WORLD BANK GROUP

IEP INDONESIA ECONOMIC PROSPECTS

People-First Housing: A Roadmap from Homes to Jobs to Prosperity in Indonesia

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The report was designed and typeset by Arsianti.

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Preface

The Indonesia Economic Prospects (IEP) is a bi-annual World Bank report that assesses recent macroeconomic developments, the outlook, and risks, as well as specific development challenges for the Indonesian economy. The IEP aims to inform the public policy debate and serves a broad audience including the general public, government, private sector, civil society organizations, and other domestic and international stakeholders.

The IEP is a product of the World Bank Jakarta office and receives strategic guidance from an editorial board chaired by Carolyn Turk, Country Director for Indonesia and Timor-Leste. The report is prepared by the Macroeconomics, Trade and Investment (MTI) Global Practice team, under the guidance of Lars Christian Moller (Practice Manager), Bjorn Philipp (Practice Manager) and Habib Rab (Lead Economist). The report is led by Wael Mansour (Senior Economist) and Luis Miguel Triveno Chan Jan (Senior Urban Development Specialist) .

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This report is available for download in English and Indonesian via: www.worldbank.org/iep
Previous report editions:

- December 2024: Funding Indonesia's Vision 2045
- June 2024: Unleashing Indonesia's Business Potential
- December 2023: Climate Action for Development

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Abbreviations and Acronyms

ADIA	Abu Dhabi Investment Authority
APBD	*Anggaran Pendapatan dan Belanja Daerah*
AI	Artificial Intelligence
BI	Bank Indonesia
BPS	*Badan Pusat Statistik*
BPJS	*Badan Penyelenggara Jaminan Sosial*
BP TAPERA	*Badan Pengelola Tabungan Perumahan Rakyat*
BSPS	*Bantuan Stimulan Perumahan Swadaya*
BTN	*Bank Tabungan Negara*
BULOG	*Badan Urusan Logistik*
BUMD	*Badan Usaha Milik Daerah*
BUMN	*Badan Usaha Milik Negara*
CAD	Current Account Deficit
CAR	Capital Adequacy Ratio
CDS	Credit Default Swap
CIO	Chief Investment Officer
CPI	Consumer Price Index
CPO	Crude Palm Oil
CSH	Contract Savings for Housing
CTAS	Core Tax Administration System
DAU	*Dana Alokasi Umum*
DAK	*Dana Alokasi Khusus*
EAP	East Asia Pacific
EMCI	Emerging Market Currency Index
EMDEs	Emerging Market and Developing Economies
FDI	Foreign Direct Investment
FFR	Federal Fund Rate
FLPP	*Fasilitas Likuiditas Pembiayaan Perumahan*
FX	Foreign Exchange
FSAP	Financial Sector Assessment Program
GDP	Gross Domestic Product
GEP	Global Economic Prospects
GOI	Government of Indonesia
GRM	Grievance Redress Mechanism
HREIS	Housing and Real Estate Information System
ICT	Information, Communication, and Technology
IDR	Indonesia Rupiah
IEP	Indonesia Economic Prospects
IMF	International Monetary Fund
INA	Indonesia Investment Authority
Jabodetabek	Jakarta Bogor Depok Tangerang Bekasi (Jakarta Metropolitan Area)
JKP	Job Loss Guarantee Program
JKN	*Jaminan Kesehatan Nasional*
KOTAKU	*Kota Tanpa Kumuh*
KUR	*Kredit Usaha Rakyat*
LAR	Loan-at-Risk
LCR	Liquidity Coverage Ratio
LDR	Loan-to-Deposit Ratio
LMAN	*Lembaga Manajemen Aset Negara*
LMIC	Lower-Middle Income Countries
LNG	Liquified Natural Gas
LPG	Liquefied Petroleum Gas
LVC	Land Value Capture
MBG	*Makan Bergizi Gratis*
MBR	*Masyarakat Berpenghasilan Rendah*
MIS	Management Information System
NAHP	National Affordable Housing Program
NPL	Non-Performing Loan
NSFR	Net Stable Funding Ratio
NTMs	Non-Tariff Measures
OECD	Organization for Economic Co-Operation and Development
OJK	*Otoritas Jasa Keuangan*
OPEC+	Organization of the Petroleum Exporting Countries and 10 Additional Non-OPEC Countries
Perda	*Peraturan Daerah*
PLM	*Penyangga Likuiditas Makroprudensial*
PRONA	*Proyek Operasi Nasional Agraria*
PSR	*Program Sejuta Rumah*
RDTR	*Rencana Detail Tata Ruang*
RISHA	*Rumah Instan Sederhana Sehat*
ROA	Return-on-Assets
ROE	Return-on-Equity
RPLN	*Rasio Pendanaan Luar Negeri*
RPPI	Residential Property Price Index

RP3KP	*Rencana Pembangunan dan Pengembangan Perumahan dan Kawasan Permukiman*
RRR	Reserve Requirement Ratio
RTRW	*Rencana Tata Ruang Wilayah*
RumahQu	Housing Queue
RUSPIN	*Rumah Unggul Sistem Panel Insan*
Satker	*Satuan Kerja*
SIAP	*Sistem Informasi dan Perencanaan Terpadu*
SMF	Secondary Mortgage Facility
SNI	*Standar Nasional Indonesia*
SOEs	State-Owned Enterprises
SRBI	*Sekuritas Rupiah Bank Indonesia*
SWFs	Sovereign Wealth Funds
UMIC	Upper-Middle Income Countries
US	United States
USD	United States Dollar
UST	United States Treasury
VAT	Value-Added Tax
YOY	Year-on-Year

Executive Summary

Executive Summary

I. Economic Update

Indonesia's economy remains resilient amid worsening global conditions. GDP grew at 4.9 percent year-on-year (yoy) in Q1-2025, slightly lower than previous post-pandemic quarters. Domestic demand was impacted by reduced government consumption and lower investment. Budget efficiency measures led to a contraction in public consumption, while investment in construction and manufacturing sectors dipped due to investors' concerns over domestic and global policy uncertainty. Meanwhile, declining commodity prices worsened Indonesia's terms-of-trade. The supply side showed notable contributions from agriculture and services sectors. Favorable climate conditions led to a significant rebound in food and crop production, which helped contain food prices and maintain headline inflation at the lower end of Bank Indonesia's (BI) target range [2.5±1 percent].

Businesses and households are adjusting to economic uncertainty but weak consumption of middle class households has been persistent since the pandemic. Businesses are facing liquidity challenges, and manufacturers are reducing inventory and hiring to sustain operations. Household savings are decreasing, particularly for low and middle-income families, with consumers turning to safe-haven assets like gold and property. Lagging consumption of the middle class has been persistent since the pandemic. From 2019 to 2024, inflation-adjusted consumption of middle-class households grew by only 1.3 percent per year compared to 2-3 percent for both the poorest and richest groups. While the poor have benefitted from social assistance, the lack of quality jobs is limiting income growth for middle-class workers. Despite rising job creation and labor force participation, 52 percent of new jobs created last year were in low value-added sectors.

Fiscal policy has adjusted to create space for priority programs and consumption stimulus packages amid revenue shortfalls. Tax and non-tax revenues declined due to temporary factors like technical glitches associated with the implementation of the Core Tax, a comprehensive digital system to modernize and integrate Indonesia's tax administration. Other factors include larger-than-expected tax rebates, as well as forgone revenues from SOE dividends, reversal of the VAT rate hike, lower commodity prices, and softer domestic demand. To address revenue shortfalls and create fiscal space for priority programs, budget efficiency and reallocation measures (of 1.3 percent of GDP) were implemented. Cuts were made in ministries involved in public investment and to sub-national transfers for infrastructure projects, raising potential long-term growth tradeoffs. By May, those measures had largely balanced the budget.

Monetary policy is easing to support growth after the Rupiah stabilized following BI intervention. Global financial volatility has affected FDI and the equity market, causing capital outflows and pressuring the Rupiah, which hit a historical low in April. This prompted BI to intervene, and the currency recovered by 2.2 percent month-on-month in May. FX reserves dropped as a result but remained adequate, covering 6.2 months of imports and debt repayments. Despite this, monetary policy eased gradually amid low inflation conditions with BI lowering the policy rate twice this year by 25 bps each. BI also eased some macroprudential measures and injected liquidity through open market operations.

In the medium-term, Indonesia's economy will continue to grow despite downside risks that require prudent macro management. Global policy uncertainty is expected to impact global demand, including that of Indonesia's main trading partners. Nevertheless, Indonesia's medium-term growth is expected to remain resilient, with projections averaging 4.8 percent annually over 2025-2027. Growth will be driven by private consumption, which will benefit from low inflation and social assistance programs, as well as investment which is expected to pick up with the government's housing program and projects from Danantara, the new sovereign wealth fund and super-holding company for State Owned Enterprises. Prudent fiscal policy is anticipated to keep the deficit around 2.7 percent of GDP, with spending expected to gradually increase by 2027 due to rollout of priority programs and rising interest payments. The GOI plans to finance this by taxing digital transactions, raising mineral and coal royalties, improving tax administration, and using big data for better tax enforcement. Meanwhile, external financing needs will gradually rise due to a widening current account deficit and increasing public debt amortization.

The GOI structural reform agenda could accelerate growth further. In response to rising global policy uncertainty, the GOI devised a program of deregulation including reforms to the business environment and licensing, investment liberalization, trade and logistics reforms, and digital services. These reforms complement other reforms currently in play, like those related to financial sector deepening, and accompany the demand stimulus that the GOI is targeting through its priority programs. If implemented, these reforms could gradually expand the economy's capacity, unlock further FDI, boost investment returns, and ensure productivity gains. The report simulates that this will translate into better jobs creation and raise GDP growth to 5.3-5.5 percent in 2026-2027.

Four policy priorities emerge though in times of rising uncertainty. First, deregulate trade and investment by removing unnecessary non-tariff measures (NTMs), streamlining import approvals, inspections, and certifications, relaxing burdensome local content requirements, and improving the national logistics ecosystem. Targeted NTM reforms could boost total exports by 10 percent and investment by 27 percent over the medium-term. Second, sustain strong policy communication, where the authorities have a strong track record. Clear policy communication and timely macro-fiscal data publication reduce market uncertainty. Third, protect capital spending. Cross-country analysis reveals that a US$1 cut in public investment could lower GDP by US$1.3 in the long-term, highlighting the need for ringfencing infrastructure and human capital investment to attract private investors. Fourth, ensure the success of Danantara with a clear strategy, effective governance, transparency, and adherence to international best practice.

II. A Roadmap from Homes to Jobs to Prosperity in Indonesia

President Prabowo has articulated bold objectives for Indonesia's future. Central to these plans are investments in housing and infrastructure, and a target to deliver 3 million housing units annually. Achieving the annual housing target will be critical to Indonesia's long-term prosperity, as well as for the health and economic growth of its population. The objective will only be attainable through a series of specific, targeted reforms, investments, and policies designed to maximize the impact of every dollar spent.

Housing construction is an engine of growth for Indonesia's economy and a source of prosperity for its people. It contributes 10 percent to Indonesia's GDP, providing 7 percent of total employment and augmenting national tax revenues by 8 percent. Safe housing complements President Prabowo's commitment to childhood and family health by lowering disease rates and mitigating climate and hazard risks. It boosts the construction and banking sectors while also improving educational opportunities for students, thereby strengthening the potential of the Indonesian workforce. For example, families living in homes with dirt floors are more exposed to illness, extreme weather, and other hazards, lowering both their health and educational outcomes. Approximately 45 percent of Indonesians live in homes with lead paint. Lead exposure is a serious health concern, especially for children, and can cause developmental delays, learning disabilities, and stunting.

This report identifies the necessary steps to reach the target of providing 3 million housing units each year. In short, to meet the housing target and supercharge current efforts, the government needs to act as both a housing provider and a housing facilitator: instituting housing regulation reforms, accelerating public funded housing programs, and creating an enabling environment that attracts private investment in Indonesia. Directly, US$3.8 billion in annual public investments can create an estimated 2.3 million jobs and mobilize US$2.8 billion in private capital. Reforms can create an enabling environment for housing investments and indirectly help multiply this impact.

The report proposes a two-pillar strategy. The first pillar focuses on housing and infrastructure investments, while the second pillar elaborates on the policy and institutional reforms needed to secure financing and sustainability of the 3 Million Housing Program.

The first strategy provides options to deliver better housing, new housing, and the supporting infrastructure needed to ensure resilience and livability. It builds on Indonesia's longstanding record of success in housing and settlement upgrading by pursuing a local, next-generation settlement and neighborhood transformation to create 750,000 jobs and deliver 1 million homes with US$1 billion of government investments. To reach the targeted economic growth rate of 8 percent will require housing production in urban centers to lead the way with a different approach, given their limited land and higher housing costs. Urbanization can lift millions out of poverty through increased employment opportunities and higher wages. For example, workers in Indonesia's urban areas earn on average 40–50 percent more than comparable rural workers, reflecting the higher productivity and concentration of economic opportunities in cities. Between 2001 and 2017, the urbanization process was accompanied by a reduction in poverty by 23 percentage points. Furthermore, investments in denser, resilient housing construction, expanded public transportation, and other infrastructure can lower housing costs and protect people and their assets.

The second strategy focuses on securing the financing required to meet the needed rate of housing expansion by increasing families' savings and access to private capital through targeted policies and reforms. With the right support, many families can afford to improve or buy their own home.

This report offers a practical, step-by-step blueprint for maximizing every dollar spent, attracting the required billions in private capital, and accelerating housing efforts in every community across Indonesia. With the right investments and reforms, it is possible to build safer homes, a stronger economy, and a "Golden Future" for all Indonesians.

Table ES.1: Static Simulation of 3 Million Housing Program: Before (2023) and After Comparison.

Indicator	Before	After
Private Capital Mobilization (US$ Million)	560	2,777
Jobs Created	868,151	2,336,616
Better Housing / Total Housing Volume Share	39%	71%
Better Housing / Total Housing Budget Share	**9%**	**28%**
New Housing / Total Housing Volume Share	61%	29%
New Housing / Total Housing Budget Share	**91%**	**72%**
Government Budget (Rp Trillion)	35.54	62.79
Government Budget (US$ Billion)	2.15	3.81
Total Number of Units Supported/Achieved	**386,222**	**1,200,000**

Note: Government programs support 36.2 percent (2015-2024) of the housing solutions delivered in the country.
Source: Ministry of Housing and Settlements (2025); Performance Reports of Directorate of Implementation of Housing Finance and Directorate General of Infrastructure Financing, Ministry of Public Works and Housing (2023); World Bank Staff calculation.

A. Economic Update

A. Economic Update

1. Recent Economic Developments

Global economic conditions have deteriorated with global policy uncertainty on the rise.

With rising uncertainty, global growth is projected to slow. Global policy uncertainty, geopolitical risks, and rising trade barriers are projected to reduce global growth to 2.3-2.4 percent in 2025-26 from previous estimates of 2.7 percent (World Bank GEP June 2025). Developing East Asia and the Pacific (EAP) continues to outpace global growth but faces challenges from lower private consumption and a subdued outlook in China. While exports in manufacturing and services have supported growth, private investment remains weak across much of the region. Growth in EAP is projected to slightly moderate to 4.5 percent this year due to economic policy uncertainty and weaker external demand. These trends are likely to hinder progress for emerging markets and developing economies (EMDEs) in closing per capita income gaps with advanced economies and reducing extreme poverty.

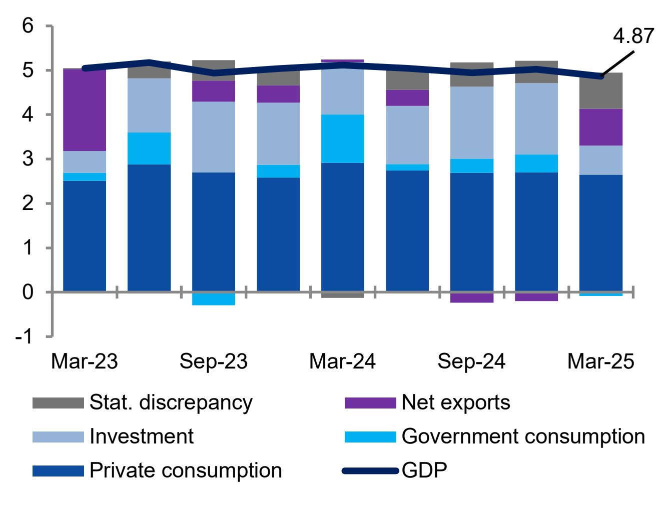
Indonesia's domestic demand is moderating with softening consumption and investment, whilst agriculture is rebounding strongly and offsetting part of the slowdown in industry.

GDP growth recorded 4.9 percent year-on-year (yoy) in Q1-25, slightly lower than previous post-pandemic quarterly growth rates (Figure A.1). While private consumption was supported by stronger purchasing power in rural areas due to rising agricultural output, domestic demand was impacted by reduced government consumption and lower investment. The government's budget efficiency measures led to a contraction in public consumption, while investment in construction and manufacturing sectors dipped due to investors' concerns over domestic and global policy uncertainty. Meanwhile, net exports contributed a notable 17 percent to GDP growth.[1] This improvement is temporal as exports were frontloaded early in the year in anticipation of the global tariff hikes. Rising exports outweighed lower imports of foodstuffs, as domestic agriculture production picked up, as well as lower imports of consumer goods.

On the supply side, services and agriculture are driving growth while manufacturing industry is slowing down. Trade, hospitality, transport, communications, and financial services accounted for 45 percent of Q1-25 growth (Figure A.2). Meanwhile, agriculture production rebounded across various categories. Food and plantation crops grew by 43 and 22 percent yoy, respectively, while livestock grew by 9 percent. Authorities reported 14 million tons of rice production in Q1-25 (up 26 percent yoy), the highest in the last seven years. This covers nearly half of the national rice needs in 2025. As a result of these harvests, production capacity utilization in the economy increased marginally to 73.3 percent in Q1-25, up from 72.9 percent in Q4-24. Conversely, capacity utilization in mining and manufacturing declined. This is attributed to lower commodity prices, reduced international demand, and rising inputs costs.

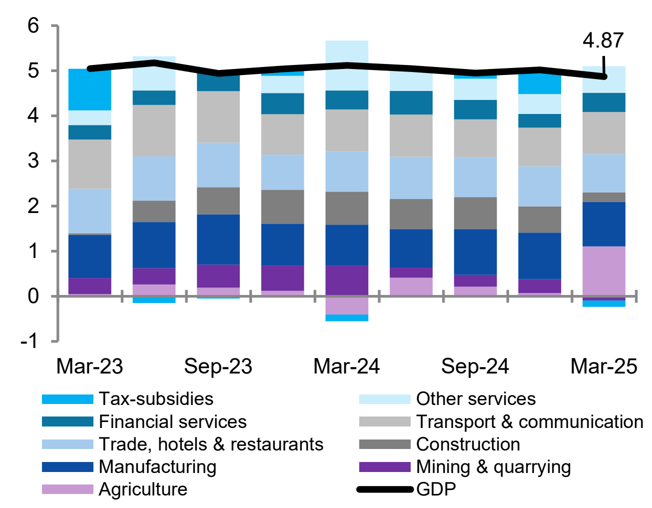
[1] The contribution of statistical discrepancies to growth in Q1-25 is currently at 17 percent, which is significantly higher than the historical average of 5.5 percent per quarter since the end of the pandemic. Statistical discrepancies arise from the differences between the GDP calculated using the expenditure approach versus the production approach. It is important to note that statistical discrepancies do not account for changes in the overall GDP figures nor do they reflect the final demand within the economy.

Figure A.1: Growth moderated due to declining domestic demand despite a temporary improvement in net exports.
(percentage points contribution to yoy growth)



Source: CEIC, BPS, World Bank staff calculations.

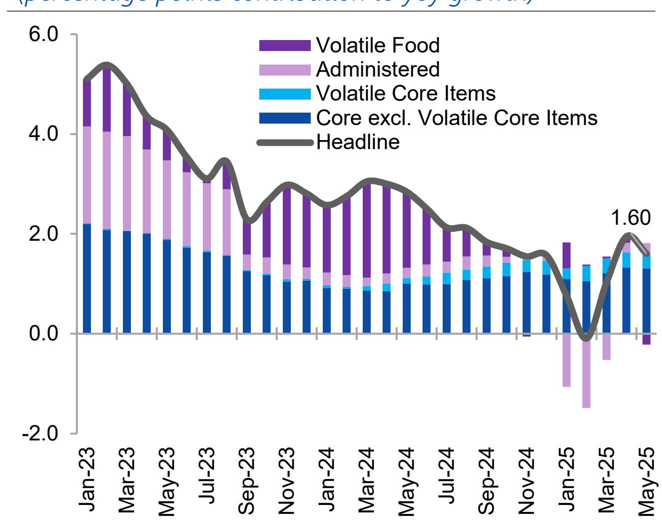
Figure A.2: Services and agriculture are driving growth while manufacturing industry is slowing down.
(percentage points contribution to yoy growth)



Source: CEIC, BPS, World Bank staff calculations.

Inflation remains subdued as food prices abated. Food prices, the largest component of the consumer price index, fell by 1.2 percent yoy in May as ample harvest and grain supplies eased the price of foodstuffs like chicken, eggs, and horticulture products (Figure A.3). Moreover, for the first time in decades Indonesia stopped importing rice, suppressing as a result the price of rice in domestic markets. However, housing utilities' prices surged by 1.5 percent yoy due to the removal of electricity tariff discounts[2] and higher clean water tariffs, pushing headline inflation to 1.6 percent, within Bank Indonesia's (BI) target range of [2.5±1 percent]. Average headline inflation remains subdued at 1.0 percent year-to-May. Core inflation also remained relatively stable at 2.4 percent yoy, showing a slight increase since the end of 2024 due to rising gold prices.[3] When excluding volatile components, core inflation stands at 2.0 percent yoy, indicating a softening domestic demand and a potentially slower closure of the output gap.

Figure A.3: Inflation is picking up after the removal of electricity tariff discounts, but it remains relatively subdued with abated food prices.
(percentage points contribution to yoy growth)



Source: CEIC, BPS, WB staff calculations.
Note: Volatile core items include gold, cooking oil, and grounded coffee.

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[2] As part of a social assistance package, the government introduced electricity tariffs discounts for January and February 2025.
[3] The core inflation index computed by Indonesia's statistical agency (BPS) incorporates volatile items like gold and coffee beans. The World Bank staff have estimated a revised core inflation indicator excluding volatile components using approximations of the weights of these volatile items in the household consumption basket.

Businesses and households are adjusting to economic uncertainty by changing investment, consumption, and savings decisions, but weak consumption of middle class households has been persistent since the pandemic.

Businesses are experiencing liquidity constraints and adjusting to slower economic activity. A survey conducted by BI revealed fewer businesses reporting improved liquidity conditions compared to those reporting a deterioration in liquidity conditions. Additionally, more businesses perceived access to credit as more challenging in Q1-25 compared to Q4-24 (Figure A.4). In April, the manufacturing purchasing managers' index (PMI) entered the contraction zone and fell below that of peer countries, ending five consecutive months of expansion.[4] This decline can also be attributed to weaker demand driven by tariff uncertainties, sluggish domestic consumer expectations, and constrained public spending. Furthermore, manufacturers have reduced inventory levels as well as hiring to maintain margins and fulfill production orders.

Rising uncertainty is also affecting household consumption and investment preferences. Consumer confidence has declined, especially regarding future economic conditions (Figure A.5). Moreover, household savings fell across all income groups, mainly affecting low- and middle-income families (Figure A.6). This is partially associated with recent layoffs in labor-intensive sectors, which mostly affect those income groups, as well as to stagnating real wages. As a result, consumption credit growth dropped to a two-year low with reduced consumer credit demand across the board.[5] Rising uncertainty also shifted household investment preferences. By Q1-25, the uncertainty index hit a five-year high.[6] Global uncertainty pushed gold prices up as central banks increased purchases. Despite significant price increase, domestic consumers followed suit and moved from equities to gold, jewelry, and property, while preference for savings and deposits accounts dropped (Figure A.7). Home and apartment ownership credit also increased by 80 percent, reflecting a shift in consumer preference towards safe-haven assets.

Middle-class consumption growth in Indonesia has been subdued since the pandemic. From 2019 to 2024, the poorest 40 percent saw consumption rise by 2-3 percent annually after accounting for inflation, and the richest 10 percent experienced a 3 percent annual increase. However, the aspiring middle class—those within the 40th-90th percentile of the consumption distribution—only saw about 1.3 percent growth per year since 2019. These outcomes reflect a structural constraint in the economy. While the poor have benefited from various social assistance programs to support their consumption, the lag in middle class consumption reflects the economy's constraint in creating middle class paying jobs and stagnating real wages. This is related to the overall decline in productivity in the economy.

Despite overall resilience, Indonesia's labor market is struggling to create middle class jobs, is experiencing layoffs in labor intensive sectors, and remains concentrated in low productivity employment.

The labor market remained strong overall with increasing labor force participation and notable job creation. Between February 2024 and February 2025, 3.59 million additional jobs were recorded, driving an increase in the labor force participation rate by 0.8 percentage points (ppts) (from 69.8 to 70.6 percent).[7] Employment growth was approximately 2.5 percent yoy, slightly above the labor force expansion of 2.4 percent yoy. The gender gap in labor market participation also improved. Female labor force participation rate increased by 1.3 ppts (now at 56.7 percent), compared to 0.3 ppts rise for male labor force participation rate (now at 84.3 percent).

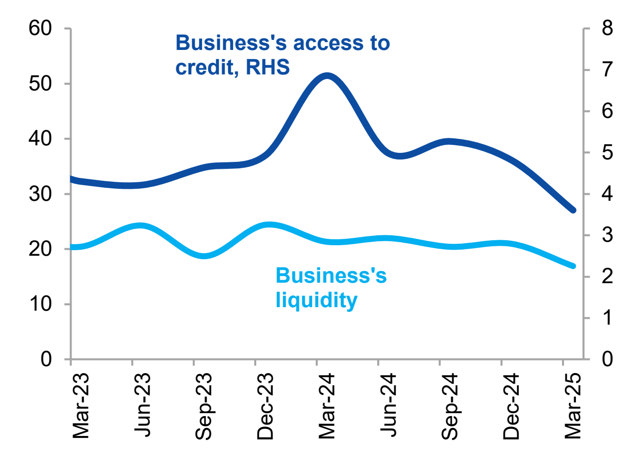
The unemployment rate is relatively low, but the rates in some demographic groups are significantly higher. In February 2025, the unemployment rate remained relatively stable around 4.8 percent (only 0.06 ppts lower than in February 2024). Although the unemployment rate for the labor force aged 15-24 decreased to 16.2 percent, it continues to be higher relative to other age groups. Furthermore, 8 percent of vocational high school graduates were unemployed, higher than other educational levels.

[4] Peer countries comparators are China, India, the Philippines, Malaysia, Thailand, and Viet Nam. The average PMI for these comparator countries has remained in expansion territory (above 50) contrary to Indonesia. In May, the PMI remained in the contraction zone and below its peer countries.
[5] Credit cards were down by 65 percent, multipurpose credit by 27 percent, non-collateral credit by 43 percent, and motor vehicle credit contracted (all yoy in Q1-25). Source: Banking Survey, Bank Indonesia.
[6] The Haver Analytics World Uncertainty Index (WUI) is a measure of global economic and policy uncertainty, calculated by counting the frequency of the word "uncertainty" (and its variants) in the Economist Intelligence Unit (EIU) country reports. This index is then normalized and rescaled (by multiplying by 1,000,000), with higher values indicating greater uncertainty.
[7] The source of the data is the Labor Surveys (Sakernas) February 2024 and 2025, Central Statistics Agency of Indonesia (BPS).

Job quality remains a concern with the low-paying sectors accounting for the highest number of jobs created, around 0.98 million in wholesale and retail trade and 0.89 million in agriculture (combined they account for 52 percent of all jobs crated throughout the year). Furthermore, almost 60 percent of workers are in informal jobs that lack job security.[8] The nominal wage grew by a mere 1.8 percent yoy in February 2025 (almost at par with inflation), compared to 3.3 percent in February 2024. Moreover, according to the Ministry of Manpower, job losses, most likely in the formal sector, increased from 3,325 in January to 18,610 in February 2025. This is double the number for the same period last year. Job losses were concentrated in Central Java, DKI Jakarta, and Riau, regions known for their manufacturing industries. Most job losses were in textiles, footwear, and electronics industries, with at least 10 manufacturing firms shutting down in Q1-25 based on data from the Ministry of Industry.

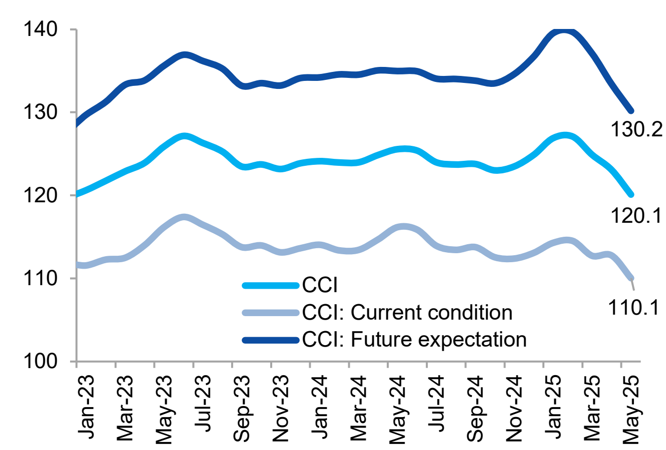
Indonesia's labor force is heavily concentrated in low-productivity sectors. As of 2024, 69 percent of workers are employed in activities that produce less than IDR 8 million per month in value added per worker. Another 21 percent work in mid-low productivity sectors generating between IDR 17–19 million per month (Figure A.9). In contrast, high-productivity sectors generating more than IDR 24 million per worker per month employ just 10 percent of the workforce. Extractives such as oil and gas, coal, and minerals, accounted for the highest-productivity tier (IDR 108 million per worker per month) and 10.4 percent of GDP, but only one percent of the labor force. As a result, a large share of the income they produce flows to corporate owners (including state-owned enterprises and investors) or to the government, rather than directly to the average Indonesian worker. The country's reliance on extractive industries and commodities has produced growth that is high in capital income but low in job creation and income growth.

Figure A.4: Business perception of access to credit and liquidity deteriorated.
(net balance of business reporting better liquidity condition, percent of respondent (LHS); net balance of business reporting easier access to credit, percent of respondent (RHS))



Source: Bank Indonesia.

Figure A.5: Consumer confidence has declined, especially regarding future economic conditions.
(index, 3mma)



Source: Bank Indonesia, WB staff calculations.
Note: An index value greater than 100 indicates more optimistic responses than pessimistic ones.

[8] Indonesia's statistics agency (BPS) provides a broad definition for informal workers. They are workers who are self-employed, employer with unpaid/ temporary worker(s), casual workers, and unpaid family workers

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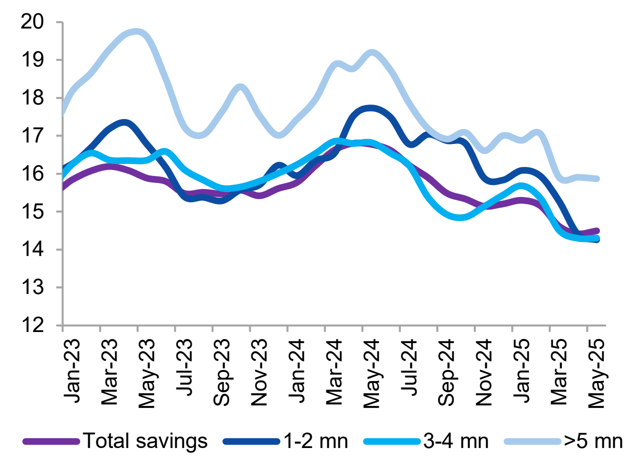
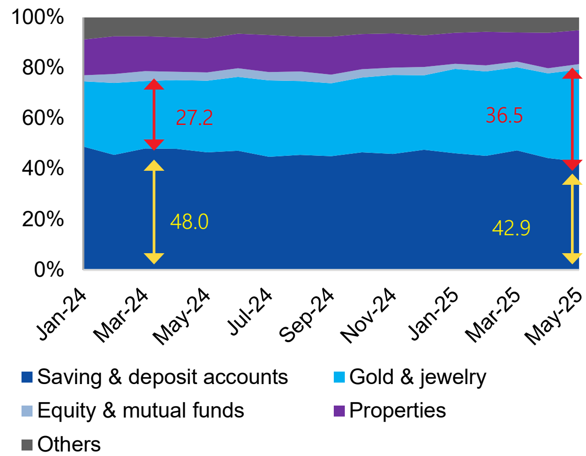
Figure A.6: Household savings, especially low- and middle-income groups, are softening…
(saving rate by income level, percent, 3mma)



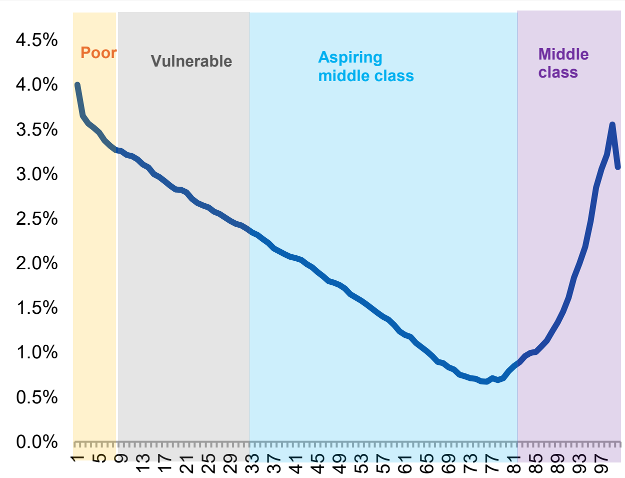
Source: Bank Indonesia.

Figure A.7: …with savings preferences shifting toward safe-haven assets like gold and property.
(percent of excess income)



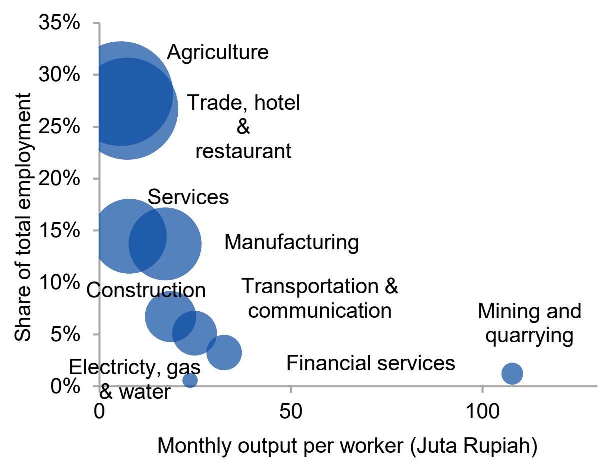
Source: Bank Indonesia.

Figure A.8: Middle-class consumption growth has been subdued.
(average growth by percentile vs. official income classes 2019-2024)



Source: World Bank staff.

Figure A.9: Indonesia's labor force is heavily concentrated in low-productivity sectors.



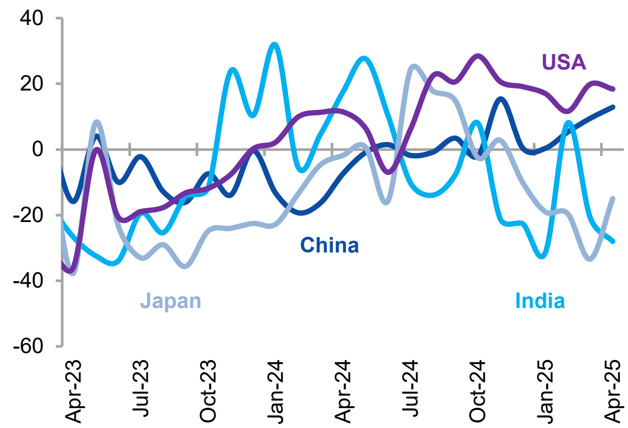
Source: World Bank staff.

Export frontloading in anticipation of global trade tariffs has almost balanced the current account, however the effect is temporal as Indonesia's terms-of-trade continue to deteriorate.

Indonesia's terms-of-trade deteriorated due to weaker commodity prices. Global commodity prices dropped sharply in April as trade policy uncertainty intensified. Compounded by weakening global demand, oil prices fell significantly following a substantial hike in oil production by OPEC+ nations. Coal and palm oil prices followed were also notably lower than last year's levels. Metal prices (including iron and steel) also decreased due to substantial challenges anticipated in global manufacturing and industrial activity. As one-third of Indonesia's non-oil and gas exports consist of coal, crude palm oil, iron and steel, their declining prices led to a deterioration in the country's terms-of-trade.

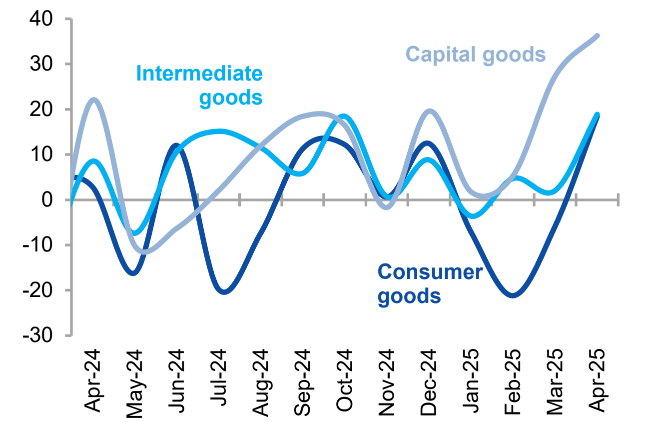
Nevertheless, a temporary surge in exports has almost balanced the current account in Q1-25. With exports to China and the US surging in anticipation of trade tariffs (Figure A.10), the goods trade surplus expanded to 0.9 percent of GDP in Q1-25 (up 0.3 ppts yoy). Metal and steel products exports saw the largest growth with nickel up by 64 percent yoy. Meanwhile, import growth slowed as domestic demand weakened, with the deceleration in consumer and intermediate goods imports offsetting the rise in capital goods (Figure A.11). Higher outbound travel coupled with lower incoming tourism contributed to the widening services deficit (up 0.1 ppt yoy); and higher portfolio investment payments coupled with company profit repatriation led to a slight widening deficit in the income account (up 0.02 ppts yoy). Overall, the current account deficit (CAD) narrowed though by around 0.2 ppts to 0.01 percent of GDP in Q1-25. After the tariff's announcement, the trend started reversing as exports, led by apparel and footwear, decelerated in April (down 10.8 percent m-o-m), reducing the goods trade surplus to 0.01 percent of GDP as of April.

Figure A.10: Exports to the US and China accelerated in March, ahead of the US tariffs.
(percent yoy growth)



Source: BPS, CEIC, World Bank staff calculations.

Figure A.11: Imports initially slowed, but they surged in April across categories.
(percent yoy growth)



Source: BPS, CEIC, World Bank staff calculations.

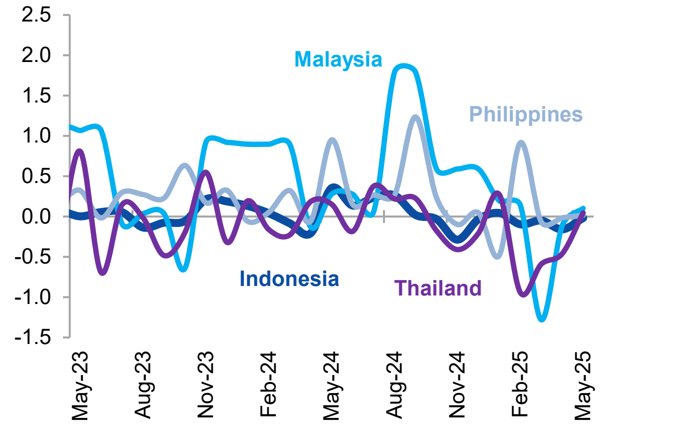
Global financial conditions have tightened during the first half of 2025, resulting in capital outflows and exerting pressure on the Rupiah.

Tightening global financial conditions led to high currency volatility in Asian EMDEs. Global uncertainty has heightened financial market volatility, leading to a global stock market decline. Global financial markets now expect fewer Federal Fund Rate (FFR) cuts as US consumer inflation expectations rose.[9] Furthermore, the yields on the 30-year United States Treasury (UST) recently increased to 5 percent, approaching the highest level since 2006. With the broad-based weakening of the US Dollar, global investors have turned to other safe-haven assets such as gold, the Swiss Franc, and the Japanese Yen. Across Asian EMDEs, including Indonesia, financial conditions also tightened as equity prices declined sharply amid capital outflows (Figure A.12).

Volatility negatively impacted Foreign Direct Investment (FDI) and the equity markets in Indonesia, offset partially by foreign investments in sovereign and corporate bonds. Despite being the largest source of external financing, FDI in Indonesia dropped by 40 percent yoy in Q1-25 to US$3.7 billion (0.3 percent of GDP). The largest drop was observed for FDI in the construction sector and financial services. The narrowing Indonesia-US interest rate gap coupled with rising uncertainty in the global economy have fueled capital outflows. Non-resident investors withdrew USD 1.9 billion from the equity market during Q1-25, while domestic investors invested US$0.4 billion in equities abroad and US$4.3 billion in other types of investment.[10] Gold, overseas real estate, and cryptocurrencies, among others, are reported to gain popularity among Indonesian investors. Those outflows were partially offset by US$3.3 billion in foreign capital inflows into sovereign and corporate bonds, as well as BI securities (SRBI) (Figure A.13). However, maturing SRBI, worth IDR289 trillion (1.3 percent of GDP), by mid-2025 warrants monitoring due to potential risk for further outflows, especially if foreign investors remain unfavorable about the Indonesian equity market.

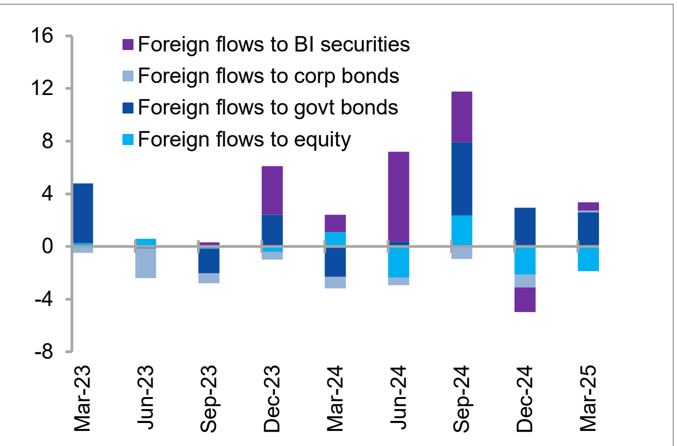
[9] The market initially expected five policy rate cuts, but is now anticipating only two cuts following the announced 90-day tariff pause.
[10] Official Balance of Payment (BOP) data showed that "other investments" category recorded a net outflow of US$4.3 billion as residents' investments abroad picked up.

Figure A.12: Asian EMDE saw capital outflows as global investors turned to safe-haven assets.
(percent of annual GDP)



Source: IIF, BI, IDX, World Bank staff calculations.

Figure A.13: Foreign investment into debt securities partially offset equity selloff in Q1-25.
(USD billion)



Source: BI, CEIC, World Bank staff calculations.

Banking sector prudential indicators are sound and have helped manage global policy uncertainty.

The banking sector's asset quality is healthy, with sufficient buffers to withstand potential adverse shocks. As of February 2025, the non-performing loans (NPL) ratio is at a low 2.2 percent. The capital adequacy ratio (CAR) stands at 26.9 percent and exceeds the regulatory minimum of 10.5 percent, while provisioning levels are at 183 percent of NPLs, ensuring substantial loss-absorption capacity (Figure A.14). The system-wide loan at risk (LAR) ratio continues to trend down, reaching only 9.3 percent by the end of 2024, markedly lower than the pandemic period levels of over 20 percent. Results from bank solvency stress tests conducted in the recent joint IMF-WB Financial Sector Assessment Program (FSAP) indicate that the overall banking sector is resilient to various shocks, although there remain tail risks for smaller banks. Three commercial state-owned banks were included as part of Danantara's holdings, giving rise to potential interconnectedness and governance risks.[11] Such risks are mitigated though by partial state ownership and strong balance sheets.

The banking sector remains highly profitable despite recent deceleration in private sector lending. As of February 2025, return-on-assets (ROA) and return-on-equity (ROE) were at a strong 2.4 and 13.3 percent, respectively. Both indicators showed a slight decline in recent months though, as lending to the private sector decelerated and reached 8.9 percent yoy in April, at the lower bound of BI's revised 2025 target of [8-11] percent[12] (Figure A.15). Furthermore, Indonesia's credit-to-GDP gap remains negative and has been widening since the second half of 2024, indicating that credit growth is growing below its long-term trend (Figure A.16). This signals subdued credit demand and moderating economic activity. Investment loan growth continues to outpace consumption and working capital loans significantly in response to BI's liquidity incentives. Credit to mining, utilities, and the transport sectors contributed 40 percent to the overall credit growth. Nevertheless, overall private sector credit remains low at 35.4 percent of GDP (end of 2024), compared to the EAP countries average of 124 percent of GDP. Low levels of credit persist despite a strong banking sector with substantial capital and liquidity, but limited incentives to pursue riskier economic segments, prioritizing stability instead.

System-wide funding and market liquidity remain adequate, despite lending growth outpacing deposit growth. As of February 2025, the liquidity coverage ratio (LCR) and net stable funding ratio (NSFR)[13] were 210 and 128 percent respectively, both exceeding the 100 percent regulatory minimum. The loan-to-deposit ratio (LDR), a key indicator of banking sector liquidity, rose to 88 percent. The increase reflects a tightening in liquidity as the gap between lending and deposits growth widened. Indeed, lending growth outpaced deposits growth by 2 to 1. Meanwhile, households' drawdown on savings rose as real wages plateaued, causing overall household deposits in the

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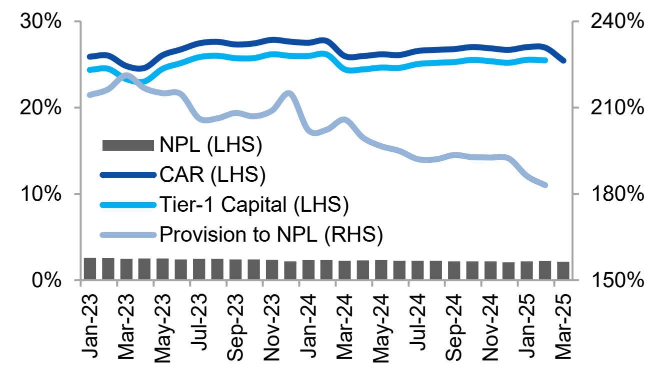
[11] Interconnectedness and contagion risks can arise from both direct, i.e. interbank exposures, and indirect linkages, i.e. exposure to common assets, information spillover or investor perception, among financial institutions. Being included as part of the same holding structure with common management and governance presumably increases such risks.
[12] In May 2025, BI revised down its credit growth target from [11-13] percent to [8-11] percent in light of a slowdown in economic activity.
[13] These indicators are used to measure bank liquidity conditions in times of stress.

banking sector to stagnate (for IDR deposits) or even slightly decline (for FX deposits). This has not affected the bank's deposit base or lending capacity so far, as deposits by the public sector and non-financial corporates continue to increase. If the deposit base shrinks or the LDR increases further, funding liquidity risks may need careful monitoring. According to international standards, an LDR between 75 and 90 percent is normal while a ratio over 100 percent is sometimes linked to liquidity strains during financial crises.

Borrowing costs and domestic funding conditions are relatively stable, although structural factors increase funding costs compared to peers. Corporate bond issuance activities remain robust in 2025. Corporate borrowing costs are stable, as the 10-year AA corporate bond[14] yield stood at 8.2 percent as of March 2025. From a market structure perspective, the capital market still lacks depth with limited secondary trading compared to global and regional peers. Although the government securities market is relatively well-developed, the corporate bond and equity markets segments remain shallow, offering limited choices for investors. The low demand from local long-term investors and a weak domestic investor base, including relatively small institutional investors, constrain market development and contributes to higher cost of borrowing relative to peers.

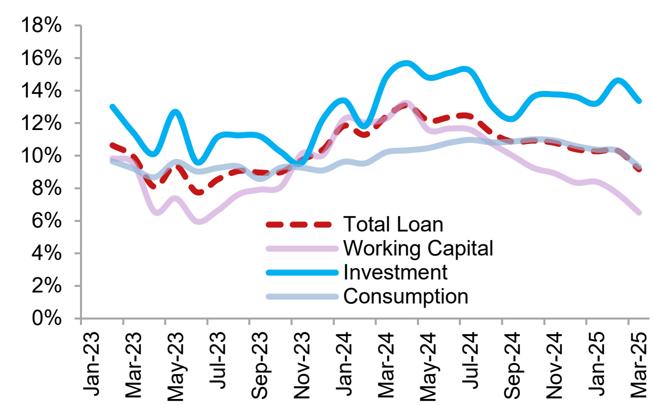
Elevated global uncertainty could tighten financing conditions or increase financial sector vulnerabilities through various channels. This includes bank credit exposure to export-oriented firms, weaker bank profitability due to slowing domestic demand and reduced investment, currency volatility, and capital outflows driven by risk aversion and negative global investor sentiments. Indonesia's close trade and FDI ties with China, which is affected by global trade policies, accentuate these impacts. Additionally, underdeveloped FX hedging instruments and Indonesia's status as a commodity exporter could increase risks on the financial sector due to banks' exposure to commodity traders and clearing services for commodity trading. A drop in commodity prices and a slowing global demand could therefore lead to a decline in FX earnings and bank deposit growth. While April saw significant equity outflows, strong financial sector buffers have helped manage so far global policy uncertainty.

Figure A.14: The banking sector's asset quality and buffers are healthy...
(percent)



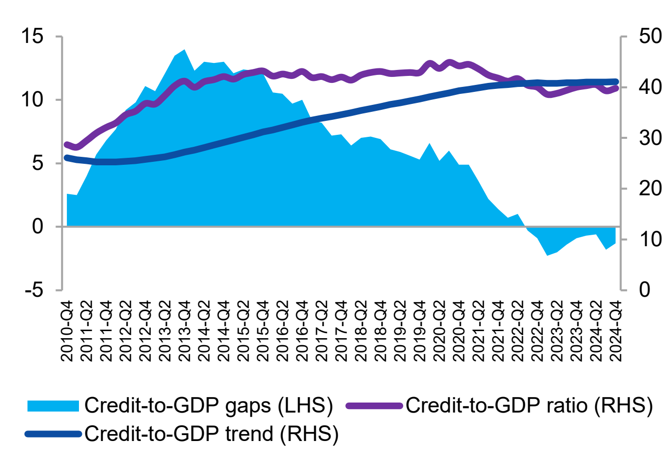
Source: The Financial Services Authority (OJK).

Figure A.15: ...but lending to the private sector has been decelerating.
(percent)



Source: The Financial Services Authority (OJK).

Figure A.16: Credit growth has been slower than its long-term trend pointing to moderating economic activity.
(percent of GDP)



Source: Bank for International Settlement.
Note: Credit refers to credit to private non-financial sector.

[14] An AA corporate bond is a type of debt security issued by a corporation that has received a high credit rating, just below the top AAA rating, indicating a low risk of default and strong capacity to meet financial commitments. This is a national rating scale though, which assesses the creditworthiness relative to other domestic issuers. These ratings are not comparable to international ratings scales.

2. The Policy Stance

Indonesia's fiscal policy stance has been influenced by temporary and structural factors affecting revenues, prompting budget efficiency measures and increased financing requirements.

Indonesia's fiscal position weakened slightly in the first five months of 2025 (5M25) because of a revenue shortfall. By May 2025, the budget recorded a small deficit of IDR 21 trillion (0.1 percent of GDP) (Figure A.17). This compares to an average surplus of 0.5 percent observed in May over the past three years. The deficit is primarily due to a larger drop in revenue collection than in expenditure. Revenue collection by May 2025 was 4.1 percent of GDP, 1.3 percentage point lower than the previous three years, while expenditure is around 0.7 percentage point lower.

Several factors have impacted revenue collection. Tax revenues declined by 0.6 percent of GDP in 5M25 compared to the same period last year (Figure A.18). Temporary factors included technical problems in the implementation of the new Core Tax Administration System (CTAS)[15] that resulted in extended payment deadlines; and a new tariff rate system for personal income tax withholding that resulted in overpayment in 2024 and to larger refunds in early 2025.[16] Other factors include: (i) lower commodity prices and lower domestic demand that impacted both tax and non-tax revenues[17]; (ii) forgone revenues from the adjustment to the planned VAT rate increase[18]; and (iii) the forgone revenue from SOE dividends that will now be collected by Danantara[19] (estimated at around 0.4 percent of GDP yearly). To mitigate some of these effects, the GOI raised the mining royalty rate in April 2025.[20]

Amid revenue shortfalls, the GOI initiated a budget efficiency and reallocation program to support priority spending. This program, equivalent to 1.3 percent of GDP, aims to offset a projected revenue shortfall (0.6 percent) and finance targeted spending (0.6 percent). This led to a 0.2 and 0.3 percent decline in material and other spending by the central government in 5M25 (Figure A.19) and 0.1 percent of GDP decline in transfers to subnational governments. The new administration's Free Nutritious Meal (MBG) program, part of its eight Quick Win Programs, was launched on January 6 and is centrally managed.[21] It is set to receive a budget increase of 0.2 percent, bringing its total allocation to 0.5 percent of GDP. The government also allocated 0.8 percent of GDP for the new village cooperative program. This is comparable to the amount allocated for energy subsidies (0.8 percent of GDP) and the combined budget of social assistance programs[22] (0.6 percent of GDP). Two fiscal stimulus packages worth 0.3 percent of GDP were also introduced: one to support household purchasing power, labor-intensive, electric vehicle, and housing sectors ahead of the scaled-down VAT hike, and the other to boost household consumption ahead of the school holidays.[23]

Budget efficiency initiatives were designed to create fiscal space for priority programs, though may have longer-term growth tradeoffs. In February, significant budget cuts were announced to public investment ministries, with reductions of 55 percent for Public Works, 44 percent for Transportation, and 35 percent for Agriculture, totaling 0.3 percent of GDP.[24] Additionally, 0.2 percent of GDP was cut from the Health

[15] CTAS integrates all business processes of tax administration from taxpayer registration, reporting of tax returns, payments and audits.

[16] The new Average Effective Tax Rate (TER) system, implemented in 2024 for monthly employee income tax (PPh 21) withholding, simplifies tax calculations by applying a fixed effective rate to gross income based on the employee's marital status and number of dependents (i.e., PTKP category). In 2024, this led to over withholding—amounting to IDR 16.5 trillion (0.07 percent of GDP)—causing an increase in tax refunds in early 2025.

[17] Moderating domestic demand has partially contributed to a decline in non-oil and gas income tax and VAT, which were lower by 0.6pp and 0.5pp respectively compared to April last year. Oil price in early June 2025 was about US$65 per barrel, compared to the 2025 Budget assumption of US$82.

[18] The Tax Harmonization Law of 2021 raised the VAT rate by 1 percentage point in April 2022 and had scheduled another increase of 1 ppt no later than January 2025. The objective was to gradually raise VAT rate from 10 to 12 percent. On December 31, 2024, the GOI limited the second increase to luxury goods only (PPnBM), keeping the VAT exemption list unchanged.

[19] On February 24, 2025, the GOI launched Danantara, a super holding company for SOEs. It will manage SOE dividends and invest them in national strategic projects. The fiscal balance is likely to be negatively affected by Danantara's creation.

[20] In April 2025, the GOI raised royalty tariffs for Nickel, Copper, Metal minerals, Peat, Asphalt, Gold, through PP 18/2025 and 19/2025.

[21] The GOI's new National Nutrition Agency, *Badan Gizi Nasional*, oversees the program with 13,000 community kitchens serving students. This diverges from the past practice of relying on local government systems for non-cash food assistance which facilitated program socialization, monitoring, evaluation, and coordination with local agencies including the delivery institutions.

[22] These programs are health insurance premium assistance (JKN), food aid, the Indonesia Smart Card, and the Family Hope Program.

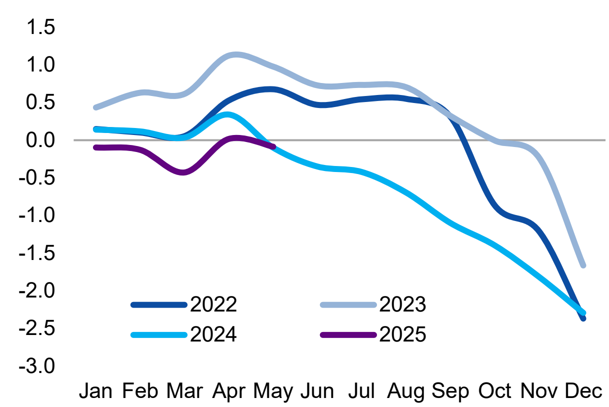
[23] The GOI granted food assistance, electricity discount and tax expenditures for electric vehicle and housing sector in the first package announced on December 16, 2024. For firms in labor-intensive sectors, the GOI provided tax expenditure for personal income tax up to IDR10mn salary per month, interest subsidy for machinery revitalization, and subsidies for employment injury insurance premium. The second package, announced on May 27, 2025, includes transportation and toll tariff discounts, and expanded social assistance such as food aid and cash transfers. It also provides wage subsidies for low-income workers and non-permanent teachers (on honorarium), along with extended insurance premium discounts for labor-intensive sectors.

[24] The budget cuts/efficiency allocations data is based on the revised budget allocation outlined in Minister of Finance letter No. S-75/MK.02/2025 dated February 13, 2025, as reported on Parliament website.

and Education ministries as well as from the ministries of defense and national policy combined. Transfers to sub-national governments for infrastructure projects were also cut by 0.1 percent of GDP.[25] While some of the budget efficiency cuts appear to be redistributed to some ministries and agencies, no information is available yet on final allocations. Allocating the limited budget to areas with high fiscal multiplier effects is crucial for growth (see section on policy priorities).

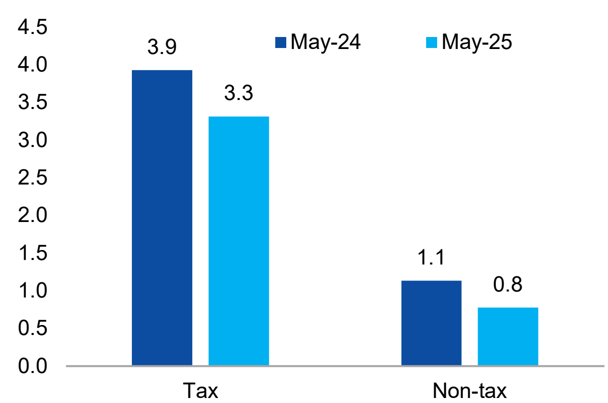
The GOI has sought higher net financing in a stable bond market despite global volatility. The deficit in 5M25 has prompted the GOI to secure 53 percent of its financing needs by end-May, compared to 16 percent last year. Most of this additional financing was sourced from commercial banks. Government bond yields and spreads with US bonds have remained steady, despite a temporary uptick during recent global fluctuations.[26] Similarly, the Credit Default Swap (CDS) spread experienced a brief increase, mirroring trends in other emerging markets. Indonesia's debt stock is stable at around 40 percent of GDP, though the interest-to-revenue ratio is rising, and remains sensitive to exchange rate and interest rate fluctuations (Figure A.20).[27]

Figure A.17: The monthly fiscal balance is slightly weaker compared to recent years.
(percent of GDP)



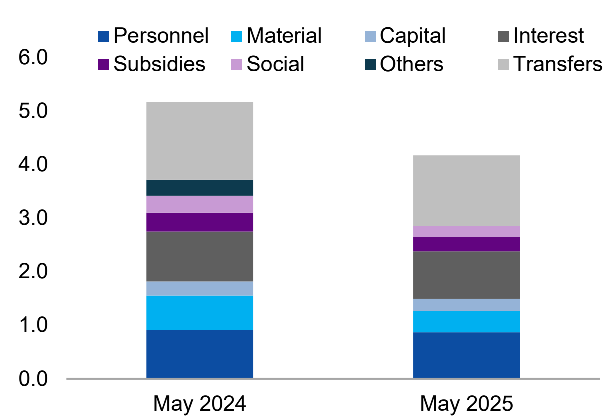
Source: CEIC, Ministry of Finance, World Bank staff calculation.

Figure A.18: This is partly caused by a decline in both tax and non-tax revenues.
(percent of GDP)



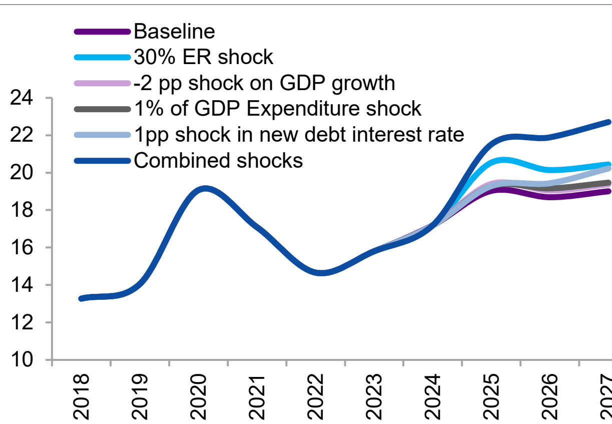
Source: Ministry of Finance, World Bank staff calculation.

Figure A.19: Contraction in material and other spending as well as transfers led to the decline in government expenditure.
(percent of GDP)



Source: CEIC, Ministry of Finance, World Bank staff calculation.

Figure A.20: Interest-to-revenue ratio is rising and sensitive to exchange rate and interest rate shocks.
(percent)



Source: Ministry of Finance, World Bank staff calculation.

[25] Specific Allocation Funds (DAK) for physical projects and General Allocation Funds (DAU) for public works were cut by 0.08 and 0.06 percent of GDP, respectively.
[26] The 10-year government bonds yield is relatively stable at around 7 percent on average in 2025.
[27] The interest to revenue ratio increased to 17 percent in 2024, continuing the increasing trend in 2023. It is also relatively higher than the regional peers' average of 9 percent.

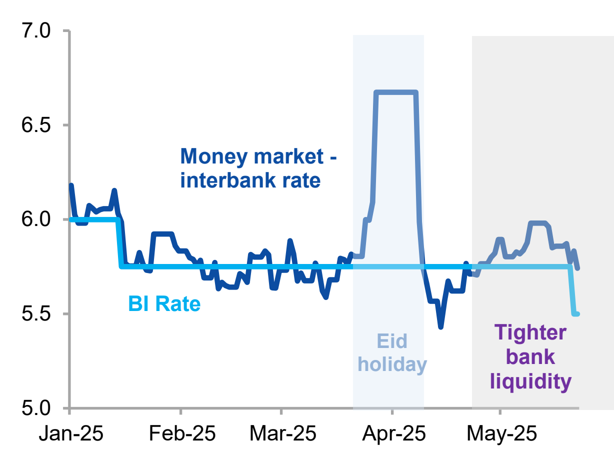
BI intervention in the FX market has helped to stabilize the Rupiah, while gradually easing monetary policy in support of economic growth.

Monetary policy has eased gradually over the first half of 2025. With low inflation, BI cut the policy rate twice this year (January and May) by 25 bps each to 5.5 percent. To boost economic growth, BI eased two macroprudential measures in 2025. First, it lowered the Reserve Requirement Ratio (RRR) for housing loans from 9 percent to 4 percent, freeing up IDR 86 trillion in bank liquidity (equivalent to 1 percent of credit to the private sector). This change took effect in April. Second, BI will raise the foreign borrowing limit for banks from 30 to 35 percent of total capital and reduce the macroprudential liquidity buffer by 100 bps to enhance banks' access to external funding.[28] These measures will be effective in June.

The easing monetary stance was supported with liquidity injections through open market operation (OMO). Tighter liquidity in the banking sector has pushed the overnight interbank lending rate (IndONIA) above the BI Rate since late April (Figure A.21), while broad money growth (M2) gradually decelerated over the year. BI allowed redemptions of SRBI (BI's monetary instrument) to consistently outpace new issuances, resulting in net injection in liquidity into the financial system. Consequently, the outstanding SRBI stock has declined, from 4.2 percent to 3.8 percent of GDP year-to-May. In addition, BI increased its holdings of government bonds through purchases both in the primary market (0.1 percent of GDP) and secondary market (0.3 percent of GDP) year-to-May.[29] As a result, BI's share of government bond ownership rose from 26.7 to 27.8 percent.

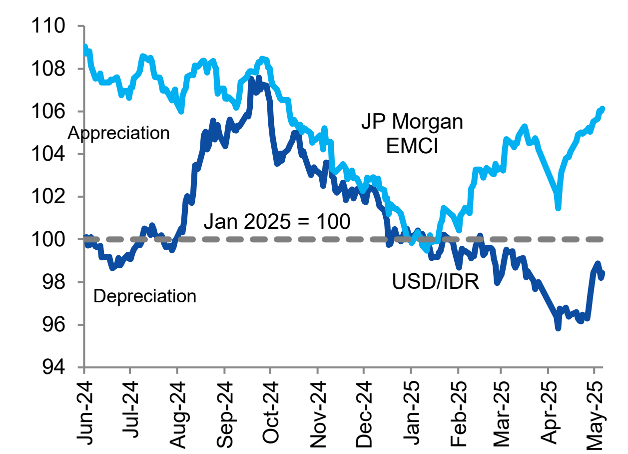
BI also intervened in the FX market to stabilize the Rupiah. In early April, the Rupiah depreciated by 4.9 percent, and briefly reached a historic low of 16,943 against the US$ as capital outflows intensified. This prompted BI to intervene in the FX market in support of the Rupiah, which strengthened by 2.2 percent in May (m-o-m). As a result, FX reserves fell by US$4.6 billion between March and April but remained adequate and covered 6.2 months of imports and debt repayments. The Rupiah still underperformed emerging market currencies in 2025 as the JP Morgan Emerging Market Currency Index (EMCI) appreciated by 5.3 percent (Figure A.22). To boost FX reserves, authorities now require 100 percent of natural resource export proceeds to stay onshore for a year starting in March. This replaces the previous rule of 30 percent for three months (see IEP December 2023). This regulation may limit exporters' working capital, though deductions and BI's investment flexibility may offer partial relief.

Figure A.21: Interbank lending rate recently exceeded BI Rate, suggesting tighter liquidity.
(percent)



Source: BI, World Bank staff calculations.

Figure A.22: The Rupiah has underperformed its EMDE peers year-to-May.
(index, Jan 1, 2025 = 100)



Source: BI, JP Morgan, World Bank staff calculations.

[28] Foreign borrowing limit for banks is designated by RPLN or *Rasio Pendanaan Luar Negeri*. Macroprudential liquidity buffer is designated by PLM or *Penyangga Likuiditas Makroprudensial.*
[29] BI's purchases of government bonds are intended to maintain the target yield of sovereign bonds, subsequently influencing the overall borrowing costs. During unfavorable global conditions, BI also often serves as a residual financier in the domestic market.

3. Outlook and Risks

The economy is projected to recover with growth accelerating if reforms are swiftly enacted, but both global and domestic risks are high and require prudent macro management and effective policy communication.

Global policy uncertainty is expected to remain high, affecting the outlook. Various factors such as global trade fragmentation, geopolitical risks, and fluctuating commodity prices are anticipated to keep global growth subdued, including that of Indonesia's main trading partners. Within this context, Indonesia's growth is expected to increase gradually over 2025-27, averaging 4.8 percent annually (Table A.1). Despite concerns about Indonesia's shrinking middle class and reduced purchasing power due to a lack of good jobs, private consumption is projected to grow, supported by low inflation and social assistance programs. Investment is expected to rise as the GOI launches its housing program and Danantara, the new sovereign wealth fund, starts rolling out projects. Various energy and infrastructure projects are set to accelerate implementation in the medium term, partially offsetting slow growth from net exports due to global trade shifts and low commodity prices. Commodity-based manufacturing, agribusiness, construction, and services will drive the supply-side, reflecting government priorities. Inflation, after easing in 2025, is forecasted to gradually increase to 2.6 percent but remain anchored within BI's target range.

The GOI structural reform agenda could accelerate growth further and help Indonesia navigate the downfalls from global uncertainty. In response to rising global policy uncertainty, the GOI has devised a program of deregulation including reforms to business environment and licensing, investment liberalization, trade and logistics reforms, and digital services (see reform priorities section).[30] These reforms complement other reforms currently in play, like those in financial sector deepening,[31] and accompany the demand stimulus drive that the GOI is targeting through its priority programs (see Part B for a discussion on the GOI's housing program). If implemented, these reforms will gradually expand the economy's capacity, unlock further FDI, boosts investment returns, and ensure productivity gains. This will translate into better jobs creation and raise GDP growth to 4.9 percent in 2025, and to 5.3-5.5 percent in 2026-2027.

The fiscal policy stance is expected to remain prudent and within fiscal rules. The fiscal deficit is projected to average 2.7 percent of GDP over 2025-27, below the 3 percent of GDP deficit rule.[32] Spending is anticipated to reach 15.1 percent of GDP by 2027 due to priority programs and rising interest payments (Table A.1). Public spending will shift more towards social assistance as priority programs and consumption stimulus programs are rolled over. However, it is forecasted that public investment will return to its originally low pre-pandemic levels to cover basic and service delivery infrastructure. Indeed, spending on basic infrastructure, including maintenance, will be necessary to support growth alongside flagship projects. Public financial management and operational constraints may slow down the disbursement of complex priority programs.[33] On the other hand, new revenue strategies and improved tax enforcement, if implemented, will partially finance this spending.[34] Tax revenues are projected to be lower than government target due to forgone revenues from the VAT rate hike adjustment, which are estimated at 0.3 percent of GDP. Non-tax revenues are expected to decline due to lower commodity windfalls and SOE dividends reallocating to Danantara. Meanwhile, elevated borrowing costs coupled with rising budget deficit are forecast to raise interest payments to 2.4 percent of GDP, or 19 percent of total revenues, and raise gross financing needs to an average of 4.8 percent of GDP over 2025-27.

External financing needs will increase due to a widening current account deficit and rising public debt amortization. The outlook assumes moderating terms-of-trade, global trade shifts, and China's slowdown will hamper export growth, while recovering domestic demand will boost imports. As a result, the

[30] A deregulation task force, comprising public sector and business association leaders, has been nominated on April 28, 2025, to lead this reform agenda. The formal launch of the task is awaiting the signature of the related presidential decree.
[31] Through the implementation of the Financial Sector Omnibus Law.
[32] The GOI, in its macroeconomic framework and key elements of fiscal policy 2026 document, projects fiscal deficit of around 2.5 percent of GDP in 2026, broadly unchanged from 2025.
[33] These are likely to include MBG, education, health, and village cooperative programs in the near term while focusing on food and energy security over the medium term.
[34] The GOI plans to tax digital transactions, further raise mineral and coal royalty rates, and leverage big data. This will be bolstered by the smooth implementation of CTAS eventually.

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CAD is projected to widen gradually and reach 1.7 percent of GDP by 2027 (Table A.1). Although larger CAD, rising public debt amortization, and maturing SRBIs will increase external financing needs, they will remain below pre-pandemic levels. FDI is expected to rise gradually to 1.5 percent of GDP by 2027 and remain the largest source of external financing. These inflows are expected to mostly target government priority sectors like industrial downstreaming, housing, energy, as well as services sectors. Portfolio flows will remain volatile but might improve slightly as global monetary conditions ease over time.

The outlook is subject to significant downside risks. Whilst the GOI has set out clear priorities, this involves major institutional changes (e.g., government reorganization, large budget adjustments, establishment of Danantara, and transfer of SOE ownership to the new SWF), which are disruptive and create uncertainty. This may slow down the implementation of investment plans and government programs. Though sovereign borrowing costs have come down, spreads on local borrowing remain high, as do interest payments to revenues. A big boost in investment without an acceleration in structural reforms could lead to declining returns to investment, a deterioration in the quality of jobs, and a slowdown in growth. Geopolitical shocks, including potential shifts in global trade, could further worsen terms-of-trade, spur inflation, and squeeze fiscal space. Global uncertainty and a reversal of planned global monetary easing could also impact portfolio flows, put pressure on the Rupiah, and raise the costs of borrowing for both public and private sectors. On the upside, stronger growth in major trading partners or higher commodity prices could boost exports, expand fiscal space, and enhance growth.

4. Policy Priorities

Indonesia's trade and deregulation reform drive could help manage global uncertainty and spur investment, growth, and jobs.

As of April 2025, Indonesia's exports to the United States have been subject to an additional import duty of 10 percent, same as other trading partners. Compared to the previously applied average tariff rate of 3.6 percent faced by Indonesia's exports to the US, this constitutes an almost fourfold increase. As a result, for instance, palm oil - Indonesia's largest export commodity to the US at US$1.5 billion in 2024 - previously exported duty-free now faces a 10 percent tariff. Similarly, tariffs on sweaters and pullovers have risen from 32 to 42 percent, and tariffs on sports footwear have increased from 20 to 30 percent.

Indonesia's direct exposure to US markets is limited. In 2024, Indonesia's merchandise exports to the US reached US$28.1 billion, accounting for 10 percent of total exports and about 2 percent of GDP. This exposure is considerably lower than that of regional peers such as Cambodia and Viet Nam, whose exports to the US represent 29 and 26 percent of GDP, respectively (Figure A.23). With US exports to Indonesia of US$10.2 billion, the goods trade surplus with the US amounted to US$17.9 billion in 2024. It is worth considering, however, that Indonesia recorded a services trade deficit of US$1.5 billion with the US, primarily driven by demand for US education and financial services, charges for the use of intellectual property, and telecommunications services.

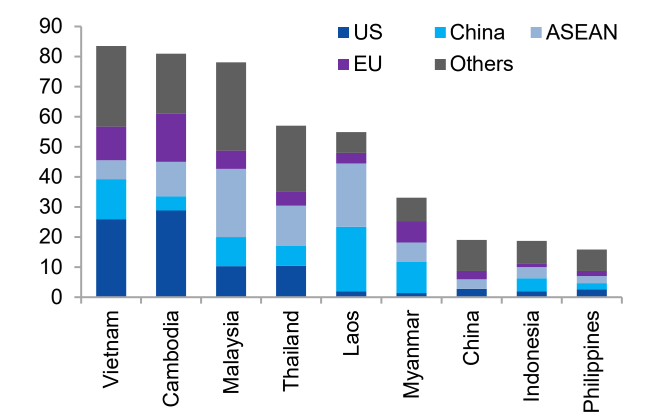
Despite modest aggregate exposure, several labor-intensive sectors with high US market exposure could be adversely impacted. These include textiles and apparel, footwear, food products and electrical equipment (Figure A.24). Notably, over half of Indonesia's exports of feather and down articles, furskins, fish fillets, furniture, and leather goods are destined for the United States. Conversely, key export commodities - coal, palm oil, iron and steel – which collectively account for close to half of Indonesia's total exports, have limited reliance on US markets. Additionally, an estimated US$1.5 billion or 5.4 percent of exports to the US - natural rubber, plywood, tin, copper, wood and nickel products – were exempted from higher tariffs (Figure A.25).

The GOI is considering several deregulation reforms. Reforms could target the relaxation of local content requirements in the ICT sector along with the evaluation of import license procedures and accelerated halal certification. Other reforms aim to simplify tax and customs procedures to reduce trade costs; lower import income taxes from 2.5 percent to 0.5 percent; reducing tariffs on US goods to 0–5 percent; adjust CPO export taxes; fast-track anti-dumping and safeguard measures; and remove import quotas and technical regulations. Additional trade facilitation measures could include simplifying import licensing via digital systems and shift to post-border control through the National Logistics Ecosystem. In addition to the establishment of a Deregulation Task Force to coordinate these reforms, a Task Force for Job Opportunities and Layoff Mitigation aims to address the increase in layoffs and develop strategies to mitigate adverse impacts.

Addressing these trade barriers could play a critical role in boosting Indonesia's long-term growth and economic transformation. Targeted reforms to reduce the costs of imported manufacturing inputs, enhance firms' access to new and existing markets all the while addressing remaining domestic bottlenecks to trade and firm growth will be key to realizing the potential of trade. Trade policy reforms aimed at streamlining and eliminating unnecessary non-tariff measures (NTMs), removing barriers to services trade, deepening and expanding trade agreements, and improving logistics and trade facilitation performance are needed to create the enabling trade policy framework in Indonesia (World Bank 2022). All in all, an open, stable, transparent, and predictable trade policy framework will be key to position Indonesia for the ongoing reconfiguration of the international trade and investment system.

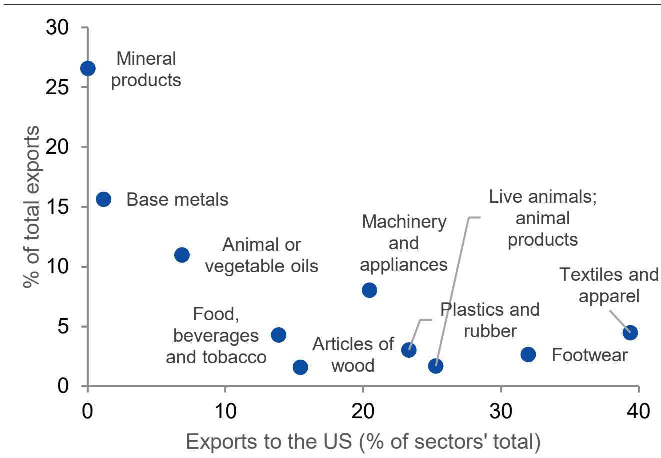
Targeted NTMs reforms could generate significant economy-wide benefits, of up to 5 percent of GDP over the medium-to-long term. NTMs amount to an estimated average tariff equivalent of 30 percent, significantly higher than average import tariffs at 2 percent. Multiple burdensome NTMs - import approvals, pre-shipment inspections, port of entry restrictions, mandatory certification with national standards (SNI) - are often applied cumulatively, further compounding compliance costs for businesses (Figure A.26). Reforms to tackle these costly NTMs could boost total exports by 10 percent and investment by 27 percent over the medium-to-long term (Figure A.27). The greatest gains could be realized through reforms of import approvals and mandatory certification with SNI, especially in high value-added advanced manufacturing industries, including computers, electronics and optical products, transport equipment, electrical equipment, and basic pharmaceutical products.

Figure A.23: Indonesia's direct exposure to US markets is considerably lower than that of regional peers.
(exports as percent of GDP)



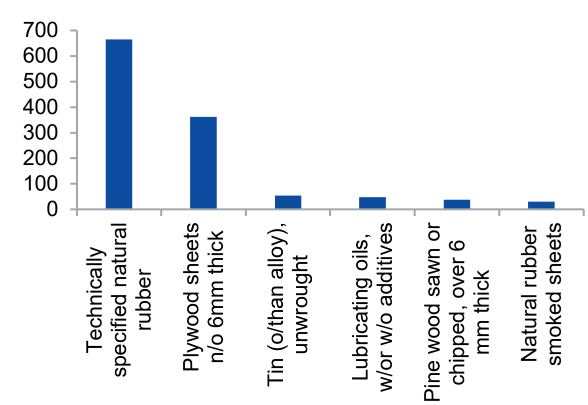
Source: World Bank.

Figure A.24: Textiles, apparel, and footwear have the highest exposure to US markets.
(exports to the US, percent of sector's total)



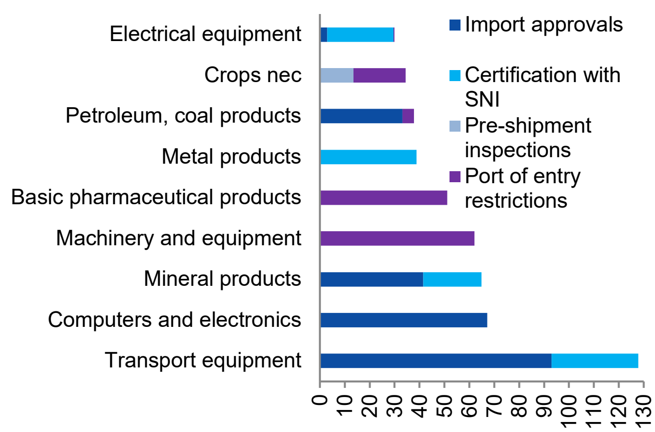
Source: USITC, World Bank.

Figure A.25: Exports of natural rubber, plywood, tin and others were exempted from higher tariffs.
(exports to the US, US$ million)



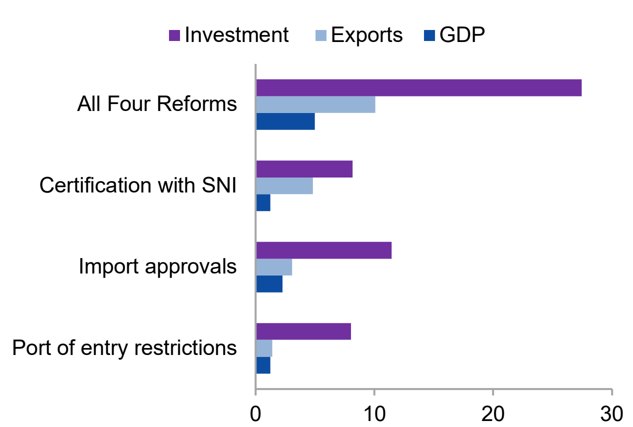
Source: World Bank.

Figure A.26: NTMs are often cumulatively applied and impose significant costs.
(percent tariff equivalent)



Source: World Bank.

Figure A.27: NTM reforms could have significant benefits for growth, exports, and investment.
(percent relative to base)



Source: World Bank.

Effective policy communication and protecting capital spending reduces business and consumers concern and boosts economic activity.

Communication and improving the quality of public spending are important to manage uncertainty. Large budget adjustments, institutional reorganization at ministerial and SOE levels, tax policy reversals and tax collection disruptions have heightened uncertainty. Compounded by global trade disruptions, this further increased concerns for investors, businesses, and consumers, affecting economic activity. These concerns eased as authorities sustained communication on policy directions, reform plans, and support packages, and doubled down on economic data publication like budget realization numbers, leading indicators, and other high frequency data. Clear communication and data transparency – important hallmarks of economic management in Indonesia – are crucial in managing shocks and reducing uncertainty. Furthermore, efficiency measures impacting infrastructure and human capital ministries raised service delivery concerns. Redirecting efficiency savings to infrastructure and human capital formation programs remains key to achieving higher growth and the Golden Indonesia 2045 Vision.

Public investment significantly boosts Indonesia's economic output, emphasizing the importance of enhancing its spending envelope in future budget allocations. A Bank staff simulation, using Input-Output table, shows that a US$1 increase in public investment raises Indonesia's output in the short-term by US$0.863. This result is within the range for EMDEs' multiplier (US$0.5-1.0) (Geli and Moura, 2023; IMF, 2014; Izquierdo et al., 2019). Moreover, using cross-country data, World Bank (2024) find that cuts in public investment tend to have a more pronounced negative impact on output in the long run: a US$1 cut in public investment leads to a US$1.3 drop in output. Meanwhile, the fall due to public consumption cuts is not statistically different from zero. Such outcome re-enforces the need to ringfence public investment and cut non-productive public consumption for improved budget efficiency.

Danantara could have a transformative role in Indonesia's development, but success is dependent on clear strategy, effective governance, transparency, and adherence to international standards.

Sovereign Wealth Funds (SWFs) can be pivotal tools for transforming volatile revenues into strategic assets. Typically funded by natural resource wealth or fiscal surpluses, SWFs can help achieve national objectives and manage state-owned enterprises (SOEs). Singapore's Temasek and Malaysia's Khazanah are notable examples of SWFs that combine commercial and strategic goals through SOE management, strong governance frameworks and clear mandates. In contrast, Norway's Government Pension Fund Global and the Abu Dhabi Investment Authority prioritize maximizing long-term returns mostly abroad, from natural resources (see Table A.2 for examples).

Indonesia's Danantara blends traditional SWF functions with an expansive domestic development mandate. Established under the revised SOE Law in 2025, Danantara manages US$900 billion in assets (about 64 percent of GDP) making it one of the world's largest SWFs. It supervises both Investment and Operating Holdings, is guided by an advisory board that includes global experts and aligns its initiatives with international standards.[35] Danantara aims to leverage SOE assets[36] through investment in key sectors like mineral processing, energy, oil refineries, and food security.

Danantara's hybrid model brings with it complex fiscal and governance risks that must be carefully managed. Danantara's creation may initially reduce short-term state revenues, with dividend income shifted from the budget to Danantara, potentially increasing the fiscal deficit by 0.2 percent of GDP. Over time, improved SOE governance and better investment outcomes could raise dividends and tax receipts, while reducing the need for capital injections. However, this is uncertain, and fiscal burden could increase if Danantara's investments underperform.

Transparency and accountability are crucial for Danantara's credibility. Although Indonesia adheres to fiscal deficit rules, the creation of Danantara raises concerns around contingent liabilities, given the scale of government-guaranteed SOE debt and potential future borrowing by Danantara itself. The SOE Law now provides legal protections to SOE boards of directors (BODs) to encourage risk-taking, but this must be paired with strong oversight mechanisms to prevent misconduct.

Danantara's success depends on adherence to global governance and accountability standards despite some risks. The consolidation of SOEs risk crowding out private sector investment, especially in commercially viable sectors. Monopoly rights granted under the new SOE Law for industries deemed vital to the state may erode competition and investor confidence. Furthermore, Danantara inherits a broad array of existing governance challenges from the SOEs it now manages. To fulfill its mandate, Danantara must adopt global best practices, such as the Santiago Principles and OECD SOE Governance Guidelines,[37] to ensure sound management, promote competitive markets, and avoid becoming a fiscal and institutional liability.

[35] Danantara is managed by Chief Executive Officer Rosan Roeslani (Minister of Investment and Downstreaming), with Pandu Sjahrir (ex-Vice President-Director, PT. TBS Energy Utama – a mining company) serving as Chief Investment Officer and Dony Oskaria (Deputy Minister of SOE) as Chief Operating Officer. Moreover, both Ministers of SOE and Finance are part of the Supervisory Board.

[36] Danantara is expected to oversee 847 SOEs (including subsidiaries), conducting comprehensive due diligence and implementing restructuring measures like mergers and closures.

[37] The internationally accepted best-practice guidelines for SWFs. There are 24 principles including: sound legal framework, clearly defined objectives, consistent with macroeconomic policy framework, good coordination with fiscal and monetary authorities, clear rules on funding and withdrawal, transparent and sound governance, independent operation, clear accountability and oversight, independent audit, subject to code of conduct, robust risk management, sound internal controls, regular disclose of information, promotes fair and transparent markets, and sound selection process of BODs.

Table A.1: Selected Macroeconomic Indicators.

	2022	2023	2024	2025	2026	2027
	Actual			WB projection		
Real GDP growth and inflation, percent change						
Real GDP	5.3	5.0	5.0	4.7	4.8	5.0
Real GDP Range – GOI reforms move forward				[4.7-4.9]	[4.8-5.3]	[5.0-5.5]
Consumer Price Inflation (average, %)	4.1	3.7	2.3	1.7	2.6	2.6
Consumer Price Inflation (end of period, %)	5.5	2.6	1.6	2.5	2.4	2.6
Private Consumption	5.0	4.9	5.1	4.9	4.9	4.9
Government Consumption	-4.4	3.0	6.6	-2.1	0.3	0.9
Gross Fixed Investment	3.9	3.8	4.6	6.1	6.2	6.3
Exports	16.2	1.3	6.5	4.8	5.1	5.5
Imports	15.0	-1.6	7.9	4.5	5.0	5.1
Fiscal accounts, central government, percent of GDP						
Revenues	13.5	13.3	12.8	11.9	12.3	12.4
of which Tax Revenue	10.4	10.3	10.1	9.9	10.3	10.5
Expenditures	15.8	14.9	15.1	14.5	15.0	15.1
Primary Balance	-0.4	0.5	-0.1	-0.4	-0.4	-0.3
Fiscal Balance	-2.4	-1.6	-2.3	-2.7	-2.7	-2.7
Central Government Debt	39.5	39.0	39.2	40.1	40.8	41.4
Balance of Payments, percent of GDP unless indicated otherwise						
Current Account Balance	1.0	-0.1	-0.6	-1.3	-1.6	-1.7
Exports, Goods and Services	23.9	21.2	21.7	22.6	22.5	22.6
Imports, Goods and Services	20.7	19.2	19.9	21.5	21.4	21.3
Net Foreign Direct Investment	1.4	1.1	1.0	1.2	1.3	1.5
Gross Reserves (months of imports of goods and services)	6.0	6.7	6.6	6.1	6.0	6.0
Memorandum items						
Nominal GDP (IDR trillion)	19,588	20,892	22,139	23,112	24,376	25,693
Real GDP Per Capita (IDR thousand)	41,952	43,599	45,320	46,966	48,751	50,726

Table A.2: Comparing Sovereign Wealth Funds across the globe.

	Indonesia's Danantara	*Norway's Government Pension Fund Global (GPFG)*	*Turkiye Wealth Fund*	*Abu Dhabi Investment Authority (ADIA)*	*Temasek Holdings*	*Indonesia Investment Authority*
Objectives	Development fund and SOE holdings.	Stable source of revenues, and savings for future generations.	Development fund.	Development and savings fund.	Development fund (initial) and savings fund (current).	Development fund (but not necessarily government projects).
Funding Sources	At initiation: consolidation of SOEs assets, with capital set at a minimum of IDR 1,000 trillion (USD 60.8 billion, 4.5 percent of GDP).					
In the future: mainly from SOE dividends	Revenues from commodities particularly oil and gas.	Transfers from SOEs, debt issuances, and securitization of public assets.	Oil related fiscal revenues.	Self-financing through dividends from portfolio companies, divestments, and fund investment earnings.	Capital injections from the State budget (USD 2 billion) and transfer of two SOE shares (USD 3 billion).	
Fiscal Relations	As Danantara is independent of central government, SOE dividends will be shifted from State Budget to Danantara. On the other hand, there will be no regular capital injections to SOEs except for special assignments (projects/subsidies).	GPFG provides a predictable revenue stream to the budget of around 6 percent of non-oil GDP.	Includes obligations from transferred SOEs, debt issuances, and financing of strategic projects.	ADIA's revenues come from petroleum income, though the specifics are not defined. There is no publicly disclosed rule on how much is transferred back to the central government, but ADIA must provide funds for withdrawal by the government as needed.	Liabilities include corporate tax, dividends owed to the government, and debts from bond issuance.	Operates independently but backed by government guarantee.
Investment Policy	Aims to support national projects focusing on mineral downstream sector, petrochemicals, oil refineries, food security and renewable energy. It will also form a joint venture with private firms, both domestically and globally.	GPFG portfolio is invested abroad with specific allocation of 60% equities, 35-40% fixed income and up to 5% on property, with real return averaging 3.6% annually since 1998.	Focuses on strategic sectors such as infrastructure, energy, technology, and financial services. Supports domestic economic development and selective foreign investments. Includes participation in Islamic finance.	Initially conservative, investing in sovereign debt of major currencies, but gradually diversified into international assets with a focus on long-term returns.	Focused on long-term, high-risk investments with a concentration in Asian equities. Initially centered on local industries but later expanded globally.	Focused on commercially viable, high-impact projects in sectors such as transportation, energy, healthcare, and digital infrastructure through co-investment with both SOEs and private firms.
Governance structure	The Board of Directors is composed primarily of private sector professionals, except for the head of Danantara (Minister of Investment), and the CIO (Vice Minister of SOEs). The Managing Directors are not affiliated with political parties. They are all appointed by the President for a 5-year term. The advisory board includes global experts.	Norges Bank manages the fund for the Ministry of Finance. The Executive Board, led by the central bank governor and deputy governor, includes five external members. Public oversight is provided by Parliament, the Ministry of Finance, the Central Bank, Norges Bank Investment Management, the Supervisory Council, and the External Auditor, each with specific roles and reporting duties.	Managed as a joint-stock company in the private company status, directly linked to the Prime Minister. The Board of Directors are private sector professionals appointed by the Prime Minister and they oversee the operations.	Fully owned by the Abu Dhabi government. However, it conducts its investment program independently without reference to the government or other institutions that invest funds on behalf of the government. Roles and responsibilities are legally separated among the owner, governing entity, and management.	Temasek is a private investment company that manages its own assets. Though fully owned by Singapore's Ministry of Finance, on behalf of the government, it operates independently. The Board includes political elites, but neither the president nor the government-as shareholders-can influence its investment decisions.	INA reports directly to the President, while its decision-making process remains independent of shareholder interests. INA uses a two-tier board system: a Supervisory Board, which includes the Finance and SOE Ministers and professionals, and a Board of Directors, consisting of professionals from leading institutions and corporations with diverse skills and backgrounds.

Source: Author's compilation based on official reports, websites and analysis.

B. A Roadmap from Homes to Jobs to Prosperity in Indonesia

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B. A Roadmap from Homes to Jobs to Prosperity in Indonesia

1. A Path to a Golden Indonesia 2045: Meeting President Prabowo's Housing and Employment Goals

President Prabowo has outlined ambitious initiatives for the nation's future, aiming to fulfill a constitutional promise of housing for all while pursuing the vision of "Golden Indonesia 2045." The President's social justice agenda prioritizes people and leverages Indonesia's vast resources,[38] seeking to establish a more equitable society, raise economic growth to 8 percent, and deliver 3 million homes each year. These goals are interconnected. The following report presents short-term opportunities to accelerate housing delivery and presents long-term strategies for achieving more equitable and sustainable economic growth. With the right interventions and investments, accompanied by an appetite for reform, the target of 3 million homes *can* be achieved. The recommended approaches are designed to leverage resources so that Indonesia can provide housing that is affordable, safe, and decent—for everyone.

Housing, which contributes 10 percent of GDP[39] and 7 percent of total employment, is an engine of economic growth and a source of prosperity for its people.[40] Every Rp 1 trillion invested in the housing sector can raise 6,000 people out of poverty and increase growth in 185 other sectors, including education and healthcare.[41] Further, the housing sector augments national tax revenues by 8 percent.[42] For most Indonesians, housing represents their largest expense and, sometimes, their only asset. Adequate housing offers numerous ancillary benefits: it elevates educational attainment, work opportunities, health, and well-being of its residents.

The right to housing is anchored in Indonesia's history. In its 1945 Constitution, the Republic of Indonesia declared: "Every person shall have the right to live well, materially and spiritually, and to settle in a house with a good and healthy environment." The 1950 Congress on Healthy Housing for People formalized housing as the state's responsibility and established public housing in Indonesia, likely introducing *Perumahan Rakyat* (people's housing) into the lexicon. Although the promise of housing for everyone has remained elusive in a nation whose population has more than quadrupled since its independence, the success of the administration's housing program could make this founding vision of Indonesia a reality.

Indonesia has a strong capacity to deliver housing and infrastructure at scale. The country boasts some of the best and largest home improvement efforts in the world (e.g., BSPS – *Bantuan Stimulan Perumahan Swadaya*, or Home improvement through Self-Help Housing), one of the most effective slum upgrading programs in history (KOTAKU – *Kota Tanpa Kumuh*, or City without Slums), the world's biggest property titling program (PRONA – *Proyek Operasi Nasional Agraria* or Agrarian National Program), and world-class capacity for post-disaster housing and settlement reconstruction. During 2015-2024, the One Million Homes Development Program (PSR – *Program Sejuta Rumah*) added more than 10 million housing units, prioritizing 75 percent for low-income residents.[43]

[38] President Prabowo's social justice agenda and natural resource initiatives are outlined in Asta Cita, which is grounded in the principles of Pancasila (belief in one God, just and civilized humanity, national unity, democracy guided by wisdom and representation, and social justice for all Indonesian people).
[39] When infrastructure is included, housing contributes 13 percent of GDP. For comparison, tourism contributes 4.8 percent, mining 10.5 percent agriculture 12.5 percent, wholesale and retail 12.9 percent.
[40] World Bank original calculations for this report.
[41] As reported in PT SMF and DTS Indonesia (2023) and supported by Cattaneo et al. (2007).
[42] World Bank original calculations for this report.
[43] 2016–2024 data was obtained from "1 Million Homes Program," Ministry of Public Works and Housing, Directorate General of Housing and Directorate of Public and Commercial Housing, accessed April 22, 2025, https://programsatujutarumah.pu.go.id/. 2015 data was obtained from Ministry of Public Works and Housing, *Profile and Assessment of Housing and Settlement Conditions in Indonesia* (Jakarta: MPWH, n.d.).

As an established partner with Indonesia, the World Bank has supported each of these programs. Jointly through the National Affordable Housing Program (NAHP), more than 1 million homes have improved in quality and disaster resiliency countrywide with BSPS (2017–2023).[44] The National Slum Upgrading Project (NSUP) supported KOTAKU, which leveraged US$1.4 billion in public financing, enhancing infrastructure for more than 2 million housing units (2016–2023). Through participatory mapping and land administration reforms, the One Map Project supported PRONA by surveying and mapping 8.36 million land parcels to enhance tenure security and registered over 4.2 million land rights in rural areas (2018–2024), accelerating the local economy by enabling credit access. The Central Sulawesi Rehabilitation and Reconstruction Project improved conditions in 3,880 homes (plus 17 schools and one university) and delivered 10,000 water connections and settlement infrastructure in 30 areas (2019–2024).

The success of these initiatives hold promise for similar efforts to be scaled and support President Prabowo's housing and employment objectives. The following recommendations optimize budgetary resources and mobilize more private capital. Indonesia can make timely, cost-effective, and strategic investments to achieve its ambitious targets.

1.1 The Opportunity

Large cities and metropolitan areas drive growth and offer better jobs and higher earnings. Indonesia's urbanization growth return on GDP has improved in the last decade (2013–2023) and currently stands at 2.7 percent.[45] This is comparable to China's 2.8 percent and the average across East Asia and the Pacific of 3.1 percent.[46] On average, urban workers in Indonesia earn 40 to 50 percent more than their rural counterparts, highlighting urbanization as a social escalator that lifts millions out of poverty. Large cities and metropolitan areas are essential to reaching economic growth targets (Table B.1).

Indonesia's major cities—including large urban centers and metropolitan areas—require more affordable housing. In the Jabodetabek metropolitan area, and Jakarta City in particular, approximately one-quarter of the population lives in overcrowded homes.[47] Talented Indonesians seeking opportunity in a metropolitan area would need to dedicate 10 additional percentage points (ppts) of their budget to move to the Jabodetabek metropolitan area and 20 additional ppts to move to Jakarta City. Defying global trends, Indonesians are moving out of high-income areas due to a lack of affordable housing.

But with the right mix of investments and reforms, Indonesian cities can build affordable homes and open their doors to attract the next generation of talent—both national and foreign. Housing and infrastructure are magnets for talent and drivers of social mobility. By investing in these sectors, Indonesia can capitalize on an opportunity to encourage entrepreneurship and creative industries that boost the economy. In Indonesia, cities host 76 percent of the middle class; meeting the demand for affordable housing will be crucial to support the social mobility of the 115 million individuals in the aspiring middle class.

Table B.1: Cities Drive Economic Growth.

Classification	Population Size	Cities With Average GRDP Growth Rate > National GDP Growth (2023)	Share Of Total (High Growth Rate)
Small	<50,000	0	0%
Medium	50,000-100,000	1	2%
Large	100,000-1,000,000	33	70%
Metropolitan	1,000,000-5,000,000	13	28%
Megapolitan	>5,000,000	0	0%

*Total cities with average Gross Regional Domestic Product (GRDP) growth rate > national GDP growth (2023) is 47 out of 94 cities (DKI Jakarta Province considered as one city).
Source: BPS (2022-2023); Susenas (2020); World Development Indicators (2023). World Bank staff calculations.

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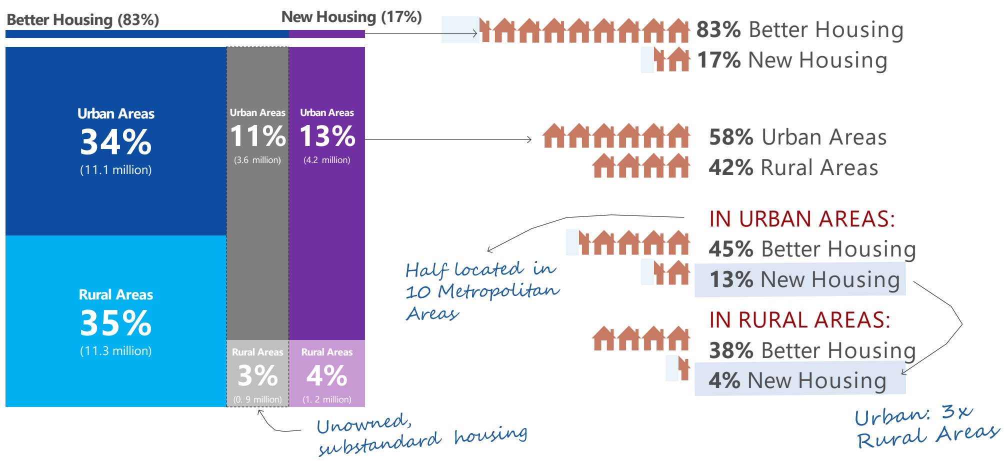
44 BSPS, as the Government program, started in 2006.
45 Urbanization growth return on GDP refers to the average increase in GDP associated with each percentage point increase in urban population share.
46 World Bank staff calculations using World Development Indicators, and United Nations, *World Urbanization Prospects: The 2018 Revision.*
47 World Bank original calculations for this report with data from Susenas (2023).

1.2 People-First Housing

Maximizing housing investments means better homes, not just new homes. Currently, five times as many Indonesian households require better housing than new housing (26.9 million households compared to 5.4 million), as shown in Figure B.1. However, financing for new homes comprises 88.6 percent of the government's housing budget,[48] compared to 11.4 percent dedicated to improving housing through BSPS. The government allocates an average of Rp 25 million (US$1,500) per unit to improve existing housing and more than Rp 100 million (US$6,000) on average to construct a new unit.[49]

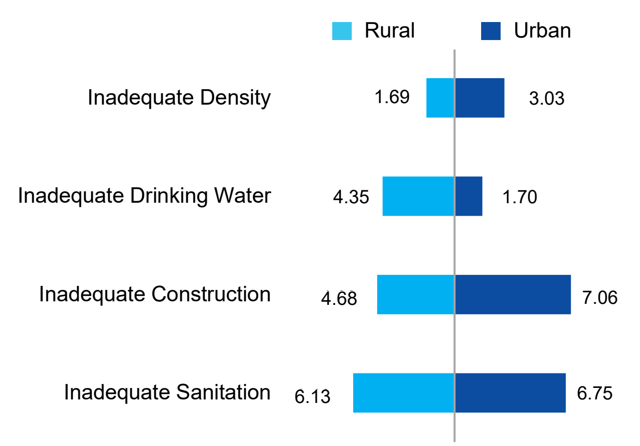
Figure B.1: Backlog of New and Better Housing.



Source: Ministry of Public Works and Housing, HREIS (2023).

Housing and infrastructure investments can complement President Prabowo's commitment to family health. As the government seeks to improve the health of children and families through the Free Nutritious Meal program, a complementary effort is improving housing quality and safety through a combination of targeted housing supports and infrastructure investments. While nine percent of Indonesians live in poverty,[50] one in three Indonesian households live in substandard conditions (Figure B.2).[51] This has secondary impacts on community health. For example, families living in homes with dirt floors are more exposed to illness, extreme weather, and other hazards, lowering both their health and educational outcomes. Approximately 45 percent of Indonesians live in homes with lead paint. Lead

Figure B.2: Substandard Housing in Urban and Rural Areas. (in millions)



Source: Ministry of Public Works, HREIS (2023).

[48] World Bank original calculations for this report with data from Government of Indonesia, Housing Budget, 2015–2024; Ministry of Housing and Settlements, 2025; and Performance Reports of Directorate of Implementation of Housing Finance and DG Infrastructure Financing, Ministry of Public Works and Housing.

[49] Estimates for improving housing are based on BSPS and new housing through FLPP (*Fasilitas Likuiditas Pembiayaan Perumahan*, or Housing Financing Liquidity Facility), which is now channeled through BP TAPERA (*Badan Pengelola Tabungan Perumahan Rakyat*, or Public Housing Savings Management Agency). FLPP constitutes most of Indonesia's new housing allocations (a number that has tripled since 2015), subsidizing 1.2 million first-time mortgages for low-income families. New housing has also been supported by other public programs, such as Vertical Housing and Subsidi Selisih Bunga (SSB, or Interest-Rate Subsidy), and, to a lesser extent, Special Housing Infrastructure and Services, *Bantuan Pembiayaan Perumahan Berbasis Tabungan* (BP2BT, or down payment assistance based on savings), *Subsidi Bantuan Uang Muka* (SBUM, or down payment assistance), and TAPERA. Data is sourced from the Ministry of Housing and Settlements. Data for SBUM in 2024 was not available in April 2025.

[50] According to BPS, Indonesia Poverty Profile in March 2023, poverty line was Rp 550,458/capita/month.

[51] Defined according to the Ministry of Public Works, HREIS, BPS: lacking at least one of the following: sufficient living space of at least 7.2 square meters per person, access to improved drinking water, access to improved sanitation, and durability (roofs from concrete, tiles, zinc, or wood/shingles; walls from brick walls, plaster/bamboo weave/wire, or wood/boards; and floors from marble/granite, ceramic, parquet/vinyl/carpet, tiles/terrazzo, wood/boards, or cement/red brick).

exposure is a serious health concern, especially for children, and can cause developmental delays, learning disabilities, and stunting. Poor housing conditions lead to larger problems, as well: In Jakarta City, home to 4 percent of the national population, it is suspected that many landed homes without access to the public water system are relying on wells, which is contributing to the sinking of the lowland coastal city.

Indonesia must stay one step ahead of housing needs, particularly given high disaster risk. In the past seven years, disasters have impacted more than 7.1 million Indonesian homes, 86.3 percent due to flooding.[52] Instead of waiting for disasters to strike and "Build Back Better" after devastating loss of life and financial investments, the recommended actions below encourage a "Build Better Before" approach.

Bridging the housing gap means ensuring access to the right housing solution, in the right place, at the right price. While building new units represents part of this strategy, it cannot be the only approach. Not everyone needs a new home—most Indonesians need a better home. Nor is homeownership a requirement: rental options can also contribute to a diverse set of housing solutions. Putting people first means enabling all Indonesians—including low-income families and the aspiring middle class—to access safe, affordable housing and the opportunity to build a better future. Leaving no one behind, this administration can forge a path to shared prosperity by beginning with where people start their days—at home.

1.3 Unified Pathways for a Prosperous Indonesia

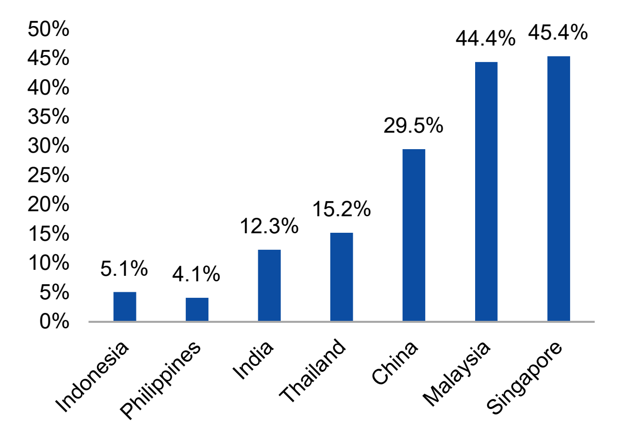
Meeting the target of 3 million housing solutions annually requires at least US$3.8 billion in direct public investments every year.[53] There are three possible sources to close this financing gap: the government, direct savings from families, and indirect savings from capital markets. For instance, a simulation conducted for this report shows that the government would need to spend at least 75 percent more on housing than currently allotted and increase the efficiency of existing programs by 60 percent to reach its housing target.[54] The recommended pillars below address the possible funding sources while improving the efficiency of every government dollar spent.

Indonesia has the building blocks to promote family savings and develop sources of capital for mortgages. With the right reforms, there is a clear opportunity to release the potential of the country's housing sector. To make this capital available, Indonesia must develop its capital markets to better support mortgage lending.[55] Emerging market economies have used various approaches to catalyze the mortgage market. Several governments have successfully used provident funds as a source of capital for mortgages (as in Brazil, Philippines, and Mexico) or stimulated voluntary contractual savings with premiums (Kazakhstan). Other governments have stepped in to jumpstart the bond market by establishing liquidity facilities or securitization platforms and, in some cases, offering government guarantees for mortgage bonds (Egypt, Malaysia, Thailand). Indonesia needs to strike a balance between costs and stability, particularly in low-income housing finance.

To achieve its vision, Indonesia can strategically attract private capital. Indonesia's housing-sector budget represents a relatively modest 0.18 percent of GDP (the OECD average is 0.46 percent).[56] The nation's mortgage debt is 5.1 percent of its GDP, a share that has grown over the last decade but remains low (Figure B.3). Typically, a mortgage-debt-to-GDP ratio in the double digits indicates lenders are effectively serving diverse households through collateralized lending. Crucially, the housing sectors of OECD countries rely heavily on diversified private finance, with mortgage lending averaging around 50 percent of GDP. In contrast, a handful of Indonesia's largest banks offer most mortgages. However, Indonesia is developing two key conditions for a strong mortgage market: a stable macroeconomic environment with price stability and clearly defined property rights.

[52] *Badan Nasional Penanggulangan Bencana* (BNPB), *Data Informasi Bencana Indonesia* (DIBI)
[53] To put this in perspective, all outstanding corporate bonds in local currency together totaled Rp 461 trillion (US$28 billion) in Q1 of 2024, while the sovereign wealth fund was launched with Rp 300 trillion (US$18 billion) of assets under management (with the goal of reaching US$900 billion).
[54] A business-as-usual scenario would require triple the budget used to achieve the 1 Million Homes target, to achieve the 3 Million Homes target. A lower budget increase would require efficiency gains in the utilization of public funding.
[55] In well-developed mortgage markets, diversified pools of investors buy long-term fixed-income securities backed by residential mortgages. In the European Union, for instance, investors hold more than €3.3 trillion (US$2.9 trillion) in mortgage-backed covered bonds (European Covered Bond Fact Book, 2024). The development of a capital market with investor demand for long-term paper (with 5-year maturity or more) relies on a stable economic and policy environment. Government guarantees and long-term bond purchases can kickstart the process.
[56] World Bank original calculations for this report with data from OECD, "PH3.1 Total government spending on housing allowances in selected OECD countries," 2022, https://www.oecd.org/content/oecd/en/data/datasets/oecd-affordable-housing-database.html.

Figure B.3: Mortgage Debt to GDP Ratio.



Source: Mortgage Loans (as percent of GDP), Helgi Library (2023); World Economic Outlook Singapore Datasets, IMF (2023).

Reforms must address not only financing, but also promote resilient construction standards, advanced technologies, and supporting infrastructure to ensure long-term sustainability. Indonesia needs to standardize housing data further to track compliance with resilience standards for all government-supported units while continuing to adapt construction technologies to meet the needs of its people and counter geophysical and climate hazards. Delivering housing solutions at scale requires strong institutions and sustained investment in supporting infrastructure and services, such as water, sanitation, solid waste management, transport, and connectivity to reduce the country's 77,000 hectares of slums.[57] Therefore, the government must play a dual role: regulating and establishing standards while also investing in infrastructure and services to close existing gaps, thereby creating markets and attracting private capital investments.

Indonesia holds untapped housing potential. The government can leverage existing programs, strengthen land management systems, and mobilize private capital through a comprehensive package of policy reforms. By applying innovative solutions and advancing targeted reforms to build trust among local and international investors, Indonesia is well-positioned to transform its housing sector into a driver of inclusive economic growth. The following strategy identifies two pillars to optimize funding and accelerate the delivery of resilient, affordable housing for all Indonesians.

2. Pillar 1. Housing and Infrastructure Investments

2.1 Next-Generation Settlement and Neighborhood Transformation

Indonesia's landmark successes with BSPS and KOTAKU demonstrate that there is a path toward housing everyone, particularly by jointly addressing poor settlement areas and home improvement. As two-thirds of the urban housing gap is concentrated in 74 cities and 42 urbanized districts, this approach would amplify investments in housing, basic services, and infrastructure. Transforming homes and neighborhoods would also involve property regularization and private investment. The lowest-cost intervention would provide access to basic services and infrastructure at an estimated Rp 25 million per unit. On the higher end, combining BSPS with neighborhood improvement efforts would cost an estimated Rp 30 million per unit. This intervention could be supplemented with housing microfinance loans. Pursuing a strategy of property regularization would maximize increases in property values and encourage home investments.

The expected return on investments from the outlined strategy is high. For US$1 billion in public investment, we expect 750,000 direct and indirect jobs, and up to 1 million homes with access to improved housing and settlement infrastructure.

Proposed strategy

Build an integrated BSPS-KOTAKU collaboration platform to address the qualitative housing backlog and reduce slums nationwide. Combining BSPS and KOTAKU to comprehensively address the qualitative backlog and substandard housing conditions through home renovation and settlement infrastructure improvement holds opportunities to apply innovative approaches and deliver quick results. The self-help approach of BSPS has proven to create jobs that are placed locally while simultaneously moving the building material industry to each area. This strategy needs regulatory reforms, policy updates, and modifications to regulatory and planning documents to bring poor settlement conditions in line with housing standards and enhance policy effectiveness. To operationalize this

[57] National Medium Term Development Plan 2025-2029.

initiative, the government would need to reform the regulations that support implementation mechanisms to integrate BSPS and KOTAKU, adding clear eligibility criteria, defining the role of local governments, and enabling private sector participation.[58]

Linking BSPS with housing microfinance would enhance financial access for low-income households and drive economic opportunities through incremental housing improvements. However, a supportive regulatory framework would be required to enable microfinance institutions and similar entities to offer non-productive housing loans tailored to the needs of informal and underserved segments. In parallel, the broader ecosystem for housing microfinance, including alternative credit scoring mechanisms and contractual savings schemes, could be strengthened through closer collaboration between the Financial Services Authority (OJK), Ministry of Finance, and Ministry of Housing and Settlements.

Enable, incentivize, and encourage local governments to replicate the integrated housing and settlement upgrading programs (BSPS and KOTAKU) with their own resources.[59] Building on existing momentum, local ownership can be further encouraged and scaled. DAK Integrasi, which combines home improvement and slum upgrading, including water and sanitation services, provides an exemplary integrated model to build capacity at the local level.

The BSPS-KOTAKU collaboration will create a platform accessible for multi-sector agencies, stakeholders, and international development partners to strengthen coordination, improve housing standards, and enhance settlement infrastructure. To support this, integrating the databases and improving housing and settlement planning documents such as *Rencana Pembangunan dan Pengembangan Perumahan dan Kawasan Permukiman* (RP3KP) and Slum Improvement Action Plans (SIAP) at the city level and Community Settlement Plans at the community level would be required to ensure data consistency across levels and improve evidence-based planning. Furthermore, optimizing the Management Information Systems (MIS) and Grievance Redress Mechanisms (GRM) would improve program effectiveness and impact.

It is essential to strengthen the capacity of the Ministry of Housing and Settlements to manage integrated housing, settlement development programs, and land provision. Clear institutional arrangements, responsibilities, and coordination mechanisms among ministries and relevant stakeholders responsible for housing, settlement infrastructure, and land provision are needed. For instance, coordination between the Ministry of Public Works and the local governments for settlement infrastructure such as water, sanitation, solid waste management, roads, and drainage. Additionally, Indonesia must enhance the capacity of local governments to align spatial planning (RDTR/RTRW), land readiness, and community engagement with the national housing and settlement infrastructure strategy through training, technical assistance, and knowledge sharing.

Indonesia needs to continue developing regulations to integrate disaster risk reduction into spatial planning alongside unified operational frameworks for resettlement, land provision, reconstruction financing, and technology deployment in the aftermath of disasters. This regulatory gap often leads to delays, fragmented implementation, and missed opportunities. For example, following the 2018 Central Sulawesi disaster, over 110,000 homes were damaged or destroyed, and more than 172,000 people were displaced. Yet, due to unresolved land issues and outdated land use plans, permanent housing construction was delayed by over a year, leaving thousands in temporary shelters well into late 2019.[60] Institutionalizing procedures, such as pre-approved land arrangements, interagency coordination protocols, and expedited financing mechanisms, can enable faster and more adaptive recovery. These guidelines should clearly define responsibilities for land readiness, reconstruction approvals, and the deployment of disaster-resilient technologies. This is a crucial step to protect all Indonesians, especially the most vulnerable, who bear a disproportionate burden when disasters occur. A unified, national housing dataset can support disaster risk planning and management by tracking renovations, home improvements, and poor-quality housing, which are often informal. This effort would need to be accompanied by regularization initiatives.

[58] This requires reviewing and aligning the assessment criteria under Ministerial Regulations No. 14/2018 and No. 2/2016 with national laws on housing and local government (UU No. 1/2011 and UU No. 23/2014), to support integrated housing and slum upgrading programs. Spatial planning instruments—such as RTRW and RDTR—should also be embedded as key references in planning and targeting interventions. Ministerial Regulation (Permen) PUPR No. 14/2018 on Slum Area Prevention and Improvement; Permen PUPR No. 2/2016 on Slum Housing Quality Improvement; Law No. 1/2011 on Housing and Settlement; Law No. 23/2014 on Local Government.

[59] More than 30 local governments have replicated BSPS and KOTAKU model using their local budgets.

[60] World Bank. *Environmental and Social Review Summary: Central Sulawesi Rehabilitation and Reconstruction Project.* Washington, DC: The World Bank, May 18, 2019.

2.2 Transformation of Urban Areas: New Housing and Growth

In Indonesia, achieving an 8 percent economic growth rate will depend on, among other things, the housing sector's performance in its urban centers. Large cities serve as the main engines of economic growth (Table B.1). However, land is limited, and increasingly high housing costs continue to deter skilled workers from settling in urban areas. Nearly 80 percent of Indonesia's new housing backlog is concentrated in urban areas, with the most significant gap in metropolitan areas like Jabodetabek and emerging metro areas like Bandung, Makassar, and Surabaya.[61] Commercial housing is double the cost of subsidized housing in the Medan metropolitan area and four to five times higher than the subsidized housing price in the metropolitan areas of Bandung, Surabaya, and Jabodetabek.[62]

Local governments have embraced national government initiatives and can partner in the next generation of infrastructure projects. For example, DKI Jakarta has set an example by providing public housing (and other public facilities) using land value capture schemes (LVC) in various locations in Jakarta, such as Pulo Gebang – East Jakarta, Daan Mogot – West Jakarta, and Muara Baru – North Jakarta.[63]

Simultaneously, crucial infrastructure investments can attract private financing for housing and revitalize cities. For instance, the government has invested US$5.5 billion in transport infrastructure.[64] To fully realize its benefits, Indonesia could focus on large-scale housing development around transport hubs by engaging local governments and leveraging private sector investment.

These initiatives have a high expected return on investment: <u>Private capital of US$3+ mobilized for every US$1 of public contribution in land or strategic infrastructure investment.</u>

Proposed strategy

Transit- and housing-oriented development can make urban areas robust economic centers where residents can conveniently access work, school, recreation, and commerce (Figure B.4). Delivering affordable, resilient, urban housing relies on an integrated, scalable approach built on two core components: 1) linking land and public asset management with institutional mechanisms and financial tools in a comprehensive framework, and 2) enabling and tracking compliance with resilient standards through data-driven and innovative construction technologies.

Public land assets—typically owned by the local government[65]—can be identified, recorded, and managed more systematically, helping to locate available land for residential development. Indonesia can improve land and housing delivery by measuring the number of buildable housing units using detailed spatial plans, estimating the land required to meet the housing backlog, and identifying suitable locations.[66] Such an assessment at the city and metropolitan level, combined with an adequate inventory of public assets—and a strategy for managing them—could reveal untapped business opportunities and guide local government decisions. Improved public asset management, including land banking, can enable the acquisition and consolidation of land in strategic locations for housing-oriented development and transit-linked infrastructure. The potential for leveraging underutilized public assets is high. For instance, there are 144 hectares and 2,585 hectares of available public land in Jakarta and Yogyakarta, respectively.[67]

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[61] According to World Bank original calculations with data derived from HREIS (2023).
[62] According to World Bank original calculations (2024), using the maximum subsidized housing prices as stipulated in the Minister of Public Works and Housing Decree Number 689/KPTS/M/2023.
[63] DKI Jakarta Provincial Public Housing and Settlement Areas Agency.
[64] Seven mass public transit in five metropolitan areas within period of 2015 – 2024, which include Light Rail Transit (LRT) in Palembang, Mass Rapid Transit (MRT) Phase 1 in Jakarta, LRT Phase 1 in Jakarta, LRT in Jabodebek, Railway system in Makassar, Bus Rapid Transit (BRT) in Bandung metropolitan area, and BRT in Medan metropolitan area, according to data by Bappenas, 2025.
[65] Central Government asset, managed by Ministry of Finance, LMAN (Lembaga Manajemen Aset Negara), technical line ministries, and Land Bank (Bank Tanah) may also be optimized.
[66] Based on a World Bank study, "Assessing Land for Housing in Indonesia," 2025.
[67] Based on data from Ministry of Public Works, "Profile and Assessment of Housing and Settlement Conditions in Indonesia," n.d.

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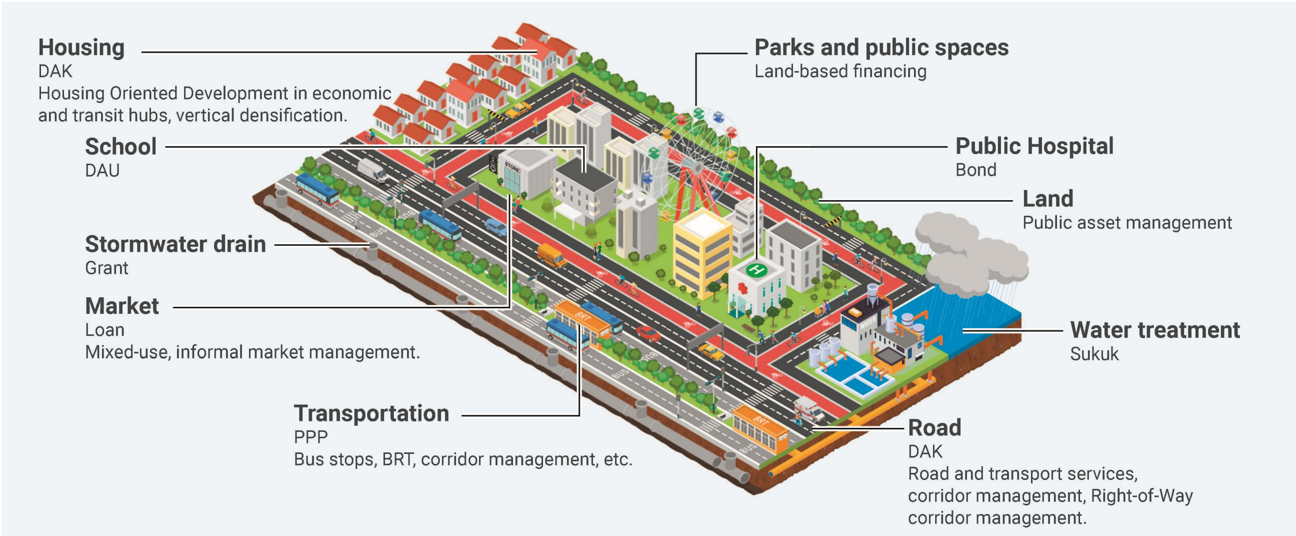
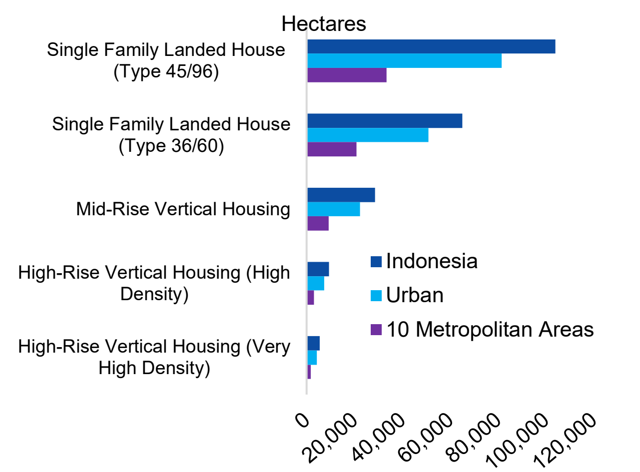
Figure B.4: Illustration for Leveraging Blended Financing for Large-Scale Integrated Infrastructure Projects.



Source: World Bank original illustration (2025).

Assessing land suitability for housing at the city and metropolitan levels means aligning land use with appropriate affordable housing types and densities based on income levels, risk exposure, and resilience needs, while evaluating their social, economic, and environmental impacts. To address the new housing gap, Indonesia needs 104,000 hectares to build 5.4 million single-family homes nationwide (Type-45 at 52 units per hectare).[68] However, if very high-density vertical housing is prioritized (1,000 units per hectare), the land requirement would decrease to 5,400 hectares (Figure B.5). Translated to the city scale, this means that for Semarang to close its quantitative housing gap, 55,349 Type-45 units require 1,063 hectares, but only 55 hectares for very high-density vertical housing.[69] The housing sector faces a trade-off: low-density housing requires more land and incurs higher infrastructure and service delivery costs. In contrast, high-density development can enhance land use efficiency, reduce emissions, and lower the costs associated with infrastructure and service delivery.

Figure B.5: Land Required to Close the Quantitative Housing Gap.



Note: The housing density offered by each type: Single Family Landed House (Type 45/96): 52 per Ha; Single Family Landed House (Type 36/60): 83 per Ha; Mid-Rise Vertical Housing: 190 per Ha; High-Rise Vertical Housing (High Density): 580 per Ha; High-Rise Vertical Housing (Very High Density): 1,000 per Ha.
Source: World Bank staff original calculations for this report (2025).

A robust and integrated data system is a core enabler of scalable and resilient housing. The government can strengthen Indonesia's housing data systems by integrating HREIS (Housing and Real Estate Information System) with RumahQu (Housing Queue) to align updated housing data and standards, alongside monitoring and evaluation to track supply, quality, and performance. Nationally synchronized housing data, including HREIS, RumahQu, and the Residential Property Price Index (RPPI), along with increased survey frequency, supports property rights, streamlines processes, enhances emergency response, and enables targeted interventions. Furthermore, a national data and coordination platform could help

[68] Type-45 refers to a typical landed housing unit with 45 square meters of floor area, commonly used as a benchmark for middle- and lower-middle-income housing in Indonesia.
[69] World Bank original staff calculation, "Assessing Land for Housing in Indonesia," 2025.

monitor compliance with licensing and enable public–private partnerships in on-demand housing projects. Capacity-building programs can be introduced to ministries[70] and local governments. Joint platform and incentive frameworks can keep Indonesia ahead of the curve and advance resilient, inclusive housing solutions nationwide.

With improved data collection and management, innovation in construction and financing would accelerate scalable, resilient housing delivery. Strategic government incentives and blended public-private financing can attract private-sector investment and drive the adoption of innovation and modular housing technologies—such as RUSPIN (*Rumah Unggul Sistem Panel Instan*, or Advanced Instant Panel System House) and RISHA (*Rumah Instan Sederhana Sehat*, or Simply and Healthy Instant House)—which have already been used in more than 60,000 units, primarily for post-disaster housing. Scaling these technologies nationwide with localized support can help "Build Better Before" and address regional needs. Promoting innovative construction also strengthens the workforce and creates quality jobs. To support this transformation, clear regulations and policies tailored to various housing types, skills training, and inclusionary zoning are essential to ensure affordability and social inclusion. Incentives such as expedited permits, increased floor-area ratios, co-investment, green certification, and carbon credits can further promote resilient construction, safeguard housing investments, and reduce vulnerability.

Indonesia's national SOEs (BUMN) and city-level Regional Owned Enterprises (BUMD) could play a pivotal role as urban operators if tasked with planning, managing, and delivering integrated urban development projects.[71] These operators would serve as institutional anchors for implementing large-scale housing and multisectoral urban investments. Their mandate would need to be strengthened, providing them with legal authority to represent local governments, coordinate across sectors, and align land use with infrastructure and service provision. They would also require the capacity to prepare and package integrated projects, manage public assets and land, and operate public-private partnerships by entering into contracts to deliver complex, area-based investments. While urban operators could help overcome common coordination challenges, the local governments could explore alternative financing options such as loans, municipal bonds, and *sukuk* (syariah bonds) to support BUMN, BUMD, and the central government in co-financing local government-led initiatives. Jakarta Mass Rapid Transit demonstrated the role of such BUMD, including leveraging alternative financing options such as LVC.[72]

National regulations could clarify the roles of state- and regional-owned enterprises, while ensuring effective coordination with local governments and private developers. Regulatory and legal changes are needed to enable public asset management aligned with land use plans and housing policies, facilitating more strategic use of land and government-owned assets to support urban housing delivery. The government has identified 79,925 hectares of abandoned land. Assessing the suitability of these areas could help determine the portion that could be used to support the 3 Million Housing Program.[73] Harnessing the full potential of this public assets, combined with the recommended regulatory changes, would enable the government to better leverage public–private partnerships and mobilize private investment for urban housing. To effectively tackle critical housing challenges, especially for low-income populations, the government should offer sufficient incentives to improve housing quality and upgrade settlements to enhance residents' socioeconomic conditions. To address the backlog, the central government could collaborate with local governments by providing incentives for quality affordable housing units through self-help and public–private partnership modalities, encompassing improvement, rental, and ownership.[74]

With these elements in operation, prioritizing transit- and housing-oriented development in metropolitan areas offers a pathway to consolidate fragmented growth, attract private investment, and enhance urban productivity and resiliency. The government can promote strategic spatial planning in key economic centers and integrated development areas, prioritizing high-density vertical housing and mixed-use developments near transit nodes and major economic centers.

[70] For instance, the Ministry of Public Works, the Ministry of Housing and Settlements, the Coordinating Ministry for Infrastructure and Regional Development, Central Statistics Agency, and so forth.
[71] Based on a World Bank study, "Supporting Implementation Modalities for Climate-Smart Urban Transformation in Jakarta," 2024.
[72] DKI Jakarta has used the three LVC approaches altogether for different projects: tax-based, fee-based, and development based. All of those instruments are included in the Perpres No.79/2024 and, thus, have the potential to be replicated.
[73] Based on data from Ministry of Agrarian Affairs and Spatial Planning, "Spatial and Land Planning Policies to Support the 3 Million Homes Program," 2024.
[74] According to the Indonesia Housing Grand Design 2020-2045 published by the Ministry of Public Works and Housing.

3. Pillar 2. Policy and Institutional Reforms

3.1 Public Housing Finance: Doing More with Less

The previous recommendations focused on maximizing the impact of public investments. But closing the financing gap for housing requires going beyond public spending to increase families' savings and the availability of private capital—and that means considering several changes to how public housing finance is structured and what it offers. Today, the Indonesian housing finance market comprises a small, high-income segment that banks serve through their own funding sources at variable rates, and a larger segment of lower-income earners heavily dependent on long-term government fixed-rate funding at deeply concessionary rates. Informal workers are largely excluded: they constitute more than half of the Indonesian labor force, but access only 2.5 percent of the country's mortgages.

Key gaps in institutional and program designs are causing people to be left behind:

- For households with the lowest incomes, the BSPS subsidy scheme has supported disaster resilience improvements with assistance from regional government facilitators. These facilitators provide guidance to ensure compliance with resilient standards. However, the program does not include housing microfinance, which limits financial leverage. Based on consumer research under the World Bank's National Affordable Housing Program in 2020, this segment reveals a preference for repairing their existing homes over building new ones.
- For low-income communities, or *Masyarakat Berpenghasilan Rendah* (MBR),[75] the FLPP-funded mortgage loans[76] exclusively support new units purchased from developers.[77] The high demand for developers using this government funding prompts low-cost ceilings for fiscal reasons, leading to substandard construction quality. Consequently, most households opt to self-build (at least 70 percent), making families the largest financiers of housing in Indonesia.
- For non-MBR housing excluded from banking services,[78] the 2016 TAPERA Fund was designed to collect savings from government and private-sector employees, but it remains non-operational. Furthermore, it has been directed to serve the MBR segment, leaving young households in expensive urban areas with limited financing options.

There are several other significant barriers to housing finance. In addition to limited mortgage products, using property as mortgage collateral is challenging in Indonesia given the absence or weakness of land titles, difficulty in enforcing one's ownership rights, costs or frictions in registering titles or obtaining construction permits, insufficient access to urban services, and, in particular, low-quality housing construction. There are few legally feasible alternatives, such as financial leasing or non-collateralized housing lending.

Short-term actions would lead to a significant expected return on investment. <u>Reforms and institutional coordination can multiply the number of units in the *status quo* scenario.</u>

Proposed strategy

Achieving the government's 3 million homes goal requires developing both private- and public-sector housing finance in parallel. To this end, public housing finance would need to undergo several shifts. Subsidies need to be rationalized to increase efficiency and reduce costs; public-sector incentives need to strike a balance between new and better housing solutions, focusing on mobilizing private investment both from family savings and capital markets; and public housing programs need to be progressively repositioned to change their scope within the ecosystem of lenders, developers, and borrowers, as well as involve microlenders.

<u>*Pragmatic Subsidies: Reforms to Offerings*</u>

Public housing finance instruments are geared towards making initial mortgage payments affordable. There are two ways to do this effectively: by *temporarily* reducing interest rates or by *temporarily* reducing principal payments. Instead, under FLPP, Indonesia has chosen to *permanently* reduce loan

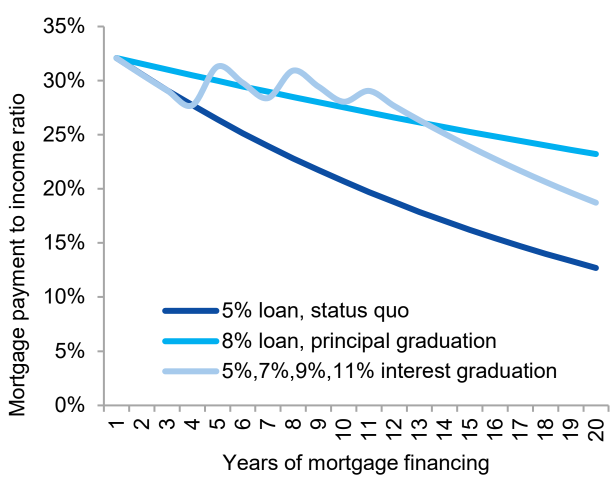
[75] Housing up to Rp 180 million is considered MBR housing.
[76] FLPP (*Fasilitas Likuiditas Pembiayaan Perumahan*, or Housing Financing Liquidity Facility) is now channeled through BP TAPERA (*Badan Pengelola Tabungan Perumahan Rakyat*, or Public Housing Savings Management Agency).
[77] Under the World Bank–funded NAHP, which tested down-payment subsidies as an alternative to the government deposit, only 1 out of 9 participating lenders was willing to finance self-construction. Lending is scarce because the underwriting and servicing costs for these financing techniques are high for banks relative to the size of the principal.
[78] This applies to housing between Rp 180 million and 500 million.

interest rates to 5 percent and keep that reduced level fixed for 20 years. This yields a modest 0.5 percent return for the government, compared to the 7 percent it must pay to bond investors. Indonesia's nominal GDP growth, a proxy for nominal household income growth, is 5 percent.

To reduce costs, the government could shorten the fixed-rate commitment to 10 years and then switch to a floating, market-determined interest rate that could be stepped up over the next 10 years. Alternatively, more acceptable returns of 4 to 5 percent can be achieved if the first 10-year phase began with a higher fixed rate of 8 percent and gradually phased in principal repayment over the next decade.[79] This would lead to the same initial payment under the current 5-percent loan, in which an additional 3 percent is charged to consumers for initial amortization.

Initial monthly payments can remain affordable to borrowers as shown in Figure B.6.[80] Most importantly, these reforms could help the government reach more families with the same fiscal expenditure and stimulate the flow of private investment.

Figure B.6: Payment-to-Income Profile for Three Interest-Rate Scenarios.



Source: World Bank staff original calculations for this report (2025).

Mobilizing Private Investment: Reforms to Incentives

Private capital for housing can either come from family savings or private investments channeled through loans. By modifying its programs, public housing finance can incentivize both sources of financing. A primary strategy in low-income housing finance is incentivizing households to save for a home. While commercial banks offer savings accounts, their reach is limited, and they lack a systematic housing benefit for savers. To fill this gap, a reinvigorated TAPERA could introduce an incentivized voluntary contract savings for housing (CSH) product, targeting informal workers, low-income households, and other households currently ineligible for government programs. CSH helps consumers signal creditworthiness to lenders and allows families to accumulate a down payment for future loans. Reforming the loan design could also enable the two current TAPERA Funds to achieve long-term yields of 5–6 percent, acceptable to their contributors. This reform assumes a portfolio mix of 35 percent securities/bank debt (5–7 percent return) and 65 percent investment in loans under the proposed changed product designs (4–5 percent return), which is typical for mandatory provident funds (e.g., Mexico, Brazil, Philippines).

To address Indonesia's large, underserved segment living in housing deficit, public housing finance tools could focus on incentivizing commercial lenders to use their ample liquidity. By implementing rational pricing of public housing finance instruments, the government can better align the supports provided with the payment capacity of beneficiaries and, thus, gain room to leverage its limited fiscal resources and attract additional funding from banks (primarily commercial banks, which are highly liquid), institutions, and, potentially, international investors. Two central channels exist for doing so: 1) co-financing and 2) supporting less-liquid lenders through buying debt.

[79] Higher interest rates are standard in public housing finance in neighboring countries. For example, the Philippines' successful government-managed Pag IBIG mutual fund offers mortgages for 8.5% for 20 years. The fund offers maturities up to 30 years to reduce the burden of principal repayment.
[80] This holds also true regarding the other key risk metric, the loan-to-value ratio. Assume that the initial loan-to-value ratio was 80%. After 10 years, even in the product design where principal is being phased in and assuming only a conservative 3 percent per year nominal house price growth, below 5% income growth, the loan-to-value ratio will have fallen already to 50%.

First, many banks do not fully utilize their resources for the 25 percent co-financing required by the FLPP. Instead, nearly half of the participating banks rely on additional support from the Secondary Mortgage Facility to meet their obligations.[81] To address this, public finance housing tools could incentivize banks to increase their contributions. One possibility is to raise bank co-financing shares for higher income brackets within the FLPP target group. For families who are now underserved, public financing could be lowered to approximately a 20 percent loan-to-value ratio, which would effectively mean those loans are offered as second mortgages, while the banks would entirely finance the rest.

Second, liquid banks could be incentivized to purchase bonds issued by the government-owned Secondary Mortgage Facility (SMF). SMF would then refinance less-liquid banks engaged in low-income housing finance. The larger ones, particularly BTN (Bank Tabungan Negara, a state-owned enterprise bank known for its specialization as a mortgage provider), could issue bonds themselves.[82] By providing these additional funding sources, the government could further decrease FLPP's financing share and eventually replace the entirely government-funded program with blended finance.

Progressively Repositioning Institutions: Reforms to Scope

To improve current housing finance challenges, Indonesia can re-examine programs that offer financing to underserved populations. Figure B.7 highlights the current and potential future positioning of institutions and programs in the low- and lower-middle-income segments.

FLPP could explore incorporating micro mortgage and non-mortgage lending, aiming to strengthen its reach into the informal-labor segment expanding from the top-left quadrant into the top-right and bottom-left). This approach would mean enabling the FLPP to finance self-construction, extension, and home improvement lending, which would be distributed through banks rather than developers, in line with other public loan programs (BP TAPERA and BPJS). When it comes to the informal-labor segment, FLPP lenders can create an enabling environment (e.g., credit scores, linking to databases, leveraging AI tools, and fintech) for lending to informal households, including those in the lowest deciles of income, by raising the quota beyond the current level of 10 percent. BTN could also take a more proactive approach in servicing this market, potentially doubling or even tripling the existing

Figure B.7: Potential Repositioning of Public Housing Finance Institutions.

FLPP →

Loan Collateralization

Labor Formality ↓

Labor Formality		Mortgage Lending	Non-Mortgage Lending
Formal	Lenders	Commercial Banks	Commercial Banks (Potential)
Formal	Government Program	Tapera Fund, FLPP	Tapera Fund, FLPP (Potential)
Informal	Lenders	Tapera Fund (Potential, voluntary), Commercial Banks (Expanded quota)	Microfinance
Informal	Government Program	FLPP/BP2BT (BTN) BSPS+	BSPS, BSPS+, FLPP Sponsored microfinance revolving fund

← BSPS

Source: World Bank staff original analysis for this report (2025).

[81] Going forward, a maximum government-supported financing of 75% could be enforced. Banks that lend to informal or low-income segments could be granted higher government financing shares.

[82] A suitable vehicle for such interbank investment could be "affordable housing bonds," whose proceeds are earmarked for low-income housing finance and come with regulatory preferences. A temporary government guarantee envelope for SMF and issuing banks for such bonds could additionally attract investments.

quota. Evidence from countries such as India supports this strategy; lenders like Aye Finance and Capital Float have successfully used alternative data (e.g., invoices, mobile transactions) and AI-based scoring to underwrite loans to informal micro, small, and medium enterprises, achieving repayment rates exceeding 95 percent. These examples, confirmed by International Finance Corporation research, demonstrate that data-linked and fintech-enabled credit tools can significantly broaden financial access while mitigating risk.[83]

The successful BSPS subsidy scheme could expand by leveraging housing microfinance, increasing access to financing for the very low-income segment. Target loans in this very low-income segment would be between two and five years, US$1,000–US$3,000 for self-construction, extensions, and improvements. This financing could be delivered through banks and, in particular, through microlenders. Similarly, the KOTAKU infrastructure subsidy scheme can be combined with housing microfinance. An important complement could be an extension of the current KUR (*Kredit Usaha Rakyat*, or The People's Business Credit) guarantee design to housing loans.

With BP TAPERA and the SMF, Indonesia already has the two central public finance institutions needed to mobilize long-term capital. To make them fully operational will require product redesign and institutional reform. Implementing the remaining regulations necessary to make TAPERA fully operational and create a more conducive bank, legal-regulatory, and government support framework for SMF will be essential.

4. Conclusion

While the government's housing goals are ambitious, they are achievable. Public funding can be optimized to accelerate the delivery of resilient and affordable housing for all Indonesians, while private capital can be leveraged to enhance housing programs (Table B.2). The reforms required in the sector are highly actionable, with a clear direction established. Nonetheless, to realize its vision, the Government of Indonesia will need to demonstrate a willingness to act decisively and swiftly. Indonesia is positioned to enter a new Golden Era, one built and designed "For the People."

Table B.2: Static Simulation of 3 Million Housing Program: Before (2023) and After Comparison.

Indicator	Before	After
Private Capital Mobilization (US$ Million)	560	2,777
Jobs Created	868,151	2,336,616
Better Housing / Total Housing Volume Share	39%	71%
Better Housing / Total Housing Budget Share	**9%**	**28%**
New Housing / Total Housing Volume Share	61%	29%
New Housing / Total Housing Budget Share	**91%**	**72%**
Government Budget (Rp Trillion)	35.54	62.79
Government Budget (US$ Billion)	2.15	3.81
Total Number of Units Supported/Achieved	**386,222**	**1,200,000**

Note: *Government programs support 36.2% (2015-2024) of the housing solutions delivered in the country.
Source: Ministry of Housing and Settlements (2025); Performance Reports of Directorate of Implementation of Housing Finance and DG Infrastructure Financing, Ministry of Public Works and Housing (2023); World Bank original calculations for this report (2025).

[83] International Finance Corporation. 2020. *Artificial Intelligence in Emerging Markets: Opportunities, Trends, and Emerging Business Models.* Washington, DC: International Finance Corporation.

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