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MIDDLE-INCOME TRAP: INDONESIA'S STRATEGY AND LESSONS LEARNED FROM THE SUCCESS OF OTHER COUNTRIES

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Abstract

The middle-income trap is when a country has reached a middle-income level but struggles to transition to high-income status. Countries in this situation often face economic stagnation, low productivity, and difficulties competing globally despite having experienced rapid growth. This paper examines the strategies necessary to overcome this condition and how Indonesia can learn from countries that have successfully escaped the middle-income trap. Key strategies include developing the MSME sector, improving human resource quality, maintaining macroeconomic stability, promoting innovation and technology, and fostering collaboration between the government, the private sector, and the community. The DPR RI, particularly Commission X of DPR RI and the Budget Committee of DPR RI, need to oversee the implementation of government programs to improve human resource quality. Indonesia's success in escaping the middle-income trap relies heavily on collaboration between the executive and legislative branches and their shared commitment to achieving long-term development goals.

Introduction

The middle-income trap is a situation in which middle-income countries cannot compete in producing low-labor-intensive goods due to relatively high wages while also lacking the productivity needed to compete in high-value-added activities. This leads to prolonged economic stagnation and difficulty achieving high-income status (Yusuf, 2023).

Indonesia, a middle-income country since 1985, now faces significant challenges in avoiding this trap. Economic growth in Indonesia has stagnated at around 3.5 percent per year, well below the growth target needed to achieve developed country status, around 5.42 percent per year (Ayu, 2018).

The World Bank has stated that developing countries like Indonesia need to achieve near-miraculous re-

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sults to avoid getting trapped in the middle-income category. A mature strategy is essential for these countries to transition into developed or prosperous nations. According to Mohammad Faisal, Executive Director of the Center of Reform on Economics (CoRE), Indonesia requires an extraordinary breakthrough to achieve consistent economic growth above six percent. Such growth is necessary for Indonesia to remain a middle-income country, making progress difficult (Hasan, 2022).

Countries caught in the middle-income trap face prolonged economic stagnation, which can stymie long-term growth and exacerbate social inequality. This stagnation occurs when a country cannot transition from middle-income to high-income status, resulting in a loss of global competitiveness. This, in turn, can lead to reduced foreign investment and hinder the potential for innovation and domestic industrial development. Prolonged stagnation can also increase unemployment and poverty as the creation of new high-quality jobs becomes more difficult, thereby worsening social and economic conditions.

Based on this, the paper examines the strategies the government needs to implement to overcome the middle-income trap and explores how Indonesia can learn from countries that have successfully escaped it.

Strategy to Escape the Middle-Income Trap

During the ten years of Jokowi's administration, Indonesia's economic growth rate has been stagnant at five percent per year. Not only has it stagnated, but growth has also relied heavily on natural resources. In the industrial sector, the government has prioritized the development of mineral smelting, which is also resource-based. This focus has come at the expense of improving the investment climate in stronger processing or manufacturing industries, which should be able to spur job creation and boost productivity (Hidayat, 2024).

Due to job cuts in various sectors, the middle class has decreased from 21 percent to 17 percent in the last five years. The opening of imports for labor-intensive industrial commodities has made it difficult for domestic products to compete with cheaper goods from abroad. Meanwhile, the increase in investment value has primarily benefited entrepreneurs, as it has been concentrated in capital-intensive upstream industries, especially the mining sector. The downstreaming of mineral resources has yet to be accompanied by the development of derivative industries that could generate greater added value (Tempo, 2024).

The Indonesian government needs to implement an integrated strategy to escape the middle-income trap. First, developing the Micro, Small, and Medium Enterprises (MSMEs) sector is essential. Currently, MSMEs contribute around 61 percent to the gross domestic product (GDP) and absorb 97 percent of the workforce in Indonesia (Nurprabowo, 2023). To maximize this potential, the government needs to improve access to financing, provide skills training, and support digital marketing for MSMEs. These efforts are expected to help MSMEs grow, participate in the global supply chain, and ultimately increase incomes and drive economic growth.

Second, improving the quality of human resources (HR) needs to be a top priority. Indonesia has been experiencing a demographic bonus since 2015, with its peak period estimated to occur between 2020 and 2035. Comprehensive education reform is crucial to preparing a skilled and innovative workforce. The government needs to ensure that the education curriculum aligns with industry needs and encourages relevant vocational training programs. By enhancing HR quality, Indonesia can boost productivity and competitiveness in the global market.

Third, maintaining macroeconomic stability through prudent fiscal management is vital. A high budget deficit can hinder investment in infrastructure and social programs essential for economic growth. The government needs to keep inflation below three percent and the current account deficit below three percent. This policy will create a more favorable investment climate and stimulate faster growth.

Fourth, the government needs to encourage innovation and technology as part of its economic diversification strategy. Investment in research and development needs to be increased to create innovative products that can compete internationally. By embracing high technology, sectors such as manufacturing and digitalization can grow rapidly, reducing dependence on natural resources. This is key to ensuring sustainable long-term economic growth.

Fifth, collaboration between the government, private sector, and civil society is crucial for escaping the middle-income trap. Mapping economic drivers will help the government formulate more effective policies.

The Prabowo Subianto administration needs to implement this strategy. By consistently applying these measures, Indonesia stands a strong chance of escaping the middle-income trap and achieving high-income status by 2035–2040.

Other Countries' Success in Escaping the Middle-Income Trap

The success of a country in escaping the middle-income trap provides important lessons for Indonesia in formulating its development strategy. One successful example is South Korea, which has transformed from a low-income country into one of the most advanced economies in the world over the past few decades. Key to South Korea's success has been its substantial investment in education and technology and its industrial policies promoting innovation. Through initiatives like the five-year economic development plans, South Korea has been able to drive the growth of its manufacturing sector and enhance its global competitiveness, achieving an average economic growth rate of around seven percent per year.

Another successful case is Taiwan, which demonstrated that economic diversification and human resource development are effective strategies. Taiwan has emphasized technical and vocational education and encouraged research and development in the high-tech sector. By building technology-driven industries, Taiwan has increased the added value of its products and created high-quality jobs. As a result, Taiwan's per capita income significantly increased, reaching around USD34,000 in 2023, marking its successful transition to high-income status (Primadhyta, 2024).

A relevant example is Singapore, which escaped the middle-income trap through a pro-business policy approach and strong infrastructure investment. Singapore adopted open policies toward foreign investment and created a favorable business climate through efficient regulation. Additionally, the Singaporean government actively invested in education and training to ensure its workforce possessed the necessary skills to compete in the global market.

The success of these three countries highlights that a combination of human resource investment, innovation, and supportive economic policies is essential for emerging from the middle-income trap. Indonesia can learn from these experiences by focusing on improving the quality of education, fostering an innovation ecosystem, and creating a better investment environment.

Conclusion

In facing the challenges of the middle-income trap, Indonesia needs to learn from countries that have successfully escaped this condition by implementing appropriate and sustainable strategies. The success of countries such as South Korea, Taiwan, and Singapore shows that investment in education, innovation, and infrastructure is key to increasing productivity and competitiveness. In addition, comprehensive structural reforms, including simplifying regulations and strengthening institutions, can create an environment conducive to inclusive economic growth. Indonesia can achieve high-income country status by harnessing the potential of quality human resources and encouraging collaboration between the government, private sector, and civil society.

Through its oversight function, the DPR RI, especially Commission X, oversees implementing government programs to improve the quality of human resources. Quality education is one of the main pillars of overcoming the middle-income trap. Improving the quality of education is directly related to economic growth, making the role of DPR RI crucial in creating a skilled workforce ready to compete in the global market. The Budget Committee of DPR RI also needs to play an active role in promoting transparency and accountability in managing the state budget. By ensuring that the budget is allocated to programs that truly support economic growth, the DPR RI can help create an environment conducive to investment and innovation. Indonesia's success in escaping the middle-income trap relies heavily on collaboration between the executive and legislative branches and a shared commitment to achieving long-term development goals.

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