SUMMARY OF INDONESIA'S POVERTY ANALYSIS

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POVERTY ANALYSIS (SUMMARY)

1. **Profile of poverty.** Economic growth averaging 5.8% since 2010 has helped to lift 3.3 million Indonesians out of poverty. Yet 28 million were still living below the government's poverty line in March 2014. Indonesia's national poverty line is set at consumption outlays of Rp 302,735 (US$25) per month per person–about 82 cents a day. If an international poverty line of $2 a day is used, then 40% of the population would be classified as poor. Some 68 million Indonesians are classified as near–poor or vulnerable. Many of them move in and out of poverty during their lifetime. Some 55% of households who were classified as poor in 2014 were not poor a year earlier, indicating the high risk of falling back into poverty.

2. **The pace of poverty reduction in Indonesia is slowing.** From 2006 to 2010, poverty incidence declined by 1.2% per annum. From 2011 to 2014, the rate of decline was just 0.5% per annum (Table 1). Increasing difficulty in reaching the remaining poor and rising disparity in economic growth have contributed to the slowdown. As the poverty rate gradually falls toward 10%, many of the remaining poor households have incomes far below the poverty line. For example, the poorest half of the population registered zero or slightly negative growth in real per capita consumption from 2012 to 2013, compared to growth of 4% in mean consumption across the entire population and average growth of 7% for the top two deciles.[1] This implies that significantly higher consumption growth of the poor is required to maintain the annual rate of poverty reduction.

3. **Majority of the poor in Indonesia live in rural areas.** In 2014, some 13.8% of the rural population was classified as poor, compared to 8.2% of the urban population. They mainly participate in low-productivity jobs in agriculture and low-end service sectors.

Table 1: Poverty Incidence, 2006 to 2014

	2006	2007	2008	2009	2010	2011	2012	2013	2014
Relative Poverty (% of population)	17.8	16.6	15.4	14.2	13.3	12.5	11.7	11.5	11.0
Absolute Poverty (in millions)	39	37	35	33	31	30	29	29	28
Rural Poverty (% living below rural poverty line)	21.8	20.4	18.9	17.4	16.6	15.7	14.3	14.4	13.8
Urban Poverty (% living below urban poverty line)	13.5	12.5	11.6	10.7	9.9	9.2	8.4	8.5	8.2

Source: BPS–Statistics Indonesia (various issues).

4. **While most of the poor live on the island of Java, poverty rate is far higher in Eastern Indonesia.** In 2014, poverty incidence was highest in the provinces of Papua (27.8%), West Papua (26.3%), East Nusa Tenggara (19.6%), Maluku (18.4%), Gorontalo (17.4%), and West Nusa Tenggara (17.1%). Collectively, these provinces had fewer poor people than were found in East Java, which had a poverty incidence of 12.3% or 4.8 million poor persons in 2014.[2]

5. **Poverty reduction and inequality.** Income and consumption inequality in Indonesia have been steadily increasing since 2000. After recovering from the 1997–1998 Asian financial crisis, Indonesia experienced a period of strong economic growth, driven in part by a commodities boom and strong domestic consumption. During this period the Gini coefficient climbed from .31

[1] World Bank. 2014. *Indonesia Economic Quarterly July 2014.* Jakarta.
[2] BPS–Statistics Indonesia. 2015. Poverty Statistics. http://www.bps.go.id/linkTabelStatis/view/id/1488

in 2000 to .43 by 2013. The distribution of consumer credit suggests that inequality could be greater still, and the World Bank estimates the Gini coefficient was as high as 0.51 in 2014, making Indonesia a high–inequity country.[3] Some 49% of national income goes to the richest quintile, and since 2003, the growth process has benefited the rich much more than lower or middle–income groups. Rising inequality is reflected in a growing gap between the rich and the poor. In 2002, average consumption per person of the richest 10% of households was 6.6 times that of the poorest 10%; by 2013, this had risen to 10.3 times.

6. **Increased inequality contributes to the slower pace of poverty reduction.** Poverty generally falls with economic growth, but the speed of poverty reduction depends on how equally growth is shared. If the pattern of growth benefits the rich more than the poor, the pace of poverty reduction slows. Had income growth been equally shared, then the average growth effect would have reduced poverty from 17.4% in 2003 to near zero levels by 2010.[4] However, the unequal distribution of income growth meant that poverty fell only by 5.4% instead, to 12% in 2013.

7. Higher inequality can also lead to slower economic growth and thus can further hamper poverty reduction efforts. The extent to which households in the bottom 40% are unable to move into the middle class could weaken middle class–driven consumption growth. This may also reduce economic growth through a number of other channels, such as low investments in human capital and decreased entrepreneurial activity. Also, inequality of opportunity can impact on the ability of children to achieve their full potential, hindering future growth.

8. **Drivers of inequality.** Poverty levels and rising inequality are both associated with a lack of good jobs in the economy. Since 2000, the majority of jobs that have been created are in low–productivity services. The agriculture sector, which absorbs about 35% of the labor force, has consistently grown at a slower rate than the country's average GDP growth. At the same time, the manufacturing sector has experienced slower growth, averaging 5.3% from 2011–2014. Growth in mining, industrial crops, timber, telecommunications, and financial services has been accelerating since 2010, while ownership in these sectors remains highly concentrated and production tends to be capital intensive. As a result, recent economic growth has benefitted mostly the country's wealthy and generated relatively few jobs. Furthermore, even those with skills have often been unable to find jobs in the formal sector, and have to settle for self–employment or informal sector jobs.

9. Returns to education are rising, which means that highly skilled workers tend to earn much more than those with a more basic education. Compared to workers with a primary education or less, those with junior secondary education now enjoy a 20% premium, those with senior secondary education a 40% premium, and those with tertiary education earn twice what those with primary education would earn. Moreover, the junior secondary and tertiary premium has increased. The resulting wage gap between the more educated and the less educated directly influences consumption inequality. Households whose head is better educated will have higher consumption, and this consumption gap has also been increasing.

10. Unequal opportunities during childhood also contribute to higher inequality. Some inequality is due to circumstances beyond the control of an individual, such as gender, ethnicity,

[3] World Bank. 2015. *Inequality in Indonesia: Why is it rising and what can be done?* Jakarta.
[4] World Bank. 2014. *Indonesia Economic Quarterly July 2014.* Jakarta.

birthplace, and family background. Just three of these factors–gender of the household head, level of education, and household location (urban or rural, which particular region of Indonesia)– accounted for 33% of total consumption inequality in 2012.

11. Children in remote and rural areas tend to experience multidimensional inequality of opportunity. They are more likely than urban children to lack access to education, health, and transportation services. Of the 35% of all urban children who lack access to at least one of these services, 20% lack access to two and only about 3% lack access to all three. By contrast, 58% of children in rural areas lack access to at least one of the services, with one–third of them lacking access to two, and another third lacking access to all three services.

12. Lack of protection from shocks makes it harder for households at the lower end of income distribution to climb out of poverty. Since 1997, Indonesian households have faced many negative economic shocks, food price surges, and natural disasters.[5] Risks specific to particular individuals or households are just as significant. These include loss of employment, illness and accidents, death of a spouse, and divorce. For many households, such a shock is sufficient to push them back into poverty.

13. **The role of infrastructure development. The poor suffer the most from a lack of economic infrastructure.** Improved public infrastructure can make a significant contribution to reducing poverty and closing gaps in income inequality.[6] Better infrastructure, particularly for transportation and power generation, would support growth in manufacturing, which generates jobs in the formal sector. The performance of manufacturing has been lackluster since the late 1990s and has started to improve only since 2013. Investment in infrastructure is also needed to address high poverty rates in rural areas. Some 41% of district roads and 24% of provincial roads throughout Indonesia are in bad condition. Development prospects are poor for rural areas that lack good access to towns and markets. Poverty in some eastern provinces is directly linked to poor infrastructure, which hinders farmers from accessing markets, limits economic opportunities, and constrains access to essential social services.

14. **Government Poverty Reduction Programs.** In the National Medium–Term Development Plan 2010–2014 (RPJMN 2010–2014), the government's poverty reduction strategy comprised three clusters. The first was social assistance, which provided direct assistance to poor households to assist them in meeting basic necessities. The second was community empowerment, which provided funds to poor communities to improve their basic social and economic services. The third cluster was microenterprise empowerment, which focused on providing access to non–collateralized credit for microenterprises. To help design and oversee these programs, a national team for accelerating poverty reduction was established, chaired by the Indonesian vice president.[7] An evaluation of these programs

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5 Indonesia was the worst–hit country by the Asian financial crisis of 1997/1998. During the 2008/2009 global financial crisis, Indonesia saw growth slow but it fared better than most countries. Indonesians have faced periods of high food prices, such as in 2005–2006, 2008, and 2010. Major natural disasters since 1998 include the 2004 tsunami in Aceh Province, earthquakes in several locations, and the 2010 eruption of Mount Merapi in Java.

6 ADB. 2012. *Asian Development Outlook 2012*. Manila. ADB. 2013. *Asian Development Outlook 2013*. Manila.

7 In February 2010 the government issued Presidential Decree No. 15/2010 on Accelerated Poverty Reduction. This decree changed the poverty reduction agency's name to the National Team for the Acceleration of Poverty Reduction (TNP2K). TNP2K has three main tasks: formulate poverty reduction policies and programs, make poverty reduction activities more synergic between ministries and institutions, and monitor and evaluate poverty reduction programs. Under the new decree, the Vice President was directed to lead TNP2K.

showed mixed results, attributed to difficulties in targeting assistance and to adverse effects of food price shocks.[8]

15. **The new national framework for poverty reduction.** The RPJMN 2015–2019 focuses on poverty reduction in the context of making the growth process more inclusive. It targets closing the growing gap in consumption per capita between different income groups and reducing poverty from 11.25% in March 2014 to 6%–8% in 2019. Over the next 5 years, the government plans to reduce inequality and poverty through several means. To greater job opportunities, the government will improve investment climate for labor-intensive industries and small business. The government will improve connectivity and accelerate development of basic infrastructure to support economic activity and sustainable livelihood in rural and border areas. At the government will improve the delivery of basic social services such as education and health to the poor and vulnerable. Government will also rollout more comprehensive and better targeted social protection programs.

8 A. Suryahadi et al. 2010. *Review of the Government's Poverty Reduction Strategies, Policies, and Programs in Indonesia.* The SMERU Research Institute. Jakarta.