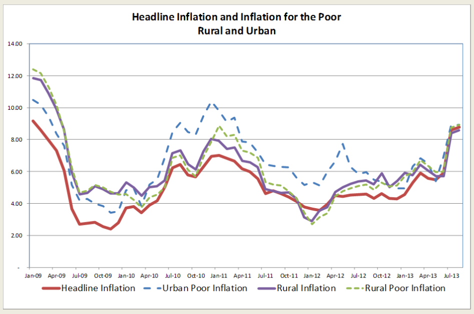
Poverty and the Economy

September 2013

INFLATION

With Idul Fitri falling early in the month, pass on effects from the fuel price increase in July, and the rapid depreciation of the rupiah, it is not surprising that the rate of inflation remained high in August at 1.1%, though much lower than July's monthly inflation rate of 3.2%. The major contributors to inflation in August reflected expected price pressures: higher food prices (the impact of Ramadan and Idul Fitri), the higher gold prices imported inflation, and rising transportation prices reflecting the impact of higher fuel prices. Seasonal increases in school fees also contributed to inflation in August. We would expect downward pressure on food prices in September, representing the other side of the seasonal increase in food prices during Ramadan. At the same time the major adjustments to the fuel price increase should have been completed, taking some pressure off of inflation. But the continuing weakening of the rupiah will put upward pressure on prices.

The year-on-year inflation for August 2013 was 8.8% while year-to-date inflation was 7.9%. Given the weak rupiah and some continuing impact from the fuel price increase, Bank Indonesia's prediction that inflation will be about 9.0 to 9.8 percent at the year-end seems reasonable.



Similar to last month, the difference between urban/rural and poor/non-poor inflation rates in August remains small due to the fact that food inflation affects the poor quite heavily, while increases in direct transportation costs have more of an impact on the non-poor. The annual inflation for food was 15.1% and 14.6% for transportation. At the beginning of 2013, the inflation of food products was higher than for transportation but since April 2013, the price of transportation has increased more. In April and May the price of foods declined substantially and since June the price of transportation increased substantially because of the fuel subsidy removal.

Monthy Inflation, 2013

Month	Food	Transportation	General
January	3.39	-0.28	1.03
February	2.08	0.08	0.75
March	2.04	0.19	0.63
April	-0.80	0.10	-0.10
May	-0.83	0.05	-0.03
June	1.17	3.80	1.03
July	5.46	9.60	3.29
August	1.75	0.95	1.12

World Food Prices

In August of 2013 food prices are down by 4% from July and by 8% from the end of 2012. Beverages increased by 1.9% from July. However, the depreciation of rupiah by over 25% more than compensated for the decline in world food prices so that domestic prices rose despite the world price decline.

DEVELOPMENT

World economic growth remains slow

World economic growth remains slow but the underlying dynamics have changed according to a statement during the G-20 summit in St. Petersburg by the International Monetary Fund (IMF). This is due to signs of recovery in Europe and more rapid growth in the US while growth of developing economies is slowing. Net world growth is accelerating.

That developed countries are showing signs of recovery, while growth in emerging markets is slowing are two sides of the same coin. At the end of the 2000s, the global financial crisis weakened the developed economies which responded with significant programs of monetary easing. With poor investment prospects in those countries, a lot of that money flowed to developing markets, including Indonesia, fueling domestic demand and increasing growth. Now that developed countries are beginning to grow again, the loose monetary policy is expected to be scaled back. In addition there are improved prospects for growth in developed countries. For both reasons investors are beginning to bring their money home, slowing growth in developing economies including Indonesia. As a result the IMF believes that there may be a "prolonged period of sluggish global growth" ahead.

Indonesia's Growth is lower than predicted

The International Monetary Fund (IMF) expects the economy of Indonesia to expand by 5.25 percent in 2013, which is considerably lower than the IMF's forecast of 6.3% in its World Economic Outlook of April 2013. Indonesia's GDP growth assumptions were quickly revised downwards after emerging markets were hit by large capital outflows when the Federal Reserve began to speculate about an end to its quantitative easing program (QE3). The main factors that contribute to the downgrade are weak exports and a slowdown in investment. Amid weak global conditions in recent years demand for commodities has plunged, resulting in low commodity prices. This has created the significant trade balance Indonesia faces today.

However, the draft of the State budget (RAPBN) 2014 has a more optimistic growth assumption of 6.4% for 2014. But Bank Indonesia more recently forecast growth at 5.8-5.9%.

Trade Balance

Indonesia's trade deficit set a new record at USD $5.65 billion in the first seven months of 2013. The deficit was caused by the oil & gas

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trade deficit (USD $7.6 billion), while the non-oil & gas sector posted a surplus of USD $1.9 billion. In the second quarter the current account deficit was equivalent to 4.4 percent of GDP.

Although the non-oil and gas sector recorded a surplus for the year-to-date, it was still lower than the same period last year and non-oil trade balance has been in deficit on a monthly basis since April. Exports of fuel, vegetables oil and fats, machinery and mechanical equipment, and rubber have declined in 2013 compared to 2012, while exports of minerals (ores, slag and ash, tin and nickel) and fertilizer increased. Non-oil and gas imports were lower in 2013 compared to 2012 but not by as much as the decline in exports. Imports of machinary, mechanical equipment and vehicles were lower in 2013, while imports of electrical equipment, iron and steel, plastics, organic chemicals, cereal and cottons were higher.

With the depreciation of rupiah and the increase in fuel prices, Bank Indonesia expects the current account deficit to ease to 3.4 percent of the country's GDP in the third quarter of 2013.

SPECIAL REPORT

Compensation Programs for Fuel Subsidy Reduction[1]

In anticipation of reducing the fuel subsidy the government implemented measures to soften the blow to low-income communities. This included the Temporary Direct Cash Transfer (*Bantuan Langsung Sementara Masyrakat – BLSM), the* Program for the Acceleration and Expansion of Social Protection (*Program Percepatan dan Perluasan Perlindungan Sosial* - P4S), and Acceleration and Expansion for Infrastructure Development Program (*Program Percepatan dan Perluasan Pembangunan Infrastruktur - P4I).* The P4S consists of the Rice Subsidy Program for Low-Income People (*Raskin)*, the Program for Family Hope which provides cash for families keeping children in school and getting them vaccinated (*Program Keluarga Harapan -PKH),* and Scholarships for Poor Students (*Beasiswa Siswa Miskin)* while the P4I includes programs for housing (P4-IP), drinking water (P4-SPAM) and water resources (P4-ISDA).

Each program reaches different numbers of beneficiaries and time of disbursement as stated in the table below:

Type of Program	Number of Beneficiary	Total Budget	Disbursement Scheme
Raskin	15.5 juta HH	Rp 21.50 trillion	every month
BSM	16.6 million srudents from 15.5 million HH	Rp 12.08 trillion	every semester
BLSM	15.5 million HH	Rp 9.32 trillion	twice: Juni/July and September/October
PKH	2.4 million HH	Rp 3.60 trillion	every quarter
P4-IP	5,500 villages	Rp 3.25 trillion	August - December
P4-SPAM	159 fishery area, 250 villages with water scarcity, 341 urban areas	Rp 2.00 trillion	August - December
P4-ISDA	27 provinces with water scarcity	Rp 2.00 trillion	Agustus -Desember

There have been some complaints regarding the BLSM both on the policy itself (that it creates dependence, that it would be better to provide a labor intensive employment program or health and education assistance) and on the mechanism of distribution (data are questionable, some post offices were attacked by unsatisfied residents, some of the people who queued have cellphones and were wearing gold-plated necklaces). However, these anecdotal examples cannot be used as a basis to evaluate the effectiveness of the program.

The designation of the recipients of BLSM was based on Targeted Households (RTS) data in the Integrated Data Base (BDT) managed by TNP2K. RTS data has been documented three times by the BPS, the last time in 2011. The 2011 PPLS data collection methodology has been refined by BPS and TNP2K to improve the accuracy of the data. Data verification to numerate all targeted Household Characteristics was conducted by BPS. The enumerated data were then processed by TNP2K to produce data on 40% households with the lowest socioeconomic status. The data was then managed as Unified Data Base (*Basis Data Terpadu - BDT*) and used as a database for all poverty alleviation programs. For the BLSM, the beneficiaries are the 25% lowest HH which cover around 15.5 million HH.

As shown in the table above, the BLSM program targets the same households as the Raskin program. This was important for the successful and rapid implementation of the BLSM. In anticipation of the possibility of implementing something like BLSM, the government of Indonesia earlier this year issued identification cards to the 15.5 million Raskin-eligible households that had their names and other identifying information on them as well as a unique identifier in the form of a bar code. This assists with the implementation of the Raskin program but was a critical first step in preparing for the BLSM.

At the same time the government began discussions with the Post Office about how the postal system could be used to make payments should a BLSM-like program be approved. Fortunately, most of the post offices were automated and included bar scanners that could read the code on the Raskin cards. (A manual system was devised for those post offices that are not on-line.) With these two pieces in place, the government was ready to implement the program.

Once the BLSM was announced, poor families were told that if they have the cards they could just go to the post office with their card and a matching ID and collect their first payment. In some cases where names were not quite right or heads of households had passed away, a letter from the village head certifying another family member as the recipient of the funds could be provided. Moreover, with the dynamic nature of the economy between 2011 and 2013, there is some inaccuracy in the selection of BLSM beneficiaries. However, the government has anticipated this and prepared a mechanism to update these data through village deliberation (*Musyawarah Desa)*, through which local communities can change the households receiving support under the program.

The success of this preparation can be seen from the fact that by the end of August, 93% of eligible recipients of the *BLSM* Phase 1 disbursement had received their funds. The government is now working with village leaders to redeploy the 7% that was not claimed to poor households that were missed in the first distribution using the Musyawarah Desa approach.

The Phase 2 disbursement, which started on September 2nd, had reached 10 million households or over 60% of recipients in two weeks. You can follow the implementation of the program in real time at http://www.kompensasi.info.

[1] Tim Nasional Percepatan Penanggulangan Kemiskinan (TNP2K), 2013, *Buku Pegangan Sosialisasi dan Implementasi Program-Program Kompensasi Kebijakan Penyesuaian Subsidi Bahan Bakar Minyak 2013*, 4th edition, June 2013.

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