Chapter 6

Aligning COVID-19 Recovery and Stimulus Measures with Low-carbon Green Growth through Green Bonds in Indonesia

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Ministry of National Development Planning, Indonesia

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1. Introduction

1.1. Recent Economic Snapshot

Between 2000 and 2018, Indonesia enjoyed steady economic growth and significant socio-economic progress, with an average annual gross domestic product (GDP) growth rate of 5.6%. During this time, Indonesia maintained stability in terms of inflation, public finances, and the balance of payments and debt. All this was despite significant headwinds, including the global financial crisis, steep declines in primary commodity prices, and repeated turbulence in global financial markets (Bappenas, 2019b).

Although Indonesian economic growth may decline during 2020, the focus of national spending is not only to face the current challenges with the novel coronavirus disease (COVID-19), but also to build a stronger human resources foundation, improve productivity and competitiveness, and develop infrastructure. Table 6.1 shows the projection of economic growth in 2021 is estimated to be in the range of 5%, supported by a gradual recovery in consumption as economic activity begins to recover in a new normal condition.

Table 6.1 GDP Growth, 2017–2021

	2017	2018	2019	2020*	2021**
	% changes, volume (2010 prices)				
GDP growth	**5.1**	**5.2**	**5.0**	**-2.07**	**4.5–5.5**
Private consumption	5.0	5.1	5.2	-2.63	4.1–4.9
Government consumption	2.1	4.8	3.2	1.94	2.5–3.5
Gross fixed capital formation	6.2	6.6	4.4	-4.95	6.0–7.1
Exports of goods and services	8.9	6.5	-0.9	-7.70	3.5–5.1
Imports of goods and services	8.1	11.9	-7.7	-14.71	4.4–5.9

GDP = gross domestic product.

Source: *Statistics Indonesia, February 2021; **Presidential Regulation No. 86/2020: Government Action Plan 2021.

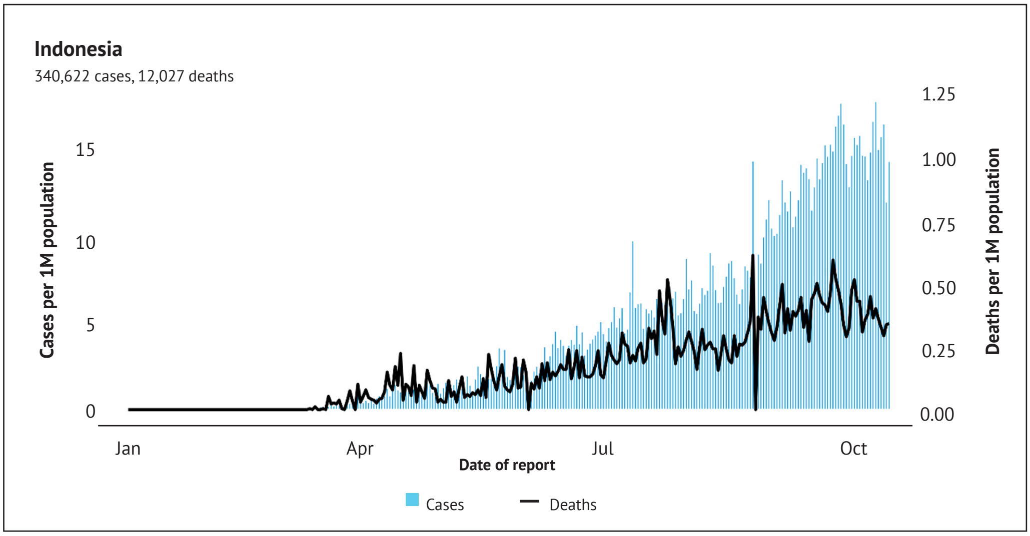
High uncertainty about the speed of the global recovery will also affect the economic projection next year. Following a sharp decline, the economy may incline and rebound in 2021 in the range of 4.5%–5.5%.

1.2 COVID-19's Spread in Indonesia

The coronavirus outbreak created a crisis for the global economy. In Indonesia, COVID-19 caused more than 1,700 deaths, infected 28,300 people, and dragged down more than 1.1 million into poverty (Ing and Vadila, 2020). The pandemic has also had a significant domino effect in the health, social, economic, and financial sectors. This is a serious challenge for the world as each country tries to prevent this crisis from getting worse (BKF, 2020).

Figure 6.1 shows more than 340,000 COVID-19 cases through October 2020, with more than 12,000 deaths. Total cases slightly declined in October 2020.

Figure 6.1 Total COVID-19 Cases in Indonesia



Source: https://worldhealthorg.shinyapps.io/covid/.

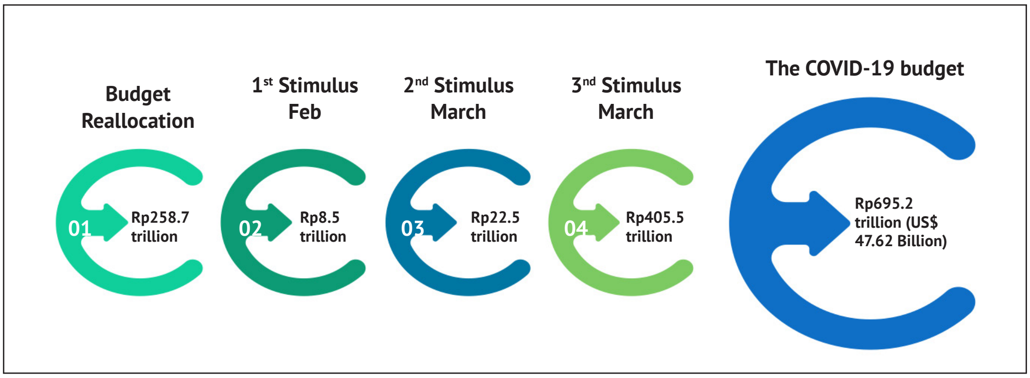
2. Stimulus Package to Combat the COVID-19 Pandemic

As a quick response to prevent worsening impacts of COVID-19 in health, social and economic sectors, Indonesia issued a regulation in lieu of law, Perppu No. 1/2020, that contains several policies for prompt and coordinated action. Perppu No. 1/2020 is expected to provide a basis for the government and related institutions to continue taking structured and systematic steps in order to overcome the COVID-19 threat in the health sector, social threats and economic threats, as well as macroeconomic financial system instability.

To mitigate the impacts of COVID-19, the government strengthened its commitment to providing economic stimulus with real benefits for the public. This is required as a jumpstart for the initial recovery of the national economy, which should then be followed by monetary expansion (BKF, 2020). The government has unveiled a Rp695.2 trillion (US$49 billion) stimulus package to fight the economic and public health impacts of COVID-19 (see Figure 6.2 on the following page).

There have been three financial stimuluses introduced by the government. The first stimulus package in February 2020 accelerated capital expenditure distribution, appointed official treasury officials, distributed social assistance and village fund transfers, and expanded the number of Staple Food Card (***Kartu Sembako***) beneficiaries. The second stimulus package of Rp22.5 trillion in February 2020 was earmarked for tax incentives, ease of export and import, and the financial sector.

Figure 6.2 COVID-19 Stimulus Package in 2020

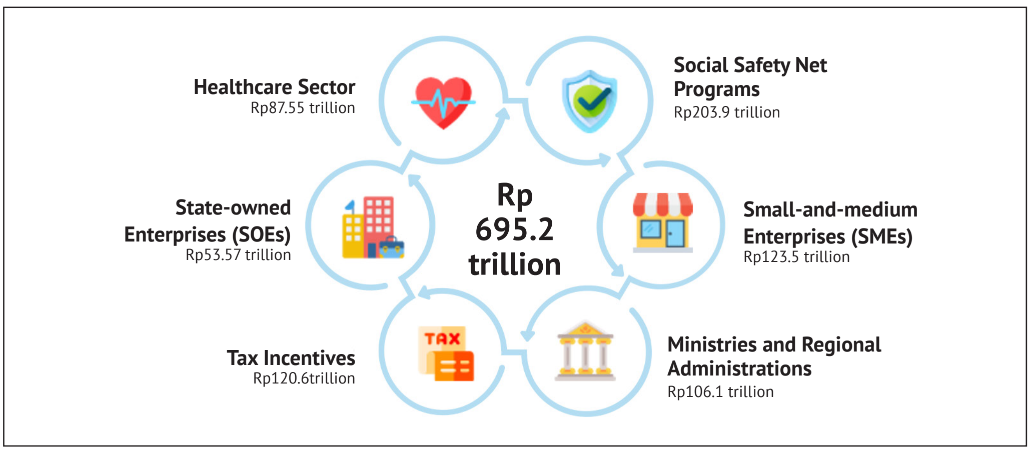


Source: National Covid Team and National Economic Recovery, Ministry of Finance, Bappenas.

Third, the government has determined to offer Rp405.5 trillion for handling the ongoing COVID-19 outbreak. The budget allocation consists of Rp75 trillion for the health sector, Rp10 trillion for the social protection/social safety net, Rp70.1 trillion for tax incentives and stimulus for a microcredit programme, and Rp150 trillion for the national economic recovery programme, as well as credit restructuring and business funding for micro, small, and medium-sized businesses (Ibadurrohman and Pamungkas, 2020).

With the stimulus packages, the government prioritised three aspects in responding to the crisis: protecting the health and life of the community; maintaining purchasing power, especially for the middle to lower class; and preventing the number of bankruptcies. These three aspects are implemented with the Large-Scale Social Restrictions policy, limiting physical distance, working and studying from home, expansion of the Family Hope Program and the Pre-employment Card, distribution of basic necessities, tax incentives, reduction of electricity bills, and National Economic Recovery Programs (BKF, 2020).

Figure 6.2 National Economic Recovery Program in 2020



Source: National Covid Team and National Economic Recovery, Ministry of Finance, Bappenas.

As a response to COVID-19, the government aims to implement the National Economic Recovery Program. This programme is an extraordinary measure as referred to in Government Regulation in Lieu of Law (Perppu) Number 1 of 2020, which is now (stipulated as) Law No. 2 of 2020 (Inayatillah and Bonaedy, 2020). The government provided Rp87.55 trillion for the healthcare sector, Rp203.9 trillion to strengthen social safety net programmes, and Rp123.46 trillion in incentives for micro, small, and medium-sized enterprises. The government also allocated Rp120.6 trillion for tax incentives and Rp106.11 trillion to support ministries and regional administrations, and Rp53.57 trillion as a stimulus for state-owned enterprises (SOEs).

Since COVID-19 is still occurring in 2021, Indonesia provide state budget around Rp. 699.43 trillion or US$ 47.91 billion. For reducing the impact of COVID-19, Indonesia allocated Rp176.3 trillion for health care, Rp157.4 trillion for accelerating the social safety net (social protection), and Rp186.8 trillion for micro, small and medium enterprises including Rp53.9 million stimulus for SOEs. The Committee for handling COVID-19 and the National Economy Recovery, headed by Coordinating Minister for Economy, explain that stimulus for the National Priority Program is Rp125.17 trillion.

3. Low-carbon Development Initiative

Indonesia is on an unsustainable development pathway, as boundless technological and innovative advances result in natural resources exploitation and investments in high amounts of carbon, and inefficient energy and transport systems, resulting in pollution, depletion of fisheries, and the damaging effects of global climate change (Bappenas, 2019b).

With this understanding, Indonesia is transforming its economy into one wherein development is measured no longer by GDP growth only, but also environmental sustainability, resource efficiency, and social equity (Bappenas, 2019b). A decline in the quality of the environment and depletion of natural resources has the potential to hamper Indonesia's economic growth, which still relies on the commodities and natural resources sectors.

Indonesia has committed to becoming a pioneer of sustainable development with its Low Carbon Development Indonesia (LCDI), which was first initiated at the 2017 United Nations Conference on Climate Change. LCDI was launched at Indonesia's Ministry of National Development Planning (Bappenas) (Bappenas, 2018).

LCDI is essential to deal with a variety of challenges stemming from increasing earth temperature, which will considerably affect food productivity and increase the risk of climate-related disasters. Likewise, deforestation, land degradation, and air pollution from peat fires and fossil fuels will negatively affect productivity and quality of life. LCDI expects to incorporate greenhouse gas (GHG) emissions reduction targets into policy planning, along with other interventions for preserving and restoring natural resources (Bappenas, 2018).

GHG emissions are the main cause of climate change. Low-carbon development is crucial, not only to minimise the risk from climate change, but also to increase the competitiveness of the Indonesian economy in a more sustainable manner. This requires that low-carbon development maintains economic and social growth through development activities to produce low GHG emissions and reduce excessive use of natural resources. Bappenas' Pembangunan Rendah Karbon concept emphasises the cross-sectoral policy trade-offs needed to balance economic growth targets and poverty alleviation with emission reduction efforts, and to encourage the growth of green investment for more sustainable development (Bappenas, 2019a).

Low-carbon development and the green economy are key to boosting economic growth while not sacrificing environmental sustainability and social inclusivity. Therefore, the Ministry of National Development Planning/Bappenas will streamline the LCDI report on low-carbon development into a Five-Year 2020–2024 National Medium-Term Development Plan (Bappenas, 2019b).

In accordance with strengthening low-carbon development, green bonds have risen as a real force in generating private sector financing for renewable energy, and other eco-friendly industries. In 2018, globally, the green bond market is predicted to attract as much as US$250 billion (Houérou, 2018). With a US$150 million investment from International Finance Corporation, a member of the World Bank Group, OCBC NISP Bank, a subsidiary of OCBC Singapore, is launching Indonesia's first green bond, which is expected to catalyse a green bond market (Houérou, 2018).

Indonesia introduced the Budget Tagging Mechanism to gauge the effectiveness and efficiency of current climate change spending. This generates recommendations in the form of output- and outcome-oriented budgeting that is regulated under Ministerial decree No. 214/2017. Another result of the budget tagging process is the creation of fiscal instruments for climate change action, one of which is Green Sukuk, issued in 2018 (UNDP, 2018).

4. Financing Low-carbon Development Before the COVID-19 Pandemic

Indonesia is vulnerable to climate-induced hydrometeorological disasters. More than 95% of disasters are related to climate change, including flash floods, landslides, forest and land fires, drought, and extreme weather (Bappenas, 2019a). In addition, an increase in sea level and surface temperature will worsen natural disasters, especially in low-lying areas throughout Indonesia, which will directly impact health, agriculture, and the economy (UNDP, 2018).

Indonesia has made several financial commitments to climate change adaptation and mitigation, such as Green Bonds and Green Sukuk (UNDP, 2018). Indonesia has designed its Green Bond and Green Sukuk framework to back or re-account Eligible Green Projects (Abubakar and Handayani, 2020). Issuance is guided with the aid of the Green Bond and Green Sukuk Framework, reviewed by international independent reviewer Center for International Climate Research and graded with colours that indicate the degree to which eligible listed projects represent the country's long-term vision for carbon emissions reduction (UNDP, 2018). The issuance of Green Bonds will attract investors to enter into environmentally based development without the risks associated with individual projects (Setiawan, Asidiq, and Sholihin, 2019).

Beside Green Bonds, Green Sukuk is the other alternative for low-carbon development financing. Green Sukuk is an innovative, shariah-compliant bond, where 100% of the return is restricted to financing or refinancing green projects (UNDP, 2018). Green Sukuk has the capacity to connect the conventional social responsibility market with the Islamic financial market. Green Sukuk can also prove shariah finance's viability, both in the Muslim and global markets (Setiawan, Asidiq, and Sholihin, 2019). Green Sukuk is a decent and promising approach to align with global trends where the world focuses on sustainability-based projects, particularly on the environment and reforestation (Abubakar and Handayani, 2020).

The issuance of Green Sukuk is one of the government's endeavours in actualizing green financing. Green finance is an expansive term that can refer to sustainable development projects and initiatives, environmental products, and policies that support sustainable development. Green finance incorporates climate finance, but is not restricted to it and can include, for example, industrial pollution control, sanitation, or biodiversity protection. Mitigation and adaptation finance are explicitly identified with climate change-connected activities: mitigation finance refers to investments in projects and programmes that contribute to reducing GHGs, whereas adaptation finance refers to investments that reduce the vulnerability of products and persons to climate change (Abubakar and Handayani, 2020).

Indonesia is the first country to be issuing Green Sukuk at the global level. In March 2018, the government issued US$1.25 billion state sukuk on the global market. Green Sukuk will exclusively go to selected Eligible Green Projects (UNDP, 2018). Indonesian Sukuk has been recognised in the global market through positive press coverage. Indonesia's Green Sukuk have been distributed around the globe into high-quality accounts, mostly top-tier funds and banks, with 32% going to Islamic markets, 25% to Asia, 15% to the European Union (EU), 18% to the United States (US), and 10% to Indonesia. In the global market, new investors who are willing to invest in green projects have reached 29% of the total (Abubakar and Handayani, 2020).

5. Financing through Green Sukuk During COVID-19

COVID-19 is different from previous crises, impacting not only the economic sector, but also the national health system, and increasing social vulnerability (Firdaus and Djumena, 2020). Indonesia needs a significant increase in funding to address their widening budget deficit due to the pandemic.

Adopting a positive perspective, COVID-19 has become a signal for countries to make structural changes that align with sustainable economic practices, and it has had a positive impact on reducing emissions, although it is estimated that it will only be temporary. As Joseph Stiglitz stated, the world needs a green economy to build a better economy (build back better). In accordance with this, economic stimulus must be in line with efforts to transition to a low-carbon economy (Firdaus and Djumena, 2020).

The Ministry of Finance mentioned three strategies that could be implemented to keep Indonesia focused on achieving climate targets: (i) aligning action plans with the National Economic Recovery Policy; (ii) prioritising plans that can simultaneously restore the economy; and (iii) developing innovative funding schemes and policies in order to encourage the participation of non-government agencies(Firdaus and Djumena, 2020).

Indonesia had sold Rp369 trillion worth of government bonds as of May 2020, an increase of 98.3% from the same period last year. The government is making plans to issue another Rp990 trillion worth of government bonds, including samurai bonds and diaspora bonds, from June to December of this year to cover the widening deficit. As with Indonesia's third global obligation issuance this year, the government is also offering sukuk (Akhlas, 2020). According to Moody's, Green Sukuk accounted for around 3% of sukuk issuance as of June 2020. Indonesia's sukuk issuance is expected to increase by about 68.75% as the government unveiled a Rp695.2 trillion (US$47.3 billion) stimulus package to fight the pandemic (Rahman, 2020).

Sukuk issuance in 2020 was set to be higher than in 2019 as the government needed to finance the widening state budget and the national economic recovery programme. As of 6 August 2020, the government issued a total of Rp236.82 trillion in domestic sukuk. The figure almost reached the 2019 amount, which was Rp258.28 trillion (Rahman, 2020).

Indonesia has raised US$2.5 billion from a three-tranche global sukuk offering to help the government fund the fight against COVID-19. Each tranche has been rated Baa2 by Moody's Investor Service, BBB by S&P Global Ratings Services and BBB by Fitch Ratings. The sukuk were offered on the Singapore stock exchange and NASDAQ Dubai in the United Arab Emirates on 23 June 2020. The 10-year maturity sukuk brought in US$1 billion, and the 5-year and 30-year maturities amounted to US$750 million each (Akhlas, 2020). This issuance of a tenor of 5- and 10-years are the lowest issuance of global sukuk by the government on the global financial market and a tenor of 30 years is the largest in Asia.

The government designates the issuance of a 5-year tenor as Green Sukuk to show global commitment, leadership, and contribution to climate change finance. This is the third issuance in the global market, apart from that of retail Green Sukuk at the end of 2019 (Antara, 2020). This transaction is in line with the government's 2020 financing plan, including dealing with the impact of COVID-19, as well as strengthening Indonesia's position in the global Islamic financial market and supporting its development in the Asian region.

This transaction received great demand from qualified and diverse global investors, which shows investors' trust in Indonesia. In 2020, the distribution of investors for a 5-year tenor was 32% Islamic investors from the Middle East and Malaysia, 5% Indonesian investors, 40% Asian investors except Indonesia, 12% US investors and 11% European investors. Meanwhile, for sukuk with a tenor of 10 years, 31% were distributed to sharia investors, 5% to Indonesian investors, 34% to Asian investors except for Indonesia, 18% to US investors, and 12% to European investors. As for Global Sukuk with a tenor of 30 years, 10% were distributed to Islamic investors, 5% to Indonesian investors, 44% to Asian investors except for Indonesia, 8% to US investors, and 33% to European investors (Antara, 2020).

This issuance of Global Sukuk received a good reaction from global and local investors. With this large orderbook, Indonesia can reduce prices up to 70 basis points from the initial offering price and below the indicative fair value. The Global Sukuk is issued by SBSN Indonesia III Issuing Company, a legal entity established solely for the purpose of issuing government sukuk (Antara, 2020).

6. Conclusion

Indonesia has a strong commitment to supporting low-carbon development, which has been mainstreamed into the Five-Year 2020–2024 National Medium-Term Development Plan. As a key to further boosting economic growth, while not sacrificing environmental sustainability and social inclusivity, low-carbon development needs a complete advancement strategy and financing system. Therefore, Indonesia became a pioneer with issuing green bonds and Green Sukuk globally.

The COVID-19 pandemic since the beginning of 2020 has had a massive impact on the global economy, including Indonesia, which is experiencing a widening deficit. However, Indonesia has turned this into an opportunity to strengthen low-carbon development. The government issued Green Sukuk in three tranches as one of the strategies to cover the deficit due to the pandemic; this global sukuk issuance received a good reaction from global and local investors.

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