

## INDONESIA

- Indonesia's GDP per capita gap relative to the most advanced OECD countries remains large, but gradually narrows as the economy is shifting away from low-productivity primary sectors to services and manufacturing. While labour utilisation is already relatively high, it is also continuing to contribute to lifting GDP per capita.
- Income inequality is rising in Indonesia although it is not particularly high in comparison with other emerging-market countries. This has largely been driven by a growing gap between the rich and the poor within cities, combined with the very rapid pace of urbanisation. Income inequality across the regions has been slowly declining.
- Progress is being made in a number of areas particularly in the provision of infrastructure. While the government is prioritising education, including by improving the quality of teaching, there are still few signs of improved outcomes. There have also been reforms to the Negative Investment List, which proscribes foreign investment in certain sectors. Nevertheless, the system remains cumbersome and arbitrary and should be abolished. A cap has been introduced on increases in the minimum wage. However, rigidities in the labour market remain, and these are contributing to the high levels of labour market informality and youth unemployment.
- The targeting and coverage of programmes designed to increase access to education should be improved, and measures to improve the quality of teaching should be stepped up. Measures to encourage private-sector participation in infrastructure investment need to be improved.
- Eliminating the remaining subsidies on diesel and electricity would allow a further reprioritisation of spending towards promoting inclusive and sustainable growth, including ramping up spending on education and sustaining spending on infrastructure. Reforms in this area would not only boost growth but also raise equity and environmental sustainability.

### Going for Growth 2017 priorities

**Enhance outcomes in education.** Public spending on education remains below the government's target (20% of government spending). Outcomes and teaching quality remain poor, including high levels of teacher absenteeism.

**Actions taken:** Programmes to improve teacher qualifications through certification and training are ongoing. However, beyond substantially increasing teacher wages, there is little evidence of improved outcomes. Improved utilisation of the national poverty database will facilitate better targeting of conditional cash transfers, including those aimed at facilitating access to education.

**Recommendations:** Continue stepping-up spending in education. Encourage higher enrolment and quality at primary and secondary levels through regular teacher assessment and professional development. More closely link teacher salaries to not just qualifications, but also performance and ongoing training.

**Improve the regulatory environment for infrastructure.** Regulatory uncertainty, particularly at the regional level, is hampering private investment in infrastructure, including via PPPs.

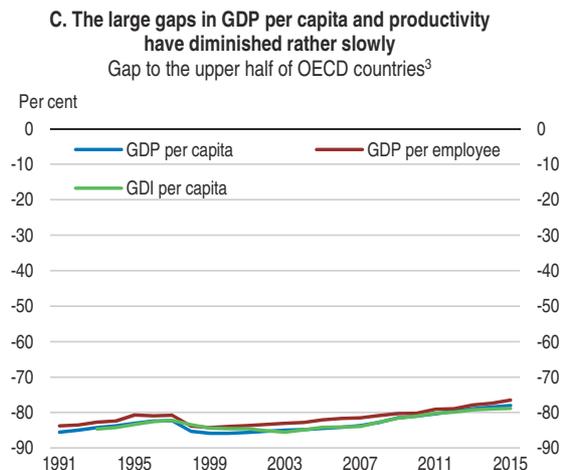
**Actions taken:** A land acquisition regime continues to be refined, which should smooth the way for the development of much needed transport infrastructure investment, including with greater private participation.

## INDONESIA

## Growth performance and inequality indicators

A. Growth		
Average annual growth rates (%)	2003-09	2009-15
GDP per capita	4.1	4.3
Labour utilisation <sup>1</sup>	0.7	0.2
Labour productivity	3.4	4.0

B. Inequality		
	Level	Annual variation (percentage points)
	2014	2008-14
Gini coefficient <sup>2</sup> (rural areas)	31.9	0.3
Gini coefficient <sup>2</sup> (urban areas)	42.8	1.0



- Labour utilisation is defined as the ratio of total employment over population.
- The Gini index measures the extent to which the distribution of disposable income among households deviates from perfect equal distribution. A value of zero represents perfect equality and a value of 100 extreme inequality.
- Percentage gap with respect to the weighted average using population weights of the highest 17 OECD countries in terms of GDP per capita, GDP per employee and GDI per capita (in constant 2010 PPPs).

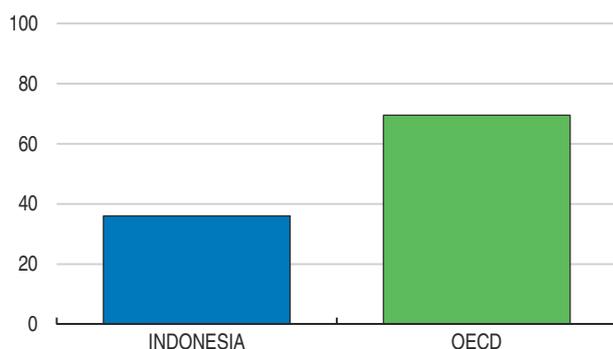
Source: OECD, *National Accounts Database*; World Bank, *World Development Indicators (WDI) Database*; International Labour Organization (ILO), *Key Indicators of the Labour Market (KILM) Database*.

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## Policy indicators

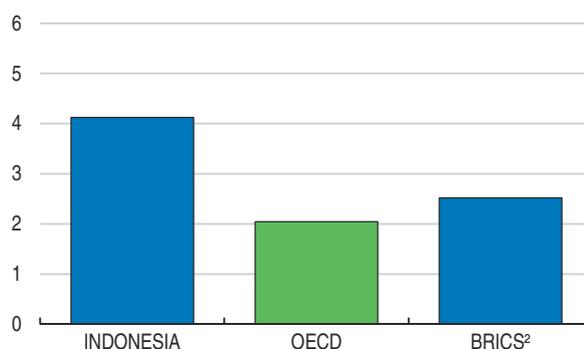
## A. The level of corruption is perceived to be high

Index scale of 0-100 from highest to lowest level of perceived corruption, 2015<sup>1</sup>



## B. Employment protection legislation for regular workers is stringent

Index scale of 0-6 from least to most restrictive, 2012



- The Corruption Perceptions Index aggregates data from a number of different sources that provide perceptions of business people and country experts of the level of corruption in the public sector. Index scale of 0-100 where a 0 equals the highest level of perceived corruption and 100 equals the lowest level of perceived corruption.
- Average of Brazil, China, India, the Russian Federation and South Africa.

Source: Panel A: *Transparency International Database on Corruption Perceptions*; Panel B: *OECD, Employment Protection Legislation Database*.

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## INDONESIA

**Recommendations:** Government spending on infrastructure should continue with a focus on transportation, logistics, and rural infrastructure. Sub-national governments should be encouraged to step up infrastructure spending, including by making greater use of targeted and matching grants. Given looming fiscal constraints, consideration should be given to issuing infrastructure bonds, including allowing sub-national governments to do so.

**Reform labour regulations to reduce informality.** Labour informality at around 50% remains high, excluding workers from security of employment, on-the-job training and social security coverage. Very high severance payments, which at around 58 weeks of wages are far in excess of those in peer countries, and other labour market rigidities, mean that potential employers are reluctant to hire, particularly young and low-skilled workers.

**Actions taken:** In 2015 a cap was put on increases in the minimum wage.

**Recommendations:** Regulations that impede labour market flexibility should be reformed. This includes reducing overly generous severance payments.

**Further reduce energy subsidies.** Subsidies on diesel and electricity, totalling around 7% of total government spending, disproportionately benefit richer households and lead to overconsumption and undesirable environment impacts.

**Actions taken:** Electricity subsidies have been scaled back in 2016.

**Recommendations:** Continue to phase out fuel and electricity subsidies, which will allow a reprioritisation of government spending programmes. Compensate the poor through existing targeted schemes, including the conditional transfer scheme.

**Ease barriers to entrepreneurship and investment, and strengthen institutions to fight corruption.** Businesses, foreign and domestic, face significant barriers to both formation and operation. The Negative Investment List is curtailing competition by restricting foreign investment in certain sectors. Inconsistencies in regulation across levels of government are obstructing investment in the regions. Corruption remains an impediment to business growth and the efficient functioning of the civil service.

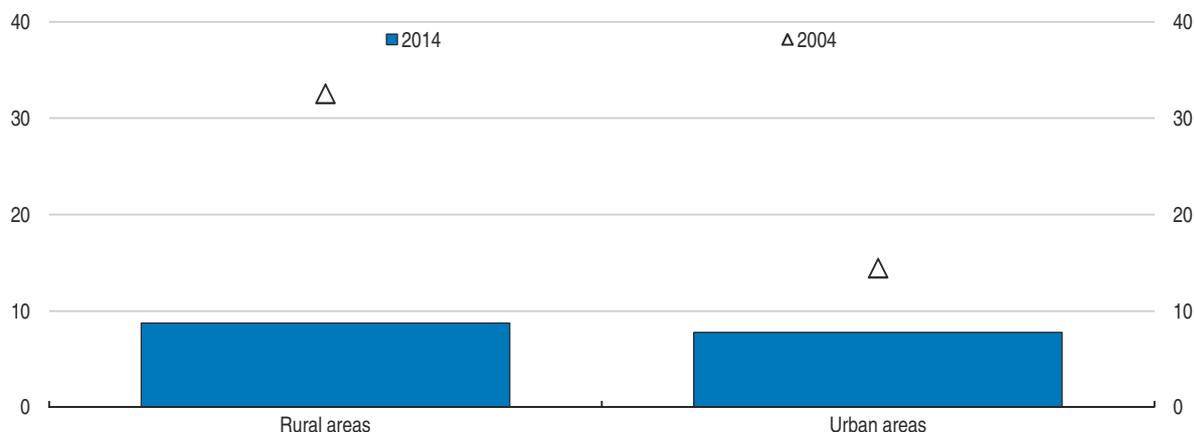
**Actions taken:** Since mid-2015, the government has prioritised reforms aimed at improving the business climate, including streamlining procedures for the setting up and running a business.

**Recommendations:** Continue to streamline business regulation, paying special attention to regulations in sub-national jurisdictions. Ease barriers to foreign investment by removing non-strategic sectors from the Negative Investment List. The fight against corruption needs to be sustained, including by increasing resources to the Corruption Eradication Commission and vigorously defending its independence.

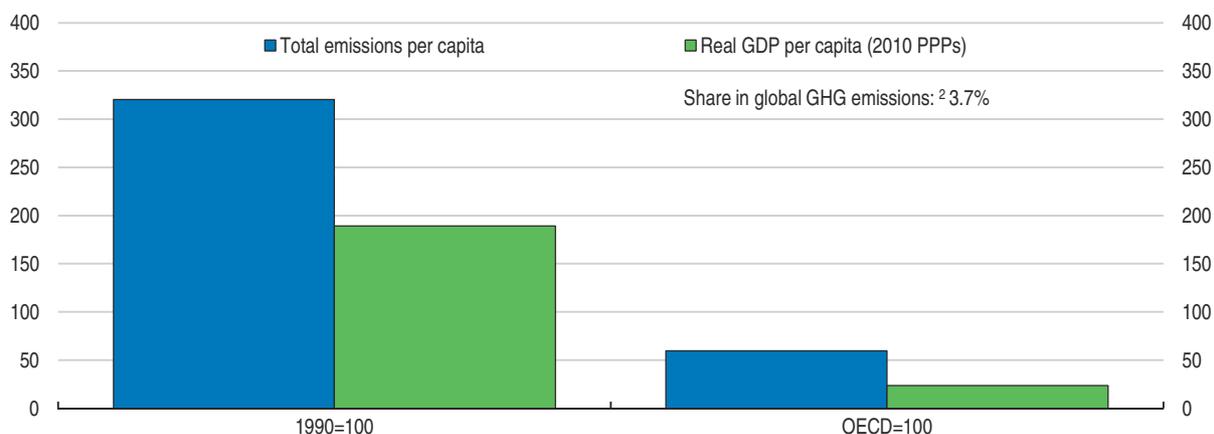
**INDONESIA**

**Beyond GDP per capita: Other policy objectives**

**A. Absolute poverty has significantly decreased in both urban and rural areas**  
 Absolute poverty headcount at the USD 1.9 per day line



**B. Emissions per capita have risen by more than GDP since 1990**  
 2010<sup>1</sup>



1. Total GHG emissions in CO<sub>2</sub> equivalents from the International Energy Agency (IEA) database. This data conform to UNFCCC GHG emission calculations but are not directly comparable to data for Annex I countries due to definitional issues. The OECD average is calculated according to the same definition.

2. Share in world GHG emissions is calculated using International Energy Agency (IEA) 2010 data.

Source: Panel A: World Bank Database; Panel B: OECD, National Accounts and Energy (IEA) Databases, United Nations Framework Convention on Climate Change (UNFCCC) Database.

StatLink <http://dx.doi.org/10.1787/888933456032>