OXFORD BUSINESS GROUP

Indonesia Digital Economy

Covid-19 Recovery Roadmap

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Pre-Covid-19 Macroeconomic Overview

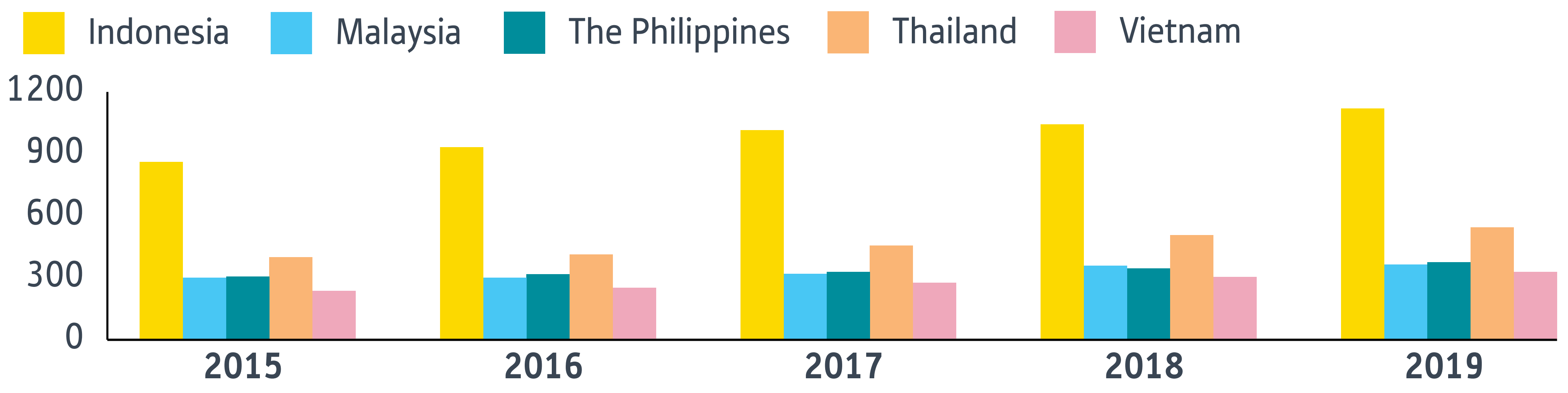
Indonesia introduced a host of targeted reforms to boost its economic resilience in the years after the 1997-98 Asian financial crisis. The crisis was characterised by high external debt, a leveraged financial system and structural rigidities in the economy, which resulted in the rapid depreciation of the rupiah. These changes proved prescient after the emergence of Covid-19 and the impact the pandemic had on global economies.

Indonesia maintained consistent levels of growth in the years leading up to the pandemic – at around 5% between 2015 and 2019 – owing to robust domestic consumption and continuing efforts to reform policy and simplify investment procedures. The country faced the pandemic with one of the lowest government debt-to-GDP ratios in ASEAN – at 30.3%, compared to the bloc's average of 39.1% in 2019 – and near-record foreign currency reserves, which totalled $131.7bn in January 2020. The increasingly diversified economy was protected from some of the immediate effects associated with the pandemic, including supply-chain disruptions and movement restrictions, as it was comparatively less dependent on the export of goods and services, and travel and tourism flows. Moreover, Indonesia's banks were cushioned from the potential impact of debt defaults, having maintained a mean financing-to-assets ratio of 87.4% and a non-performing financing ratio of 2.4-2.7% in the six months leading up to the pandemic.

Digitalisation and infrastructure development were central components of pre-pandemic diversification efforts, a factor that further supported the economy as business operations and communications went online. Construction accounted for 10.8% of GDP in 2019, while at the same time the country was home to four unicorn start-ups and one decacorn.

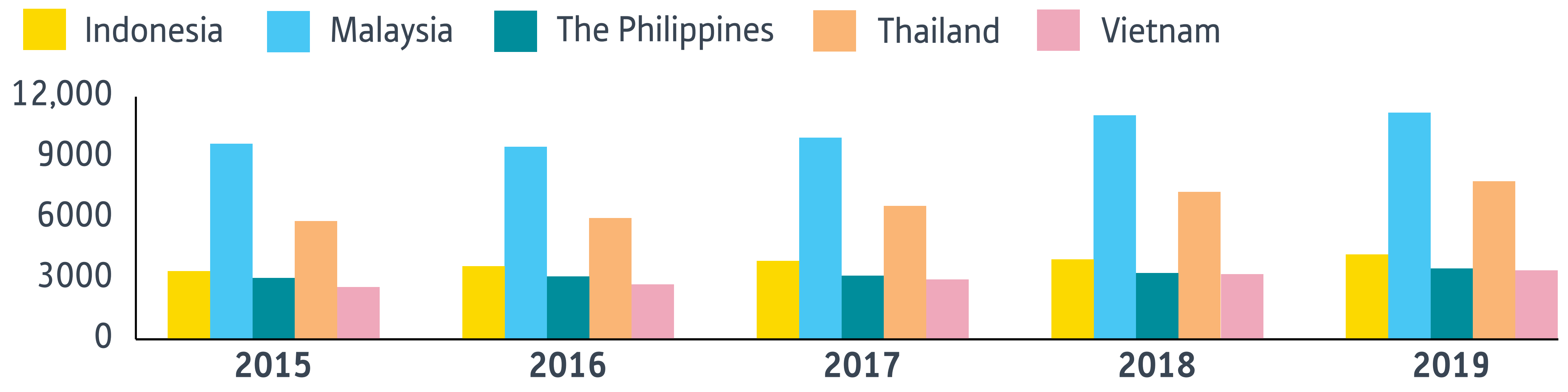
The re-election of President Joko Widodo, better known as President Jokowi, in May of that year signalled the government's continuing commitment to welcoming foreign investment. One key element of the current administration's reform drive was the Omnibus Law on Job Creation, which President Jokowi signed into law in November 2020. The law overhauled the country's legislative and regulatory framework, and comprised over 70 amendments to existing legislation with provisions to liberalise the labour market, support business development, stimulate private investment and improve the ease of doing business. These developments – combined with the archipelago's geographic location, human capital development agenda and progress in free-trade agreements – placed ASEAN's most populous country in an advantageous position in the years leading up to the pandemic.

GDP of selected ASEAN economies*, 2015-19 ($ bn)



*current prices

GDP per capita of selected ASEAN economies*, 2015-19 ($)



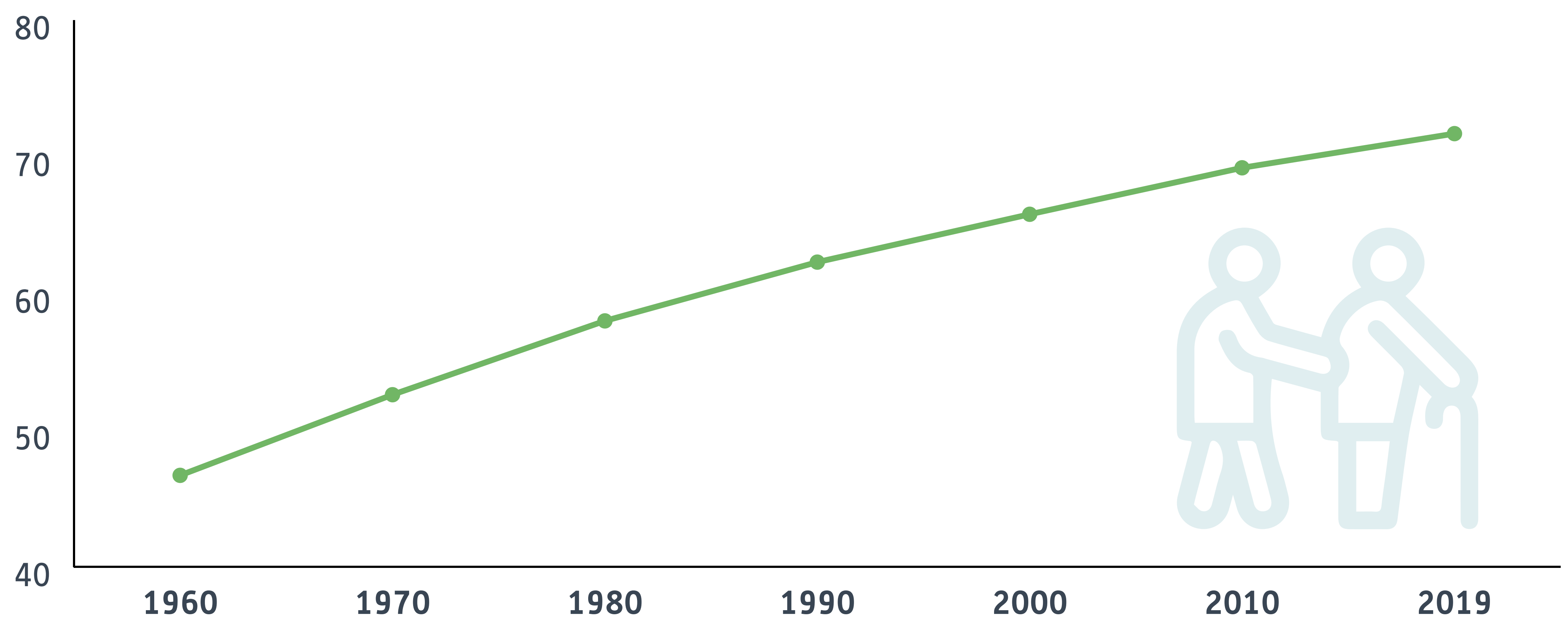
*current prices

Graph source: *IMF*

Health Care

Investment in health infrastructure, enhanced access to health services and better living conditions due to a developing economy have all helped Indonesia's health indicators progress in recent years. These improvements were especially notable given the challenge of providing care to residents spread across the expansive archipelago. Life expectancy has been on the rise, from 65.8 in 2000 to 71.7 in 2019, according to the World Bank. This has been reflected in health expenditure per capita increasing nearly six-fold between 2000 and 2018 – from $16.20 to $111.68 – as well as the construction of 3336 new health care facilities between 2014 and 2017.

Life expectancy at birth, 1960-2019 (years)



Moreover, the number of primary care outpatients doubled between 2014 and 2017; the ratio of nurses and midwives relative to the population doubled between 2010 and 2018; and the ratio of physicians relative to the population more than tripled over the same period. These factors, combined with Indonesia's demographic advantage – the country is home to one of the most youthful populations in the G20 – helped to enhance Indonesia's resilience to the most significant health effects of Covid-19.

Central to the improved provision of health has been the rollout of universal health care. Proposed in 2014, the plan aimed to cover the population of over 268m by the end of 2019; while this initial target was not met, around 80% of Indonesians were covered as of August 2019, up from around 50% when the programme was first proposed. The plan primarily relies on public providers, but also includes private players that opted to join the scheme.

Access to health care – particularly specialised services – beyond urban centres nonetheless remained a challenge leading up to the pandemic. While the national bed-to-population ratio stood at 1.17 per 1000 in 2018, it belied considerable variation by locality: according to the Ministry of Health, for example, that year the ratio was 0.71 in West Nusa Tenggara, 0.85 in West Java and 0.98 in Riau. Health technology platforms helped to increase access to care for some underserved communities prior to the pandemic, but uptake was constrained by ICT infrastructure challenges – particularly beyond urban centres, where internet connections can be unreliable – and a general lack of awareness and trust among both patients and health care practitioners.

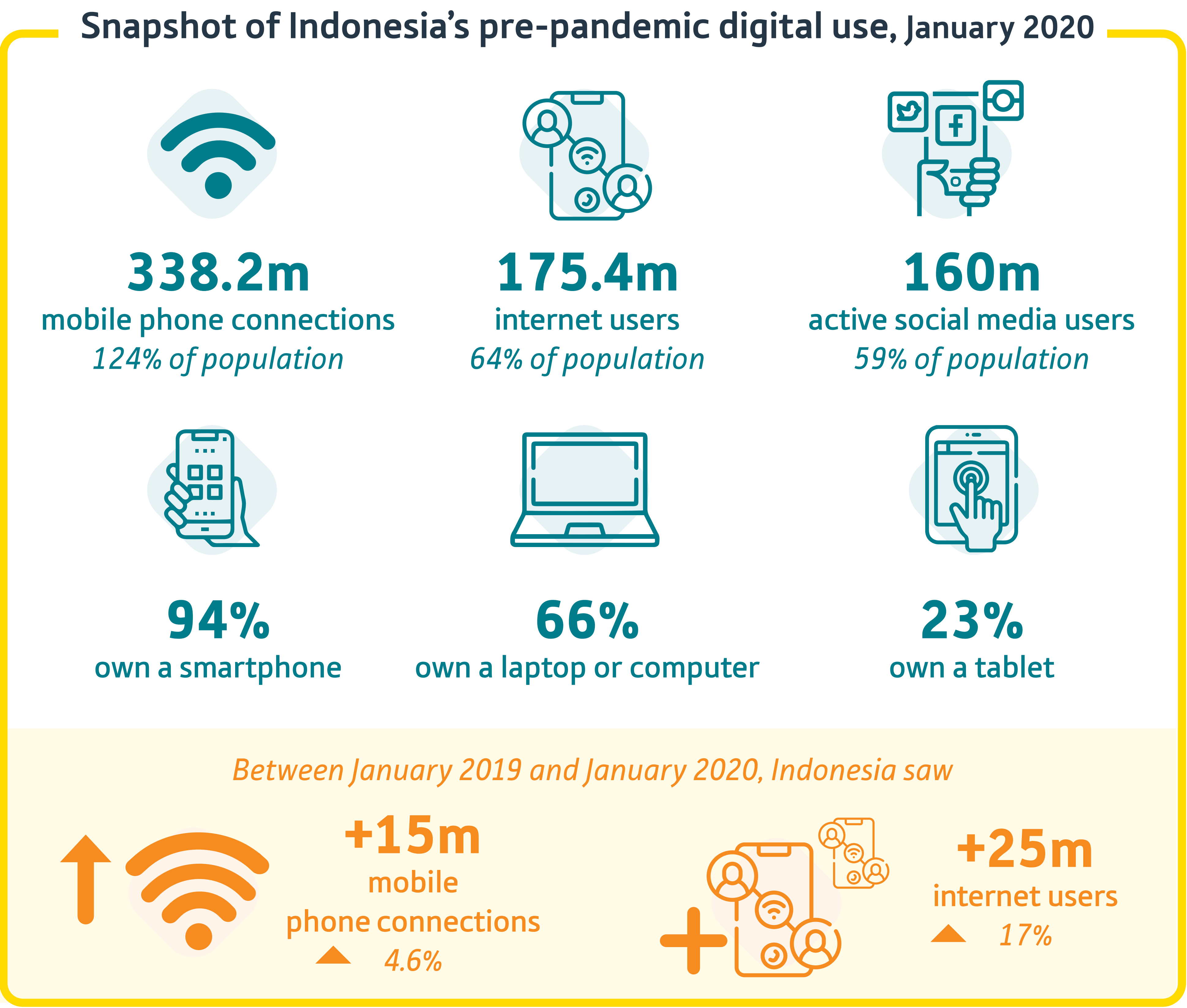
Graph source: *World Bank*

Digital Economy

Indonesia boasted the largest and fastest-growing ICT market in South-east Asia prior to the pandemic: the country's digital economy quadrupled in size between 2015 and 2019 – at an average growth rate of 49% per year – to reach an estimated gross merchandise value (GMV) of $40bn, according to a report from Google, Temasek and Bain & Company. This expansion was reflected in expanded GMV in several sectors over the same period, including ride hailing (from $900m to $6bn) and e-commerce (from $1.7bn to $21bn). This burgeoning market presented an enticing opportunity for investors, especially due to favourable demographics and a supportive ecosystem. For example, the country's list of pioneer industries – which are eligible for tax holidays linked to the size of their investment – was expanded in 2019 to include key segments of the digital economy, such as data processing and related activities.

By January 2020, 175.4m Indonesians, or 64% of the population, were connected to the internet – an increase of 25m year-on-year (y-o-y) – according to a report from the UK's digital marketing agency We Are Social and Canada's social media management platform Hootsuite. Meanwhile, mobile phone penetration was 124% in January 2020, an increase of around 15m subscriptions y-o-y. The report also found that Indonesians largely turned to smartphones to get online: 94% of Indonesians owned a smartphone, compared to the 66% who owned a laptop or computer and 23% who owned a tablet. Moreover, 3G connections were more widespread than 4G or fixed broadband connections.

These factors have helped Indonesia become home to the highest number of tech unicorns among all ASEAN members, with local digital payments firm OVO joining their ranks in October 2019. Other unicorns include e-commerce site Bukalapak and travel provider Traveloka. Gojek, originally a ride-hailing app, became a decacorn in April 2019 and announced a merger – estimated to be valued at $18bn – with e-commerce unicorn Tokopedia in May 2021 to form GoTo.



Infographic source: *Hootsuite; We are Social; World Bank*

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Economic Support Mechanisms

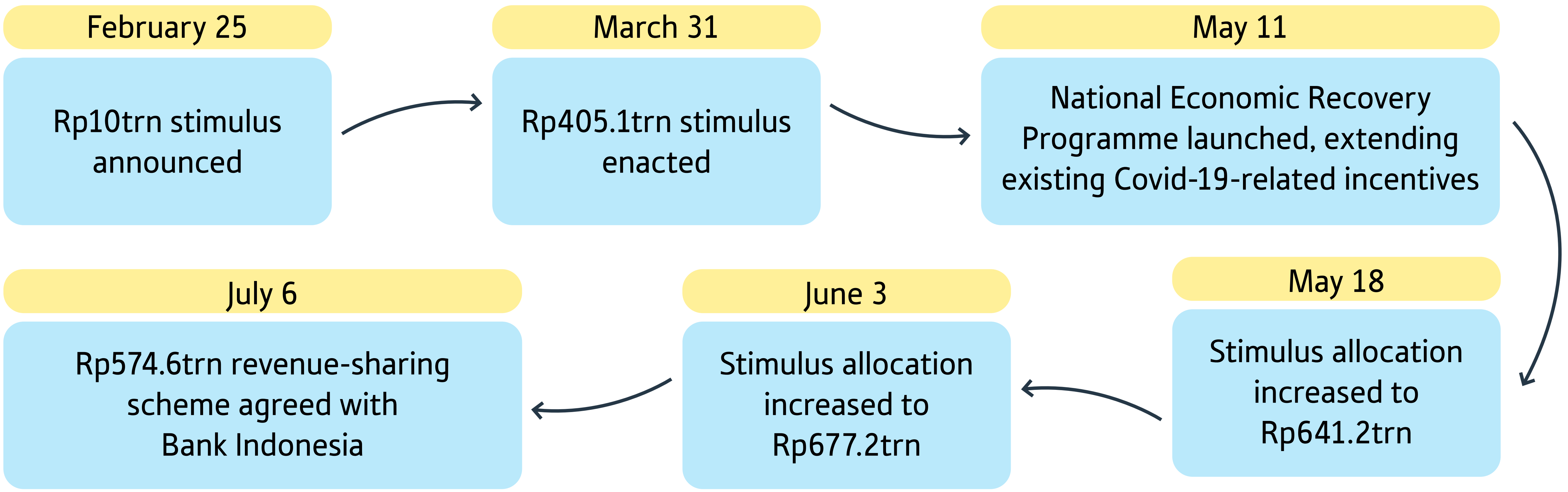
In an effort to balance public health concerns with national economic interests, Indonesia promoted social distancing and personal responsibility in the early months of the pandemic. Phased, localised restrictions were then put in place according to caseloads. Decisive measures in the first half of 2020 included the March 31 signing of a national stimulus package totalling Rp405.1trn by President Joko Widodo, better known as President Jokowi – who had already announced a Rp10trn stimulus on February 25 – and the declaration of a national health emergency on the same day.

With respect to movement restrictions, international arrivals were banned from April 2, while a government regulation was announced on April 3 permitting local administrations to implement large-scale social restrictions, known locally with the acronym PSBB. PSBB was introduced in Jakarta one week later, and was extended multiple times to June 21. After that date the capital's restrictions were gradually eased over a six-week period.

The government incrementally increased economic support during the early months of the pandemic. On May 11, for instance, the National Economic Recovery Programme was launched, extending existing Covid-19-related incentives such as tax breaks, liquidity support for the banking industry and financial assistance for vulnerable households. On May 18 the stimulus allocation was raised to Rp641.2trn, and the package was increased again on June 3 to Rp677.2trn. Some of the additional stimulus was funded by a Rp574.6trn revenue-sharing scheme between the government and the country's central bank, Bank Indonesia, agreed on July 6. This enabled the bank to purchase government bonds at below-market yields to help fund the national response.

In early August 2020, with the public health authorities seeking to boost compliance with Covid-19 restrictions, President Jokowi signed an executive order allowing local authorities to impose fines or punishments for failure to wear face masks or follow pandemic-related business regulations. At the end of that month the governor of Bali cancelled September plans to welcome back international tourists as cases surged; tourism is viewed as a priority sector for recovery. In mid-September PSBB was reintroduced in Jakarta, before restrictions were eased from October 12 to the end of 2020 as case counts moderated once again. In January 2021 the government closed the country's borders to prevent the entry of new variants that were spreading elsewhere, and retightened social restrictions in certain parts of Java and Bali.

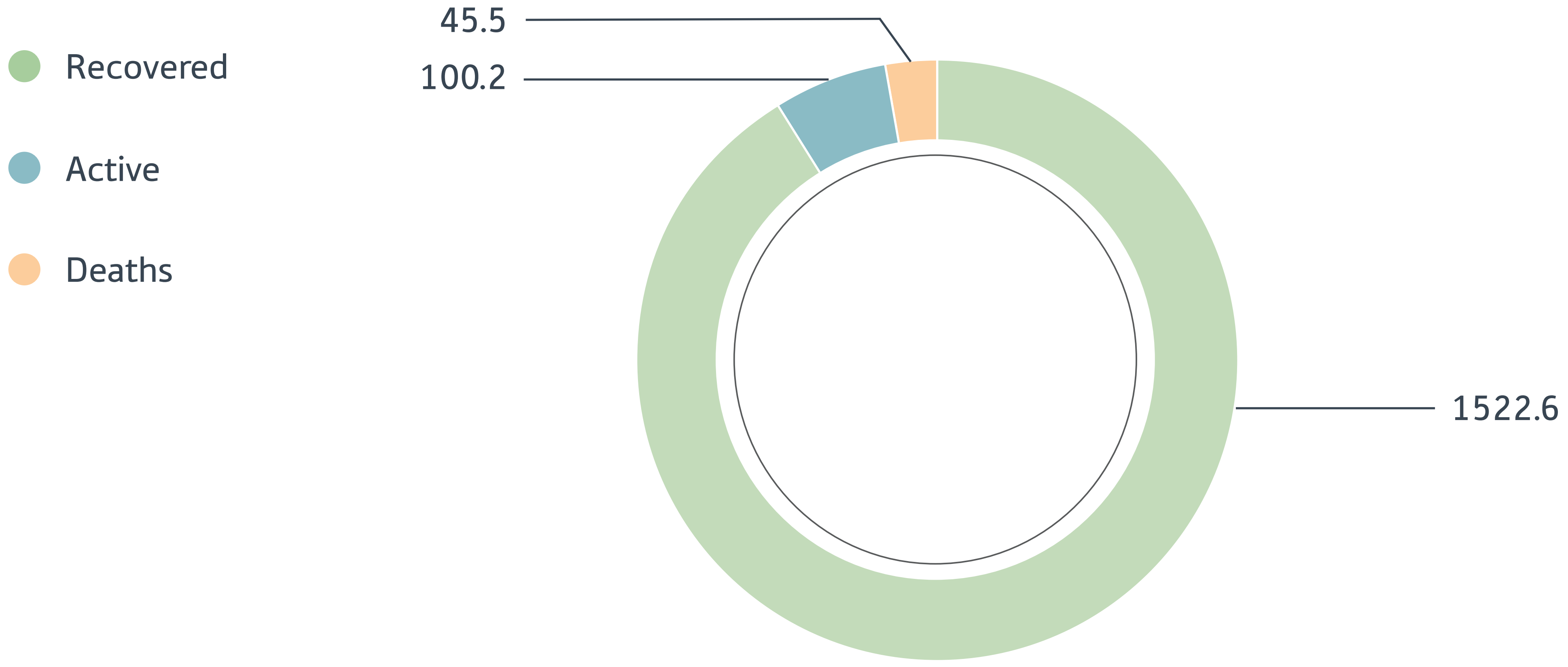
Financial support measures adopted by the Indonesian government in 2020



Health Measures

Indonesia's first two Covid-19 cases were confirmed in Jakarta on March 2, 2020; the country recorded its first Covid-19-related death nine days later, in Bali. Despite adapting restrictions at the local level in accordance with fluctuating case counts, Indonesia – like much of the rest of the world – had difficulty stemming transmission. After efforts to ramp up testing and facilitate the early identification of cases, Indonesia had confirmed almost 1.7m cases among its 270m-strong population as of April 30, 2021. By that date the fatality rate stood at 2.7%. Marking a step forwards for the country's health technology (health-tech) providers, the pandemic prompted the Ministry of Health (MoH) to issue Circular Letter HK.02.01/MENKES/303/2020, titled "Organisation of Health Services through the Utilisation of ICT to Prevent the Spread of Covid-19". Among other things, this clarified the authority of doctors to evaluate, diagnose and provide treatment for a patient's condition via health-tech solutions. The regulation was intended to reduce unnecessary physical interactions between health workers and patients, while also expanding access to health care. Meanwhile, the MoH partnered with private health-tech provider Halodoc and unicorn Gojek to facilitate remote diagnosis and treatment – underlining the public sector's commitment to leverage digital tools.

Breakdown of total cases in Indonesia as of April 30, 2021 (000)



Indonesia began work to develop a Covid-19 vaccine as early as April 2020 through collaboration between state-owned pharmaceutical company Bio Farma and Beijing-based biopharmaceutical company Sinovac. In January 2021 the government launched a campaign to vaccinate 181.5m Indonesians before the end of the year. By early February 2021 Indonesia was one of three ASEAN members, alongside Singapore and Myanmar, to have commenced vaccination – relying on imported Sinovac doses for the first phase of vaccination, before launching Bio Farma vaccines for the second phase in mid-February. By the end of March the country had vaccinated 1.2m health workers – 87% of the total – with two doses under the first targeted vaccination phase. Phase two, to inoculate 21.5m elderly persons and 17m public workers, commenced in February: 1.4m and 4.4m in this cohort, respectively, had received their first dose by the end of March. While India's embargo on exports of the AstraZeneca vaccine due to the country's own rising caseload posed a threat to Indonesia's ambitious goals, discussions with China for the supply of up to 100m additional Chinese-manufactured doses began in early April 2021.

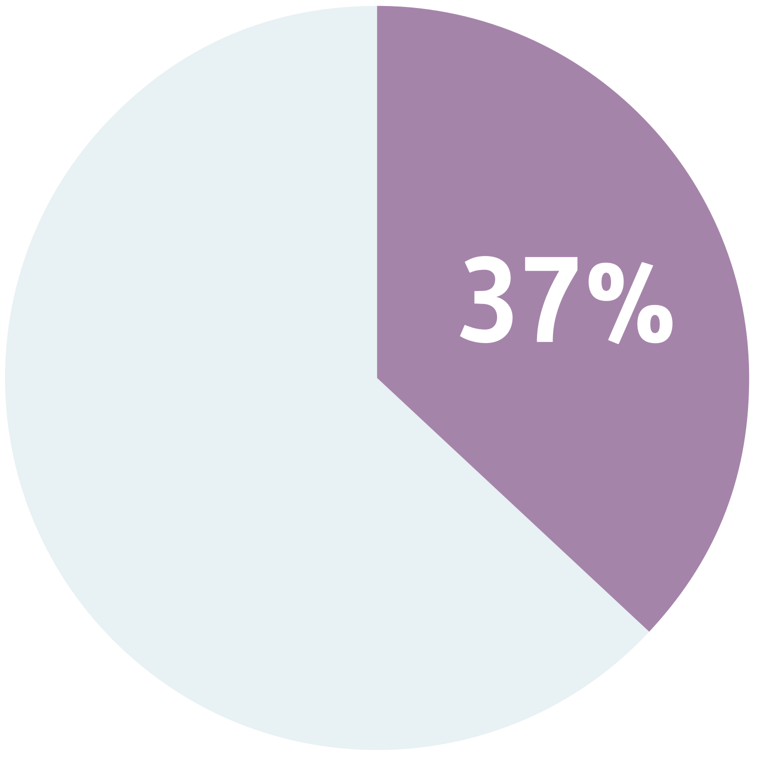
Graph source: *Our World in Data; Worldometer*

Accelerated Digitalisation

Adhering to social-distancing advisories, individuals and companies across Indonesia turned to digital tools for the completion of everyday tasks, spanning work, education, banking and commerce. This saw Indonesia account for approximately one-fifth of ASEAN's total internet economy during 2020, according to analysis by Bain & Company, published in a November 2020 report in conjunction with Google and Temasek.

A key growth opportunity in Indonesia's digital ecosystem is collaboration between traditional banks and financial technology (fintech) players, particularly for payments, lending and deposit services. Vital for meeting the Covid-19-related acceleration in digital financing demand, Indonesia's fintech ecosystem is supported by solid foundations, with 364 players in total as of April 2020. Peer-to-peer lenders accounted for 43% of this footprint, payment providers for 18% and digital finance innovators for 16%. The segment had witnessed a period of robust expansion prior to the pandemic: peer-to-peer lenders, for example, had distributed a total of Rp87.7trn by April 2020, marking a rise of around 86% compared to March 2019. Indonesians were swift to leverage these strong fundamentals: between March and May 2020, 65% of surveyed Indonesian consumers reported increased use of digital payments compared to pre-Covid-19 levels, according to a study from India-based management consulting company RedSeer. Other digital segments that saw a rise in online activity, according to the same report, were e-commerce (where 69% of respondents noted greater use), health-tech (41%) and education technology (38%).

The overwhelming majority of Indonesia's new digital consumers look set to stay. Of the country's total digital consumer base, roughly 37% had used digital services for the first time during the pandemic, and 93% of these new digital consumers expected to continue using at least one digital service after the pandemic. It seems, then, that the acceleration in digital services induced by the health crisis is paving the way for Indonesia's digital segment to play an increasingly critical role in everyday life in the coming years, with opportunities presented by the country's sizeable population and large, dynamic economy.



Share of digital consumers who used digital services for the first time during the pandemic

Share of new digital consumers who expect to continue using at least one digital service after the pandemic

Infographic source: *Google, Temasek and Bain & Company*

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Outlook and Growth Drivers

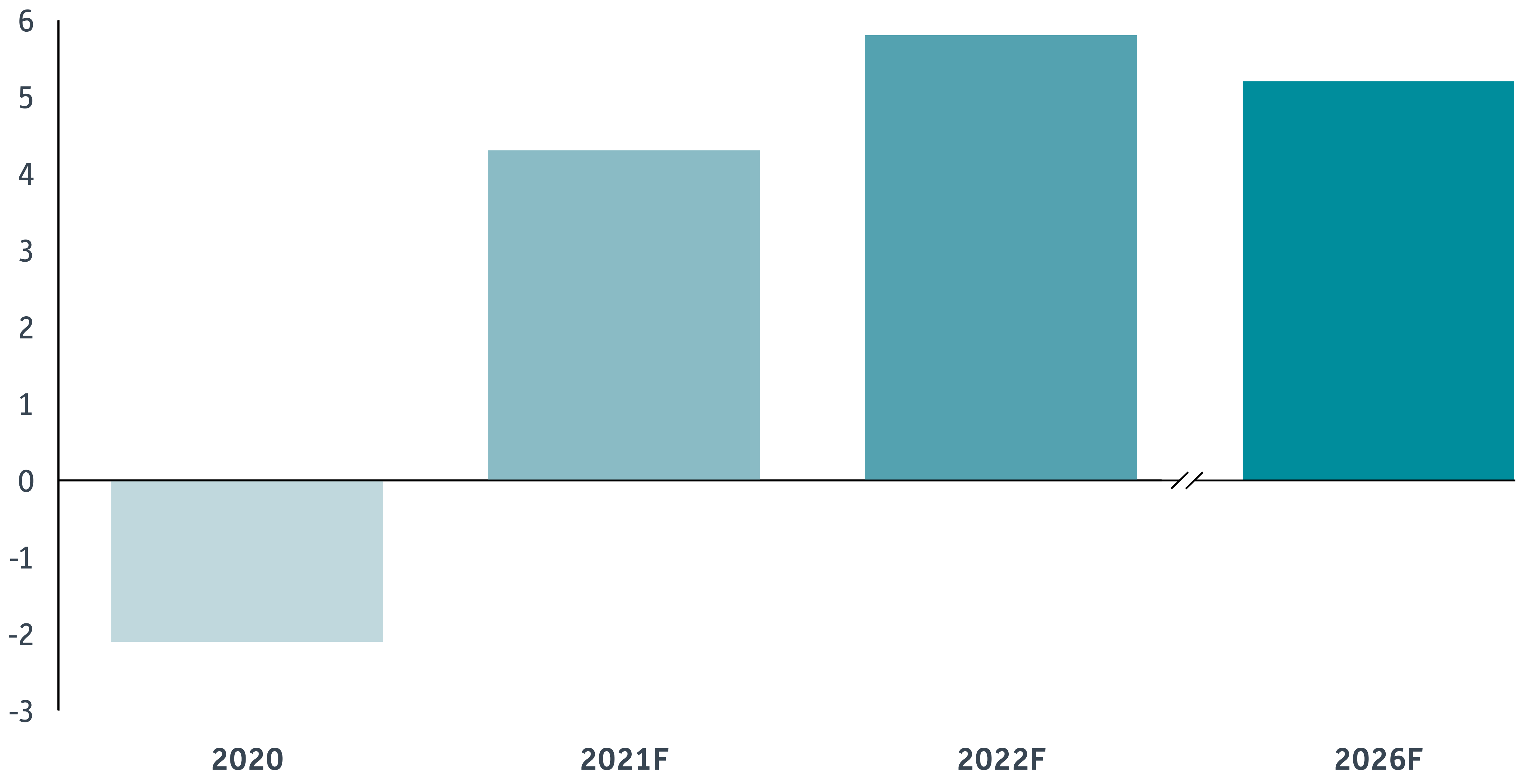
With a 2.1% contraction in real GDP, Indonesia's economy experienced a milder slowdown over 2020 than all of its ASEAN-5 neighbours, according to the IMF's April 2021 World Economic Outlook. Singapore, Malaysia, Thailand and the Philippines shrunk by 5.4%, 5.6%, 6.1% and 9.5%, respectively. Indonesia also fared better than 16 of its fellow G20 members. China – Indonesia's largest bilateral trade partner – led the group with 2.3% growth. Turkey was the only other member to expand, at a rate of 1.8%. Korea came in third place, with a contraction of 1%, followed by Indonesia (-2.1%), Australia (-2.4%), Russia (-3.1%) and the US (-3.5%). The remaining G20 economies slowed by more than 4% during the year.

In spite of ongoing Covid-19-related challenges, the IMF expects Indonesia's economy to rebound to 4.3% in 2021 and continue expanding to 5.8% in 2022 – which would mark the highest growth rate since 2012. With a 5.2% expansion predicted for 2026, the IMF underlines the sustainable growth potential of ASEAN's most populous member over the coming years.

Indonesia's digital economy is well placed to remain a key growth driver in 2021 and beyond, owing to its large, consumption-driven domestic market and the accelerated uptake of digital tools over 2020. Financial technology (fintech) and digital payments, e-commerce and food delivery, for example, look poised for ongoing expansion; these tools could widen financial inclusion, create jobs and offer a broader customer base for the country's micro-, small and medium-sized enterprises (MSMEs). The growth of Indonesia's digital economy should also help the country keep pace with the ever-evolving demands of the Fourth Industrial Revolution, characterised by the application of new digital and automated technologies in production processes and service delivery.

Alongside other fundamental growth strategies, including channelling investment into priority areas, and kick-starting construction and infrastructure development, Indonesia's digital economy looks set to boost the country's competitiveness and enable long-term, sustainable growth over the coming years.

Real GDP growth, 2020-26F (%)



Graph source: *IMF*

Digital Potential

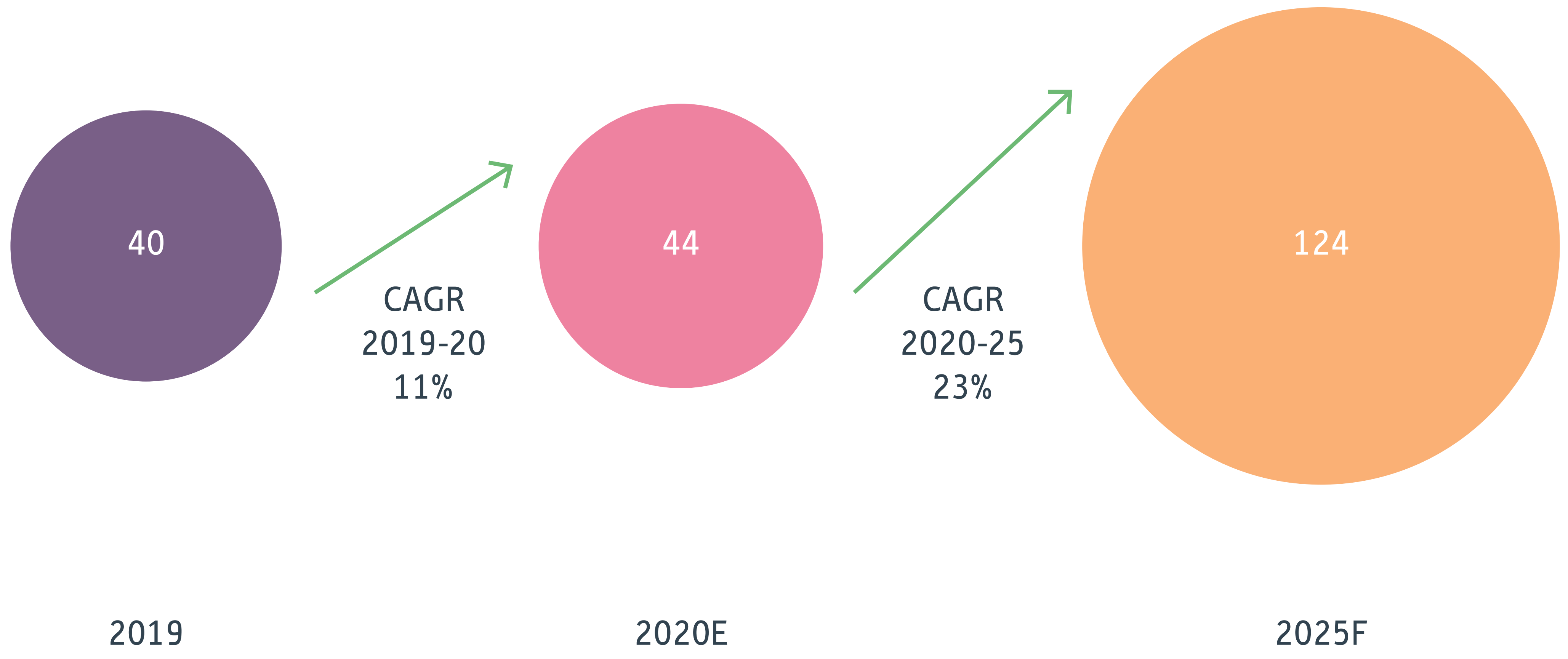
The digital economy, including the rising number of local MSMEs that rely on the segment, are a crucial source of employment in Indonesia: of around 70m Indonesians – or one-quarter of the population – employed in the informal economy, around 8m are freelance or gig-economy workers who drive the country's digital ecosystem. These include ride-hailing and delivery drivers, who are key to the success of the country's so-called "super apps" – online or mobile platforms that combine multiple services into one app.

In 2020 the government launched a Pre-Employment Card Programme to extend pandemic relief to the country's informal employees, as well as 5.6m laid-off workers and MSME business owners; in November of that year the programme's funding was doubled to Rp20trn – underlining the socio-economic significance of the group. This public sector commitment could prove vital in enabling Indonesia to realise its full digital potential – and reap the associated economic rewards – as the country's digital economy is on track to remain the largest and fastest-growing in South-east Asia over the coming years. During 2019-20 Indonesia's internet economy recorded a compound annual growth rate (CAGR) of 11%, rising from $40bn to $44bn, according to a November 2020 report by Google, Temasek and Bain & Company. The CAGR is forecast to rise to 23% over 2020-25, bringing the valuation to $124bn. This would see Indonesia account for 48% of ASEAN-5's digital economy at the end of the period, remaining over twice as valuable as Thailand, the group's second-largest digital economy with an estimated value of $53bn in 2025.

With Indonesian consumers becoming increasingly acclimatised to a range of digital tools, the digital ecosystem presents wide-ranging investment potential. This includes a robust fintech segment, which looks set to grow with institutional support from both Bank Indonesia – the central bank – and the financial services authority, Otoritas Jasa Keuangan (OJK); an expanding e-commerce ecosystem, which not only provides opportunities for local MSMEs, but also creates related demand for digital payments and delivery players; and agile super apps, which provide a range of services across the fintech, e-commerce and delivery value chain.

Indonesia's digital economy, 2019-25F

Gross merchandise value ($bn)



Graph source: *Google, Temasek and Bain & Company*

Case Study

Established in 1986, Inke Maris & Associates (IM&A) is a public relations (PR) consultancy that works with multinational and domestic companies, as well as public institutions. The firm specialises in public affairs, corporate communications and reputation management, and operates across a range of industries including ICT, health care and banking.

> The pandemic offered significant growth opportunities for enterprises that were able to quickly adapt to the changing environment

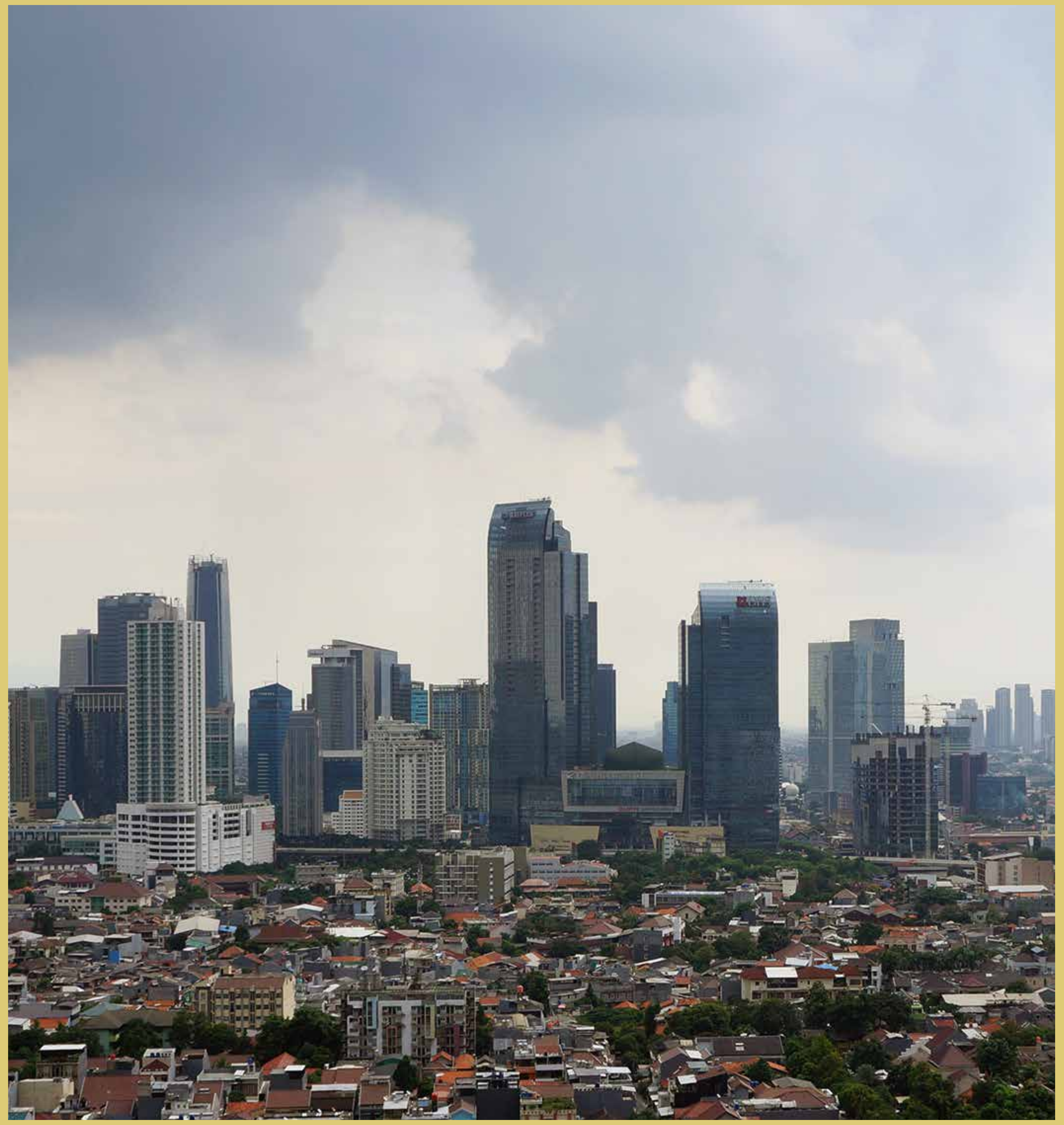
PR has evolved in recent years, and has begun to favour sector-specific strategies rather than the traditional universal approach. This enables companies to create more tailored and effective communications materials.

While it is uncertain when the global economy will fully recover from the Covid-19 pandemic, the health crisis underlined the importance of PR, as communications and reputation management emerged as fundamental strategic elements throughout the pandemic.

Indonesian companies introduced a range of initiatives to adapt their business strategies and enable operational continuity throughout 2020. IM&A launched a strategy to capitalise on emerging digital opportunities. The initiative had four parts: new ways of work, including an online and offline system and reporting structure, and rotating on- and off-site staffing; the development of digital services including fully virtual and hybrid models; marketing to educate clients and encourage them to launch communications initiatives; and regular internal communication via Zoom.

The company also launched a digital talk show called IMA Afternoon Talks to build its clients' brand awareness, while fostering relationships with industry experts, clients and other businesses. IM&A expects to continue to pursue similar initiatives aimed at serving the community in 2021, as well as target additional opportunities in health care and consumer lifestyle.

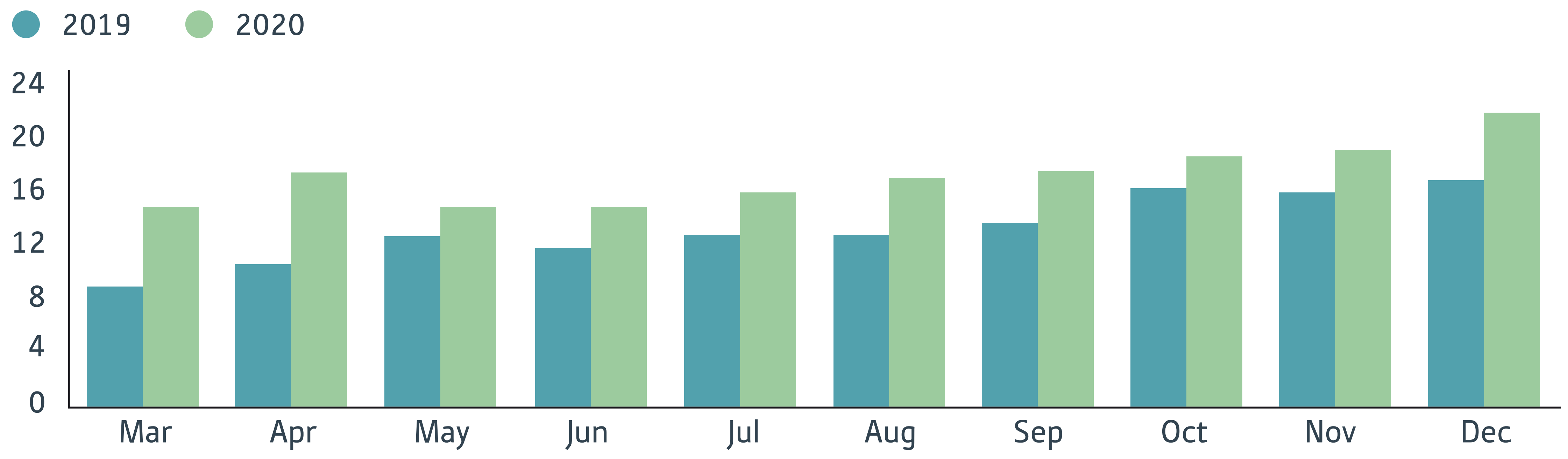
"As witnessed during previous crises, the pandemic offered significant growth opportunities for enterprises that were able to adapt quickly to the changing environment," Isma Natanegara, CEO of IM&A, told OBG. "We have also seen how important the PR and communications industry has been in responding to the crisis, and it is expected that PR will be increasingly important for companies' operations across the Indonesian economy in the future."



Fintech

Indonesia's burgeoning fintech ecosystem was bolstered in 2020 by actions to support digital payments, which enabled the contactless transferral of funds amid the health threat and helped to increase Indonesia's digital competitiveness for the long term. Bank Indonesia, for example, supported cashless social aid programme disbursements; provided payment system infrastructure to aid the digitalisation of MSMEs under the Made in Indonesia Movement; and launched a standardised, interoperable, national QR code system. Furthermore, the central bank lowered fees for digital payments and enhanced collaboration with fintech players. This has paved the way for digital tools to support financial inclusion efforts over the coming years. In August 2020 the OJK launched the Digital Finance Innovation Roadmap and Action Plan 2020-24, which aims to ensure stable digital financial services with appropriate risk-management practices; support digital financial services that empower Indonesians and extend financing to MSMEs; and enable inclusive financial services that are affordable, convenient and scalable.

Indonesia's e-money transactions, 2019-20 (Rp trn)



Case Study

Sucor Asset Management

Sucor Asset Management has managed public funds in Indonesia since obtaining an asset management licence in 1999.

Several new partnerships were established with banks and selling agents between 2016 and early 2020, before the Covid-19 pandemic reached the country. In addition to growing the value of the company's assets under management, these partnerships helped Sucor Asset Management's customer base shift to the retail segment, enabled the online onboarding of new customers, and facilitated digital transactions – which proved particularly important during the year amid lockdowns and social-distancing regulations.

The firm implemented remote working early in 2020 to ensure the continuity of business operations. Retaining this model, engagement activities with partners and investors are expected to take place through virtual meetings and social media until at least the end of 2021, at which point Sucor Asset Management plans to continue communications with stakeholders through a variety of channels.

Looking towards potential growth avenues over the course of 2021, an increase in the number of domestic investors is expected to drive expansion in Indonesia's environmental, social and governance (ESG) arena, as well as in the sharia investment ecosystem. Sucor Asset Management, now having developed the required infrastructure for sustainable investments, intends to launch an ESG fund and sharia products in 2021.

"Aligned with the general industry trend, continuous innovation and consistent performance will remain priorities," Jemmy Paul Wawointana, CEO of Sucor Asset Management, told OBG. "Despite pandemic-related restrictions and limitations, we will also continue working to increase transparency for the benefit of all stakeholders, as well as boost inclusion through strategies such as financial education programmes delivered via social media."

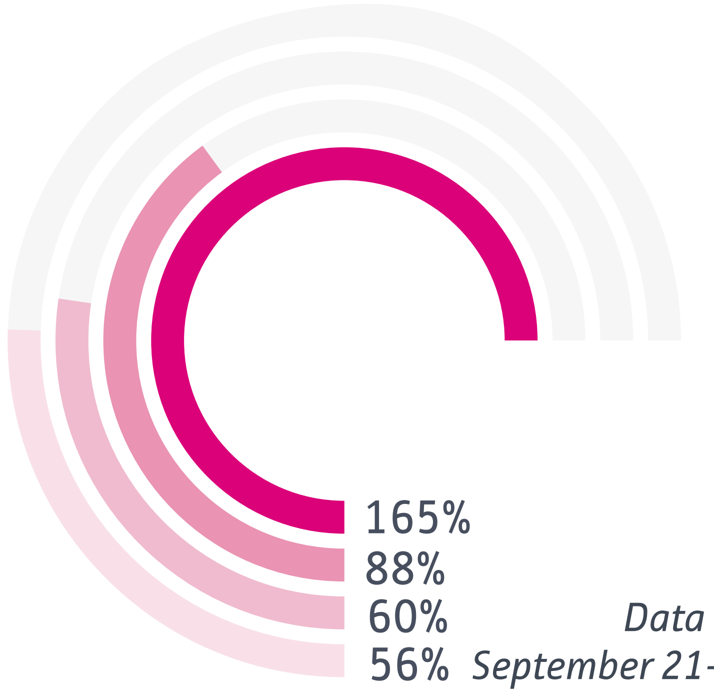
Graph source: *Bank Indonesia*

E-commerce

Over half of Indonesian consumers tried a new digital shopping method during the first six months of the pandemic, according to a McKinsey survey published in November 2020. Furnishings and appliances, groceries and medicine were among the segments that recorded considerable growth as Indonesians spent more time at home; this facilitated a 54% CAGR in the gross merchandise value of e-commerce purchases in Indonesia, which rose from $21bn in 2019 to approximately $32bn in 2020, according to the November 2020 report from Google, Temasek and Bain & Company. The overwhelming majority of new digital commerce users – at 88% – intend to continue using this method, according to the same McKinsey study, after the Covid-19 period. The pandemic-related increase in online commerce consumers has laid the foundation for long-term growth: it is forecast that Indonesia's e-commerce segment will enjoy a CAGR of 21% over 2020-25, to reach $83bn. As the reach of digital commerce expands, this will present a range of digital payments opportunities for fintech players, grow delivery demands for super apps and other courier services, and widen the consumer base for MSMEs across the country.

Consumers plan to sustain higher e-commerce usage in Indonesia

- Consumers who tried a new digital shopping method over the pandemic period
- Growth in consumers who purchase online for most types of products
- Consumers who intend to continue using a new digital shopping method
- Growth in consumers who purchase largely or wholly online, across product categories



Data collected September 21-30, 2020

Case Study

Depo Bangunan (Depo) is an Indonesian building materials one-stop solution for buildings and renovations. Established over 24 years ago, Depo is the second-largest building materials retailer in the country by sales volume.

The Indonesian ceramics industry is the sixth-largest in the world, with two-thirds of output sold to the domestic market, and an anticipated compound annual growth rate of around 9% between 2017 and 2025. By March 2020, however, roughly 50% of Indonesian ceramic companies halted production due to Covid-19-related restrictions. Production generally resumed in June that year, with capacity reduced to an average of 30%. Many local manufacturers reshaped their corporate strategy due to the disruptions to global supply chains.

While the value of real estate construction activity in the country decreased in 2020, the number of projects remained constant, and public projects proved more resistant to the pressures of the crisis than private projects. To fuel private sector activity during the period, the government introduced policies aimed at lowering gas prices – which enabled industry players to reduce their overheads by around 15% – and boosting regional financial incentives.

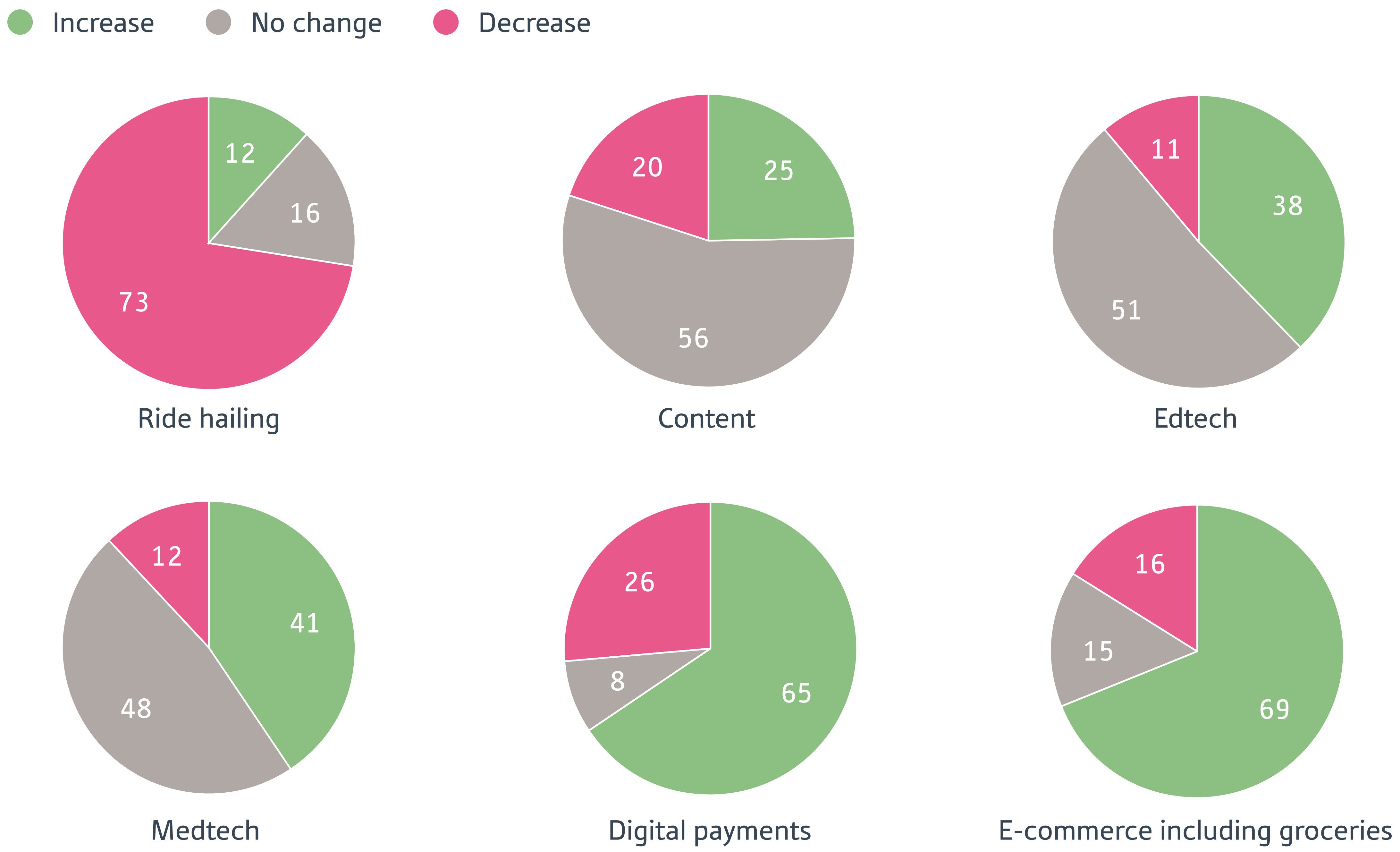
Depo experienced increased demand for high-end products in 2020, accompanied by decreased demand for low-end items. This suggests that, despite economic pressures, consumers were willing to invest in their homes, where they were required to spend significant amounts of time during lockdowns. Meanwhile, Depo's online sales rose from 0% to 7% within the first month of the pandemic. Like other companies, Depo leveraged digitalisation to enable business continuity during the crisis: orders were placed through WhatsApp and payments processed thereafter via bank transfers. Companies that demonstrated such flexibility will be well positioned to adapt to changes in the post-pandemic era, which is likely to prove one of 2020's greatest lessons.

Graph source: *McKinsey*

Super Apps

Covid-19-related challenges and movement restrictions forced Indonesia's super apps to reorganise their operations and close some services. For instance, Gojek – which initially launched to provide ride-hailing services via a call centre in Jakarta in 2010, before broadening its service offering by launching a mobile app and extending into new markets – announced in June 2020 that it would lay off 9% of its workforce, equivalent to 430 employees. The homegrown super app also announced the closure of GoLife, which offered household cleaning and on-demand massage services, and GoFood Festivals, which operated physical food halls. Underlining its agility amid the challenging conditions, Indonesia's first decacorn – or company valued at $10bn – recorded a 10% increase in its annualised gross transaction value (GTV) in 2020, supported by a five-fold increase in GTV for its grocery services and an 80% spike in registered customers using its GoFood restaurant delivery service.

Indonesian consumers turned to digital solutions, May 2020 (% change compared to pre-pandemic times)



As another promising sign for Indonesia's super apps, as well as the gig economy workers who rely on them for employment, Singapore-headquartered super app Grab announced in April 2021 that it would launch on the New York Stock Exchange via a special purpose acquisition company (SPAC), or blank-cheque company. With a valuation of approximately $39.6bn, this marks the world's largest SPAC listing thus far, and underlines investor confidence in the region's digital economy.

According to local media, the Indonesia Stock Exchange plans to implement SPAC regulations by July 2021, signalling further opportunities for the country's technology players down the line. These developments are expected to reassure international investors of the dynamism of Indonesia's burgeoning tech ecosystem and underscore the potential for digitally enabled, inclusive growth over the coming years.

Graph source: *RedSeer*

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Construction-driven Growth

Construction looks set to be another key driver of sustainable growth over the coming years, amid the government's renewed commitment to increase infrastructure spending. After slight growth of 0.2% in 2020, Indonesia's construction industry is expected to register a 5.1% expansion over 2021, according to a January 2021 forecast from the South-east Asia Iron and Steel Institute. With Indonesia aiming to complete 4900 infrastructure packages in 2021, early bidding was already under way for 1900 projects as of November 2020. Meanwhile, Rp414trn was earmarked for construction in the 2021 budget: over one-third of this was allocated to the Ministry of Public Works and Housing. Moreover, the government plans to issue Rp27.6trn in *sukuk* (Islamic bonds) during 2021, for the financing of 870 infrastructure projects.

As part of a wider trend, construction looks set boost intra-regional trade and facilitate domestic travel over the coming years as ASEAN authorities work to address the region's infrastructure deficit and promote sustainable, long-term growth.

Indonesia's construction industry is poised for growth

+ 0.2% growth

2020

+ 5.1% expected growth

2021

Rp414trn for construction in 2021 budget

Early bidding under way in November 2020 for 1900 of 4900 total planned 2021 infrastructure packages

Government plans to issue Rp27.6trn in sukuk in 2021 to finance 870 infrastructure projects

Case Study

nyaman

L&M Systems Indonesia (L&M) is a construction company with over 25 years of experience in infrastructure projects across the country, mostly related to ports, toll roads, and the normalisation of rivers and dams. Although measures to protect the health of the population were prioritised during the Covid-19 period in 2020, the government nevertheless strived to meet predetermined deadlines for infrastructure projects that had commenced before the onset of the pandemic, as well as those that were not yet under way. However, the costs associated with public health efforts resulted in inevitable delays to infrastructure payments. This led many construction companies, including L&M, to focus on private contractors, since these players were generally better positioned to release expenses than public sector contractors.

Due to the financial strain caused by the pandemic, the government suggested that companies grant payment extensions to clients. Although Indonesian players sought financing from local banks to facilitate this, many financial service providers were unwilling to lend companies the necessary funds due to the perceived lack of liquidity in the system. A healthy cash flow thus became vital for companies operating in the country – particularly in capital-intensive industries such as construction.

To mitigate liquidity challenges during the Covid-19 period, L&M shifted 30% of its resources to the business-to-consumer (B2C) market with the introduction of its mobile app *nyaman* (comfort). The B2C segment has shorter collection periods than the business-to-business (B2B) space: B2C collections average seven days, compared to three to six months for B2B collections. While the B2B market remains the backbone of the company's revenue stream, B2C is growing rapidly and looks poised for continued expansion in the years to come – offering an opportunity to boost growth after the pandemic.

Infographic source: *SEASISI*

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Bahlil Lahadalia

Minister of Investment

To what extent did the Covid-19 pandemic impact investment inflows, and which areas of the archipelago saw the most investment activity?

Despite the pandemic, Indonesia exceeded its target of Rp817trn of investment in 2020, reaching Rp826.3trn. The inflows were almost equally balanced between foreign direct investment (FDI) and domestic direct investment (DDI): FDI accounted for Rp412.8trn, or 49.9%, of the total, while DDI comprised Rp413.5trn, or 50.1%. Areas beyond Java enjoyed marginally higher levels of investment than the archipelago's most populous island over the course of the year, with investment outside Java reaching Rp417.5trn, or 50.5% of the total. Indeed, the provinces around Java no longer rank among the top-five destinations for investment. West Java led with \$4.8m, the capital region of Jakarta placed second, with \$3.6m, and North Maluku received the third-highest FDI allocation (\$2.4m). Java's Banten province received the next-largest allocation, at \$2.1m, followed by Central Sulawesi, with \$1.8m. This breadth highlights the potential for investment to enable inclusive growth across the archipelago.

How can the Regional Comprehensive Economic Partnership (RCEP) encourage investment?

The November 2020 signing of the RCEP by ASEAN members and their dialogue partners further expanded opportunities for financing in Indonesia. The country will now have access to a larger market, as member countries account for one-third of the world's population and 29% of global GDP. In terms of maintaining competitiveness, Indonesia's focus on downstream natural resources – primarily nickel and other minerals used for batteries – has strengthened its position in the global supply chain, particularly in light of the green revolution that is currently under way. Moreover, Indonesia enhanced its investment climate with the November 2020 enactment of the Omnibus Law on Job Creation.

What are the segments and activities that have the greatest potential to boost investment and support sustainable growth?

We aim to transform Indonesia from a country that largely exports raw commodities into one that leverages downstream processing to support value-added production. The Indonesia Investment Coordinating Board (BKPM) has been channelling investment into priority areas, especially export-oriented and labour-intensive industries such as pharmaceuticals and health equipment, automotive, electrical products, construction, energy and mining. Downstream nickel activity is emerging as a major investment opportunity: global players, including Contemporary Amperex Technology and LG Chem, have made, or expressed an interest in making, investments in the country. Additionally, infrastructure development is ongoing across the archipelago, primarily in eastern Indonesia. BKPM has prioritised collaboration with micro-, small and medium-sized enterprises (MSMEs), and has matched 56 FDI and DDI companies with 196 local MSMEs in several sectors. To support smaller firms further, BKPM ensured that every beneficiary of investment incentives – whether tax holidays, tax allowances or exemptions from import duties – works with MSMEs and entrepreneurs to encourage the even distribution of funding across the archipelago, create jobs and enable a swift recovery.

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