this job growth, the unemployment rate in North Maluku rose to 4.31% in August 2023, up from 3.98% in 2022.

According to the Institute for Development of Economics and Finance (“INDEF”), there are other threats such as weak environmental protection, which could threaten other livelihoods such as agriculture and fisheries that support employment and price stability, which means it is necessary to pay attention to the quality of investment in these industries, not just the quantity, ensuring strong environmental and social safeguards are in place.

5.2 Inflation rate

Figure 5.5 Inflation in Indonesia



Source: BPS Statistics Press Release (Jan 2024); Bank Indonesia Inflation Press Release (Feb 2024)

Inflation in the fourth quarter of 2023 showed an increasing trend from October to November, then fell to 2.61% (YoY) in December. At the beginning of 2024, inflation fell to 2.57% (YoY), but increased in February to 2.75% (YoY). Ignoring the pandemic period from 2020 to the beginning of 2022, inflation in October 2023 was the lowest in the last 20 years[20]. Inflation in Q4 2023 was mainly contributed by the price of chillies, rice, onions, sugar, and gold whereas inflation in January and February 2024 was mainly contributed by the price of tomatoes, rice, onions, gold, cooking oil, and an increase in cigarette excise duty.

A global slowdown in inflation has been occurring since Q2 2023. This situation is mainly caused by two external factors, namely the decline in commodity prices and the excess capacity of Chinese industry resulting in falling prices and pressure on China's trading partners, especially Indonesia. The impact could be significant even though Indonesia has a much lighter public and private debt burden than developed countries. Slowing inflation could trigger a reverse "money illusion" effect where reduced

[20] Ministry of State Apparatus Utilisation and Bureaucratic Reform, 2024, Throughout 2023 Indonesia's inflation will be under control, https://www.menpan.go.id/site/berita-terkini/berita-daerah/sepanjang-2023-inflasi-indonesia-terkendali#:~:text=Capaian%20inflasi%202023%20tersebut%20tercatat,%2C51%20persen%20%28yoy%29.

commodity export revenues make economic actors reluctant to increase consumption and investment, which has the potential to make the expectation of an economic downturn a self-fulfilling prophecy.

The administered prices inflation in December 2023 fell to 1.72% (YoY), down from November's 2.07%, reflecting minimal adjustments in commodity prices set by the government. Air transportation rates filtered clove cigarettes and white clove cigarettes were the commodities contributing to consumer price index ("CPI") inflation in December 2023.

Inflation from volatile food decreased to 6.73% (YoY) in December 2023 compared to the previous month. The weather disturbances caused by El Nino led to suboptimal food production, especially in regard to rice and various types of chilli. This resulted in increased prices for rice and chillies, making both commodities the main contributors to inflation throughout 2023. The government intervened to control rice prices by importing to fill rice reserves, which were partly used to increase supply in areas experiencing high price increases[21].

Looking back at 2022, which recorded inflation of 5.5% (YoY), the inflation rate in 2023 was much lower and succeeded in beating World Bank and Bank Indonesia ("BI") projections for the year. Restrictions on fuel prices in September 2022 caused gasoline prices to rebound in 2023 by 30%[22]. Meanwhile, the Russia-Ukraine conflict, high energy prices, and imported inflation due to increases in global interest rates and the weaker Rupiah exchange rate were the primary causes of high inflation in 2022. However, in the last quarter of 2023, inflation was successfully controlled and maintained through monetary consistency and strong synergy between Bank Indonesia and the government.

Throughout 2023, Bank Indonesia increased the benchmark BI 7 days Repo rate (BI7DRR) twice, reaching 6.00%, to stabilise the Rupiah and manage inflation. Additionally, the year witnessed a decline in international crude oil prices, prompting adjustments to non-subsidised fuel prices by Pertamina. Most other subcategories posted slightly lower inflation readings compared to the previous year.

Outlook 2024:

The IMF expects Indonesia inflation to be around to 2.6% in 2024[23], aligning with Bank Indonesia's target of 2.5%±1%[24] and PwC Global's average inflation projection of 3.1%[25] in 2024. The expectation of lower inflation is attributed to lower commodity prices and a normalisation of domestic demand growth following the post-pandemic recovery. However, there is upward pressure on food prices due to the El Nino weather pattern, which may disrupt food production. The prolonged El Nino in late 2023 resulted in droughts, damaging crops and raising food prices until April 2024. Nevertheless, with global food and fuel prices stabilising, inflation is expected to gradually decrease from the second quarter of 2024. Furthermore, the impact of tightened monetary policies introduced in 2023 is anticipated to curb domestic demand, helping to reduce inflation.

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[21] Coordinating Ministry for Economic Affairs, 2024, Indonesia's 2023 inflation is under control, returning to target range and lowest in two decades, https://ekon.go.id/publikasi/detail/5578/inflasi-indonesia-2023-terkendali-kembali-pada-rentang-sasaran-dan-terendah-dalam-dua-dekade

[22] LPEM Universitas Indonesia, 2023, macroeconomics Analysis Series, https://lpem.org/inflasi-oktober-naik-karena-beras-seri-analisis-makro-bi-board-of-governor-meeting-2023/

[23] International Monetary Fund (IMF), 2024, 2024 projected consumer prices, https://www.imf.org/en/Countries/IDN

[24] Bank Indonesia, 2024, inflation press release, https://www.bi.go.id/id/publikasi/ruang-media/news-release/Pages/sp_264224.aspx#:~:text=Ke%20depan%2C%20Bank%20Indonesia%20meyakini,%2C20%25%20(mtm).

[25] PwC, 2024, Global economy watch projection, https://www.pwc.com/gx/en/research-insights/economy/global-economy-watch/projections.html

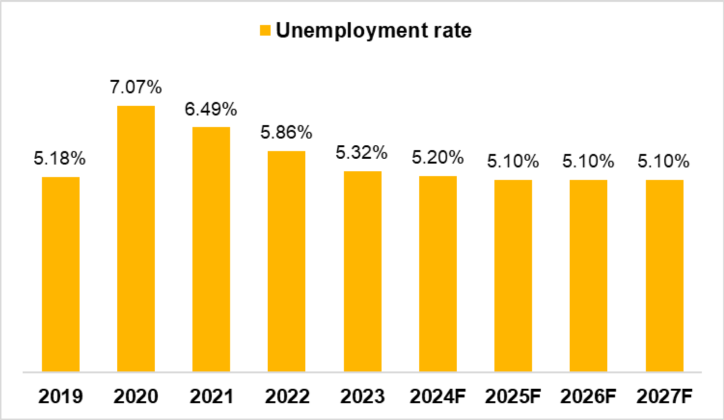
5.3 Employment

The employment rate in Indonesia as of February 2024 was 69.80%[26]. Based on a report from the Organization for Economic Co-operation and Development ("OECD"), the employment rate in Indonesia is one of the highest among the G20 economies[27]. Unemployment and labour under-utilisation in Indonesia are low when compared with other emerging economies. However, the labour market in Indonesia is highly segmented and the share of informal workers in total employment is higher than in other countries in the region. As of February 2024, the percentage of workers in the informal sector was higher than in the formal sector by 40.83%.

On the other hand, the Ministry of Investment, or *Badan Koordinasi Penanaman Modal* ("BKPM") has reported that investment realisation in 2023 surpassed the target, reaching 1,418.9 trillion (101.3% of the target)[28]. However, Indonesia's investment landscape still grapples with a significant challenge, namely the dominance of sectors that are less suited to absorbing the workforce. New investments tend to be in the capital-intensive and technology-driven industries, which absorb less labour. As a result, the government's goal of creating employment opportunities for 3 million individuals through investment remains unfulfilled.

Recognising the need for a transformative shift, the Indonesian Employers Association, or *Asosiasi Pengusaha Indonesia* ("APINDO") emphasises the importance of investment orientation towards sectors that directly impact the livelihoods of the masses, including the downstreaming of agriculture and the development of maritime industries, for instance. Furthermore, the government is also still striving to optimise investments in labour-intensive sectors, such as agriculture, tourism, construction, textile manufacturing and so on, with the aim of accommodating workers with lower skill levels.

Figure 5.6 Unemployment rate (2019-2027)



Source: Statistics Indonesia (2024), IMF (October 2023)

[26] Badan Pusat Statistik, 2024, Tingkat Pengangguran Terbuka (TPT) sebesar 4,82 persen dan Rata-rata upah buruh sebesar 3,04 juta rupiah per bulan, https://www.bps.go.id/id/pressrelease/2024/05/06/2372/tingkat-pengangguran-terbuka--tpt--sebesar-4-82-persen-dan-rata-rata-upah-buruh-sebesar-3-04-juta-rupiah-per-bulan.html.
[27] Organisation for Economic Cooperation and Development, 2023, Transitions to and from formal employment and income dynamics: Evidence from developing economies, https://www.oecd-ilibrary.org/docserver/bc186b3b-en.pdf?expires=1716545838&id=id&accname=guest&checksum=AB6A92238B02AD0C2D520D217F792A94.
[28] Kontan, 2023, Investasi Sektor Padat Modal Masih Mendominasi, Bahlil: Ini Jebakan Batman, https://nasional.kontan.co.id/news/investasi-sektor-padat-modal-masih-mendominasi-bahlil-ini-jebakan-batman

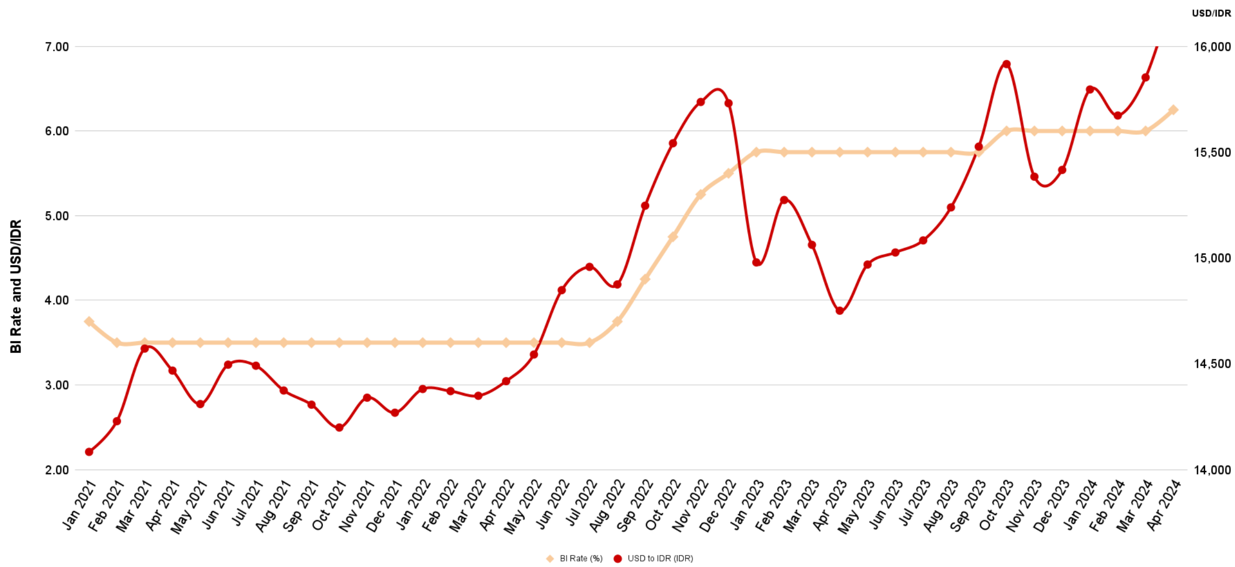
Recent data suggests a promising trend in Indonesia's employment rates, indicating a gradual recovery from Covid period. The unemployment rate in Indonesia decreased to 5.32% in 2023. This decline could be attributed to several factors, including the country's efforts to revive economic growth and the implementation of targeted policies to support job creation. However, this figure remains slightly higher than the pre-pandemic rate of 5.18% in 2019.

The IMF forecasted that the unemployment rate in Indonesia would reach 5.20% in 2024 and then stabilise at 5.10% from 2025 to 2027[29].

[29] International Monetary Fund, 2023, World Economic Outlook Database, https://www.imf.org/en/Publications/WEO/weo-database/2023/October/

6. Monetary and Financial System

Figure 6.1 BI rate and currency USD to IDR (2021-Feb 2024)



Source: Bank Indonesia middle rate (Feb 2024); Bank Indonesia BI rate (Feb 2024)

The USD exchange rate against the Rupiah (IDR) continues to show an upward trend. The Bank Indonesia interest rate in Q4 2023 increased by 0.25 basis points compared to the previous quarter and was maintained at 6.0% in January until March 2024, then increased in April 2024 to 6.25% in line with slowing global economic market uncertainty.

IDR's weakest position to USD throughout 2023 was IDR15,916/USD in October 2023 and IDR16,249/USD in April 2024, which was the weakest figure in the last 3.5 years, while the strongest position was IDR14,751/USD in April 2023.[30] The hawkish attitude of the United States Central Bank (the Fed) in tightening monetary policy by raising interest rates to tame inflation is one of the causes of the depreciation of the Rupiah.

There are many in the market who believe that the Fed will not raise interest rates further and will even start lowering interest rates in 2024. However, banks and central governments have largely maintained their rhetoric of higher long-term rates. Analysts from Cresset Capital via Reuters said that the Fed Chairman's statement shows that the US economy is strong enough to grant the Fed more flexibility to hold interest rates at high levels. Even though monetary policy interest rates, including the Federal Funds Rate ("FFR"), are predicted to have reached their peak, FFR could remain high for a long time (higher for longer)[31].

[30] Bank Indonesia, 2024, Middle Rates of Several Major Currencies Against the Rupiah at Bank Indonesia, https://www.bi.go.id/id/statistik/ekonomi-keuangan/seki/default.aspx#headingFour
[31] CNBC Indonesia, 2024, Wait for the Results of the Fed Meeting, https://www.cnbcindonesia.com/research/20240221063321-128-516204/tunggu-hasil-rapat-the-fed-harga-emas-malah-lari-kencang

Data on US consumer prices and producer prices that were higher than expected at the end of April reduced hopes for an interest rate cut in 2024. The President of the Federal Reserve Bank of Atlanta, Raphael Bostic, said interest rates likely won't be lowered until the fourth quarter of this year.

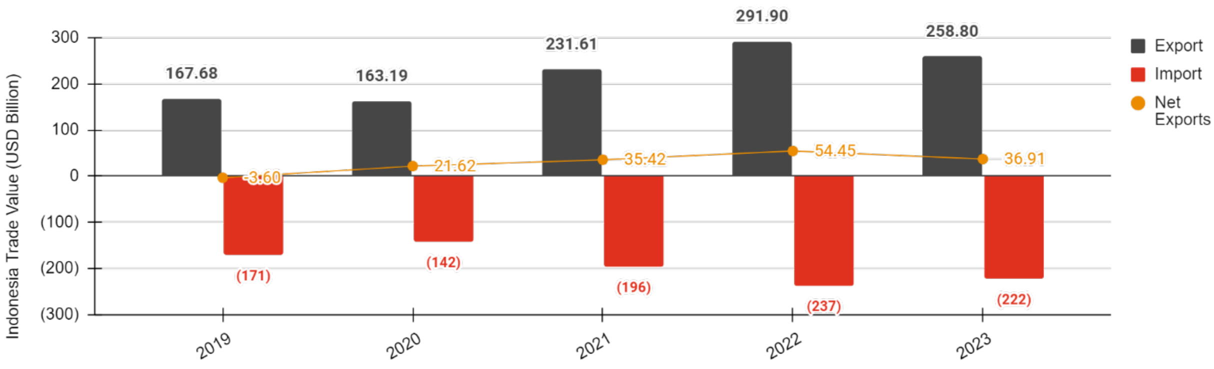
Throughout 2023, Bank Indonesia optimised pro-market monetary instruments such as Bank Indonesia Rupiah Securities or *Sekuritas Rupiah Bank Indonesia* (“SRBI”), Bank Indonesia Foreign Currency Securities or *Sekuritas Valuta Asing Bank Indonesia* (“SVBI”), and Bank Indonesia Foreign Exchange Sharia Bonds or *Sukuk Valuta Asing Bank Indonesia* (“SUVBI”). It was aimed to strengthen efforts to deepen the money market and support efforts to attract portfolio inflows, by utilising Indonesia Government Bonds, or *Surat Berharga Negara* (“SBN”) and foreign currency letter assets owned by Bank Indonesia. These various instrument innovations were expected to support pro-market monetary operation strategies and attract capital inflows to strengthen the external resilience of the Indonesian economy and protect it from the impact of global spillovers[32].

[32] Bank Indonesia, 2024, Indonesia Economic Report 2023, https://www.bi.go.id/id/publikasi/laporan/Documents/LPI_2023.pdf

7. Trade

Indonesian trade: At a glance

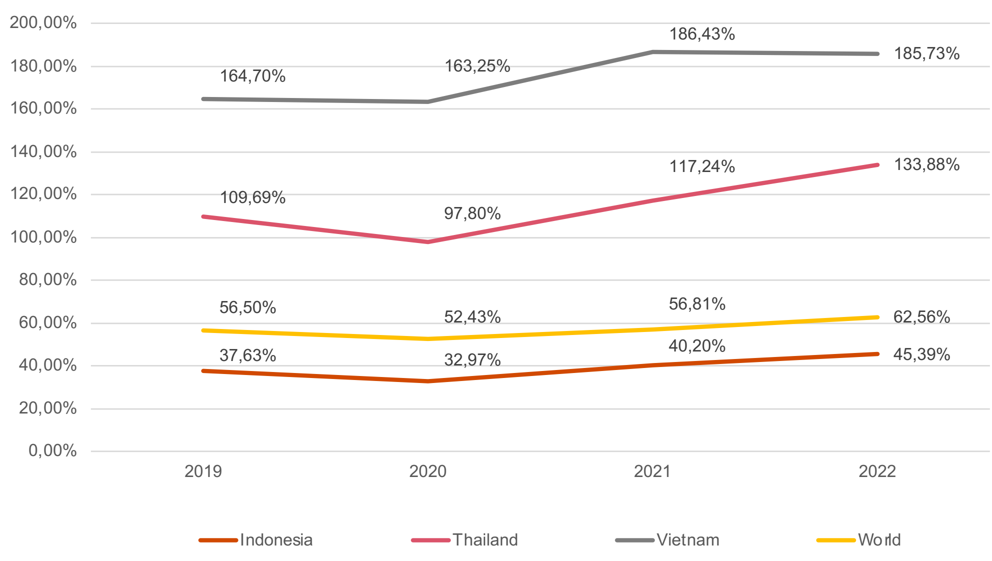
Figure 7.1 Indonesia trade value, export-import (2019-2023)



Sources: Central Bureau of Statistics Indonesia (BPS) (2024)

In 2023, Indonesia recorded a positive trade surplus of USD 36.91 billion, marking the fourth consecutive year of maintaining such a surplus. However, this was a 32.22% (YoY) reduction from USD 54.45 billion, with the decline in exports exceeding the simultaneous decrease in imports. Despite the decrease in trade surplus value, the volume of exports actually increased from 646.67 million tonnes in 2022 to 701.97 million tonnes in 2023. An increase in export volume occurring with a decrease in export value suggests a decrease in the selling prices of certain exported goods, which will be explored later in this section.

Figure 7.2 Trade to GDP ratio compared to other countries (2019-2022)



Sources: World Bank (2024)

The trade-to-GDP ratio, as a percentage, signifies the relative significance of international trade in a country's economy by dividing the combined value of imports and exports by the gross domestic product over a specific period. According to the World Bank, in 2022 Indonesia recorded a trade-to-GDP ratio of 45%. This ratio has steadily increased in recent years, improving from 40% in 2021. However, it remains below the world average of 63%, with benchmarked ASEAN countries such as Thailand and Vietnam showing significantly higher ratios (134% and 186%, respectively). Thailand, with a notably higher GDP per capita, and Vietnam, which is experiencing faster economic growth (8% in 2021), highlight the importance of international trade as a contributor to economic growth and development. Indonesia's openness to trade is increasing, yet there is a need for further improvement to unlock its full potential.

Figure 7.3 Indonesia’s top 5 trade partners (2023)

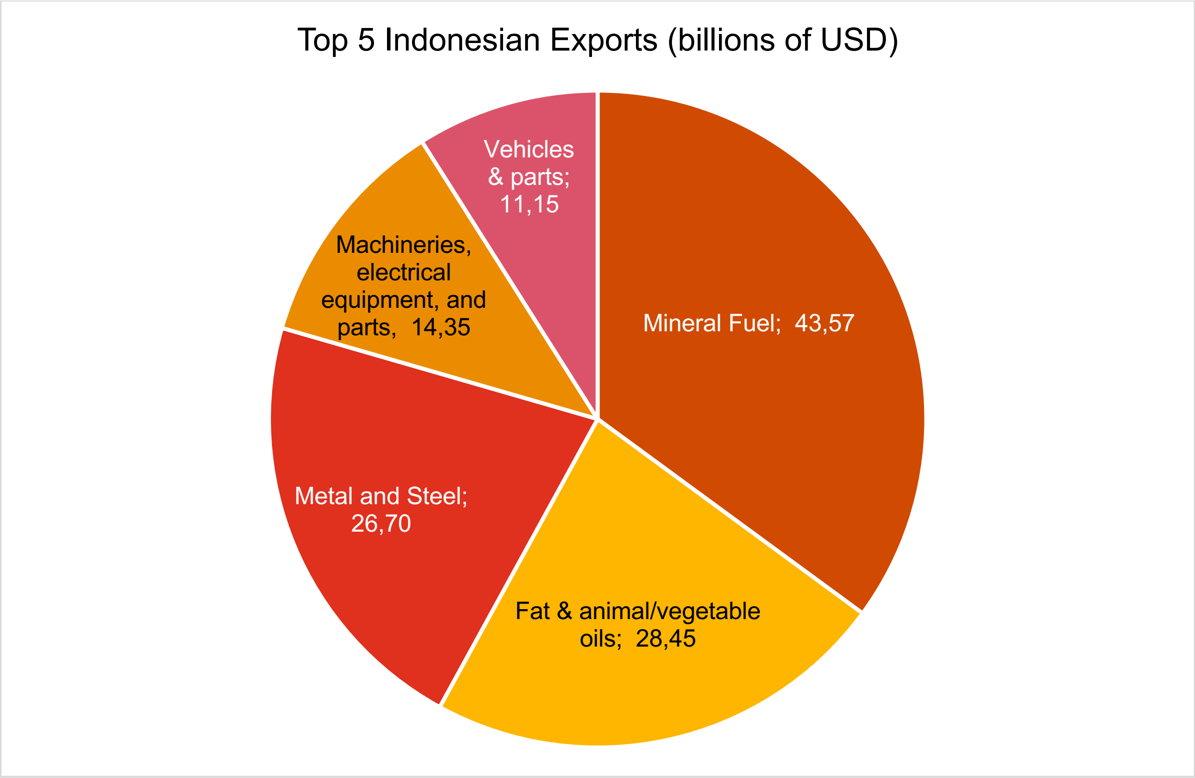
Value of exports from Indonesia				
China $64.94B (-1.4%)	USA $23.25B (-17.5%)	Japan $20.79B (-16.4%)	India $20.29B (-13.2%)	Malaysia $12.46B (-19.2%)

Value of imports to Indonesia				
China $62.09B (-1.0%)	Japan $16.52B (-3.8%)	USA $11.28B (-2.8%)	South Korea $10.53B (-10.2%)	Thailand $10.25B (-6.7%)

Sources: Central Bureau of Statistics Indonesia (BPS) (2024)

China stands as Indonesia’s most significant trade partner, serving as both the largest export destination and import supplier. In 2023, Indonesia exported USD 65.94 billion worth of goods to China, with imports slightly lower at USD 62.18 billion. Other top export destinations include the USA (USD 23.25 billion), Japan (USD 20.79 billion), India (USD 20.29 billion), and Malaysia (USD 12.46 billion). The increased reliance on China as a partner, with Indonesia exporting nearly three times as much compared to the USA, poses challenges. The unfolding property and demographic crises in China and Japan respectively could possibly affect demand for Indonesian exports, and this has culminated in a more pessimistic trade outlook for these key export destinations. Indonesian trade currently shows signs of slight decline, influenced by both global trends and unique domestic factors.

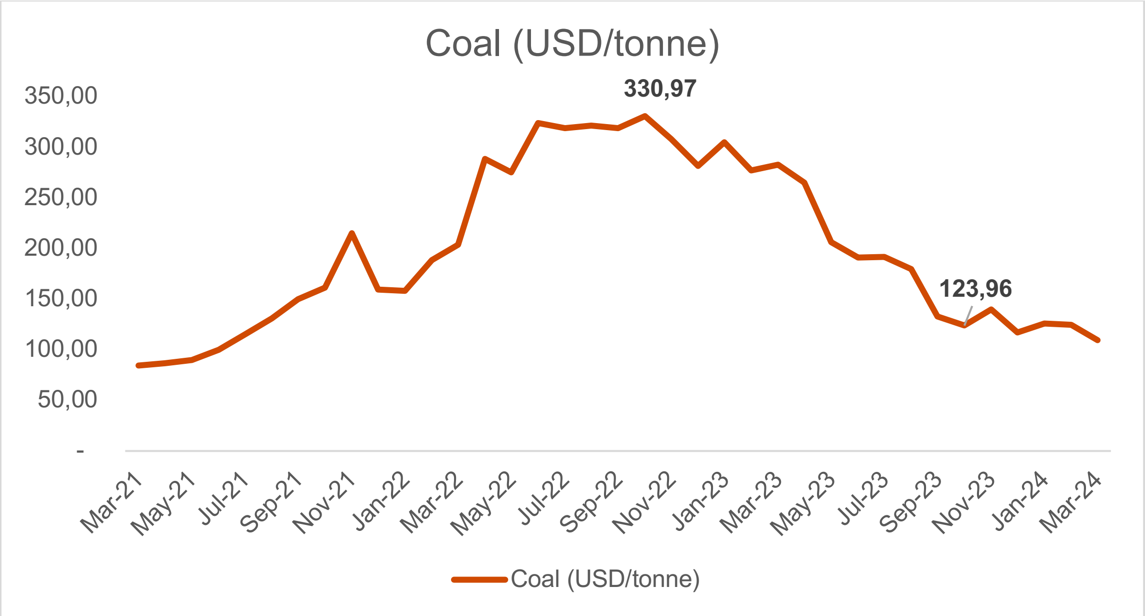
Figure 7.4 Indonesia top 5 exports by category (2023)



Sources: Central Bureau of Statistics Indonesia (BPS) (2024)

The primary cause of Indonesia's declining trade performance lies in its dependence on commodities. Mineral fuel exports, primarily coal, amounted to USD 43.6 billion in 2023, comprising 16.8% of total exports and representing Indonesia's most valuable export category. The "Fat & Animal/Vegetable Oils" category, which is mainly made up of Palm Oil, ranks as the second most valuable export, with a Free on Board ("FOB") value of USD 28.45 billion. Manufacturing-based exports, such as vehicles and machinery, also contribute but remain overshadowed by commodity-based industries. While commodities such as coal and palm oil are an important source of revenue and foreign exchange especially in periods of high commodity prices, they are also exposed to significant price volatility.

Figure 7.5 Reference Prices of Coal (March 2021- 2024)



Sources: Ministry of Energy and Mineral Resources (2024)

Table 7.1 Coal exports by destination (2019-2023)

	2019	2020	2021	2022	2023
Volume exported by destination (thousands of tonnes)					
India	121,693	98,243	70,779	110,155	108,932
China	65,671	62,493	108,487	69,685	81,683
Japan	28,436	26,965	22,978	26,392	25,278
South Korea	29,550	24,832	21,011	25,823	25,284
FOB value exported by destination (millions USD)					
India	4,836	3,391	4,078	10,595	7,256
China	3,143	2,652	9,143	7,795	6,975
Japan	2,333	1,695	25,481	7,174	4,761
South Korea	1,407	1,042	1,423	2,847	2,235

Sources: Central Bureau of Statistics Indonesia (BPS) (2024)

Indonesia's most important export, coal, has experienced high price volatility, with global prices falling from an all-time high of $331 USD/tonne in 2022 to $124 USD/tonne in 2023, marking a 62% decrease in price. This decline corresponded to a 38.6% (YoY) decrease in the total value of all mineral fuel exports. Consequently, the largest five flows of Indonesian coal exports all decreased in value from the previous year, with the value of exports to the largest recipient, India, in particular falling 46%. On the other hand, volume exported has not significantly decreased for these recipients, and exported coal volume has even increased to China. The fall in global coal prices significantly impacted Indonesia's overall export values, emphasising the need for diversification away from commodity reliance.

Under the Jokowi administration, the government has made concerted efforts to industrialise away from the raw extraction and sale of commodities through an emphasis on downstreaming industrial activities, or "*hilirisasi*" in Indonesian. The policy involves putting more of an emphasis on more advanced products and stages of the industrial value chain. Traditionally, Indonesia has played more of an upstream role in the industrial value chain, focusing on the exports of raw minerals and natural resources. While Indonesia's abundance of natural resource commodities has historically been a crucial component of Indonesian economic growth and development, the price volatility of such commodities exposes the commodity-dependent Indonesia economy to substantial risk. To mitigate such risk, government policy has been focused on the development of downstream industrial activities that create more added value, that are an important source of higher-quality employment, and that are most importantly less exposed to changes in global prices. In 2020, the Government banned all exports of raw nickel ore, a move which at the time drew controversy and dispute from the World Trade Organization ("WTO") due to Indonesia's role as the world's largest exporter of raw nickel.

Table 7.2 Indonesian exports of nickel products (2019-2023)

Sources: Central Bureau of Statistics Indonesia (BPS) (2024), and PwC Analysis

The table demonstrates the overall success of the policy. The 2020 ban on raw nickel exports effectively eliminated them from 2020 onwards. Refined nickel products such as ferro alloy nickel experienced substantial increases as smelting activities relocated domestically. Smelted and refined nickel products, like ferro alloy nickel, achieved an annual growth rate of 48% from 2020 to 2023 post-nickel ban, reaching an exported value of $15.3 billion in 2023. Similarly, the export of manufactured stainless-steel products, which rely on nickel as a key component, also saw significant growth with a 22% compound annual growth rate ("CAGR") from 2019 to 2023.

The success of the policy prompted the government to enact a similar ban on raw bauxite (aluminum) ore in June 2023 and consider a ban on raw copper, aiming for downstreaming success similar to that seen in the nickel industry and coinciding with the construction of multiple smelters in East Java and West Nusa Tenggara.[33] Therefore, current downstreaming policies could serve as a new source of growth for Indonesian trade and exports. While refined and manufactured nickel products have benefited significantly from the ban on raw nickel, the ultimate objective is to establish Indonesia as a major producer and exporter of nickel-reliant electric vehicles (EV). This initiative is slated to commence in 2024 with the establishment of numerous major EV players in the industry.[34] These refined and smelted nickel products will serve as inputs for Indonesia's future EV industry, enabling Indonesian EV products to benefit from economies of scale, driving down prices and providing them with a competitive edge against other EV manufacturers. Another benefit of this downstreaming policy will pertain to government tax revenues, which have continued to increase, as will be explored in a further section.[35] A significant portion of the increase in taxation revenue has been contributed by the manufacturing industry, which has enjoyed the greatest benefits from downstreaming. This has enabled the government to increase its ability to fund priority programmes such as the *Badan Penyelenggara Jaminan Sosial Kesehatan* (BPJS), or the Social Health Insurance Administration Body.

However, several implications have arisen from this policy. Firstly, the strategy is seen as trade protectionism, potentially conflicting with Indonesia's obligations to the WTO, and Indonesia may face retaliatory trade policies from other countries in the long term. Moreover, restrictive policies such as export bans must be complemented by supportive measures such as subsidies and incentives for targeted downstream industries to effectively achieve the government's objectives in developing these industries. While in theory "invisible hand" free-market dynamics would eventually lead to the increase of players in more advanced downstream industries due to export bans in upstream industries, in practice barriers such as a lack of technical capacity, financial capacity, and red tape could impede growth in these targeted industries. For this reason, increased government intervention would be required as a "helping hand" to promote development more effectively in downstream industries and this would require additional government expenditure.

Furthermore, there has been criticism regarding this policy regarding the potential overall benefits for the Indonesian economy. Although smelted nickel and mineral products do have more added value than raw ore, they are not high-tech products, rather very basic manufactured products and are still in essence close in their form to commodities that depend heavily on global commodity prices. EV industries in Indonesia are not yet fully developed, and smelted products are usually purposed to be exported as soon as they are smelted, while growth in other dependent manufacturing industries that would use smelted products as inputs has not yet been optimal. The job creation effect from this policy has also not had as much of a positive effect as was previously expected, as unemployment is still higher than pre-pandemic levels and has even risen in provinces such as Central Sulawesi and Maluku, in which major downstream projects are based.

Additionally, concerns have been raised about Indonesia's potential domestic nickel ore deficit. The government's delay in approving work and budget plans, or *Rencana Anggaran dan Biaya* ("RKAB") for nickel mines, with only 107 out of 731 submitted plans approved, suggests a cautious approach

[33] Cabinet Secretariat of The Republic of Indonesia, 2023, President Jokowi to Announce Copper Ore Export Ban, https://setkab.go.id/en/president-jokowi-to-announce-copper-ore-export-ban/
[34] D Insights, 2024, Indonesia's Nickel Downstream Industry: Trapped in the Import Web?, https://dinsights.katadata.co.id/read/2024/03/26/indonesias-nickel-downstream-industry-trapped-in-the-import-web
[35] Ministry of Finance, 2024, Recent Macroeconomic and Fiscal Development, https://fiskal.kemenkeu.go.id/files/red/file/1705999253_fpa_macro_fiscal_updates_january_2024.pdf

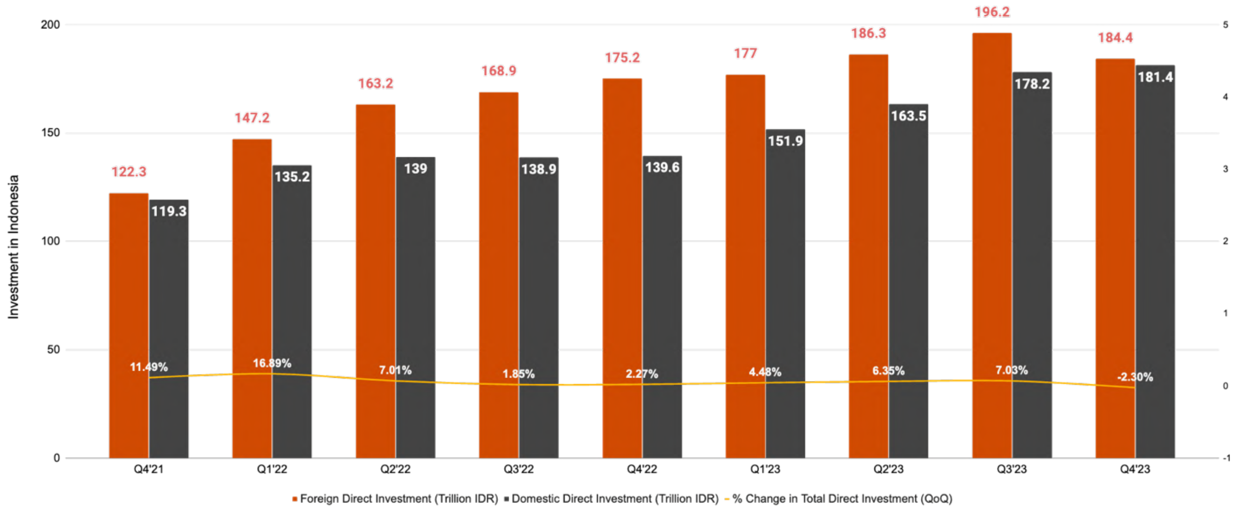
possibly aimed at stabilising global nickel prices while protecting reserves for future BEV industries. [36] However, this delay could create bottlenecks in the supply chain for domestic smelters due to a shortage of raw nickel. Consequently, Indonesia may need to import raw nickel ore from countries like Australia and Philippines to meet the demand of its smelters. In conclusion, while Indonesia's downstreaming policy has shown promise in boosting exports of refined nickel products and may stimulate the development of industries like EV battery production, it also raises concerns regarding trade practices, supply chain management, and domestic resource sustainability. Balancing these considerations will be crucial for Indonesia's long-term economic growth and trade competitiveness. Efforts to address these challenges, such as developing a coordinated plan for domestic resource extraction while promoting downstream industries, would be essential for Indonesia to realise the full potential of its industrialisation strategy while navigating complex global trade dynamics.

All in all, although Indonesian trade has slowed due to the end of the commodity-price boom, in the medium-to-long term there is room for optimism due to the potential benefits of the current downstreaming strategy of the government. It is imperative that Indonesia successfully industrialises away from its reliance on commodities, so that it mitigates its exposure to price volatility and diversifies its economy with more important value-adding exports in more advanced manufacturing sectors. While the current downstreaming policy has had some success and has created more added value than before, particularly through smelted mineral products, the range of manufactured exports must be further developed to include more higher-tech products and expanded to ensure economic benefits are maximised for the Indonesian economy through both increased export revenue and job creation.

[36] Bloomberg Technoz, 2024, RI Rawan Gangguan Produksi, ESDM Akhirnya Restui 107 RKAB Nikel?, https://www.bloombergtechnoz.com/detail-news/32869/ri-rawan-gangguan-produksi-esdm-akhirnya-restui-107-rkab-nikel

8. Investment

Figure 8.1 Investment in Indonesia (2021-2023)



Source: Kominfo (Jan 2024); BKPM (Jan 2024)

Indonesia's total investment realisation in Q4 2023 was IDR365.8 trillion. If considered as a whole, this figure exceeded the 2023 investment target, reaching 101.3% of the total target of IDR1,400 trillion or 129% of the National Medium-Term Development Plan, or *Rencana Pembangunan Jangka Menengah Nasional* ("RPJMN") target of IDR1,099 trillion. Investment realisation in Q4 2023 increased 16.2% (YoY) but fell 2.30% compared to the previous quarter. In line with the decrease in investment, there was a decrease in employment absorption by -11.34% QoQ (in Q4 2023 457,895 workers were absorbed). Labour absorption in 2023 reached 1,823,543 workers, which marked a 20% increase from the achievement in 2022 at 1,500,000 workers, partly due to this investment realisation throughout 2023.

In the fourth quarter of 2023, the realisation of FDI was 50.4%, higher than domestic direct investment ("DDI"). However, FDI growth was 5.3% (YoY), lower than DDI, which was 29.9% (YoY). In total, the realisation of investment outside Java was 51%. However, the top three largest provinces for investment receipts were still West Java, East Java and DKI Jakarta.

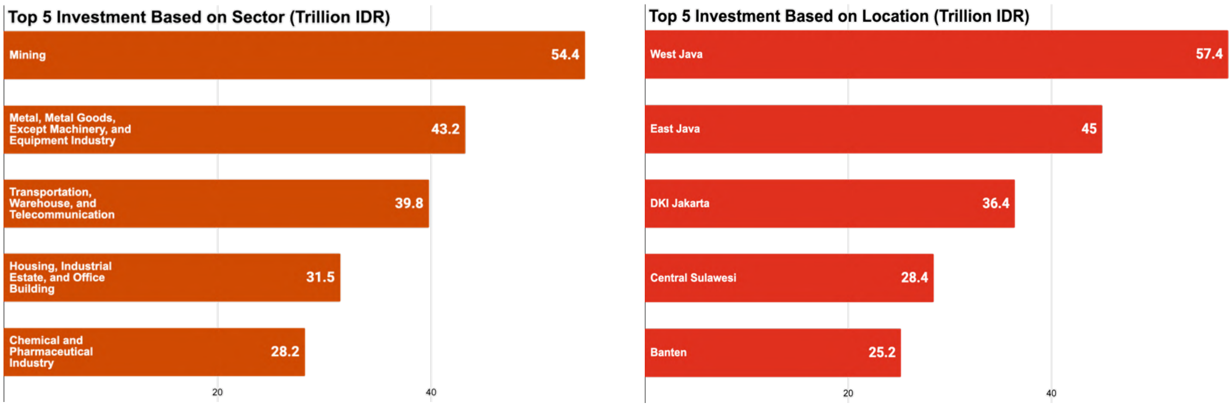
DDI realisation in 2023 amounted to IDR 674.9 trillion or 47.6% of total investment in 2023. This DDI realisation grew 22.1% compared to 2022. Meanwhile, realisation of FDI reached IDR 744 trillion or 52.4% of total investment in 2023. The value of FDI grew 13.7% compared to 2022.

Outlook 2024:

In 2024, the government is targeting investment worth IDR 1,650 trillion, an increase of 17.85% compared to the 2023 target. Of this amount, at least 50% would be contributed by FDI. The investment needs in the national strategic agenda in 2024 are IDR 77.5 trillion for the development of special economic zones and IDR97 trillion for the development of the Batam, Bintan and Karimun areas. These values do not include the IKN megaproject of IDR466 trillion, nor national strategic projects. Meanwhile, internal factors that may have delayed investment in 2024 include the elections.

Investment based on sector and location

Figure 8.2 Investment based on sector Q4 2023



Source: Kominfo (Jan 2024); BKPM (Jan 2024)

Regionally, West Java occupies the highest position as the area with the greatest amounts of both FDI and DDI, which collectively total IDR57.4 trillion. In second place is East Java at IDR 45 trillion, in third place is DKI Jakarta with realisation of IDR36.4 trillion, in fourth place is Central Sulawesi with realisation of IDR28.4 trillion, and in fifth place is Banten with realisation of IDR25.2 trillion.

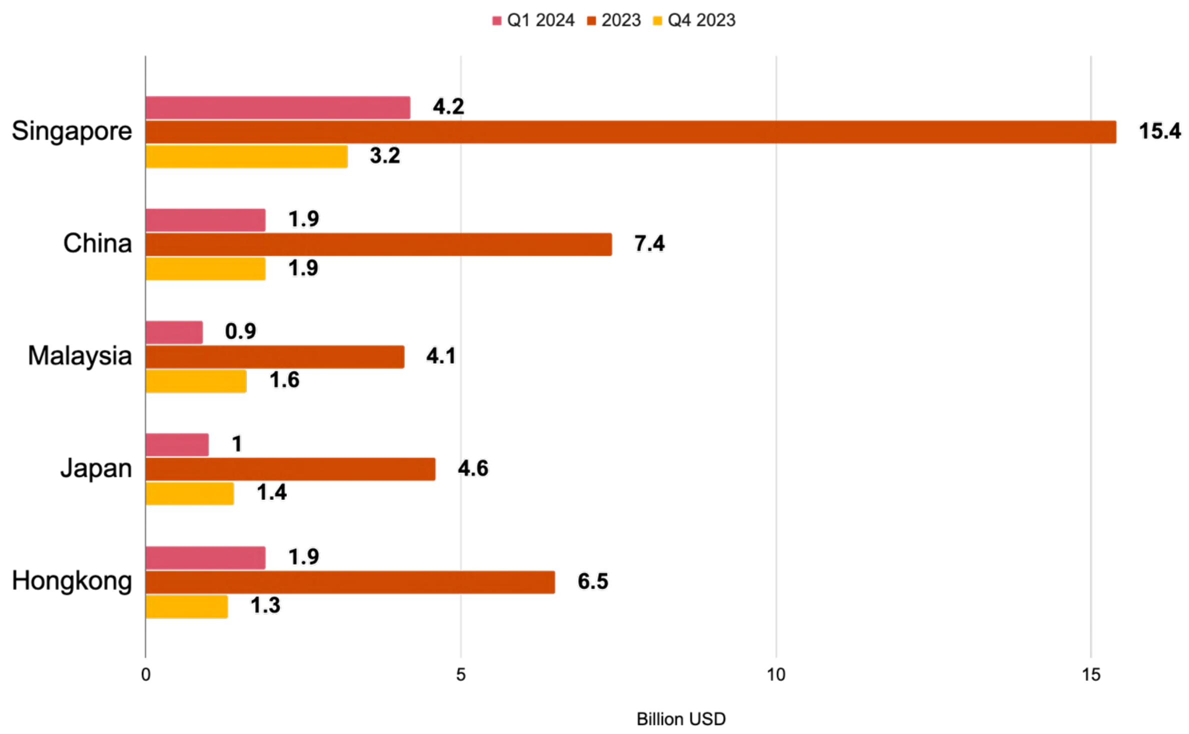
The sector that receives the most investment is mining, with the basic metal, metal goods, non-machinery and equipment sector in second position, the transportation, warehouse, and telecommunication sector in third position, the housing, industrial estate, and office building sector in fourth position, and the chemical and pharmaceutical industry in fifth position.

In line with the government's focus on improving the performance of the manufacturing industrial sector as the main driving force of national growth, investment in the industrial downstream sector continues to increase. In Q4 2023 the downstream industry contributed 29.9% of total investment or IDR109.4 trillion. The top five largest sectors are minerals (IDR65.1 trillion), forestry (IDR17 trillion), oil and gas (IDR14.7 trillion), agriculture (IDR11.3 trillion), and the electric vehicle ecosystem (IDR1.3 trillion). When viewed as a whole, investment realisation in these downstream sectors during 2023 (January-December) reached IDR375.4 trillion or 26.5% of the total investment realisation throughout 2023 amounting to IDR1,418.9 trillion.

Currently downstreaming is the main contributor to increasing foreign investment. It is still in its initial stages even though there are signs that these efforts are bearing fruit. This is because Indonesia has banned exports of mineral ore, thereby increasing shipments of refined metals. However, this is still dominated by products with lower added value such as stainless steel and nickel intermediate products compared to higher value EV battery components.

FDI based on investment country of origin

Figure 8.3 Investment based on country-of-origin



Source: Kominfo (Jan 2024); BKPM (Jan 2024)

Singapore is still in the lead as the country that contributed the most to FDI realisation. In Q4 2023, investment realisation of Singapore is USD 3.2 billion. In second place is China with a total investment of USD 1.9 billion. In third position is Malaysia with USD 1.6 billion. In fourth position is Japan with USD 1.4 billion and in fifth position is Hong Kong with USD 1.3 billion. In Q1 2024, the United States was in sixth position in q4 2023 with USD 0.8 billion, but in Q1 2024 the US was in fourth position with USD 1.1 billion as the country of origin for investment in Indonesia[37].

[37] Ministry of Investment / Indonesia Investment Coordinating Board (BKPM), 2024, Open data of national single window for investment, https://nswi.bkpm.go.id/data_statistik?_gl=1*1lshee8*_ga*MjY4NTg4NDcyLjE2OTk5NTAyMzA.*_ga_BT2NVHY1TH*MTcxNjU1MjEyMy4yMS4xLjE3MTY1NTIxMzYuNDcuMC4w

9. Government Budget

2023 state budget realisation

Entering late 2023, the interim realisation of state revenue and grants up to 31 December 2023 amounted to IDR2,774.30 trillion, which was 112.64% of the state budget target or 105.20% of the amended target (Presidential Regulation Number 75/2023).[38] The achievement surpassed 2022 by 5.25% (YoY), having maintained a positive performance trend from early 2023 onwards due to strong domestic consumption. The interim realisation of taxation revenue reached IDR2,155.42 trillion, non-tax state revenue amounted to IDR 605.89 trillion, and grants realisation stood at IDR12.99 trillion. Despite the moderation in commodity prices and global economic uncertainty, non-tax revenue still had a positive performance. Non-tax revenue was supported by an increase in coal royalty rates.

Figure 9.1 2023 preliminary state budget realisation

State Budget (in Trillion Rupiah)	2022			2023				
	Presidential Regulation 98/2022 (Amendment)	Realisation until Q4	% of State Budget	State Budget	Presidential Regulation 75/2023 (Amendment)	Realisation until Q4 (Preliminary)	% of State Budget	% of Pres. Reg 75/2023
A. State Revenue	**2,266.20**	**2,635.84**	**116.31**	**2,463.02**	**2,637.25**	**2,774.30**	**112.64**	**105.20**
I. Domestic Revenue	**2,265.62**	**2,630.15**	**116.09**	**2,462.62**	**2,634.15**	**2,761.31**	**112.13**	**104.83**
1. Tax Revenue	1,783.99	2,034.55	114.05	2,021.22	2,118.35	2,155.42	106.64	101.75
Tax	1,484.96	1,716.77	115.61	1,718.03	1,818.24	1,869.23	108.80	102.80
Custom & Excise	299.03	317.78	106.27	303.19	300.11	286.19	94.39	95.36
2. Non-Tax Revenue	481.63	595.59	123.66	441.39	515.80	605.89	137.27	117.47
II. Grant	**0.58**	**5.70**	**982.33**	**0.41**	**3.10**	**12.99**	**3,172.42**	**418.99**
B. State Expenditure	**3,106.43**	**3,096.26**	**99.67**	**3,061.18**	**3,117.18**	**3,121.94**	**101.99**	**100.15**
I. Central Government Expenditure	**2,301.64**	**2,280.03**	**99.06**	**2,246.46**	**2,302.46**	**2,240.65**	**99.74**	**97.32**
1. Line Ministries	945.75	1,084.67	114.69	1,000.84	1,000.84	1,153.46	115.25	115.25
2. Non-Line Ministries	1,355.89	1,195.35	88.16	1,245.61	1,301.61	1,087.18	87.28	83.53
II. Regional Transfer & Village Fund	**804.78**	**816.23**	**101.42**	**814.72**	**814.72**	**881.30**	**108.17**	**108.17**
C. Primary Balance	**(434.36)**	**(74.08)**	**17.05**	**(156.75)**	**(38.53)**	**92.24**	**(58.84)**	**(239.41)**
D. Surplus (Deficit)	**(840.23)**	**(460.42)**	**54.80**	**(598.15)**	**(479.93)**	**(347.64)**	**58.12**	**72.44**
% Deficit to GDP	(4.5)	(2.35)		(2.84)	(2.27)	(1.65)		
E. Financing	**840.23**	**590.98**	**70.34**	**598.15**	**479.93**	**359.51**	**60.10**	**74.91**

Source: Ministry of Finance (2024), Fiscal Policy Agency (2024)

The realisation of state expenditures up to 31 December 2023 amounted to IDR3,121.94 trillion, which was 101.99% of the state budget or 100.15% of the amended target. The realisation includes central government expenditures of IDR 2,240.65 trillion and transfers to regions, or *Transfer ke Daerah* ("TKD") of IDR881.30 trillion. The central government expenditures increased compared to the previous year by 0.83%. This increase primarily supported infrastructure budgets, including dam and irrigation projects, the procurement of specialised materials (almatsus), main weapon system equipment (alutsista), and the construction of IKN office buildings.

The positive performance of the state budget led to the primary balance for 2023 successfully returning to a positive value of IDR 92.24 trillion, marking the first surplus since 2011. However, taking into account all financial flows, including interest payments, the budget realisation revealed a deficit of IDR347.64 trillion, equivalent to 1.65% of GDP. Meanwhile, the realisation of budget financing up to 31

[38] Ministry of Finance, 2024, Publikasi APBN KiTa Edisi Januari 2024 https://media.kemenkeu.go.id/getmedia/00d3acf5-5aa8-499a-b7e3-ceadc5be7094/Publikasi-APBN-KiTa-Edisi-Januari-2024.pdf?ext=.pdf

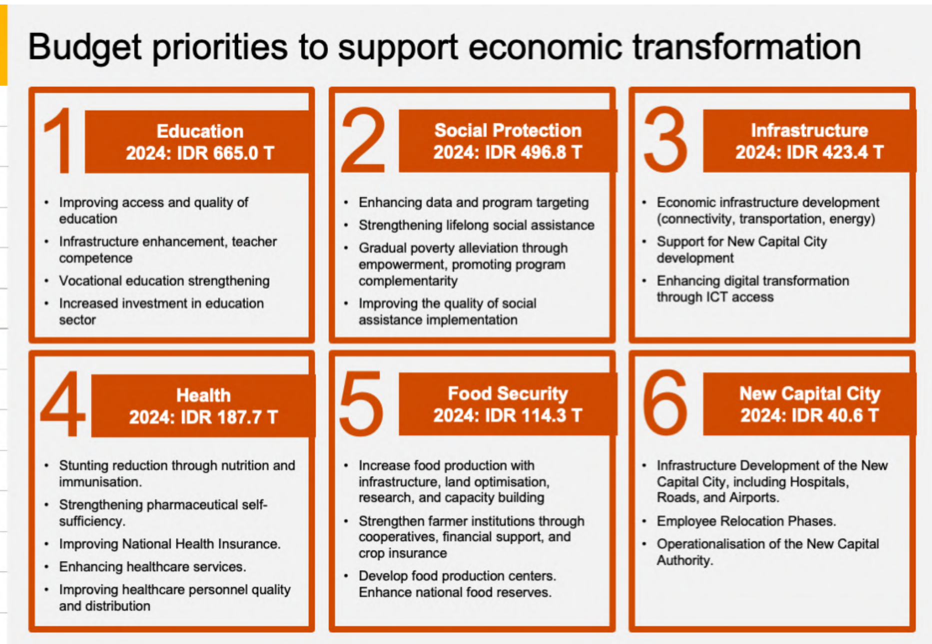
December 2023 reached IDR359.51 trillion (60.10% of the target or 74.91% of the amended target). As of 31 December 2023, the unspent budget allocation (SILPA/SIKPA) stood at IDR11.86 trillion (0.05% of GDP).

2024 state budget's posture of supporting economic transformation

The 2024 State Budget was officially enacted as Law Number 19 of 2023 on 16 October 2023. The State Budget for the Year 2024 remains committed to supporting inclusive and sustainable economic transformation, maintaining socio-economic stability, and supporting national priority programmes.[39]

Figure 9.2 2024 state budget posture and priorities

State budget (in trillion Rupiah)	2024
A. State Revenue	2,802.3
I. Domestic Revenue	2,801.9
1. Tax Revenue	2,309.9
2. Non-Tax Revenue	492.0
II. Grant	0.4
B. State Expenditure	3,325.1
I. Central Government Expenditure	2,467.5
1. Line Ministries	1,090.8
2. Non-Line Ministries	1,376.7
II. Regional Transfer & Village Fund	857.6
C. Primary Balance	(25.5)
D. Surplus (Deficit)	(522.8)
% Deficit to GDP	(2.29)
E. Financing	522.8



Source: Ministry of Finance (2024), Fiscal Policy Agency (2024)

In terms of fiscal targets, the 2024 state budget aims to achieve state revenue of Rp2,802.3 trillion, state expenditure of Rp3,325.1 trillion, and a deficit of Rp522.8 trillion. Notably, priority expenditures for 2024 include education (Rp665 trillion), social protection (Rp496.8 trillion), health (Rp187.5 trillion), infrastructure (Rp423.4 trillion), food security (Rp114.3 trillion), law and defence (Rp331.9 trillion), and research and innovation (Rp40.6 trillion).[40]

[39] Ministry of Finance, 2023, Buku II Nota Keuangan APBN TA 2024, https://media.kemenkeu.go.id/getmedia/833bd326-7056-486f-89b7-9b79855ff545/BUKU-II-NOTA-KEUANGAN-APBN-TA-2024_2.pdf?ext=.pdf
[40] Fiscal Policy Agency, 2024, Recent Macroeconomic and Fiscal Development, https://fiskal.kemenkeu.go.id/files/red/file/1705999253_fpa_macro_fiscal_updates_january_2024.pdf

To attain the target level of state revenue in 2024, it will be necessary to maintain a favourable investment climate amidst global uncertainties and to focus on tax reforms.[41] Such efforts may include implementing the Harmonisation of Tax Regulations Act, providing targeted and measurable fiscal incentives for strategic economic activities, enhancing tax compliance, and expanding the tax base. In the realm of non-tax revenue, increased revenue generation could be achieved through the improvement of the quality of public services, conservation of the environment, and improved governance.

Strategies considered by Ministry of Finance to achieve the target state expenditure in 2024 include enhancing human resource quality, completing priority infrastructure projects, expediting the transition to a green economy, implementing bureaucratic and state apparatus reforms, as well as implementing new measures to strengthen national resilience and security.

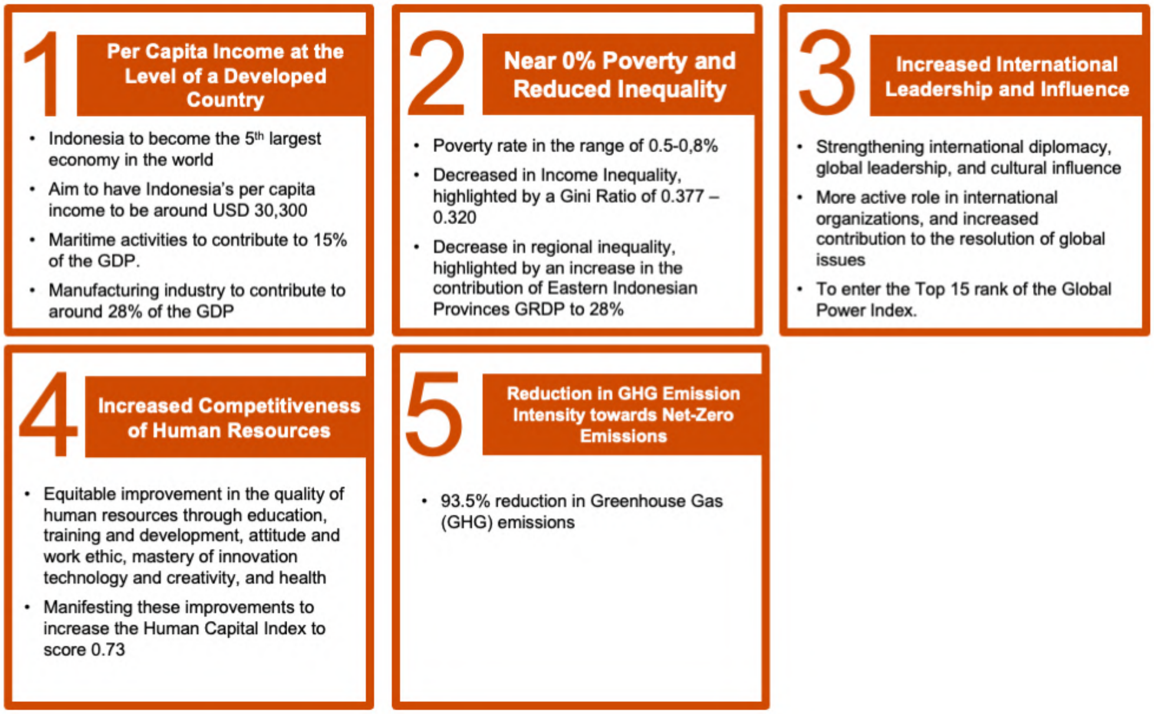
Moreover, to enable seamless transfer to regions, it is crucial to enhance policy synergy by harmonising central and regional expenditures. Furthermore, support should be provided for the payment of government employees under the Regional Work Agreement, or *Pegawai Pemerintah dengan Perjanjian Kerja* ("PPPK"), particularly teachers and healthcare workers. Other key areas of focus include improving public services in regions, supporting school operations, addressing extreme poverty, and reducing stunting.

[41] CNBC Indonesia, 2024, APBN Tahun 2024: Bekerja Keras Melindungi Rakyat dan Ekonomi Indonesia, https://www.cnbcindonesia.com/opini/20240108103447-14-503674/apbn-tahun-2024-bekerja-keras-melindungi-rakyat-dan-ekonomi-indonesia

10. Development

Indonesia stands on the brink of a transformative era, aiming to redefine its position on the global stage by 2045 through its ambitious Long-Term Development Plan, or *Rencana Pengembangan Jangka Panjang* ("RPJP").[42] This vision, termed "Golden Indonesia 2045," envisions the nation emerging as a developed, high-income country, ranking as the world's fifth-largest economy. Central to this vision are strategic goals focused on economic growth, poverty reduction, human capital development, and environmental sustainability.

Figure 10.1 Golden Indonesia vision 2045

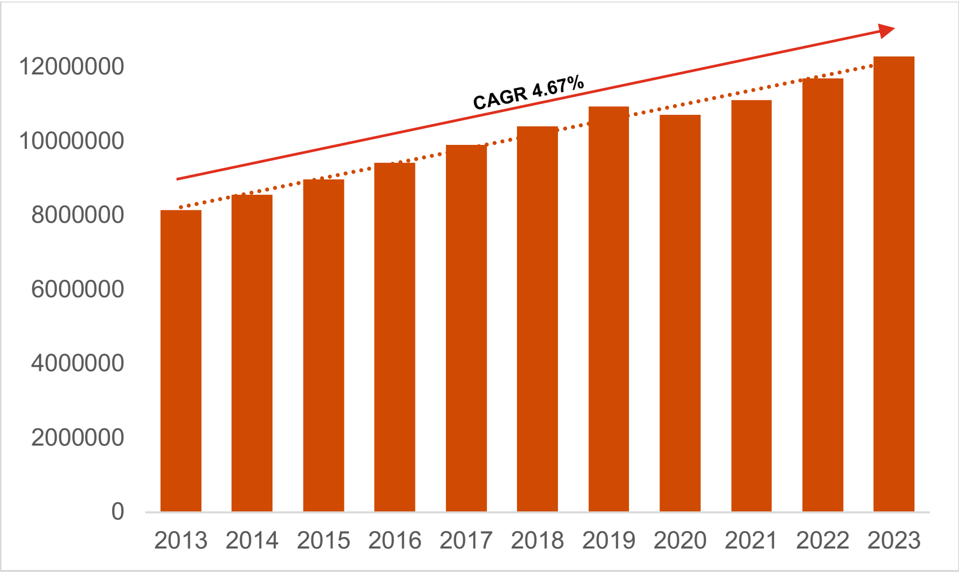


Source: BAPPENAS (2023)

At the heart of Indonesia's development vision is the goal to elevate its GDP per capita to USD30,300 by 2045, a significant leap from USD4,919.70 in 2023. The last decade has shown a consistent upward trajectory in GDP per capita (excluding the pandemic), growing from USD3,602.9 in 2013 to its current figure. This growth signifies a resilient economy that, despite global economic fluctuations, has managed to sustain an upward growth curve.

[42] BAPPENAS, 2023, Indonesia Emas 2045, https://indonesia2045.go.id/

Figure 10.2 Real GDP for the past 10 years



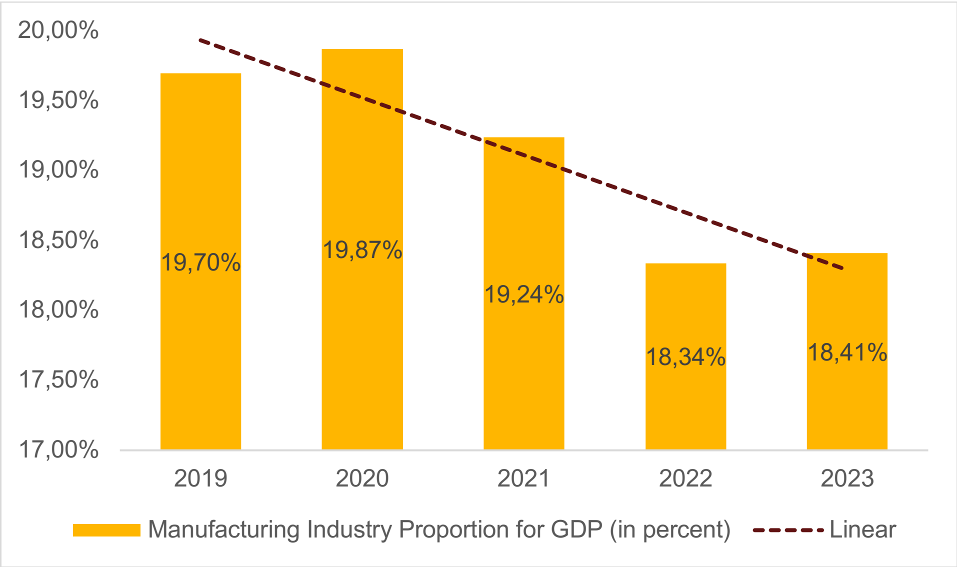
Source: Central Bureau of Statistics (BPS) (2024)

However, achieving the 2045 target would necessitate an unprecedented GDP growth rate of 9.45% from 2024 onwards. Considering the growth trends from 2013 to 2023, where the GDP experienced fluctuations but ultimately reflected growth, reaching the target requires sustained economic reforms, increased investment in technology, human capital, and infrastructure, and enhancement of the manufacturing sector's productivity.

Indonesia's strategic focus on bolstering its maritime economy and manufacturing sector is evident from its policy directions over the past decade. The maritime sector, a historical cornerstone of Indonesia's economy, has seen significant growth, particularly in the fisheries subcategory which grew at a CAGR of 7.68% annually from 2017-2022, outpacing the average rate of growth of the Indonesian GDP in that same period. This growth was propelled by strategic initiatives against illegal fishing and enhancements in fishery production infrastructure, demonstrating the potential of targeted government interventions in stimulating sector-specific growth.

Conversely, the manufacturing industry, despite its potential as a major economic driver, has encountered challenges. Data indicates a declining trend in the sector's contribution to GDP, from 20.16% in 2017 to 18.34% in 2022. This decline underscores the need for a strategic pivot to rejuvenate the sector with an emphasis on innovation, upgrading industrial technology, and navigating international trade policies such as the EU's Carbon Border Adjustment Mechanism (“CBAM”), which poses a significant threat to Indonesia's steel exports.

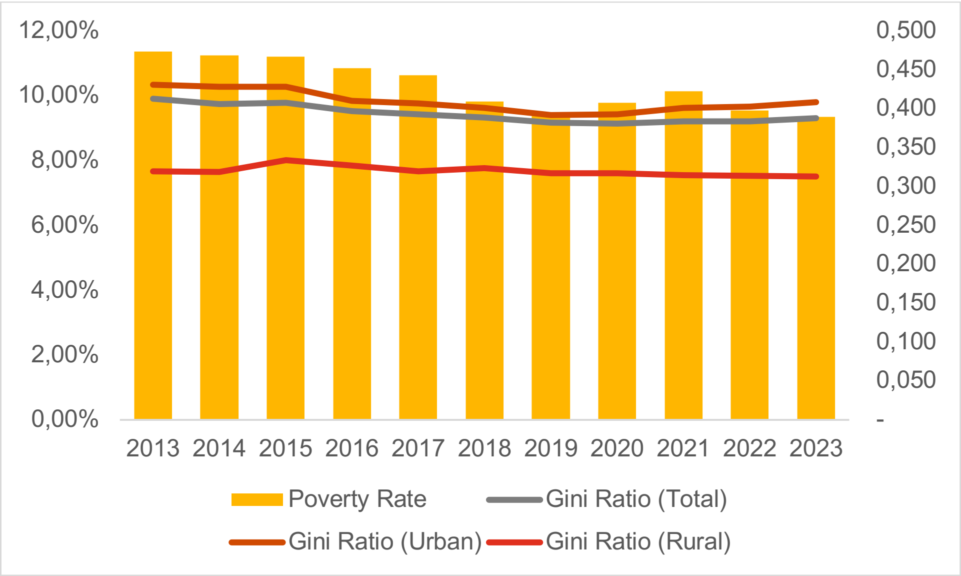
Figure 10.3 Proportion of manufacturing industry in GDP formation in the last five years



Source: Central Bureau of Statistics (BPS) (2024)

Indonesia's commitment to reducing poverty and inequality is reflected in the decreasing poverty rate, which fell from 11.36% in 2013 to 9.36% in 2023, and the decline in the extreme poverty rate during the same period. These trends signify progress in improving the standard of living for millions of Indonesians. Government initiatives such have assisted in this improvement in the standard of living. The Hopeful Family Program or *Program Keluarga Harapan* ("PKH"), provides assistance to poor and financially vulnerable families to enable them to meet basic needs, such as food, education, and health services. The Product-Intensive Program or *Program Padat Karya* ("PDK") aims to provide temporary employment opportunities for unemployed and underemployed individuals through projects such as infrastructure and public works. Both programs have played pivotal roles in this achievement by providing social assistance and empowering the impoverished through employment and entrepreneurial opportunities.

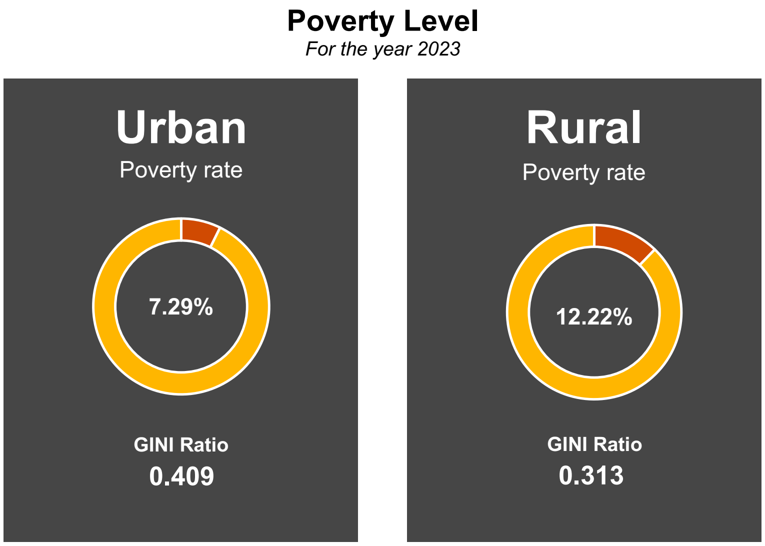
Figure 10.4 Poverty rate and GINI ratio for the past ten years



Source: Central Bureau of Statistics (BPS) (2024), Central Bureau of Statistics (BPS) (2023),

Despite these advances, challenges persist, especially in rural areas and the eastern regions of Indonesia, where poverty rates remain disproportionately high. Addressing these disparities requires a multifaceted approach that combines direct assistance with long-term investments in education, healthcare, and economic infrastructure to ensure inclusive growth.

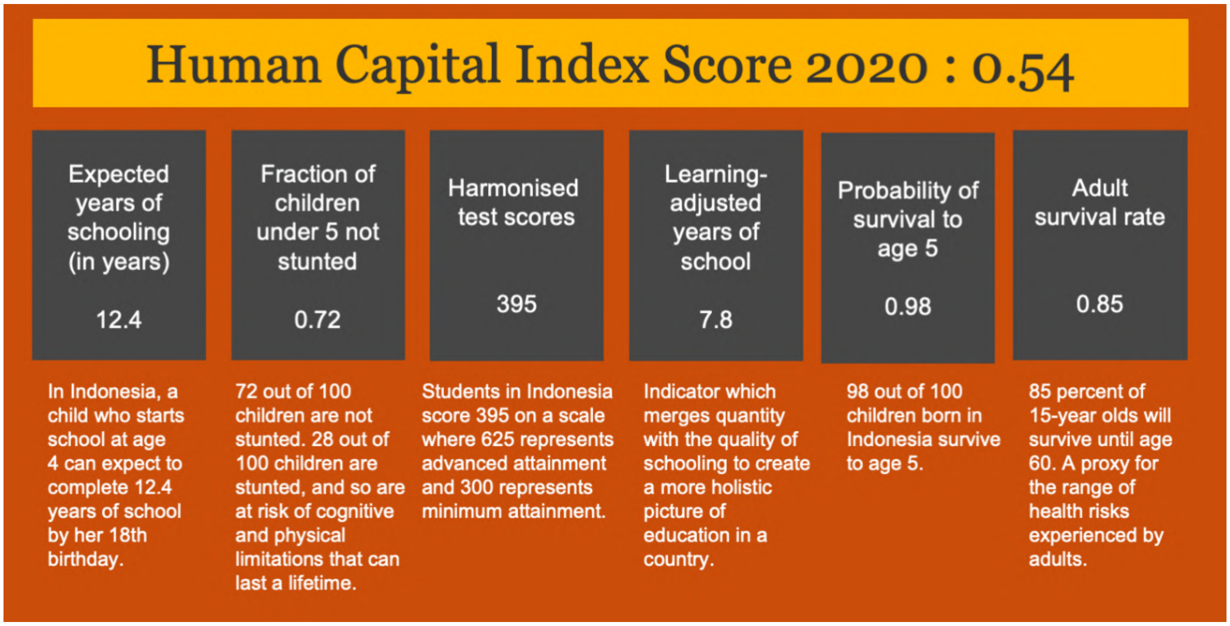
Figure 10.5 Poverty level in urban vs rural areas in 2023



Source: Central Bureau of Statistics (BPS) (2024), Central Bureau of Statistics (BPS) (2023)

Enhancing human capital through improvements in education and health is crucial for Indonesia's ambition to become a developed nation. The Human Capital Index ("HCI") data, which indicates a score of 0.54, underscores the importance of continued investment in education quality and accessibility, healthcare services, and child nutrition.

Figure 10.6 Human Capital Index Score for 2020



Source: World Bank (2020)

In parallel, Indonesia's commitment to environmental sustainability and reducing greenhouse gas emissions is integral to its development vision. The nation's strategy to achieve net-zero emissions involves increasing the share of renewable energy in the electricity mix and implementing policies that encourage sustainable practices across all sectors of the economy. In 2023, the Indonesia Carbon Exchange was operational, with two products: the "Allowance Market" and "Offset Market". Although it is too early to judge the impact the exchange will have in terms of CO2 emissions reduction, it nevertheless shows Indonesia's commitment to achieving its CO2 reduction target.

Indonesia's journey towards "Golden Indonesia 2045" is marked by significant ambitions and noteworthy progress in various sectors. The nation's strategic focus on economic growth, poverty reduction, human capital development, and environmental sustainability lays a solid foundation for achieving its development targets. However, realising these goals requires more effective and agile policy implementation, more effective regulation, innovative strategic thinking, and collaborative governance that prioritises inclusivity and sustainability. With the right policies and initiatives in place, Indonesia would have the possibility to overcome the challenges ahead and achieve its vision of becoming a developed, high-income country by 2045.

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