From Containment to Recovery: The Outlook for Indonesia

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Entering Q4 2020, the road to recovery seems to remain long...
1. Recent developments

Large scale social restrictions in Jakarta were relaxed in early June, then reintroduced in mid-Sept.
1. Recent developments

Indonesia had the first economic contraction in Q2, after more than two decades.
1. Recent developments

Sectors exposed to external shocks and mobility restrictions were hit the hardest; knowledge-intensive services held up.

Manufacturing, trade, hotels, restaurants and transport contracted sharply in Q2
(contribution to real GDP growth year-on-year, percent)

<table>
<thead>
<tr>
<th>Sector</th>
<th>Average 2017 - 2019</th>
<th>Q1 2020</th>
<th>Q2 2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>0.9</td>
<td>0.6</td>
<td></td>
</tr>
<tr>
<td>Manufacturing</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trade, transport &amp; hospitality</td>
<td></td>
<td></td>
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<tr>
<td>Knowledge intensive services</td>
<td></td>
<td></td>
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<tr>
<td>Tax-subsidy</td>
<td></td>
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<tr>
<td>Construction</td>
<td></td>
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<tr>
<td>Other industry</td>
<td></td>
<td></td>
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<tr>
<td>Health, edu. &amp; public admin.</td>
<td></td>
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<tr>
<td>Other services</td>
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</tbody>
</table>

Source: BPS, World Bank staff calculations
Notes: Knowledge intensive services consist of information and communication, financial and insurance activity, real estate, and business services. Trade, transport & hospitality consist of wholesale and retail trade, repairs, transportation and storage, and accommodation and F&B activities.
1. Recent developments

Foreign tourist arrivals sunk to a record low, leading to a tourism freeze.

Tourism Indicators
(yoy growth, LHS; yoy growth for GDP, RHS)

Source: BPS, World Bank staff calculations
1. Recent developments

Despite the widening service trade deficit, the current account deficit narrowed to a three-year low, as goods imports fell deeper than exports.
1. Recent developments

Capital inflows stabilized in Q2, supported by the large issuance of global bonds.
1. Recent developments

Bank’s credit growth decelerated to the lowest rate since 2003

Graph: Banks’ Credit Growth by Type of Loans (yoy growth, percent)

- Investment loans
- Consumption loans
- Working capital loans

Source: Bank Indonesia, CEIC and World Bank staff calculations
1. Recent developments

Non-performing loans remained low, but started to rise recently, while banks remain adequately capitalized.
1. Recent developments

Cumulative expenditure by end-August grew 10.5 percent yoy, driven by social aid spending, while cumulative revenue declined by 13.0 percent yoy.
Peer countries have also been affected heavily
1. Recent developments

<table>
<thead>
<tr>
<th>Category</th>
<th>Allocation</th>
<th>% of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Healthcare</td>
<td>IDR 87.6 trillion</td>
<td>0.5%</td>
</tr>
<tr>
<td>Social Protection</td>
<td>IDR 203.9 trillion</td>
<td>1.2%</td>
</tr>
<tr>
<td>Sectoral &amp; SNG Spending</td>
<td>IDR 106.1 trillion</td>
<td>0.7%</td>
</tr>
<tr>
<td>Support to MSMEs</td>
<td>IDR 123.5 trillion</td>
<td>0.8%</td>
</tr>
<tr>
<td>Financing for Corporations</td>
<td>IDR 53.6 trillion</td>
<td>0.3%</td>
</tr>
<tr>
<td>Tax Incentives for Firms</td>
<td>IDR 120.6 trillion</td>
<td>0.7%</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance, as of 11 August 2020

The Government announced a series of fiscal packages amounting to IDR 695 trillion (4.2 percent of GDP)
1. Recent developments

Until September, the Government has disbursed 36.6% of the spending budgeted for stimulus.

Source: Monthly budget disbursement data from Ministry of Finance, as of September 16, 2020
1. Recent developments

Most safety nets have reached their target coverage, but some vulnerable households still have not received any.

**Beneficiaries of social assistance programs and other relief measures**

(Percent of households)

As of early August 2020, 90% of households in the bottom 40% reported benefiting at least one economic relief measure. However, around 10% of households in the bottom 40% who have experienced income shocks have not received any.

Source: World Bank’s High-Frequency Monitoring of COVID-19 Impacts, Round 3
1. Recent developments

Employment recovery begins...

...but still a long way to go

While 24 percent of households’ primary breadwinners had stopped working by early, many have resumed working by August. As a result, 90% of primary breadwinners have continued working in August.

A lower incidence of income reduction is observed. However, nearly 50% of breadwinners who continued working still experiencing income losses.

Source: World Bank’s High-frequency Monitoring of COVID-19 Impacts, Round 1 and 3
2. Outlook

The economic recovery will be gradual, and fiscal deficit is expected to remain above 3 percent through 2022.

Indonesia’s GDP is projected to **contract by 1.6 percent in 2020**, contributing to a narrowing of the current account deficit.

**Severe Scenario:** Mobility restrictions were reintroduced in Jakarta on Sept 14 and could be expanded to other provinces. In such a scenario, the GDP growth could drop further to -2.0 percent in 2020.

Source: World Bank’s estimates and forecasts. Central Bureau of Statistics (BPS); Bank Indonesia; Ministry of Finance.

Note: 2020-2022 are estimated and forecast figures.

#ResilientRecovery #EAPUpdate worldbank.org/eapupdate
2. Outlook

Extreme poverty* is projected to increase for the first time since 2006, from 3.1 to 3.4 percent between 2019 - 2020.

*) Based on USD 1.9 per day poverty line

Poverty rates over time
(poverty rate in percent)

Source: World Bank’s estimates and forecasts; Central Bureau of Statistics (BPS)
Note: Nowcast on 2019; forecast from 2020 onwards. The forecast is based on the scenario of absence in mitigation responses.
Now the road to recovery has three sharp curves that policy makers must handle.
3. Accelerating towards recovery

Handling the pandemic curve

Robust health system preparedness to handle the pandemic curve gives safety and confidence for the recovery

Monitor
Trace & Isolate
Expand Capacity
3. Accelerating towards recovery

...Turning around the recession curve

- Addressing challenges in delivering social assistance will help families today and tomorrow
- Firms across many sectors will still need help to stay afloat - and then to start and restart
- Avoiding spillovers from the real to the financial sector and deepening reforms is critical to the recovery

FAMILIES
FIRMS - BANKS
need CASH to slow the descent and restart
3. Accelerating towards recovery

…and accelerating towards recovery

Reforms to improve the investment climate including improving firms’ access to capital, labor and production inputs has the potential to turbocharge the economic recovery.

Workers seeking jobs in the post-COVID economy are likely to require different and often higher-order skills.

Resuming the effort to close Indonesia’s large infrastructure gap will be key to the post-Covid recovery.

Reallocation and elimination of subsidies will help increase investments in infrastructure and human capital…

…but given spending needs, only tax reforms can stop Indonesia from climbing further along the debt curve.
Download the East Asia and Pacific Economic Update: worldbank.org/eapupdate

Download Indonesia’s Outlook: bit.ly/idmpo-oct2020

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