Dealing With Current Account Deficit:
Indonesia’s Experience

Policies for a Sustainable Current Account in Indonesia
OECD Development Center
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Fiscal Policy Agency, Ministry of Finance
Indonesia is a country with relatively high yet stable economic growth. But as an open economy, slowing global growth has adversely impacted Indonesia’s economy; one of them is the widening current account deficit (CAD);

Indonesia’s CAD is caused by both external factors (slowdown in major trading partner and significant decline in commodity prices) and domestic factors (while import is still strong in line with robust domestic economic activities) ➔ external imbalances;

CAD is a reasonable consequence of countries in the development stage like Indonesia, where savings can’t fulfill all investment needs, but it should be (i) managed at a reasonable level, (ii) supported by adequate financing, and (iii) free from structural problems, such as unhealthy fuel subsidy regime, too much reliance on commodity based export, etc.

To manage CAD at a reasonable and sustainable level, government and the relevant authorities have been and will be issuing a series of policy measures, both for short term and and long term.
Indonesia at Glance
Indonesia has demonstrated consistently strong and robust macroeconomic performance...

- According to Moody’s, Indonesia’s peers will grow at 3.6% in 2013

**Strong and Consistent GDP Growth**

<table>
<thead>
<tr>
<th>Year</th>
<th>Real GDP (yoy Growth)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2003</td>
<td>5.3%</td>
</tr>
<tr>
<td>2004</td>
<td>6.5%</td>
</tr>
<tr>
<td>2005</td>
<td>6.1%</td>
</tr>
<tr>
<td>2006</td>
<td>6.8%</td>
</tr>
<tr>
<td>2007</td>
<td>6.3%</td>
</tr>
<tr>
<td>2008</td>
<td>6.0%</td>
</tr>
<tr>
<td>2009</td>
<td>4.6%</td>
</tr>
<tr>
<td>2010</td>
<td>4.3%</td>
</tr>
<tr>
<td>2011</td>
<td>4.1%</td>
</tr>
<tr>
<td>2012</td>
<td>3.7%</td>
</tr>
<tr>
<td>Q3 2013</td>
<td>5.8%</td>
</tr>
<tr>
<td>Outlook</td>
<td>5.7%</td>
</tr>
<tr>
<td>Budget</td>
<td>6.0%</td>
</tr>
</tbody>
</table>

Source: Ministry of Finance, Bank Indonesia, BPS, Moody’s

**Well Diversified Economy**

**GDP by Sector (% of total GDP) as of 30 Sep 2013**

- Financial, Real Estate and Business Services: 24%
- Trade, Hotels and Restaurants: 14%
- Manufacturing: 11%
- Mining and Quarrying: 11%
- Agriculture, Livestock, Forestry and Fisheries: 7%
- Construction: 10%
- Transport and Communications: 6%
- Public Consumption: 5%
- Private Consumption: 4%
- Gross Domestic Fixed Capital Formation: 3%

Source: BPS

(1) Numbers do not add up to 100%

**Manageable Debt Position and Sustainable Fiscal Deficit**

**GDP by Expenditure (% of total GDP) as of 30 Sep 2013**

- Change in Stocks: 9%
- Public Consumption: 6%
- Private Consumption: 65%
- Gross Domestic Fixed Capital Formation: 33%
- Agriculture, Livestock, Forestry and Fisheries: 15%
- Construction: 10%
- Transport and Communications: 6%
- Manufacturing: 7%
- Trade, Hotels and Restaurants: 14%
- Financial, Real Estate and Business Services: 24%

Source: Ministry of Finance

Note: 2013 Total Debt / GDP from 2013 Revised Budget

**Favored by Investors With Increasing Direct Investments**

- 2011 Growth: 20.5%
- 2012 Growth: 24.6%
- 2013 Growth: 18.3%

<table>
<thead>
<tr>
<th>Year</th>
<th>Total: US$27.9bn</th>
<th>Foreign: US$16.8bn</th>
<th>Domestic: US$11.1bn</th>
</tr>
</thead>
<tbody>
<tr>
<td>1Q</td>
<td>4.40</td>
<td>0.80</td>
<td>3.60</td>
</tr>
<tr>
<td>2Q</td>
<td>4.70</td>
<td>0.87</td>
<td>3.83</td>
</tr>
<tr>
<td>3Q</td>
<td>5.16</td>
<td>0.71</td>
<td>4.45</td>
</tr>
<tr>
<td>4Q</td>
<td>5.73</td>
<td>0.71</td>
<td>5.02</td>
</tr>
<tr>
<td>1Q</td>
<td>6.24</td>
<td>0.68</td>
<td>5.56</td>
</tr>
<tr>
<td>2Q</td>
<td>6.29</td>
<td>0.72</td>
<td>5.57</td>
</tr>
<tr>
<td>3Q</td>
<td>6.31</td>
<td>0.78</td>
<td>5.53</td>
</tr>
<tr>
<td>4Q</td>
<td>7.05</td>
<td>1.05</td>
<td>6.00</td>
</tr>
<tr>
<td>1Q</td>
<td>7.17</td>
<td>1.01</td>
<td>6.16</td>
</tr>
<tr>
<td>2Q</td>
<td>6.86</td>
<td>0.80</td>
<td>6.06</td>
</tr>
<tr>
<td>3Q</td>
<td>6.83</td>
<td>0.83</td>
<td>6.00</td>
</tr>
</tbody>
</table>

Source: BKPM

Note: IDR/US$ exchange rate as at end of reporting period.
(1) Cumulative up to 3Q 2013
Indonesia economic growth is much stable compared to others...

Selected ASEAN Members GDP Growth (%yoy)

G-20s, Q3 2013 GDP Growth (%yoy)

Source: WEO, Bloomberg,
Indonesia trade relies heavily on Asian trading partners, whereas non-oil export destinations are still dominated by Asian countries.

**Non oil and Gas Export by Destination Country Jan - Nov 2010**
- **Export to Asian Countries = US$68 billion**

**Non Oil and Gas Import by Country of Origin Jan - Nov 2010**
- **Import from Asian Countries = US$64.6 billion**

**Non Oil & Gas Export by Destination Country Jan - Nov 2013**
- **Export to Asian Countries = US$78.5 billion**

**Non Oil & Gas by Country of Origin Jan - Nov 2013**
- **Import from Asian Countries = US$84.4 billion**
Most non-oil & gas exports are commodity based products such as coal, palm oil, and rubber...

**Major Commodities Export (% of Total Non-Oil & Gas Export)**

Jan – Nov 2013

- **Mining Products Excluding Petroleum & Gas**: 13.3%
- **Agricultural Products**: 2.3%
- **Industrial Products**: 48.6%

**Commodity Export by Value as a share of Total Export by Value, 2012**

- Coal
- Natural gas
- CPO
- Crude oil
- Rubber
- Copper
- Nickel
- Tin

**Source:** World Bank 2013

### Agricultural Products

<table>
<thead>
<tr>
<th>Product Description</th>
<th>Value (US$ millions)</th>
<th>% of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shrimps: Fresh and Frozen</td>
<td>704</td>
<td>0.5</td>
</tr>
<tr>
<td>Coffee</td>
<td>671</td>
<td>0.5</td>
</tr>
<tr>
<td>Fish</td>
<td>625</td>
<td>0.5</td>
</tr>
<tr>
<td>Others Agricultural Products</td>
<td>271</td>
<td>0.2</td>
</tr>
<tr>
<td>Cocoa Beans</td>
<td>252</td>
<td>0.2</td>
</tr>
<tr>
<td>Spices</td>
<td>244</td>
<td>0.2</td>
</tr>
<tr>
<td>Fruits</td>
<td>112</td>
<td>0.1</td>
</tr>
</tbody>
</table>

### Industrial Products

<table>
<thead>
<tr>
<th>Product Description</th>
<th>Value (US$ millions)</th>
<th>% of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vegetable Oil: Palm Oil</td>
<td>9,032</td>
<td>6.6</td>
</tr>
<tr>
<td>Preparation Rubber Products</td>
<td>5,720</td>
<td>4.2</td>
</tr>
<tr>
<td>Garments Products</td>
<td>4,666</td>
<td>3.4</td>
</tr>
<tr>
<td>Electrical Apparatus Products</td>
<td>4,096</td>
<td>3.0</td>
</tr>
<tr>
<td>Processed Food Products</td>
<td>3,079</td>
<td>2.3</td>
</tr>
<tr>
<td>Other Textiles Products</td>
<td>3,020</td>
<td>2.2</td>
</tr>
<tr>
<td>Paper and Paper Goods Products</td>
<td>2,242</td>
<td>1.6</td>
</tr>
<tr>
<td>Chemicals Products</td>
<td>1,989</td>
<td>1.5</td>
</tr>
<tr>
<td>Tin Products</td>
<td>1,429</td>
<td>1.0</td>
</tr>
<tr>
<td>Plywood Products</td>
<td>1,270</td>
<td>0.9</td>
</tr>
</tbody>
</table>

### Mining Products Excluding Petroleum & Gas

<table>
<thead>
<tr>
<th>Product Description</th>
<th>Value (US$ millions)</th>
<th>% of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Coal</td>
<td>14,866</td>
<td>10.9</td>
</tr>
<tr>
<td>Copper Ores and Concentrates</td>
<td>1,305</td>
<td>1.0</td>
</tr>
<tr>
<td>Nickle Ores and Concentrates</td>
<td>901</td>
<td>0.7</td>
</tr>
<tr>
<td>Bauxite</td>
<td>711</td>
<td>0.5</td>
</tr>
<tr>
<td>Other Mining Products</td>
<td>344</td>
<td>0.3</td>
</tr>
</tbody>
</table>

**Note:** Value in US$ millions, % of total non-oil & gas exports
Indonesia Current Account Deficit: Current and Structural Problems
Various factors, both external and domestic, have caused the recent pressures on Current Account deficit...

**Current account deficits**
- Trade Balance deficits:
  - Export: commodity prices, oil lifting
  - Import of oil & gas, Raw materials and capital goods
- Service account deficits (Freight, Insurance)
- Income account deficits (Interest, Dividend)

**Domestic Factors**
- Economic activity
- Investment

**External Factors**
- Global slowdown
- Liquidity risks

**Pressures on Financial Account**
- Portfolio investment
- Direct investment

**Reserves & Exchange rates**

**Inflation**

**Interest rate**

**Yield of Obligation**

**Poverty**

**Unemployment**

**Economic growth**
Indonesia Balance of Payment has recorded deficit for three consecutive quarters, but CAD began to narrow in Q3-2013...

<table>
<thead>
<tr>
<th>ITEM</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Q1</td>
<td>Q2</td>
<td>Q3</td>
</tr>
<tr>
<td><strong>A. CURRENT ACCOUNT</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Goods Trade Balance</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a. Export, fob</td>
<td>45.9</td>
<td>51.8</td>
<td>52.4</td>
</tr>
<tr>
<td>b. Import, fob</td>
<td>-36.6</td>
<td>-42.6</td>
<td>-42.7</td>
</tr>
<tr>
<td>2. Services</td>
<td>-1.8</td>
<td>-3.1</td>
<td>-2.6</td>
</tr>
<tr>
<td>3. Income</td>
<td>-5.5</td>
<td>-6.8</td>
<td>-7.4</td>
</tr>
<tr>
<td>4. Current Transfer</td>
<td>1.0</td>
<td>1.0</td>
<td>1.0</td>
</tr>
<tr>
<td><strong>B. CAPITAL &amp; FINANCIAL ACCOUNT</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1. Capital Account</td>
<td>0.0</td>
<td>0.0</td>
<td>0.0</td>
</tr>
<tr>
<td>2. Financial Account</td>
<td>4.8</td>
<td>11.6</td>
<td>-3.1</td>
</tr>
<tr>
<td>a. Direct Investment</td>
<td>3.8</td>
<td>2.5</td>
<td>2.1</td>
</tr>
<tr>
<td>b. Portfolio Investment</td>
<td>2.9</td>
<td>5.2</td>
<td>-4.6</td>
</tr>
<tr>
<td>c. Other Investment</td>
<td>-1.9</td>
<td>3.9</td>
<td>-0.7</td>
</tr>
<tr>
<td><strong>C. TOTAL (A + B)</strong></td>
<td>7.8</td>
<td>11.9</td>
<td>-2.3</td>
</tr>
<tr>
<td><strong>D. NET ERRORS AND OMISSIONS</strong></td>
<td>-0.1</td>
<td>0.0</td>
<td>-1.6</td>
</tr>
<tr>
<td><strong>E. OVERAL BALANCE (C + D)</strong></td>
<td>7.7</td>
<td>11.9</td>
<td>-4.0</td>
</tr>
<tr>
<td><strong>Reserve Assets Position</strong></td>
<td>105.7</td>
<td>119.7</td>
<td>114.5</td>
</tr>
<tr>
<td>(In months of imports &amp; official debt repayment)</td>
<td>7.5</td>
<td>7.9</td>
<td>7.1</td>
</tr>
<tr>
<td>Current Account (% GDP)</td>
<td>1.5</td>
<td>0.1</td>
<td>0.3</td>
</tr>
<tr>
<td>Debt Service Ratio (%)</td>
<td>18.4</td>
<td>21.9</td>
<td>19.8</td>
</tr>
</tbody>
</table>

Source: Bank Indonesia, Kemenkeu

- The current account deficit began to narrow to a USD8.4 billion (3.8% GDP) compared to the previous quarter at USD10 billion (4.4% GDP). This is a deficit for the 8th consecutive quarter.
- Goods trade deficit fell to USD7 million from USD0.7 billion due to non-oil trade balance improvement.
- The capital and financial account surplus fell to USD4.9 billion as weakening portfolio and other investments
- FX reserves at the end of Dec 2013 has improved to US$ 99.4 billion
Current Account turned to deficit starting at the end of 2011 due to declining export while import is still solid...

- CA turned to be deficit due to deficit in goods trade balance.
- Export was slowdown, mostly because of declining price, while export volume was quite stable.
- As domestic market expanded, import has been increasing, especially raw materials (76% of total import) and capital goods (17% of total import).

*Source: Bank Indonesia, Kemenkeu*
The widening of current account deficit is mainly due to deterioration of goods trade balance, especially oil and its products, combined with other accounts (Service and Income Accounts)...

- Extensive trade balance deficits are mainly caused by higher imports growth than export growth, particularly in oil and gas.
- Increasing fuel subsidy in 2013 was caused by increased oil and gas import and consumption.
The service account has been deficit for years, that is in line with deficit in the transportation sector (freight) caused by the increasing trends in import-export activities and insurance business...

- The service account tends to move in line with export-import.
- Freight services deficit → increasing payments to foreign shipping and airline companies due to lack domestic capacity
- Insurance services deficit → the use of foreign insurance services in trade and transportation sectors, most of the risk from domestic insurance company is absorbed by foreign reinsurers
The income account has also been deficit for years...

Indonesia Income Account Deficits (USD Billion)

- Compensation of Employees
- Investment Incomes
- Total Income Account Deficits
- FDI

Rising income deficit due to growing FDI income (growing profitability) as a result of increase in FDI → This is partly funded by reinvested earnings of foreign-owned companies

2013* as of September/Q3
Direct investment (net FDI) has increased while CA deficit started to worsen, resulting in the widening basic balance deficit.
Although the recent trend of portfolio investment is still increasing, but it still can’t fully support the financing needs for CAD...

Average annual portfolio investment in 2012-2013 is around USD9.0 billion, although it is still relatively volatile. On the other hand, the annual average basic balance deficits is USD11.0 billion, implying there is still financing deficit to support CAD.
Emerging economies, including Indonesia, are still vulnerable, with the risks mostly coming from external side...

Some Emerging Economies Indicators

<table>
<thead>
<tr>
<th>3Q 2013</th>
<th>Brazil</th>
<th>Indonesia</th>
<th>India</th>
<th>Afrika Selatan</th>
<th>Turki</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP (% yoy)</td>
<td>2.2</td>
<td>5.8</td>
<td>5.3</td>
<td>1.8</td>
<td>4.7</td>
</tr>
<tr>
<td>Inflation (% yoy)</td>
<td>6.1</td>
<td>8.6</td>
<td>10.8</td>
<td>6.3</td>
<td>8.3</td>
</tr>
<tr>
<td>Unemployment Rate (%)</td>
<td>5.3</td>
<td>6.3</td>
<td>4.7</td>
<td>24.7</td>
<td>9.9</td>
</tr>
<tr>
<td>Fiscal Deficits (% PDB)</td>
<td>(2.5)</td>
<td>(1.9)</td>
<td>(7.0)</td>
<td>(5.2)</td>
<td>(3.0)</td>
</tr>
<tr>
<td>Current Account (% PDB)</td>
<td>(3.7)</td>
<td>(3.8)</td>
<td>(1.2)</td>
<td>(6.8)</td>
<td>(7.7)</td>
</tr>
<tr>
<td>Exc. Rates (% QtoQ)</td>
<td>(15.9)</td>
<td>(16.9)</td>
<td>(15.0)</td>
<td>(5.2)</td>
<td>(10.4)</td>
</tr>
<tr>
<td>Foreign Reserves</td>
<td>364.5</td>
<td>97.0</td>
<td>277.2</td>
<td>49.3</td>
<td>134.2</td>
</tr>
<tr>
<td>Debt to GDP</td>
<td>19.4</td>
<td>24.0</td>
<td>49.6</td>
<td>40.0</td>
<td>45.9</td>
</tr>
</tbody>
</table>

Sources: IMF December 2013, World Bank, EIU, Kementerian Keuangan RI, BPS, Biro Statistik Brazil India, Afrika Selatan dan Turki
Note: Data adalah untuk 3Q2013 kecuali for fiscal balance, exchange rate and Rasio Utang PDB yang merupakan angka 2013.

Cadangan devisa merupakan angka terakhir di bulan Desember 2013

- In 2012, the Indonesia CAD could still be financed by FDI and portfolio activities, while in 2013, those sources couldn’t catch up with the CAD
- The problem is not unique for Indonesia, other countries such as S. Africa, Thailand, and Turkey also experienced CAD together with its financing
- Due to current financial turbulence, most emerging economies mostly face the inflation pressure, CAD, Fiscal Deficits, and/or volatility of exchange rates.
Policy Packages to Deal with Current Account Deficit Problems
To deal with the CAD problems, the government of Indonesia has taken some fiscal policy measures...

Additional budget for social protection and infrastructure:
- Conditional Cash Transfer ("PKH"): IDR0.7tn
- Unconditional Cash Transfer ("BLSM"): IDR9.3tn
- Poor Students Aid ("BSM"): IDR7.5tn
- Additional allocation of rice for the poor ("Raskin"): IDR4.3tn
- Basic infrastructure development: IDR7.2tn
- Implementing higher deficit for expansionary reason. Deficit is revised from 1.7% to 2.4%

Support of Small and Medium Enterprise:
- Simplification of Business License application process
- Easier access to electricity
- Improved access to loans
- Support for the simplification of regulations regarding Bankruptcy Settlement, Recording of Land & Building Rights and Recording of Land & Building Ownership

1. Additional income tax for selected goods. The criteria includes:
   - Goods not used for domestic industries
   - Household consumption goods
   - Non-inflationary goods.
2. Additional relaxation of goods imported for export activity
   The package is to be fully implemented by January 2014

2013 Revised Budget
- June
- July

Subsidized Fuel Price Adjustment
- Subsidized fuel prices increased by 44.4% per liter for gasoline and 22.2% per liter for diesel

2014 Budget

Macroeconomic Assumption | 2013 Revised Budget | 2014 Budget
---|---|---
Growth (%) | 6.3 | 6.0
Inflation (%) | 7.2 | 5.5
Exchange Rate (IDR / US$) | 9,600 | 10,500
Interest Rate (SPN 3 months) (%) | 5.0 | 5.5
ICP (US$ / barrel) | 108 | 105
Oil and gas Lifting
  a. Oil Lifting (MBCD) | 840 | 870
  b. Gas Lifting (MBOEPD) | 1,240 | 1,240

2014 Key Government Policies
- Government capital expenditure to support economic growth
- Support of infrastructure development guarantees
- Government incentives with respect to investments
- Price stabilization policies to maintain purchasing power
- Improvements to the Negative Investment List (DNI)
- Increase productivity through incentives for R&D activity and training as well as Social Security and Labor Policy

August Policy Package
- October Policy Package
- December Policy Package
- 2014 Policy Package
- 2013 Revised Budget
- 2014 Budget
- Macroeconomic Assumption
- 2014 Key Government Policies
Central Bank (BI) has also issued some monetary policies...

<table>
<thead>
<tr>
<th>Date</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jun 11, 2013</td>
<td>- Deposit Facility (&quot;DF&quot;) Rate ↑ by 25bps to 4.25%</td>
</tr>
<tr>
<td>Jul 18, 2013</td>
<td>- FX Swap initial offering</td>
</tr>
<tr>
<td>Aug 23, 2013</td>
<td>- Extension of FX TD maturity</td>
</tr>
<tr>
<td>Aug 29, 2013</td>
<td>- BI Rate ↑ by 50bps to 7.00%, DF Rate ↑ by 50bps to 5.25%, Lending Facility Rate ↑ by 25bps to 7.00%</td>
</tr>
<tr>
<td>Oct 8, 2013</td>
<td>- Maintain BI Rate at 7.25%, Establish a bilateral KRW/IDR swap arrangement worth USD10bn</td>
</tr>
<tr>
<td>Dec 13, 2013</td>
<td>- Expand BSA between BI and BoJ to USD22.76bn</td>
</tr>
<tr>
<td>Jun 13, 2013</td>
<td>- BI Rate ↑ by 25bps to 6.00%, maintaining DF Rate at 4.25% and Lending Facility (&quot;LF&quot;) Rate at 6.75%</td>
</tr>
<tr>
<td>Jul 11, 2013</td>
<td>- BI Rate ↑ by 50bps to 6.5%, DF Rate ↑ by 50bps to 4.75% and maintain LF Rate at 6.75%</td>
</tr>
<tr>
<td>Aug 15, 2013</td>
<td>- Maintain BI rate at 6.5%</td>
</tr>
<tr>
<td>Aug 23, 2013</td>
<td>- Issuance of SDBI</td>
</tr>
<tr>
<td>Aug 29, 2013</td>
<td>- Rising Reserve Requirement (RR) and – LDR to 78% - 92% (starting on Dec 1, 2013)</td>
</tr>
<tr>
<td>Sep 12, 2013</td>
<td>- BI Rate ↑ by 25bps to 7.25%, DF Rate ↑ by 25bps to 5.5% and maintain LF Rate at 7.25%</td>
</tr>
<tr>
<td>Oct 1, 2013</td>
<td>- Extend BSA between BI and BoC worth USD15bn</td>
</tr>
<tr>
<td>Nov 12, 2013</td>
<td>- BI Rate ↑ by 25bps to 7.50%, DF Rate ↑ by 25bps to 5.75% and LF Rate to 7.50%</td>
</tr>
</tbody>
</table>

Pre-Emptive and Bold Measures in Policy Rate to help Drive Down Current Account Deficit...

... Supported by a Comfortable Foreign Exchange Reserve Cushion

Source: Bank Indonesia
Some Results of Recent Initiatives
Recent Initiatives have so far shown some promising results...

**Surplus Trade Balance in November – Highest in 20 Months**

- **(US$mm)**
  - 2010: 0
  - 2011: 12,000
  - 2012: 17,000
  - 2013: 23,000

Source: BPS

**Rebounding Financial Account Capital Flows**

- **(US$mm)**
  - Q1 2011: 0
  - Q2 2011: 3,000
  - Q3 2011: 6,000
  - Q4 2011: 9,000
  - Q1 2012: 12,000
  - Q2 2012: 15,000
  - Q3 2012: 12,000
  - Q4 2012: 9,000
  - Q1 2013: 6,000
  - Q2 2013: 3,000

- **Yield (%)**
  - Q1 2011: 0
  - Q2 2011: 3%
  - Q3 2011: 6%
  - Q4 2011: 9%
  - Q1 2012: 12%
  - Q2 2012: 15%
  - Q3 2012: 12%
  - Q4 2012: 9%
  - Q1 2013: 6%
  - Q2 2013: 3%

Source: Bank Indonesia

**Inflation Stabilization Following Fuel Price Adjustment Policy**

- **CPI (% yoy)**
  - 2010: 11.8%
  - 2011: 5.0%
  - 2012: 8.4%
  - 2013: 8.3%

- **US$mm**
  - 2011: 1,000
  - 2012: 2,000
  - 2013: 3,000

Source: Bank Indonesia

**Stabilization of Onshore Yields**

- Outstanding government bonds held by foreign investors (LHS)
  - DMO buyback 10 June 2013
  - DMO buyback 20 June 2013
  - BI buyback 12 June 2013

- Yield (%)
  - 2010: 0
  - 2011: 3
  - 2012: 6
  - 2013: 9

Source: Bank Indonesia, Bloomberg

**Stabilization of Foreign Exchange Market**

- Convergence between offshore NDF and spot rate

Source: Bank Indonesia
Outlook of 2013/2014 Current Account Deficit and short term policy direction...

• With the issuance of policy measures by the government and BI as well as better global economic condition, the 2013 CAD is estimated to be 3.3%-3.6% of GDP and for 2014 will be 2.5% - 3.0% of GDP.

• Short term 2014 policies in pipeline:
  – Trade Account Deficit → improving the fuel subsidy through price adjustments or applying the fixed subsidy policy, and controlling fuel consumption through (i) fuel restriction/rationing policy, (ii) implementing gas-fuel conversion program, (iii) and encouraging the use of alternative energy → the mandatory level of biodiesel policy in diesel fuel
  – Service Account Deficit → merging a number of insurance SOEs to create a more powerful and well capitalized local insurance company
  – Income Account Deficit → providing tax incentive for companies that reinvest their profit (retained earnings) in Indonesia

• Up side risks → the raw (ore) minerals export ban policy
  – In the short term, this policy may increase the trade balance deficit, but in the medium/long term, it is expected to increase the value of export
Medium Term Challenges and Policy Direction: Continuous Structural Reform
Medium Term Development Challenges

Global Challenges
- Risks from global and major trading partner uncertainty
- Liquidity pressures
- Price volatility

Domestic Challenges
- Domestic Economy performances below its potential growth
- Production capacities constraint
- Supply bottleneck
- Overheating risks

Economic Resiliency
- Import dependency → capital goods and raw materials
- Commodities export → price volatility
- Food and energy security

Global Competitiveness
- Infrastructure facilities (energy, roads and port)
- Human resources capacity
- Technology and innovation
- Bureaucracy systems and procedures, and interlinkage regulations

Current Account Deficits
- Decreasing in oil lifting and external demand
- Increasing trend of oil and gas import to support investment activities
- The widening of trade balance deficits
- Current account deficits and exchange rates pressures

Financial Stability
- Relatively high foreign ownership → vulnerable to negative sentiments and sudden reversal risks
- Private sector’s foreign debt is increasing as a result of financing needs → debt risks increases
- Regulation frameworks to encounter these issues.

Fiscal
- Limited fiscal space – too much mandatory pending
- Narrowed tax base
- Quality spending
- Sensitive to external shocks
- Large portion of energy subsidy.

Other Relevant Issues
- Poverty
- Unemployment
- Inequality
- Health and education facilities
Medium Term Policy Directions

**Strengthening domestic economy**
- Increase productivity
- Increase domestic goods competitiveness
- Improve institutional capacity and human resources quality
- Maintain macro stability and fiscal sustainability
- Assure food and energy security

**Increasing production capacity and managing supply sides**
- Improve investment climate
- Increase national production capacity
- Improve infrastructures facilities
- Support development of technology and innovation
- Enhance financial deepening and financial inclusion

**Reducing poverty and improving income distribution**
- Improve health and education facilities
- Improve financial support for SME’s
- Provide social security for all people
Thank you