The Long Road to Recovery

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Entering 2020, the road seemed long but straight...

2019: Indonesia crosses Upper-Middle Income threshold

Competitiveness reforms to boost Indonesia’s speed:
- Openness
- Human capital
- Infrastructure
...but then...

AWAS!
COVID DI DEPAN

KURANGI KECEPATAN SEKARANG
covid-19 led to a major global economic shock...
Commodity Prices and Projections
(Index: 2019 = 100)

Source: World Bank commodity price projections, April, 2020
Note: 2019=100, (e) is estimated, (f) is forecast

...lower commodity prices...
...massive capital outflows from emerging markets...

Source: IIF, BI, BIS, World Bank staff calculations
Note: October 2019 =100 for NEER and 10-year bond yield
...and freezing tourism flows

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

Visitors Arrivals
Services Exports
Services Exports (Transportation)
(GDP) Accommodations

Source: BPS, World Bank staff calculations
Domestic mobility restrictions to manage the spread of Covid limited both supply and demand.
Labor-intensive sectors slowed, while knowledge-intensive sectors were resilient.
The shock deepened in Q2, likely leading the economy to contract.
Livelihoods have been severely affected

Source: World Bank staff calculation.
Note: Job loss here includes both unemployment and working age individuals whom become inactive. This is because it was not feasible to distinguish between the two in Susenas March 2019 data from which the simulation is based on. (*) Pre-crisis level refers to year 2019, and adjusted with the actual coverage of social assistance (SA) measures
In response to the shock, the government announced a series of fiscal packages...

- **Healthcare**
  - IDR 84.6 trillion (0.5 percent of GDP)

- **Social Protection**
  - IDR 139.8 trillion (0.9 percent of GDP)

- **Supporting MSMEs**
  - IDR 121.1 trillion (0.7 percent of GDP)

- **Support to SOEs**
  - IDR 112.2 trillion (0.7 percent of GDP)

- **Tax Relief**
  - IDR 123 trillion (0.8 percent of GDP)

Source: World Bank staff compilation from various sources.
Note: The written figure may be different from the Government-announced stimulus package.
...which includes a massive expansion of social assistance to protect livelihoods

<table>
<thead>
<tr>
<th>Program name</th>
<th>Increased coverage above pre COVID-19</th>
<th>Benefit incidence &amp; duration</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Sembako</strong> (Staple food)</td>
<td>Additional of 5 million households (HH) to <strong>20 million HH</strong>, identified among those already in the DTKS</td>
<td>Increased benefits of IDR 200,000/month (for 12 months)</td>
</tr>
<tr>
<td>PKH</td>
<td>Additional of 800 thousands HH to <strong>10 million HH</strong>, identified among those already in DTKS</td>
<td>Increased benefits by 25% for 12 months</td>
</tr>
<tr>
<td><strong>Kartu Prakerja</strong> (Pre-employment card)</td>
<td>Additional of 3.6 million to <strong>5.6 million individuals</strong> in total</td>
<td>Training: IDR 1 million/month, Benefits: IDR 600,000/month (4 months), IDR 50,000/months (3 months)</td>
</tr>
<tr>
<td><strong>UCT</strong> (Non-Jabodetabek)</td>
<td>9 million HH</td>
<td>IDR 600,000/month (3 months), then IDR 300,000/month (6 months)</td>
</tr>
<tr>
<td><strong>Sembako</strong> (Jabodetabek)</td>
<td>• <strong>1.2 million HH</strong> in Jakarta, • <strong>600,000 HH</strong> in periphery districts (Bodetabek)</td>
<td>Food package equivalent to IDR 600,000/month (3 months), then IDR 300,000/month (6 months)</td>
</tr>
<tr>
<td><strong>Electricity Subsidy</strong></td>
<td>All households subscribing to 450VA and 900VA electricity connection.</td>
<td>HHs with 450 VA – fee waiver (6 months)</td>
</tr>
<tr>
<td><strong>BLT Dana Desa</strong> (Village Fund)</td>
<td><strong>11 million rural HH</strong>, prioritizing those who lost main source of income due to COVID-19</td>
<td>IDR 600,000/month (3 months), then IDR 300,000/month (3 months)</td>
</tr>
</tbody>
</table>

Source: World Bank staff compilation from various sources. Note: The written figure may be different from the Government-announced stimulus package.
Overall, the recovery will be gradual and GDP is expected to be flat in 2020, contributing to a narrowing of the current account deficit.

### Key economic indicators (Indonesia)

<table>
<thead>
<tr>
<th>Baseline Scenario</th>
<th>2019</th>
<th>2020e</th>
<th>2021f</th>
<th>2022f</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Real GDP</strong></td>
<td>5.0</td>
<td>0.0</td>
<td>4.8</td>
<td>6.0</td>
</tr>
<tr>
<td><strong>Consumer price index</strong></td>
<td>2.8</td>
<td>2.6</td>
<td>2.8</td>
<td>3.0</td>
</tr>
<tr>
<td><strong>Current account balance</strong></td>
<td>-2.7</td>
<td>-1.9</td>
<td>-2.0</td>
<td>-2.1</td>
</tr>
<tr>
<td><strong>Government budget balance</strong></td>
<td>-2.2</td>
<td>-6.3</td>
<td>-4.1</td>
<td>-3.1</td>
</tr>
</tbody>
</table>

**Severe Scenario**
- Under the assumptions of longer mobility restrictions and deeper global economic contraction, the annual real GDP growth is estimated to reach -2.0 percent in 2020.

Source: Bank Indonesia; Central Bureau of Statistics (BPS); Ministry of Finance; World Bank staff calculations
Note: 2020-2022 are estimated and forecast figures.
Without Government support, millions would fall into poverty.

Source: BPS, World Bank staff calculation.

Note: Benchmark level refers to forecasted changes in poverty level in 2020 without Covid-19 (Poverty rate = 8.7 percent). 'SA' stands for Social Assistance. Mild Impact assumes zero growth, whereas Severe Impact assumes 2 percent growth. 'No additional SA' refers to change in poverty rate relative to the pre-crisis level when there is absence of government compensation; 'Full Additional SA' scenario shows 2020 poverty rate (simulated), after taking into account the full social assistance package. 1 percentage points of poverty equals 2.6 million individuals.

<table>
<thead>
<tr>
<th>Change in the poverty rate in 2020 from 2019 under multiple scenarios (poverty rate in percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td>No Covid19</td>
</tr>
<tr>
<td>No Covid19</td>
</tr>
<tr>
<td>-0.7</td>
</tr>
<tr>
<td>-1.2</td>
</tr>
</tbody>
</table>
Household-Heads who received Social Assistance Programs*
(percentage of household-heads)

<table>
<thead>
<tr>
<th></th>
<th>HH Bottom 40</th>
<th>HH-head experiencing income loss</th>
<th>HH-head experiencing job loss</th>
</tr>
</thead>
<tbody>
<tr>
<td>Do not receive any Social Assistance Program</td>
<td>46</td>
<td>51</td>
<td>56</td>
</tr>
<tr>
<td>Receive any Social Assistance Program</td>
<td>54</td>
<td>49</td>
<td>44</td>
</tr>
</tbody>
</table>

Source: World Bank staff calculation.
Note: The above figure presents number of surveyed household-head who receive any kinds of social assistance as of Round 1 Hify Survey (1-17 May 2020). (*) includes PKH, Sembako, BLT, Kartu Pra-Kerja, public works.

Assistance needs to reach more of those in need to fulfil its full potential to mitigate the shock.
The Long (and Winding) Road to Recovery

Jalan panjang yang berliku
Namun kuharus mampu menempuh
Now the road to recovery has three sharp curves that policymakers must handle.
Handling the pandemic curve

(daily confirmed new COVID-19 cases, thousands)

Source: Our World in Data
Robust health system preparedness to handle the pandemic curve gives safety and confidence for the recovery.

- Scaling up capacity for **confirmatory and sample-based testing** to regularly track and monitor infection transmission and progression.
- **Undertaking contact tracing and isolation** of confirmed cases and their contacts to contain spread.
- Expanding the capacity of the health care system to meet possible surges in COVID-19 cases **while being able to continue basic health services**.
Turning around the recession curve...

Share of firms experiencing difficulties in May and June 2020, percent

- YoY sales drop: 82%
- Large sales drop: 74%
- Reduced cashflow availability: 71%
- Reducing labor costs: 65%
- Difficulty repaying loans: 21%
- Difficulty paying wages: 20%
- Difficulty paying utilities: 13%
- Difficulty paying rent: 9%
- Filed for bankruptcy: 5%
Addressing challenges in delivering social assistance will help families today and tomorrow.

- **Dynamic database**
  - Reaching all poor and vulnerable families has been challenging: current efforts need to be sustained and leveraged towards a larger, more dynamic DKTS.

- **Broaden target groups**
  - Assistance has focused on poor households with children – the elderly and people living with disabilities can also be targeted.

- **Reach the ‘missing middle’ and ‘newly poor’**
  - High informality and limited social insurance means many ‘newly poor’ have not been covered – reaching this group will be important now and in the future.
Firms across many sectors will still need help to stay afloat - and then to start and restart.

**Help firms ‘keep the lights on’ by ensuring they have enough cash to pay for minimum expenses.**

**Help firms start, re-start or expand production, to take advantage of growing demand and adapt to changing demand patterns.**

Recovery will be slow for some firms and could involve new opportunities for others, **calling for a targeted approach.**
Avoiding spillovers from the real to the financial sector and deepening reforms is critical to the recovery.

Restructuring or relief?

Current restructuring efforts and loan forbearance may only delay a spike in non-performing loans (NPLs) if firms remain illiquid longer – **additional measures to manage banks’ asset quality may be required**.

Expand resolution to boost system resilience

**Updating recovery and resolution planning for banks** and putting in place NPL management frameworks with industry-backed resolution funding would make the sector more resilient.

Keep minimum prudential standards

**Minimizing moral hazard among banks and their clients and maintaining prudential standards and risk management** is paramount to financial stability.
...and accelerating towards recovery
The Omnibus Bill has the potential to turbocharge the economic recovery, but some proposed reforms could be detrimental.

Revising the Investment Law and eliminating discrimination against FDI in sectoral laws will boost investments and create jobs.

The Bill will help plug Indonesia into Global Value Chains by making importing-to-export easier – introducing a risk-based approach to import/export licensing can reduce trade costs.

The Bill also includes reforms that could be detrimental to the environment, health and safety, and incomes of Indonesians – dropping or modifying them will ensure the Bill brings maximum benefit for everyone.

Openness=Investment=Jobs

Indonesia joins GVCs

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

School closures amplify the dropout risk for lower income students – working with schools to lower this risk limits the erosion to Indonesia’s skills base.

Programs such as Kartu Prakerja can incentivize skills acquisition through short-term training in an enhanced TVET system that helps develop the skills needed to adjust to work post-COVID.

Improve the quality of labor market information and use it to inform education and training and to support efforts to match workers with jobs.
Resuming the effort to close Indonesia’s large infrastructure gap will be key to the post-Covid recovery.

- **Increasing public resources available for infrastructure** at all levels of government and across sectors – including expanding digital connectivity – remains key to competitiveness.
- Public funds will not be sufficient – improving the regulatory, institutional and financial environment for **private sector participation in infrastructure** is needed.
- **Recalibrating the role and incentives of SOEs** will catalyze private sector entry, increase competition, and boost infrastructure quality.

**More public resources**

**Better laws & institutions**

**SOEs need to make room for the private sector**
If Indonesia does not flatten the debt curve, mounting interest payments can reduce fiscal space, undermine its hard-earned investment-grade rating and derail the recovery.
Reallocation and elimination of subsidies will help increase investments in infrastructure and human capital...

LPG, diesel, and fertilizer subsidies are expensive and poorly-targeted.

Eliminating energy subsidies could yield 0.4 percent of GDP in fiscal savings after compensating the poor and vulnerable.

Share of central government spending in 2018, percent:

- Fertilizer subsidies: 2.3%
- Energy subsidies: 10.6%
- Social assistance: 3.9%
- Health: 4.9%
- Capital: 12.7%
...but given spending needs, only tax reforms can stop Indonesia from climbing further along the debt curve.

Inclusive taxation

More firms should be **brought under the scope of major taxes** such as the VAT and CIT.

**Gotong Royong**

Raise personal income taxes, including in the **middle**, while also ensuring that those who have more, contribute more.

**Excise taxes are smart taxes**

Expand the use of **excise taxes** on tobacco, plastics, sugar-sweetened beverages and fuel to raise revenues and create incentives to reduce use.
Terima Kasih

Questions
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