Indonesia's strategy for growth

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Entering 2016, the global economy continues its period of uncertainty that has lingered since the global financial crises of 2008. With global growth declining and inflation remaining low, another sign of ambiguity in the global economy has emerged, which is the divergence of economic and monetary policies among major economies.

Pressures in the financial markets at the beginning of 2016, in the midst of an uncertain bottoming-out of oil prices, have added to concerns about global growth. Conversely, the deteriorating macroeconomic outlook and worries about medium-term vulnerabilities in the global economy have unsettled financial markets. With financial institutions under renewed pressure, adverse feedback effects between finance and the real economy could become significant. The emerging economies have withstood the recent global economic turmoil by taking advantage of credit-fuelled growth as a spill-over effect from lax, accommodative monetary policy in the advanced economies. Put simply, we may face a period of emerging market-originating spillbacks, from the previous emerging market-receiving spill-overs.

Despite tangible results from efforts to increase resilience to external shocks, the vulnerability of emerging economies remains, due to their rather weak economic structure. Indonesia's economy, in particular, has managed to pick up its growth in 2015 with the help of increased government consumption on goods and investment in infrastructure projects.

In the meantime, dissipating global economic uncertainty and improved confidence in Indonesia's economy have led to a surplus in the capital and financial accounts during the last quarter of 2015, bolstered by an increase in foreign capital inflows, mainly to government securities.

This confidence in Indonesia's economy also contributed to a more stable rupiah, with an upward trend and less volatility, while foreign exchange reserves still hover well above the international standards. Moreover, the low global prices amid weakened domestic demand also caused domestic CPI inflation to slow down.

Against the background of maintained stability, with carefully monitored vulnerabilities, we are still optimistic that domestic economic growth will be slightly higher in 2016, supported by the acceleration of infrastructure projects on the fiscal side, and increased private investment as a result of government policy packages and measurable monetary easing while maintaining macroeconomic stability. Inflation is expected to be at around of the 4.1 per cent inflation target, with the current account deficit projected to be below 3 per cent of GDP.

Infrastructure issues pose a major constraint for Indonesia's accelerated growth. Connectivity issues among regions, including the need for high-quality and high-capacity sea ports, airports, roads and railways in Indonesia have spurred logistical costs. Import/export-related manufacturing activities are especially in need of seven appropriate ports, even for Java region which contributes the lion's share to the national economy.

In addition, energy – particularly electricity – also becomes a crucial issue, and serves as important prerequisite for domestic industry's development. A reliable and adequate supply of electricity would attract investors' interest to build manufacturing facilities in Indonesia. This increased foreign direct investment will also enhance Indonesia's role within the global value chain. Bank Indonesia has found that a modest increase in electricity capacity and human development will each enhance growth by around 0.25 per cent per year, while enhancement in the quality of human capital will contribute to an increase in employment of around 0.5 per cent.

To address the existing challenges, I believe we have come to a common understanding that reforms to improve the economic structure should be underlined and properly implemented. Cyclical policies from the monetary and fiscal domains remain indispensable, but are not sufficient on their own, as they only respond to short-term recurrent symptoms. Thus far, Bank Indonesia's monetary and macro-prudential policies have been among the key factors in safeguarding macroeconomic stability, which support the structural reforms pursued by both the central and regional governments.

To address infrastructure problems, providing sufficient land for power plants, improving the business climate for investment in infrastructure, and enhancing regional tax collection, as well as public-private partnership to raise funds for infrastructure projects, should become priority policies for implementation.

In conclusion, a good balance of monetary, fiscal and structural reform will take the country many steps forward toward faster and more sustainable growth. F