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BRIEFING NOTE

The Future of Social Welfare Programs in Indonesia: From Fossil-Fuel Subsidies to Better Social Protection

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This briefing note examines the relationship between fossil-fuel subsidies and Indonesia's broader policy interventions to promote social welfare. Traditionally, Indonesia has used fossil-fuel subsidies to help alleviate poverty and to control inflation. However, over time, this policy has grown increasingly expensive. It has also been criticized for being inefficient and regressive, given that the rich enjoy a greater proportion of the benefits than the poor. This paper reviews the evidence to explore two contrary beliefs: on the one hand, that fossil-fuel subsidies cannot be reduced because this would harm the poor; and, on the other hand, that reforming fuel subsidies is in fact fundamental to the improvement of social welfare policy in Indonesia. Who is right? What are Indonesia's ambitions to improve social welfare and how do fossil-fuel subsidies fit in?

Introduction

Over the past decade, the Indonesian government has several times increased the price of fuel. At every increase, a range of compensation programs has targeted the poorer segments of the population to help them cope with the adverse effects. In the same decade, the government has introduced a number of poverty alleviation programs. While still far from perfect, the programs represent the building blocks of a comprehensive social welfare system.

The aim of this paper is to explore how Indonesia has combined attempts to reform fossil-fuel subsidies with its broader efforts to improve and deliver social welfare policies. Can energy subsidies be reduced without harming the poor? And can these subsidies play a larger role in the improvement of Indonesia's social welfare policies?

The paper is structured in three parts: first, it sets out Indonesia's ambition, strategy and targets with respect to poverty eradication; second, it discusses the linkages between fuel subsidies and social welfare reforms; and third, it summarizes what is known about the effectiveness of the current subsidy-related welfare or poverty programs that are being managed by the central government. The paper concludes with some thoughts derived from this evidence.

1.0 An Overview of Social Welfare in Indonesia

1.1 Poverty situation

Indonesia's effort to reduce poverty is an international success story. Currently, 28 million Indonesians, or 11 per cent of the population, are poor (BPS, 2013), compared to 19 per cent of the population in 2001 (see Figure 1 and Figure 2, below). Except for a brief post-crisis period in 1998-99, and following big increases in the international prices of oil and food in 2005-06, poverty in Indonesia has been in decline since the 1970s.

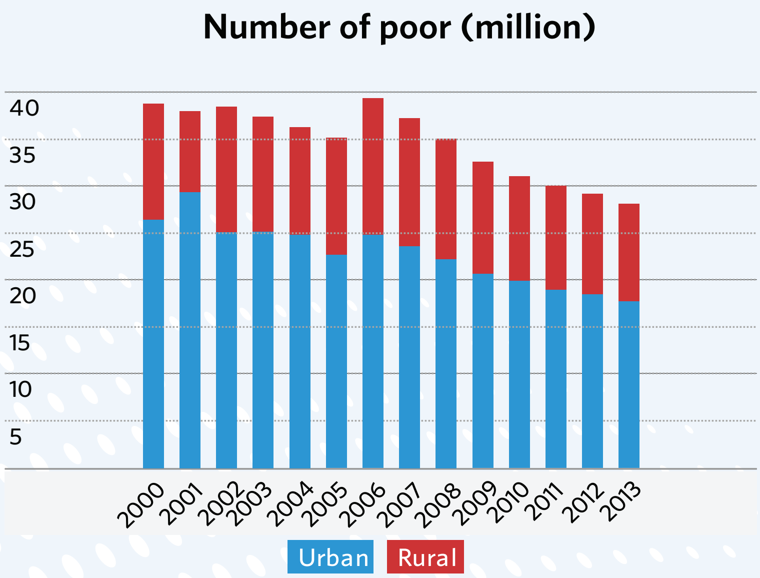

FIGURE 1. NUMBER OF PEOPLE LIVING IN POVERTY IN INDONESIA (2001-2013)

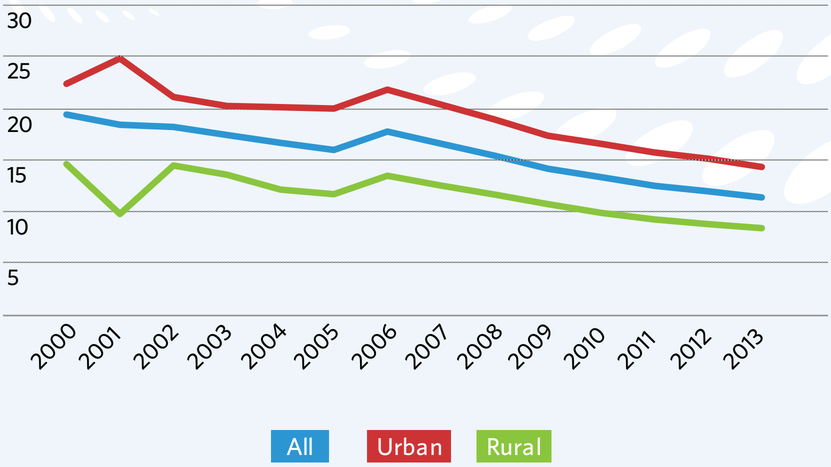

FIGURE 2. PROPORTION OF PEOPLE LIVING IN POVERTY IN INDONESIA (2001-2013)

Note: Poverty in Indonesia is calculated using the "cost of basic needs" approach. A person in poverty is defined as an individual whose expenditure is below a certain threshold ("poverty line") required to purchase a basket of food and non-food commodities considered as the minimum standard of living. Data is taken from the annual National Socio-Economic Survey (SUSENAS), collected by Indonesia's Central Board of Statistics every year.

A further breakdown of the data shows that poverty in Indonesia is higher in rural areas, both by the number of poor and the per centage of population below the poverty line. Data also suggest that poverty rates are higher in the Eastern provinces than in the Western ones. However, most of the population lives on the island of Java, so most of the poor also live in Java.

Challenges to data interpretation remain, of course. First, while the number of poor has been declining steadily, many non-poor are living close to the poverty line. Consequently, poverty numbers are very sensitive to the choice of poverty line. Table 1 illustrates this. If we raise the poverty line by 20 per cent, both the number of poor and poverty rate almost double; if we raise it further by 40 per cent then the poverty rate is almost tripled.

TABLE 1. NUMBER OF POOR AND POVERTY RATES USING DIFFERENT POVERTY LINES

ASSUMED POVERTY LINE	INDONESIAN RUPIAH	2010	
		NO. OF POOR (MILLION)	% POVERTY
Actual	211,726	31.0	13.33
1.1 X Poverty line	232,899	43.4	18.64
1.2 X Poverty line	254,071	56.7	24.38
1.4 X Poverty line	296,416	80.9	34.74
1.6 X Poverty line	338,762	101.4	43.56
1.8 X Poverty line	381,107	119.4	51.29
2.0 X Poverty line	423,452	135.0	58.00

Source: TNP2K staff calculation

Second, poverty is very dynamic. At any given year, many people can escape poverty, yet at the same time a significant number of other people fall into poverty. Table 2 shows that 53 per cent of 2008's poor escaped poverty in 2009 and became near-poor or even non-poor. But we also see that 22 per cent of 2008's near-poor and 5 per cent of 2008's non-poor fell into poverty in 2009. A strong social protection system can reduce the probability of the non-poor falling into poverty, while helping the poor to escape.

TABLE 2. DYNAMICS OF POVERTY (2008-2009)

	... WHO WERE CATEGORIZED IN 2009 AS...			TOTAL
	POOR	NEAR-POOR	NON-POOR	
Share of poor (%) in 2008 ...	46.71	20.28	33.01	100.0
Share of near-poor (%) in 2008...	22.32	21.53	56.15	100.0
Share of non-poor (%) in 2008...	5.37	7.65	86.98	100.0

Source: Suryahadi et al., 2012. The cells shaded grey show the proportion of the total population of the poor, near-poor and non-poor that has remained in the same category between 2008 and 2009. The cells shaded in green show the proportion of the poor in 2008 who had exited poverty by 2009, to become either near-poor or non-poor. The cells shaded in red show the proportion of the near-poor and non-poor in 2008 that had entered poverty in 2009.

1.2 Poverty reduction target and strategy

Indonesia's 2009-2014 medium-term development plan set a target to bring down the poverty rate to 8-10 per cent by 2014, a reduction of 2-3 per cent from the poverty rate of 11-12 per cent in 2013 (Government of Indonesia, 2009). This is much more ambitious than the poverty target set by the Millennium Development Goals (MDGs), which was to halve between 1990 and 2015 the proportion of people whose income is less than US$ 1.25 a day. In 1990, 54.3 per cent of Indonesia's population lived on less than US$ 1.25 per day, but Indonesia had in fact already more than halved this rate by the time the MDGs were formally adopted in September 2000.

The government strategy to achieve its target collected Indonesia's poverty reduction programs into three clusters, based on the major group targeted by each one (TNP2K, 2011):

1. **Cluster 1:** Programs targeting households. This cluster consists of several social assistance programs: subsidized rice (Raskin); a conditional cash transfer program (PKH or Program Keluarga Harapan); educational assistance for poor students (BSM or Bantuan Siswa Miskin); and subsidized health care (Jamkesmas).

2. **Cluster 2:** Programs targeting communities. Consists of several community-driven development programs under the umbrella of PNPM (Program Nasional Pemberdayaan Masyarakat).

3. **Cluster 3:** Programs targeting micro, small- and medium-sized enterprise (MSME). The government is offering a guarantee scheme for bank credit called Kredit Usaha Rakyat (KUR).

2.0 *How do Fossil-Fuel Subsidies Fit In?*

2.1 Overview

To date, the government of Indonesia has used energy subsidies as a core policy instrument for stabilizing prices and protecting the general welfare of the population. *Premium*-brand gasoline, *Solar*-brand diesel, kerosene, liquefied petroleum gas (LPG) and electricity for some brackets of consumers are all sold in the domestic market below their economic prices. These items are subsidized because they are perceived as 'strategic' commodities—that is to say, commodities that affect the welfare of most people. In Indonesia, both kerosene and LPG are used for daily cooking purposes. Gasoline is significant for private transport and diesel fuel is used by most transport services. Electricity is an input for many business and household activities.

To some extent, subsidized energy prices have acted as a form of social welfare policy. Low prices of gasoline and diesel fuel bring down transportation costs. In principle, this can help stabilize low prices of goods transported from rural to urban areas, or between cities. For lower- and middle-income households, subsidized fuel should also lower the cost of transport services. Similarly, low-cost energy for lighting and cooking should, in principle, reduce the cost of these activities.

However, over the years energy subsidies have become less effective and efficient. Transport costs depend not only on fuel prices, but also on road infrastructure and the quality and availability of public transport. Bad roads and inefficient public transport have increased transport costs more than subsidies have reduced them.[1] Moreover, benefits are only conferred if subsidized goods actually reach consumers. In fact, apart from Java, many areas in Indonesia report energy prices that are far above their official subsidized levels, and have also experienced recurrent fuel shortages due to companies being unable to recover the cost of supply to remote areas. And as Indonesia has grown wealthier, a larger and larger share of benefits has been captured by the growing middle- and high-income population, purchasing larger quantities of gasoline and diesel for direct use in private vehicles. At the same time, increasing global fuel prices and dwindling petroleum reserves have increased the fiscal cost of subsidies for the government. As a result, energy subsidies consume around one fifth to one quarter of government expenditure, a sum larger than expenditure on defence, education, health and social security combined (Tumiwa et al., 2012). This has more than just a financial implication. High and increasing energy subsidies mean less room for government expenditure for social welfare and infrastructure.

Energy subsidies also have unequal distributive effects. Since there is no restriction on the purchase of subsidized fuel in retail outlets, every household, both poor and rich, has an equal chance to buy subsidized fuel (Widodo et al., 2012). However, data shows that high and upper-middle classes consume more energy, and hence most of the subsidy allocation is enjoyed by these richer households (see Figure 2). This is particularly the case for gasoline and diesel subsidies: low-income households cannot afford to own vehicles or to purchase these fuels, and only benefit from the indirect impacts subsidies have on the cost of transport services and other goods.

[1] For a discussion of infrastructure and poverty, especially rural roads, see World Bank (2006).

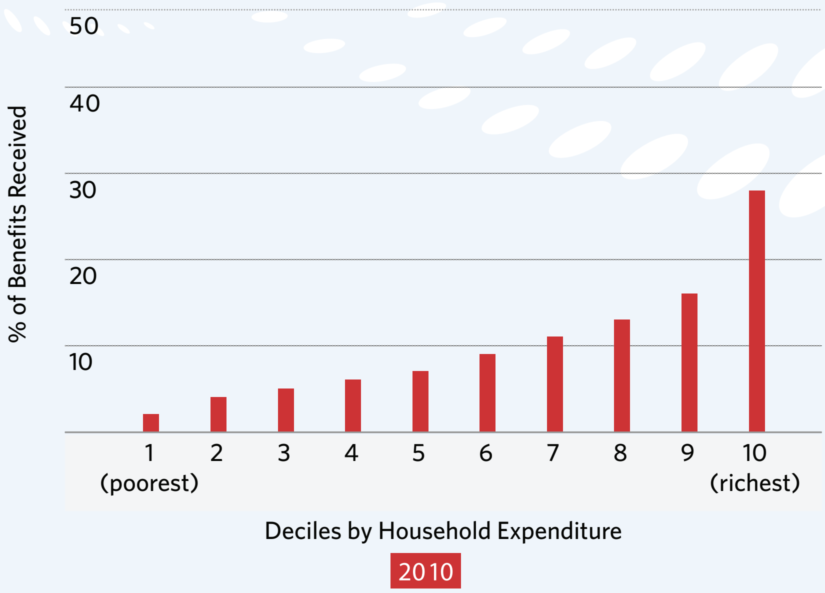

FIGURE 3. DISTRIBUTION OF BENEFITS OF FUEL PRICE SUBSIDY, BY HOUSEHOLD

Source: Agustina et al. (2012), based on Susenas (2010).

In short, energy subsidies—although having some positive effect on general welfare—do not support low-income households very efficiently and, as they become increasingly expensive, can effectively "crowd out" government spending on alternative policies.

2.2 The past: From general subsidies to targeted poverty alleviation measures

Social assistance programs targeting households are a relatively new development in Indonesia. During the New Order, the government chose to deliver universal subsidies to stabilize the prices of fuel and other commodities. Some programs involved rudimentary forms of targeting. For example, rural infrastructure programs or block grants to poor villages aimed at particular geographic areas, while policies such as credit for farmers targeted specific employment sectors. Although the extent of targeting was limited, from the early 1970s until the late 1990s Indonesia did achieve significant poverty reduction using this broad-brush approach.

Through a combination of shocks to GDP and high inflation, the Asian financial crisis in late 1997 suddenly reversed much of the poverty reduction of the previous three decades. In 1998, the number of poor in Indonesia jumped to 49 million (around 24 per cent of the population).[2] While high economic growth had succeeded in raising living standards during the "good times", the crisis showed that a significant share of the population lacked adequate social protection or other means of coping with a big economic shock.

Responding to the social impacts of the crisis, the government delivered a set of programs known as the Social Safety Net (*Jaring Pengaman Sosial*, or JPS). The JPS package consisted of a number of programs: job creation (various labour-intensive programs, block grants and small-scale revolving credit), a food security program, a subsidy for basic health services and an education assistance program designed for children of poor families.[3] According to

[2] On the impact of the financial crisis, see Booth (1999) and Feridhanusetyawan (2000).
[3] For an overview, see Daley and Fane (2002).

some studies, the JPS programs were not greatly effective in providing protection against the shock. These indicate that the improvement in living standards, including the declining poverty rate after the crisis, was more due to the government's macro-level economic stabilisation measures, especially the management of rice prices (see World Bank, 2006). Nevertheless, the JPS represented a new model of social programs in Indonesia, directly targeting the poor. In the years following the crisis, the government has developed and introduced a number of ongoing targeted welfare programs. Until recently, these programs were scattered, not comprehensive and used different targeting databases to identify recipients. But gradually the government has strengthened and improved the programs, and built a better database for targeting.[4]

2.3 The present: A decade of price rises combined with social protection measures

The government of Indonesia has cut fuel subsidies several times since 1998. In 2001, President Abdurrahman Wahid increased fuel prices by 30 per cent. Then in 2005, President Yudhoyono increased fuel prices by almost 100 per cent. He again increased fuel prices in 2008 by about 30 per cent, although in 2009 the price was returned to the end-2005 level in a move seen by many as a bid for reelection. Then in 2013, after a year of delay from the initial plan, street protests and heavy political wrangling in parliament, fuel prices were increased to slightly above the 2008 prices. In each instance, social protection measures were either introduced or expanded at the moment that fuel subsidies were reduced, to help households cope with the impact on their welfare.

As of 2014, fuel prices are still administered by the government. Any price changes must be implemented via a presidential or government decree. There have been talks about a change in subsidy mechanism, whereby the government would set a certain subsidy amount per unit of energy sold (e.g. IDR 2,000 per liter) instead of simply fixing prices. This would keep some measure of price support, but allow prices to fluctuate in response to international markets and keep costs under control. But so far such discussion has not been followed by a political decision.

Nevertheless, Indonesia needs to reduce its dependency on fossil fuels and to set domestic energy prices closer to the economic price. At the same time, reducing fuel subsidies provides a fiscal space for the government to invest in social welfare programs. This raises sequencing challenges, however. Before the government can move further in eliminating fuel subsidies, it has to build a strong social welfare system to provide its population with better ways to cope with the resulting economic shocks. As of 2014, the government has introduced a number of social welfare programs that together can be seen as building blocks for a comprehensive welfare system.

2.4 The future: Policy reform going forward

Indonesia's experiences show strong two-way linkage between energy subsidies and social welfare policy reforms.

To start with, energy subsidy reform—reducing subsidies and increasing domestic prices—has created the need to deliver compensation programs. The government is under pressure to show that price rises will not unfairly hurt the poor. In practice, the resulting welfare programs have created real change: the government has used fuel subsidy cuts and the associated mitigation policies as instruments to reduce inequality, ensuring a more progressive distribution of benefits concentrated on the poor.

[4] For a more detailed discussion on past social assistance programs, see Perdana and Maxwell (2012)

The Indonesian government's use of cash transfer programs in 2005, 2008 and 2013 will not be the end of the story. The weaknesses and shortcomings of cash transfers in managing energy subsidy reform have stimulated a search for better social welfare programs. One might argue that social welfare programs should be an independent and sustainable effort, and should not depend on subsidy reform. In reality, however, it was the shock of energy subsidy reductions that can be seen as having provided the impetus for social welfare reforms.

This can also work the other way around: a successful social welfare system can strongly justify further energy subsidy reform. In Indonesia, political opinion on government social welfare programs is still mixed. Nevertheless, when the government again introduced a fuel subsidy cut in 2013, negative reactions were more muted than in 2005 and 2008. The subsequent cash transfer program was also met with a relatively calm response, compared to the often angry criticism of previous years. The government had learned from the experience of previous cash transfer programs, and were more prepared in 2013. At the time of writing, the critics have not been silenced yet, but government confidence in implementing this kind of dual energy-and-welfare policy reform has grown.

3.0 *Social Assistance Programs Used to Compensate for Fuel Subsidy Removal*

As described in Section 2, the central government runs a number of poverty reduction programs grouped into three clusters. In addition to these programs, there are other programs managed by local governments, as well as smaller programs run by the central government, which are not part of official poverty reduction programs but nonetheless may have some bearing on poverty reduction efforts.

This section briefly summarizes the four social assistance programs that are part of the Cluster 1 programs targeting households[5] and have been used in the past decade to help cushion the impact of fuel subsidy reforms. These are 'regular' programs, meaning they are delivered on an ongoing, permanent basis. In 2005, 2008 and 2013, the government combined these ongoing support programs with temporary and unconditional direct cash transfer programs.

3.1 Raskin – Subsidized Rice Program

Raskin (*Beras Miskin* or "rice for the poor") is a social assistance scheme that was part of the initial 1998 social safety net programs. In 1998 it was called 'Beras OPK' ("market operation for rice"). The basic idea of Beras OPK was to supply the market with subsidized rice at several distribution points throughout the country, so low-income households would still able to purchase rice. Later, when the economy recovered, the government continued the program and changed the name to Raskin.

Today, Raskin targets some 15 million households (the poorest 25 per cent of the population), although at one point it was allocated to around 20 million households. Bulog (the central government's logistic agency) delivers subsidized rice to 'distribution points' (usually at the village level) each month. Eligible villagers—usually identified by a coupon or a letter signed by the village head stating that they are poor households—then line up once a month to purchase up to 15 kilograms of rice each at 20-30 per cent of the market price.[6]

[5] See also World Bank (2012) for a detailed discussion of these programs.

[6] According to the current program design, Raskin is to be delivered monthly. However, in practice, many villages receive Raskin once every two to three months, sometimes even less often, due to logistical constraints. In 2013, as part of the compensation offered for the fuel price increase that year, Raskin was to be distributed 15 times a year through 2014.

As with energy subsidies, food subsidy programs like Raskin rarely perform as intended. Many studies have documented the problems and weaknesses of the program. Although it targets poor households, in practice non-poor households are also able to purchase the subsidized rice. In many cases, village heads have not allowed beneficiaries to purchase their full 15 kilogram allotment, giving the remaining rice to other villagers whom they consider just as poor. Sometimes, poor households themselves have voluntarily given up their rice entitlement because they do not have money to purchase the whole 15 kilograms. Other problems include delayed rice distribution. In many regions, especially remote ones, Raskin is sometimes delivered only once every three to six months. Villagers often also have to pay more than the stated price, due to additional transport and packaging costs, or in some cases corruption and fraud by village officials.[7]

3.2 Jamkesmas – Health Insurance

Like Raskin, Jamkesmas (*Jaminan Kesehatan Masyarakat*, the public health insurance system) originated in the 1998 social safety net era. In 1998, the central government waived the fees for outpatient and inpatient care at the Community Health Clinics (Puskesmas) or Class III services at public hospitals for poor households holding a letter of certification from their village heads. The scheme was called JPK Gakin ("health care for poor households"). After the crisis, the government continued to provide such services under different names and management. For example, between 2004 and 2007 the program was called Askeskin (*Asuransi Kesehatan Untuk Masyarakat Miskin*, health insurance for the poor) and run by the government-owned insurance company PT Askes. Since 2008, the Ministry of Health—the central government agency responsible to the program—terminated the agreement with PT Askes and has run Jamkesmas under a program funded by the state.

Today, Jamkesmas targets 76.4 million Indonesians, about 30 per cent of the population. In reality the number of Jamkesmas cardholders should be less than this, since many cards have not reached their intended owners due to difficulties in the distribution process. As with its previous incarnations, Jamkesmas provides beneficiaries with free health care services at Puskesmas and Class III public hospital services. The scheme covers practically all health care services (including, for example, heart by-pass surgery). As a scheme to mitigate the impacts of fuel subsidy reform, Jamkesmas does not help households cope with a higher cost of living in the short-term, but it does have the potential to significantly improve their wellbeing in the medium- to long-term. However, the utilization rate is still very low because of supply-side constraints. In many regions, especially rural and remote areas, health facilities are simply not available or inadequate for the performance of many health services.

3.3 BSM – Assistance for Poor Students

BSM (*Bantuan Siswa Miskin*, literally "assistance for poor students") is a cash assistance program for students from poor households who are enrolled in elementary school, junior secondary school and high school. The program was introduced in 2008. It provides a cash transfer of from IDR 360,000 (US$ 36) to IDR 1,000,000 (US$ 100) per student per year, depending on the school level. The amount is intended to cover school-related expenses other than tuition expenses, mainly the cost of transport.

In 2008, the BSM provided assistance to some 3 million students at all levels of elementary and secondary education. By early 2013, the program was already targeting 8 million students. In the second half of 2013, following an increase in fuel prices, the BSM was expanded even further to target all students from households in the bottom 25 per centile, a number equivalent to 15.4 million students (Rahayu, 2013).

[7] Hastuti and Maxwell (2003), Suryahadi and Sumarto (2010).

Initially, BSM assistance reached students via their schools, and not all beneficiaries received cash. Some schools decided to replace BSM assistance with books or uniforms. Other schools converted BSM cash into student saving accounts, managed by the school. Subsequently, the BSM was changed to a system that distributed payments via post offices. This was done to ensure that most students received cash payments, although many schools were reported to still be insisting on providing their students with BSM assistance in kind.

As a social-assistance measure to help households cope with the withdrawal of fuel subsidies, BSM provides support in several ways: as an income supplement for households that have education-related expenditure, as a way of easing the short-term shock of an increase in the cost of energy, and by promoting greater school attendance. In this latter case, BSM also constitutes a long-term intergenerational investment in breaking the cycle of poverty. At the same time, however, BSM assistance only benefits households with children of school age, and thus does not extend to all households affected by energy price increases.

3.4 PKH – the conditional cash transfer

The growing popularity of conditional cash transfer (CCT) programs in Latin America in the 1990s and early 2000s set a new trend of CCT adoption in many countries, including Indonesia. In 2007, the government launched Program Keluarga Harapan (PKH, or The Family of Hope Program) in seven provinces, covering 350,000 families. PKH was designed using Mexico's Opportunidades and Brazil's Bolsa Familia as its model.

PKH targets households at the bottom 7-10 per cent (considered as 'very poor') comprising at least one of the following: a pregnant mother; children under the age of 6; elementary school children (aged 7-12); or junior secondary school children (aged 12-15). PKH households need to ensure that pregnant mothers visit a health care center at least four times during their pregnancy; that children under 6 visit a health clinic to measure their weight and height as well as receive vitamins and scheduled immunization; and that school-aged children are enrolled in schools and maintain a minimum 85 per cent attendance each month.

By 2013, PKH was already operating in 70 per cent of all districts. The program covers 2.4 million households, and will expand to cover 3.2 million households in 2014. Households will receive up to IDR 2,800,000 per year (US$ 280), depending on how many family members are enrolled in the PKH, and if they fully comply with all conditions for eligibility. On average, PKH households in 2013 received IDR 1,400,000 (US$ 140) per year (Nazara and Rahayu, 2013).

Disparity in supply-side availability is the biggest challenge for PKH expansion. In remote areas, mainly in the Eastern part of the country, poor households may live in an area without adequate access to transport and where the closest health facility is more than 50 km away. Children may have to walk up to two hours to school every day—and are lucky to have teachers in the school. In such situations, the enforcement of PKH eligibility criteria amounts to punishment for the poor.

Maintaining PKH as a conditional cash transfer is another challenge. Even in the current PKH areas, enforcing conditionality is not easy. Data from the program's information system shows that 80-90 per cent of PKH beneficiaries meet the conditions. However, reports from different field visits suggest that in many cases the program cannot verify whether PKH members did in fact regularly visit their health clinic or maintain the minimum school attendance rate. Thus, a significant number of PKH beneficiaries are only 'assumed' to meet their conditionality.

3.5 Discussion on the effectiveness of the current program

Indonesia's four social assistance programs that target households (the 'Cluster 1' group comprising Raskin, Jamkesmas, BSM and PKH) plus the incidental, non-permanent unconditional cash transfer scheme known as BLSM (see below) have laid a good foundation for a comprehensive social welfare regime in the future. The maintenance of these social assistance programs, as well as programs in the other 'clusters', means that if the government continues reducing the fuel subsidy, budget can be reallocated to improve the current programs.

Nevertheless, there are some areas where the current programs need improvement.

1. *Targeting*. Prior to 2011, different programs used different methods and mechanisms to target beneficiaries. For example, village heads were responsible for selecting the beneficiaries of the Raskin rice-distribution plan, and school headmasters had the authority to select students who would receive BSM. As a result, definitions of the beneficiaries of social assistance programs have varied. Since 2012, the central government has required that Indonesia's main social assistance programs use a system known as the "Unified Database" for targeting. The database consists of 96 million individuals in the least-advantaged 40 per cent of population. The data was collected in 2011, and at the time of writing the government was preparing another wave of data collection and updating in 2014. All four of the previously-described social assistance programs, plus the unconditional cash transfer scheme introduced in 2013 (the Bantuan Langsung Sementara Masyarakat (BLSM), or "temporary direct cash assistance"), have used the Unified Database. The hope is that this improved targeting system will make social assistance programs more effective in helping households cope with increases in the cost of living.

2. *Complementarity of programs*. In theory, since all programs target the same 40 per cent segment of Indonesia's population, most households—especially those at the lower end of income distribution—should receive multiple programs. In practice, however, the four main social assistance programs are managed and operated by different ministries. Each ministry has different budget and reporting lines. As the result, they do not always deliver their programs to the same households. Hence, instead of a synergy between programs, different programs run independently of each other, reducing the effectiveness of poverty reduction. For example, students who receive PKH should theoretically also be receiving BSM. But there is no formal mechanism to ensure that this happens on the ground. In fact, schools often decide not to give BSM to students who received PKH because they consider the PKH students as already benefitting sufficiently from one government program and want to allocate the BSM to other, non PKH beneficiaries. However, since PKH students come from the poorest households (the bottom 5-7 per cent of income distribution), the government's original intention was actually to provide them with multiple social assistance programs, as complementary programs would have a greater cumulative effect for households at the very bottom of income distribution.

3. *Building extended programs*. The four programs at the time of writing dealt with specific issues: food (Raskin), health (Jamkesmas), education (BSM), and human capital investment (PKH). However, to build a solid social welfare system, the country also needs programs that target the elderly, the disabled, out-of-school children, the unemployed, the malnourished, and so forth. If Indonesia intends to liberalize markets for volatile basic commodities like energy, it must also develop programs that respond to international price volatility. In Brazil, the government first used Bolsa Familia as the core social assistance program, and then gradually expanded the program to include other activities. Indonesia could follow this path.

4.0 Conclusion and lessons learned

Indonesia needs to continue reforming its energy policy while still in the midst of improving and expanding its welfare policies. Energy subsidies have consumed a significant portion of the national government's budget. Fuel price increases have created some room for the government to spend on other things, from infrastructure to social welfare programs. But the yawning gap between economic and domestic fuel prices continues to distort the signal of scarcity and lead to overconsumption. And, as a non-targeted instrument, energy subsidies continue to benefit the poor less than the rich, who consume more fuel.

Since 2000, the government has several times has attempted reform by increasing domestic fuel prices; the last increase at the time of writing took place in June 2013. So far, the reforms have been more ad hoc than programmatic, triggered essentially by increases in international oil and gas prices. The government has yet to deliver a comprehensive plan on energy reform. Nevertheless, some small measures have been taken, such as conversion from kerosene to LPG as the main cooking fuel for the poorest group. The government may also introduce a subsidy cap or fixed subsidy plan. This would mean that the domestic price, while still below the international price, could fluctuate but the maximum amount of subsidy allocated in the national budget would be set at a definite maximum level.

The government has also introduced a number of social welfare programs. Following the 2005, 2008 and 2013 fuel subsidy reductions, the government delivered temporary cash transfer programs targeting low-income households, to relieve the burden due to higher prices. Apart from that, the government has also introduced a number of more permanent social assistance programs, which together could be strengthened and improved further into a more comprehensive social welfare system. Indonesia's experience so far demonstrates the striking complementarity of fuel subsidy and social welfare reforms. One side of the reforms can provide strong justification for the other.

There is still much work to do. The government needs to set out a comprehensive plan for energy sector reform aiming to reduce dependency on fossil fuels. Subsidy cuts should be just one part of the larger energy sector reforms, the purpose of which should be to narrow the gap between domestic and international fuel prices, and to make prices more efficiently reflect scarcity. The extra budget derived from fuel subsidy cuts could be reallocated to three broad areas: infrastructure development, public transport facilities and further improvement of social welfare programs. The main social welfare programs in need of greater government funding concern health, nutrition and education. But despite the challenges it faces, Indonesia's government does not need to "reinvent the wheel". It has already developed many instruments that can serve as the building blocks of a more effective and efficient future welfare system.

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