Indonesia is the world’s third most populous democracy, the biggest archipelagic state and the largest Muslim-majority nation. Real gross domestic product (GDP) growth, which slowed to an estimated 5.8 percent in 2013, is expected to remain sluggish at 5.4 percent in 2014, as a tighter monetary policy dampens consumer spending. Economic expansion is projected to accelerate between 2015–2018, averaging 6.4 percent a year.

Country overview

Geography and climate

- **Location:** south-eastern Asia, archipelago between the Indian Ocean and the Pacific Ocean
- **Climate:** tropical; hot, humid; more moderate in highlands
- **Regions:** 31 provinces, 1 autonomous province, 1 special region and 1 national capital district
- **Major cities:** Jakarta (9.12 million), Surabaya (2.51 million), Bandung (2.41 million), Medan (2.13 million), Semarang (1.30 million) (2009)

Political system

- **Type of government:** republic
- **Capital:** Jakarta

Population, language and religion

- **Population:** 250.8 million
- **Urban population:** 50.7% (2011)
- **Demographics:** 0–14 years: 26.2%; 15–24 years: 17.1%; 25–64 years: 42.3%; 65 years and over: 6.4% (2014 estimate)
- **Median annual household income:** 3,488 US dollars (US$)
- **Official language:** Bahasa Indonesia
- **Prominent religions:** Muslim, Christian, Roman Catholic, Hindu, other (includes Buddhist and Confucian)

Currency and central banking

- **Local currency:** Indonesian rupiah (IDR)
- **Exchange rate:** IDR1 = US$0.0001 (1 April 2014)
- **Interest rate (average annual rate):** 6.5% (2014); 4.8% (2013); 4% (2012); 5.6% (2011); 6% (2010); 7.2% (2009)
- **Foreign exchange reserves:** US$83.45 billion (31 December 2013 estimate)
- **Total debt (2013):** external: US$223.8 billion; internal public debt: 24.2% of GDP (2013 estimate)

Business environment

Economic environment

- **GDP in 2013 was US$1,293.64 billion.** It is forecast to rise to US$1,389.1 billion in 2014, with 6.4 percent annual growth in the period 2015–2018. Private consumption growth is expected to slow, while the rate of increase in investment should remain stable between 2013–2017. Median household income is predicted to increase to US$5,966 by 2017.
- **Foreign direct investment (FDI) (billions):** inbound: US$9.3 (2008); US$18.6 (2013); US$34.2 (2018 forecast); outbound: US$5.9 (2008); US$3.7 (2013); US$11.0 (2018 forecast)
- **Exports free on board (FOB) (billions):** US$187.3 (2012); US$182.3 (2013); US$219.8 (2018 forecast)
- **Imports FOB (billions):** US$178.7 (2012); US$177.4 (2013); US$288.7 (2018 forecast)
- **Sector breakdown:** service sector: 39.9%; industrial sector: 45.7%; agriculture sector: 14.4%
- **Trade balance (billions):** surplus of US$8.7 (2012); US$4.8 (2013); US$31.0 (2018 forecast)
- **Stock exchanges:** IDX, JFX

GDP growth and inflation (average consumer price index (CPI))

Source: Economist Intelligence Unit, 2014
Investment climate

Key considerations

- **Fiscal and monetary policy:** Indonesia’s central bank is likely to keep monetary policy on hold in 2014. Interest rates are not expected to be increased until early 2015, owing to an expected slowdown in private consumption growth in 2014.

- **Competition policy:** The Indonesian government has dismantled the monopolies and price controls that once dominated the economy, opened new industries to competition and enforced better targeting mechanisms for fuel and electricity subsidies. Despite these measures, the protectionism inherent in the country’s ‘negative investment list’ are still a cause for concern. Indonesia’s Competition Law (Law 5/1999) is implemented by the Business Competition Supervisory Commission (Komisi Pengawas Persaingan Usaha (KPPU)). Law 5/1999 on Anti-monopoly and Unfair Competition prohibits any single company from holding more than 50 percent share of the domestic market and prohibits two or three companies from sharing 75 percent of the market. The law attracts a fine of IDR 100 billion (US$10 million) and a 6 month prison sentence. Indonesia’s Company Law permits mergers with the consent of 75 percent of shareholders. The new Indonesian Company Law (Law 40/2007) introduced ‘de-mergers,’ which allow an absolute division to occur when all of a company’s assets and liabilities are transferred to two or more other companies. Several amendments to merger regulations have recently been introduced. Government Regulation 57/2010 provides for consultations with the Business Competition Supervisory Commission (KPPU) before any merger and acquisition, while Regulation 3/2012, offers an opportunity to propose remedies to the KPPU, if any objectionable provisions in the consolidation agreement are found during pre-merger consultations.

- **FDI policy:** FDI in Indonesia has been increasing since 2010–2011. The top sources during the first quarter of 2013–2014 were Japan, Singapore, US, UK, South Korea and Singapore. In 2014–2015, it should be easier to obtain investment licenses, due to reforms implemented by the Investment Co-ordinating Board (BKPM), although regulations and limits imposed on foreign investors continue to deter inward investment. Regulations that harm foreign investment and exports are expected to be eased by 2017–2018.

- **Foreign trade and exchange controls:** Foreign policy is likely to remain influenced by non-alignment, with the government resisting close trade relations with the US and China. In the face of volatile foreign capitals flows, the government’s main priority is to stabilize the currency. Restrictions on short-term capital flows are unlikely to be tightened significantly, and Bank Indonesia appears to have ceased selling foreign reserves to support the rupiah. In 2014–2015, limited controls on foreign exchange flows are expected to be maintained. In the longer run, trade liberalization should proceed – but in a start-stop manner.

- **Financing policy:** During 2014–2015, there is likely to be new legislation to tighten the rules on foreign ownership in the banking sector. The ongoing presence of foreign institutions will hopefully encourage greater competition, modernization and a transparent operating regime. The nominal interest rate is forecast to reach 13.5 percent in 2014–2015.

- **Taxes:** The standard rate of corporate income tax is 25 percent for all companies with income exceeding IDR 4.8 billion (US$480,000). Public companies that satisfy a minimum listing requirement of 40 percent and other conditions are entitled to a tax reduction of 5 percent off the standard rate. Government regulation 46/2013 sets a flat rate of 1 percent of turnover for individual and corporate taxpayers that have a gross annual income of less than IDR 4.8 billion (US$480,000). The regulation does not apply to corporate taxpayers that have yet to commence commercial operations, nor to foreign companies with permanent establishments in Indonesia. Efforts are being made to modernize tax offices and improve tax payment methods by implementing electronic filing procedures. The government is also planning to increase transparency in local government spending.

KPMG in Indonesia

KPMG member firms are among the world’s leading providers of Tax, Audit and Advisory services. In Indonesia, KPMG has approximately 600 professionals located in the capital city of Jakarta.

KPMG in Indonesia aims to respond to complex business challenges facing customers and to take a comprehensive approach that spans professional disciplines, industry sectors and national boundaries.

For more information, please visit the KPMG in Indonesia website: kpmg.com/id/en

Sources: Economist Intelligence Unit, 2014; Central Intelligence Agency, 2014; World Stock Exchange, 2014