Foreword

Indonesia has undergone a remarkable transformation over the past 20 years. The national poverty rate has halved, from 19.1 percent of the population in 2000 to 9.2 percent in 2019. Growth has averaged 5.5 percent annually since 2000, and Indonesia, the world’s fourth most populous nation, has emerged as a vibrant middle-income country with a rapidly expanding middle-class. However, challenges still remain. Out of a population of around 264 million, about 25.9 million Indonesians still live below the poverty line and a further 20.2 percent of the population are vulnerable to fall into poverty, as their income hovers just above the national poverty line. Inequality is and will likely remain a key challenge threatening Indonesia’s future growth and prosperity. These lingering inequalities and vulnerabilities can have significant adverse consequences for growth, as well as for social and political stability. Indonesia will also need to be prepared for a future that will look different from today – an ageing population, technological advancements that will impact how and where people work, disasters related to climate change, and - as recent experience has shown - pandemics. In fact, the COVID-19 pandemic is likely to significantly increase the number of people living in poverty, a testament to the remaining vulnerabilities Indonesia face.

Indonesia continues to set ambitious goals for achieving a more inclusive development model. The Government’s vision for 2045—when Indonesia celebrates 100 years of independence—is to achieve high-income status and reduce poverty to nearly zero. In addition to sustained growth and income opportunities for all, an inclusive and efficient social protection system (SP) will be essential to meet these ambitious goals. Indonesia will need a set of modern and future-ready social protection programs and systems that can adapt and operate in the context of continuous change.

And Indonesia already has a solid base to build from. The country’s social protection system has been fundamentally transformed over the past two decades. Household-based social assistance programs have improved their ability to reach poor households as a result of investments in a social registry of poor and vulnerable households, and there has been significant expansion in coverage of both social assistance and social insurance programs, especially for health insurance but also the pension system. In parallel to the expansions, better spending allocations and a build-up of the needed platforms to deliver programs effectively and efficiently has made this transformation possible.

While significant efforts have been made to improve the social protection system in Indonesia, the transformation remains incomplete. To be future-ready, a rethink of the current social contract and continued efforts to move towards adequate coverage against current and future shocks is needed. As the population ages and informality in the labor market persists, this is urgent – without such reforms it will be difficult to reach the ambitious poverty reduction and inclusive growth targets that have been set out for 2045. With a rapidly expanding middle class, comprising about 61 million people, and the rise of an aspiring middle class, currently comprising of 126 million Indonesians many remain at risk of being left behind due to the incomplete coverage and in some cases inadequate benefit levels for groups such as the elderly, disabled or households without children. Indonesia can also apply the lessons from the impressive coverage expansion of social health insurance to pension reform, and put in place a modern unemployment insurance system. And to deliver these programs, continued investments in systems for identification, targeting and payments are required. As the COVID-19 crisis demonstrates, countries that have social registries that cover a majority of the population are able to respond more rapidly and comprehensively to support households facing livelihoods shocks. Expanding the existing social registry accordingly therefore emerges as a key priority for Indonesia, as this report also suggests.

There is no better time than now to think about how to improve social protection in Indonesia. Our hope is that this report will stimulate a much-needed conversation about how to forge policy paths that will make the social protection system more efficient, effective and relevant in a rapidly changing world. The social protection system in Indonesia will need to further develop the ability to support millions of people to gain the right skills to compete in today’s changing jobs market, and give millions of children the opportunity to go school and have access to health care, making them ready to traverse labor markets in the not too distant future. We acknowledge that these investments are not minor and will come with significant costs, but we also believe that by standing together – the government alongside civil society, and the private sector, with the support of development partners – the country can achieve its 2045 vision of a future that protects and serves all people.
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Over the past two decades, Indonesia’s Social Protection system has been fundamentally transformed.
1. The Government of Indonesia's Vision for 2045 sets an ambitious path that will require significant investments in human capital and social protection

Indonesia continues to set ambitious goals for its growth and development. The Government of Indonesia's (GoI) vision for 2045—when the country celebrates 100 years of independence—is to achieve high-income status and reduce poverty to nearly zero. In addition to sustained growth and income opportunities for all, an inclusive and efficient social protection (SP) system will be essential to meet these ambitious goals. In most countries today, effective risk-sharing and SP policies play important roles in building equity, resilience and opportunity, and in strengthening human capital. Indonesia is no different. Risk-sharing interventions can reduce and efficiently.

But while significant, the transformation remains incomplete. The coverage expansion of social assistance is concentrated mostly among poor households with children, but other groups such as the elderly and disabled are not adequately covered. High incidence of labor informality—a persistent feature in Indonesia, in stark contrast with other major East Asia and Pacific (EAP) economies that managed to industrialize rapidly—has also left social insurance coverage low, inadequate (in terms of benefits provided), and stagnant. And delivery systems are still often fragmented and not yet fostering strong coherence across social assistance and social insurance realms. Most importantly, new challenges and opportunities are emerging, such as demographic changes, changes in how people work (including more flexible arrangements), technological advances, climate change and even health pandemics such as COVID-19. The current SP system is not yet prepared to face these new trends adequately.

Over the past two decades, Indonesia’s SP system has been fundamentally transformed. In particular, it has moved from the dominance of regressive consumer subsidies and ad-hoc crisis response to targeted and household-based social assistance programs, with a massive coverage expansion. In terms of social insurance, recent years have seen an ongoing building and integration of its policies and institutions. This has all been made possible through better spending allocations and a build-up of the needed platforms to deliver programs effectively and efficiently.

But while significant, the transformation remains incomplete. The coverage expansion of social assistance is concentrated mostly among poor households with children, but other groups such as the elderly and disabled are not adequately covered. High incidence of labor informality—a persistent feature in Indonesia, in stark contrast with other major East Asia and Pacific (EAP) economies that managed to industrialize rapidly—has also left social insurance coverage low, inadequate (in terms of benefits provided), and stagnant. And delivery systems are still often fragmented and not yet fostering strong coherence across social assistance and social insurance realms. Most importantly, new challenges and opportunities are emerging, such as demographic changes, changes in how people work (including more flexible arrangements), technological advances, climate change and even health pandemics such as COVID-19. The current SP system is not yet prepared to face these new trends adequately.

This report outlines a vision for Indonesia’s future SP system. It builds on recent success but is also bold in forging additional policy paths that will make the SP system more effective and relevant in a changing and often fluid environment. It also recommends the “how to” of realizing this vision, in terms of how to finance a more inclusive SP system and achieve a more robust delivery platforms. It further provides policy recommendations for the next few coming years (2025), as well as over the long term (2045), addressing emerging challenges that other high-income economies also face.

This section draws on the following sources: World Bank (2016a) and World Bank (2019a). Overall, public spending in SP will have to become more efficient, and additional sources of revenue will need to be identified. Making these investments today will give Indonesia a head start in ensuring that it protects and promotes all as it moves toward achievement of its ambitious 2045 targets.

Indonesia has made major gains in economic growth and poverty reduction in the past two decades. Relatively strong economic growth, averaging 5.5 percent per year since 2000, has been accompanied by a sustained decline in poverty rates: from 19.1 percent of the population in 2000 to 9.2 percent of the population in 2019. However, this progress contrasts sharply with Indonesia’s performance in shared prosperity. Inequality, as measured by the Gini coefficient, rose from its lowest value of 30 points in 2000 to 41 points in 2014, reducing to 38 points in September 2019. Inequality remains a key challenge threatening Indonesia’s future growth and prosperity. Vulnerability is also high: while 24.7 million Indonesians live below the poverty line, a further estimated 64 million live less than 50 percent above poverty. Inequality and vulnerability can have significant adverse consequences for growth, as well as for social and political stability, and without adequate protection small shocks can easily send the vulnerable back into poverty.

Strong economic growth has enabled Indonesia to reach middle-income status. Indonesia is experiencing a rapid expansion of its middle class, comprising about 61 million people, and the rise of an “aspiring middle class.” Currently, 126 million Indonesians, or 48 percent of the population, are considered as the aspiring middle class. While free from chronic poverty, this group has yet to achieve the economic security of the middle class. In fact, nearly one-fifth of the aspiring middle class in 1993 had become vulnerable to poverty by 2014. Two-thirds also suffer deprivation on at least one non-monetary dimension of welfare.

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2. This is the right time for Indonesia to rethink how the social protection system can achieve its objective in the future

Indonesia’s future SP system will need to be identified. Making these investments today will give Indonesia a head start in ensuring that it protects and promotes all as it moves toward achievement of its ambitious 2045 targets.
Reaping the demographic dividend will require Indonesia to create an adequate number and types of jobs for the millions that join the labor force every year. It will also require the labor force to have adequate skills for what the jobs market of the future will require. Technology and automation will likely further affect the labor market, and reshape the skills needed for work. Furthermore, it is likely that a larger share of the workforce will move away from traditional one-job-per-career patterns toward having many sources of employment over the course of their careers, including periods of non-wage/self-employment. The informal sector in Indonesia still employs more than 50 percent of total workers (70 percent in rural areas), and it is likely that a high level of informality will persist.

Indonesia is vulnerable to disaster risk and climate change. The World Risk Index ranks Indonesia’s exposure to natural hazard-related risk at the highest level. The annual economic impact of natural disasters between 2000 and 2016 was estimated at IDR 22.8 trillion (or US$1.4 billion), or about 0.3 percent of Indonesia’s gross domestic product (GDP). This excludes the estimated direct damages and losses from the West Nusa Tenggara (Lombok) earthquakes and the Central Sulawesi (Palu) earthquake and tsunami in 2018, which are estimated to have cost at least US$1.8 billion (0.2 percent of GDP).

<table>
<thead>
<tr>
<th>Disaster type</th>
<th>Location</th>
<th>Year</th>
<th>Direct Impacts on People</th>
<th>Financial Damage (USD billion)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Indian Ocean Tsunami</td>
<td>Aceh</td>
<td>2004</td>
<td>167,000 fatalities</td>
<td>7</td>
</tr>
<tr>
<td>Earthquake</td>
<td>Yogyakarta</td>
<td>2006</td>
<td>6,000 fatalities, 3.2 million affected</td>
<td>2.3</td>
</tr>
<tr>
<td>Flood</td>
<td>Jakarta</td>
<td>2007</td>
<td>68 fatalities, 2.2 million affected</td>
<td>0.6</td>
</tr>
<tr>
<td>Earthquake</td>
<td>Padang</td>
<td>2009</td>
<td>1,395 fatalities, 2.5 million affected</td>
<td>2.1</td>
</tr>
<tr>
<td>Volcanic Eruption</td>
<td>Mt Merapi</td>
<td>2010</td>
<td>322 fatalities, 137,000 affected</td>
<td>0.4</td>
</tr>
<tr>
<td>Flood</td>
<td>Jakarta</td>
<td>2013</td>
<td>34 fatalities, 250,000 affected</td>
<td>0.83</td>
</tr>
<tr>
<td>Earthquake</td>
<td>West Nusa Tenggara</td>
<td>2018</td>
<td>564 fatalities, 396,000 affected</td>
<td>0.86</td>
</tr>
<tr>
<td>Earthquake and Tsunami</td>
<td>Central Sulawesi</td>
<td>2018</td>
<td>2,256 fatalities, 1.5 million affected</td>
<td>1.3</td>
</tr>
</tbody>
</table>

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1 Source: World Bank (2016a) and World Bank (2019b).
2 This section draws on the following: World Bank (2016a) and World Bank (2017a).
3 Only five common natural hazards are considered—earthquakes, cyclones, floods, droughts, and sea level rise.
The poor and vulnerable are disproportionately affected by disasters.\(^1\) This is because they are often more exposed to living in vulnerable areas such as flood-prone land and steep hillsides, or inhabit housing settlements that have been poorly designed and constructed. Shocks can also force poor households to resort to negative or damaging coping strategies, such as liquidating savings and assets, reducing nutrition levels, taking children out of school to work, and postponing or neglecting health needs. They can also kill, injure or displace family members. In all these cases, limited ability to respond and recover quickly pushes already poor households deeper into poverty, and the vulnerable into poverty. It is thus common for households to transition in and out of poverty due to disaster and climate change-related shocks.

Across the world, SP systems, through social assistance, social insurance and labor market programs, aim to build resilience, improve equity and promote opportunity.\(^2\) Social protection can also make significant contributions in building, employing and protecting human capital. Social assistance programs can build human capital by providing consumption support and ensuring all citizens are able to get adequate nutrition and schooling. Social insurance and labor market programs help citizens employ their human capital by contributing to a modern and effective labor market with adequate provisions for pensions, unemployment support and access to productive work through active labor market interventions, such as employment services and targeted training or skills development programs. Finally, social protection programs protect human capital from disease and disasters, and build resilience by insuring against adverse impacts from shocks. Social protection programs can also allow individuals to invest in their human capital or firms, instead of saving for precautionary reasons.

Indonesia’s future SP system needs to adapt and respond to a changing world and evolving objectives. In contrast with many other large economies in the region (China, the Republic of Korea, Japan, Vietnam, Thailand, Malaysia), Indonesia never achieved a strong manufacturing base. This has, in part, undermined efforts to increase the share of formal employment—a main assumption behind the current social insurance contributory model. Moreover, technological change, including changes in how and where people work, and demographic developments, will impact the type of SP system and programs needed, and further question the sustainability of this contributory model approach. This will require a rethink of the social contract that can promote prosperity for all, and enable Indonesia to reach the ambitious poverty reduction, human capital and inclusive growth targets that it has set out for 2045. To respond, Indonesia will need a comprehensive SP system that makes the poor and vulnerable more resilient to shocks, with human capital and skills that ensure workers are better prepared for job disruptions and transitions, and one that encourages economic mobility by promoting social and productive inclusion for all Indonesians.

What do these opportunities and risks imply for Indonesia’s SP system, including social assistance and social insurance programs?

The SP system must continue to build human capital and do so better. Social assistance programs are already core parts of the GoI’s commitment to accelerate investments in human capital, including the National Strategy to Accelerate Stunting Reduction (Strategi Nasional Percepatan Pencegahan Stunting, or StraNas Stunting). Social assistance programs can play a key role in building the human capital of Indonesia by incentivizing the demand for, use of, and access to education, health, nutrition and other services.

**Indonesia should invest further in its young and expanding labor force to reduce inequality and prepare workers for transitions brought about by the changing nature of work.** Education quality needs to improve, as well as skills upgrading opportunities for professional development, including on-the-job training. Social assistance programs can also include “productive inclusion” type elements to connect the unskilled poor and vulnerable with wage- and self-employment. Creating a workforce for the future will rest on meeting the growing demand for advanced cognitive skills and skill combinations that are predictive of adaptability, such as reasoning and self-efficacy. An inclusive social insurance system that is available to all and not tied to how or where people work (i.e., formal wage-employment) promotes labor force participation and employment, and also accommodate changes in the labor market from technology, automation and the emergence of the ‘gig’ economy.

**Indonesia should continue to evolve policies and programs that protect people’s human capital and ensure they are resilient against shocks.** Adequate coverage and benefit levels of social assistance programs can play a key role in protecting human capital and building resilience. A well-functioning, adaptive and responsive SP system can protect poor and vulnerable households against risks and shocks along the lifecycle. This minimizes negative coping behaviors (e.g., sacrificing productive investment to maintain minimum consumption) and contributes to beneficiaries’ human and financial capital in the long run.

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\(^1\) Estimates from Rush (2013) suggest that, at the district level, a one standard deviation increase in disaster harm can increase the poverty rate by 0.8 percent and the poverty gap by 0.3 percent.

\(^2\) World Bank (2013a).
4. Indonesia laid a solid foundation for its future SP system over the past two decades

4.1 Building and protecting human capital: composition and performance of Indonesia’s social assistance programs

Social assistance programs are key policy instruments for the GoI to reduce poverty and inequality, and to build and protect human capital. Indonesia’s social assistance system was only introduced in the late 1990s, yet it has already undergone significant expansion and achieved important results. It has evolved from providing temporary support in times of need, such as with subsidy reform (BLSM/BLT), to implement a set of core permanent programs that today include a conditional cash transfer program (Program Keluarga Harapan, PKH), an cash transfer for poor and vulnerable students (Program Indonesia Pintar, PIP), a food assistance program (BPNT, now renamed to Sembako), and subsidized health insurance premiums (JKN-PBI). These programs are targeted to the poor and vulnerable, and aim to support their consumption and reduce poverty. Today, the social assistance system also plays an important role in building and protecting Indonesia’s human capital.

<table>
<thead>
<tr>
<th>Program</th>
<th>Purpose</th>
<th>Targeted Coverage</th>
<th>Budget (IDR billion)</th>
<th>Benefit (nominal / average)</th>
<th>Adequacy (% of median monthly consumption of the poorest 10%)</th>
<th>Coverage of the poorest eligible 10%</th>
<th>Beneficiary incidence to the poorest eligible 10%</th>
<th>Implementing Agency</th>
</tr>
</thead>
<tbody>
<tr>
<td>PKH</td>
<td>Poverty reduction, strengthening human capital</td>
<td>10 million families</td>
<td>34,100</td>
<td>Conditional cash transfers – IDR 315,000/ month/HH (average)</td>
<td>2%</td>
<td>47%</td>
<td>24%</td>
<td>Ministry of Social Affairs</td>
</tr>
<tr>
<td>PIP</td>
<td>Lower costs of attending school</td>
<td>10m-HHs/20 million students</td>
<td>11,200</td>
<td>Cash transfers – IDR 10,000/ month/HH (average)</td>
<td>7%</td>
<td>56%</td>
<td>13%</td>
<td>Ministry of Education and Ministry of Religious Affairs</td>
</tr>
<tr>
<td>Sembako</td>
<td>Boost food security and improve nutrition</td>
<td>15.6 million HHs</td>
<td>20,800</td>
<td>IDR 150,000/ month/HH for rice, eggs and others (nominal)</td>
<td>10%</td>
<td>42%</td>
<td>17%</td>
<td>Ministry of Social Affairs</td>
</tr>
<tr>
<td>PBI-JKN</td>
<td>Preventing health shocks</td>
<td>22.4 million people</td>
<td>26,700</td>
<td>Health service fee waiver (nominal)</td>
<td>1%</td>
<td>54%</td>
<td>15%</td>
<td>BPJS &amp; Ministry of Health</td>
</tr>
</tbody>
</table>

Table 1: Main social assistance programs in Indonesia, 2019

By design, the social assistance benefit package for households with children provides a very significant level of protection for households in the poorest 15 percent of the population. In particular, households entitled to receive PKH should receive an average 21 percent of median consumption in direct cash transfer. Thus, if a household receives PKH, it is by design receiving the minimum level of protection.12 On PIP, BPNT/Sembako and PBI-JKN to PKH renders a very adequate package of protection for the poorest 15 percent of households with children, at an average 37 percent of median consumption. PIP and BPNT/Sembako benefits each constitute an average of 7 percent median consumption, thus receiving PIP and BPNT/Sembako only (about 14 percent of consumption budget supported), or just one or the other, would not provide an adequate package of assistance. The population beyond the poorest 20 percent thus receives a minimal package of protection, and those beyond the poorest 40 percent receive no assistance, by design. With BPNT/Sembako’s benefit level increase in 2020, the overall package is further increased in adequacy.

Figure 3. “De jure” value of social assistance benefits for households with children, 2020

Source: Susenas 2018 and World Bank staff calculations.

Indonesia currently puts a strong emphasis on social assistance programs for households with children. The current ‘de-jure’ social assistance package shows that poor families with children are well covered. Figure 3 depicts the ‘de-jure’ adequacy of the benefit of the main household targeted social assistance programs along a welfare distribution. The depiction is “de jure” in the sense that the cut-off points along the horizontal axis represent what the GoI aims to reach with each program, though actual allocations stretch further along the distribution due to inclusion errors.

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11. Bantuan Langsung Sementara Masyarakat (BLSM) and Bantuan Langsung Tunai (BLT) were targeted unconditional cash transfer programs that were launched to compensate for the effects of energy subsidy reform; BLSM was last used in 2015, at the same time as the reduction of the fuel subsidy.

12. The minimum level of protection has been defined relatively as the minimum level of consumption required to bring an average household that is poor above the poverty line, also defined as the poverty gap index. A potential concern would be labor disincentive effects among recipients. However, the literature has shown that in countries including Indonesia delivering cash transfers representing no more than a quarter of median consumption for beneficiaries, these effects are not present (Banerjee at al. 2015).
The elderly is a population segment that is vulnerable today (around 36 percent are either poor or vulnerable) and will become increasingly so in the future given the rapid speed of aging. Although social assistance programs exist and are implemented by the Ministry of Social Affairs (MoSA). The Social Assistance for the Elderly program for the poor elderly aged 60 years and above, Social Assistance for the Elderly Affair (PBI) helps protect covered households from health-related shocks.

The adequacy of PBI-JKN, though it is a fee waiver program with no direct benefits provided, can be thought of in similar terms. Put simply, the value of the PBI fee waiver can be constructed as the value of the premium paid for the household by the GoI. This assumes a constant elasticity of demand to PBI-JKN. Another measure of adequacy for PBI-JKN’s large coverage beyond its target group is a function of its large program size and the ability of local governments to nominate beneficiaries under the previous scheme, Jamkesda. A similar arrangement is in place for PIP, which also likely explains, in part, its current rate of inclusion errors. It is worth noting, however, that while such targeting errors exist, their severity is minimal. Inclusion of those in percentile 40 to 70 is in some sense admissible, as the welfare distribution is relatively flat until just about percentile 70, suggesting small differences in welfare status among households in this part of the distribution.

There is thus a need to fill coverage gaps for certain groups in the social assistance system, primarily the elderly. The elderly is a population group in Indonesia that is vulnerable today (around 36 percent are either poor or vulnerable) and will become increasingly so in the future given the rapid speed of aging. Although social assistance programs for the elderly to address the risks of old age do exist, they are very limited. The disabled is another group that needs to be significantly better covered. A final coverage gap relates to social assistance for the poor and vulnerable adversely affected by natural disasters and climate-related shocks and stresses, as the current social assistance system does not fully accommodate their needs to ‘bounce back’ after such events.

Social assistance support for the elderly in Indonesia is low. Around 36 percent of the elderly are either poor or vulnerable, and around 30 percent are either living by themselves or with another person. This, coupled with a low and regressive overall old age pension coverage (Figure 6), makes income security for the elderly a significant concern, toward which the policy response has been inadequate to date. A cash transfer program to help address the risks of old age exists and is implemented by the Ministry of Social Affairs (MoSa). The Social Assistance for the Elderly (Asistensi Sosial Lanjut Usia Terlantar, ASLUT) is a program for the poor elderly aged 60 years and above, with a physical condition that makes them reliant on other people, have no other source of income, and are not PKH recipients. The monetary assistance is IDR 200,000 per month given once every four months, and was provided to 30,000 beneficiaries in 2017.
Social Protection For Indonesia’s 2045 Vision

Social insurance can help households and individuals to weather major shocks that affect most of the population. These include those related to the cost of medical procedures, unemployment, disability, death and old age. While social assistance aims to lift people out of chronic poverty, effective social insurance allows households to smooth consumption over the lifecycle. By pooling risk, it mitigates the impact of shocks at the household level outcomes in health and education. This is particularly true for PKH. The latest impact evaluation, published in 2018, found that stunting among PKH beneficiaries declined by 9 to 11 percentage points (stunting is estimated to affect 27 percent of all children) and enrolment to primary school increased by 4 percentage points among beneficiaries, which is very impressive given that the net primary school enrolment rate is already high, at around 93 percent. For junior secondary school, enrolment increased by about 8 percentage points, with a net enrolment rate in junior secondary school at around 78 percent. Positive impacts of PKH on consumption and healthy behaviors with respect to maternal and neo-natal practices have also been found.\(^1\)

### 4.2 Employing and protecting human capital: composition and performance of Indonesia’s social insurance programs

Social assistance contributes significantly to improved human capital as evidenced by positive impacts on health and education outcomes. This is particularly true for PKH. The latest impact evaluation, published in 2018, found that stunting among PKH beneficiaries declined by 9 to 11 percentage points (stunting is estimated to affect 27 percent of all children) and enrolment to primary school increased by 4 percentage points among beneficiaries, which is very impressive given that the net primary school enrolment rate is already high, at around 93 percent. For junior secondary school, enrolment increased by about 8 percentage points, with a net enrolment rate in junior secondary school at around 78 percent. Positive impacts of PKH on consumption and healthy behaviors with respect to maternal and neo-natal practices have also been found.\(^1\)

**Social insurance** allows households and individuals to invest in their human capital or livelihoods instead of saving for precautionary reasons. Indonesia’s social insurance system is relatively young, and centrally allocated PBI beneficiaries (targeted directly through the DTKS) are allocated much more efficiently (58 percent of total beneficiaries found in the poorest 40 percent) than the local government PKI (47 percent of total beneficiaries found in the poorest 40 percent).

Incidence analysis shows that household targeted cash transfer programs, in particular PKH, have been most efficient in allocating benefits to the poor and vulnerable. In 2018, PKH and PIP allocated 71 percent and 63 percent of benefits, respectively, to the poorest 40 percent. Further efforts are needed to improve targeting and ensure full utilization of the social registry (DTKS) to improve the allocative efficiency of social assistance benefits. Interestingly, in the case of PBI-JKN, the recently, PKH has included disabled and elderly household members, which has led to significant increases in coverage for both groups. In 2019, under PKH, about 84,000 persons with disability received a benefit top-up of IDR 2,400,000 per year, while 1.1 million elderly received the same benefit level. The policy is set to continue and will render a significant level of support to disabled and elderly living in PKH families who are not receiving support through ASLIUT or ASPDB, the disability support program (discussed below). However, these cash transfers are transferred to each family’s KKS card and not to the disabled/elderly person themselves, which would have allowed them to access their benefits independently.

Recent changes have been made to the legal framework and institutional arrangements for employment and protecting human capital. The latest impact evaluation, published in 2018, found that stunting among PKH beneficiaries declined by 9 to 11 percentage points (stunting is estimated to affect 27 percent of all children) and enrolment to primary school increased by 4 percentage points among beneficiaries, which is very impressive given that the net primary school enrolment rate is already high, at around 93 percent. For junior secondary school, enrolment increased by about 8 percentage points, with a net enrolment rate in junior secondary school at around 78 percent. Positive impacts of PKH on consumption and healthy behaviors with respect to maternal and neo-natal practices have also been found.\(^1\)

### Table 2: Main social insurance programs, 2019

<table>
<thead>
<tr>
<th>Program</th>
<th>Broad purpose</th>
<th>Targeted coverage</th>
<th>Coverage of the eligible</th>
<th>Amount of contribution</th>
<th>Benefit description</th>
<th>Implementing Agency</th>
</tr>
</thead>
</table>
| JKN (social health insurance) | Preventing health shocks and providing cash benefit for work-related accidents and/or fatality | 268 million people\(^1\) | 223 million; 83% (2019) | 5% of monthly income (salaried) or IDR 42,000-IDR 160,000 (non-salaried) | Health service fee waivers | BPJS Health  
| JKK (work-accident benefit) | Health service and cash benefit for work-related injury and/or fatality | 120 million people\(^2\) | 17.8 million; 15% (2017) | 0.24%–1.75% of monthly income | Medical treatment, home care services, and cash benefit\(^3\) | BPJS Health  
| JKM (death benefit) | Cash benefit to beneficiary (heir) in the event of death of the participant | 120 million people\(^2\) | 15.4 million; 12% (2018) | 5.7% of monthly income (salaried) or around 3% (non-salaried) | Lumpsum cash payment upon retirement\(^4\) | BPJS Employment  
| JHT (old-age savings) | Ensuring participant has savings when entering retirement | 45 million people\(^5\) | 11.8 million; 26% (2018) | 3% of monthly income | Monthly cash payment | BPJS Employment  

Source: World Bank staff calculation.

\(^1\) The number of total population in July 2019 including PBI. “Working population in 2018: the number of formal employees excluding civil servants in 2018,” 2017 data, excluding the number of construction workers.\(^1\) Depending on severity of injury (disability) and monthly income. \(^1\) Regulation enabling early withdrawal includes work termination and resignation as a form of retirement. Note: Article 1 of The Law No 40-2004 on SDA defines the definitions and boundaries of 5-SDA. It stipulates that “social insurance is a mandatory fund pooling mechanism which comes from contribution and is used to protect against socio-economic risks.” Article 1(9). Furthermore, the law defines “insurers are individuals who are working and who receivs salary, wages, or other form of rewards, Article 1(9).
However, while utilization of health insurance is increasing, there are still significant problems in terms of access for the poor, especially in remote areas of the country. There is a need to address the existing gap in coverage, with an estimated 50 million not yet covered. Furthermore, the cost of health insurance to the GoI is increasing and deficits have been rising in the past few years (totaling about 0.1 percent of GDP in 2018).

The expansion of social insurance coverage for other risks has been much slower, and pension for those covered will be inadequate for most. By 2018, only 14 and 11 million workers were covered for old age savings (Jaminan Hari Tua, or JHT) and pensions (Jaminan Pensiun, or JP), respectively. Coverage is lower than for JKN, partly due to the absence of any government contribution for informal sector workers. However, it is also because most formal sector workers are found in enterprises with fewer than 20 employees (small and micro enterprises) and are therefore not mandated to contribute. Furthermore, the adequacy for current workers is low from the JP scheme because of the earnings measure used to calculate benefits. Adequacy from the JHT scheme is also being compromised due to early withdrawals from the scheme which have been allowed since 2015 (Figure 7).

There is no unemployment benefit system in Indonesia. This, combined with a severance pay system that is not adequately implemented, has led to large number of early withdrawals from JHT, weakening its function as part of the pension system and instead serving as a de-facto unemployment account for many workers (Figure 7).

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**Figure 7: Withdrawals from JHT (old age savings) have risen sharply since Government Regulation No. 60/2015**

![Withdrawals from JHT (old age savings) have risen sharply since Government Regulation No. 60/2015](image)

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**Source:** BPJS Employment Administrative Data (2019).

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16 The earnings measure in the pension benefit formula is average earnings valorized with prices.

17 Government Regulation No. 60/2015 on “The Amendment to Government Regulations No. 46/2015 on the Implementation of Old Age Social Security Program”. Government Regulation No. 60/2015 was issued two months after the Government Regulation No. 46/2015 on Implementation of Old-Age Savings came into effect, creating a loophole that enabled JHT early withdrawal. The regulation has fundamentally changed JHT withdrawal requirement by allowing discontinuation of work, whether it is voluntary (resignation) or forced (termination), as a form of reaching retirement age which therefore allow withdrawal without having to fulfill the minimum of 10 years of contribution. Following the amendment, Ministry of Manpower Regulation No. 19/2015 on JHT Benefit Payment was issued to enable the payment. The requirement for JHT early withdrawal due to resignation and termination is further explicitly mentioned by the Ministry of Manpower Regulation No. 33/2015.”
In the short-term, fiscal pressure would arise largely from growing health insurance deficits but in the medium to long term pension expenditure for civil servants will grow and deficits from JP scheme will emerge. The current health insurance system leads to a series of cross-subsidies that when netted out leave a significant deficit that must be covered by the central budget, the ultimate guarantor of the scheme’s finances. Civil service pensions are currently financed on a pay-as-you-go basis and costs will rise over time owing to system demographics and rising life expectancy. However, current rules for calculating pension benefits for Civil Servants (CS) is inequitable and leads to inadequate pensions for a majority of CS. A move to correct for these inequities would need to be accompanied with parametric changes in scheme rules to avoid increasing deficits any further. Meanwhile, the SJSN pension scheme covering the private sector will amass significant reserves but will eventually run deficits, unless the contribution rate is increased to the actuarially fair rate.

As in other emerging East Asian countries, population aging is outpacing the development of traditional contributory pensions, hence a need to find an approach which covers all working age adults without causing labor market distortions. The National Social Security System (Sistem Jaminan Sosial Nasional, or SJSN), which started operating in 2015, will pay full pensions only after 2050. Although coverage is increasing as firms and employees are registered, international experience (Figure 8) suggests that potential coverage based on formal sector employment is limited. Without additional measures to bring in informal sector workers and to ensure the poor elderly are covered by social assistance, the percentage of the elderly living in poverty will almost certainly rise.

The increased risks encountered in the changing nature of work also call for adjustments to the existing system of worker protection. A new social contract could provide a SP system that is decoupled from firms and employees and internationals experience suggests that potential coverage based on formal sector employment is limited. Without additional measures to bring in informal sector workers and to ensure the poor elderly are covered by social assistance, the percentage of the elderly living in poverty will almost certainly rise.

The rapidly changing environment, including Indonesia’s changing demographic profile and the nature of work, coupled with persistent informality in the labor market, presents a challenge to the SP policies and programs that should be in place to help people manage risks to their lives and livelihoods. It is therefore an opportune time to re-think risk-sharing in the social contract and for Indonesia to continue to evolve its overall SP system to adequately meet the changing demands for its services in a rapidly evolving context. Such a system should offer adequate protection for all, regardless of their employment status and whether they work in formal or informal jobs. Indonesia has established solid programs and systems in both social assistance and social insurance, and this is the time to further strengthen coverage, implementation and efficiency in both areas into a cohesive system that serves all people in need, and is inclusive, adequate, sustainable and efficient for the needs of the future.

Serving a changing country in a changing world, the Indonesian social protection system should support households and individuals during different states of transition: from unemployment to employment; from poverty or vulnerability to prosperity; from youth to old-age; from one job to another; between geographic locations; during periods of sickness or injury; or in the aftermath of shocks. In doing so, the system will meet the changing needs of a middle-income country’s population and its expectations that the state and social protection system provide adequate protection in old age, support job search, and provide financial support in the event of shocks. Indonesia’s social protection system should be one that contributes to national wealth and human capital accumulation, responds to new social dynamics and needs, and actively supports an emerging middle-class. Importantly, it should aspire to be universal and accessible to all the Indonesian population, irrespective of whether they are employed in formal or informal jobs.

To achieve this, the GoI will need a comprehensive package of safety nets, insurance, savings and services that protect people from shocks and give them the tools to manage risks and uncertainty. The increased risks encountered in the changing nature of work also call for adjustments to the existing system of worker protection. A new social contract could provide a SP system that is decoupled from how or where people work, increasing coherence across social assistance and social insurance, and could establish a system that:

1. Provides its people with a “guaranteed minimum” protection across the lifecycle through a more consolidated package of programs; and
2. Complements the guaranteed minimum with a coherent set of mandated and individually financed social insurance programs for consumption-smoothing.

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*Source: World Bank (2016b).*

*Source: World Bank pension database.*

*Packard (2019).*

*Patient (2019).*
6. **How can this be achieved?**

**6.1 Establishing a guaranteed minimum to provide a protection floor**

The policy objective of a core “guaranteed minimum” is to prevent poverty among those vulnerable at or near the poverty line and the further impoverishment of people who are already poor, i.e., to provide a basic protection floor for all. In addition, the guaranteed minimum could promote other priority objectives, such as human capital acceleration, productivity and labor mobility, and disaster response by continuing to employ instruments, such as conditional cash transfers, establishing linkages to employment or skills programs, and by incorporating resilience-building and responsive financing mechanisms.

With today’s welfare distribution, ensuring a minimum level of protection will entail expanding the needs-based and publicly-financed social assistance package to a larger share of the population. In Indonesia, the differences in welfare between households from the 40th to the 70th percentiles are minimal today, and this could mean potentially covering some households all the way to the 70th percentile. It is important to note that, while the proposed guaranteed minimum would provide universal coverage in principle, benefit payments could be contingent and progressive, meaning that benefits are available when and where needed. This could be achieved by applying progressive universalism and a tapering of the publicly-financed benefits for people higher in the income distribution. Furthermore, many benefits may not be needed by many people in a given period, or even at all, so what is important is the universality of entitlement for coverage against impoverishing losses. Those who do not suffer such losses may be covered by the guarantee, but never actually receive a payout.
The range of social assistance programs currently operating in Indonesia provides a solid basis, and could be further consolidated and reformed to include currently uncovered gaps for the poor/vulnerable disabled, households without children and the elderly. While the nascent pension scheme (JHT) is designed to protect the current working age population from old age poverty in the future, the 5.4 million elderly and 3.5 million disabled that are poor or vulnerable today will be particularly vulnerable groups going forward. Special measures will be needed to bring the elderly more comprehensively into the social assistance system and to ensure that they are also protected by a guaranteed minimum. The SJSN pension scheme will not provide income in old age for most Indonesians, since middle-aged and elderly people today will not have time to contribute for a sufficient period before they need their pensions. Without additional measures for these cohorts to ensure the poor elderly are covered by social assistance while the contributory scheme matures, the percentage of the elderly living in relative poverty will almost certainly increase. There is therefore an urgent need to extend

1 Consolidating cash transfers by integrating the PKH and PIP programs

The current PKH and PIP programs serve similar population groups and objectives. Integrating the two programs under PKH would strengthen program targeting and delivery, as it would converge under the much stronger PKH systems. An integrated PKH and PIP would also lead to higher coverage among the poor, and PIP beneficiaries would receive a much more adequate benefit through an increase in the average benefit from 7 to 21 percent of median consumption. From an efficiency standpoint, PIP and PKH integration could yield a small reduction of about 4 percent in the poverty headcount. Administrative costs in running PIP would also be saved.

2 Increasing the coverage of PKH and Sembako with tapered benefit levels

The welfare distribution in Indonesia is relatively flat, and about 40 percent of households that are poor in a given year were not poor the year before. The vulnerable segment of the Indonesian population is therefore only slightly better off than the poor. Thus, there is ample reason to extend social assistance beyond the current level of coverage. Better protection could be provided by extending current programs such as PKH and Sembako, and adjusting their benefit levels. Ideally, such a package of cash transfers would consist of an unconditional transfer (Sembako), with a conditional top-up (PKH). The value of the extended cash transfer could be anchored to welfare levels and be tapered down the consumption distribution, considering their mean relative position from the vulnerability line. A first tier considers the value of PKH and Sembako at existing levels, which are sufficient to bring the average poor households above the poverty line. The second tier views the position of the average vulnerable household with respect to the vulnerability line, and sets an average package of protection enough to bring those households just above the vulnerability line. This would significantly reduce the likelihood of these households falling into poverty. In addition, all households in the poorest 40 percent should by design already be receiving health insurance fee waivers, which would protect them from falling into poverty through health shocks. This policy change combined with the merger of PIP and PKH described above would render an increased level of protection for households both with and without children, and could reduce poverty by about 41 percent from the current rates, all else being equal. Vulnerability could decline by about 12 percent and the Gini reduce about 1.4 points.

3 Improving protection along the lifecycle, in particular for the elderly

For households without children, the guaranteed minimum could be achieved by increasing, potentially doubling, the unconditional and poverty-targeted Sembako benefit. A doubled Sembako benefit could reduce poverty by an additional 0.8 of a percentage point and vulnerability by 0.5 of a percentage point. In 2020, the GoI implemented an increase of about 40 percent in the Sembako benefit, and has included a wider spectrum of food items, including fish, meat and nuts. Over time, the GoI may also consider transitioning the Sembako benefit to a cash transfer program, which could promote greater flexibility and generate local economic multipliers. A poverty targeted base transfer delivered in cash would then form the first layer of a “guaranteed minimum” for all households, regardless of their family composition.

Given the levels of elderly poverty and the demographic transition in Indonesia, the elderly will be a particularly vulnerable group going forward. Special measures will be needed to bring the elderly more comprehensively into the social assistance system and to ensure that they are also protected by a guaranteed minimum. The SJSN pension scheme will not provide income in old age for most Indonesians, since middle-aged and elderly people today will not have time to contribute for a sufficient period before they need their pensions. Without additional measures for these cohorts to ensure the poor elderly are covered by social assistance while the contributory scheme matures, the percentage of the elderly living in relative poverty will almost certainly increase. There is therefore an urgent need to extend...
What are the estimated impacts of these reforms taken together?

In comparison to the current situation, where around 60 percent of the poorest 10 percent receive at least one program (PKH or Sembako), the three reforms proposed above would see 90 percent of the poor receive at least one program (among PKH, Sembako or elderly or disability support). Such a safety net would thus be much more inclusive and protective than the current one. The cumulative estimated impacts of these different scenarios would be sizable (Table 3). Policies that lead to greater inclusion, coverage and adequacy of social assistance programs could lead to further reductions in poverty (to around just under half the current level, all else remaining equal), vulnerability (by about 12 percent), and inequality (reduction in Gini coefficient by about 1.8 points).

<table>
<thead>
<tr>
<th>Model</th>
<th>Components</th>
<th>Poverty rate</th>
<th>Vulnerability rate</th>
<th>Inequality (Gini)</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>Merging PIP with PKH</td>
<td>-4%</td>
<td>-7%</td>
<td>-0.0</td>
</tr>
<tr>
<td>A+B</td>
<td>Expand PKH, Sembako to 40% coverage with tapered benefit levels</td>
<td>-31%</td>
<td>-9%</td>
<td>-1.3</td>
</tr>
<tr>
<td>A, B + C1</td>
<td>Expand elderly assistance to 70% coverage</td>
<td>-4%</td>
<td>-12%</td>
<td>-1.8</td>
</tr>
<tr>
<td>A, B + C2</td>
<td>Expand disability assistance to 70% coverage</td>
<td>-32%</td>
<td>-10%</td>
<td>-1.4</td>
</tr>
</tbody>
</table>

Note: From World Bank CEQ Modelling. The impact estimations for model B, C1 or C2 are cumulative and include the previous models within them. The impacts are indicative and subject to change due to the headline growth, inflation as well as the incidence of growth and inflation across the welfare distribution. Through successive models A and B and including C1 or C2 in the table, impacts due to increases in adequacy and expansion of programs, up to 40 percent of the general population and up to 70 percent of the elderly and disabled population, both existing and new are modelled. The discussions here concern PKH, Sembako, PIP and elderly and disability assistance programs.

Contingent coverage of catastrophic losses (health, natural disaster/climate change). Many shocks result in losses that would overwhelm minimum income guarantees. These include the costs from health events (lost working time/earnings/costs of medical treatment and medication), disability, death and natural disasters. The potentially impoverishing impacts of such shocks, a case in point being the COVID-19 pandemic, can affect households along the whole welfare distribution. In Indonesia, the health shocks through subsidised premiums of JKN through the PBI. In doing so, it extends contingent coverage against large, catastrophic losses by integrating people who cannot afford premiums into the risk-pooling system with everybody else.

Similarly, the SP system could be better adapted to respond to shocks such as natural disasters and pandemics such as COVID-19 to better support disaster victims to meet basic needs and rebuild their lives back faster. Without a systematic and timely response, disaster-affected households face prolonged periods of destitution and may not fully recover from loss of their livelihoods. Current disaster response in Indonesia is mostly designed and operated separately from the core social assistance programs, and is often not timely due to the budget reallocation process. For social assistance to be adaptive and scalable in response to disaster, the system should be able to increase benefits to existing recipients, extend benefits to new recipients, and introduce new benefits under the existing programs. These should be implemented under a strong adaptive SP framework that includes early warning systems, predictable financing, and scalability of key programs to respond to disaster in a timely and predictable manner.

Social insurance is crucial to help individuals and households weather shocks that affect most of the population, including those related to the cost of medical procedures, unemployment, disability, death and old age. A large share of future employment in Indonesia is likely to be undertaken without standard work contracts, and thus without the benefits of traditional contributory social insurance schemes or mandated worker protection. If Indonesia continues to rely on a traditional contributory social insurance scheme that links coverage with formal labor market status, it will exclude most workers and their families from coverage against short-term risks and may lose the race between pension coverage and population aging. Introducing new incentives to encourage voluntary participation in social insurance, including to cater for “future works”, could help mitigate this risk. Future social insurance should be made accessible to all the Indonesian population, irrespective of whether they are employed in formal or informal jobs. Over time, the intention should be for all workers, including the self-employed and informal sector, to be covered against these risks.

6.2 Consumption smoothing through mandated and individually financed social insurance programs
The 2014 reform has gone a long way in rationalizing SI in Indonesia but important gaps still exist in the SJSN pension system in terms of adequacy, sustainability and coverage. Pension coverage in particular, both current and future, is a matter of concern given the aging of the population and high rates of informality. These social insurance programs could be made more efficient and effective by implementing a number of reforms to the SJSN system, including a gradual increase in the retirement age. To ensure sustainability, improvements in adequacy require additional measures such as contributions in the valuation of benefits, while coverage should ideally be expanded after measures have been taken to ensure sustainability.

Contribution rates in the SJSN scheme could be increased to postpone deficits into the distant future, but this would increase the tax wedge—the gap between labor costs and take-home wages—and could encourage greater informalization. An alternative approach to expanding social insurance coverage without creating labor market distortions is already being implemented for health insurance in Indonesia, namely, to have the GoI pay the premium for poor informal sector workers. A similar approach, combined with expanded social assistance coverage for the elderly, would help address the coverage gap just at the time population aging will begin to accelerate. To reach universal social insurance coverage, Indonesia could therefore rely on a combination of self-financed insurance for those who can afford it, and explicit government contributions or redistribution for those who cannot. The self-financed element would be financed by contributions, while contributions from the government would be covered by the budget.

A seamless system such as this would allow portability regardless of employment status and would reduce administrative costs relative to having multiple funds. As with the guaranteed minimum package, the government contribution for contingent coverage can be tapered gradually as people’s income or consumption rises.

Reforms to rationalize the civil service pension scheme and move younger civil servants into the national scheme will also be required. To ensure the adequacy of pensions under current civil service rules, the earnings base that is used to calculate the pension needs to be redefined from one based on base salary alone to one which includes allowances. However, any increase in the earnings base need to be accompanied with other parametric reforms, in order to keep pension debt relatively unchanged. The affordability of the civil service pension scheme is also an immediate issue due to the wave of retirements coming in the next few years. If the GoI wishes to improve pension benefits while keeping the cost of the civil service pension scheme unchanged, any viable solution will involve increasing retirement ages and changing to inflation indexing. These two changes create the fiscal room needed for benefit improvements as benefits would begin at a later age and benefit increases following retirement would be smaller. Once these two changes are made, there are options available for changing the pension program’s design and financing to make the system fairer, adequate and equitable across generations of civil servants. A systemic reform for new civil servants would also pave the way for eventual integration of the civil service and SJSN scheme, as envisioned in the law.

Social insurance reforms could also incorporate the current severance pay system by prefunding unemployment savings accounts to be managed together with the existing old age savings program. The current worker protection provisions in Indonesia do not contain insurance against the loss of employment, with the exception of the severance pay system, which provides very limited de facto protection to workers. The introduction of an unemployment benefit would help manage these risks. A “mixed” unemployment benefit system could integrate current severance payment obligations and the old age saving system, while reducing the economic burden on workers and employers. The “mixed” unemployment benefit system in Indonesia could consist of an individual savings pillar and a newly created solidarity fund. Workers and employers would both contribute to the individual savings pillar. Such a design allows employers to offset (part of) their severance obligations by contributing to workers’ individual accounts, effectively integrating severance payment obligations in the system. Upon depletion of the fund in the individual account, unemployed workers could receive access to the solidarity component based on certain conditionalities. These could involve the participation in active labor market programs, including job counselling, job search, and skills training. Overall, with these reforms, income protection in case of unemployment would be much more effective and adequate than today’s system.

The framework to improve JKN implementation, and eventually aiming at improving its sustainability, should include:

- **Raising revenue.**
- **Update JKN premiums based using robust actuarial analysis.**
- **Consider extending government contributions to informal sector to attract healthier members to join the risk pool.**
- **Identify, mobilize potential resources especially from tobacco taxation.**
- **Managing medical expenditure growth.**
- **Strengthen the purchasing role of BPJS-K which will empower them to manage resources more efficiently, and enable them to create incentives to influence provider behavior for more effective service delivery, efficient use of resources, and higher quality of care.**
- **Rationalize and make explicit the benefits package.**
- **Provide the provider payment design, e.g., address open-ended hospital payments where most spending occurs.**
- **Improve the quality and use of data by investing in the quality and interoperability of various information systems.**

Social protection for Indonesia’s 2045 vision?

7. What will it cost to strengthen Indonesia’s social protection system?

Government spending on social assistance, excluding subsidies, more than doubled in real terms between 2009 and 2018, reaching IDR 87.5 trillion in 2018. Nearly 90 percent of total national spending is from the central government, with the remainder spent by subnational governments. The spending reflects massive increases in coverage; PKH and PIP quadrupled the number of beneficiaries between 2010 and 2017, and PKH now reaches 10 million families with cash transfers. However, total spending on social assistance remains low at 0.7 percent of GDP; which is less than the average of lower middle-income countries (Figure 11). When comparing Indonesia to some of its regional peers in the East Asia and Pacific region (EAP), the share of GDP for social assistance is similar to countries such as Vietnam and Thailand. It is, however, lower than most Latin American (LAC) and East Europe and Central Asia (ECA) countries. Global evidence shows that aggregate spending of social assistance (social safety net) averages 1.6 percent of GDP, with the average for low-income countries at about 1.5 percent of GDP. 55

Source: World Bank ASPIRE and World Bank staff calculations.

Note: Selection based on data availability. Grey highlights indicate countries that have similar revenue collection performance as Indonesia, highlighted in black.

Figure 11: Social assistance spending as a share of GDP (%) — selected countries

![Figure 11: Social assistance spending as a share of GDP (%) — selected countries](image-url)

55 World Bank (2016).
As a result of the relatively late start of the BPJS pension scheme, contributory pension spending as a share of GDP will also continue to be lower than many countries at Indonesia’s stage of demographic aging. A universal approach would require significant government contribution to expand the non-contributory portion, at least in the short to medium term. Ultimately, overall spending levels will have to rise to achieve reasonable levels of adequacy and continue to reduce out-of-pocket spending. It will cost a total of 0.8 percent of GDP in 2019 to pay for the elderly social assistance to the poorest 70 percent of those above age 65 (0.17 percent), and contribution subsidies for all workers aged 20 to 64 (0.71 percent). The grey line shows what the cost will be if social pensions of IDR 200,000 per month are indexed to wage growth and paid to all those over the age of 65.

The incremental spending requirements on the SP system will be around 1.5% of GDP.

<table>
<thead>
<tr>
<th>Intervention</th>
<th>Program</th>
<th>Reform Scenario</th>
<th>Total</th>
<th>Incremental</th>
</tr>
</thead>
<tbody>
<tr>
<td>Social Assistance</td>
<td>PKH* and Sembako</td>
<td>Expanded PKH, Sembako to 40% coverage with tapered benefit levels.</td>
<td>0.77%</td>
<td>0.24%</td>
</tr>
<tr>
<td>Elderly assistance</td>
<td>Expanded elderly assistance to 70% coverage for elderly.</td>
<td>0.17%</td>
<td>0.15%</td>
<td></td>
</tr>
<tr>
<td>Disability assistance</td>
<td>Expanded disability assistance to 70% coverage for people living with disabilities.</td>
<td>0.03%</td>
<td>0.03%</td>
<td></td>
</tr>
<tr>
<td>Combined SA</td>
<td></td>
<td></td>
<td>0.97%</td>
<td>0.41%</td>
</tr>
<tr>
<td>Social Insurance</td>
<td>Work Accident (JKK) &amp; Death Benefit (JKM)</td>
<td>Offer a government contribution of 0.54% of minimum wage* to all adults.</td>
<td>0.12%</td>
<td>0.12%</td>
</tr>
<tr>
<td></td>
<td>Pension</td>
<td>Offer a pension contribution, by the government, of 3% of minimum wage* to all adults.</td>
<td>0.71%</td>
<td>0.71%</td>
</tr>
<tr>
<td>Combined SI</td>
<td></td>
<td></td>
<td>0.83%</td>
<td>0.83%</td>
</tr>
<tr>
<td>SP</td>
<td>SA + SI</td>
<td></td>
<td>1.8%</td>
<td>1.2%</td>
</tr>
<tr>
<td>Health</td>
<td>Health insurance subsidies</td>
<td>Offer and expand health insurance coverage to all adults.</td>
<td>0.49%</td>
<td>0.28%</td>
</tr>
<tr>
<td>Total, SA + SI + full health coverage</td>
<td></td>
<td></td>
<td>2.3%</td>
<td>1.5%</td>
</tr>
</tbody>
</table>

Notes: *The minimum wage is the observed minimum wage for all workers from the 2018 labor force survey. The minimum ‘observed’ wage for 2018 that we deduced from the data is IDR 2 million per month. The minimum wages are assumed to grow at the rate of wage growth in the economy. For social insurance estimates, in our calculations include all individuals aged 20 to 64. JKK and JKM calculations assume government contribution equal to 0.54 percent of average monthly wage of IDR 2 million paid to all adults/the bottom 40 percent of adults. Note that under current law, JKK/JKM/JP cover only a subset of all adults. An increase in health coverage would involve covering the remaining 60 million individuals. The pension contribution by the government is equal to 3 percent of IDR 2 million monthly and this contribution would give future retirees a monthly pension equivalent to IDR 200,000 monthly, today.
8. Implementing and financing Indonesia’s social protection system

8.1 Effective implementation of a social protection system

A well-functioning integrated delivery system will be required to provide the guaranteed minimum and to implement a coherent and efficient set of social insurance programs. Effective implementation of SP programs requires integrated delivery systems for identifying, enrolling, and paying the targeted populations. Modern systems of monitoring and evaluation and adequate error, fraud and corruption mechanisms are also essential. Indonesia has built a solid foundation and integrated platforms to better deliver multiple programs, including the unified social registry (DTKS)\(^4\) for identification of beneficiaries, an integrated payment gateway under the collection of state-owned banks (Himbara), as well as partnering with local governments to test digital service windows, enable dynamic data updates and grievance redressal. Further efforts will be needed to make these and other components more effective and responsive to the changing needs of the SP system. It will also be essential for Indonesia to strengthen its currently incomplete and ad-hoc data protection and privacy regime.

Indonesia has a well-developed social registry, the UDB, to assess needs and conditions to determine eligibility for SP programs. Although use of the UDB has expanded significantly since it was launched in 2012, only PKH and PIP have fully adopted it for eligibility determination, beneficiary selection and enrolment.\(^5\) Furthermore, the Ministry of Social Affairs (MoSA) has initiated local government-led updating activities, but some of the data are still based on a survey last conducted in 2015. The data capture information on households at a certain point in time and are not continuously updated on changes in needs and conditions. Finally, limiting coverage to the poorest 40 percent leaves a large vulnerable population and an “aspiring middle class”\(^6\) who are not yet economically secure and at risk of being pushed into vulnerability or poverty due to shocks. The DTKS is therefore of limited use for programs that need to conduct eligibility assessments for people that are poor, vulnerable and in the aspiring middle class such as for electricity subsidies, skills training, health insurance or in disasters. Even for programs that are meant to cover the poorest 40 percent, the DTKS cannot contain a complete and accurate set of people with no errors of inclusion or exclusion. There would be significant gains in efficiency and transparency. However, there is still only partial digitization of processes between payment providers and recipients. Program beneficiaries incur significant private transaction costs to withdraw cash, as they may live far away from a bank branch/ATM and have no other means to access or use the cash virtually. Furthermore, only PKH and PIP make use of the integrated payment gateway under the collection of state-owned banks (Himbara). Other programs still use state-owned banks to deliver payments, but follow different procedures in administering payments and use different cards to allow beneficiaries to cash out their transfers. Bank interoperability, which should allow beneficiaries to cash out their benefit at any bank ATM or agent, is planned but currently not yet implemented. Going forward, it is essential to develop a shared payments delivery system for achieving greater effectiveness and efficiency.

A robust ID system is a crucial input for an integrated SP system, enabling the authentication of beneficiaries’ identity and facilitating sharing of information about beneficiaries (e.g., income, benefit levels) across programs. The SP system in Indonesia could more systematically use foundational ID systems for identification and authentication. The Ministry of Home Affairs (MoHA) supports the SIAK ID system that issues a unique identification number (Nomor Induk Kependudukan, or NIK) to all registered persons through their family cards (Kartu Keluarga, KK) and national ID cards (Kartu Tanda Penduduk, or KTP), using biometrics to deduplicate individuals. While 95 percent of the population have a NIK in the SIAK system, it is not always used and/or verified. For example, the SJSN employment program does not require the NIK for registration for workers. Even when individuals have NIKs and other functional IDs such as family welfare cards (Kartu Keluarga Sejahtera, or KKS) and BPSJS cards, programs offer diverse and sometimes incompatible authentication methods and practices.

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8.2 Social protection financing

Indonesia relies mostly on general revenue, payroll taxes and compulsory contributions to finance its SP system. General revenues are used to fund social assistance and the subsidized health insurance component (JKN-PBI), while social security contributions and payroll taxes fund social insurance. Despite significant cross-subsidies between formal and informal sector households, the health insurance cost to the GoI is increasing and deficits have emerged.

In addition, population aging is outpacing the expansion of traditional contributory pensions. Without additional measures to bring in informal sector workers and to ensure the poor elderly are covered by social assistance, the share of the elderly living in relative poverty will rise. In order to finance its future SP system, Indonesia should consider a combination of:

1. Working within the existing revenue and expenditure envelopes to better allocate and use these resources; and

2. Gathering additional resources through improved revenue mobilization.

The allocation and efficiency of current SP spending could be further improved. Despite an overall decline since 2014, spending on poorly targeted energy subsidies has recently increased and remains sizeable (IDR 153.5 trillion, or 1.0 percent of GDP in 2018). Further reallocation away from regressive subsidies toward targeted transfers such as PKH and Sembako will improve the overall efficiency of social spending. In addition, the proposed merger of PKH and PIP, more rigorous targeting and stronger beneficiary monitoring would increase efficiency.

The extent of SP spending is also constrained by the general revenues that the GoI can generate. More resources to the SP sector would entail a consideration of how to most optimally increase fiscal revenues. There are different alternatives in terms of realistic possibilities of increased collection and of fair burden, avoiding measures that place a significant burden on the population intended to benefit from social protection expansion, namely those at the bottom of the distribution. Reductions in VAT exemptions would increase resources, but could place a significant burden on the poor who tend to consume the most exempted goods. Another promising alternative may be tobacco taxes, which offer the additional public health benefit for the poor, who have higher consumption elasticity. Finally, there is scope to increase collection from personal income tax by reducing evasion and lowering deductions. Ultimately, the GoI will have to match ambition in terms of expanding coverage of the SP system and undertaking fiscal reform that can meet expectations.

Reductions in VAT exemptions are a promising way to increase resources. The current structure of VAT exemptions translates to IDR 90.6 trillion, equivalent to US$21.6 billion (in 2011 PPP terms), or 0.67 percent of GDP. Revenue generation in this manner would need to be accompanied by some sort of compensation for those in the lower end of the consumption distribution, for whom the additional VAT burden of removing exemptions is the greatest. This should be possible, as the additional revenue would be large enough to amply compensate the poor and could be achieved if the fiscal space created by closing VAT exemptions could be utilized more broadly to improve coverage and/or generosity of some of the existing (poverty targeted) programs that Indonesia already has.

Excise taxes on tobacco represent another alternative. For a country with one of the highest prevalences of adult smoking in the world, the burden of taxes on tobacco is still lower than in many countries and insufficient to have...
meaningful influence on consumption behavior. Such taxes can also offer an additional public health benefit for the poor. Given their higher consumption elasticity, the burden of such a tax would fall more proportionally on the middle class. Again, the size of the potential revenue generated would be large enough to compensate those who bear the brunt of additional excise. For example, consider the social assistance package which proposes the expansion of PKH and BPNT/Sembako to cover all households in the bottom 40 percent, along with social assistance for the elderly and disabled also in the bottom 40 percent. At an estimated cost of around 0.7 percent of GDP, this package would be half of the additional revenue that could be generated from increasing the price of cigarettes by 84 percent.

Simulations show that successful implementation of some key reforms in the revenue system could generate additional fiscal space of up to 1.8 percent of GDP for spending on priority sectors. The combined impact of reallocating energy subsidies including LPG and diesel, removing poorly targeted VAT exemptions and raising the tobacco excise could raise a combined 1.8 percent of GDP. The proposed SP reforms comprising 1.5 percent of GDP would therefore be well within the government’s fiscal capacity while continuing to target a 2 percent of GDP fiscal deficit (Table 5). The level of fiscal gain required to finance these reforms is well within the Government’s own fiscal capacity while continuing to target a 2 percent of GDP. The proposed SP reforms comprise 1.5 percent of GDP.

<table>
<thead>
<tr>
<th>Fiscal Gain</th>
<th>Source: World Bank (2020a) and CEQ calculations (for the VAT figures).</th>
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</thead>
<tbody>
<tr>
<td>Gains from eliminating energy subsidies</td>
<td>0.7</td>
</tr>
<tr>
<td>Gains from tobacco excise reform</td>
<td>0.7</td>
</tr>
<tr>
<td>Gains from removal of VAT exemptions</td>
<td>0.4</td>
</tr>
<tr>
<td>Total</td>
<td>1.8</td>
</tr>
<tr>
<td>Total cost of incremental SP reform</td>
<td>1.5</td>
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9. **Concluding remarks**

The GoI’s vision for 2045 is to be a sovereign, fair, and prosperous country, and to move from middle- to high-income status. An inclusive and efficient SP system will be essential to achieving these ambitious goals, and it will need to operate in the context of technological development, changes in the nature of work, demographic change, changes in how and where people work, and climate-related events such as increased disasters. While the COVID-19 pandemic has motivated an impressive response via social protection programs, it has also exposed some gaps in the existing levels of coverage and the ability of deliver benefits to the right people, at the right time and in the right amount. Achieving Indonesia’s vision and having a SP system that protects and serves all will require a rethink of the current social contract in Indonesia. This is urgent, because otherwise it will be difficult to reach the ambitious poverty reduction and inclusive growth targets that have been set out for 2045.

These reforms are not small and they come with significant costs. They will also impact the social contract and require a continued move toward a system where the state finances those who cannot insure themselves against current and future shocks, while in the upper layers of the income distribution employers and citizens contribute to insurance mechanisms such as pensions and unemployment benefits. Poverty prevention is essential to the new risk-sharing strategy, and justifies increased government contributions for the poor and to finance these from broad-based taxes such as VAT. It can be done with the right reforms, such as ending unhelpful subsidies and overhauling taxation policies.

This is the right time to think about how to improve SP in Indonesia. Indonesia’s human capital deficit will require significant investments for years to come to prepare the Indonesia people for the future of work. Social assistance and insurance programs tailored to the changing work force will be key. At the same time, good jobs help people acquire and build human capital, which can then create a virtuous cycle by enabling them to become more productive or to move on to better jobs. The SP system in Indonesia can support millions of people to acquire the right skills to compete in today’s changing jobs market and millions of children with better education and health care to make them ready for the future labor market. Making these investments today will give Indonesia a head start to ensure it protects and promotes all as it moves toward achievement of its ambitious 2045 targets.
Investing in social protection today will give Indonesia a head start to ensure it protects and promotes all as it moves toward achievement of its ambitious 2045 targets.