1 Indonesia

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I. Introduction

The name of “Indonesia”, formerly known as the https://www.britannica.com/place/Dutch-East-Indies (or Netherlands East Indies), is derived from historical sequences that occurred in the middle of 19th century. Indonesia did not become the country’s official name until the time of independence. Some historical manuscripts revealed that Indonesia is a set of islands that spread between Indo-China and Australia by various names. Eduard Douwes Dekker (1820-1887), known as “Multatuli”, cited Indonesia as Indian islands. On the other side, “Indonesia”, this name means Indian Islands, invented by J. R. Logan, in Malaya in 1850. Taken from the Greek, *indos*, meaning “India”, and nesos, meaning “island”, it has parallels in Melanesia, meaning "black islands"; Micronesia, meaning "small islands"; and Polynesia, "many islands." A German geographer, Adolf Bastian, used it in the title of his book, Indonesien, in 1884. Thus, Indonesian nationalists adopted it as the name of their nation in 1928.

Consisted of more than 17,000 islands (8,844 named and 922 permanently inhabited), Indonesian lands spread out between two big continents Asia and Australia and are located off the coast of mainland Southeast Asia in the Indian and Pacific oceans. The country share land borders with Papua New Guinea to the east, East Timor to the south, and the eastern part of Malaysia to the north. Other neighboring countries include Singapore, Vietnam, and Philippines to the north, Australia to the south, Palau to the northeast, and India's Andaman and Nicobar Islands to the northwest. Indonesia is an archipelago that lies across the Equator and spans a distance equivalent to one-eighth of Earth’s circumference.

After Indonesia’s independence day in August 17th 1945, the national anthem titled “Indonesia Raya” have been sung by children throughout the country to begin the school day, by civil servants at flag-raising ceremonies, over the radio to begin and close broadcasting; in cinemas and on television and at national day celebrations since 1950. Radio and television, government owned and controlled for much of the second half of the twentieth century, produced nationalizing programs as diverse as Indonesian language lessons, regi`onal and ethnic dances and songs, and plays on national themes. Officially recognized "national heroes" from diverse regions are honored by schools and biographies and with statues for their struggles against the Dutch; some regions monumentalize local heroes of their own.

Indonesia is a unitary state that called “Negara Kesatuan Republik Indonesia” (The Unitary States of The Republic of Indonesia). It extended from west to east (Sabang to Merauke) and from north to south (Mianggas to Rote Island). After its independence day, Indonesia founding fathers decided that unitary state is an ideal form for Indonesia. It was not easy for them to establish unitary state because Indonesia was Dutch’s colony. Through some diplomacies and conferences, Dutch recognized Indonesia’s sovereignty as unitary state in Round Table Conference (Konferensi Meja Bundar) in December 27th 1949.

The national motto of Indonesia is the “Bhinneka Tunggal Ika”, an old Javanese expression usually translated as "unity in diversity." The concept is that this country always united even the country's citizen divide themselves along a vast slew of ethnicities, clans, tribes and even castes. The nation's official ideology, first formulated by President Sukarno in 1945, is the Pancasila, or Five Principles: belief in one supreme God; just and civilized humanitarianism; Indonesian unity; popular sovereignty governed by wise policies arrived at through deliberation and representation; and social justice for all Indonesian people.

I.1 History and Culture

The modern of Indonesia begins in the period from 2500 BC to 1500 BC with a wave of light brown-skinned Austronesia immigrants, thought to have originated in Taiwan. This Neolithic group of people, skilled in open-ocean maritime travel and agriculture are believed to have quickly supplanted the existing, less-developed population. Indonesian archipelago history has been influenced by foreign powers drawn to its natural resources. Muslim traders and Sufi scholars brought the now-dominant Islam, while European powers brought Christianity and fought one another to monopolize trade in the Spice Islands of Maluku during the Age of Discovery. Although sometimes interrupted by the Portuguese, French and British, the Dutch were the foremost European power for much of their 350-year presence in the archipelago. In the early 20th century, the concept of "Indonesia" as a nation-state emerged, and the independence movement began to take shape. At the end of World War II, Indonesia proclaimed its independence in 1945. However, it was not until 1949 that the Netherlands recognized Indonesia's sovereignty following an armed and diplomatic conflict between the two.

Most islands are multiethnic, with large and small groups forming geographical enclaves. Towns within such enclaves include the dominant ethnic group and some members of immigrant groups. Large cities may consist of many ethnic groups; some cities have a dominant majority. Regions, such as West Sumatra or South Sulawesi, have developed over centuries through the interaction of geography (such as rivers, ports, plains, and mountains), historical interaction of peoples, and political-administrative policies. Some, such as North Sumatra, South Sulawesi, and East Java are ethnically mixed to varying degrees; others such as West Sumatra, Bali, and Aceh are more homogeneous. Some regions, such as South Sumatra, South Kalimantan, and South Sulawesi, share a long-term Malayo-Muslim coastal influence that gives them similar cultural features, from arts and dress to political and class stratification to religion. Upland or upriver peoples in these regions have different social, cultural, and religious orientations, but may feel themselves or be perforce a part of that region. Many such regions have become government provinces, as are the latter three above. Others, such as Bali, have not.

There is no one unified Indonesian culture as such, but the Hindu culture of the former Majapahit empire does provide a framework for many of the cultural traditions found across the central islands of Sumatra, Java, Bali and Lombok. Perhaps the most distinctively "Indonesian" arts are wayang kulit shadow puppetry, where intricately detailed cutouts act out scenes from the Mahabharata and Ramayana and other popular folk stories, and its accompaniment the gamelan orchestra, whose incredibly complex metallic rhythms are the obligatory backdrop to both religious ceremonies and traditional entertainment. Modern-day Indonesian popular culture is largely dominated by the largest ethnic group, the Javanese.

Indonesia consists of 34 provinces. Each province has its own culture. It could be looked at from Traditional houses, cultural events, traditional clothing, folk songs, local languages, traditional dances and some local wisdom. Regarding language, National language is Indonesian (Bahasa Indonesia). Indonesian has been united Indonesia from communication perspective formally even though local people still use local language informally. Indonesia still upholds hierarchy in daily life continuously. Hierarchy is very important in Indonesian society and people's status should be respected at all times. Status is mainly based on a person's age and (job) position. Most Indonesians - but in particular those of higher status - should be addressed with a specific title (Bapak for men and Ibu for women). This can be in combination with their name (Bapak Aditya, meaning “Mr. Aditya”) or position (Bapak Presiden, meaning “Mr. President”). These titles should continuously be used when talking to a person of higher or similar status. And it is always good to talk in a subtle (almost soft) manner. Like other Asian countries, personal relationship is very important for Indonesian people like building business relationship, involving in social community and Working Together (Gotong Royong).

Indonesia has the largest Muslim population of any country in the world, and many ethnic groups are exclusively Muslim, where religious and ethnic differences may be related. Dutch policy allowed proselytization by Protestants and Catholics among separate groups who followed traditional religions; thus today many ethnic groups are exclusively Protestant or Roman Catholic. They are heavily represented among upriver or upland peoples in North Sumatra, Kalimantan, Sulawesi, Maluku, and the eastern Lesser Sundas, though many Christians are also found in Java and among the Chinese. Tensions arise when groups of one religion migrate to a place with a different established religion. Political and economic power becomes linked to both ethnicity and religion as groups favor their own kinsmen and ethnic mates for jobs and other benefits.

I.2 Geography and Climate

Indonesia lies between latitudes 11°S and 6°N, and longitudes 95°E and 141°E. It is the largest archipelagic country in the world, extending 5,120 kilometers (3,181 mi) from east to west and 1,760 kilometers (1,094 mi) from north to south. According to the country's Coordinating Ministry for

Maritime Affairs, Indonesia has 17,504 islands (16,056 of which are registered at the UN), scattered over both sides of the equator, and with about 6,000 of them inhabited. Indonesia also has 34 provinces that located along with 108,000 kilometers of beaches, and each province has its own capital cities as shown in Table 1.

Table 1: Provinces and Capital Cities

Name of Province	Name of Capital City
Nanggroe Aceh Darusalam	Banda Aceh
Sumatera Utara (North Sumatra)	Medan
Sumatera Barat (West Sumatra)	Padang
Riau	Pekanbaru
Kepulauan Riau (Riau Islands)	Tanjung Pinang
Jambi	Jambi
Bengkulu	Bengkulu
Sumatera Selatan (South Sumatra)	Palembang
Kepulauan Bangka Belitung (Bangka Belitung Islands)	Pangkal Pinang
Lampung	Lampung
Banten	Serang
DKI Jakarta	**Jakarta** (Indonesia’s Capital City)
Jawa Barat (West Java)	Bandung
Jawa Tengah (Central Java)	Semarang
Special Region of Yogyakarta	Yogyakarta
JawaTimur (East Java)	Surabaya
Bali	Denpasar
Kalimantan Barat (West Kalimantan)	Pontianak
Kalimantan Tengah (Central Kalimantan)	Palangkaraya
Kalimantan Selatan (South Kalimantan)	Banjarmasin
Kalimantan Timur (East Kalimantan)	Samarinda
Kalimantan Utara (North Kalimantan)	Tarakan
Sulawesi Barat (West Sulawesi)	Mamuju
Sulawesi Selatan (South Sulawesi)	Ujung Pandang
Sulawesi Tengah (Central Sulawesi)	Palu
Sulawesi Utara (North Sulawesi)	Manado
Sulawesi Tenggara (South East Sulawesi)	Kendari
Gorontalo	Gorontalo
Nusa Tenggara Barat (West Nusa Tenggara)	Mataram
Nusa Tenggara Timur (East Nusa Tenggara)	Kupang
Maluku	Ambon
Kepulauan Maluku Utara (North Maluku Islands)	Sofifi
Papua Barat (West Papua)	Manokwari
Papua	Jayapura

Indonesia consists of all or part of some of the world's largest islands—Sumatra, Java, most of Kalimantan (Borneo, shared with Brunei and Malaysia), Sulawesi (Celebes), Halmahera, the west half of New Guinea (Papua, shared with Papua New Guinea), and East Timor on the island of Timor, and maritime borders with Singapore, Malaysia, Vietnam, the Philippines, Palau, and Australia - and numerous smaller islands, of which Bali (just east of Java) is best known.

The Puncak Jaya Mountain is Indonesia's highest peak at 4,884 meters (16,024 ft.) and Lake Toba in North Sumatra is the largest lake with an area of 1,145 km2 (442 sq. mi). Indonesia's largest rivers are in Kalimantan and New Guinea and include Kapuas, Barito, Mamberamo, Sepik and Mahakam. They serve as communication and transport links between the island's river settlements.

The Ring of Fire Indonesia has more than 400 volcanoes, of which 130 are considered active, as well as many undersea volcanoes. The island of New Guinea (on which the Indonesian province of Papua is located) is the second largest island in the world. Here are some main islands in Indonesia:

- Sumatra (incl. the Riau Islands and Bangka-Belitung), wild and rugged, the 6th largest island in the world has a great natural and cultural wealth with more than 40 million inhabitants. It is habitat for many endangered species.
- Kalimantan (Borneo), the vast majority of this, the world's third largest island, is covered by the Indonesian province. Uncharted jungles, mighty rivers, home of the orangutan, a paradise for the adventurer.
- Java (and Madura), the country's heartland, big cities including the capital Jakarta, and a lot of people packed on this island. Also features the cultural treasures of Yogyakarta, Borobudur temple and Prambanan temple.
- Bali, by far the most popular visitor destination in Indonesia, Bali's blend of unique culture, legendary beaches, spectacular highland regions and unique underwater life make it a perennial favorite amongst global travelers.
- Sulawesi (Celebes), strangely shaped, this island houses a diversity of societies and some spectacular scenery, Toraja culture, rich flora and fauna, world class diving sites.
- Nusa Tenggara, also known as the Lesser Sunda Islands, the "Southeast Islands", contain scores of ethnic groups, languages and religions, as well as Komodo lizards and more spectacular diving.
- Maluku (Moluccas), the historic Spice Islands, fought over to this day, largely unexplored and almost unknown to the outside world.
- Papua (Irian Jaya), the western half of the island of New Guinea, with mountains, forests, swamps, an almost impenetrable wilderness in one of the most remote places on earth.

Indonesia is a warm place. It has no spring, summer, autumn, or winter, just two seasons: rainy and dry, both of which are relative (it still rains during the dry season, it just rains less). While there is significant regional variation, in most of the country (including Java and Bali) the dry season is April to October, while the wet season is November to March. In the highlands temperatures will naturally be cooler, and there are even snow-covered peaks in Papua, whose mountains can soar above 5000 meter.

Since the country is very large, Indonesia is divided into three time zones:

GMT +7: Western Indonesian Time (WIB, *Waktu Indonesia Barat*) Sumatra, Java, West/Central Kalimantan.

GMT +8: Central Indonesian Time (WITA, *Waktu Indonesia Tengah*) Bali, South/East Kalimantan, Sulawesi, Nusa Tenggara.

GMT +9: Eastern Indonesian Time (WIT, *Waktu Indonesia Timur*) Maluku, Papua.

I.3 Demography

In 2018, Indonesia has more than 265 million populations. The population is unevenly spread throughout the islands within a variety of habitats and levels of development, ranging from the megalopolis of Jakarta to tribes in Papua Provinces are usually grouped around larger islands and include smaller surrounding islands. Indonesia also has the world's largest Muslim population. Ethnically it is highly diverse, with more than 300 local languages. The people range from rural hunter-gatherers to a modern urban elite. To get appropriate the fixed number of population, Indonesia government carries out population census every ten years.

The 2010 census recorded Indonesia's population as 237.6 million, with high population growth at 1.9%. Fifty-eight per cent of the population lives in Java, the world's most populous island. The population density is 138 people per km2 (357 per sq. mi), ranking 88th in the world, although Java has a population density of 1,067 people per km2 (2,435 per sq mi). The spread of the population is uneven throughout the islands with a varying habitat and level of development, ranging from the megalopolis of Jakarta to uncontacted tribes in Papua. In 1961, the first post-colonial census recorded a total of 97 million people. It is expected to grow to around 295 million by 2030 and 321 million by 2050. The country currently possesses a relatively young population, with a median age of 30.2 years (2017 estimate). About 8 million Indonesians live overseas; most settled in Malaysia, the Netherlands, Saudi Arabia, the United Arab Emirates, Hong Kong, Singapore, the United States, and Australia. The table 2 below shows the distribution of populations from 1971 until 2010 by provinces:

Table 2: Distribution of Population

Province	Population					
	1971	1980	1990	1995	2000	2010
Aceh	2,008,595	2,611,271	3,416,156	3,847,583	3,930,905	4,494,410
Sumatera Utara	6,621,831	8,360,894	10,256,027	11,114,667	11,649,655	12,982,204
Sumatera Barat	2,793,196	3,406,816	4,000,207	4,323,170	4,248,931	4,846,909
Riau	1,641,545	2,168,535	3,303,976	3,900,534	4,957,627	5,538,367
Jambi	1,006,084	1,445,994	2,020,568	2,369,959	2,413,846	3,092,265
Sumatera Selatan	3,440,573	4,629,801	6,313,074	7,207,545	6,899,675	7,450,394
Bengkulu	519,316	768,064	1,179,122	1,409,117	1,567,432	1,715,518
Lampung	2,777,008	4,624,785	6,017,573	6,657,759	6,741,439	7,608,405
Kepulauan Bangka Belitung	-	-	-	-	900,197	1,223,296
Kepulauan Riau	-	-	-	-	-	1,679,163
DKI Jakarta	4,579,303	6,503,449	8,259,266	9,112,652	8,389,443	9,607,787
Jawa Barat	21,623,529	27,453,525	35,384,352	39,206,787	35,729,537	43,053,732
Jawa Tengah	21,877,136	25,372,889	28,520,643	29,653,266	31,228,940	32,382,657
DI Yogyakarta	2,489,360	2,750,813	2,913,054	2,916,779	3,122,268	3,457,491
Jawa Timur	25,516,999	29,188,852	32,503,991	33,844,002	34,783,640	37,476,757
Banten	-	-	-	-	8,098,780	10,632,166
Bali	2,120,322	2,469,930	2,777,811	2,895,649	3,151,162	3,890,757
Nusa Tenggara Barat	2,203,465	2,724,664	3,369,649	3,645,713	4,009,261	4,500,212
Nusa Tenggara Timur	2,295,287	2,737,166	3,268,644	3,577,472	3,952,279	4,683,827
Kalimantan Barat	2,019,936	2,486,068	3,229,153	3,635,730	4,034,198	4,395,983
Kalimantan Tengah	701,936	954,353	1,396,486	1,627,453	1,857,000	2,212,089
Kalimantan Selatan	1,699,105	2,064,649	2,597,572	2,893,477	2,985,240	3,626,616
Kalimantan Timur	733,797	1,218,016	1,876,663	2,314,183	2,455,120	3,553,143
Sulawesi Utara	1,718,543	2,115,384	2,478,119	2,649,093	2,012,098	2,270,596
Sulawesi Tengah	913,662	1,289,635	1,711,327	1,938,071	2,218,435	2,635,009
Sulawesi Selatan	5,180,576	6,062,212	6,981,646	7,558,368	8,059,627	8,034,776
Sulawesi Tenggara	714,120	942,302	1,349,619	1,586,917	1,821,284	2,232,586
Gorontalo	-	-	-	-	835,044	1,040,164
Sulawesi Barat	-	-	-	-	-	1,158,651
Maluku	1,089,565	1,411,006	1,857,790	2,086,516	1,205,539	1,533,506
Maluku Utara	-	-	-	-	785,059	1,038,087
Papua Barat	-	-	-	-	-	760,422
Papua	923,440	1,173,875	1,648,708	1,942,627	2,220,934	2,833,381
INDONESIA	119,208,229	147,490,298	179,378,946	194,754,808	206,264,595	237,641,326

Note: Includes Non-Permanent Residents (Homeless, Seafarers, Boat Houses, and Space Shuttle / Resident Residents).
Source: Population Census 1971, 1980, 1990, 2000 and 1995 Inter-census Population Survey (SUPAS), by Statistics Indonesia, 2019.

The Indonesian archipelago has been an important region for trade since at least the seventh century, when Srivijaya and then later Majapahit traded with China and India. Local rulers gradually absorbed foreign cultural, religious and political models from the early centuries CE, and Hindu and Buddhist kingdoms flourished. From this point onward, dozens of kingdoms and civilizations flourished and faded in different parts of the archipelago. Some notable kingdoms include Sriwijaya (7th-14th century) on Sumatra and Majapahit (1293-c.1500), based in eastern Java but the first to unite the main islands of Sumatra, Java, Bali and Kalimantan as well as parts of Peninsular Malaysia. Indonesia also consists of hundreds of distinct native ethnic and linguistic groups, with the largest and politically dominant ethnic group being the Javanese. In a numerical scale, the largest ethnic groups are the Javanese (45%) from central and eastern Java, the Sundanese (14%) from western Java, the Maduranese (7.5%) from the island of Madura, and Coastal Malays (7.5%), mostly from Sumatra. This leaves 26% for the Acehnese and Minangkabau of Sumatra, the Balinese, the Iban and Dayaks of Kalimantan, and a bewildering patchwork of groups in Nusa Tenggara and Papua.

The population is unevenly spread throughout the islands within a variety of habitats and levels of development, ranging from the megalopolis of Jakarta to uncontacted tribes in PapuaProvinces are usually grouped around larger islands and include smaller surrounding islands. Indonesia also has the world's largest Muslim population. Ethnically it is highly diverse, with more than 300 local languages.

The people range from rural hunter-gatherers to a modern urban elite.

Religion, does play a very important role in Indonesian society. Indonesian nationals are obliged to adhere to one of the six religions that have been officially recognized by the government (Islam, Protestantism, Roman Catholicism, Hinduism, Buddhism and Confucianism), with indigenous religions only partly acknowledged. Indonesia is the world's most populous Muslim-majority country with approximately 87.2 percent of the total Indonesian population or 227 million individuals in absolute numbers adherents in 2017. Almost 10% of Indonesians are Christians, while the rest are Hindus, Buddhists, and others. Most Hindus are Balinese, and most Buddhists are Chinese Indonesians.

However, Indonesia is not an Islamic nation (only in the special region of Aceh on the northern tip of Sumatra Islamic Sharia law is being applied). But despite being a secular democracy, principles based on Islamic doctrine do play a large role in the politics, the economy and society of Indonesia. There are also some 16.5 million Protestants (6.9 percent of the total population), 6.9 million Catholics (2.9 percent of the population), and 4 million Hindus (1.7 percent) living in Indonesia. Lastly, there exist small minorities of Buddhists as well as those who practice Confucianism, mostly members of the ethnic Chinese community.

I.4 Government and Political Situation

The Indonesian governmental system consists of three branches, executive branch, legislative branch, and judicial branch. The executive branch consists of the president, the vice president and the cabinet. Both the president and vice president are chosen by the Indonesian electorate through presidential elections. They serve for a term of five years that can be extended once by another term of five years when re-elected by the people. During these elections the president and vice president run as a fixed, inseparable pair, which implies that the composition of this pair is of great political strategic importance. Important matters that are of influence include ethnic (and religious) background and (previous) social position in Indonesian society.

Indonesia's legislative branch is the People’s Consultative Assembly (Majelis Permusyawaratan Rakyat, abbreviated MPR). It has the power to set or change the Constitution and appoints (or impeaches) the president. The MPR is a bicameral parliament that consists of the People’s Representative Council (Dewan Perwakilan Rakyat, abbreviated DPR) and the Regional Representative Council (Dewan Perwakilan Daerah, abbreviated DPD).

The DPR, consisting of 560 members, draws up and passes laws, produces the annual budget in cooperation with the president and oversees the general performance of political affairs. It is elected for a five-year term through proportional representation based on general elections. The DPD deals with bills, laws and matters that are related to the regions, thus increasing regional representation at the national level. Every Indonesian province elects four members to the DPD (who serve for a five-year term) on non-partisan basis. As Indonesia contains 33 provinces, the DPD consists of a total of 132 members.

The highest court in Indonesia's judiciary system is the independent Supreme Court. It is the final court of appeal and also deals with disputes between lower courts. A relatively new court, established in 2003, is the Constitutional Court, which monitors whether decisions made by the cabinet and parliament (MPR) are in line with the Indonesian Constitution. However, most of the legal cases in Indonesia are handled by the public courts, administrative courts, religious courts and military courts. A Judicial Commission oversees the maintenance of honor, dignity and behavior of Indonesian judges.

II. Overview of Macroeconomics Activity and Fiscal Position

II.1 Macroeconomic Activity

Home to more than 260 million people, Indonesia is the fourth most populous country in the world and the largest economy in Southeast Asia. With GDP of about US$1 trillion, the country is the world's sixteenth largest economy and the seventh largest in purchasing-power-parity terms. It has played an increasingly prominent role in the global policy debate, including as a member of the Association of Southeast Asian Nations (ASEAN) and the Group of 20 (G20), an international forum bringing together 20 of the world's largest advanced and emerging market economies.

Indonesia economy has passed various conditions from different era. There were some obstacles and achievements that Indonesia had got. Indonesia economy activities have been started since from colonial era until now. Many steps and policies have been implemented.

In colonial era, Indonesia economy resource was only developed in the interest of colonizers through the concentration on agriculture, especially plantations, with most of product sold abroad. As a result, the structure of the Indonesia economy became unbalanced because of too great an emphasis on the heavily export-import oriented agriculture.

During the decade knows as Old Order Era (1945-1966), the economy was a servant to politics. Rational Economic principles were unacknowledged and ignored. Furthermore, domestic and foreign resources were squandered. The direct result of these conditions was a drastic decline in the economy, accompanied by hyperinflation which reached more than 600 per cent in 1966. During this period, food production did not keep pace with population growth. Export proceeds decreased significantly, while imports were paid for by increasing loans from abroad.

Monetary policy received greater attention when the New Order Government came into the power. A new Bank Indonesia Act was stipulated in 1968 with multiple objectives, namely, to achieve and maintain price stability, stimulate economic growth and create employment. The monetary policy focused on controlling inflation and coordinating with fiscal authority to achieve economy stability. Inflation could finally and drastically be controlled to below 10 per cent in 1969. Thereafter, between 1969 and 1981, economic growth averaged about 7.86 per cent, with high revenue coming mainly from oil exports.

The first financial liberalization took place in June 1983. At this time the direct monetary policy was replaced with an indirect monetary policy through an open market operation using Bank Indonesia Certificate (Sertifikat Bank Indonesia) as its main instrument and couple with intervention in money market when necessary. To achieve the multiple objectives stated before, Bank Indonesia implemented a base money (quantity) targeting framework. Further deregulation took place in October 1988, when the reserve requirement was significantly reduced from 15 per cent to 2 per cent and restrictions on permits to open new banks were eased. Since then, the banking sector has grown rapidly to participate as an agent of development. As a result, short-term capital could flow freely in and out of the country and exposure to foreign exchange risk increase while the financial sector and real sector decoupled. Consequently, controlling supply money become complex.

The 1997-1998 Asian Financial Crisis hit Indonesia through a contagion effect from the currency crisis in Thailand in July 1997. This crisis struck Indonesia's economy so hard that led to both a triple financial crisis (currency, banking and foreign debt) and political crisis. As a monetary authority, Bank Indonesia initially responded by adopting a free floating exchange rate regime. Previously, Bank Indonesia had adopted a managed floating exchange rate regime. However, the government decided to turn to the IMF for help and entered into a Standby Arrangement with it on November 5th 1997. Later, on August 25th 1998, this was stepped up and became known as an Extended Fund Facility. The table below shows condition in some countries when Asian Financial Crisis happened:

Table 3: Asian Financial Crisis Outlook

Country	Year	Type of Crisis	NPL (%)	Fiscal Cost (% GDP)	Output Loss (% GDP)	Growth (%)
Indonesia	1997	Banking, Currency, Debt	32.5	56.8	67.9	-13.1
Korea	1997	Banking, Currency	35.0	31.2	50.1	-6.9
Malaysia	1997	Banking, Currency	30.0	16.4	50.0	-7.4
Philippines	1997	Banking, Currency	20.0	13.2	0.0	-0.6
Thailand	1997	Banking, Currency	33.0	43.8	97.7	-10.5
Vietnam	1997	Banking, Debt	35.0	10.0	19.7	4.8

In order to tackle the impact of Asian Financial Crisis, Indonesia's government implemented some policies. In the spanning period of 1997-1999, monetary authority under the Monetary Board, was chaired by Minister of Finance with Governor of Bank Indonesia, took actions to handle this condition. These actions resulted inflation dropped to 1.92% and economic growth improved to positive 0.3% in 1999. In 2000, inflation increased to 9.35% and economic growth improved further to 4.9%. The table below shows what Monetary Policies that launched by Indonesia Authority in 1997-1999:

Table 4: Indonesia Monetary Policy 1998

Economic Conditions	Monetary Policies
● Overheated economy. ● Structural Weaknesses. ● Foreign debt was not be hedged. ● Contagion effect started from currency crisis in Thailand in July 1997. ● Banking distress: NPL increased, margin, ROA, and CAR became negative. ● Bank runs in November 1997.	● Tight money policy. ● Closing of 16 hopeless ailing bank on November 1st 1997 (before implementing Blanket Guarantee). ● Letter of Intent with IMF: - Blanket Guarantee in January 1998; - Bailout other ailing banks; and - Aggressively raising interest rate. ● Banking Act 1998: Central Bank Act 1999.
Economic Conditions	**Monetary Policies**
● Budget Deficits. ● Public Debt US$ 60 billion.	● Cutting back government spending ● Structural reform.
Economic Conditions	**Monetary Policies**
● Speculation/rush in foreign exchange market caused IDR to fall since August 1997.	● Widen intervention band in July 1997. ● Floating exchange rate regime in August 1997.

Indonesia's economy started to recover in 1999, indicated by declining inflation and stronger rupiah currency, which provided room for a phased reduction of interest rate. Significant progress was also recorded in the restructuring of bank and external debts, especially those of banks and government. With positive hindsight, it can be seen that the stock market was bullish, signaling an initial return of investor confidence in Indonesia's economy prospect. However, the process of economic stabilization and recovery in Indonesia was, in fact, slower than that in other Asian countries in crisis.

As a result, a new Central Bank act No. 23 of 1999 entered into force in 1999. Bank Indonesia, became an independent central bank which focused on a single objective, was to achieve and maintain IDR (Indonesia Rupiah) stability. The new Bank Indonesia Act of 1999 made a fundamental change in the conduct of monetary policy from multiple objectives using quantity targeting to single objective using price targeting, known as Inflation Targeting Framework (ITF). To further refine the efficacy of monetary management, the Bank Indonesia act of 1999 was amended in 2004. Initially, Bank Indonesia implemented light ITF. Later, however, in July 2005, it implemented a full-fledged ITF as a response to aftermath of structural changes where interest rates started to take on an increasingly important role (compared with money supply) in influencing inflation.

In July 2007, the global economy witnessed a financial crisis precipitated by the subprime mortgage crisis in the US banking system. The situation became worse in 2008, marked by oil price soaring up to more than US$ 100 per barrel, which further escalated to US$ 147 per barrel in July 2008 but soon after that. The crisis was first transmitted to Indonesia through the capital market. The composite stock index was started from around 2,700 in December 2007 became 1,241 in November 2008. The ownership share of foreign investor decreased significantly and had been started from 66.3 % in December 2007 to 63.2 % in August 2008. In October 2008, Indonesia's currency also was depreciated by US dollar. Indonesia Rupiah (IDR) was brought down to IDR 10,995 to the US Dollar and continued to weaken further to IDR 12,151 in November 2008. As an independent monetary authority, Bank Indonesia has single objective for achieving and maintaining the stability of the rupiah by taking into account the general economic policies of the government. The results of the monetary policy in 2009 had brought the inflation dropped to 2.78 %, the GDP growth reached 4.4 %, the interest rate lowered to 6.5 %, the strong exchange rate at IDR 9,300/US$ 1, and the unemployment decreased to 9.0 %.

Table 5: Indonesia Monetary Policy 2008

Economic Conditions	Monetary Policies
• Global Financial Crisis started in July 2007. • Stock Market index started to slide since 03/2008; oil price continued to increase drastically and reach US$ 147 in July 2008. • Global banking systemic contagion worsened in September 2008; tight liquidity problem in the banking system. • Inflation pressure lessened in September 2008; many central banks started to lower their policy rates.	• Tight monetary policy; gradual Bank Indonesia (BI) rate increase since May 2008. • Eased statutory reserve requirement and facilitating Short Term Financing for Banks that have low Capital Adequate Ratio. • BI rate increased 25 basis points in October 2008 and kept unchanged in November 2008. • Bailout one troubled small bank in November 2008. • Eased Monetary Policy aggressively from December 2008 until early 2010.
Economic Conditions	**Monetary Policies**
• Fiscal sustainability pressure since early 2008; increased cost of subsidies.	• Budget tightening by 10 % in 2008; decreased subsidy; raised gas price in May 2008. • Increased minimum deposit insurance 20 times. • Established Financial System Stability Committee (Finance Minister and Bank Central Governor) and necessary regulations. • Bilateral Currency Swap with China and Japan. • Lowered gas price in December 2008.
Economic Conditions	**Monetary Policies**
• Capital outflow since early 2008. • Depreciation to IDR 12, 150/US$ 1 in November 2008; increased volatility.	• Stabilization policy in Foreign Exchange Market.

The government responded to the crises of 1998 and 2008 in different ways. The IMF recommended that Bank Indonesia responded to the weakening of the rupiah by raising interest rates during the Asia Financial Crisis (AFC). Because the Non-Performing Loans (NPLs) were high, raising interest rates increased the probability of default, which led to the banking crisis. The banking crisis had worsened the economy and encouraged capital outflows. This is consistent with Stiglitz and Greenwald's (2003) argument that as an economy enters a deep recession and contraction devaluation causes many firms to be distressed. In contrast with the AFC, during the global financial crisis, Bank Indonesia responded by lowering the interest rate and ensuring that there was enough liquidity in the financial system. As a result, the probability of default was relatively low in 2008, and the impact of NPLs on the banking sector was also relatively small.

Amid the positive momentum on multiple fronts, challenges emerged that hampered the pace of domestic economic recovery. These challenges were rooted in cyclical and structural problems, both global and domestic. In adding to the complexity of the challenges, the Indonesian economy was simultaneously undergoing an adjustment phase in response to changes in the global and domestic environment. Taken together, these conditions held the domestic economy back from mounting a quick, robust recovery.

Indonesia's economic recovery progressed gradually and at the same time became more stable. Economic growth edged upwards and the structure of growth was seen in the second half of the year. The economic growth in 2017 was recorded at 5.07%, slightly up from 5.03% in 2016. Macroeconomic stability was also well in hand, with inflation remaining within the target range, a prudent current account deficit level and a sufficiently stable exchange rate. Financial system stability was also carefully maintained, despite unresolved challenges relating to the still-limited performance in banking intermediation.

Four main cyclical challenges impeded economic recovery in 2017. First, the normalization of monetary policy by some advanced nations presented a challenge. Global financial markets were influenced by the direction of this monetary policy normalization, most importantly that undertaken by the United States. Even though markets were generally prepared for it, pressure on global financial markets did intensify at the end of the third quarter of 2017 as the US dollar strengthened over nearly every other currencies. This pressure exacerbated uncertainty on global financial markets and in capital flows and threatened to rein in a more rapid global recovery, including Indonesia. This became a challenge which given the risk that normalization in advanced nations could cause instability by triggering a capital reversal from emerging markets, including Indonesia.

Second, the limited domestic fiscal space posed a challenge. It limited government's capacity to create economic stimuli and to leverage positive momentum for the benefit of the domestic economy. The lack of a sizeable stimulus is explained in part by below-target taxation. In 2017, the tax ratio came to 9.9% of GDP, representing a decline compared to the preceding two years; the tax-to-GDP ratio in 2015 was 10.7% and in 2016 edged down to 10.4%. The capacity of fiscal stimulus to give a strong boost to the economic recovery was therefore limited, as evident in the dynamics of government financial operations during 2017.

Third, domestic corporate consolidation had not yet fully run its course, though it is now winding down. During this period of consolidation, companies generally did not expand, but instead were focused on putting their house in order. Corporate behavior was also influenced by adverse global developments in 2016 that damaged corporate confidence and discouraged them from expanding. In addition, corporate expansion plans were stifled by the modest fiscal stimulus and the still-sluggish household consumption. At the same time, bank intermediation underperformed, hitting corporate business financing and in turn impacting on corporate expansion. These factors led to inadequate levels of domestic non-construction investment, particularly in the first half of 2017. This caused concern because incorrect handling could hampered the recovery process.

For these reasons, short-term measures were taken to boost the confidence of domestic economic actors at a time when Indonesia was receiving positive recognition from abroad for the improvement in its economic fundamentals. Fourth, as noted above, banking intermediation had not fully recovered, limiting the driving force of the economy. Slackness in credit growth was the result of both demand-and supply-side factors. On the demand side, the incomplete corporate consolidation slowed business expansion and therefore also demand for credit. At the same time, banks remained cautious and selective in extending new loans and continued to apply high lending standards.

II.1.1 Policy Response in 2018

Bank Indonesia, the Government and relevant authorities acted resolutely and consistently to implement a policy mix that would strengthen economic stability – in particular rupiah stability – while sustaining the economic recovery. The challenges to the economy in 2018 emerged mostly from external balances, while internal balances were solid. For this reason, policy was focused on mitigating external sector risks that could adversely impact the Balance of Payment (BoP) and pressure the exchange rate. Immediate action was necessary to forestall these developments which, unchecked, could have destabilized the economy.

Policy also sought to strengthen the existing momentum for economic recovery. According to Bank Indonesia estimates, the upwards trend of Indonesia's economic growth did not disrupt internal balances, given that growth remained below potential capacity. The policy mix was geared to provide continued support for economic growth, enabling growth to climb towards the potential capacity of the economy. The pro-growth measures were also consistent with the financial cycle which, according to indicators, was below long-term projections, despite being on an upward trend. Overall, the policy mix was balanced with inflation control measures in order to keep inflation on target and financial systems stable.

Bank Indonesia, the Government and other authorities synergized their policy choices. Bank Indonesia optimized a mix of monetary, financial market deepening, macroprudential and payment system policies with the aim of maintaining stability and supporting economic growth. The Bank Indonesia policy mix was managed in synergy with the fiscal and structural policies of the Government and the Financial Services Authority (OJK) to safeguard the resilience of the financial system and growth momentum.

The direction of the monetary policy rate in 2018 was placed within a framework of determining an optimum monetary policy for a nation with an open economy. Changes were introduced to formulate the policy rate independently, taking account of two other important elements: free movement of foreign capital and continued exchange rate flexibility. Interest rate policy on one hand sought to create adequate interest rate differentials and bolster the attractiveness of investing foreign capital in domestic financial market assets. On the other hand, the policy rate also needed to remain consistent with measures to keep inflation on target. At the same time, exchange rate policy was focused on maintaining exchange rate stability at about the level of fundamentals, so that it could serve as an instrument for mitigating shocks to the economy from external factors.

Exchange rate policy was aimed at maintaining flexibility in movement of the rupiah in line with fundamentals, and while maintaining market mechanism. The rupiah stabilization policy was used to minimize the rising volatility in a period of global uncertainty that, it was feared, could influence the expectations of economic actors. The rupiah stabilization policy was implemented in a twofold strategy. First, this policy involved a strategy for optimizing dual interventions by Bank Indonesia on the forex market and the government bonds market. This strategy was pursued to maintain exchange rate stability, while safeguarding an adequate level of rupiah liquidity. Second was a strategy for management of forex liquidity to maintain adequate forex market liquidity. This policy was supported by measures to deepen the forex market; these included the development of hedging instruments including overnight index swaps (OIS), interest rate swaps (IRS) and domestic non-deliverable forwards (DNDF).

The direction of monetary policy was reinforced by an operational strategy to maintain adequate liquidity on the money market and in the banking system. This was needed because a decline in foreign capital inflows would reduce money market and banking liquidity, and could have impacted financial system stability. To this end, Bank Indonesia employed a number of strategies in the second and third quarters of 2018 to ensure the availability of liquidity on the money market and forex market, amid mounting global pressures. Bank Indonesia increased the frequency of auctions of short-term government securities reverse repo (RR SBN) instruments with tenors of one week, two weeks and one month during this period.

In the fourth quarter of 2018, the focus of the monetary operations strategy began to shift towards support for economic financing while continuing to safeguard economic stability. This policy direction also took account of the economic stability that was under control, which afforded space for implementing this strategy. During this period, Bank Indonesia strengthened the monetary operations by introducing broader access for the banking system via term repos, as a measure to increase liquidity. This strategy was taken forward by continuing the strengthening of monetary operations, including fine tune operations and auctioning of foreign exchange (FX) swaps.

To improve economic stability and, in particular, to maintain subdued inflation, Bank Indonesia forged closer cooperation with the Government through the Central Inflation Controlling Team (TPIP) and Regional Inflation Controlling Teams (TPID). Bank Indonesia worked with national and regional government to ensure affordability of prices, availability of supply, expeditious distribution and effective communications on policy to anchor inflation expectations. This coordination in inflation control also demonstrated the commitment of the Government and Bank Indonesia to achieving the inflation target of 3.5%±1% in 2019 and 3.0%±1% in 2020 and 2021.

Bank Indonesia also proceeded with the financial market deepening policy, aiming to expand the role of the financial market in supporting sustainable economic growth. To this end, Bank Indonesia, OJK and Ministry of Finance worked together in the Coordination Forum on Development Financing by Means of Financial Markets (FK–PPPK) to write the National Financial Market Development and Deepening Strategy (SN-PPPK) for accelerating the pace of financial market deepening.

The financial market deepening policy was also designed to support the development of long-term investment on the capital market. Other measures for strengthening the role of financial markets included more extensive innovation of instruments for financing infrastructure projects. This was achieved in coordination with the Government, OJK and a number of financial institutions. Under this coordinated action, financing agreements for strategic infrastructure projects worth USD13.6 billion were concluded in October 2018. Macroprudential policies were targeted at strengthening the momentum for economic growth while continuing to safeguard financial system stability. Measures to promote higher economic growth were introduced in a number of accommodative macroprudential policies. Among these was the relaxation of the loan-to-value ratio (LTV) to facilitate home ownership for first-time buyers and promote investment in the housing sector. Bank Indonesia also held a consistent course in improving financial access for micro, small and medium enterprises (MSMEs) by establishing a minimum 20% target for MSME loan in 2018, with sanctions for non-compliance, consistent with phased implementation that was adopted in 2015.

The accommodative macroprudential policies put in place also included changes to the loan-to-funding ratio (LFR), which is now known as the macroprudential intermediation ratio (RIM). This instrument was developed by expanding economic financing from credit to include purchasing of quality securities issued by non-financial sector corporates. Bank Indonesia also increased flexibility in bank liquidity management through introduction of the macroprudential liquidity buffer (MLB) regulation, an enhancement of the secondary statutory reserve requirement. The MLB provisions comprise a secondary statutory reserve requirement of 4% of deposits, which requires banks to hold securities that can be traded with Bank Indonesia in repo transactions. In 2018, the percentage of securities that could be traded in repo transactions with Bank Indonesia was increased to 4% of deposits from 2%. Alongside this, the capital requirement for the countercyclical capital buffer (CCB) was maintained at 0% to strike a balance between promotion of intermediation and mitigation of risks. In other actions, Bank Indonesia worked with OJK to strengthen surveillance of the financial system, principally for large banks and corporates, and to establish closer coordination under the Financial System Stability Committee (KSSK), while strengthening collaboration in international forums.

Payment system policy was similarly directed at supporting economic activity by making payment transactions more secure and efficient. In this regard, Bank Indonesia strengthened the policy strategy for the payment systems for both non-cash and cash transactions. On the non-cash side, Bank Indonesia promoted the acceleration and expansion of electronic processing of non-cash payments in a variety of areas, including disbursements under government social programs, payments in the transport sector and management of regional government financial transactions. Bank Indonesia also went further, strengthening the payments ecosystem and digital finance by implementing the national payment gateway (NPG) and developing the ecosystem for financial technology (fintech), most importantly within the scope of the payment system. For cash payments, Bank Indonesia worked steadfastly to ensure that currency fit for circulation was provided throughout Indonesia. Amid this drive to support economic activity, Bank Indonesia also continues to ensure payment system services are prudently implemented, by employing risk management and consumer protection measures. Last, Bank Indonesia also worked with other institutions to ensure that the national payments system worked efficiently and securely.

The Government pursued a prudent fiscal policy aimed at supporting economic stability while continuing to optimize space for promoting economic growth. In regard to upholding economic stability, the objective of fiscal policy in 2018, as before, was to safeguard the fiscal sustainability outlook by managing the primary balance and the overall state budget deficit. In 2018, the primary deficit came to -0.01% of GDP (IDR1.8 trillion), representing a significant reduction from the previous year’s level of -0.91% (IDR124.4 trillion). Positive developments were also reflected in the 2018 budget deficit of 1.8% of GDP, narrowing from 2.5% of GDP in 2017. In turn, this enabled the Government to hold the level of official debt at a comfortably safe level of 29.8% of GDP.

In 2018, the Government continued to optimize fiscal policy as an instrument to promote economic growth. Among other measures, the Government increased spending on social assistance from the beginning of 2018. And in a further action to improve the investment climate, the Government provided a tax incentive in which pioneer industries could benefit from a tax holiday of between 5 and 20 years, depending on the value of their investment.

Regional fiscal policy and infrastructure project construction played an increased role in fiscal policy strategy. To strengthen the fiscal role of the regions, Indonesia pursued measures to increase regional government revenues, with a primary emphasis on optimizing local sources of regional government revenues and central government transfers. Parallel with this, issues with regional spending were addressed, primarily to improve the quality of regional government spending and direct it towards more productive outcomes.

Relating to infrastructure project construction, the Government pressed forward with infrastructure development with involvement from state-owned enterprises and by promoting private sector participation. In 2018, the focus was on accelerating construction of projects that would improve interregional connectivity in Indonesia. Working through the Committee for Acceleration of Priority Infrastructure Delivery (KPPIP), the Government selected strategic and highly urgent projects and provided facilities to expedite project execution. These projects were all national strategic projects (NSP).

The policy mix implemented by Bank Indonesia, the Government and other authorities proved successful in safeguarding the Indonesian economy through 2018. Economic stability returned to a comfortably safe level in the fourth quarter of 2018, and economic growth momentum was sustained.

Positive developments were reflected in the rise in foreign capital inflows in the fourth quarter of 2018. Data from the Institute of International Finance shows that foreign capital inflows into Indonesia were higher than capital inflows into all other emerging markets. This resulted in an increase in the capital and financial account surplus USD15.7 billion in the fourth quarter of 2018, up from the second and third quarters of the year.

At the same time, imports slowed in line with the positive impact of policy. In the fourth quarter of 2018, growth in total non-oil and gas imports reached 12.5% yoy, down from 21.3% yoy in the third quarter of 2018. However, efforts to reduce the current account deficit through the slowdown in non-oil and gas imports were hampered by the concurrent fall in exports. Exports fell in response to flagging growth in the world economy and falling commodity prices. Against this background, Indonesia posted a USD 5.4 billion surplus in its BoP in the fourth quarter of 2018, reversing the deficit of the preceding quarter as seen in the following table.

Table 6: Indonesia Domestic Indicators

Component	2015	2016	2017	2018
Economic growth (%, yoy)	4.88	5.03	5.07	5.17
Household consumption (%, yoy)	4.96	5.01	4.94	5.05
Government consumption (%, yoy)	5.31	-0.14	2.13	4.80
Gross Fixed Capital Formation (GFCF) (%, yoy)	5.01	4.47	6.15	6.67
GFCF construction (%, yoy)	6.11	5.18	6.24	5.45
GFCF non-construction (%, yoy)	1.93	2.43	5.90	10.31
Export of goods and services (%, yoy)	-2.12	-1.66	8.91	6.48
Import of goods and services (%, yoy)	-6.25	-2.41	8.06	12.04
Consumer Price Index (CPI) Inflation (%, yoy)	3.35	3.02	3.61	3.13
Core Inflation (%, yoy)	3.95	3.07	2.95	3.07
Volatile Food Inflation (Percent, yoy)	4.84	5.92	0.71	3.39
Administered Prices Inflation (%, yoy)	0.39	0.21	8.70	3.36
Balance of Payment				
Current Account Deficit (%, GDP)	2.0	1.8	1.6	3.0
Capital and Financial Account (USD billion)	17.1	29.3	28.7	25.2
Overall Balance (USD billion)	-1.1	12.1	11.6	-7.1
Official Reserve Assets (USD billion)	105.9	116.4	130.2	120.7
Exchange rate (Average; USD/IDR)	13,392	13,305	13,385	14,246
Jakarta Composite Index (JCI) (Index)	4,593	5,297	6,356	6,056
10-year government bond yields (%)	8.76	7.90	6.30	8.00
Banking				
Total Credit (%, yoy)	10.4	7.9	8.2	11.8
Capital Adequacy Ratio (CAR) (end of period, %)	21.2	22.7	23.0	22.9
Non-Performing Loans (end of period, %)	2.5	2.9	2.6	2.4
State Budget				
Tax (% GDP)	10.7	10.4	9.9	10.3
Primary balance (% GDP)	-1.2	-1.0	-0.9	0.0
State budget deficit (% GDP)	2.6	2.5	2.5	1.8

Source: Statistics Indonesia, 2019; and 2018 Economic Report on Indonesia published by Bank Indonesia, Ministry of Finance, Financial Service Authority, and Indonesia Stock Exchange.

Overall, the improving trend in foreign capital inflows and imports in the fourth quarter of 2018 had a positive effect on external sector resilience. The current account deficit remained at a prudent level of 2.98% of GDP, despite widening from 1.60% of GDP in 2017. Other indicators also demonstrate that external resilience remained sound.

At the end of 2018, foreign reserves stood at USD120.7 billion, more than enough to finance six and a half months of imports and servicing of government external debt, and also sufficient to guard against the possibility of foreign capital outflows. Bank Indonesia also established closer international cooperation with other Asia-Pacific central banks – under the Global Financial Safety Net (GFSN).

Inflation remained low and stable in 2018, amid turbulence in the external sector. Consumer prices inflation came in at 3.13% in 2018, within the 3.5%±1% target range, with core inflation, volatile foods (VF) and administered prices (AP) inflation subdued. Indonesia's inflation has been on target for the past four years.

A downward trend in inflation resulted from both cyclical and structural factors. Cyclical factors such as falling global prices for food commodities and steady demand led to a steady decline in inflationary pressure. On the other hand, the effect of structural improvements in the character of Indonesia’s inflation were positive, having

Financial system stability remained well under control with the support of robust banking capital and adequate liquidity. The banking system maintained high capital ratios; the capital adequacy ratio stood at 22.9% at the end of 2018. Banking liquidity also remained at adequate levels during 2018, reflected in the 19.3% ratio of liquid instruments to deposits. Bank placements in monetary operations instruments also increased, coming in at IDR382.8 trillion at the end of 2018.

Strong resilience amid the heightened global uncertainties kept Indonesia’s economic growth on a solid footing. In 2018, economic growth reached 5.17%, up from 5.07% in 2017, and the highest level for the past five years. The gain in economic growth was driven by strong domestic demand fueled by brisk growth in consumption and ongoing investment in infrastructure construction. However, the net export contribution was negative, as imports grew rapidly and export growth tapered off. By region, higher growth in Java, Sumatra and Maluku-Papua (Mapua) underpinned the 2018 economic growth. By sector, economic growth was driven primarily by businesses linked to the strong growth in domestic demand and commodity exports.

II.1.2 International Environment

The global economic was characterized by increased uncertainty, prompted by three unfavorable developments. First, global economic growth slowed to 3.6% in 2018 from 3.8% in 2017. This was accompanied by a reduced world trade volume and lower international commodity prices. Second, the Federal Reserve raised the Federal Funds Rate (FFR) more aggressively than in 2107, thus triggering the risk of a sudden capital reversal from developing economies. Third, global financial market uncertainty has increased as an outcome of several factors: escalating trade tensions between the United States and several of its trading partners, particularly China; simmering geopolitical risks such as the Brexit negotiations; and crises in a number of developing economies, including Argentina and Turkey. Together, these three factors compelled global investors to withdraw funds from developing economies and threatened to undermine external stability in the developing countries. Consequently, significant broad- based depreciation against the US dollar ensued, creating vulnerabilities to macroeconomic and financial system instability.

Table 7: World GDP Growth

(%, yoy)

GROUP OF COUNTRIES	2015	2016	2017	2018
World Output	**3.5**	**3.4**	**3.8**	**3.6**
Advanced Economies	2.3	1.7	2.5	2.3
United States	2.9	1.6	2.4	2.9
Euro Area	2.1	1.9	2.5	1.9
Germany	1.7	2.2	2.5	1.5
France	1.1	1.1	2.3	1.7
Italy	0.9	1.1	1.7	0.9
Spain	3.6	3.2	3.0	2.6
Japan	1.2	0.6	1.9	0.8
United Kingdom	2.3	1.8	1.8	1.4
Canada	0.7	1.1	3.0	1.9
Other Advances Economies	2.3	2.4	2.9	2.6
Australia	2.5	2.8	2.4	2.7
Emerging Market and Developing Economies	4.3	4.6	4.8	4.5
Emerging Market and Developing Asia	6.8	6.7	6.6	6.4
China, People's Republic of	6.9	6.7	6.8	6.6
Korea, Republic of	2.8	2.9	3.2	2.7
Hong Kong SAR	2.4	2.2	3.8	3.0
Taiwan Province of China	0.8	1.5	3.1	2.6
India	8.0	8.2	7.2	6.8
ASEAN-5 Countries	4.9	5.0	5.3	5.2
Indonesia	4.9	5.0	5.1	5.2
Malaysia	5.0	4.4	5.7	4.7
Philippines	6.1	6.9	6.7	6.2
Singapore	2.9	3.0	3.7	3.1
Thailand	3.1	3.4	4.0	4.1
Emerging Market and Developing Europe	0.8	1.8	3.9	3.1
Russia Federation	-2.3	0.3	1.6	2.3
Turkey	6.1	3.2	7.5	2.8
Latin America and the Caribbean	0.3	-0.6	1.2	1.0
Argentina	2.7	-2.1	2.7	-2.5
Brazil	-3.6	-3.3	1.1	1.1
Mexico	3.3	2.9	2.1	2.0
Middle East and Central Asia	2.6	5.0	2.3	1.9
Saudi Arabia	4.1	1.7	-0.7	2.4
Sub-Saharan Africa	3.1	1.4	3.0	3.2
Nigeria	2.7	-1.6	0.8	1.9
South Africa	1.2	0.4	1.4	0.8

Source: 2018 Economic Report on Indonesia published by Bank of Indonesia, World Economic Outlook Real GDP data update in December 13, 2019.

Overall, the economic performance of 2018 was lower than expected at the beginning of the year. The global economic slowdown was also accompanied by an uneven economic growth composition. Advanced economies recorded slower aggregate economic growth in 2018 – 2.3%, down from 2.5% in 2017. However, global economy was unevenly moderated, with the US economy continuing to post gains whereas majority of other advanced economies decelerated.

US economic growth accelerated in 2018, driven by large fiscal stimuli. The US economy expanded by 2.9% in 2018, up from 2.4% in the previous year. Fiscal stimuli significantly increased the contribution of government spending to economic growth in 2018, but also amplified the risks associated with the budget deficit and fiscal sustainability.

In Euro Area, economic growth decelerated to 1.9% in 2018 from 2.5% in 2017. The surge in economic growth in the second half of 2017 was not sustained in 2018 due to weakening exports. Euro Area exports decreased in line with moderated growth in trading partner economies, and increased uncertainty due to simmering trade tensions. Simultaneously, domestic demand also retreated. Fiscal consolidation in several Euro Area member countries further impeded consumption and investment growth. In addition, domestic demand across Europe was impaired by increasing uncertainty stemming from geopolitical risks in Germany, Italy, and France, coupled with deteriorating labor market dynamics. Fading external and domestic demand was reflected in the Purchasing Managers Index (PMI), which trended downward throughout 2018. The weakening export performance, coincided with weak domestic demand, have in turn triggered an economic downswing.

In line to dynamics in Euro Area, economic growth in Japan also moderated compared to 2017. Japan’s economy expanded 0.8% in 2018, down from 1.9% in 2017. The slowdown occured as the impact of fiscal stimuli diminished, external demand weakened, and considerable impact from natural disasters that befell the country in the third quarter.

Growth in developing economies also slowed in 2018, dipping slightly to 4.5% from 4.8% in 2017. This downturn was primarily attributable to slower economic growth in China and some Latin American countries, in contrast to accelerating growth in India. China’s economic growth decelerated to 6.6% in 2018 from 6.8% in 2017 as a result of a tighter deleveraging policy and worsening trade relations with the United States. To control risks in the financial system, China’s government adopted deleveraging policies laid out in several regulations to transfer off-balance sheet activities to on-balance sheet, thus providing adequate risk mitigation. At the same time, China’s export and investment performance also slowed due to uncertainty associated to deteriorating trade relations with the United States.

The global economy in 2018 was also beset by high uncertainty in global financial market. Triggered by the knock-on effect of monetary policy normalization in the United States, global financial uncertainty was exacerbated by deteriorating trade relations between the United States and several of its trading partners, including China, Canada, Mexico, and Europe. Global financial market uncertainty was also influenced by geopolitical risks, including the unresolved Brexit negotiations between the UK and European Union, and the economic issues plaguing Italy. The economic crises disrupting Argentina and Turkey prompted an outpouring of negative sentiment on developing economies, as reflected in the large capital reversal from developing economies.

In 2018, countries adopted differing policy responses to sustain the economic recovery against a backdrop of accumulating external pressures. Each nation implemented policies tailored to the specific dynamics and challenges faced in each jurisdiction. Policy responses were taken by optimizing the interaction between monetary policy, fiscal policy, and structural policy. While most developing economies did adopt a tighter monetary policy stance to mitigate the risk of a capital reversal. They also sought to maintain sustainable economic growth, which was threatened by dwindling external demand. Structural policies were also required to expand economic capacity and stimulate quality growth.

Strengthening structural reforms has become a priority in the global economic policies. Structural reforms continues to boost productivity, improve labor market conditions, and accelerate potential economic growth which has been reined in by aging populations.

International cooperation plays an important role in addressing the uncertain global economic dynamics. Global efforts to strengthen cooperation in 2018 focused on achieving strong, sustainable, balanced, and inclusive growth, while maintaining economic resilience in the face of challenges and widespread global uncertainty. Cooperation to stimulate economic growth includes efforts to finance infrastructure, and to ensure that technological innovation provides optimal benefits. International cooperation to strengthen resilience in the financial sector was oriented towards reinforcing global and regional financial safety nets.

International cooperation forums have emphasized the importance of maintaining global economic growth momentum. The G20 and IMF have strived to realize strong, sustainable, balanced, and inclusive economic growth in order to overcome global economic fragilities. In 2018, the G20 agreed on commitments regarding follow- up from member countries to achieve SSBIG by using monetary, fiscal, and structural policies both individually and collectively. In addition, advanced economies have prioritized clearer policy communication in order to prevent adverse impacts of economic policies toward developing economies. At the 2018 IMF–World Bank Annual Meetings in Bali, the IMF stressed the importance of continuing with structural policy and reforms to sustain economic expansion, mitigate global risks, provide fiscal space, strengthen economic resilience, and improve the medium-term growth outlook.

International cooperation has also focused on optimizing technology to stimulate inclusive economic growth, and Indonesia provides a solid example in terms of the policies instituted. Indonesia is supporting the provision of science and technology parks, tax incentives to draw foreign direct investment to high-tech sectors, and is initiating a big data project. The project aims to improve data collection from various sources to support effective policy formulation. Indonesia has successfully collected and collated data related to job vacancies, the property market, the automotive sector, information technology, and e-commerce.

The global economic dynamics plagued with high uncertainty have increased the urgency to strengthen economic resilience through multilateral, regional, and bilateral cooperation. Multilateral cooperation forums have strived to bolster the international monetary system and Global Financial Safety Net (GFSN), while implementing a reform agenda for the financial system. Furthermore, regional cooperation forums have reinforced the Chiang Mai Initiative Multilateralization (CMIM) with collaboration and synergy in the GFSN, and have expanded the role of the ASEAN+3 Macroeconomic Research Office (AMRO) as a surveillance institution. Bank Indonesia has also actively sought bilateral cooperation with other central banks in order to strengthen external resilience through swap arrangements.

II.1.3 Balance of Payment (BoP)

The balance of payments (BOP), also known as balance of international payments, summarizes all transactions that a country's individuals, companies and government bodies complete with individuals, companies and government bodies outside the country. These transactions consist of imports and exports of goods, services and capital, as well as transfer payments such as foreign aid and remittances. Balance of payments and international investment position data are critical in formulating national and international economic policy. Certain aspects of the balance of payments data, such as payment imbalances and foreign direct investment, are key issues that a nation's policymakers seek to address.

Unfavorable global economic dynamics coupled with solid domestic economic fundamentals presented an onerous balance of payments (BoP) challenge in 2018. Adverse global economic conditions amplified pressure on the BoP through the trade and financial channels. Pressures accumulated at the beginning of 2018 and escalated in the second and third quarters. During that period, the current account deficit widened on high import growth to meet solid domestic demand, while exports declined as a consequence of global economic slowdown. In addition, gradual Federal Funds Rate (FFR) hikes – together with financial market uncertainty – eroded foreign capital inflows. Consequently, Indonesia posted a BoP deficit in the first three quarters of the year.

The policy response also maintained the strong external resilience. Despite the challenges that arose, various external resilience indicators remained sound, even though the BoP recorded an overall deficit for the year. The current account deficit was controlled within a manageable threshold of 3% of gross domestic product (GDP). Meanwhile, the position official of reserve assets at the end of 2018 stood at USD 120,654 million, equivalent to 6.7 months of imports or 6.5 months of imports and servicing government external debt, which is well above the international adequacy standard of three months. External resilience was also safeguarded by the second line of defense, namely the Global Financial Safety Net (GFSN). Furthermore, the profile and structure of external debt remained under control, bolstered by policy consistency designed to optimize the role of external debt in terms of economic financing and to minimize the risks to economic stability. The Table 8 below shows Indonesia's Balance of Payment in spanning 2015-2018.

Table 8: Indonesia's Balance of Payment 2015-2018

(million USD)

ITEMS	2015	2016	2017	2018
I. Current Account	**-17,519**	**-16,952**	**-16,196**	**-31,060**
A. Goods	**14,049**	**15,318**	**18,814**	**-431**
- Exports	149,124	144,470	168,883	180,747
- Imports	-135,076	-129,152	-150,069	-181,178
1. General Merchandise	**13,319**	**14,744**	**17,915**	**-422**
- Exports	147,725	143,105	167,002	178,724
- Imports	-134,406	-128,360	-149,087	-179,146
a. Non-Oil and Gas	**19,023**	**19,516**	**25,264**	**11,166**
- Exports	130,541	130,188	151,429	161,082
- Imports	-111,518	-110,672	-126,164	-149,917
b. Oil and Gas	**-5,703**	**-4,772**	**-7,349**	**-11,587**
- Exports	17,184	12,916	15,573	17,642
- Imports	-22,887	-17,688	-22,922	-29,229
2. Other Goods	**730**	**574**	**899**	**-9**
- Exports	1,400	1,365	1,881	2,022
- Imports	-670	-792	-982	-2,032
B. Services	**-8,697**	**-7,084**	**-7,379**	**-7,101**
- Exports	22,221	23,324	25,328	27,932
- Imports	-30,918	-30,407	-32,707	-35,034
C. Primary Income	**-28,379**	**-29,647**	**-32,131**	**-30,420**
- Receipts	2,822	4,048	5,575	9,162
- Payments	-31,201	-33,695	-37,706	-39,582
D. Secondary Income	**5,508**	**4,460**	**4,500**	**6,892**
- Receipts	10,362	9,832	9,967	12,217
- Payments	-4,853	-5,371	-5,467	-5,325
II. Capital Account	**17**	**41**	**46**	**93**
- Receipts	17	41	46	93
- Payments	-	-	-	-
III. Financial Account	**16,843**	**29,306**	**28,686**	**25,108**
- Assets	-21,489	15,920	-18,410	-20,113
- Liabilities	38,332	13,386	47,096	45,221
1. Direct Investment	10,704	16,136	18,502	13,841
a. Assets	-9,075	11,594	-2,008	-6,330
b. Liabilities	19,779	4,542	20,510	20,171
2. Portfolio Investment	16,183	18,996	21,059	9,342
a. Assets	-1,268	2,218	-3,356	-5,173
b. Liabilities	17,451	16,778	24,415	14,515
- Public Sector	17,386	16,835	21,877	9,504
- Private Sector	65	-57	2537	5,011
3. Financial Derivatives	20	-9	-128	-74
4. Other Investment	-10,064	-5,817	-10,747	1,999
a. Assets	-11,812	1,499	-13,487	-9,228
b. Liabilities	1,748	-7,316	2,740	11,227
- Public Sector	-190	-2,369	-1,353	-983
- Private Sector	1,938	-4,947	4,093	12,210
IV. Total (I + II + III)	**-659**	**12,394**	**12,536**	**-5,859**
V. Net Error and Omissions	**-439**	**-305**	**-950**	**-1,272**
VI. Overall Balance (IV + V)	**-1,098**	**12,089**	**11,586**	**-7,131**
VII. Reserves and Related Items [3]	**1,098**	**-12,089**	**-11,586**	**7,131**
A. Reserve Asset Transactions	1,098	-12,089	-11,586	7,131
B. Credit and Loans with IMF	-	-	-	-
C. Exceptional Financing	-	-	-	-
Memorandum:				
- Reserve Assets Position	105,931	116,362	130,196	120,654
In Months of Imports & Official Debt Repayment	7.39	8.42	8.3	6.5
- Current Account (% GDP)	-2.03	-1.82	-1.6	**-2.98**
- Debt Service Ratio (%)	-	-	-	-
O/w Government & Monetary Authority DSR (%)	-	-	-	-

Source: Bank of Indonesia, February 2019

II.1.4 Current Account

The full year 2018 current account deficit was influenced by slowing growth in non-oil and gas exports. Non-oil and gas exports grew 6.4% in 2018, down from 16.5% in 2017. However, non-oil and gas imports posted high growth of 19.6%, up from 13.9% in 2017 to meet growing domestic demand for infrastructure. The oil and gas trade balance therefore recorded USD 11,587 million deficit in 2018, as imports outpaced exports. Nevertheless, the wider deficit of oil and gas trade balance was partly-offset by the surplus in gas balance of USD6.8 billion due to the higher Indonesian gas prices.

In response, Bank Indonesia, the Government, and other authorities implemented various policy responses to control imports and stimulate exports. Such government measures were: promoting the use of domestically produced crude oil; expanding the use of a diesel/biofuel mix Biodiesel 20 (B20); reviewing infrastructure projects with a high import content; and stimulating tourism.

The first policy, was to purchase domestic crude oil to reduce crude oil imports. The Government instructed Pertamina to purchase – at the export price – exportable crude oil held by oil and gas partnership contractors. This policy aimed to reduce crude oil imports used as raw material for refinement by Pertamina, which totaled 199.63 million barrels in 2017. In addition, this policy was also aimed to reduced import service fees, particularly freight costs.

The second policy, was to diversify energy sources by using more B20 – a fuel comprising 80% diesel and 20% CPO biofuel. A new rule on B20 use was stipulated in Minister of Energy and Mineral Resources Regulation No. 12/2015, overriding a previous regulation that made B20 use mandatory only for public service obligation (PSO). In September 2018, the Government expanded the B20 program to also include non-PSO transport, manufacturing, mining, and the electricity sector. This B20 policy is designed to preserve foreign reserves by reducing diesel imports, increase the value-added of the downstream CPO industry, and reduce carbon emissions from vehicles.

The third policy, was to review and postponed infrastructure projects with high import contents, such as power stations, and raised the domestic contents requirements. Certain incomplete infrastructure projects were postponed by one to two years, which was expected to reduce imports and preserve foreign reserves, considering that electrification projects have a low domestic content of around 20-50%. Through Presidential Decree No. 24/2018, the Government expanded the domestic content requirements to all manufacturing sectors, not only automotive industry, but also other products including mobile phones and computer tablets. This policy was expected to encourage local industries to meet domestic market demand.

The fourth policy, the Government raised the coal production quota for exports and introduced policies to boost tourism. Through Minister of Energy and Mineral Resources Decree No. 1924/K/30/MEM/2018, the Government increased the coal production quota by a combined 100 million tons for 31 firms that have satisfied domestic market obligation in July 2018.

In terms of the tourism sector, the Government instituted policies to increase the number of international arrivals to Indonesia. The Government issued policies to increase airport capacity and international flights at Ngurah Rai International Airport, while also adding more international flights to and from Soekarno Hatta International Airport. The Government also accelerated development of the New Yogyakarta International Airport.

These strategies have had a favorable impact on the current account deficit, which remained within the manageable threshold of 3% of GDP throughout 2018. Moving forward, efforts to improve exports and reduce dependence on imports, need to be further strengthen, in order to ensure improvement in the current account deficit performance and, therefore, achieve sustainable economic growth.

II.1.5 Trade Balance

The non-oil and gas trade balance declined as imports rose to meet solid domestic demand. All import components rose, including raw materials, capital goods, and consumer goods. Imports of raw materials – to fuel increasing production activity – drove the higher non-oil and gas imports. The surge in imports of raw materials was primarily led by processed raw materials for industry. These materials support production activity for domestic consumption and export demand. Imports of raw materials were also nudged upwards by demand for spare parts and equipment relating to capital goods for electrification and telecommunications projects. In addition to raw material imports, imports of capital goods and consumer goods also increased to meet growing domestic demand. The rise of capital goods imports triggered in part by faster investment growth, among others, to support government infrastructure projects. Consumer goods imports rallied in line with increasing domestic household and government consumption.

The declining non-oil and gas trade balance also stemmed from slower growth of non-oil and gas exports, as the result of global economic slowdown and sliding international commodity prices. Exports of primary goods, which account for more than 50% of total exports, fell due to declining export of crude palm oil (CPO) and coal. CPO prices were weighed down by lower prices of viable substitutes, primarily soybean. CPO export volume also decelerated, held back by lower shipments to India, a major export destination, after the country raised import duties on CPO at the beginning of the year. The slowdown are mainly due to the decreasing coal export bound for China in line with the country's environmental policy to reduce pollution by restricting use of low-calorie coal. For the whole year, the goods trade balance deteriorated in 2018 to record a USD 431 million deficit after posting a USD 18,785 million surplus in 2017 because of strong import growth (20.7% yoy) combined with moderate export growth (7.0% qtq). Such developments were explained by a reduced non-oil and gas trade surplus together with a larger oil and gas trade deficit.

The oil trade deficit increased to USD 18,392 million in 2018 from USD 12,816 million in 2017. A higher oil import value was the main contributor to the larger oil trade deficit, affected by the increasing global oil price amid stronger domestic demand. Growth of oil exports slowed, however, the decrease was influenced by lower oil lifting, which fell to 778.000 barrels per day in 2018 from 803,000 barrels per day in 2017, due to natural decline across various oil fields.

In addition to the impact of declining world trade volume, a significant drop in the Indonesia Commodity Export Price Index (IHKEI) also undermined export growth. The declines were led by coal and vegetable oil due to deeper price corrections. Furthermore, a large coal inventory in China and the introduction of import quotas linked to China's energy policy also amplified downside pressures on coal prices. The table shows Indonesia's Trade Balance in spanning 2015-2018 as below:

Table 9: Indonesia's Trade Balance 2015-2018

(million USD)

ITEMS	2015	2016	2017	2018
Goods	**14,049**	**15,318**	**18,814**	**-431**
- Exports	149,124	144,470	168,883	180,747
- Imports	-135,076	-129,152	-150,069	-181,178
A. General merchandise	**13,319**	**14,744**	**17,915**	**-422**
1. Non-oil and gas	**19,023**	**19,516**	**25,264**	**11,166**
a. Exports	130,541	130,188	151,429	161,082
b. Imports	-111,518	-110,672	-126,164	-149,917
2. Oil	**-13,106**	**-9,680**	**-12,816**	**-18,392**
a. Exports	7,833	6,267	7,503	7,867
b. Imports	-20,938	-15,947	-20,319	-26,259
3. Gas	**7,402**	**4,908**	**5,467**	**6,805**
a. Exports	9,351	6,649	8,070	9,776
b. Imports	-1,949	-1,741	-2,604	-2,971
B. Other goods	**730**	**574**	**899**	**-9**
o/w Nonmonetary gold	730	574	899	-9
a. Exports	1,400	1,365	1,881	2,022
b. Imports	-670	-792	-982	-2032
Memorandum:				
1. Nominal				
a. Total exports (fob)	149,124	144,470	168,883	180,747
- Non-oil and gas	131,941	131,554	153,310	163,104
- Oil and gas	17,184	12,916	15,573	17,642
b. Total imports (fob)	-135,076	-129,152	-150,069	-181,178
- Non-oil and gas	-112,189	-111,464	-127,146	-151,948
- Oil and gas	-22,887	-17,688	-22,922	-29,229
2. Growth (%, yoy)				
a. Total exports (fob)	-14.93	-3.12	16.9	7.00
- Non-oil and gas	-9.96	-0.29	16.5	6.40
- Oil and gas	-40.24	-24.83	20.6	13.30
b. Total imports (fob)	-19.75	-4.39	16.2	20.70
- Non-oil and gas	-12.17	-0.65	14.1	19.50
- Oil and gas	-43.6	-22.72	29.6	27.50
3. Crude oil unit prices (USD/barrel)	48.79	39.27	51.3	68.20
4. Crude oil production (million barrels per day)	0.79	0.83	0.802	0.78

Source: Bank of Indonesia, 2019

II.1.6 Service Account, Primary Income Account and Secondary Income Account

In general, the services trade balance improved in 2018, backed by a larger travel services surplus in line with government efforts to boost foreign exchange receipts from tourism. Consequently, the services trade deficit narrowed 4.3% (yoy) in 2018 to USD 7,101 million from USD 7,379 million in 2017 (see Table 10). The improvements primarily stemmed from a wider travel services surplus as the number of visits by international travellers to Indonesia soared 7.7% (yoy) from 12,199 million in 2017 to 13,138 million in 2018 . Nonetheless, further gains in the services trade balance were negated by increasing freight services payments consistent with growing imports of goods.

The services trade performance improved and compared with conditions in the previous period, thereby negating further increases in the current account deficit. The smaller services trade deficit stemmed from a larger travel services trade surplus in line with seasonal trends and also boosted by the hosting of international events. Travel services payments were decreasing in the previous period in line with the spending patterns of Indonesian travelers visiting abroad, which declined in the reporting period despite an increase in the number visit of Indonesian travellers.

On the other hand, travel services receipts from international travellers stood and decreased as the number of visits to Indonesia by international travelers, among other as a corollary of natural disasters and aviation incidents in the reporting period. Nevertheless, further declines of travel services receipts were restrained by several international events, including the Asian Para Games contested in Jakarta and the IMF-World Bank Annual Meetings held in Bali, as well as the prevailing spending habits of international travelers that tend to increase in the reporting period. Most international travelers visiting Indonesia originated from Malaysia, Singapore, and China, with Bali, Jakarta, and Batam still recognized as the preferred destinations.

As the dominant contributor to the services trade deficit, transportation services deficit expanded on the back of increasing freight services payments and in line with an upswing of goods import. In addition, passenger transportation services also recorded a larger deficit as more Indonesian travellers journeyed abroad.

Table 10: Indonesia's Service Account 2015-2018

(million USD)

ITEMS	2015	2016	2017	2018
Services	**-8,697**	**-7,084**	**-7,379**	**-7,101**
- Exports	22,221	23,324	25,328	27,932
- Imports	-30,918	-30,407	-32,707	-35,034
A. Manufacturing services	**356**	**351**	**354**	**382**
- Exports	356	351	354	382
- Imports	-	-	-	-
B. Maintenance and repair services	**-340**	**-353**	**-178**	**-201**
- Exports	284	411	169	242
- Imports	-624	-764	-348	-443
C. Transport	**-6,146**	**-5,544**	**-6,864**	**-8,837**
- Exports	3,456	3,572	3,472	3,600
- Imports	-9,602	-9,116	-10,336	-12,438
a. Passenger	-1,215	-1,006	-1,105	-1,371
- Exports	1,293	1,360	1,552	1,486
- Imports	-2,508	-2,366	-2,656	-2,857
b. Freight	-5,204	-4,387	-5,581	-6,922
- Exports	1,406	1,676	1,283	1,537
- Imports	-6,610	-6,064	-6,865	-8,458
c. Other	273	-151	-178	-545
- Exports	758	536	637	577
- Imports	-484	-687	-815	-1,122
D. Travel	**3,469**	**3,639**	**4,850**	**5,338**
- Exports	10,761	11,206	13,139	14,110
- Imports	-7,292	-7,566	-8,289	-8,772
E. Construction	**-74**	**93**	**183**	**278**
- Exports	379	226	369	417
- Imports	-453	-133	-186	-139
F. Insurance and pension services	**-888**	**-661**	**-570**	**-643**
- Exports	54	80	83	86
- Imports	-942	-741	-653	-728
G. Financial services	**-497**	**-577**	**-442**	**-439**
- Exports	248	336	640	658
- Imports	-744	-913	-1082	-1,097
H. Charges for the use of intellectual property	**-1,601**	**-1,686**	**-1,851**	**-1,401**
- Exports	52	47	50	61
- Imports	-1,653	-1,732	-1,901	-1,462
I. Telecommunications, computer, and information services	**-820**	**-1,175**	**-1,536**	**-1,583**
- Exports	971	970	997	1,294
- Imports	-1,791	-2,146	-2,533	-2,877
J. Other business services	**-2,670**	**-1,836**	**-1,947**	**-939**
- Exports	4,917	5,359	5,261	5,997
- Imports	-7,587	-7,194	-7,208	-6,936
K. Personal, cultural, and recreational services	**45**	**36**	**74**	**278**
- Exports	111	89	131	367
- Imports	-67	-53	-57	-89
L. Government goods and services	**469**	**630**	**547**	**666**
- Exports	632	678	663	717
- Imports	-163	-48	-115	-52
Memorandum: Number of traveler (thousands of people)				
- Inbound	9,794	10,860	12,199	13,138
- Outbound	8,345	8,509	9,077	9,756

Source: Bank of Indonesia, 2019

For overall year 2018, the primary income account deficit narrowed from USD 32,131 million in 2017 to USD 30,420 million in 2018 (see Table 11), supported by lower net payments on direct investment and other investment income in line with the higher rates of return on various offshore investment instruments. The performance of the primary income account improved thus contributing to improvements in the current account. The primary income account deficit reduced and buoyed by lower interest payments on government debt securities following historical trends. Moreover, an influx of income receipts on Indonesia direct investment abroad also contributed to a smaller primary income account deficit.

Table 11: Indonesia's Primary Income Account 2015-2018

(million USD)

ITEMS	2015	2016	2017	2018
Primary Income	**-28,379**	**-29,647**	**-32,131**	**-30,420**
- Receipts	2,822	4,048	5,575	9,162
- Payments	-31,201	-33,695	-37,706	-39,582
A. Compensation of employees	**-1,361**	**-1,553**	**-1,507**	**-1,503**
- Receipts	213	219	228	241
- Payments	-1,574	-1,772	-1,735	-1,744
B. Investment income	**-27,018**	**-28,094**	**-30,624**	**-28,916**
- Receipts	2,609	3,829	5,347	8,921
- Payments	-29,627	-31,923	-35,970	-37,837
a. Direct investment income	**-18,504**	**-17,593**	**-19,773**	**-17,129**
1) Income on equity capital	-17,081	-16,557	-18,816	-16,007
- Receipts	72	1,101	1,999	4,895
- Payments	-17,153	-17,658	-20,815	-20,902
2) Income on debt (interest)	-1,423	-1,036	-957	-1122
- Receipts	16	74	14	42
- Payments	-1,440	-1,109	-971	-1164
b. Portfolio investment income	**-6,460**	**-8,318**	**-8,600**	**-9,718**
1) Income on equity capital	-1,936	-1,920	-2,457	-3,183
- Receipts	283	828	395	464
- Payments	-2,219	-2,748	-2,852	-3,646
2) Income on debt (interest)	-4,525	-6,398	-6,144	-6,536
- Receipts	1,812	1,134	2,157	2,449
- Payments	-6,337	-7,532	-8,301	-8,985
c. Other investment income	**-2,053**	**-2,183**	**-2,250**	**-2,069**
- Receipts	426	694	782	1,071
- Payments	-2,479	-2,876	-3,032	-3,140

Source: Bank of Indonesia, 2019

The secondary income account for the whole 2018 recorded a USD 6,892 million surplus, improving from USD 4,498 million in 2017 (see Table 12). The increase stemmed from a surge of net remittances in line with government efforts to empower Indonesian migrant workers. Such developments were explained by an increase of private and government grant receipts relating to the recent natural disasters. Meanwhile, personal transfer receipts in the form of remittances from Indonesian migrant workers remained stable and still represent the main source of the secondary income account surplus.

At the end of 2018, a total of 3.65 million Indonesians were employed as migrant workers abroad. Data from the National Board for the Placement and Protection of Overseas Workers (BNP2TKI) indicated that around 70% of Indonesian migrant workers were placed in the Asia-Pacific region, dominated by Malaysia, Hong Kong, Taiwan, and Singapore. Meanwhile, the remainder were located in the Middle East and Africa, primarily in Saudi Arabia, United Arab Emirates, and Jordan. By country of origin, Indonesian migrant workers located in the Asia-Pacific region were the main contributors of remittances, totalling USD1.7 billion, followed by the Middle East and Africa at USD1.1 million.

Table 12: Indonesia's Secondary Income Account 2015-2018

(million USD)

ITEMS	2015	2016	2017	2018
Secondary Income	**5,508**	**4,460**	**4,500**	**6,892**
- Receipts	10,362	9,832	9,967	12,217
- Payments	-4,853	-5,371	-5,467	-5,325
A. General government	**149**	**365**	**411**	**384**
- Receipts	150	366	416	384
- Payments	-1	-1	-5	-
B. Other sectors	**5,360**	**4,095**	**4,089**	**6,508**
1. Personal transfers	6,415	5,309	5,319	7,567
- Receipts	9,447	8,687	8,761	10,971
- Payments	-3,031	-3,378	-3,442	-3,404
2. Other current transfers	-1,056	-1,214	-1,230	-1,059
- Receipts	765	778	790	862
- Payments	-1,821	-1,992	-2,019	-1,921
Memorandum:				
- Number of Indonesian migrant worker/TKI (thousands of people)	3,686	3,511	3,549	3,650
- Number of foreign migrant worker/TKA (thousands of people)	86	97	96	94

Source: Bank of Indonesia, 2019

II.1.7 Capital and Financial Account

In year 2018, the capital and financial account surplus narrowed for the whole year compared with dynamics in 2017 as a consequence of high uncertainty blighting global financial markets that triggered a rebalancing of foreign capital, especially in the stock and government debt security markets. Therefore, the capital and financial account surplus declined from USD 28,732 million in 2017 to USD 25,201 million in 2018, influenced by smaller portfolio investment and direct investment surpluses. On the other hand, other investment regained upward momentum to record a surplus, thus preventing further erosion of the capital and financial account surplus.

Optimism surrounding the Indonesian economic outlook coupled with competitive yields on domestic financial assets contributed to a significant increase in the capital and financial account surplus 2018. The gains mainly stemmed from a larger portfolio investment surplus driven by an influx of non-resident capital inflows drawn to long-term rupiah denominated securities along with mounted issuances of global bonds by the Government and private sector. In addition, a bigger other investment surplus also contributed to the capital and financial account surplus, induced by withdrawals of private sector offshore deposits and trade credits by the corporate sector to fund strong import growth.

II.1.8 Investment

The Indonesian market can be regarded as a paradise for investors, both local and foreign. This is because, Indonesia has become one of the most potential markets in the Asian region, where in 2018 investment development in Indonesia increases. Indonesia is still categorized as developing countries and this status drives many invasions by both domestic investors and foreign companies want to expand their product or service marketing network to Indonesia.

There are several factors that are quite influential in slowing the growth of investment realization in 2018. The fluctuation of the rupiah exchange rate and the United States trade war with China have an impact on slowing the pace of investment and entering a political year that will continue until next year. Within these conditions that are full of uncertainties, investment seems to be slowing down and investors are waiting.

Overall, the Indonesian economy showed improved performance with a stronger structure. Throughout 2018, economic growth was recorded at 5.17% and was the highest in the last four years. The improvement in economic performance was supported by a stronger structure in line with increased investment and export performances. The increase in investment performance is in line with the continued development of infrastructure and the continued high level of non-construction investment in anticipation of increased demand going forward.

In order to increase BKPM investment through the government, it will ensure that various facilities and simplification of procedures for investment activities that have been issued by the Government, both through Government Regulations, Presidential Regulations and Regulations of Ministers/Institutions concerned, run well that can provide legal certainty and business certainty. For this reason, government will always open itself to various efforts to improve what businesses still encounter obstacles in the businesses field.

BKPM noted, the performance of the Indonesian economy in the last 3 years showed an increase, where domestic investment was realized throughout 2017 reached Rp 262.35 trillion, an increase of 21.33% compared to 2016 which only reached Rp 216.23 trillion. The increase in the value of domestic investment was also followed by an increase in the number of projects that absorbed the value of the investment, the number of projects absorbed increased from 7,511 projects in 2016 to 8,838 projects in 2017 or an increase of 17.67%.

The total investment flowed by the public or domestic companies in 2018 reached Rp 328.35 trillion. Compared to the previous year, this value showed an increase of 25.25%. Likewise, the number of projects that were able to absorb the value of investment in 2018 also increased by 22.37% to 10,815 projects.

II.1.9 Direct Investment

For the whole 2018, maintained foreign investor confidence in Indonesia's economic outlook spurred long-term investment in the country, precipitating a net surplus of direct investment totalling

USD13,841 million. Nonetheless, the surplus was lower than the USD18,502 million achieved in 2017, primarily as a result of increasing Indonesian direct investment in companies abroad.

Investor perception on Indonesia continues to improve, thereby precipitating positive direct investment performance. In 2018, direct investment recorded primarily from foreign inflows of direct investment (liability side). The surplus narrowed because the decline of direct investment inflows on the liability side exceeded the decreased outflows of Indonesian direct investment abroad on the asset side. On the asset side, the net outflow of direct investment by Indonesian residents was recorded down due in part to the acquisition of an Australian coal mine. On the liability side, foreign direct investment recorded down 2018. The smaller surplus was attributed to outflows apropos of stock acquisitions by domestic firms of several FDI companies operating in the mining. By omitting those transactions, however, the net foreign inflow of direct investment in 2018 exceeded amongst others supported by capital injection into a number of Indonesian start-up companies.

The acquisition of an Australian mining firm in 2018 triggered a higher direct investment outflow on the asset side in 2018 compared with 2017. On the other hand, the net inflow of foreign direct investment (liability side) stood down slightly from 2017. Such stability is in line with strong domestic investment activity, as corroborated by 6.67% (yoy) growth of Gross Fixed Capital Formation (GFCF) compared with 6.15% (yoy) in 2017.

Based on the direction of investments, the net inflow of foreign direct investment (FDI) in Indonesia for the whole year was recorded the net inflow of FDI stood at USD 21,980 million in 2018, up from USD 20,579 million in 2017. By sector, trade and manufacturing continued to dominate FDI inflows in 2018 for both sectors compared with the previous year. Nevertheless, the mining sector booked a FDI outflow, amongst others influenced by the acquisition of several FDI companies in the sector by domestic firms.Similar dynamics were observed on an annual basis, with manufacturing again dominating FDI inflows in 2018, followed by trade, with both sectors attracting a total of USD20.7 billion, up 46.2 % on the USD14.2 billion realised in 2017.

By country of origin, emerging Asia (including China) led FDI inflows booked in 2018, followed by investors from ASEAN and Japan. A similar trend was apparent annually, with emerging markets in Asia (including China) dominating FDI inflows to Indonesia, followed by investors from the ASEAN region.

The FDI reading for 2018 is relatively consistent with the FDI realisation data published by the Indonesia Investment Coordinating Board (BKPM) . Based on BKPM numbers, FDI realisation for the whole year totalled Rp 392.7 trillion (equivalent to USD 29.3 billion), decreasing from Rp 430.5 trillion (equivalent to USD 32.1 billion) in 2017. By sector, BKPM reported that FDI realisation in 2018 was concentrated in the utilities sector (Electricity, Water, and Gas supply), followed by the Transportation, Storage, and Telecommunications sector; the Mining sector; the Residential, Industrial and Office sector: as well as the Base Metals, Articles of Metal, Machinery and Electronics Industry. Based on country of origin, however, Singapore, Japan, Malaysia, China, and Hong Kong were the largest investors to account for 70.4% of total FDI.

Table 13: Indonesia's Direct Investment 2015-2018

(million USD)

ITEMS	2016	2016	2017	2018
Direct Investment	**10,704**	**16,136**	**18,502**	**13,841**
A. Assets	**-9,075**	**11,594**	**-2,008**	**-6,330**
1. Equity capital	-7,998	10,676	-2,603	-5,517
2. Debt instruments	-1076	919	595	-813
B. Liabilities	**19,779**	**4,542**	**20,510**	**20,171**
1. Equity capital	18,822	4,684	18,839	20,377
2. Debt instruments	957	-142	1,671	-205
a. Inflow	75,588	50,638	49,415	48,203
b. Outflow	-74,631	-50,780	-47,744	-48,408
Memorandum:				
Direct investment based on directional principle	**10,704**	**16,136**	**18,502**	**13,841**
A. Direct investment abroad	**-5,937**	**12,215**	**-2,077**	**-8,139**
1. Equity capital	-4,237	12,058	-2,133	-5,449
2. Debt instruments	-1,700	156	56	-2,690
B. Direct investment in Indonesia	**16,641**	**3,921**	**20,579**	**21,980**
1. Equity capital	15,060	3,301	18,369	20,309
2. Debt instruments	1,581	620	2,210	1,671

Source: Bank of Indonesia, 2019

II.1.10 Portfolio Investment

For the whole 2018, the net surplus of portfolio investment decreased significantly to USD 9,342 million from USD 21,059 million in 2017 as foreign capital poured out of the stock market and rupiah government debt securities, particularly during the first three quarters of the year, coupled with a large number of maturing government global bonds in 2018.

Mirroring portfolio investment developments in the public sector, the net foreign inflow to private sector debt instruments stemming primarily from corporate global bond issuances. Therefore, the Jakarta Composite Index (JCI) traded up and rally recorded was echoed by improving stock market performance in the Philippines, juxtaposing the corrections experienced in Thailand, Malaysia, and Singapore. Stock market activity in Indonesia Stock Exchange during 2018 was supported by 20 additional new issuers of initial public offerings (IPO). The total value fell short recorded by 16 new issuers in the previous period. By sector, the private and public sectors, both contributed surplus of portfolio investment recorded in 2018. The private sector regained a USD 5,011 million surplus in the in 2018 after recording a USD 2,537 million surplus in 2017. Meanwhile, the public sector posted a USD 9,504 million surplus, decreasing from USD 21,877 million in 2017.

Table 14: Indonesia's Portfolio Investment 2015-2018

(million USD)

ITEMS	2015	2016	2017	2018
Portfolio Investment	**16,183**	**18,996**	**21,059**	**9,342**
A. Assets	**-1,268**	**2,218**	**-3,356**	**-5,173**
1. Public Sector	392	1,795	-9	228
a. Equity capital	-	-	0	0
b. Debt securities	392	1,795	-9	228
2. Private Sector	-1,660	423	-3,346	-5,401
a. Equity capital	-758	-210	-1,560	-1,419
b. Debt securities	-903	633	-1,787	-3,981
B. Liabilities	**17,451**	**16,778**	**24,415**	**14,515**
1. Public Sector	17,386	16,835	21,877	9,504
a. Equity capital	N/A	N/A	N/A	N/A
b. Debt securities	17,386	16,835	21,877	9,504
1) Central bank	-135	114	-104	62
2) Government	17,521	16,720	21,982	9,441
a) Short term	-38	-444	1,715	-1,069
b) Long term	17,559	17,164	20,267	10,510
2. Private Sector	65	-57	2,537	5,011
a. Equity capital	-1,547	1,319	-2,538	-3,668
b. Debt securities	1,612	-1,376	5,075	8,679
1) Short term	-2,335	-291	318	-732
2) Long term	3,947	-1,085	4,757	9,412
Memorandum:				
Government's debt securities, liabilities	**17,521**	**16,720**	**21,982**	**9,441**
1. Denominated in Rupiah	7,518	8,047	12,794	3,963
2. Denominated in foreign currency	10,003	8,673	9,188	5,479

Source: Bank of Indonesia, 2019

II.1.11 Portfolio Investment

For overall 2018, other investments transactions recorded a net surplus of USD 1,999 Million, reversed from a USD 10,747 billion deficit in 2017. The reversal was not only due to private sectors' deposits withdrawals from foreign banks yet also the result of a larger surplus on the liability side of private sectors' other investments, driven by a surge of corporate sectors' withdrawals of loans and trade credits. The improving performance of other investment was mainly driven by the reducing deficit of other investment transactions on the asset side and the increasing surplus of other investments transactions on the liabilities side.

On the asset side, private sectors' other investments decreased its deficit to USD 9,228 million from a USD 13,487 million deficit in 2017. The narrower deficit stemmed from withdrawals of private sectors' deposits in foreign banks and a decrease of loans extended by the private sectors to non-residents. On the liability side, private sector's other investments transactions in 2018 recorded a net inflow totalling USD 12,210 million, higher than USD 4,093 million in 2017 due to an increase of corporates' trade credits.

Meanwhile, public sectors' other investments liabilities experienced a USD 983 million deficit in

2018, decreased from USD 1,353 million deficit recorded in 2017. The deficit was caused by the government's foreign loan payments amounting more, while the government only drew less in the form of program loans and project loans.

Table 15: Indonesia's Other Investment Account 2015-2018

(million USD)

ITEMS	2016	2016	2017	2018
Other Investment	**-10,064**	**-5,817**	**-10,747**	**1,999**
A. Assets	**-11,812**	**1,499**	**-13,487**	**-9,228**
1. Public Sector	-	-269	-	-
2. Private Sector	-11,812	1,768	-13,487	-9,228
a. Currency and deposits	-7,411	2,940	-8,193	-3,646
b. Loans	-1,034	-480	-2,422	-3,557
c. Trade credit and advances	-2,232	-725	-1,265	-736
d. Other assets	-1,134	33	-1,607	-1,288
B. Liabilities	**1,748**	**-7,316**	**2,740**	**11,227**
1. Public Sector	-190	-2,369	-1,353	-983
a. Currency and deposits	-	-	-	-
b. Loans	202	-574	-1,362	-755
1) Central bank [1]	-33	-48	-145	-
a) Drawings	-	-	-	-
b) Repayments	-33	-48	-145	-
2) Government	235	-525	-1,217	-755
a) Drawings	5,139	4,619	3,645	4,588
(1) Program	3,891	2,772	1,612	3,492
(2) Project	1,248	1,847	2,033	1,097
(3) Other	-	-	-	-
b) Repayments	-4,904	-5,145	-4,862	-5,344
c. Other liabilities	-392	-1,795	9	-228
2. Private Sector	1,938	-4,947	4,093	12,210
a. Currency and deposits	768	-471	186	125
b. Loans	883	-5,282	2,064	9,503
1) Drawings	30,372	20,400	23,252	33,345
2) Repayments	-29,489	-25,683	-21,187	-23,843
c. Trade credit and advances	401	998	1,626	2,460
d. Other liabilities	-114	-192	216	123

Note: [1] Excludes credit and loans with IMF
Source: Bank of Indonesia, 2019

II.1.12 Export

For the whole year, oil exports expanded 4.9% (yoy) in 2018 on rising export prices despite lower export volume due to less lifting and a greater allocation to meet domestic demand. The decline of oil exports was precipitated by lower oil prices and decreased export volume, affecting crude oil in particular. Annually, crude oil lifting was realised at 0.778 million barrels per day in 2018, which is below the target stipulated in the 2018 state budget of 0.800 million barrels per day as well as the 0.803 million barrels per day realised in 2017. The downturn was due to weaker performance than expected at new wells, a greater decline rate affecting maturing wells, and postponement of new well development programs.

For the whole year, gas exports reached USD 9.8 billion, or expanding 21.1 % (yoy), on rising gas export prices in line with higher international oil prices. Gas exports recorded annual (26.8% yoy) gains in 2018. The gains come amidst increasing liquefied natural gas (LNG) imports due to higher export prices.

For the whole year, growth of non-oil and gas exports to Indonesia's main trading partners decelerated in 2018 compared with dynamics in 2017. Exports declines affected most major trading partners in 2018 such as China, United States, Japan, India, Singapore, Malaysia, South Korea, Philipine, and Thailand, except Vietnam. The non-oil and gas export decline was attributed to real exports of primary products, which experienced a deeper contraction, as well as slower rising export prices. For the whole year, non-oil and gas exports totalled USD 162,841.0 million in 2018, with growth decelerating to 6.4% (yoy) from 15.9% (yoy) in 2017 due to a real export contraction along with flatter price growth.

Exports of the major non-oil and gas commodities in 2018 are coal, vegetable oil, textiles and textile products, articles of basic metals, electrical apparatus, processed foods, vehicles and parts, processed rubbers, machineray and mechanical appliances, and footwear.

Table 16: Indonesia's Export 2015-2018

(million USD)

ITEMS	2015	2016	2017	2018
EXPORT	150,366.3	145,186.2	168,828.2	180,012.7
- OIL AND GAS	18,574.4	13,105.5	15,744.3	17,171.7
- NON OIL AND GAS	131,791.9	132,080.8	153,083.9	162,841.0

Source: Statistics Indonesia, 2019 and Bank of Indonesia, 2019

II.1.13 External Debt

External resilience was underpinned by a sound and controlled external debt profile. External debt grew 6.9% in 2018 to USD 376.8 billion, decelerating from 10.1% growth in 2017. The slowdown primarily stemmed from slowing public sector borrowing in line with the narrower fiscal deficit. Public sector external debt accounts for 49.4% of the total external debt, with growth of 3.1%, down significantly from 14.1% growth in 2017. On the other hand, growth in private external debt, accounting for the remaining 50.6%, accelerated to 10.9% in 2018 from 6.3% from 2017. A manageable level of external debt was accompanied by a sound external debt structure, as reflected by a ratio of external debt to GDP of 36.18% at the end of 2018, a slight increase from 34.68% in 2017. The external debt ratio in Indonesia was consistent within the average range of peer countries.

External debt risks also remain manageable, in line with the consistency of Bank Indonesia and the Government in monitoring and minimizing external debt risks. Bank Indonesia’s monitoring of external debt developments are primarily conducted through the application of prudential principles for external debt management. Bank Indonesia pursues a policy of prudential principles implementation (KPPK) for the management of non- bank private external debt to mitigate exchange rate risk, liquidity risk, and overleverage risk. Bank Indonesia’s requirements have been soundly implemented, with implementation and reporting compliance increasing throughout the first three quarters of 2018. Low and contained external debt risks were also identified by the comparatively small portion of short-term non-affiliated non-bank private sector external debt, accounting for just 8% of total private external debt. Meanwhile, the Government remained committed to maintain a manageable level of external debt with a sound structure. Furthermore, the Government constantly optimizes external debt management and the role of external debt to support financing without triggering risks that could potentially disrupt economic stability.

Table 17: Indonesia's External Debt 2015-2018

(%)

Debt Burden Indicators	2016	2016	2017	2018
Short Term Debt by Original Maturity to Total Debt Ratio	12.46	12.68	13.91	13.71
Short Term Debt by Remaining Maturity to Total Debt Ratio	17.86	17.1	15.54	15.77
Short Term Debt by Original to Reserve Ratio	36.55	34.88	37.63	42.82
Short Term Debt by Remaining Maturity to Reserve Ratio	52.39	47.02	42.06	49.24
Debt Service Ratio – Quarterly				
- DSR Tier	30.57	35.35	25.16	24.08
- DSR Tier	62.95	61.56	52.42	52.85
Debt Service Ratio - Annualized				
- DSR Tier	30.57	35.35	25.16	24.08
- DSR Tier	62.95	61.56	52.42	52.85
Debt to Export Ratio - Annualized	168.39	176.14	167.73	163.8
Debt to GDP Ratio	36.09	34.3	34.68	36.18

Source: 2018 External Debt Statistics of Indonesia by Bank of Indonesia

II.1.14 Exchange Rate

In 2018, pressure on the rupiah exchange rate was triggered to a large extent by escalating global uncertainties due to increases in the FFR and heightened uncertainty on global financial markets. This resulted in global appreciation of the US dollar, as seen in rising dollar index (DXY) to an average of 95.5 in August 2018 from 93.4 in December 2017. These adverse developments have led to increased risk-averse behavior with regard to capital flows to emerging markets. As a result, foreign capital inflows into emerging economies fell significantly during 2018. Data from the Institute of International

Finance shows foreign capital flows to emerging markets plunged to USD 8 trillion in 2018 from USD 102 trillion in 2017.

Pressure on the rupiah exchange rate was also driven by a decline in Indonesia's net exports in 2018. High demand for foreign currency resulted from a surge in imports for the first three quarters of 2018 driven by solid domestic demand. For the first three quarters of 2018, non-oil gas imports grew 22.5% on average, well above the 13.9% growth in the previous year. However, supply of foreign currency from exports declined in the second half of 2018, due to weakening global economic growth and falling commodity prices. In addition, non-oil and gas exports grew by 4.0% in the second half of 2018, well below the 16.7% growth in the full year 2017.

These global and domestic developments strengthened net forex demand and put downward pressure on the rupiah from February to the end of October 2018. During this period, the rupiah depreciated 12.5%, reached the lowest level at IDR 15,235 to the US dollar. Rupiah volatility in this period also climbed to 8.1% from 7.0% recorded in January 2018.

Pressure on the rupiah also came from the escalating trade tensions between the US and China, which prompted higher risk premiums in emerging markets, was China took retaliatory action by imposing tariffs on 106 products imported from the US after US decision to impose a 25% tariff on imports from China in April 2018.

Besides China, trade tensions also escalated between the US and its other trading partners. The US announced plans to double the import tariffs on steel and aluminum, which has major consequences for the countries exporting those products, particularly Turkey. The lira exchange rate weakened dramatically, and on 15 August 2018 – depreciated by as much as 7.02%. These conditions ultimately led to higher risk premiums and contributed directly to exchange rate depreciation in emerging markets, including Indonesia.

Geopolitical risks triggered higher risk premiums in emerging marketand also put pressure on the rupiah between February and October 2018. Geopolitical issues included those related to escalating tensions on the Korean peninsula and in the Middle East, the dynamics of the Brexit negotiations between the United Kingdom and the European Union, and economic problems in Italy. The crises in Turkey and Argentina also led to heightened perceptions of risk in other emerging economies.

Amid these dynamics, the rupiah recorded average depreciation of 6.05% in 2018, at IDR14,246 to the US dollar from the 2017 of IDR13,385. Point to point (end-2018 versus end-2017), the rupiah weakened 5.65% to close 2018 at a level of IDR14,380 to the US dollar.

Table 18: Indonesia's Exchange Rate 2015-2018

(Rupiah

CURRENCY	2015	2016	2017	2018
USD ($1)	13,795	13,473	13,568	14,380

Source: 2018 External Debt Statistics of Indonesia by Bank of Indonesia

II.1.15 Inflation

In 2018, inflation remained at a low, subdued level within the 3.5±1% target range despite the rupiah depreciation over this period. At the end of 2018, December CPI inflation was 3.13%, marking the fourth consecutive year that inflation remained on target. Inflation was low in 2018 both in comparison to the 2017 level (3.61%) and the combined average for the preceding four years (4.59%).

The low inflation can be explained in part by global and domestic cyclical factors. Global food prices fell, helped to keep domestic food prices under control. And, at home, controlled demand levels also led to steady decline in inflationary pressure. Low VF inflation and the minimal AP inflation also contributed to low overall inflation in 2018.

More importantly, however, the low inflation could not have been achieved without the structural improvements of inflation characteristics in recent years. Bank Indonesia has implemented consistent monetary policy that has anchored the inflation expectations of economic actors. This more competitive market structure is also aligned to the increasingly competitive structure of retail market competition amid rapid growth in e-commerce.

Furthermore, improvements in the transparency of food pricing at the consumer level contributed to the downward trend in inflation. Information is provided by institutions such as the Strategic Foods Price Information Center. Another structural improvement contributing to reduced inflation was the more seamless goods distribution and more efficient logistics networks. This achievement was the result of close coordination between Bank Indonesia and the central and regional governments via the Central Inflation Control Team (TPIP) and Regional Inflation Control Teams (TPID). This coordination influenced inflation behavior through the smooth supply of goods especially foods. In addition, the energy subsidies reform held since 2015 has influenced the reduction of the second-round effects of increases in AP on overall inflation.

These structural improvements has a positive effect on inflation behavior. Bank Indonesia's consistent monetary policy successfully anchored inflation expectations to the inflation target. Bank Indonesia estimated that the contribution of forward-looking expectations in the formation of inflation has increased. This has led to a reduction in inflation persistence and in sensitivity of exchange rate pass-through to inflation. Lastly, there was steady decline in the second-round effects of increases in VF inflation and AP inflation on core and overall inflation. The reduction in second-round effects of AP inflation has also influenced by the positive effects of energy subsidy reforms in early 2015.

The positive cyclical developments and beneficial structural changes led to reduction in various components of CPI inflation in 2018. Core inflation remained low in 2018 at 3.07%. VF inflation was also low at 3.39%, below the combined three-year average for the preceding three years, while AP inflation came to 3.36%, well below the 2017 level.

Table 19: Indonesia's Inflation Rate 2015-2018

(%)

Month	2015	2016	2017	2018
January	-0.24	0.51	0.97	0.62
February	-0.36	-0.09	0.23	0.17
March	0.17	0.19	-0.02	0.20
April	0.36	-0.45	0.09	0.10
May	0.50	0.24	0.39	0.21
June	0.54	0.66	0.69	0.59
July	0.93	0.69	0.22	0.28
August	0.39	-0.02	-0.07	-0.05
September	-0.05	0.22	0.13	-0.18
October	-0.08	0.14	0.01	0.28
November	0.21	0.47	0.20	0.27
December	0.96	0.42	0.71	0.62
Inflation Rate	3.35	3.02	3.61	3.13

Source: Statistics Indonesia, 2019

II.1.16 Financial System

Bank Indonesia put in place accommodative macroprudential policies – having considered the current the current financial cycle that is below its long-term trend – and these were supported by wider access to liquidity and adequate capital. These policies were aimed at supporting the intermediation function of banks and stimulating economic growth. In determining Indonesia's macroprudential direction, Bank Indonesia continued to take into account financial system stability, and paid particular attention to risks arising from heightened global uncertainty.

Bank Indonesia made use of several tools in implementing macroprudential policy. First, the loan-to-value (LTV) and financing-to-value (FTV) ratios for home ownership loans were relaxed to drive growth in the property sector, as this has a large multiplier effect on the economy. Second, Bank Indonesia raised the mandatory credit ratio requirement for micro, small and medium enterprises (MSME) to 20% in 2018 from 15% to drive forward MSME. Third, Bank Indonesia brought in macroprudential intermediation ratio (RIM) provisions, which widened the definition of intermediation by including purchases of securities in the ratio calculation. This gives banks more options to channel financing beyond conventional loan financing. Fourth, Bank Indonesia eased its macroprudential liquidity buffer (MLB) policy by giving flexibility to banks in managing higher liquidity: banks can repo to Bank Indonesia securities (SSB) they own representing 4% of rupiah deposits, up from 2%. Fifth, the countercyclical capital buffer (CCB) was maintained at 0% to achieve a balance between efforts to encourage intermediation and efforts to mitigate risks.

Bank Indonesia strived to strengthen macroprudential supervision, while also improving coordination with the Government and financial authorities in order to maintain financial system stability. The strengthening of supervision was focused on banks and corporations that significantly affect the financial system and the strengthening of coordination was focused on synergies between macroprudential and microprudential policies, and also on crisis prevention and handling. In addition, Bank Indonesia actively participated in reforming the global financial sector through its membership of the Financial Stability Board (FSB). The table shows Indonesia's Banking Operation from 2015 until 2018 as below:

Table 20: Indonesia's Banking Industries Operation 2015-2018

(million USD)

Indicator	2015	2016	2017	2018
Distribution of Funds				
Commercial Banks	5,952,279	6,570,903	7,177,549	7,809,987
Rural Banks	98,604	109,389	121,296	130,724
SBI and SBIS [1)]	53,567	96,103	19,901	39,441
Source of Funds				
Commercial Banks	4,909,707	5,399,210	5,921,039	6,475,110
Rural Banks	84,728	93,622	103,874	111,679
Total Assets				
Commercial Banks	6,095,908	6,729,799	7,387,634	8,068,346
Rural Banks	101,713	113,501	125,945	135,693
Total Banks				
Commercial Banks	118	116	115	115
Rural Banks	1,636	1,633	1,619	1,597
Total Bank Offices				
Commercial Banks	32,949	32,73	32,285	31,618
Rural Banks	5,982	6,075	6,192	6,273

Note: [1)] Sharia Indonesian Banking Certificate

r) revised figures

Source: Indonesia Banking Statistics, Vol. 17, No. 10 September 2019

Bank Indonesia's accommodative macroprudential policy has contributed to increasing bank intermediation. Loans grew 11.8% in 2018, up from 8.2% in 2017. Based on loan type, the higher loans growth in 2018 was driven by working capital loans and investment loans, which together grew 12.3%. Higher loan growth was seen in all sectors of the economy, but the highest growth was recorded in the construction sector. Construction loans grew 22.1% in 2018 due to infrastructure development. The increase in bank intermediation was accompanied by a maintained level of risk, whereby the ratio of NPL of banks declined to 2.4% at the end of 2018 from 2.6% at the end of 2017. The NPL ratios for all sectors were within the safe limit of 5%, but mining was highest at 4.7%.

The high growth of bank intermediation in 2018 lessened the impact of the decline in financing from the financial markets. Financing from financial markets dropped 31.1% in 2018, versus 2017 growth of 30.6%. This meant that the overall role of financial markets financing declined to 15.6%. The reduced role reflects, at least in part, the heightened uncertainties in global financial markets, which affected the behavior of the domestic market. Furthermore, the increase in corporate bond yields in line with the increase in policy rates raised the cost of funds for bond issuances.

Amid the accommodative policy response, macroprudential policy consistently maintained financial system stability. This stability, although pressured at times by the heightened global uncertainty, remained in the safe zone for the first three quarters of 2018 and then declined again in the fourth quarter. But the key risk indicators of financial institutions remained within safe and normal limits. The slower growth in deposits compared to loans growth did not significantly affect bank liquidity, as reflected in the liquid assets of banks, which remained within safe limits. Also, the exposure of banks to foreign currencies remained below the maximum permitted limit, though it did increase temporarily due to exchange rate depreciation in the first three quarters of 2018. The stability of the financial system was also underpinned by banks' solid capital level.

Table 21: Indonesia's Commercial Banks Performances in 2015-2018

(billion Rp)

Indicator	2015	2016	2017	2018
Capital Adequacy Ratio (%)	**21.39**	**22.93**	**23.18**	**22.97**
Capital	914,657	1,052,597	1,166,002	1,269,616
Risk Weighted Assets	4,276,555	4,589,611	5,029,816	5,526,581
Core Capital Ratio to ATMR (%)	**19**	**21.19**	**21.5**	**21.29**
Core Capital (Tier I)	812,59	972,35	1,081,234	1,176,700
Risk Weighted Assets	4,276,555	4,589,611	5,029,816	5,526,581
Return On Assets Ratio (%)	**2.32**	**2.23**	**2.45**	**2.55**
Profit	132,601	136,048	165,196	186,912
Average total assets	5,703,813	6,106,959	6,730,350	7,329,250
Operating Expenses/Operating Income (%)	**81.49**	**82.22**	**78.64**	**77.86**
Operating Expenses	569,141	624,173	603,178	638,99
Operating Income	698,404	759,146	766,975	820,646
Net Interest Margin Ratio (%)	**5.39**	**5.63**	**5.32**	**5.14**
Interest income net	293,824	329,913	342,731	360,412
Average total earning assets	5,449,642	5,854,786	6,445,076	7,016,192
Loan to Deposits Ratio (%)	**92.11**	**90.7**	**90.04**	**94.78**
Total Credit to third party	3,903,936	4,199,713	4,548,155	5,092,584
Total Third Party Funds	4,238,349	4,630,352	5,050,984	5,372,841
Liquid Assets Ratio (%)	**16.7**	**17.5**	**18.56**	**14.96**
Primary Liquid Asset	736,72	837,433	963,833	899,937
Secondary Liquid assets	251,623	296,098	353,504	259,472
Total Assets	5,919,390	6,475,602	7,099,564	7,751,621

Note: Data shown is not included the performance data of Commercial Sharia Banks
Source: Indonesia Banking Statistics, Vol. 17, No. 10 September 2019

II.2 Regional Economic Developments

II.2.1 Economic Overview in the Fourth Quarter of 2018

National economic momentum continued to build in the fourth quarter of 2018 on the back of domestic demand. Indonesia’s economy expanded 5.18% in the reporting period, up from 5.17% in the third quarter of 2018. Strong domestic demand stemmed primarily from household consumption in all regions on rising incomes and in line with anchored and rational inflation expectations. In addition, consumption by non-profit institutions serving households (NPISH) also accelerated in the majority of regions in preparation for the legislative and presidential elections to be contested in 2019. Government consumption has also underpinned economic growth through personnel expenditure and social assistance disbursements (bansos), particularly in Java. Solid investment growth has been driven by maintained investor optimism in the domestic economic outlook, despite investment growth decelerating on the previous period due to the completion of infrastructure development projects relating to hosting the Asian Games 2018 in Jakarta and Palembang.

Consonant with strong domestic demand, high import growth persisted against a backdrop of slower export growth triggered by global economic moderation. By sector basis, the main drivers of economic growth in the fourth quarter of 2018 were agriculture, mining and services. Spatially, recent national economic gains were corroborated by stronger economic growth reported in Java, Kalimantan as well as Bali and Nusa Tenggara. Java’s economy accelerated to become the main driver of national economic gains on the back of domestic demand Economic growth in Java hit 5.82%.

On the other hand, economic moderation in Sumatra was caused by investment and exports, yet further declines were offset by increasing private consumption Sumatra’s economy expanded 4.46% Solid domestic demand also contributed to offset economic moderation in Eastern Indonesia caused by the external sector. By region, slower economic growth in Eastern Indonesia was primarily attributable to the contraction experienced in Maluku-Papua together with weaker economic growth in Sulawesi.

II.2.2 Economic Growth

National economic momentum continued to build in 2018 on the back of solid domestic demand in all regions, while net export growth was restrained. The domestic economy grew 5.17% in 2018, representing the fastest pace on record for the past five years. In total, 22 out of 34 Indonesian provinces achieved growth above the national average, led by Java, Sulawesi and Mapua. Compared to 2017 performance, the national economic expansion was supported by faster growth in 18 provinces, particularly Java, Sumatra and Mapua. Domestic demand was the key of economic growth in all regions, which was maintained by improving purchasing power as the Government expanded its social assistance program (bansos) and increased The Village Funds disbursements, backed by low and stable inflation. Furthermore, spending on the local elections in 2018, preparations for the legislative and presidential elections in 2019 as well as ongoing private and government investment continued to elevate domestic demand in 2018. Nevertheless, strong domestic demand also drew higher imports, including consumer goods, raw materials and capital goods, which curbed stronger growth in all regions. Nationally, export growth was relatively subdued due to weak export performance reported in Sumatra, Kalimantan and Bali and Nusa Tenggara.

Economic improvements in Java were the main engine of national economic gains. The sources of growth stemmed from increasing consumption and international exports as well as high investment. Export performance improved in line with CBU exports regaining access to the primary market (Vietnam), expanding automotive exports to Sri Lanka and Thailand as well as a growth surge of services exports as international travellers visited Indonesia to participate in and watch the Asian Games. Solid investment growth was maintained in Java in 2018 despite moderating compared with 2017 after 13 National Strategic Projects were completed, the Government postponed several electrification projects and the corporate sector pared back capital spending. By sector, faster economic growth in Java was led by the Trade sector in line with increasing domestic demand as well as the Manufacturing Industry, which served to confirm persistently solid manufacturing export performance.

Sumatra's economy also gained momentum on increasing domestic demand despite flagging export performance. Sumatra led all other regions in terms of investment growth, driven by government infrastructure development projects, primarily toll roads and sports venues for the Asian Games, the 500kV Sumatra Transmission project and Kuala Tanjung Port. On the other hand, Sumatra also faced escalating pressures due to sliding prices of CPO, rubber and coffee, combined with dwindling demand for CPO from India as a result of import tariffs and a large inventory of soybean oil. By sector, mining, manufacturing and trade were the key growth sources in Sumatra. Mining accelerated on increasing coal production to meet demand from the domestic market. The food and beverage industry as well as trade sector also expanded in line with domestic demand. In addition, the Government's policy to implement the B-20 biodiesel program stimulated the CPO processing industry, with Sumatra positioned as the main supplier.

Indonesia moderated in 2018 due to rapid import growth to meet stronger domestic demand, which accelerated in nearly all provinces of the region due to several factors, namely the completed construction of national strategic projects and non-national strategic projects in nearly all provinces of Eastern Indonesia, infrastructure development for the IMF-World Bank Annual Meetings in Bali and Nusa Tenggara, reconstruction in areas affected by natural disasters and increasing household consumption. Consequently, the impact was a spike in imports of equipment and raw materials to develop underground mines in Mapua, imports of capital goods to support industrial development in Sulawesi as well as imports bound for infrastructure development. On the other hand, export growth improved relatively, primarily due to LNG exports against a backdrop of declining coal prices and demand. Spatially, lower economic growth in Eastern Indonesia was attributable to moderation in Sulawesi, Kalimantan as well as Bali and Nusa Tenggara, mainly due to coal mining performance in Kalimantan.

II.2.3 Growth Domestic Product by Expenditure

Strong domestic demand was the main driver of national economic expansion in 2018. Domestic demand grew 5.62% in 2018, the fastest rate since 2012, driven by household consumption, non-profit institutions serving households (NPISH) and the Government Consumption. In addition, robust growth of gross fixed capital formation (GFCF), supported by both non-construction and construction investment, also contributed to the increasing domestic demand. In turn, strong domestic demand helped offset the external sector's net negative contribution in 2018 – the result of declining exports and high imports.

Table 22: Gross Domestic Product Growth by Expenditure in 2015-2018

(percent, yoy)

Component of GDP	2015	2016	2017	2018
Domestic Demand[1)]	**4.94**	**4.39**	**5.13**	**5.62**
Private Consumption	4.84	5.04	4.98	5.13
Household Consumption	4.96	5.01	4.94	5.05
Non-Profit Institutions Serving Households (NPISH) Consumption	-0.62	6.64	6.93	9.08
Government Consumption	5.31	-0.14	2.13	4.80
Investment[2)]	**3.00**	**4.99**	**5.69**	**8.52**
Gross Fixed Capital Formation (GFCF)	5.01	4.47	6.15	6.67
Construction	6.11	5.18	6.24	5.45
Non-Construction	1.93	2.43	5.90	10.31
Change in Inventories	-0.59	0.23	-0.07	0.71
Net Exports*	**0.94**	**0.13**	**0.31**	**-0.98**
Exports	-2.12	-1.66	8.91	6.48
Imports	-6.25	-2.41	8.06	12.04
Gross Domestic Product	**4.88**	**5.03**	**5.07**	**5.17**

Note: 1) Domestic Demand is equal to Consumption Expenditures (Private + Government) and Gross Fixed Capital Formation
2) Investment is equal to Gross Fixed Capital Formation and Change in Inventories
*Contribution to GDP

Source: Bank of Indonesia, 2019

II.2.4 Growth Domestic Product by Industrial Origin

By sector, economic expansion in 2018 was primarily driven by the secondary and tertiary sectors. Congruent with solid domestic demand, wholesale and retail trade accelerated to 4.97% in 2018 from 4.46% in 2017. Furthermore, increasing domestic demand stimulated intermediation activity among wholesalers, and enabled them to create value added in the trade sector. International events, such as the Asian Games and IMF–World Bank Annual Meetings also boosted trade. Consequently, the Retail Sales Index rose, with growth accelerating to 3.74% in 2018 from 2.89% in 2017. Automotive sales also rallied, which fed through to wholesale and retail trade of motor vehicles, motorcycles, and repairs.

As the dominant contributor to GDP, manufacturing industry performance has remained stable due to improvements achieved in several subsectors. Manufacturing sector growth stood at 4.27% in 2018, relatively stable compared with 4.29% in 2017. By subsector, the main drivers of growth were the textiles and clothing industries, rubber, plastics and plastic items, and tobacco. Exports of clothing and rubber also rose. A number of subsectors grew only moderately, including the food and beverages industry, CPO, and the furniture industry. In contrast, two subsectors experienced contractions: the chemical, pharmaceutical and traditional medicaments industry, and fabricated metal products, computers, electronics, optical products and electrical equipment. The performance of such subsectors demands attention in order to maintain and expand the role of the manufacturing industry.

Table 23: Gross Domestic Product Growth by Industrial Origin in 2015-2018

(percent, yoy)

Component of GDP	2015	2016	2017	2018
Agriculture, Forestry, and Fishery	3.75	3.36	3.87	3.91
Mining and Quarrying	-3.42	0.95	0.66	2.16
Manufacturing	4.33	4.26	4.29	4.27
Electricity	0.9	5.39	1.54	5.47
Water Supply, Sewerage, Waste Management and Remediation Activities	7.07	3.6	4.6	5.46
Construction	6.36	5.22	6.8	6.09
Wholesale and Retail Trade, Repair of Motor Vehicles and Motorcycles	2.54	4.03	4.46	4.97
Transport and Storage	6.71	7.45	8.49	7.01
Accommodation and Food Services	4.31	5.17	5.39	5.66
Information and Communication	9.7	8.88	9.63	7.04
Financial Services	8.58	8.9	5.47	4.17
Real Estate	4.11	4.69	3.66	3.58
Business Services	7.69	7.36	8.44	8.64
Public Administration, Defense and Compulsory Social Security	4.63	3.19	2.06	7.02
Education Services	7.33	3.8	3.7	5.36
Health Services and Other Activities	6.69	5.15	6.84	7.13
Other Services	8.08	8.02	8.73	8.99
Taxes Less Subsidies on Products	32.55	19.2	13.33	10.58
Gross Domestic Product	**4.88**	**5.03**	**5.07**	**5.17**

Source: Bank of Indonesia, 2019

II.2.5 Domestic Demand

Solid growth of domestic demand, in turn, pushed up imports in 2018. Import growth hit 12.04% in 2018, up from 8.06% in 2017. Import growth quickened to meet increasing domestic demand for infrastructure projects, which will enhance economic productivity moving forward.

All categories of goods imports, namely raw materials, capital goods and consumer goods, increased in 2018. Accounting for more than 80% of total non- oil and gas imports, imports of raw materials, such as iron and steel, organic chemicals, animal feed and gold, increased to support production activity. These imports of raw materials were also in high demand to meet requirements for spare parts and equipment for capital goods associated with electrification and telecommunications projects. And solid non-construction investment also pushed up imports of capital goods, particularly of machinery and equipment. Similarly, consumer goods imports increased in line with household consumption gains. The impact of the policy mix instituted by the Government and Bank Indonesia, including a government program to control imports, affect to significant decline to imports and to stabilize rupiah exchange rate.

II.2.6 Growth of Household Consumption

Household consumption expanded beyond 5% due to rising incomes. And household income growth remained strong due to low inflation and the positive impact of fiscal stimulus and various large events organized in 2018. The Government boosted fiscal stimulus by increasing the number of beneficiaries under the social assistance program (bantuan sosial or bansos), and also by increasing the amount that beneficiaries received. At the same time, the Government adjusted energy subsidies to maintain purchasing power among low-income earners. Meanwhile, several large events also contributed to household consumption, including the local elections, Asian Games, IMF–World Bank Annual Meetings and preparations for the general election. Income growth was also maintained, as reflected by increases in the farmers' terms of trade (ToT), real farmworker wages and wages in the informal services sector, which all surpassed 2017 figures.

Growing consumer confidence was reflected in solid household consumption. Bank Indonesia's Consumer Confidence Index rose across all spending brackets during the first half of the year. Consumer optimism was felt in both components: confidence in both current and in future economic dynamics for the next six months. Consumers were upbeat on current economic conditions due to rising incomes and improving conditions for buying durable goods, coupled with a stable job market. However, consumer confidence retreated modestly in the latter half of 2018 as exchange rate pressures grew.

II.2.7 Government Consumption

Government consumption also contributed to increasing domestic demand. Government consumption in 2018 grew by 4.8%, up significantly from 2.13% in the previous year. Expansive government consumption originated from increases in and refinements to employee benefits, and increasing procurement linked to international events and to local elections. Furthermore, current government expenditure policy focuses on maintaining public purchasing power and prioritized short-term stimulus in the form of social assistance disbursements (bansos). Fiscal stimulus from local government – as reflected in the high budget absorption – also shored up economic performance in the reporting period.

In 2018, a total of 32 national strategic projects (PSN) were completed worth approximately USD23.7 billion. In addition to the completed projects, another 32 projects were partially operating or had moved into the completion phase. This includes the 35,000MW electrification program and programs to develop economic equity. The acceleration of infrastructure projects will increase activity in the property sector, residential property in particular.

II.2.8 Employment, Welfare, Poverty, and Inequality

In August 2018, open unemployment fell to its lowest level in ten years. It came in at 5.34% in August 2018, down from 5.5% in August 2017 (Table 24). Furthermore, the number of labor force increased due to the demographic bonus – a dominant working-age population – currently enjoyed by Indonesia. The participation rate increased to 67.26% in August 2018 from 66.67% in August 2017, as more homemakers and school-leavers entered the labor force.

The absorption of labor into the formal sector increased in 2018. Greater uptake of formal workers stemmed from an increase in employer assisted by permanent worker/ paid worker, which grew at a faster rate than increases in other formal workers categories. Indeed, data published in August 2018 showed that the number of permanent employees had increased. Increasing absorption of formal workers was also highlighted by other indicators, including job vacancies online and in print media. Indonesia's job vacancy index climbed to 137.8 in August 2018 from 134.1 in August 2017. Additionally, the number of workers in informal sector has continued to decline, although still dominated the labor force with 56.84% share.

Broad-based labor market improvements were achieved in various regions. In total, 32 provinces recorded lower open unemployment in August 2018, compared with just 16 provinces in August 2017. All provinces in Sumatra, Kalimantan, Sulawesi and Mapua recorded declines in open unemployment, most significantly in Maluku where the rate fell to 7.27% in August 2018 from 9.29% in August 2017. Strong declines in open unemployment were confirmed in Jakarta and Banten, as the primary industrial base. Jakarta decelerated to 6.24% in 2018 from 7.15% in 2017, and Banten to 8.52% from 9.28%. In Java, all provinces posted lower open unemployment, except Yogyakarta. Labor market dynamics improved in line with an increase of secondary and tertiary sector activities in some regions in response to solid domestic demand. In contrast, West Nusa Tenggara experienced an increase in open unemployment – to 3.72% in 2018 from 3.32% in 2017 – as the local economy contracted.

Tabel 24: The Unemployment Rate by Province in 2015-2018

(%)

Provinsi	2015		2016		2017		2018	
	Feb	Aug	Feb	Aug	Feb	Aug	Feb	Aug
Aceh	7.73	9.93	8.13	7.57	7.39	6.57	6.55	6.36
Sumatera Utara	6.39	6.71	6.49	5.84	6.41	5.60	5.59	5.56
Sumatera Barat	5.99	6.89	5.81	5.09	5.80	5.58	5.55	5.55
Riau	6.72	7.83	5.94	7.43	5.76	6.22	5.72	6.20
Jambi	2.73	4.34	4.66	4.00	3.67	3.87	3.65	3.86
Sumatera Selatan	5.03	6.07	3.94	4.31	3.80	4.39	4.02	4.23
Bengkulu	3.21	4.91	3.84	3.30	2.81	3.74	2.70	3.51
Lampung	3.44	5.14	4.54	4.62	4.43	4.33	4.33	4.06
Kepulauan Bangka Belitung	3.35	6.29	6.17	2.60	4.46	3.78	3.61	3.65
Kepulauan Riau	9.05	6.20	9.03	7.69	6.44	7.16	6.43	7.12
DKI Jakarta	8.36	7.23	5.77	6.12	5.36	7.14	5.34	6.24
Jawa Barat	8.40	8.72	8.57	8.89	8.49	8.22	8.16	8.17
Jawa Tengah	5.31	4.99	4.20	4.63	4.15	4.57	4.23	4.51
DI Yogyakarta	4.07	4.07	2.81	2.72	2.84	3.02	3.06	3.35
Jawa Timur	4.31	4.47	4.14	4.21	4.10	4.00	3.85	3.99
Banten	8.58	9.55	7.95	8.92	7.75	9.28	7.77	8.52
Bali	1.37	1.99	2.12	1.89	1.28	1.48	0.86	1.37
Nusa Tenggara Barat	4.98	5.69	3.66	3.94	3.86	3.32	3.38	3.72
Nusa Tengggara Timur	3.12	3.83	3.59	3.25	3.21	3.27	2.98	3.01
Kalimantan Barat	4.78	5.15	4.58	4.23	4.22	4.36	4.15	4.26
Kalimantan Tengah	3.14	4.54	3.67	4.82	3.13	4.23	3.18	4.01
Kalimantan Selatan	4.83	4.92	3.63	5.45	3.53	4.77	3.86	4.50
Kalimantan Timur	7.17	7.50	8.86	7.95	8.55	6.91	6.90	6.60
Kalimantan Utara	5.79	5.68	3.92	5.23	5.17	5.54	4.68	5.22
Sulawesi Utara	8.69	9.03	7.82	6.18	6.12	7.18	6.09	6.86
Sulawesi Tengah	2.99	4.10	3.46	3.29	2.97	3.81	3.19	3.43
Sulawesi Selatan	5.81	5.95	5.11	4.80	4.77	5.61	5.39	5.34
Sulawesi Tenggara	3.62	5.55	3.78	2.72	3.14	3.30	2.79	3.26
Gorontalo	3.06	4.65	3.88	2.76	3.65	4.28	3.62	4.03
Sulawesi Barat	1.81	3.35	2.72	3.33	2.98	3.21	2.45	3.16
Maluku	6.72	9.93	6.98	7.05	7.77	9.29	7.38	7.27
Maluku Utara	5.56	6.05	3.43	4.01	4.82	5.33	4.65	4.77
Papua Barat	4.61	8.08	5.73	7.46	7.52	6.49	5.67	6.30
Papua	3.72	3.99	2.97	3.35	3.96	3.62	2.91	3.20
Indonesia	**5.81**	**6.18**	**5.50**	**5.61**	**5.33**	**5.50**	**5.13**	**5.34**

Source : Statistics Indonesia, 2019

In general, rising incomes and maintained consumer confidence supported non-food consumption gains, with the exception of medical care and education. Incomes rose, supporting the ongoing shift in consumer preferences towards leisure and lifestyle, as reflected by spending related to transport and communication, and restaurants and hotels. Several other factors also contributed to the gain, including a nascent middle class, growing access to technology and the demographic bonus of a dominant productive-age population.

Tabel 25: The Average of Wages/Salary by Education Attainment in 2017-2018

(Rupiah)

Educational Attainment	2017		2018	
	February	August	February	August
No Schooling	1,196,831	1,274,562	1,067,432	1,174,897
Not/Not Yet Completed Primary School	1,396,636	1,434,207	1,480,179	1,537,465
Elementary School	1,633,614	1,666,573	1,621,163	1,789,463
Junior High School	1,847,374	1,918,092	1,808,698	2,016,258
High School (General)	2,537,845	2,666,627	2,503,664	2,729,730
High School (Vocational)	2,613,633	2,678,607	2,595,390	2,748,326
Diploma I/II/III/Academy	3,432,911	3,543,796	3,454,620	3,679,023
University	4,551,988	4,515,054	4,417,217	4,587,783
Average	**2,702,590**	**2,742,621**	**2,654,070**	**2,829,130**

Source : Statistics Indonesia, 2019

Poverty also decreased significantly in 2018. Indonesia's relative poverty figure stood at 9.82% in March 2018 and 9.66% in September 2018, the lowest reading since the economic crisis in 1998. Fundamentally, declining poverty since 2015 has been attributable to increasing domestic economic growth momentum, accompanied by lower unemployment and controlled inflation. Indonesia's significant poverty improvements have also been supported by an expansion of government social protection programs. Urban and rural poverty rates have declined, with a faster pace of decline recorded in rural areas. Such developments were consistent with improvements in real farmworker wages and farmers' ToT in September 2018, when compared with September 2017. Furthermore, rural prosperity has also been built by the Village Fund program, which was designed to finance labor-intensive development.

Lower poverty rates were achieved in nearly all of Indonesia's provinces in 2018; 32 out of a total of 34 achieved a lower poverty rate in 2018 versus 2017, while in 2017 just 25 provinces achieved a lower poverty rate compared with 2016. In addition, the five provinces with the highest poverty levels in 2017 – Papua, West Papua, East Nusa Tenggara, Maluku and Gorontalo – posted improvements. Moreover, all provinces in Sumatra, Java, Kalimantan and Bali-Nusra recorded lower poverty rates. Such accomplishments were inextricably linked to the Government's commitment to stimulate balanced and equitable local economic development by improving connectivity and expanding the social assistance programs (bansos).

Tabel 26: The Percentage of Poor People by Province in 2015-2018

(%)

Province	2015		2016		2017		2018	
	Semester		Semester		Semester		Semester	
	I	II	I	II	I	II	I	II
Aceh	17.08	17.11	16.73	16.43	16.89	15.92	15.97	15.68
Sumatera Utara	10.53	10.79	10.35	10.27	10.22	9.28	9.22	8.94
Sumatera Barat	7.31	6.71	7.09	7.14	6.87	6.75	6.65	6.55
Riau	8.42	8.82	7.98	7.67	7.78	7.41	7.39	7.21
Jambi	8.86	9.12	8.41	8.37	8.19	7.90	7.92	7.85
Sumatera Selatan	14.25	13.77	13.54	13.39	13.19	13.10	12.80	12.82
Bengkulu	17.88	17.16	17.32	17.03	16.45	15.59	15.43	15.41
Lampung	14.35	13.53	14.29	13.86	13.69	13.04	13.14	13.01
Kepulauan Bangka Belitung	5.40	4.83	5.22	5.04	5.20	5.30	5.25	4.77
Kepulauan Riau	6.24	5.78	5.98	5.84	6.06	6.13	6.20	5.83
DKI Jakarta	3.93	3.61	3.75	3.75	3.77	3.78	3.57	3.55
Jawa Barat	9.53	9.57	8.95	8.77	8.71	7.83	7.45	7.25
Jawa Tengah	13.58	13.32	13.27	13.19	13.01	12.23	11.32	11.19
DI Yogyakarta	14.91	13.16	13.34	13.10	13.02	12.36	12.13	11.81
Jawa Timur	12.34	12.28	12.05	11.85	11.77	11.20	10.98	10.85
Banten	5.90	5.75	5.42	5.36	5.45	5.59	5.24	5.25
Bali	4.74	5.25	4.25	4.15	4.25	4.14	4.01	3.91
Nusa Tenggara Barat	17.10	16.54	16.48	16.02	16.07	15.05	14.75	14.63
Nusa Tengggara Timur	22.61	22.58	22.19	22.01	21.85	21.38	21.35	21.03
Kalimantan Barat	8.03	8.44	7.87	8.00	7.88	7.86	7.77	7.37
Kalimantan Tengah	5.94	5.91	5.66	5.36	5.37	5.26	5.17	5.10
Kalimantan Selatan	4.99	4.72	4.85	4.52	4.73	4.70	4.54	4.65
Kalimantan Timur	6.23	6.10	6.11	6.00	6.19	6.08	6.03	6.06
Kalimantan Utara	6.24	6.32	6.23	6.99	7.22	6.96	7.09	6.86
Sulawesi Utara	8.65	8.98	8.34	8.20	8.10	7.90	7.80	7.59
Sulawesi Tengah	14.66	14.07	14.45	14.09	14.14	14.22	14.01	13.69
Sulawesi Selatan	9.39	10.12	9.40	9.24	9.38	9.48	9.06	8.87
Sulawesi Tenggara	12.90	13.74	12.88	12.77	12.81	11.97	11.63	11.32
Gorontalo	18.32	18.16	17.72	17.63	17.65	17.14	16.81	15.83
Sulawesi Barat	12.40	11.90	11.74	11.19	11.30	11.18	11.25	11.22
Maluku	19.51	19.36	19.18	19.26	18.45	18.29	18.12	17.85
Maluku Utara	6.84	6.22	6.33	6.41	6.35	6.44	6.64	6.62
Papua Barat	25.82	25.73	25.43	24.88	25.10	23.12	23.01	22.66
Papua	28.17	28.40	28.54	28.40	27.62	27.76	27.74	27.43
Indonesia	**11.22**	**11.13**	**10.86**	**10.7**	**10.64**	**10.12**	**9.82**	**9.66**

Note: Semester I (March) and Semester II (September)
Source: Statistics Indonesia, 2019

Income inequality, or economic inequality, has also declined, as shown by a declining Gini ratio. A lower Gini ratio points to less inequality in both rural and urban areas. Indonesia's Gini ratio was 0.384 in September 2018 and 0.389 in March 2018, improving from 0.391 in September 2017 and 0.393 in March 2017 (Table 27). Nevertheless, urban areas have tended to consistently dominate the improvements since March 2015. In addition, lower inequality was also reflected in the growth of spending per capita among the lowest 40% of the population, which outpaced spending growth by the middle 40% and top 20%, in line with rising incomes among low-income earners, boosted by social assistance disbursements (bansos).

Improving inequality was also corroborated by declines in the Gini ratio in some dominant urban regions. A total of 20 provinces achieved a lower Gini ratio in September 2018 compared with 18 provinces one year earlier. The deepest declines were reported in the provinces of East Java, South Sulawesi, Central Sulawesi, North Sumatra, and South Sumatra, each with significant urban areas. Furthermore, nearly all of Java's provinces recorded a lower Gini ratio, with declines ranging from 0.008 to 0.044 basis points. The Gini ratio in West Java, however, increased slightly. And in Mapua nearl all provinces recorded a higher Gini ratio, albeit by a moderate increment of between 0.004 and 0.006 basipoints.

Tabel 27: Gini Ratio by Province in 2015-2018

(%)

Province	2015		2016		2017		2018	
	Semester		Semester		Semester		Semester	
	I	II	I	II	I	II	I	II
Aceh	0.334	0.339	0.333	0.341	0.329	0.329	0.325	0.318
Sumatera Utara	0.336	0.326	0.319	0.312	0.315	0.335	0.318	0.311
Sumatera Barat	0.342	0.319	0.331	0.312	0.318	0.312	0.321	0.305
Riau	0.364	0.366	0.347	0.347	0.325	0.325	0.327	0.347
Jambi	0.361	0.344	0.349	0.346	0.335	0.334	0.334	0.335
Sumatera Selatan	0.360	0.334	0.348	0.362	0.361	0.365	0.358	0.341
Bengkulu	0.376	0.371	0.357	0.354	0.351	0.349	0.362	0.355
Lampung	0.376	0.352	0.364	0.358	0.334	0.333	0.346	0.326
Kepulauan Bangka Belitung	0.283	0.275	0.275	0.288	0.282	0.276	0.281	0.272
Kepulauan Riau	0.364	0.339	0.354	0.352	0.334	0.359	0.330	0.339
DKI Jakarta	0.431	0.421	0.411	0.397	0.413	0.409	0.394	0.390
Jawa Barat	0.415	0.426	0.413	0.402	0.403	0.393	0.407	0.405
Jawa Tengah	0.382	0.382	0.366	0.357	0.365	0.365	0.378	0.357
DI Yogyakarta	0.433	0.420	0.420	0.425	0.432	0.440	0.441	0.422
Jawa Timur	0.415	0.403	0.402	0.402	0.396	0.415	0.379	0.371
Banten	0.401	0.386	0.394	0.392	0.382	0.379	0.385	0.367
Bali	0.377	0.399	0.366	0.374	0.384	0.379	0.377	0.364
Nusa Tenggara Barat	0.368	0.360	0.359	0.365	0.371	0.378	0.372	0.391
Nusa Tengggara Timur	0.339	0.348	0.336	0.362	0.359	0.359	0.351	0.359
Kalimantan Barat	0.334	0.330	0.341	0.331	0.327	0.329	0.339	0.325
Kalimantan Tengah	0.326	0.300	0.330	0.347	0.343	0.327	0.342	0.344
Kalimantan Selatan	0.353	0.334	0.332	0.351	0.347	0.347	0.344	0.340
Kalimantan Timur	0.316	0.315	0.315	0.328	0.330	0.333	0.342	0.342
Kalimantan Utara	0.294	0.314	0.300	0.305	0.308	0.313	0.303	0.304
Sulawesi Utara	0.368	0.366	0.386	0.379	0.396	0.394	0.394	0.372
Sulawesi Tengah	0.374	0.370	0.362	0.347	0.355	0.345	0.346	0.317
Sulawesi Selatan	0.424	0.404	0.426	0.400	0.407	0.429	0.397	0.388
Sulawesi Tenggara	0.399	0.381	0.402	0.388	0.394	0.404	0.409	0.392
Gorontalo	0.420	0.401	0.419	0.410	0.430	0.405	0.403	0.417
Sulawesi Barat	0.363	0.362	0.364	0.371	0.354	0.339	0.370	0.366
Maluku	0.340	0.338	0.348	0.344	0.343	0.321	0.343	0.326
Maluku Utara	0.280	0.286	0.286	0.309	0.317	0.330	0.328	0.336
Papua Barat	0.440	0.428	0.373	0.401	0.390	0.387	0.394	0.391
Papua	0.421	0.392	0.390	0.399	0.397	0.398	0.384	0.398
Indonesia	**0.408**	**0.402**	**0.397**	**0.394**	**0.393**	**0.391**	**0.389**	**0.384**

Note: Semester I (March) and Semester II (September)
Source: Statistics Indonesia, 2019

II.3 Fiscal Situation

In 2018, Indonesia successfully maintained fiscal sustainability while continuing to support economic growth. The prospects for fiscal sustainability improved as reflected in the 2018 primary balance deficit, which declined to IDR 1.86 billion or 0.01% of gross domestic product (GDP). Consequently, the realized 2018 budget deficit declined to 1.76% of GDP. The ratio of government debt to GDP remained at a safe level of around 30% in 2018. Meanwhile, spending on social protection programs and a higher regional fiscal stimulus, in addition to infrastructure spending, all helped to propel economic growth.

Fiscal policy direction in 2018 was focused on efforts to maintain fiscal sustainability, while continuing to create room for economic growth. This policy took into consideration the importance of fiscal resilience in maintaining economic stability amid heightened global uncertainty. The Government continued to view the state and regional budgets (APBN, APBD) as a countercyclical macroeconomic policy tool to maintain the momentum of economic recovery. In line with this, structural policies were strengthened further to increase economic capacity, which itself sustains stability and economic growth over the medium term.

Policy direction was pursued through strategies in each component of the 2018 State Budget. In terms of state revenue, Indonesia aimed to increase state revenues from taxes by using an updated tax database and improving tax compliance. In terms of state expenditure, Indonesia sharpened the focus of spending by supporting economic growth through social protection programs, better-targeted subsidies, and the strengthening of fiscal decentralization to hasten the reduction of poverty and social inequality. In terms of financing, efforts were made to ensure that financing strategies were put into practice in a prudent, efficient, balanced and productive manner so as to support fiscal sustainability. National policy strategy was supported by regional fiscal policy and the development of infrastructure projects through varied financing schemes. Structural reforms also continued through an array of structural policies aimed at improving the business climate.

II.3.1. State Revenues

The Government adopted various strategies to optimize state revenue, both through tax revenues and non-tax state revenues (NTR). To optimize tax revenues, the Government persisted with tax reform policies. This included strengthening the capacity of the tax office, utilizing the momentum of the implementation of automatic exchange of financial information between countries, and improving national tax administration. In relation to NTR, the Government continued to strengthen the management of this revenue stream and improve the performance of state-owned enterprises. Better NTR management was achieved by improving regulations, including on NTR tariffs, better cost recovery efficiencies, and the application of a gross split system for oil and gas.

The Government pursued six main tax policies in 2018. First, it simplified and accelerated the provision of tax refunds. This is designed to encourage investment and assist companies, including small and medium enterprises (SME), with business financing by hastening the return of value-added tax (VAT). It is also intended to encourage growth in business activities and drive sustainability, improve the ease of doing business for individual and corporate taxpayers and raise Indonesia’s ranking in the World Bank Ease of Doing Business survey. Second, Indonesia introduced joint inspection by three agencies in assessing the efficiency and accuracy of the value of the profit-sharing obligation and income tax of oil and gas contractor partnership contracts. The three agencies are the Directorate General of Taxation, the Financial and Development Supervisory Agency (BPKP), and the Special Task Force for Upstream Oil and Gas Business Activities (SKK Migas). The joint inspections began in 2018. Third, Indonesia simplified the VAT exemption policy and/or sales tax on imported luxury goods (PPnBM) or the transfer of taxable goods and taxable services, which applied to representatives of foreign countries and international bodies. Fourth, Indonesia adjusted the tariffs on Article 22 income tax on the import of 1,147 types of goods, with effect from September 2018. Fifth, tax holidays were provided for 18 types of ‘pioneer’ industry. These tax holidays ranged from five to 20 yearsdepending on the value of the investment. The sixth and final tax policy was the provision of tax incentives for export proceeds from industries based on natural resources, regulated in a sixteenth economic policy package.

Policy strategy in the field of taxation was supported by tax intensification efforts – the expansion of the tax base and increased tax compliance. Data shows that the number of registered taxpayers increased compared to 2017, testament to the positive impact of the tax amnesty program. The program led to an increase in the number of registered taxpayers who must submit an annual tax return. Along with the increasing tax base, the compliance rate also improved: the submission of tax returns increased to 73% in 2018 from 70% in 2017.

The Government also reformed NTR by updating the relevant legal provisions. These revisions were designed to gather and optimize NTR, encourage good governance, and simplify or reduce the types and rates of NTR, particularly related to basic services, without reducing the responsibility to continue providing these basic services. The legal provisions cover: (i) grouping NTR objects into six groups or clusters; (ii) regulating tariffs and the impact on the community; (iii) improving governance through self-assessment verification; (iv) strengthening of supervision of tax office employees by government internal supervisors; (v) more extensive checks on NTR management agencies, partners of NTR management agencies, and NTR compulsory payments; and (vi) the right to waivers on compulsory payments under certain circumstances.

These policies helped actual state revenues exceed the 2018 State Budget target to IDR 1,894,095 billion (102.5%), with growth of 16.6% from 2017. Both tax revenues and NTR grew at higher rates than in 2017. The 2018 tax revenues rose sharply by 13.2%, also exceeding the combined average for the last seven years. This positive performance pushed up the ratio of tax revenues to GDP to 10.3% in 2018 from 9.9% in 2017. The table below shows the budgeted and actual Indonesia's State Revenue from 2015 until 2018 as below:

Tabel 28: State Revenues in 2015-2018

(billion Rupiah)

Items	2015	2016	2017	2018
Budget				
A. Government Revenues	**1,761,643**	**1,786,225**	**1,736,060**	**1,894,095**
I. Tax Revenues	**1,489,255**	**1,539,166**	**1,472,710**	**1,618,095**
1. Domestic Taxes	1,439,999	1,503,295	1,436,731	1,579,395
2. International Trade Taxes	49,257	35,872	35,979	38,700
II. Non Taxes Revenues	**269,075**	**245,084**	**260,242**	**275,428**
1. Natural Resources	118,919	90,524	95,643	103,675
2. Profit Transfers From SOE's	36,957	34,164	41,000	44,695
3. Other Non-Tax Revenues	90,110	84,124	85,058	83,753
4. Revenue from Public Service Institution	23,090	36,271	38,541	43,305
III. Grants	**3,312**	**1,975**	**3,108**	**1,197**
Actual				
A. Government Revenues	**1,508,020**	**1,555,934**	**1,666,376**	**1,943,675**
I. Tax Revenues	**1,240,419**	**1,284,970**	**1,343,530**	**1,518,790**
1. Domestic Taxes	1,205,479	1,249,499	1,304,316	1,472,908
2. International Trade Taxes	34,940	35,471	39,214	45,882
II. Non Taxes Revenues	**255,628**	**261,976**	**311,216**	**409,320**
1. Natural Resources	100,972	64,902	111,132	180,593
2. Profit Transfers From SOE's	37,644	37,133	43,904	45,061
3. Other Non-Tax Revenues	81,697	117,995	108,835	128,574
4. Revenue from Public Service Institution	35,315	41,946	47,345	55,093
III. Grants	**11,973**	**8,988**	**11,630**	**15,565**

Source: Ministry of Finance on Central Government Financial Reports for year 2018, Audited

II.3.2. State Expenditures

State expenditure in 2018 reached IDR 2,213,118 billion, up 10.25% from 2017. This was accompanied by higher absorption of spending in 2018 than in 2017. The growth in state expenditure was mainly driven by central government spending, which reached IDR 1,455,325 billion, up 15.01% compared to an increase of 9.65% in 2017. The higher budget absorption at the beginning of the year came on the back of central government spending, particularly government consumption, distribution of social assistance and subsidies since the beginning of 2018. By comparison, for other expenditure – such as goods and capital – higher absorption was only seen in the second half of 2018, having been reined in during the first half. The table below shows the budgeted and actual Indonesia's State Expenditures from 2015 until 2018 as below:

Tabel 29: Indonesia's State Expenditures in 2015-2018

(billion Rupiah)

Items	2015	2016	2017	2018
Budgeted				
B. Government Expenditures	**1,984,150**	**2,082,949**	**2,133,296**	**2,220,657**
I. Central Government Expenditures	**1,319,549**	**1,306,696**	**1,366,957**	**1,454,494**
1. Personnel Expenditures	293,129	342,447	343,656	365,692
2. Goods and Services Expenditures	238,818	304,242	294,716	340,130
3. Capital Expenditures	275,788	206,567	226,144	203,879
4. Debt Interest Payment Expenditures	155,731	191,218	219,196	238,607
5. Subsidies	212,104	177,754	168,877	156,228
6. Grant Expenditures	4,644	8,537	5,532	1,461
7. Social Assistance Expenditures	107,670	53,404	58,962	81,260
8. Others Expenditures	31,664	22,525	49,874	67,237
II. Transfer to the Regions and Village Funds	**664,601**	**776,253**	**766,339**	**766,163**
Transfer to the Regions	**643,835**	**729,271**	**706,339**	**706,163**
1. Balance Budget	**521,761**	**705,459**	**678,596**	**676,603**
a. Revenue Sharing Funds	110,052	109,076	95,377	89,225
b. General Allocation Funds	352,888	385,361	398,582	401,490
c. Special Allocation Funds	58,821	211,022	184,637	185,888
2. Special Autonomy Funds	**122,074**	**23,812**	**27,743**	**29,560**
Village Funds	**20,766**	**46,982**	**60,000**	**60,000**
Actual				
B. Government Expenditures	**1,806,515**	**1,864,275**	**2,007,352**	**2,213,118**
I. Central Government Expenditures	**1,183,304**	**1,154,018**	**1,265,359**	**1,455,325**
1. Personnel Expenditures	281,143	305,142	312,729	346,891
2. Goods and Services Expenditures	233,281	259,647	291,459	347,468
3. Capital Expenditures	215,434	169,474	208,657	184,128
4. Debt Interest Payment Expenditures	156,010	182,761	216,568	257,952
5. Subsidies	185,971	174,227	166,401	216,883
6. Grant Expenditures	4,262	7,130	5,446	1,521
7. Social Assistance Expenditures	97,151	49,614	55,297	84,318
8. Others Expenditures	10,052	6,024	8,803	16,164
II. Transfer to the Regions and Village Funds	**623,140**	**710,257**	**741,992**	**757,793**
Transfer to the Regions	**602,373**	**663,578**	**682,226**	**697,934**
1. Balance Budget	**485,818**	**639,766**	**654,483**	**668,643**
a. Revenue Sharing Funds	78,053	90,535	88,232	93,704
b. General Allocation Funds	352,888	385,361	398,582	401,490
c. Special Allocation Funds	54,877	163,870	167,668	173,450
2. Special Autonomy Funds	**116,555**	**23,812**	**27,743**	**29,290**
Village Funds	**20,766**	**46,679**	**59,767**	**59,859**

Source: Ministry of Finance on Central Government Financial Reports for year 2018, Audited

The Government adopted several strategies to sharpen the role of state expenditure in stimulating the economy. In general, this strategy was undertaken through more effective social protection programs and better-targeted subsidies. More specifically, Indonesia achieved this through social assistance (transfer of funds to the poor), strategic subsidies, expenditure on education and healthcare, and on transfers of funds from central to local or provincial governments, and Village Funds.

The Government’s policy to stimulate the economy is illustrated by the acceleration of social assistance distribution from the beginning of 2018. This also demonstrates the Government’s focus on reducing poverty and social inequality. To achieve this goal, the Government increased the number of families entitled to benefits under the Family Hope Program to 10 million from 6 million. As a result, the program budget rose to IDR 18 trillion in 2018 from IDR 11 trillion in 2017. The Government also expanded the number of families entitled to non-cash food assistance to 10 million in 2018 from 1.2 million in 2017. This social protection strategy was accompanied by better data on the beneficiaries of the Family Hope Program and the recipients of non-cash food assistance subsidies.

The Government also adopted strategies to maintain purchasing power. One such strategy related to subsidies. Fixed subsidies on diesel were increased to IDR 2,000 per liter from IDR 1,500 per liter. This was done to offset the impact of rising global crude oil prices and the weak rupiah exchange rate, which significantly overreached the budget assumption. The increase in energy subsidies was countered, however, by improvements in the distribution of subsidies and by more accurately targeting the recipients of the subsidies. The adjustment to the diesel subsidies contributed to realized subsidies in 2018 reaching 138.7% of the ceiling set in the state budget. This high level of subsidies was also due to payments made in 2018 to Pertamina, PLN and Pupuk Indonesia to cover underpayment of subsidies in 2017.

The Government also showed consistency in continuing to implement education and healthcare national development priority programs. In an effort to improve the quality of education, the state education budget remained at 20% of both central and regional government spending. With the high education budget, the number of students receiving Indonesia Smart Cards (KIP) increased to 19.7 million students in 2018 from 18.2 million students in 2017. The number of recipients of Bidik Misi scholarships rose to 401,500 in 2018 from 290,000 in 2017. The Government also maintained the health budget at 5% of state expenditure. Some of the central health budget was allocated to the Ministry of Health to implement the national health insurance program through the distribution of the Indonesia Health Card to 92.4 million people. For the transfers to the regions, the health budget allocation was channeled through health and family planning special allocation funds (DAK), health operational assistance and family planning operational assistance.

Sharpening of the role of state expenditure was also achieved through transfers to the regions and via Village Funds (TKDD). This policy was focused on improving the quality of public services in the regions, poverty reduction and reduction in regional inequality and improving the effectiveness of budget spending. Specifically, TKDD policy covered: (i) strengthening the synchronization of TKDD planning and budgeting with the spending allocation of ministries and institutions; (ii) better management of general and special transfer funds; (iii) reformulation of regional incentive funds allocation; and (iv) reformulation of the Village Funds allocation.

In line with this strategy, TKDD channelled to the regions in 2018 reached IDR 757,793 billion or 98.91% of the 2018 target, versus 96.82% in 2017. The growth in TKDD was supported by high growth in the distribution of revenue-sharing funds, particularly in the fourth quarter of 2018, but also by a shortfall in revenue-sharing payments in previous years. Growth in physical DAK contracted, although to a lesser degree than in 2017. The disbursement of non-physical DAK and Village Fund money was sluggish, given changes in the distribution pattern and additional requirements for disbursement. In general, the role of the regions in supporting national development priority programs increased. This can be seen in the higher portion of the health budget channeled through TKDD in 2018.

II.3.3. Budget Financing

The Government's policy strategy supported fiscal sustainability and the ongoing health of the 2018 State Budget. The primary balance deficit in the 2018 State Budget declined to IDR 1.8 trillion, or 0.01% of GDP, from 0.91% of GDP in 2017. On the back of this development, the state budget deficit declined to 1.76% of GDP in 2018, versus the deficit target of 2.19% of GDP, and financing reached IDR 305,693 billion, 6.21% lower than the financing target of IDR325.9 trillion. The table below shows the budgeted and actual Indonesia's State Financing from 2015 until 2018 as below:

Tabel 30: Indonesia's State Financing in 2015-2018

(billion Rupiah)

Items	2015	2016	2017	2018
Budgeted				
C. State Budget Surplus/Defisit	**(222,507)**	**(296,724)**	**(397,236)**	**(325,937)**
D. Government Financing (Net)	**222,507**	**296,724**	**397,236**	**325,937**
I. Domestic Financing	**242,515**	**299,251**	**412,656**	**354,951**
1. Government Account	-	19,011	-	-
2. Receipt of Installment Payments on Loans Forwarding	4,785	6,350	4,047	3,885
3. Privatization and Asset Selling of Restructuring Program	350	325	300	183
4. Government Bonds (Net)	297,698	364,867	467,314	414,521
5. Domestic Loans (Net)	1,691	3,389	1,733	3,138
6. Government Capital Participation & Investment Funds	(58,844)	(88,985)	(49,234)	(50,654)
7. Guarantee Obligation	(844)	(652)	(1,005)	(1,121)
8. National Education Development Funds	-	5,000	(10,500)	(15,000)
9. Others Financing	(2,322)	(54)	-	-
II. Foreign Financing (Net)	**(20,008)**	**(2,527)**	**(15,420)**	**(29,014)**
1. Foreign Loans Withdrawals (Gross)	48,647	72,959	57,500	51,346
a. Program Aid / Cash Loans*)	7,500	35,775	20,100	13,400
b. Project Aid / Activity Loans*)	41,147	37,184	37,400	37,946
2. Aid Channeling/Loans Forwarding	(4,472)	(5,834)	(7,716)	(10,575)
3. Amortization/Principal Installment Payments on Foreign Loans	(64,183)	(69,652)	(65,204)	(69,785)
E. State Financing Surplus/Deficit	**-**	**-**	**-**	**-**
Actual				
C. State Budget Surplus/Defisit	**(298,495)**	**(308,341)**	**(340,976)**	**(269,443)**
D. Government Financing (Net)	**323,108**	**334,503**	**366,624**	**305,693**
I. Domestic Financing	**307,858**	**344,923**	**386,891**	**302,516**
1. Government Account	-	19,011	-	-
2. Receipt of Installment Payments on Loans Forwarding	4,855	6,781	4,817	4,830
3. Privatization and Asset Selling of Restructuring Program	342	552	359	164
4. Government Bonds (Net)	362,257	407,259	441,826	358,398
5. Domestic Loans (Net)	832	1,052	648	1,354
6. Government Capital Participation & Investment Funds	(59,655)	(84,080)	(49,254)	(46,114)
7. Guarantee Obligation	-	(652)	(1,005)	(1,121)
8. National Education Development Funds	-	(5,000)	(10,500)	(15,000)
9. Others Financing	(773)	-	-	5
II. Foreign Financing (Net)	**15,250**	**(10,420)**	**(20,267)**	**3,177**
1. Foreign Loans Withdrawals (Gross)	83,821	63,424	51,727	88,610
a. Program Aid / Cash Loans*)	55,085	35,325	20,948	50,625
b. Project Aid / Activity Loans*)	28,737	28,099	30,779	37,985
2. Aid Channeling/Loans Forwarding	(2,576)	(5,118)	(6,869)	(9,100)
3. Amortization/Principal Installment Payments on Foreign Loans	(65,995)	(68,726)	(65,125)	(76,333)
E. State Financing Surplus/Deficit	**24,613**	**26,162**	**25,648**	**36,250**

Note: *) Account name in 2018

Source: Ministry of Finance on Central Government Financial Reports for year 2018, Audited

In line with its prudent financing strategy, the Government adjusted the government securities (SBN) issuance plan by taking on more foreign loans. This was designed to reduce SBN interest costs, which had risen on the back of pressure from increases in global interest rates. Meanwhile, the interest rate on SBN denominated in foreign currency was on average twice as high as the interest rates on foreign loans. By adopting this strategy, the Government was able to take on IDR 88,610 billion of foreign loans (gross) in 2018, up from IDR 36,883 billion in 2017. This strategy underscores the Government’s goal of maintaining fiscal sustainability.

Given the direction of fiscal policy in 2018 and, in turn, the financing strategies, the Government’s debt position was maintained at a low and healthy level. The ratio of government debt to GDP was kept in a safe corridor in 2018 at 29.8% of GDP, slightly higher than the 29.1% of GDP in 2017. Most of the debt was comprised of SBN (81.8% of total debt), and the remainder was foreign loans. The debt ratio remains at a lower level than that of other countries in the Asia region, including India, China and Malaysia.

III. Tax Structure: Institution and Reality

III.1 Historical Background

Tax is an important component in the journey of a nation. Almost all countries in the world apply a rule or scheme regarding taxation both directly and indirectly, and no exception in Indonesia. The long history of taxation in Indonesia has been going on since the days of the kingdom, colonial until now. So that the Indonesian people themselves are actually no stranger to the word "tax". However, because the imposition of each era is different where in the previous era it tends to harm the community that eventually causing resistance to the tax itself.

III.1.1 Pre-Independence Era (From Kingdom to Colonialism)

The Indonesian people already knew a kind of tax levy even before being colonized by Europeans and Japanese. The community is familiar with tribute, which is a type of taxation which is forced. The difference is that tribute is given to the king as an offering. Because at that time the king was considered as a representative of God and what happened in the community was considered influenced by the king, with a reward in the form of security and order from the king.

In the historical record of the Dutch autonomous body, Vereenigde Oost-Indische Compagnie (VOC), collected taxes including House Tax, Business Tax and Head Tax on Chinese traders and other foreign traders. However, the VOC did not collect taxes in its territories such as Batavia, Maluku and others. Then during the period of Governor General Daendels, there was also a tax collection that is collecting taxes from the gates (both people and goods) and taxes on the sale of goods on the market (bazarregten), including tax collection on houses.

Entering the era of British occupation, Governor-General Raffles was also known for the tax collection system known as the landrent stesel which mimics the taxation system in Bengali, India, namely the imposition of taxes on community land leases to the colonial government. This was the forerunner of the imposition of Land and Building Tax (PBB).

In addition, there were also rules regarding income tax in the colonial era. The tax rules on income were imposed on both natives and non-natives who earned income in the Dutch East Indies, as Indonesia was then. This rule was applied by the Dutch colonial government in the early 19th century. Income tax for natives was levied on business activities such as trade that it was known as business tax whereas non-natives were imposed on business patents in the fields of industry, agriculture, handicraft, manufacturing that so called tax patent duty. In the Japanese colonial era was not much known. Considering at that time, the Japanese government focused more resources on the costs of the war. Therefore, it was difficult to separate which constitutes tax from the government itself to the people.

By these, the people of Indonesia are so close with taxes up to now. However, there is negative impacts as a result of taxation in the colonial era and the previous era. That makes some people consider the tax is only a form of superiority of the authorities to their people.

III.1.2 Post-Independence Era

On August 19, 1945 the Ministry of Finance was formed as part of the government in charge of state finances. Within the Ministry of Finance organization there was a Tax Authority, which was the part dealing with taxation in Indonesia at that time. After the new government was established, it turned out the First Dutch Military Aggression pillion by NICA that succeeded in controlling the capital of Jakarta. By that, the government moved its capital to Yogyakarta and placed Ministry of Finance near the new capital city. That's why the first tax office is in Magelang.

The government adopted a number of rules regarding the inheritance tax of the colonial government. Among others, the 1944 Income Tax Ordinance and formed several sub-organizations in implementing tax collection. Such as the Tax Bureau, Customs and Excise Bureau and the Bureau of Land Tax at the Directorate General of Monetary. At that time, the government implemented an official assessment system in the imposition of taxes to the public, namely the tax collection system by determining the tax authorities. Society as a taxpayer was passive and tax debt would arise when the Tax Assessment Letter was issued. Even though Indonesia has become independent, tax laws have not changed much. The changes made are not fundamental, so the applicable tax law still layed its foundation on the administrative authority of the tax administration.

Because the government wanted to increase tax revenue, in 1967 a new tax collection system was introduced, known as the Menghitung Pajak Sendiri system (Calculating Self Taxes) and Menghitung Pajak Orang Lain sytem (Calculating Other People's Taxes) with Law No. 867 junto Government Regulation No.11 of 1967. This new tax collection system was called as self assessment system.

This system emerged after the government's evaluation of the failure of the old tax collection system where the role of tax calculation was carried out unilaterally by the tax authorities. Whereas in this new system, most tax calculations were performed by taxpayers. Taxpayers were given the authority to calculate their own income and wealth and then given the authority to calculate their own taxes.

III.1.3 Tax Reform Era

Fundamental yet comprehensive changes in Indonesia tax administration occurred in January 1, 1984: The first tax reform. Since then, laws were regularly amended in order to address the rapidly changing business environment within the country as well as to support the objectives of the government in improving the investment climate while increasing tax revenues at the same time.

The first tax reform came into force with the implementation of three primary tax laws i.e. Law of General Tax Provisions and Procedures, Law of Income Tax as well as The Law of Value-Added Tax (VAT) and Luxury-goods Sales Tax (LST). The reform continued the next year with the enactment of Law of Land and Building Tax and Law of The Stamp Duty.

The year of 1994 was the commencement of the second tax reform whereby some regulations were amended such are General Tax Provisions and Procedures, VAT and LST, Income Tax and Land and Building Tax. The second reform came into effect on January 1, 1995, with changes, additions and deletions of several articles from previous legislation.

The third tax reform was in 1997 with the enactment of three tax laws. First, the Law of Tax Dispute Settlement Agency under which a new agency was established while replacing the legacy from Dutch Law. Previously, provisions concerning appeal in Indonesia law system were mentioned in Regeling van het Beroep in Belastingzaken, lastly amended in 1959. Second, Law of Tax Collection with Distress Warrant and third, Law of Acquisition Duty of Rights on Land and Building. Besides that the new Tax Court law was also enacted as a revision to Law of Tax Dispute Settlement Agency. Based on Tax Court Law, the administrative appeal body was no longer a part of the tax institution but became an institution under Tax Court Secretary, Ministry of Finance where trials are conducted in Jakarta, Yogyakarta, and Surabaya.

III.2 Tax System

III.2.1 Introduction

Tax is a compulsory contribution to the state which is payable by any individual or entity that is enforced based on the law, without any direct benefit in return and is used for the maximum welfare of the people. Tax payments constitute the realization of the citizen obligation and the role of the taxpayer to the state financing and national development. Such responsibility is in accordance with the self-assessment system implemented in the Indonesian.

Taxes in Indonesia are divided into two parts: Central Taxes and Local Taxes. Central Taxes are administered by the central government under the Ministry of Finance which is mostly managed by the Directorate General of Taxes (DGT), as well as the Directorate General of Customs and Excise (DGCE) responsible for import duty, export duty, and excise. DGT administers taxes as follows:

1. Income Tax
   Income tax is imposed on any taxable individual, entity or permanent establishment upon the income received or accrued within a taxable year comprises both resident and non-resident.
2. Value Added Tax (VAT)
   VAT is imposed on the consumption of taxable goods and/or taxable services within the territory

of Indonesia. Persons, corporations, or governments who consume taxable goods and/or taxable services are subject to VAT. Basically, any goods and services are taxable goods and/or taxable services, unless otherwise provided by the Laws.

3. Luxury-goods Sales Tax (LST)
   In addition to VAT, the consumption of certain taxable goods classified luxuries are also subject to LST. The goods classified as luxury are:
   a. It is not a basic necessity; or
   b. Goods are consumed by certain communities; or
   c. In general, goods are consumed by high-income people; or
   d. It is consumed to show status; or
   e. If consumed can damage the health and morale of society, and disturb the public order.
4. Stamp Duty
   Stamp duty shall be imposed on the use of documents, such as letters of agreement, notarial deeds, and receipts of payments, securities and securities, containing the amount of money or nominal amount above a certain amount in accordance with the provisions.
5. Land and Building Tax Other Than Urban and Rural Sector (LBT)

Separate regulations are applied to plantation, forestry, and mining which consists of mineral and coal mining, oil, gas and geothermal mining, as well as other industries located in national waters outside territory of regional area.

Local taxes administered by the regional government are mainly structured as follows:

1. Provincial taxes, that are:
   a. Vehicle Tax;
   b. Transfer of Motor Vehicle Title;
   c. Motor Vehicle Fuel Tax;
   d. Surface Water Tax;
   e. Cigarette Tax.
2. District/City Taxes, that are:
   a. Hotel Tax;
   b. Restaurant Tax;
   c. Entertainment Tax;
   d. Advertisement Tax;
   e. Street Lighting Tax;
   f. Non-Metallic and Rock Mineral Taxes;
   g. Parking Tax;
   h. Groundwater Tax;
   i. Swallow's Nest Tax;
   j. Land and Building Tax on Urban and Rural Sector;
   k. Acquisition of Land and/or Building Rights.

III.2.2 Profile of the Directorate General of Taxes

DGT is an echelon-I unit under the Ministry of Finance which has a responsibility for formulating and implementing policy and technical standardization of taxation. The tasks are further described within the implementation of the following functions:

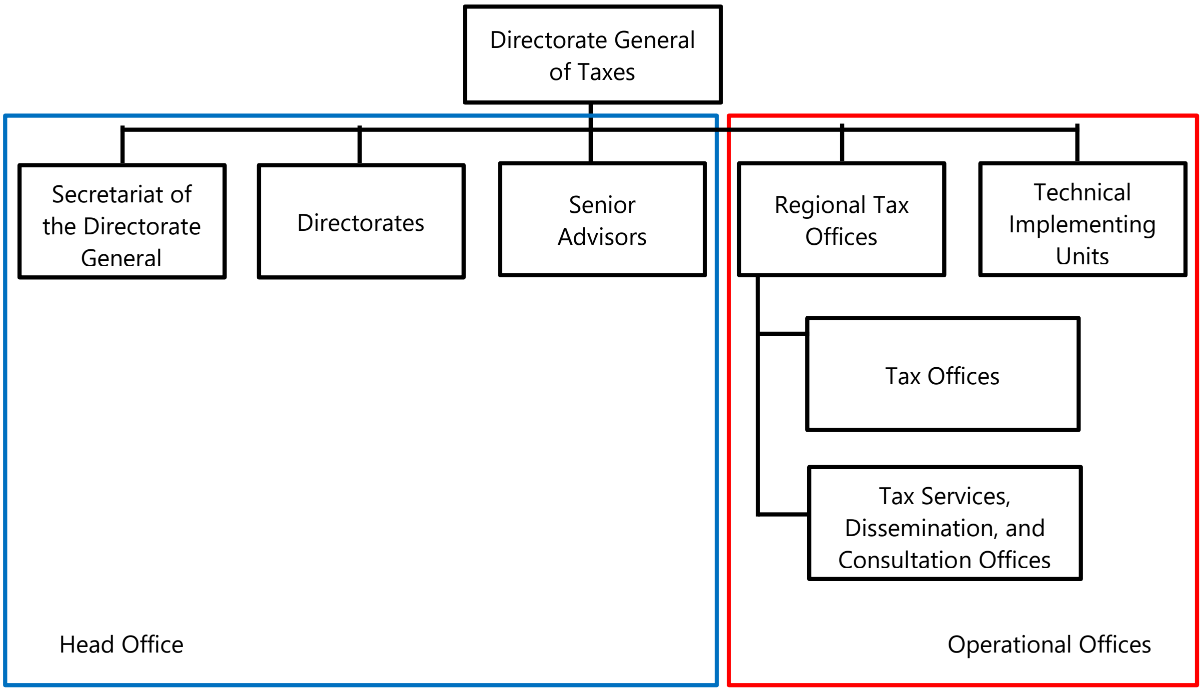
a. Formulating taxation policy;
b. Implementing taxation policies;
c. Formulating taxation norms, standards, procedures, and criteria;
d. Providing taxation technical guidance and supervision;
e. Performing monitoring, evaluation, and reporting in taxation;
f. Performing the administration of DGT; and
g. Performing other functions assigned by the Minister of Finance.

In general, DGT responsibles to collect tax revenue. The vision of DGT is to become the best state tax administrator to ensure state sovereignty and autonomy. The Mission of DGT are to ensure the implementation of a sovereign and self-governing state by: (i) Collecting tax revenue based on a high level of voluntary tax compliance and just law enforcement; (ii) Providing modern technology-based services to ease tax obligation fulfilment; (iii) Building tax officers who are competent, professional and owning high level of integrity; and (iv) Providing competitive rewards based on performance management system.

Overall, DGT consists of head office and operational offices. The head office runs several functions including the formulation of policies and technical standardization, the analysis and development (transformation), as well as the administrative supports (governance, human resources, finance, general affairs and logistics). Meanwhile, the operational offices conduct technical operational and/or support functions.

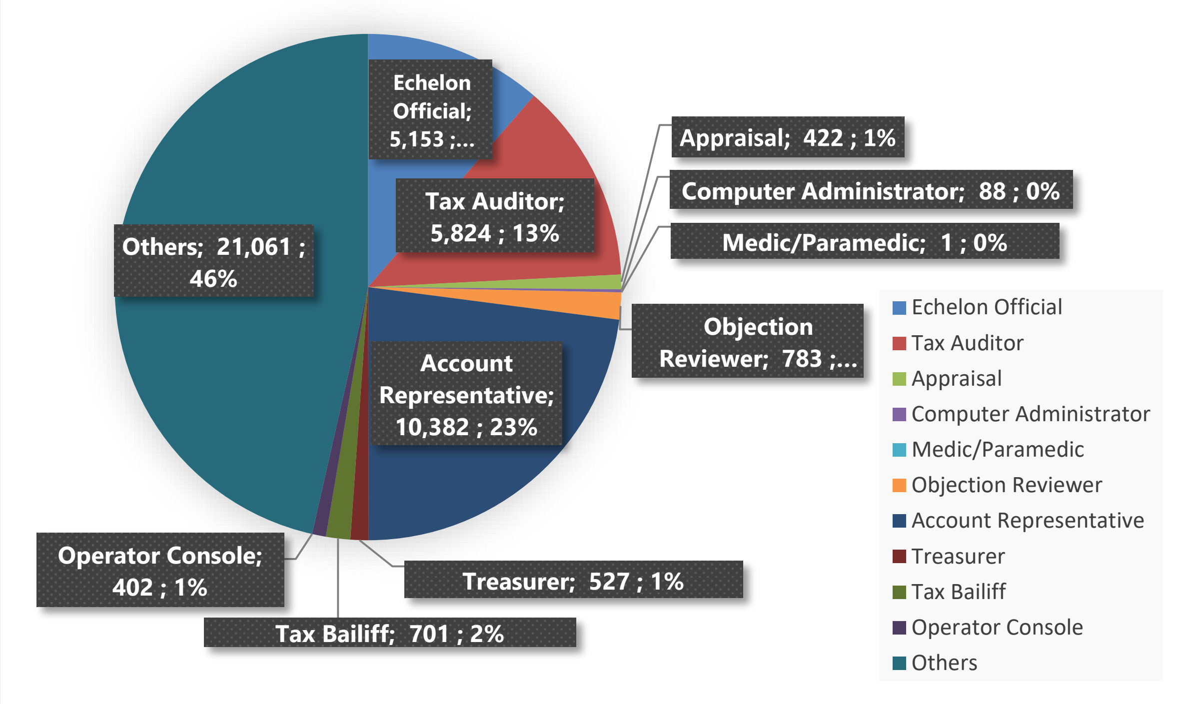
DGT Head Office consists of the Secretariat of the Directorate General, 14 Directorates, and 4 Senior Advisors. DGT operational offices consist of the Regional Tax Offices/Kantor Wilayah (34); the Large Tax Offices/KPP Wajib Pajak Besar (4); the Medium Tax Offices/KPP Madya (29); the Small Tax Offices/KPP Pratama (319): the Tax Services, Dissemination, and Consultation Offices/KP2KP (204); and the Technical Implementing Units/UPT (4) all over Indonesia. The UPT consists of the Taxation Data Processing and Documentation Center (PPDDP), the Taxation Data and Document Processing Office (KPDDP), and the Information and Complaints Service Office (KLIP).

Figure 1: DGT Organization Chart



The total number of personnel as of December 2018 accounted for 45,344 comprises 65.82% men and 34.18% women respectively. By age, most personnel (8,773 personnel) are at their 21-25 of ages while 1,135 others aged 56-60 as the least group in population. By educational level, 15,747 are undergraduate, 6,067 are graduate, and 52 are post-graduate. Moreover, by grade class, 2 are Class I, 20,452 are Class II, 21,567 are cLass III, and 3,323 are Class IV. Further, based on job position, the distribution of personnel is depicted in the following graph.

Figure 2: Number of Personnel by Job Position



Source: DGT Annual Report, 2018

III.2.3 Tax Revenue

Until the end of 2018, DGT has succeeded collected tax revenue of IDR 1,313.32 trillion or 92.23% of the target. Realization of tax revenue in 2018 grew by 14.10% (yoy), increasing far compared to the growth in 2017 which only reached 4.07% (yoy). The positive performance of 2018 tax revenue growth is supported by double digit growth in large part types of tax, namely Non-Oil and Gas Income Tax (14.89%), VAT and LST (11.76%), LBT (15.95%), and Oil and Gas Income Tax (28.61%). More details as follow:

Tabel 31: DGT Net Tax Revenue

(trillion Rupiah)

Year	Non-Oil & Gas Income Tax	VAT & LST	Land & Building Tax	Other Taxes	Oil & Gas Income Taxes	Total	
						Excluding Oil & Gas Income Tax	Including Oil & Gas Income Tax
2014	459.08	408.83	23.48	6.29	87.44	897.68	985.13
2015	552.22	423.71	29.25	5.57	50.11	1,010.75	1,060.86
2016	630.12	412.21	19.44	8.10	36.10	1,069.87	1,105.97
2017	596.48	480.72	16.77	6.74	50.32	1,100.71	1,151.03
2018	685.28	537.26	19.44	6.63	64.71	1,385.86	1,313.32

Source: DGT 2018 Annual Report

III.2.4 Taxpayer Compliance: A Tax Return Submission Outlook

As the main contribution to the state revenue, taxes become the most important discussion every year. It is not only the realisation of tax revenue that DGT may achieve, but also the tax complaince. Therefore, DGT performs a number of efforts in achieving a high level of compliance by continuing to provide insight to the public awareness of registering, paying and reporting taxes regarding the sustainable development.

First, to be registered taxpayers, a taxpayer is able to perform registration either by using "e-registration" mechanism or simply visiting the service counter in every tax office. DGT puts e-Registration as a tool intended to increase the number of registered taxpayer. As seen on the following Table 32, there are three types of taxpayers: Individual, Corporate, and Treasurer. A treasurer defines as a person acted as a state treasurer who runs the treasury in any units of government institutions and also has to register themselves to get a Tax Identification Number (TIN).

Tabel 32: The Number of Registered Taxpayers, 2014-2018

(taxpayers)

Type	2014	2015	2016	2017	2018
Individual	27,421,041	30,184,682	33,005,315	35,540,985	38,651,308
Corporate	2,463,878	2,674,406	2,912,882	3,110,887	3,320,020
Treasurer	413,819	454,567	479,892	499,731	508,157
Total	**30,298,738**	**33,313,655**	**36,398,089**	**39,151,603**	**42,479,485**

Source: DGT 2018 Annual Report

Second, DGT also finds another effort to improve tax awareness of the taxpayers by intensifying tax education. By giving such tax education program ranges, for instance face-to-face meeting to various workshops, disseminations, seminars, sports events, car free day and other outdoor activities or in the form of indirect contact via www.pajak.go.id website, television and radio, or in the form of printed media such as newspapers, school text books, booklets, and or by using online and social media. Those are intensively conducted by every unit in DGT.

In addition, with the emerging use of internet in Indonesia, DGT provides a simpler tax return submission based on electronic system using djponline.pajak.go.id rather than coming directly to the tax office nearby. Taxpayers can freely to choose the media of filing return by using e-SPT application or directly visit to the e-Filing website. Hence, the goal is to increase the number of tax return submission as shown on the Table 33 below.

Tabel 33: Compliance Ratio of Annual Income Tax Return Submission, 2014-2018

(taxpayers)

Uraian	2014	2015	2016	2017	2018
Registered Taxpayers Obliged to Submit Tax Return	**18.357.833**	**18.159.840**	**20.165.718**	**16.598.887**	**17.653.046**
a. Corporate	1.166.036	1.184.816	1.215.417	1.188.488	1.451.512
b. Individual - Employee	14.455.480	14.920.292	16.817.086	13.446.068	13.748.881
c. Individual - Non-Employee	2.736.217	2.054.732	2.133.215	1.964.331	2.452.653
Annual Income Tax Return	**10.854.819**	**10.972.950**	**12.249.793**	**12.047.967**	**12.551.444**
a. Corporate	552.959	681.488	706.798	774.188	854.354
b. Individual - Employee	9.659.375	9.445.376	10.607.940	10.065.056	9.875.321
c. Individual - Non-Employee	642.485	846.086	935.055	1.208.723	1.821.769
Compliance Ratio	**59,13%**	**60,42%**	**60,75%**	**72,58%**	**71,10%**
a. Corporate	47,42%	57,52%	58,15%	65,14%	58,86%
b. Individual - Employee	66,82%	63,31%	63,08%	74,86%	71,83%
c. Individual - Non-Employee	23,48%	41,18%	43,83%	61,53%	74,28%

Source: DGT 2018 Annual Report

III.3 Current Tax Law and Regulation

III.3.1 Corporate Income Tax

III.3.1.1 Overview

An entity is considered taxable if it has a presence and conducts business within the country. Such definition includes a place of management, branch, representative office, office building, agent, factory or workshop, construction or mining site. Such entity is required to register at the relevant DGT office for their location/status at the time or shortly after establishment thereafter an annual income tax return should be filed including its worldwide income. In addition, tax paid offshore in relation to foreign source income can be credited in the same tax year subject to certain limitations.

III.3.1.2 Tax Rates

A single flat rate of 25% has been applied since 2010. Public enterprises that satisfy a minimum listing requirement of 40% and other conditions are entitled to a tax discount of 5% of the standard rate, giving an effective tax rate of 20%. To be eligible, a public enterprise must have at least 40% of the outstanding shares owned by at least 300 persons, each holding less than 5% of the paid-in shares, and this condition must be maintained for at least 183 days in a taxable year. Small enterprises, i.e. corporate taxpayers with an annual turnover of not more than IDR 50 billion, are entitled to a tax discount of 50% of the standard rate for taxable income of up to IDR 4.8 billion.

III.3.1.3 Tax Residence

An entity is treated as a resident of Indonesia for tax purposes by virtue of having its establishment or its place of management in Indonesia. A foreign company carrying out business activities through a Permanent Establishment (PE) in Indonesia will generally have to assume the same tax obligations as a resident taxpayer.

III.3.1.4 Taxable Income

The object of tax is income, which is defined as any economic benefit received or accrued by a taxpayer, whether originating from within or outside of Indonesia, which is used for consumption, or which increases the wealth of the taxpayer, in whatever name or form. A company income can be defined as follows:

1. Gross profits from business;
2. Gains upon the sale or transfer of property (realized capital gains);
3. Interest, dividends, and royalties (subject to certain exceptions);
4. Rents;
5. Income from debt forgiveness and;
6. Surplus on revaluation of assets (favorable tax rate may apply).

Exchange gains or losses resulting from normal movements in currency exchange rates are, in most cases, included in taxable income in the current fiscal year irrespective of whether they are realized or unrealized. Gains or losses arising from a change in currency rates resulting from a government regulation or decree (revaluation or devaluation) may be subject to special concessions.

III.3.1.5 Exempted Income

Excluded from the definition of taxable income are, among others:

1. Gifts or donations that are not related to the business or profession of the parties involved;
2. Dividends received by a resident company from another resident company, provided:
    a. The dividend is sourced from retained earnings, the recipient owns at least 25 percent of paid up capital.
    b. The holding companies no longer need to undertake any other business activities due to removal of the ”active business” criteria for holding companies. Therefore any interest expense incurred in relation to the holding company’s investment will not be deductible since the dividends received are not taxable.
3. Income received by venture capital companies in the form of profits or dividends, as long as the investee companies meet certain requirements and the companies are not listed on the stock exchange and.
4. Income from the capital invested by the pension fund, in the fields of certain specified by regulation of the Minister of Finance.

III.3.1.6 Capital Gains Tax

Capital gains or losses may come from sales of a company’s assets. It is calculated as the difference between the sales proceeds and the tax written down value of the assets concerned. Capital gains are assessable while a capital loss is tax-deductible only if the asset concerned is used in the running of the business, i.e. for obtaining, collecting, and securing assessable income. The exemptions are for transactions in stock on the Indonesian stock market and on private property. The gain or loss is ignored and tax is instead charged on the transaction value. The tax rate is 0.1% of transaction value of stock, except for founder shares sold by founder 0.5% of transaction value. For Land and building, tax rate is

5 % of transfer value – final tax for individuals, foundations and corporations.

III.3.1.7 Dividend

Tax is withheld from dividends as follows:

1. Resident recipients. Dividends received from an Indonesian company by a limited liability company incorporated in Indonesia as Perseroan Terbatas (PT), a cooperative, or a state-owned company (BUMN/BUMD), are exempt from income tax if the following conditions are met: the dividends are paid out of retained earnings; and the company earning the dividends holds at least 25% of the paid-in capital in the company distributing the dividends;
2. Non-resident recipients: 20% (lower for treaty countries) final withholding tax is due on dividends paid to a non-resident recipient.

If these conditions are not met, the dividends are assessable to the company earning the dividends at the ordinary tax rates alongside the company's other income. Upon declaration, dividends are subject to Article 23 Income Tax at 15%, which constitutes a prepayment of the corporate tax liability for the company earning the dividends. Dividends received by firma, commanditaires, foundations and similar organizations are always subject to 15% withholding tax. Dividends received by resident individual taxpayers are subject to final income tax at a maximum rate of 10%.

III.3.1.8 Deductions

The taxable income is determined after deducting allowable deduction cost from gross income. The list of allowable deduction costsis as follows:

1. The costs of deriving, recovering and conserving such income including, the costs of materials, wages, salaries of employees, employee bonuses, honoraria, cash allowances, interest, rent, royalties, travel expenses, waste treatment costs, insurance premiums, administrative costs, and taxes other than income tax;
2. Promotional and sales costs;
3. Bad debts, provided strict conditions are fulfilled;
4. Depreciation of the acquisition cost of property and amortization of costs incurred in obtaining rights and other costs that have a useful life of more than one year;
5. "Zakat" donations if paid to an approved body by a Moslem individual or Moslem-owned business;
6. Losses from the sale or transfer of assets;
7. Foreign exchange losses;
8. Costs of research and development performed in Indonesia;
9. Scholarships, apprenticeships and training costs;
10. Donations (as regulated by Government Decree) in relation to: national disasters, research and development in Indonesia, the provision of educational facilities, and development of sports;
11. The provisioning of reserves for re-forestation and closure/maintenance of industrial waste storage locations are deductible for these business sectors (as further regulated by Minister of Finance Decree);
12. Goodwill can be capitalized and amortized;
13. Office refreshments;
14. Prior year losses; and
15. Contributions to a pension fund approved by The Ministry of Finance (MoF).

Additionally, entertainment costs are an allowable deduction where they relate to securing, acquiring and collecting income, but substantiation requirements exist. Full details of each expense are required to be lodged with the annual tax return. Moreover, there are also some non-allowable deductions cost from gross income as follows:

1. Benefits-in-kind (BIK) for instance, free housing, 50% of the acquisition and maintenance costs of certain company provided cars, except food and drink provided to employees in the workplace, employee benefits required for job performance, such as protective clothing and uniforms, transportation costs to and from the place of work, accommodation for ship crews and the likes, the cost of providing BIKs in remote areas, and 50% of the acquisition and maintenance costs of cellular phones;
2. Private expenses;
3. Non-business gifts and aid, except Islamic alms ("Zakat");
4. Provisions: However, certain types of provision d. are claimable as deductible expenses: provision for doubtful accounts for banking and financing companies, insurance claims provision for insurance companies, deposit security provision for the Deposit Security Blanket Institution (LPS), reclamation provision for mining companies, forestation provision for forestry companies, and area closure and maintenance provision for industrial waste processing businesses;
5. Income tax payments;
6. Tax penalties;
7. Profit distributions;
8. Employer contributions for life, health and accident insurance and contributions to unapproved pension funds, unless the contributions are treated as part of the taxable income of employees;
9. Expenses relating to income which is taxed at a final rate, e.g., interest on loans relating to time deposits;
10. Expenses relating to income which is exempt from tax, e.g., interest on loans used to buy shares where dividends to be received are not subject to income tax;
11. Salaries or compensation received by partnership or firm as members where their participation is not divided into shares.

III.3.1.9 Losses

Losses may be carried forward for a maximum of 5 years. However, for a limited category of businesses in certain regions or businesses subject to certain concessions, the period can be extended for up to ten years. The carrying-back of losses is not allowed while tax consolidation also is not applicable.

III.3.1.10 Capital Allowances

Expenditure incurred in relation to assets with a beneficial life of more than one year are categorized and depreciated from the month of acquisition by the consistent use of either the straight-line or the declining-balance method, as follows:

1. Category 1: 50% (declining-balance) or 25% (straight-line) on assets with a beneficial life of four years. Examples of assets in this category are computers, printers, scanners, furniture and equipment constructed of wood/rattan, office equipment, motorcycles, special tools for specific industries/services, kitchen equipment, manual equipment for agriculture, farming, forestry and fishery industries, light machinery for the food and drink industries, motor vehicles for public transportation, and equipment for the semi-conductor industry.
2. Category 2: 25% (declining-balance) or 12.5% (straight-line) on assets with a beneficial life of eight years. Examples of assets in this category are furniture and equipment constructed of metal, air conditioners, cars, buses, trucks, speed-boats, containers and the like. The category also covers machinery for agriculture, plantations, forestry activity, fisheries, and for food and drink, and light machinery, logging equipment, equipment for construction, heavy vehicles for transportation, warehousing, and communication, telecommunications equipment, and equipment for the semi-conductor industry.
3. Category 3: 12.5% (declining-balance) or 6.25% (straight-line) on assets with a beneficial life of 16 years. Examples of assets in this category are machines for general mining other than in the oil and gas sector, machines for the textile, timber, chemical, and machinery industries,

heavy equipment, docks and vessels for transportation and communication, and other assets not included in the other categories.

4. Category 4: 10% (declining-balance) or 5% (straight-line) on assets with a beneficial life of twenty years. Examples of assets in this category are heavy construction machinery, locomotives, railway coaches, heavy vessels, and docks.
5. Building: 5% (straight-line) on assets in the permanent building category with a useful life of 20 years; or 10% (straight-line) on assets in the non-permanent building category with a useful life of ten years. Included in the cost of the buildings is the land and building transfer duty (DAL&BR) on building rights.

Intangible property or costs, including the cost of extending building use rights, rights for business use, rights for use and DAL&BR on land rights with a useful life of more than one year, should be amortized on the following bases, as appropriate:

1. By using the straight-line or the declining-balance method at the rates specified in categories 1, 2, 3, and 4 under Depreciation, based on the useful life of the property: Category 1: 4 years; Category 2: 8 years; Category 3: 16 years; Category 4: 20 years.

Membership of the category is determined on the basis of the nearest useful life (e.g., an intangible asset with a useful life of six years may fall under Category 1 or Category 2, while an intangible asset with a useful life of five years is under Category 1).

2. The costs of incorporation and expansion of the capital of an enterprise are claimed in full in the year in which the expenditure is incurred or are amortized using either the declining-balance or straight-line method at the following rates:

Category 1: 50% declining-balance; 25% straight-line
Category 2: 25% declining-balance; 12.5% straight-line
Category 3: 12.5% declining-balance; 6.25% straight-line
Category 4:10% declining-balance; 5% straight-line

3. Costs incurred for acquiring the right to oil and natural gas concessions with a beneficial life of longer than one year are amortized using the production-unit method.
4. Costs incurred in the acquisition of mining rights, forest concessions, and other rights to exploit natural resources and natural products with a beneficial life of longer than one year are amortized using the production-unit method but not may not exceed 20% per annum.
5. Costs incurred before the commencement of commercial operations with a useful life of longer than one year are capitalized and amortized according to the rates set out.

Subject to DGT approval, corporate taxpayers and PEs who maintain Rupiah accounting may undertake a revaluation of their non-current tangible assets for tax purposes. This may be carried out once every 5 years. Each revaluation must include all business-related assets which are owned by the company and located in Indonesia, except for land and buildings (these may be omitted). Before requesting the DGT's approval, the company concerned must determine that it has settled all of its outstanding tax liabilities

The revaluation must be conducted on a market or fair value basis. The market values must be determined by a government-approved appraiser. These are subject to DGT adjustments if the values, in DGT's view, do not represent the fair or market values of the assets. Once approved, the depreciation applied to depreciable assets must be based on the new tax book values (approved values) on the basis of a full useful life (in other words, as if the assets were new). The excess of the fair market value over the old tax book value of the revalued assets is subject to final income tax at a rate of 10%. Subject to DGT approval, taxpayers facing financial difficulties may pay this tax in installments over 12 months. Fixed assets falling under categories 1 and 2 must be retained at least to the end of their useful life.

Land, buildings, and assets falling under categories 3 and 4 must be retained for at least 10 years of the revaluation date. Additional final income tax at a rate of 10% is imposed on the original revaluation gains if the revalued assets are sold or transferred before the end of this minimum retention period (this does not apply to assets transferred because of force majeure, assets transferred based on government decision/policy/court decision or assets transferred in the course of a tax-neutral business merger, a consolidation, or a business split and fixed asset withdrawal because of irreparable damage).

III.3.1.11 Tax Payments

Resident taxpayer and PE of foreign companies have to settle their tax liabilities either by direct payments, third party withholdings, or a combination of both. Foreign companies without a PE in Indonesia have to settle their tax liabilities for their Indonesian-sourced income through withholding of the tax by the Indonesian party paying the income as follows:

1. Monthly tax installments (Article 25 Income Tax) constitute the first part of tax payments to be made by resident taxpayers and Indonesian PEs. As a prepayment of their current year corporate income tax liability, a monthly tax installment is generally calculated using the most recent corporate tax return. Special installment calculations apply for new taxpayers, finance lease companies, banks and state-owned companies, listed companies and other taxpayers with periodical reporting requirements;
2. The tax withheld by third parties on certain income (Article 23 Income Tax) or tax to be paid in advance on certain transactions (e.g., Article 22 Income Tax on imports) constitute other prepayments for the current year corporate tax liability of the income recipient or the party conducting the import;
3. If the total amounts of tax paid in advance through the year (Articles 22, 23, and 25 Income Taxes) and the tax paid abroad (Article 24 Income Tax) are less than the total corporate tax due, the company concerned has to settle the shortfall before filing its corporate income tax return. Such a payment is referred to as Article 29 Income Tax.
4. Certain types of income earned by resident taxpayer and Indonesian PE are subject to final income tax. In this respect, the tax withheld by third parties (referred to as Article 4 Paragraph 2 Income Tax) constitutes the final settlement of the income tax for that particular income;
5. For foreign companies without a PE in Indonesia, the tax withheld from their Indonesia-sourced income by the Indonesian party paying the income (Article 26 Income Tax) constitutes a final settlement of their income tax due.

III.3.2 Individual Income Tax

III.3.2.1 Overview

The extent of the Indonesian income tax liability depends upon the individual’s residence status in Indonesia. Resident individuals are taxed on their worldwide income, regardless of where such income arises from or for whom work or service is performed. For Indonesian-source income, there is an extensive framework of withholding taxes so that income tax is often collected by deduction at source, for example in relation to employment income, interest, dividends, royalties, rent and income from sales of property, and listed shares.

Non-resident individuals are exempted from the worldwide income reporting obligation and tax is imposed only on income derived in Indonesia. Deductions are limited to individual personal allowances. Resident individual taxpayer who receive or earn annual income exceeding the income threshold must register with the tax office and file annual income tax returns. The tax return should state the individual’s income, including compensation from employment, investment income, capital gains, overseas income, and other income. Tax return also provides a summary of the individual’s assets and liabilities.

A family is generally regarded as a single tax reporting unit with only a single TIN in the name of the head of the family (typically the husband). His wife and his dependent children’s income must be reported on the same tax return in his name. A married woman has two options. She can choose to have her own tax identification number and report her own income tax return separately from her husband. Otherwise, she can merge her income to her husband’s tax return.

III.3.2.2 Tax Rates

Most income earned by individual tax residents is subject to income tax at the normal tax rates:

Table 34: Individual Income Tax Rate

Taxable Income	Rate
Up to IDR 50,000,000	5%
Above IDR 50,000,000 up to IDR 250,000,000	15%
Above IDR 250,000,000 up to IDR 500,000,000	25%
Above IDR 500,000,000	30%

Source: Indonesia's Law of Income Tax

III.3.2.3 Main Personal Relief

The amount of annual non-taxable income (PTKP) for resident individuals firstly implemented on June 27, 2016 are as follows:

Table 35: Individual Main Personal Relief

Layers	Amount (IDR)
Taxpayer	54,000,000
Spouse	4,500,000
Each dependent (max of 3)	4,500,000
Occupational expenses (5% of gross income, max Rp.500,000/month)	6,000,000
Employee contribution to *Jamsostek* for pension fund (2% of gross income)	Full amount
Pension maintenance expenses (5% of gross income, max Rp.200,000/month)	2,400,000

Source: Indonesia's Law of Income Tax

III.3.2.4 Tax Residence

Indonesian tax law distinguishes between resident and nonresident taxpayers. Residents are defined as individual if he/she fulfills any of the following conditions:

a. resides in Indonesia;
b. presents in Indonesia for 183 days or more in any continuous 12-month period;
c. presents and resides in Indonesia during the fiscal years and intend to remain in Indonesia.

Non-resident taxpayers are individuals present in Indonesia for fewer than 183 days with no intention to reside. Nonresidents need not register for tax purposes. Resident individual taxpayers are taxed on their worldwide gross income less allowable deductions and nontaxable income. Non-resident employees in the oil and gas sectors are taxed on deemed salaries based on job titles. The provisions of tax treaties may override these rules.

III.3.2.5 Taxable Income

Income is defined as any economic benefit received or accrued by a taxpayer that is used for consumption or that increases the wealth of the taxpayer, in whatever name or form. The following types of income are subject to tax:

1. Compensation or payments received or earned in connection with work or services;
2. Lottery, prizes, and awards;
3. Gross profits from individual business activities;
4. Gains from the sale or transfer of assets;
5. Refunds of tax payments already deducted as expenses;
6. Interest; and
7. Dividends, in whatever name or form, paid by a corporation, payments of dividends by an insurance company to policy holders.

III.3.2.6 Benefits-in-kind

Benefits in kind received by employees, including discounted or free housing, are not taxable to the employee nor deductible to the provider/employer. However, company cars and cellular phones provided to the employee are deductible at 50% of the acquisition cost by way of depreciating those assets over their useful lives (8 years and 4 years), while cellular phone refill vouchers and repair expenses can be claimed as deduction at 50%. A full deduction however applies to food and drinks provided to employees in the workplace and employee benefits required for job performance such as protective clothing and uniforms, transportation costs to and from the place of work, accommodation for ship crews and the like, and also for housing provided in remote areas approved by the Minister of Finance.

III.3.2.7 Tax Payments

A substantial part of individual income is collected through withholding by third parties. Employers are required to withhold Article 21/26 Income Tax on a monthly basis from the salaries and other compensation payable to their employees. If an employee is a resident taxpayer, the amount of tax withheld should be based on the normal tax rates (as set out above). If he/she is a non-resident taxpayer, the withholding tax is 20 percent of the gross amount (and may be set at a lower rate under a tax treaty). Various other payments to individuals also call for withholding tax obligations from the payers. These include, among others: pension payments made by government-approved pension funds; severance payments; old-age security saving payments from *Jamsostek*; scholarships; fees for services; prizes/awards. Typically the amount of tax withheld from this income is based on normal tax rates. Fees for certain professionals, such as lawyers, notaries, accountants, architects, doctors, actuaries and appraisers, are required to be calculated based on 50% of the gross income.

III.3.3 Tax Rate for Small and Medium Enterprises and Individual Business

Government Regulation Number 23 of 2018 concerning Income Tax on Income from Business Received/Earned by Taxpayer with Certain Gross Turnover has been enacted on 8 June 2018 and come into effect beginning from 1 July 2018 – it revoked the lastly applied Government Regulation Number 46 of 2013. The regulation stipulates that individual (individual businesses with small to medium range trading and services activities other than professional services, such as lawyers, accountants, translators, insurance agents, etc.) as well as corporate taxpayers other than permanent establishments having annual income up to IDR 4.8 billion are subject to final tax at 0.5%. However, taxpayers can only benefit from such new regulation only for some time limitations: 7 years for individual; 4 years for cooperative, limited partnership, or firm; and 3 years for limited liability company. Excluded also on the basis of types of taxpayers among others are taxpayers who choose to apply normal tax rate based on Article 17 or 31E Law of Income Tax, individual taxpayers in the form of limited partnerships/firms delivering services categorized as freelance business activities, taxpayers who benefit from tax holiday or tax allowance, and as already mentioned, taxpayers in the form of PEs.

III.3.4 Withholding Tax

Income tax collection is mainly conducted through withholding taxes system whereby a particular income item is subject to withholding tax, the payer is generally held responsible for collection by withholding the tax.

III.3.4.1 Article 21 – Salaries and Other Payments to Individuals

Employer is required to withhold Article 21 Income Tax from the salaries payable to their employees and pay the tax to the State Treasury on their behalf. The same withholding tax is applicable to other payments to non-employee individuals (e.g., fees payable to individual consultants or service providers). Resident individual taxpayers without TIN are subject to a surcharge of 20 % in addition to the standard withholding tax.

III.3.4.2 Article 22 – Imports

Article 22 income tax is typically applicable in the following events:

1. Importation of goods;
2. Sale of goods to the government calling for payments from the State Treasury, the State Budget General Directorate, or certain state-owned companies;
3. Sale/purchase transactions of steel, automotive, cigarettes, cement, and paper products; and
4. Sale/purchase of luxurious goods.

III.3.4.3 Article 4 Paragraph (2) – Final Income Tax

Resident companies, PEs, representative of foreign companies, organizations, and appointed individuals are required to withhold final tax from the following gross payments to resident taxpayers and PEs:

Table 36: Final Income Tax Rate

Description	Tax Rate
Rental of land and/or buildings	10%
Proceeds from transfer of land and building right	5%
Fees for constructions work performance	2/3/4%
Fees for constructions work planning	4/6%
Fees for constructions work supervision	4/6%
Interest on time or saving deposits and on Bank Indonesia Certificates (SBIs) other than that payable to bank operating in Indonesia and to government-approved pension funds	20%
Interest on bonds other than that payable to banks operating in Indonesia and government- approved pension funds	15%
Proceeds from sale of shares on Indonesian stock exchanges. Founder shareholders may opt to pay tax at 0.5% of the market price of their shares upon listing, otherwise, gains on subsequent sales are taxed under normal rules	0.1%
Income from lottery prizes	25%
Certain income received by individuals and corporates (except PEs) with gross turnover of not more than IDR 4.8 billion in one fiscal year.	0.5%

III.3.4.4 Article 23 – Residents

Certain types of income paid or payable to resident taxpayer are subject to Article 23 Income Tax at a rate of either 15% or 2% of the gross amount. Article 23 Income Tax sets 15% rate of the gross amount on dividends, interest (including premiums, discounts and loan guarantees fees), royalties, prizes and awards.

III.3.4.5 Article 26 – Non-Residents

Resident taxpayers, organizations, and representatives of foreign companies are required to withhold 20% tax from the following payments to non-residents:

1. On Estimated Net Income (ENI), being a specified percentage of the gross amount:

Table 37: Non Resident Estimated Net Income

Description	ENI	Effective Tax Rate
Insurance premiums paid to non-resident insurance companies:		
By the insured	50%	20%
By Indonesian insurance companies	10%	2%
By Indonesian reinsurance companies	5%	1%
Sale of non-listed shares by non-residents	25%	5%
Sale for by the non-residents holding of Indonesian of a conduit company companies hares/where PE serves as an intermediary	25%	5%

2. On gross amount, the object of tax would be in the form of dividend; interest including premiums, discounts (interest), swap premiums, and guarantee fees; royalties, rents and payments for the use of assets; fees for services, work, and activities; prizes and awards; and pensions and any other periodic payments. After-tax profit of a PE is exempted from withholding tax if it reinvest in Indonesia in the form of equity participation in a company

established and domiciled in Indonesia for which such PE acts as the founder or one of the founders.

III.3.5 Income Tax on Certain Income in the Form of Net Assets

To provide legal certainty and simplicity while improving taxpayer's compliance after Tax Amnesty Program, Government Regulation Number 36 of 2017 concerning Imposition of Income Tax on Certain Income in the form of Net Assets Treated/Deemed as Income, Minister of Finance Regulation Number 165 of 2017 Tax Amnesty and Regulation Implementation, and Director General of Taxes Regulation Number 23 of 2017 concerning Procedures for Submission of Monthly Final Income Tax Return on Disclosure of Net Asset have been enacted, further known as Voluntary Asset Disclosure – Final Tax Rate policy.

Final rate of 25% applies for corporate taxpayer, 30% for individual taxpayer, and 12.5% for certain taxpayer. Meanwhile, types of income belong to this category are:

1. Additional net assets as referred to Article 13 par. (4) of Tax Amnesty Law;
2. Net assets owned by the end of preceding tax year which had not been disclosed or less disclosed as referred to Article 18 par. (1) of Tax Amnesty Law;
3. Net assets owned by the end of preceding tax year which had not been disclosed in Income Tax Return as referred to Article 18 par. (2) Of Tax Amnesty Law.

III.3.6 Income Tax on Land/Building Rent

Based on Government Regulation Number 34 of 2017 concerning Income Tax on Income from Rent of Land and/or Building, enacted on 2 January 2018, income derived from rental activity of land and/or building either by individual or corporation that holds land rights from related investors through the implementation of Build-Operate-Transfer (BOT) agreement is subject to 10% final tax rate.

III.3.7 Value Added Tax and Luxury-Goods Sales Tax

Either entity or individual, in any form, which in the course of his operations consisting production, import or export of taxable goods, trading activities or taxable services, is required to register as a Taxable Entrepreneur to DGT,however, registration by non-resident is not allowed.

III.3.7.1 Taxable Goods and Services

VAT is typically due to events involving transfers of taxable goods or provisions of taxable services in the Customs Area. Such taxable events include:

1. Deliveries of taxable goods in the Customs Area by an enterprise;
2. Importation of taxable goods;
3. Deliveries of taxable services in the Customs Area;
4. Use or consumption of taxable intangible goods originating from outside the Customs Area in the Customs Area;
5. Use or consumption of taxable services originating from outside the Customs Area in the Customs Area;
6. Export of taxable goods (tangible and intangible) by an enterprise; and
7. Export of taxable services by an enterprise.

Delivery of taxable goods are defined broadly and include the following: deliveries of a title to taxable goods according to an agreement; transfers of taxable goods according to a leasing-with-option or finance-lease agreement; deliveries of taxable goods to an intermediary trader or an auction official; own-use and/or free gift of taxable goods; remaining taxable goods and certain assets originally not for sale at a company's dissolution; deliveries of taxable goods within a company (e.g., between branches, or between the head office and its branches) unless the company, at the DGT's approval, centralizes its

VAT reporting; deliveries of taxable goods on consignment; deliveries of taxable goods by a taxable entrepreneur in the framework of sharia-based financing, whereby the deliveries are deemed to take place directly from the taxable entrepreneur to the party in need of the taxable goods.

Several exemptions apply on goods for basic necessities, mining taken from natural resources, food served in hotels and restaurants including food and drinks provided by catering services, money, gold and securities. Some other exemptions on broad area of services are medical, social and religious services, postal and account transfer services, banking, insurance and non-banking financial leasing, educational services, finance leasing, art and entertainment services, radio and television broadcasting services other than advertisements, public transportation services in land, sea and domestic air transportation, manpower and recruitment services, hotel and boarding house services, services provided by the government related to public administration and formality requirements, parking services, public telephone (by coin) services, food and catering services.

III.3.7.2 Tax Rates and Tax Base

Normal rate of 10% is imposed on importers, manufacturers, wholesalers and retailers as well as on the provision of services. While VAT law and regulation permit amendments of the rates for individual items, products with rate other than 10% are cigarettes and used cars. Services such as package deliveries and travel agents are taxed at 1%. Export of taxable goods are effectively excluded from VAT by being subject to the tax at a 0% rate.

VAT for a particular taxable event is calculated by applying the VAT rate to the relevant tax base. In most cases, the tax base is the transaction value agreed between the parties concerned. For certain events or situations, other parameters must be used as the tax base, including:

1. Market value for transactions between related parties, remaining inventories of taxable goods at a company's dissolution, and sales of (non-inventorial) assets originally not for sale;
2. Cost of sales for own-use or free gifts and internal deliveries of taxable goods (e.g., between branches, from the head office to branches);
3. Auction price for deliveries of taxable goods to an intermediary trader of an auction officer;
4. Agreed price for deliveries of taxable goods through an intermediary trader;
5. Average result per film for movies;
6. IDR 12 million per copy of imported movies;
7. 20% of total costs incurred or paid, exclusive of the acquisition price of land, for the self-construction of a building;
8. Retail selling prices for deliveries or imports of tobacco products;
9. 10% of the actual billing for package shipment services;
10. 10% of the actual billing for tour and tourism agency services whose deliveries are not based on commissions;
11. 20% of selling price on the deliveries of gold jewelry, including services carried out by the factory in relation to gold jewelry;
12. 10% of actual billing on the deliveries of freight forwarding services in which billing includes freight charges.

III.3.7.3 Relief for Export Manufacturers

A number of relief schemes allows export manufacturers to operate on a virtually VAT and duty-free basis including bonded zones, economic development zones (KAPET) and free trade zones. For example, free trade zones (Sabang, Batam, Bintan, and Karimun) as well as free ports are located in Indonesia but are considered outside the customs area thereby goods brought into these areas are exempted from import duties, VAT and LST. Business activities which are able to be carried out in a free trade zone, among others, are trade, services, mining, transportation, banking and manufacturing.

III.3.7.4 VAT Reporting

A company carrying out business activities through a number of business units/branches in the working areas of different tax offices must have its units/branches registered to relevant tax offices depending on the location/domicile. Such mechanism applied is in accordance with the context that internal deliveries of taxable goods within a company line of business are subject to VAT. Hence, corporation and individual as taxable entrepreneurs are obliged to report their business activities as well as to settle their VAT liabilities on a monthly basis.

Upon approval from DGT, a company is permitted to centralize its VAT reporting and thereby is allowed to exclude internal deliveries of taxable goods from VAT. In order to obtain such approval, several conditions must be met including centralization of sales administration, however, such company is also allowed whether to choose to centralize their VAT reporting without fulfilling other conditions if it files e-tax returns. Also, companies registered to Special Tax Office, Large Tax Office, and Medium Tax Office are required to centralize their VAT reporting.

III.3.7.5 Input-Output Mechanism

VAT liabilities are settled by an input-output mechanism. First, a vendor of taxable goods or a taxable service typically charges VAT to its buyer. From the vendor's perspective, it is regarded as an output tax. Second, the buyer has to pay VAT to the vendor as an input tax. In such input-output mechanism, both vendor and buyer must be registered as taxable entrepreneurs.

Input tax can be credited against output tax. A vendor isallowed to offset the output tax against its input tax on the acquisition of taxable goods or taxable services, and so is the buyer. If the amount of accumulated output tax (output tax derived from many transactions) for a particular month exceeds the amount of accumulated input tax for the same period, taxable entrepreneur has to settle the amount difference by the following month. On the contrary, if the amount of accumulated input tax for a particular month exceeds the amount of accumulated output tax, such taxable entrepreneur may ask for a refund at the end of tax year or else he could carry over excess amount oftax paid (input tax) for following months.

With regards to invoice used for the input-output mechanism, DGT has begun implementing the use of electronic VAT invoices (e-VAT invoice) for all registered entrepreneurs since 1 July 2016. It is regarded the samelegal invoice withpaper-based invoice and taxable entrepreneur shall use IDR currency and apply hisdigital signature.

III.3.7.6 VAT Refund

Refund application can be filled and submitted at the end of an accounting year. DGT then would determine on a refund application within 12 months by conducting a VAT audit. Relevant supporting documents for a VAT refund must be submitted to DGT within a month after the date of application. In addition, an early VAT refund is applicable to certain taxpayers regarded obedient.

III.3.8 Luxury-Goods Sales Tax (LST)

The VAT law also imposes LST on delivery of luxury goods by foreign manufacturers into Indonesia as well as on the importation of luxury goods by residents. Rates vary depending on the category of the goods (up to 200% rate) and such LST is imposed only once by multiplying the applicable rate by the sales/import price excluding VAT.

Similar to VAT, no LST is imposed on the export of luxury goods, hence, purchase of luxury goods cannot be credited against the collectable VAT when suchluxuries are subsequently sold. In broad terms, some of the main types of goods are subject to LST includes passenger vehicles, alcoholic beverages, certain food and non-alcoholic beverage products, household appliances and electronic goods, cosmetics, luxury homes and apartments, and so forth.

III.3.9 Stamp Duty

Under Law Number 13 of 1985, stamp duty is nominal and payable as a fixed amount of either IDR 6,000 or IDR 3,000 on certain documents. Examples of documents subject to stamp duty are as follows:

1. Letters of agreement and other letters (such as authorization letters, letters bestowing gifts, or declarations) which are prepared for the purpose of being used as evidence of act, fact, or condition of a civil nature.
2. Notary's deeds and their copies.
3. Deeds prepared by a designated land notary ("PejabatPembuatAkta Tanah").
4. All documents bearing a sum of money which:
   a. State the receipt of money;
   b. State the recording or deposit of money in a bank;
   c. Contain notification of a bank balance;
   d. Contain the acknowledgement of debt wholly or partly paid or compensated;
   e. Are in the form of valuable documents such as drafts, promissory notes, or acceptances;
   f. Are in the form of securities, in whatever name or form;
   g. Are in the form of cheque.
5. Documents to be used as instruments of evidence before a court:
   a. Ordinary letters or internal papers
   b. Paper originally exempt from stamp duty on the basis of their purpose of use, if they serve other aims or are used by other parties, and deviate from their original purpose.

The IDR 6,000 rate is applicable to (a), (b), (c), and (e). For (d), the rate is IDR 6,000 when the money value stated in the document is more than IDR 1 million, and IDR 3,000 when the value is between IDR 250,000 and Rp1 million. Values below IDR 250,000 are not subject to stamp duty. For cheque, the rate is IDR 3,000 regardless of the monetary value stated.

III.3.10 Land and Building Tax Other than Urban and Rural Sectors

Minister of Finance Regulation Number 131 of 2017 concerning Administration on Land and Building Tax on Mining Sectors for Petroleum, Natural Gas, and Geothermal regulates the payment procedure and its adjustment of terminology to provision of Geothermal Law. Moreover, Minister of Finance Regulation Number 81 of 2017 and Number 82 of 2017 regulate deduction of administration fines of land and building tax along with deduction/cancellation of tax assessment/collection and criteria for granting deduction of land and building tax respectively. As depicted on the following table, there were 10,179 objects registered on respective land and building tax.

Table 38: Object of Land and Building Tax

Sector	2014	2015	2016	2017	2018
Plantation	13,663	8,637	4,275	4,401	4,472
Forestry	569	562	647	683	701
Mining	4,252	4,803	4,760	5,095	4,502
Others	-	405	719	982	1,255
Total	**18,484**	**14,407**	**10,401**	**11,161**	**10,930**

Source: DGT 2018 Annual Report

III.3.11 Tax Assessment

Indonesian taxation relies on a self-assessment system under which taxpayers are trusted to calculate, pay, and report their own taxes by themselves in accordance with prevailing tax laws and regulations. However, the DGT may issue tax assessment letters to a particular taxpayer if it finds that, based on a tax audit or other information the taxpayer has not fully paid its tax liabilities. A tax assessment letter may also be issued by the DGT to a taxpayer who ignores a warning letter to file a tax return in a specified period. Failure to maintain books in accordance with the prescribed standards is another condition that may lead the DGT to perform an official tax assessment.

III.3.11.1 Notice of Tax Assessment

A notice of tax assessment pertains only to one specific tax for one particular tax period or year which includes:

1. Notice of Tax Collection (NTC) which is a form of a notice for the collection of tax and oradministrative penalties in the form of interest and or fines;
2. Notice of Tax Underpayment Assessment (NTUA) which specifies a principle amount of tax payable, amount of tax credit, a principle amount of underpayment tax payable, amount of administrative penalties, and total of tax due;
3. Notice of Additional Tax Underpayment Assessment (NATUA) which specifies an additional amount of tax payable over previously issued tax assessment;
4. Notice of Nil Tax Assessment (NNTA) which specifies the principle amount of tax payable is as much as the amount of tax credit, or, there is no tax payable and no tax credit;
5. Notice of Tax Overpayment Assessment (NTOA) which specifies an amount of tax overpayment as a result of the amount of tax credit is greater than the tax payable, or the tax paid should not have been payable.

III.3.12 Tax Audit

According to Article 29 Law of General Provisions and Tax Procedures, DGT is authorized to perform audit to assess tax compliance, in the form of risk-based audit and routine audit, and for other purposes with respect to the implementation of tax laws and regulations. Tax compliance audit is generated by 2 condition of cases. The first condition is mandatory requirement by tax law with regards to the taxpayer's rights and obligations, and the second condition is that DGT detects some risks or tax gaps from the business sector or specific tax payer as a result of either bottom-up risk analysis or top-down risk analysis.

III.3.12.1 Objectives of Tax Audit

In the framework of exercising administrative supervision, DGT shall undertake audit for the purpose of assessing tax compliance and for other purposes in respect of the implementation of the tax laws and regulations as structured below:

1. Audit for the purpose of assessing taxpayer's compliance:
   a. Overpayment tax return including those that have been granted preliminary tax returns;
   b. Loss-reported tax return;
   c. Overdue or not-submitted tax return (beyond the time period specified in the Letter of Reprimand) delivered;
   d. Performing a merger, consolidation, division, liquidation, dissolution, or having intention to leave Indonesia permanently;
   e. Tax return which meet the selection criteria based on the results of the analysis (risk-based selection) is regarded as non-compliant.
2. Audit for other purposes:
   a. To issueTIN ex-officio;
   b. To terminatea taxpayer's TIN;
   c. To confirm or revoke taxable person for VAT purposes;
   d. Taxpayer lodges objection;
   e. To collect material for determination of net deemed-profit;
   f. To verify data and/or information;
   g. To determine whether taxpayer is located at remote area;
   h. To designate one or more places where VAT is payable;
   i. Audit is in the framework of tax collection;
   j. To determine the commencement of production or extending the time period of loss compensation relating to granting tax incentives; and or
   k. To fulfill information request from treaty partner country with respect to the implementation of exchange of information of the tax treaty.

III.3.12.2 Closing-Conference

In the final stage of tax audit, tax auditors will provide the taxpayer a written notification of the findings containing a proposed tax audit corrections. Then, taxpayer shall respond within 7 days – in some cases, as auditor's discretion, time limit can be extended up to 21 days. Within 3 weeks, a final discussion about the tax audit findings (closing-conference) will be held between tax auditors and the taxpayer.

A closing-conference serves as the last opportunity for the taxpayer to reassert its position with regards to the tax audit corrections by presenting relevant supporting documents. Tax auditors may change some of proposed corrections in light of the taxpayer's response to audit findings notification and the closing-conference discussion. The results of such final discussion are then summarized into a closing-conference document which states agreement or disagreement from the taxpayer. By the end of the closing conference, tax auditors and the taxpayer have to sign the closing-conference document.

III.3.13 Tax Investigation

Tax investigation is the ultimate tax enforcement method conducted when other approaches e.g. reminder, counseling, and audit are considered to be ineffective. It can only be conducted by Certified Tax Officers with technical support from the Police. In details, tax crime is regulated on article no. 38, 39, and 39A of the General Law.

Generally, tax crime can be divided into 2 categories:

1. Pure tax crime case. It is mostly related to invoice based on fictitious transaction and other fictitious tax documents. A clear proof of crime usually detected within tax administration. For such cases, tax investigation takes the first place to conduct a covered preliminary-investigation;
2. Escalated tax fraud case. It is the kind of fraud conducted by evading tax amount or tax obligation. Such crime requires tax investigation to be preceded by other enforcements, yet in a preliminary-investigation, tax payer can avoid investigation by declaring a self-correction or an adjustment related to data or information in accordance with tax regulations.

As stated in the law, there are four major modus operandi of tax crime, as follows:

1. By issuing or using tax invoice which is not based on real transactions;
2. By withholding tax, but do not pay such withheld amount;
3. By submitting incorrect or incomplete information Tax Return;
4. Not submitting the Tax Return.

III.3.14 Tax Dispute Settlement

Judicial process of tax administration can be divided into 2 main categories: administration of impartial justice in DGT and Partial Justice in Tax Court and Supreme Court as shown in the following table. Impartial Justice in DGT covers Objection, Correction, Deduction, Annulment, and Cancellation of Tax Assessment, while Partial Justice in Tax Court and Supreme Court covers Appeal, Lawsuit and Review.

III.3.14.1 Impartial Justice in DGT

In the implementation of the provisions of the tax law and regulations, there are several legal measures which could be taken by taxpayers if they disagree with the tax assessment, namely:

1. Tax objection over NTUA, NATUA, NNTA, and NTOA, Notice of Land and Building Tax Payable, Notice of Land and Building Tax Assessment, Notice of Acquisition Duty of Right on Land and Building Assessment Underpayment, Notice of Additional Acquisition Duty of Right on Land and Building Assessment Underpayment, Notice of Acquisition Duty of Right on Land and Building Assessment Overpayment, Notice of Nil Acquisition Duty of Right on Land and Building Assessment, and other withholding tax by third parties;

2. Correction of notice of tax assessment, Notice of Tax Collection (NTC), and decrees for any error in writing, miscalculations, and mistake in the application of certain provisions of tax law and regulations;
3. Deduction or annulment of administrative penalties either due to the negligence of taxpayers or not;
4. Deduction or cancellation of incorrect tax assessment notice;
5. Deduction or cancellation of incorrect NTC;
6. Deduction of administrative penalty for Land and Building Tax;
7. Deduction of payable for Land and Building Tax and Duty of Rights on Land and Building Acquisition; and
8. Cancellation of tax audit result or Notice of Tax Assessment resulted from audit that conducted without notification of tax audit finding or without closing-conference with taxpayers.

III.3.14.2 Partial Justice in Tax Court and Supreme

III.3.14.2.1 Appeal and Lawsuit

In relation to tax disputes in the partial administrative court process, taxpayers can only file appeals and lawsuit to Tax Court. Appeals is submitted based on the Decree of Objection, while the lawsuit is submitted by taxpayers against:

1. Execution of Distress Warrant, Notice of Seizure, or Auction Announcement;
2. Decision on prevention in framework of tax collection;
3. Decision pertaining to the execution of tax;
4. Decision, other than those stipulated in Article 25 par. (1) And Article 26 Law of GeneralProvisions and Tax Procedures; or
5. Issuance of notice of tax assessment or decision on tax objection that is not in accordance with the procedures set out in tax law provisions.

III.3.14.2.2 Judicial Review

Both taxpayers and DGT have the rights to take extraordinary legal attempts to the Supreme Court, known as Review. Review can be submitted within a maximum period of three months since a decision has been delivered by a Tax Court. Further, Review is filed by DGT to the Supreme Court in form of Memory of Review. Upon the Review filed by taxpayers to theSupreme Court, DGT shall be obliged to respond in the form of Counter Memory of Review.

Appeal decisions or claim from Tax Court could be filed for Review by taxpayers and DGT for several reasons, namely:

1. The Tax Court verdicts are based on falsity or deceit of the counterparty which is revealed after the cases have been ruled or based on evidence which then declared as false by the judges;
2. There is new and decisive written evidence, which if presented at the trial in the Tax Court may result in different verdict;
3. Some issues, that were not charged or more than what have been charged, have been granted except that issues have been terminated under the Article 80 paragraph (1) letter b and c of Tax Court Law;
4. Concerning a part of the lawsuit which is yet to be decided without being given duly consideration; and
5. There is a verdict which clearly is not in accordance with the provisions of prevailing law and regulations.

III.3.14.3 Other Dispute Settlements and Granting of Legal Assistance

III.3.14.3.1 Case Handling

Case handled by DGT includes lawsuit, bankruptcy, state property disputes, state administrative lawsuit, and those related to information dispute resolution to the Public Information Commission. In general, types of lawsuit filed by taxpayers are:

1. Investigation, preliminary investigation, and tax crime investigation, with several case examples, namely:
   a. Audit period exceeds the standard audit period stated in the provisions of tax law and regulations;
   b. Understanding of tax crime as ultimumremedium, in which taxpayers believe that audit must be conducted prior to preliminary investigation, and correspondingly, investigations must be preceded by a preliminary investigation;
   c. taxpayers raise the issues on tax stipulation expiration (Article 13 Law onGeneral Provisions and Tax Procedures) and prosecution of tax crimes (Article 40 Law on General Provisions and Tax Procedures), in which taxpayers consider that if an annual tax return is not disputed for five years, then it is regarded legal, thus consequently cannot be audited or investigated;
   d. Related to the granting of power of attorney by taxpayers to tax consultants to represent them in investigation process, in which the tax consultants consider themselves could properly represent the taxpayers without obtaining tax consultant permit;
   e. Pre-trial request by taxpayers who are under investigation or suspected of committing tax crime.
2. Tax debt collection related to confiscation, hostage-taking/*gijzeling*, and bankruptcy, with several cases as follows:
   a. Tax offices are late in collecting tax arrears, for example, being late in carrying out auction for confiscated assets;
   b. Schemes where company management structure are strategically changed in an attempt to escape responsibility as tax bearers;
   c. Wrongful confiscation of taxpayers' assets by tax offices;
   d. Resistance from Taxpayers subject to hostile-taking/gijzeling by submitting pretrial requests;
   e. Taxpayers use bankruptcy scheme as an effort to avoid the obligation to pay tax debt. This is made possible due to different opinion between DGT, curator, and judge in determining preferential creditor.
3. Dispute on state properties, for example:
   a. Procurement process;
   b. Documentation of ownership; and
   c. Insufficient maintenance.

III.3.14.3.2 Legal Assistance

DGT actively provides legal assistance for its employees, retired employees, or former employees who are summoned by law enforcement officials as witnesses and experts related to their duties as DGT employees. Additionally, DGT also monitors lawsuit process in which its employees, retired employees, or former employees is a suspect. In general, DGT provide legal assistance in 2018 in its capacity as a witness, both in the investigation and trial process.

III.3.14.3.3 Legal Opinion

DGT provides legal opinion to tax offices classified as follows:
1. Implementation of Tax Amnesty Law;
2. Tax collection and tax crimes investigation;
3. Preparation of memorandum of understanding, contracts and cooperation agreements between DGT and other institutions;
4. Legislative drafting of Law, Government Regulation in Lieu of Law, Government Regulation, Minister of Finance Regulation, and Director General of Taxes Regulation;

5. Mitigation of legal risk for tasks implementation, particularly related to strategic programs such as the development of DGT information technology systems, urgent regulations preparation, plans for *gijzeling* and preliminary investigation, as well as procurement of goods and services.

III.3.14.3.4 Judicial Review

Overall, the handling of judicial review conducted by DGT in 2018 is explained in following table.

Table 39: List of Judicial Review Cases handled by DGT, 2018

Case Number	Subject Matter of Request	Status
Constitutional Court		
63/PUU-XV/2017 Dated September 5, 2017	Judicial review of Article 32 paragraph (3) letter a of the Law of General Provisions and Tax Procedures	Partially Granted
102/PUU-XV/2017 Dated December 22, 2017	Judicial review of Article 1, Article 2, and Article 8 of Law Number 9 of 2017 concerning Access to Financial Information for Taxation Purposes	Rejected completely (Won)
3/PUU-XVI/2018 Dated January 3, 2018	Judicial review of Article 4 paragraph (1) and paragraph (2) of the Law of Land and Building Tax	Rejected completely (Won)
10/PUU-XVI/2018 Dated February 6, 2018	Judicial review of Article 9 paragraph (2), Article 13 paragraph (1), Article 13 paragraph (3) letter c of the Law of General Provisions and Tax Procedures, and Article 9 paragraph (9) of the Law of value Added Tax	Rejected completely (Won)
19/PUU-XVI/2018 Dated March 5, 2018	Judicial review of Article 6 paragraph (1) and paragraph (2) of the Law of Land and Building Tax	Rejected completely (Won)
Supreme Court		
05 P/HUM/2018 Dated January 3, 2018	Judicial review of Regulation of the Minister of Finance No. 252/PMK.011/2012 concerning Value Added Tax (VAT) of Liquefied Natural Gas (LNG) on natural gas which is included in the types of goods that are not subject to VAT	Grant the entire request (Lose)
32 P/HUM/2018 Dated May 23, 2018	Application for the Rights of Judicial Review of Regulation of the Minister of Finance No. 116/PMK.010/2017 concerning Staple Goods Not Subject to VAT	Process (Waiting for Decision)

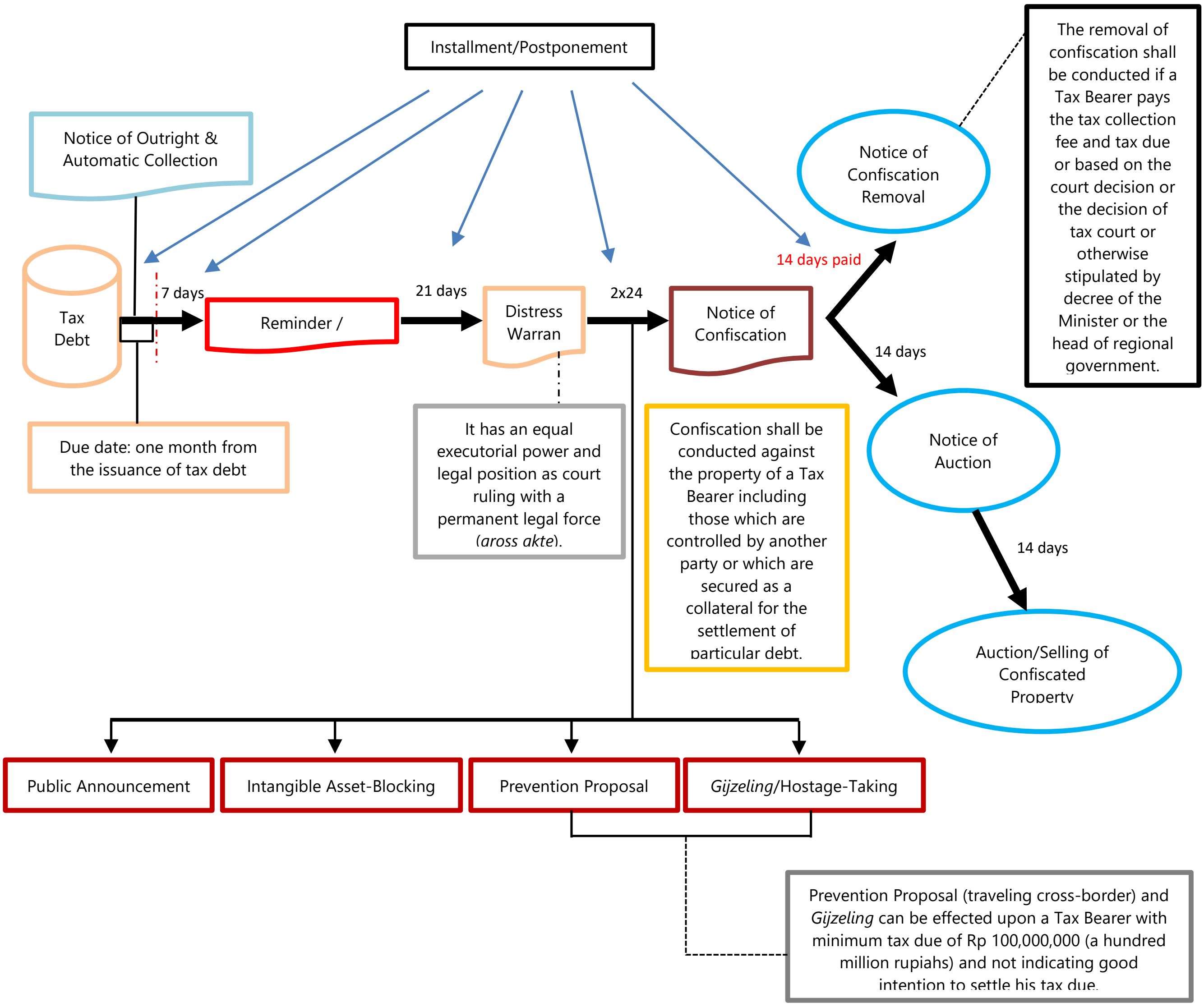
Source: DGT Annual Report, 2018

III.3.15 Tax Collection

Law Number 19 of 2000 concerning Tax Collection With Distress Warrants defines Tax Collection as a series of measures intended to make a tax bearer settle his/its tax debts and tax collection fees by serving him/it a reminder/a warning, implementing outright and automatic collection, notifying distress warrants, proposing prevention, implementing confiscation, implementing hostage-taking and selling confiscated property. For more detailed collection enforcement mechanism, see figure 3 below.

A distress warrant shall have at its heading the words of "FOR THE SAKE OF JUSTICE ON THE BASIS OF GOD THE ALMIGHTY" and shall have an equal executorial power and legal position as a court ruling with a permanent legal force. Thus, tax collection with distress warrants shall be performed without assistance from any court ruling, even more, it could not be effected by any appeal. However, a lawsuit could be regarded a legal effort only against the implementation of tax collection procedure and ownership of property as regulated in the prevailing laws.

Figure 3: Tax Collection Enforcement



The basis for tax collection which contribute to the formation of tax debt, among others are: NTC, NTUA, NATUA, Decision on Objection (DO), Notice of Tax Correction (NTCR), Decision on Appeal (DA),and Decision on Review (DR) as well. In particular, NTCR is notice for correcting errors in writing, calculation, and or errors in the application of particular provisions of the tax laws found in a notice of tax assessment, NTC, DO, Decision on Deduction or Annulment of Administrative Penalties, Decision on Deduction or Cancellation of Inaccurate Tax Assessment, or Decision on Pre-audit Refund of Tax Overpayment, tax assessment notices issued by the Directorate General of Customs and Excise, as well as tax assessment notices issued by Regional Taxes authorities (including official assessment notices of Land and Building for Urban and Rural Area Tax which previously issued by DGT).

Thus, there are two key unique issuesregarding Law Number 19 of 2000. First, Tax Collection Law applies to both Central and Regional collection of taxes. In the meantime, the implementation of the law is performed by Central Taxes Authorities i.e. DGT and Directorate General of Customs and Excise – the implementation by Regional Taxes authorities is undergoing mostly on regional regulations enactment phase.Second, the executor who is assigned to perform tax collection measures by such Law is Tax Bailiff who acts as prosecutor of the Law. All Tax Bailiff’s tasks i.e. implementing a letter of instruction for outright and automatic collection, notifying a distress warrant, implementing the confiscation of the property of a tax bearer on the basis of a letter of instruction for the implementation of confiscation, and implementing hostage-taking on the basis of a letter of instruction for hostage takingis supported by the authorization to enter and examine all rooms including opening cupboards, drawers and other places in order to find the objects of confiscation at a business place of the tax bearer and conduct confiscation at his domicile or at his residence, or at other places which may alleged as places where the objects of confiscation are kept.

III.3.16 International Taxation

III.3.16.1 Tax Treaties

Tax treaties provide tax benefits in the form of withholding tax exemptions for service fees as well as in the form of reduced withholding tax rates on dividends, interest, royalties, and branch profits received by resident of a country with which Indonesia signed a tax treaty. Such tax exemption on the service fees is typically granted only if the foreign party earning the income from Indonesia does not have any PE in Indonesia. Hence, to claim the reduced rates, foreign party shall present its certificate of residence (CoR) to DGT through itsrelated Indonesian party. Failure submittingsuch document, itis not entitled to tax benefit therein tax is withheld at a rate of 20%.

Regarding interest, dividends, and royalties, it is the beneficial owner acknowledged as the party entitled to the tax treaty benefits.In order to benefit from tax treaties, such following criteria should be met:

1. An individual who does not receive income as an agent or nominee;
2. An institution that is explicitly named in the tax treaty or one that has been agreed by the Competent Authority in Indonesia and its treaty partner;
3. An offshore company that earns income through a custodian from share or bond transactions in Indonesian Stock Exchange (except interest and dividends), that is not an agent or nominee.
4. A company whose shares are listed on the stock exchange and traded regularly;
5. A bank; or
6. Any other company that meets specific requirements:
   a. The company is established in the tax treaty partner country and the way transactionsconductedare not merely to enjoy tax treaty benefits – business activities are managed by the company’s own management thatpossesses sufficient authority to carry out transactions;
   b. The company has employee(s);
   c. The company has activities or an active business;
   d. Income derived from Indonesia is taxable in the recipient’s country;
   e. The company does not allocate more than 50% of its total income to fulfill its obligationssuch as interest, royalty, or other payments to other parties.

The tax treaty (P3B) between the Government of Indonesia and the governments of partner countries is guided by the Organization for Economic Co-operation and Development of the Tax Convention on Income and on Capital (OECD Model) and the United Nations Double Tax Convention Model between Developed and Developing Countries (UN Model) while still taking into account the interests of Indonesia's domestic taxation.

Throughout 2018, the Government of Indonesia has ratified two new P3Bs, with Government of the Republic of Belarus in May 9, 2018 by Presidential Regulation Number 6 of 2018 and Government of the Republic of Serbia in December 13, 2018 by Presidential Regulation Number 75 of 2018. In addition, the withholding tax rates applicable under tax treaties are summarized as below.

Table 40: Indonesia Tax Treaty Networks and Its Withholding Tax Rates

No.	Country	Dividends		Interest	Royalties	Branch Profit Tax
		Portfolio	Participatory			
1	Algeria (1995)	15%	15%	15%	15%	10%
2	Armenia (2005)	15%	10%	10%	10%	10%
3	Australia (1992)	15%	15%	10%	15%; 10%	15%
4	Austria (1986)	15%	10%	10%	10%	12%
5	Bangladesh (2003)	15%	10%	10%	10%	10%
6	Belarus (2013)	10%	10%	10%	10%	18%
7	Belgium (1997)	15%	10%	10%	10%	10%
8	Brunei (2000)	15%	15%	15%	15%	10%
9	Bulgaria (1991)	15%	15%	10%	10%	15%
10	Canada (1979)	15%	10%	10%	10%	15%
11	China (2001)	10%	10%	10%	10%	10%
12	Croatia (2002)	10%	10%	10%	10%	10%
13	Czech Republic (1994)	15%	10%	13%	13%	13%
14	Denmark (1985)	20%	10%	10%	15%	15%
15	Egypt (1998)	15%	15%	15%	15%	15%
16	Finland (1987)	15%	10%	10%	15%; 10%	15%
17	France (1979)	15%	10%	15%; 10%	10%	10%
18	Germany (1990)	15%	10%	10%	15%; 10%; 7.5%	10%
19	Hong Kong (2010)	10%	5%	10%	5%	5%
20	Hungary (1989)	15%	15%	15%	15%	N/A
21	India (2012)	10%	10%	10%	10%	10%
22	Iran (2004)	7%	7%	10%	12%	7%
23	Italy (1990)	15%	10%	10%	15%; 10%	12%
24	Japan (1982)	15%	10%	10%	10%	10%
25	Jordan (1996)	10%	10%	10%	10%	N/A
26	Kuwait (1997)	10%	10%	5%	20%	10%
27	Laos (2011)	15%	10%	10%	10%	10%
28	Luxembourg	15%	10%	10%	12.5%; 10%	10%
29	Malaysia (1991)	10%	10%	10%	10%	12.5%
30	Mexico (2002)	10%	10%	10%	10%	10%
31	Mongolia (1996)	10%	10%	10%	10%	10%
32	Morocco (2008)	10%	10%	10%	10%	10%
33	Netherlands (2002)	15%; 10%	5%	10%	10%	10%
34	New Zealand (1987)	15%	15%	10%	15%	N/A
35	North Korea (2002)	10%	10%	10%	10%	10%
36	Norway (1988)	15%	15%	10%	15%; 10%	15%
37	Pakistan (1990)	15%	10%	15%	15%	10%
38	Papua New Guinea (2010)	15%	15%	10%	10%	15%
39	Philippines (1993)	20%	15%	15%	15%	20%; 15%
40	Poland (1992)	15%	10%	10%	15%	10%
41	Portugal (2003)	10%	10%	10%	10%	10%
42	Qatar (2006)	10%	10%	10%	5%	10%
43	Romania (1996)	15%	13%	13%	15%;12.5%	13%
44	Russia (1999)	15%	15%	15%	15%	13%
45	Saudi Arabia (1991)[1]	N/A	N/A	N/A	N/A	N/A
46	Serbia (2011)	15%	15%	10%	15%	15%
47	Seychelles (1999)	10%	10%	10%	10%	20%
48	Singapore (1990)	15%	10%	10%	15%	15%
49	Slovakia (2000)	10%	10%	10%	15%; 10%	10%
50	South Africa (1997)	15%	10%	10%	10%	10%
51	South Korea (1988)	15%	10%	10%	15%	10%
52	Spain (1995)	15%	10%	10%	10%	10%
53	Sri Lanka (1993)	15%	15%	15%	15%	14%
54	Sudan (1998)	10%	10%	15%	10%	10%
55	Suriname (2003)	15%	15%	15%	15%	15%
56	Sweden (1989)	15%	10%	10%	15%; 10%	15%
57	Switzerland (1988)	15%	10%	10%	10%	10%
58	Syria (1997)	10%	10%	10%	20%; 15%	10%
59	Taiwan (1995)	10%	10%	10%	10%	5%
60	Thailand (2001)	20%	15%	15%	15%	10%
61	Tunisia (1992)	12%	12%	12%	15%	12%
62	Turkey (1997)	15%	10%	10%	10%	10%
63	Ukraine (1996)	15%	10%	10%	10%	10%
64	United Arab Emirate (1995)	10%	10%	5%	5%	5%
65	United Kingdom (1993)	15%	10%	10%	15%; 10%	10%
66	United States (1988)	15%	10%	10%	10%	10%
67	Uzbekistan (1996)	10%	10%	10%	10%	10%
68	Venezuela (1997)	15%	10%	10%	20%; 10%	10%
69	Vietnam (1997)	15%	15%	15%	15%	10%

Note: [1] Limited to both countries airline companies

III.3.16.2 Thin Capitalization

Based on Minister of Finance Regulation number 169 of 2015 (PMK-169), the ratio of debt to equity (DER) has been set to 4:1. Any borrowing cost on debt which exceeds this ratio will not be tax-deductible for corporate income tax purpose. The ratio is used to limit the amount of deductible interest expense related to income tax calculation in order to meet the arm's length principle.

Some sectors are exempted from this regulation, such as banks, financial institutions, insurance and re-insurance companies, mining, oil and gas enterprises that are bound by production sharing contract (PSC), Contract of Work or Coal Contract of Work which itself governs the DER. In case a contract does not mention any provision for the DER or the contract has come to its expiry, PMK- 169 will prevail and those exempted companies are subject to final income tax and infrastructure companies.

The implementation of PMK-169 is clarified under Director General of Taxes Regulation Number 25 of 2017 (PER-25) enacted on 28 November 2017. Not only does it provide details on thin capitalization implementation but also it includes the obligation to report DER calculation and private loan details as part of a corporate income tax return to DGT.

III.3.16.3 Controlled Foreign Company (CFC) Rules

Under Minister of Finance Regulation Number 107 of 2017 which revoked PMK-256/2008 and partially Minister of Finance Decree Number 164 of 2002 concerning Foreign Tax Credit (FTC) for dividend paid by a CFC, a dividend is deemed to be derived from a CFC located in certain countries ifone or more Indonesian resident taxpayers hold at least 50% of the paid-up capital in such foreign company. Such measure is established in order to curb tax avoidance by resident taxpayers through offshore investments. This condition applies if onlya CFC does not trade its share on the stock exchange.

In case there is no dividend derived from offshore company, the resident taxpayer must calculate and report the deemed dividend on its corporate tax return. Otherwise, the Ministry of Finance would do so – the dividend is deemed to be derived either within 4 months following the deadline for filling the tax return in the offshore country, or seven months after the offshore company's tax year ends.

In brief, key aspects to such new regime encompasses detail definition of CFC which captures not only a non-listed foreign entity but also captures indirect CFC, introduction of "deemed dividend" concept, taxable dividend calculation, CFC income exemption, carried forward "deemed dividend", unrecognized CFC's loss, no distinction either on CFC's active or passive income, and FTC. Particularly, FTC limitation is based on under following limits whichever is the lowest:

1. The effective tax treaty rate that is payable;
2. Foreign income tax;
3. An amount which is calculated based on the proportion of dividend received from a direct CFC and the deemed dividend multiplied by the income tax due on such deemed dividend.

In order to claim the FTC, a taxpayer shall submit documents among others are financial statements, copy of corporate income tax return, calculation of after-tax profit for past five years, and a tax payment slip on actual dividend paid. Nevertheless, in case dividends are derived from several countries, a per-country limitation applies.

III.3.16.4 Transfer Pricing

Detailed transfer pricing guidelines has been issued which in principle is in-line with The Organization for Economic Co-operation and Development (OECD) guidelines i.e. Director General of Taxes Regulation number 43 of 2010 and number 32 of 2011 concerning The Application of The Arm's Length Principle within Related Party Transactions. Subsequently, The Minister of Finance Regulation number 213 of 2016 has been enacted for the implementation of the three-tiered transfer pricing documentation approach regarding master file, local file, and country-by-country report.

Based on the above-mentioned Minister of Finance Regulation, any taxpayer having related-party transactions shall prepare the master file and the local file when it satisfies several conditions, among others are, having preceding tax year gross revenue exceeding IDR 50 billion, having preceding tax year tangible transactions exceeding IDR 20 billion, having preceding tax year intangible transactions exceeding IDR 5 billion, and such related party transactions is conducted with the affiliated party located in lower tax rate jurisdiction at any amount.

III.3.16.5 Base Erosion and Profit Shifting (BEPS) Measures

The Base Erosion and Profit Shifting (BEPS) is general tax avoidance strategy conducted by multinational companies by exploiting taxation loopholes in various countries. BEPS causes reduction in the tax base of a country which is caused by a shift in profits to countries that have lower tax rates or there is no tax at all so the total tax which is paid as a whole is very small or not even taxed at all (double non-taxation).

The tax authority of the countries in the world participated in The BEPS Project which initiated by the G20 and OECD in order minimize the impact of BEPS. The BEPS Project published 15 Action Plans containing instruments domestic and international for tax authority to overcome BEPS. Indonesia has officially become an associate member of Inclusive Framework on BEPS and declared ready to apply the four minimum standards, namely:

a. Action 5: Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance;
b. Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances;
c. Action 13: Transfer Pricing Documentation and Country-by-Country Reporting (CbCR); and
d. Action 14: Making Dispute Resolution Mechanisms More Effective.

III.3.16.6 Mutual Agreement Procedure (MAP)

Mutual Agreement Procedure (MAP) is an international tax dispute settlement procedure as stipulated in the provisions of the Avoidance of Double Taxation (P3B) or income tax treaty to resolve issues relating to the implementation of tax treaty and/or in connection with the occurrence of multiple taxation through negotiations between two tax authorities.

MAP requests to DGT can be submitted by Indonesian domestic taxpayers or foreign taxpayers through authorized officials of P3B partners. The MAP request is filed in the event that there is discrimination in the area of taxation, tax treatment that is not in accordance with tax treaty, and actions that result in the imposition of double taxation. The implementation of the MAP can be carried out simultaneously (in parallel) with efforts to resolve tax disputes through objections and appeals. However, the MAP process will be terminated if an appeal hearing has been sufficient.

As a member of the G20 and BEPS Associate, Indonesia committed to implementing minimum standards of BEPS action plans, one of which is BEPS Action 14: Making Dispute Resolution and Mechanisms More Effective. BEPS Action 14 aims to ensure the implementation of international tax dispute handling can be done quickly, effectively, and efficiently. To ensure that the implementation of MAP complies with the BEPS Action 14 minimum standards, the OECD Forum on Tax Administration of MAP (FTA-MAP) conducted a peer review of Indonesia and 79 other countries which took place until 2019.

Based on DGT Annual Report 2018 from the Directorate of International Taxa data, the handling of MAP cases as of December 31, 2018 are 130 submitted cases, 70 completed cases, and 60 remained cases. The Distribution of MAP Cases in process by Region as of December 31, 2018 are 60 cases which cover America (13 cases), Australia (2 cases), Asia (29 cases), and Europe (16 cases).

III.3.16.7 Advance Pricing Agreement (APA)

Transfer Price Agreement (Advance Pricing Agreement/APA) is a written agreement between the Director General of Taxes and the Taxpayer or between the Director General of Taxes and authorized officials of tax treaty (P3B) partners to determine the fair price or reasonable profit in advance and/or agree on the criteria in determining transfer prices Taxpayer's transactions with parties who have a special relationship.

There are two types of APA, namely unilateral APA and bilateral APA. A unilateral APA is an agreement made between the DGT and the Taxpayer without involving the state tax authority/partner jurisdiction. Whereas bilateral APA is an agreement between DGT and the state tax authorities/partner jurisdictions related to Taxpayer affiliate transactions in two countries/jurisdictions. Bilateral APA is carried out through negotiations with the state tax authorities/partner jurisdictions within the MAP framework. Bilateral APA is valid for a maximum of four years, while unilateral APA is valid for a maximum of three years after APA approval. Taxpayers can submit APA applications within six months before the start of the tax year that will be covered by APA.

A number of APA benefits for the DGT and the Taxpayer, namely:

a. provide legal certainty for taxpayers;
b. eliminate double taxation;
c. prevent transfer pricing disputes, because the affiliated transactions covered by APA will not be corrected in the examination in the future as long as the Taxpayer carries out all the provisions in APA;
d. protect the tax base in accordance with taxation rights owned by each country so that the tax base and revenue can be measured and maintained during the APA period;
e. WHAT saves taxpayer or DGT resources related to audits; and
f. enhance the confidence of the world community in Indonesia's commitment to the prevention and resolution of transfer pricing disputes, which in turn will increase investment attractiveness.

Based on DGT Annual Report 2018 from the Directorate of International Tax data, the handling of Unilateral APA cases as of December 31, 2018 are 17 submitted cases, 12 completed cases, and 5 remained cases. The handling of Bilateral APA cases as of December 31, 2018 are 37 submitted cases, 9 completed cases, and 28 remained cases. The Distribution of Bilateral cases in process by Region as of December 31, 2018 are 28 cases which cover America (3 cases), Australia (1 cases), Asia (16 cases), and Europe (8 cases).

III.3.16.8 Exchange of Information (EOI)

Along with the increasingly widespread cross-border financial transactions carried out by taxpayers, cooperation between tax authority is increasingly needed in order to prevent and combat the practice of tax evasion and embezzlement that may occur in these various transactions. One of the cooperation instruments that DGT continues to promote is the exchange of taxation information or what is known as the Exchange of Information (EoI).

All information exchange cooperation in 2018 can be carried out effectively thanks to the extensive scope of Indonesia's international master agreement for EoI, which consists of tax treaty (P3B) with 67 partner countries/jurisdictions; Tax Information Exchange Agreement (TIEA) with 4 jurisdictions, namely Guernsey, Jersey, Isle of Man, and Bermuda; and Convention on Mutual Administrative Assistance in Tax Matters (MAC) with 125 countries/jurisdictions of other signatories, thus Indonesia can also collaborate on EoI with signatory countries/jurisdictions that have ratified the MAC.

During 2018, Indonesia sent and received 248 EoIs both requests from Indonesia to partner jurisdictions (outbound), and vice versa (inbound) that consist of 156 EOI on requests, 82 Spontaneous EOIs, and 10 Automatic EoI for Withholding Taxes. In 2018, Indonesia puts its first year implementation for Automatic EoI for CbCR activity where Indonesia received country reports from 33 countries/jurisdictions and sent reports per country to 14 countries/jurisdictions, and Automatic EoI for Financial Account lnformaiton (AEoI) based on the Common Reporting Standard (CRS) activity where Indonesia received information of Indonesian taxpayer finances from 69 partner countries/jurisdictions and send financial information on foreign tax subjects to 54 partner countries/jurisdictions.

In addition, there are also important achievements in 2018 related to international agreements for the benefit of EoI, namely the signing of the Bilateral Competent Authority Agreement for the Exchange of Country-by-Country Reports (BCAA on CbCR) between Indonesia and the United States. With this signing, Indonesia and the United States can exchange Reports Per Country periodically as a way to reduce the risk of scouring the tax base and transferring profits (BEPS).

In order to ensure the implementation of EoI in each country is consistent with international standards, an assessment has been carried out by international organizations, with Second Round Review on EoI on Request and Peer Review of the Implementation of the Action 5 Transparency Framework.

III.3.17 Tax Incentives

The meaning and purposes of granting tax incentives are primarily to promote the direct investment in Indonesia either foreign investment or domestic investment in certain business sectors or certain areas which have the highest national priority covering the possibility of agreements with another country or countries in the field of trade, investment and other areas as also mentioned earlier on BEPS Action Plan 5. Moreover, DGT has set one of its performance target 2018 to arrange a selective tax incentive provision to support competitiveness of national industries.

III.3.17.1 Corporate Tax Benefit and Tax Allowances

Tax Allowance is in the form of income tax facilities for investors who invest their capital in certain business fields and/or certain regions. Both of these tax incentives are expected to be one of the factors that can encourage investors to invest their capital in Indonesia, which is one of the emerging countries.

Corporate taxpayers investing in certain approved industry sectors (stipulated by the government and/or geographical areas may benefit form income tax benefit in the form of:

1. An additional reduction in net income up to 30% of the amount invested in tangible assets allocated for six years;
2. Accelerated depreciation;
3. Extension of loss carry forward for up to 10 years; and
4. A reduced 10% withholding tax rate on dividend paid to non-resident.

III.3.17.2 Tax Holiday

It is intended to new domestic/foreign investment in specific pioneer industries. Such regime grants beneficial treatment to projects in high priority sectors such re upstream metals, crude oil refining and infrastructure, basic organic chemicals, industrial machinery, agriculture, forestry and fishery-based processing, telecommunication, information, communication, and economic infrastructure other than government cooperation scheme i.e. a corporate income tax reduction from 10% to 100% for the minimum investment of IDR 1 trillion and a corporate tax reduction up to 50% for taxpayers in telecommunication, information, and communication sectors with a minimum investment value IDR 500 billion at least yet not more than IDR 1 trillion. Further, the period of tax holiday normally lasts from 5 years to 15 years, however, extension up to 20 years shall apply depending on the competitiveness and strategic value of the industry – depends on discretion of The Ministry of Finance.

III.3.17.3 Upstream Oil and Gas Business Activities

In order to increase national oil and gas reserve, to promote investment climate, and to provide legal certainty for the business, Government Regulation Number 27 of 2017 regulates tax incentive for upstream oil and gas business activities, among others are:

1. Exemption from import duty, VAT/LST, Article 22 Income Tax of import, and 100% deduction on Land and Building Tax during exploration and exploitation phase;
2. Exemption from income tax and VAT for cost-sharing charges and indirect expenditure of head office cost allocation;
3. Easing of non-cost recoverable into cost recoverable e.g. environment and local community cost during exploitation phase, employee income tax paid as income tax incentive, and interest recovery as incentive cost.

In addition, to enhance investment, Government Regulation Number 53 of 2017 targeted oil and gas upstream business activities with “gross split” PSC without mechanism for operating cost recovery.

Under such PSC regime, taxpayer can benefit from following tax incentives:

1. Exemption from import duty, VAT/LST, Article 22 Income Tax of import, and 100% deduction on Land and Building Tax during exploration and exploitation phase;
2. Exemption for VAT for cost-sharing charges; and
3. Fiscal loss compensation starts from subsequent tax year up to ten years.

IV. Country Specific Fiscal Issues

IV.1 Fiscal Incentives to Promote Economic Growth

In 2018, the Government implemented various fiscal policies designed to boost the general welfare of the population, improve the ease of doing business and increase investment. This included the provision of tax incentives. The provision of tax incentives constitutes state expenditure that is not given in the form of money, but via a partial reduction in tax obligations, or an exemption from tax obligations. Tax incentives have already helped the economy to grow at a faster pace. Tax spending is estimated to have contributed 1% of GDP in recent years, primarily via tax holidays and tax allowances. Improvements made in 2018 to fiscal incentives have already had a positive impact on the economy.

Tax holidays and tax allowances have been in place in Indonesia for some time. Tax holidays were first awarded in 1967, although the regulations continued to change up until 2018. In 2018, the Government issued a regulation on tax holidays that expanded the definition of pioneer industries to encompass more industries, and provided more attractive incentives. For tax allowances, the Government has made regulatory changes on several occasions since the inception of its policy in 1983. Most recently, in 2016, Indonesia put in place four types of tax allowance related to income tax.

The Government's tax spending is significant. In 2018, the Government issued tax spending reports for the first time. These reports contain a summary of the number of tax incentives given during 2016 and 2017. The value of tax spending rose to IDR 154.7 trillion in 2017 from IDR 143.6 trillion in 2016. Tax spending is responsible for 1.2% of GDP in 2017, up from 1.1% in 2016. The significance of this can be seen when compared to the contribution of government spending on goods, which came to 2.2% of GDP in 2017 and 2.1% in 2016. This significance is also clearly seen when compared to government capital expenditure – 1.5% of GDP in 2017 and 1.4% in 2016.

Tax spending mostly went towards tax allowances and incentives on VAT and sales tax on luxury goods, with the financial services sector receiving the largest amount of incentives. Government spending on VAT-related incentives include exemptions for small businesses below IDR4.8 billion and a reduction in the base for the luxury goods sales tax calculation for low cost green cars. The financial services sector obtained the most tax allowances, in relation to the types of services excluded from tax payments. Meanwhile, spending on tax holidays is categorized as multi-sector, because it benefits many sectors.

Households are the biggest recipients of tax incentives. Indeed, given the fact that the largest chunk of tax spending is VAT-related, then households as the last consumer paying VAT receive the greatest benefits from the Government's tax incentives. The majority of tax allowances are given in the form of tax exemptions on goods and services and are intended to boost purchasing power. Such goods and services relate to basic needs, public transport, education and health. As such, the main purpose of providing tax incentives is to increase the general welfare of the population.

Tax incentives provided in the form of tax holidays and tax allowances are also intended to attract investment. To this end, the Government has continued to encourage foreign investment through the implementation of fiscal incentive schemes. In April 2018, the Government changed the procedures and criteria by which investors may obtain tax holidays. This was necessary because, in 2017, only five companies were receiving such fiscal incentives. As a result of the rule changes: (i) both new companies, and existing companies that wish to expand, may apply for tax holidays; (ii) tax holidays will be set at a single rate of 100%; previously a range of 10% to 100% was applied; and (iii) 18 industries are now covered by the rules, compared to eight previously. These changes elicited a positive response: the number of taxpayers receiving tax holidays reached eight companies within only a few months, with the value of the corporate investment amounting to IDR161.3 trillion.

The Government continued to improve the incentives scheme to attract more investors. In the sixteenth economic policy package implemented in November 2018, the Government also relaxed the terms and procedures for granting corporate income tax reduction to companies in pioneer industries. This mostly applied to the percentage of corporate income tax which, from a previous rate of 100%, was split into two rates based on the scale of investment: a 50% tax allowance for investments in the range of IDR100 billion to IDR500 billion, and a 100% tax reduction (tax holiday) for investments of at least IDR500 billion. The number of pioneer industries that can apply for incentive facilities has been increased to 18.

Overall, fiscal incentives policy in the field of taxation played an important role in attracting investors. The fiscal incentives scheme needs to be continuously improved in order to ensure that Indonesia has at least comparable appeal to other countries in the region, amid competition to attract capital flows and higher foreign investment. The fiscal incentives scheme, as well as economic conditions and political stability, input prices and market size, is a key determinant of investment entering the country. Improvements to the fiscal incentives scheme also need to target encouraging growth in Indonesia's economic sectors, particularly those that are export-oriented and provide high added value to the economy.

IV.2 Tourism to Boost Foreign Exchange

Tourism is being developed to increase foreign exchange earnings, and improve the balance of services account. It will also boost employment, and represents an effort to diversify sources of economic growth. There is still plenty of space to increase foreign exchange revenues from tourism given that tourism is underdeveloped in some regions. In this regard, Thailand's tourism sector should be investigated, as the country enjoys the highest tourism rates in the region. Indonesia needs to improve in several key areas that shape tourism competitiveness, particularly those areas in which it currently lags behind peers. More particularly, Indonesia must improve in areas in which it falls behind Thailand. These key factors include connectivity infrastructure, particularly air transport, tourism service infrastructure including amenities, business climate, human resource quality and payment systems.

The Government has set some optimistic tourism goals for the short to medium term. To achieve these goals, the Government is targeting a number of major tourist destinations for national tourism branding and is prioritizing four destinations for tourism development. It is hoped this will lift the contribution of the sector to foreign exchange earnings. The four areas are Lake Toba, Borobudur temple, Mandalika Special Economic Zone and Labuan Bajo. Meanwhile, current major tourist destinations such as Jakarta, Bali, the Riau islands, Banyuwangi and Bromo require further development to improve the quality of infrastructure and services, and maintain the competitiveness of Indonesian tourism as a whole.

The development of Indonesia's tourism sector will be expedited via three main strategies pertaining to the enhancement of destinations, market access, institutions and the tourism business ecosystem. The first strategy is to improve attractions, access and amenities. Improving the quality of attractions involves improving the quality and sustainability of destinations and encouraging increased tourist spending. Improving accessibility involves enhancing the quality of connectivity infrastructure in various destinations, particularly priority destinations that are still under development. Improving the quality of amenities involves making the tourism experience more comfortable by improving the quality of accommodation, restaurants, trusted local transport, cleanliness and payment infrastructure, among other things. The second strategy centers on an effective marketing campaign: to improve the promotion of Indonesia as a tourism destination and increase brand awareness of Indonesia. The third strategy is to strengthen coordination concerning tourism development, to assist tourism-related businesses, including by ensuring tourism workers are available, and to provide finance for such businesses. This is mainly to support the development of tourism in destinations outside Java and Bali.

The development of tourism needs to be supported by greater promotion and the availability of reliable and up- to-date tourism data. Indonesia's destination marketing and tourism branding must be managed professionally and consistently in order to raise and maintain brand awareness. Promotions should be carried out in potential markets, including countries whose citizens tend to visit other ASEAN+6 (Association of Southeast Asian Nations +6) countries besides Indonesia, as well as tourists from the Middle East. In addition, a strategy to enhance institutional cooperation, including with flight services, needs to be pursued to help push up tourist arrivals.

Furthermore, synergy must be strengthened between institutions at the central and regional levels, and between communities and the private sector. Strategic government efforts to support tourism development need to be maintained and accelerated. These include improving the quality of connectivity infrastructure, increasing access to financing for tourism businesses, and measures to enhance destination management and tourism-related human resources. Bank Indonesia will continue to provide support for national tourism development as part of efforts to reinforce the structure of the economy and improve the current account balance. A number of steps are being taken by Bank Indonesia in this regard, including optimizing the role of its investor relations unit in supporting tourism investment, developing halal value chains to support halal tourism, and developing MSMEs that support regional tourism.

Bank Indonesia is continuously improving the quality of the payment system – one of the reasons for this is to support the development of priority tourism destinations. Various steps have been taken, including the expansion of payment channels and use of non-cash instruments, meaning debit and credit cards. Improving the ease of using non-cash payment instruments in accommodation and tourism facilities is one of the first steps in encouraging the wider expansion of non-cash payments in those locations. Furthermore, the more businesses that can accept electronic payments, the more tourists will spend – and this will lead to greater foreign exchange revenues from tourism.

IV.3 Strengthening the Sharia Economic Development Platform

Under the Bank Indonesia Sharia Finance and Economy Development Blueprint, the year 2018 represented the final stage in laying the foundations of the development program. By 2018, sharia programs had successfully and sustainably achieved several goals. There are three main pillars to the sharia strategy. The first focuses on the national sharia economic development strategy, and the second on developing Islamic finance by deepening the sharia financial market to support economic financing based on sharia principles. The third pillar focuses on strengthening knowledge of the sharia economy and finance through education, and on increasing public understanding through outreach programs and public campaigns across Indonesia, including with the involvement of international parties.

One of the first-pillar programs seeks to enhance the economic independence of pesantren (Islamic boarding schools that also function as community centers). This program forms part of the national halal value chain development strategy aimed at improving the structure of the economy, and includes the integrative and comprehensive development of all factors in the pesantren business unit ecosystem. The missions of the program are as follows: (i) to build the economic capacity of pesantren to optimize pesantren assets; (ii) to build good governance in pesantren; (iii) to build the skills of pesantren managers and teachers; and (iv) to enhance the curriculum with new subjects. All these missions are performed in stages according to the road map. In line with this road map, the capacities of pesantren are built through the application of accounting systems suitable for them, and also through the replication of existing pesantren business models from several business sectors. The capacities of pesantren are also built through the development of virtual markets, in line with the dynamics of burgeoning digital technology, so as to maintain their competitiveness.

Another program related to halal value chain development is the strengthening of sharia businesses through product- and financing-based programs. In the product-based program, development is first focused on Muslim fashion and halal food. To encourage the development of sharia businesses in both these sectors, Bank Indonesia is cooperating with sharia business players to establish a platform for the Indonesian Sharia Creative Industry (IKRA Indonesia). The IKRA Indonesia platform aims to produce excellent, high-value sharia business products that can compete with global brands. As part of the financing-based program, a sharia business group pilot project has been developed with financing from zakat infaq shadaqah waqf (ziswaf) funds – funds based on sharia principles – in the agricultural sector. This will be replicated in other sectors by the development of business models with financing.

Under the second pillar, the deepening of the sharia financial market is carried out to support the financing of halal sharia businesses. This strategy involves expanding the variety of sharia financial instruments available, which will increase investment attractiveness and transaction volumes. But regulations and infrastructure must also be strengthened. The scope of this second pillar also includes sharia commercial finance programs and sharia social finance programs. These two sharia finance sectors will be integrated, and will reach production units that need financial access. So far, achievements include the creation of several sharia financial instruments, including sharia-based deposit certificates, SukBI (Bank Indonesia Sukuk, or Islamic bonds), and hedging instruments based on sharia principles.

The development of sharia social finance programs uses an ecosystem-based approach. In order to strengthen the supporting infrastructure, core principles have been developed to improve governance and accountability in sharia social finance. To complement the zakat core principles, which were launched in 2016, Bank Indonesia collaborated with the Indonesian Waqf Agency to launch the waqf core principles at the 2018 IMF–World Bank Annual Meetings in Bali. In addition, cooperation between

Bank Indonesia, the Ministry of Finance and Indonesian Waqf Agency in this program has produced cash waqf-linked sukuk products. These products are intended to allow people to play an active role in the construction of public facilities through cash waqf funds.

The third pillar aims to improve public knowledge of the sharia economy and sharia finance. This also includes building the competency of human resources to make people more reliable, professional and internationally competitive, and enhancing public understanding of the sharia economy and finance through a variety of outreach programs. In practice, Indonesia will develop more education programs with strong relevance to industrial needs, will develop relevant curricula for schools, and will enrich vocational and professional programs. Bank Indonesia has also been active in outreach. It has held the ISEF five times, and in the previous two years cooperated on this with the National Islamic Finance Committee and other sharia stakeholders. As part of the 2018 event, sharia festivals were also held in Java, Sumatra and Eastern Indonesia. In conclusion, it is noted that outreach and education play an important role in supporting the first and second pillars. It must be stressed that the success of all sharia economic and financial development programs depends on the level of public understanding of sharia economic and financial issues.

IV.4 The Tax Imposition on e-Commerce

Today, Indonesia is one of the countries with the fastest economic growth in the world since the turmoil of the Asian economic crisis in 1997. The largest income sector in the economy that was once export-based commodities such as oil and gas is now slowly shifting with the ongoing tax reform. Along with the rapid use of the internet in the era of globalization, the growth of electronic-based transactions has also increased. In the span of twenty years (1998–2018), Indonesia’s internet users have increased significantly, from 500 thousand to more than 100 million internet users. As a result, Indonesia is now an online market with the largest number of consumers in Southeast Asia.

Looking at the rapid increase in online market transactions, Indonesian government strongly supports this economic digitalization era. The result of the achievements of four Indonesia’s start-ups that have won the title of unicorns (Go-Jek, Tokopedia, Traveloka, and Bukalapak) have encouraged the government to continue to improve the country's digital economy industry. Look at the analysis, the e-commerce sector is able to become a significant supporter of the Indonesian economy in the next 5 years.

According to a report by Google and Temasek, in 2018, the Gross Merchandise Value (GMV) of internet economy in Indonesia was US$ 27 billion, where in 2015 was only US$ 8 billion or 49% for its Compounded Annual Growth Rate (CAGR), and supported 2.9% of Gross Domestic Product (GDP). From this digital economy values in 2018, Indonesian e-commerce contributes US$ 12.2 billion or raise 94% from its GMV in 2015 that was only US$ 1.7 billion. It is forecasted that Indonesian e-commerce will hit US$ 53 billion or grow 41% in 2025. From Indonesian internal data, Data from Indonesian Central Bank (BI) states, online shop transactions (e-commerce) in Indonesia throughout 2018 then reached 77.766 trillion rupiahs. This figure has skyrocketed 151% compared to the previous year which reached 30,942 trillion rupiahs. Based on census data from the Indonesian Central Statistics Agency (BPS) said that the e-commerce industry in Indonesia in the last 10 years increased by 17% with a total number of e-commerce businesses reaching 26.2 million units. The main actors of Indonesian e-Commerce are individuals and corporates that support 90% of Indonesian economic actors.

As the fourth most populous country in the world, Indonesia becomes a potential market for global e-commerce players. Some global e-commerce players (e.g., eBay, Amazon, Yahoo auction, Google, Alibaba, Facebook, Apple, Instagram, Youtube) have entered the Indonesian domestic market. The cross-border transactions are unavoidable, and clearly affect the domestic market. The digitalization not only changes the way of doing business but also raising a number of pressing matters in the areas of privacy and security, jobs as well as other policy areas including taxation. E-Commerce not only contributes to the economy, but also has promising tax potential in the future.

Indonesia’s taxation system for the digital economy is currently in the gray area and far from taxation. This means that there is no certainty from the government in responding to the digital economy. The government has tried to form a regulation through PMK No. 210 of 2018 concerning Tax Treatment of Sales Transactions through Electronic Systems (e-Commerce) at the end of 2018. However, the policy is still too premature to be enforced because it causes many problems, starting from the not yet created level playing field between formal and informal online transaction platforms, the risk of economic distortion, the lack of socialization to the community, the rumor of inequality of tax treatment among business people, and to the use of political issues. At the end, the regulation was revoked before it could take effect as of April 1, 2019. So that, the digital economy still does not have a clear legal corridor for Indonesia tax system until now.

The complexity of the characteristics of the digital economy is itself a challenge for government to formulate policies accordingly. Based on the challenges faced by almost all countries, in general, the problems that arise in the era of digitalization lie in the problem of detecting the identity of companies that play a major role as e-commerce businesses and the mechanism of taxation of VAT from cross border transaction activities. This condition has created a challenge for DGT. Countries such as India, Japan, France and United Kingdom have actually begun to implement regulations to regulate e-Commerce taxation. In addition, the availability of international proposals such as EU Commission and OECD to tax digital economy can be used as a guideline for government.

To the best of my knowledge, the Indonesian Directorate General of Taxes (DGT) has regulated the taxing procedures of e-commerce transaction in Director General of Taxes Circular Letter Number 62/2013 (SE-62/PJ/2013) and Number 06/2015 (SE-06/PJ/2015). These circular letters categorized the e-commerce transaction models (i.e., an online marketplace, classified ads, daily deals, and online retail) along with the taxation procedures for each model. Since the Indonesian tax system employs self-assessment, the tax administration relies on the periodic/annual tax returns data to assess the compliance of taxpayers operates in this business. This raises the issue of the construction of an inclusive taxpayers' transaction monitoring system to ensure the fair share tax payment.

The main challenges and constraints are transaction data that is difficult to detect, and tax regulations that are still based on conventional. In addition, taxation policies are often seen as hampering economic growth and investment, as well as used as commodities in political issue. So how to approach to digital economy issue? Making a comparative study of other countries regulations and plans are the best way to get action in approaching e-commerce taxation policy. But before that Indonesia must be able to capture the whole relevant process and data of e-commerce and bring synergy between existing institutions. DGT, as the responsible institution, needs to make coordination with Central Bank (BI), Statistical Central Agency (BPS), and Commission for the Supervision of Business Competition (KPPU) to collect information regarding e-commerce transactions.

So next year, before the e-Commerce business becomes too big to control, the government wishes to introduce new regulations that will cover everything related to e-Commerce transactions, data collection, privacy, digital finance, cross-boarder transactions and tax.

V. Conclusion: Where We Stand and Where We Go?

V.1 Global Environment

The global economy grew in 2018 but at a slower pace than in 2017, and with uneven growth among countries. The slowdown in global economy particularly commenced in the second semester of 2018. Overall, the economic performance of 2018 was lower than expected at the beginning of the year.

During th whole year 2018, global economic and financial developments were fraught with an uncertainty that threatened the economies of some nations. A series of potentially destabilizing events occurred in quick succession: the increased frequency and magnitude of increases in the Federal Funds Rate, trade tensions from actions launched by the United States against countries including China, falling commodity prices, the uncertainty over Brexit and a number of geopolitical risks. In consequence, global investors engaged in a large-scale rush to withdraw funds from emerging markets, thus threatening the external stability of these countries, including Indonesia. Not only did various currencies depreciate sharply against the US dollar, but balance of payments disequilibrium also exacerbated risks of macroeconomic and financial system instability. Argentina and Turkey were hit by crisis, while other emerging market nations struggled hard to bolster the external resilience of their economies against the adverse impact of this global contagion.

Global economic uncertainty triggered a diversity of policy responses in countries seeking to optimize the interactions between monetary and fiscal policy. In advanced economies, several countries excluding US adopted a loose-bias monetary policy stance to maintain growth momentum. Meanwhile, these advanced economies also pursued gradual fiscal consolidation, contrasting with dynamics in the United States where large-scale fiscal stimuli were introduced. In developing economies, the most pressing challenge to economic policy was how to optimize the monetary and fiscal policy mix in response to the buildup of external risk. The majority of developing economies adopted a tight-bias monetary policy stance in response to the tightening of global monetary policy which triggered the capital outflows. On the other hand, fiscal policy stance continues to be balanced in order to safeguard economic growth and while maintaining fiscal sustainability.

Structural reforms in various countries has continued to support sustainable economic growth. The reforms were aimed towards enhancing productivity, boosting employment, and increasing potential economic growth which has been blighted by aging population. International cooperation was also strengthened bilaterally, regionally, and multilaterally in order to ensure solid, balanced, and sustainable economic growth, while maintaining economic resilience.

The adverse global developments were unavoidable and posed a challenge for Indonesia's external sector in the trade and financial channels. In the trade channel, global uncertainties began to affect Indonesian exports from the second half of 2018. The gradual decline in world economic growth, partly in response to declining growth in the economies of Indonesia's key trading partners such as China, resulted in lower demand for goods exported from Indonesia. Exports also weakened further because at the same time, Indonesia's terms of trade (ToT) deteriorated due to the fall in prices for Indonesia's export commodities.

At the same time, the complexity of challenges from the trade channel was exacerbated by high imports that persisted for the first three quarters of 2018 in line with buoyant domestic demand, particularly for infrastructure projects. The increase in raw material imports was driven mainly by industries producing goods for the domestic market, as well as export-oriented manufacturing. These developments represented the effect of sustained and robust domestic demand and the upward trend in world oil prices.

In the financial channel, global uncertainties weighed on foreign capital inflows into Indonesia. The increases in the FFR reduced the attractiveness of assets in emerging markets and prompted an exodus of capital from emerging market nations, including Indonesia. Furthermore, uncertainty on global financial markets, also impacted foreign capital inflows in Indonesia. The decline in foreign capital inflows during the second and third quarters of 2018 also impacted domestic liquidity. Although capital inflows remained at a safe level, the drop in these inflows contributed to reduced growth in economic liquidity.

Amid the pressure on Indonesia's external balance, developments in the internal balance and the financial system stability remained favorable. The economy grew solidly driven by domestic demand, which itself was driven primarily by infrastructure projects. These have generated multiplier effects in household consumption and in construction and non-construction investment. Inflation was subdued, reflecting healthy internal balances. Rupiah depreciation did not push inflation upwards excessively. Meanwhile, financial system stability remained strong, as indicated by high levels of capital, higher growth in lending and credit risk maintained at low levels.

V.2 Fiscal Policy

The synergy among various authorities in the policy mix is key to reinforcing the structure of the national economy. Monetary, fiscal and financial sector policies will be directed at maintaining macroeconomic and financial system stability. At the same time, it is necessary to expand and increase the pace of structural reforms in the real sector. These structural reforms will be decisive in improving competitiveness, productivity, investment, trade, labor conditions and legal certainty.

More needs to be done to speed up the efficiency improvements in bureaucracy at the central government and regional levels, and to upscale the implementation of the integrated licensing program (OSS) in order to enhance the business and investment climate. Construction of infrastructure must be carried out on a broader scale, particularly for connectivity, and should be targeted to support the development of economic and tourism zones.

Bank Indonesia, the Government and relevant authorities acted resolutely and consistently to implement a policy mix that would strengthen economic stability – in particular rupiah stability – while sustaining the economic recovery. The challenges to the economy in 2018 emerged mostly from external balances, while internal balances were solid. For this reason, policy was focused on mitigating external sector risks that could adversely impact the BoP and pressure the exchange rate. Immediate action was necessary to forestall these developments which, unchecked, could have destabilized the economy.

Policy also sought to strengthen the existing momentum for economic recovery. According to Bank Indonesia estimates, the upwards trend of Indonesia's economic growth did not disrupt internal balances, given that growth remained below potential capacity. The policy mix was geared to provide continued support for economic growth, enabling growth to climb towards the potential capacity of the economy. The pro-growth measures were also consistent with the financial cycle which, according to indicators, was below long-term projections, despite being on an upward trend. Overall, the policy mix was balanced with inflation control measures in order to keep inflation on target and financial systems stable.

Bank Indonesia, the Government and other authorities synergized their policy choices. Bank Indonesia optimized a mix of monetary, financial market deepening, macroprudential and payment system policies with the aim of maintaining stability and supporting economic growth. The Bank Indonesia policy mix was managed in synergy with the fiscal and structural policies of the Government and OJK to safeguard the resilience of the financial system and growth momentum.

The direction of the monetary policy rate in 2018 was placed within a framework of determining an optimum monetary policy for a nation with an open economy. Changes were introduced to formulate the policy rate independently, taking account of two other important elements: free movement of foreign capital and continued exchange rate flexibility. Interest rate policy on one hand sought to create adequate interest rate differentials and bolster the attractiveness of investing foreign capital in domestic financial market assets. On the other hand, the policy rate also needed to remain consistent with measures to keep inflation on target. At the same time, exchange rate policy was focused on maintaining exchange rate stability at about the level of fundamentals, so that it could serve as an instrument for mitigating shocks to the economy from external factors.

V.3 Tax Administration

MSME is a business group with a sizable amount in Indonesia. According to data from the National Development Planning Agency, the Central Statistics Agency, and the United Nations Population Fund the number of MSME actors in Indonesia in 2018 was 58.97 million. When compared to the total population of Indonesia in 2018 which reached approximately 265 million people, then around 23 percent of the population were SMEs. The large number of MSME actors has made the Government pay serious attention to the development of MSMEs. This can be proven as on one of the XII Economic Policy Package in 2016 which contains trimming licenses, procedures, time, and costs for ease of doing business in Indonesia.

Long before that, the Government has issued Government Regulation No. 46 of 2013 concerning Income Taxes on Income from Businesses Received or Obtained by Taxpayers with a Specific Gross Distribution (PP 46). In the implementation of PP 46 from 2013 to 2017, the data held by DGT shows that the trend of the number of taxpayers and tax receipts always experiences enhancement. This adds to the Government's belief that MSMEs are a sector with great potential.

After almost five years of implementation, the Government revised PP 46 and issued Government Regulation No. 23 of 2018 (PP 23). This, of course, is good news for business taxpayers with a turnover of up to IDR 4.8 billion per tax year. Through PP 23, the Government reduced the previous tax rate by 1 percent to 0.5 percent. This tariff reduction alleviates the tax burden that must be paid so that the Taxpayer can further develop his business.

In order to provide better justice to taxpayers, the imposition of PPh based on PP 23 is optional, this is certainly different from PP 46 which imposition is mandatory. Taxpayers who are entitled to use PP 23 can choose to calculate their taxes based on accounting. However, taxpayers who have chosen not to be subject to income tax based on PP 23, are not permitted to return using the provisions of PP 23. The imposition of final PPh based on PP 23 can be done for a certain period of time. The enactment of a certain period is intended as a learning period for taxpayers to be able to organize bookkeeping before being subject to income tax with the general regime.

Implementation of PPh obligations based on PP 23 can be done through self-payment by the Taxpayer or withheld/collected by the tax collector. Taxpayers who have the obligation to pay their own income tax, can make payments through various channels, including through perception banks, post offices, internet banking, mobile banking applications, and ATM machines. Taxpayers who want to withhold tax at a rate of 0.5 percent, must submit a Certificate to the tax cutters.

Since the enactment of the provisions of PP 23, until the end of 2018 a total of 673,374 Taxpayers who had not previously made payments began to make final MSME Final Income payments and as many as 372,675 newly registered Taxpayers and made payments for the Final MSME Final Income. This shows the positive response of the public to the issuance of PP 23. Through the reduction in tariffs and various facilities set out in PP 23, the Government is trying to encourage the development of MSMEs while at the same time providing the community the opportunity to contribute in funding development through tax payments. It is hoped that the community can continue to increase their awareness and compliance with taxation rights and obligations.

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