

Working Paper

Vol. 1, 2026



Embedding a Green Paradigm in Indonesia's **Economic Framework and Fiscal Policy for 2027**

Authors:

Hadi Prayitno
Achmad Taufik
Triono Hadi



Embedding a Green Paradigm in Indonesia's Economic Framework and Fiscal Policy for 2027

Authors:

Hadi Prayitno; Executive Director of The Reform Initiatives

Achmad Taufik; Deputy Director of The Reform Initiatives

Triono Hadi; Program Director of The Reform Initiatives

Abstract

The Indonesian government has positioned the 2027 Macroeconomic Framework and Fiscal Policy Principles (KEM-PPKF) as the foundation for preparing the 2027 State Budget (APBN). The document is more than a technocratic instrument; it also reflects the political direction of national economic development. Under the theme “Grow Higher, Prosper Faster,” the government targets economic growth of 5.8–6.5 percent, a deficit of 1.80–2.40 percent of gross domestic product, and state expenditure of 13.62–14.80 percent of gross domestic product. It also identifies food, energy, downstream processing, industrialization, education, health, infrastructure, housing, disaster resilience, the village economy, and poverty reduction as major national priorities.

This working paper examines the 2027 KEM-PPKF through the lenses of the green economy, fiscal governance, ecological justice, and constitutional obligations. The analysis finds that the 2027 KEM-PPKF sets a course for fiscal consolidation, clarifies welfare objectives, and strengthens coordination among the APBN, monetary policy, the financial sector, and Danantara. Yet it has not established the green paradigm as a fundamental principle for shaping economic growth, state revenue, expenditure, financing, and central–regional fiscal relations. The government therefore remains exposed to the risks of extractive growth, fiscal illusion, the concentration of economic power through strategic investment financing, and weak public participation in the budget process.

This paper proposes a green economic and fiscal policy framework to redirect fiscal policy in 2027. It integrates economic growth, environmental protection, the energy transition, forest and land restoration, ecological financing, climate-responsive budgeting, gender-responsive budgeting, and stronger rights for Indigenous Peoples and local communities. The President, the Minister of Finance, the House of Representatives (DPR RI), and regional governments should make the 2027 APBN an instrument of low-carbon economic transformation, rather than merely a vehicle for expanding expenditure and accelerating investment.



Keywords: 2027 KEM-PPKF; green state budget; ecological financing; fiscal policy; green economy; Danantara; downstream processing; constitution.

1. Reading the Direction of the 2027 KEM-PPKF

The government has prepared the 2027 KEM-PPKF as the initial document for drafting the 2027 APBN. It fulfills the mandate of Law No. 17 of 2003 on State Finance and provides the basis for preliminary discussions between the government and the DPR. The government uses the 2027 KEM-PPKF to guide economic and fiscal policy amid global uncertainty and to address development needs over the short, medium, and long term.

The theme “Grow Higher, Prosper Faster” reflects the government’s considerable ambition. It seeks to accelerate economic growth while improving people’s welfare. This direction is translated into eight clusters of National Priority Work Programs and one supporting cluster. The eight main clusters cover food sovereignty; energy and water self-sufficiency; education; health; downstream processing and industrialization; infrastructure; housing and disaster resilience; the people’s and village economies; and poverty reduction. The supporting cluster covers defense, security, law enforcement, governance, digitalization, and economic diplomacy.

The government positions the APBN as a catalyst for development. It is expected to mobilize private-sector investment, counter economic cycles, strengthen social protection, finance public needs, and maintain fiscal discipline. Monetary policy is positioned as an anchor of stability, the financial sector as a channel for financing, and Danantara as a vehicle for accelerating productive and strategic investment. Taken together, this approach reflects an intention to strengthen policy coordination.

The 2027 KEM-PPKF sets state revenue at 11.82–12.40 percent of gross domestic product, state expenditure at 13.62–14.80 percent of gross domestic product, and the deficit at 1.80–2.40 percent of gross domestic product. The government also sets targets for economic growth of 5.8–6.5 percent, inflation of 1.5–3.5 percent, poverty of 6.0–6.5 percent, open unemployment of 4.30–4.87 percent, a Gini ratio of 0.362–0.367, a human capital index of 0.575, a farmers’ welfare index of 0.8038, and a formal job creation share of 40.81 percent.

The Reform Initiatives considers the 2027 KEM-PPKF a document with a strong policy direction that nevertheless remains exposed to

familiar risks. The government has narrowed the projected deficit range and sharpened its welfare targets. Yet it has not adequately explained the institutional arrangements needed to ensure transparency, participation, oversight, performance audits, and accountability in strategic investment financing. Nor has it placed the DPR, the Audit Board (BPK), regional governments, civil society, the media, and citizens at the center of fiscal policy design.

This working paper views the 2027 KEM-PPKF as both an opportunity and a warning. The government can use the 2027 APBN as an entry point for green economic transformation. It could also repeat an established pattern of pursuing high growth through large projects, extractive expansion, and centralized financing that carries fiscal risks. These choices will determine whether the 2027 APBN strengthens public prosperity or increases the ecological and fiscal burdens borne by future generations.

2. Weighing the Risks Behind Fiscal Optimism for 2027

The 2027 KEM-PPKF presents an optimistic growth outlook. The government targets economic growth of 5.8–6.5 percent, above Indonesia’s recent trend of around five percent. It relies on productivity, investment, downstream processing, the financial sector, food, energy, and Danantara to accelerate growth. This narrative reflects a developmental-state orientation in which the state seeks to direct fiscal, financial, and investment resources toward priority sectors.

Evans (1995) explains that a developmental state requires a capable and autonomous bureaucracy embedded in productive networks. Mazzucato (2013) likewise argues that the state can play an entrepreneurial role through strategic investment and the creation of new markets. The 2027 KEM-PPKF bears traces of these ideas, particularly in its treatment of the APBN, monetary policy, the financial sector, and Danantara as instruments of coordination. Developmental-state theory also offers an important warning: a strong state without adequate accountability can become a rent-seeking or patrimonial state that concentrates economic benefits among particular groups.

The first risk stems from the highly ambitious growth target. The government has not adequately explained whether growth of 5.8–6.5

percent will come from sustainable green sectors or from sectors based on natural resource extraction. The target could encourage greater investment in minerals, coal, large-scale plantations, extractive infrastructure, and energy-intensive industries. Indonesia needs industrial transformation, but that transformation must break the longstanding link between economic growth, deforestation, land degradation, and carbon emissions.

Kuznets (1955) showed that changes in economic structure can affect inequality. Experience across many developing countries, however, demonstrates that economic growth does not automatically reduce inequality or ecological damage. Stiglitz, Sen, and Fitoussi (2009) caution that gross domestic product alone is insufficient as a measure of welfare because it overlooks distribution, quality of life, and sustainability. The 2027 KEM-PPKF does include targets for poverty, unemployment, the Gini ratio, human capital, and farmers' welfare, but the government has not made ecological indicators core macro-fiscal targets.

The government should use reductions in emissions and deforestation, restoration of degraded land, improvements in air and water quality, and reduced disaster risk as measures of fiscal performance. Without such indicators, the 2027 APBN may generate apparently strong growth while concealing substantial ecological costs. Those costs will eventually surface through floods, droughts, forest fires, crop failures, water crises, environmentally related illnesses, land conflicts, and lost livelihoods.

The second risk concerns Danantara. The government sees it as a means of accelerating productive and strategic investment. This could strengthen development financing, particularly when the APBN has limited fiscal space. Yet Danantara could also become a new center of concentrated economic power unless the government establishes strict rules governing transparency, audits, parliamentary oversight, and the disclosure of fiscal risks. TRI has warned that innovative financing can create hidden liabilities if the government does not disclose all fiscal risks to the public.

Musgrave (1959) identifies three principal functions of fiscal policy: allocation, distribution, and stabilization. Danantara could improve allocation if it finances productive sectors that deliver public benefits. It could weaken

distribution, however, if strategic investments merely concentrate capital, transfer risks to the state, and channel benefits to large economic groups. It could also undermine fiscal stabilization if contingent liabilities and state guarantees grow without rigorous oversight. The government should therefore include Danantara in the public sector's fiscal risk balance sheet rather than treat it as financing beyond fiscal scrutiny.

The third risk arises from downstream processing. The government has designated downstream processing and industrialization as a priority cluster. Downstream processing can increase domestic value added, extend supply chains, and reduce exports of raw materials. It is not necessarily synonymous with industrialization, however. If industry fails to develop technology, research, innovation, labor productivity, and domestic linkages, downstream processing may simply relocate the initial stage of processing onshore.

Hirschman (1958) argues that industrial development requires both backward and forward linkages. Mineral downstream processing may fail to constitute genuine industrialization if smelters merely process raw materials using fossil energy, depend on imported technology, create few high-quality jobs, and cause extensive environmental harm. The government must ensure that downstream processing generates technology, decent jobs, lower emissions, and strong domestic industrial linkages.

The 2027 KEM-PPKF should also examine the relationship between downstream processing, employment, and the quality of growth. The government targets open unemployment of 4.30–4.87 percent and a formal job creation share of 40.81 percent. These targets matter, but the government should explain which sectors are expected to generate formal employment. The green economy can create jobs through renewable energy, energy efficiency, forest and land rehabilitation, peatland restoration, mangrove rehabilitation, regenerative agriculture, waste management, the circular economy, public transport, and ecosystem services. The ILO (2018) emphasizes that a green economic transition can generate new jobs when the state provides skills development, social protection, and fair labor market policies.

The fourth risk comes from major spending programs. The Free Nutritious Meals program, for example, has a legitimate social purpose:

improving children's nutrition, developing human capital, and supporting vulnerable families. Yet large-scale programs can create fiscal illusion if the government obscures long-term costs, crowds out other priorities, or fails to demonstrate benefits through rigorous evaluation. Buchanan (1967) explains that fiscal illusion occurs when citizens underestimate the costs of policies because revenue and expenditure arrangements make fiscal burdens less visible. TRI has likewise warned that costly populist programs can burden future generations through greater debt and higher taxes.

The fifth risk lies in central–regional fiscal relations. The 2027 KEM-PPKF devotes a chapter to harmonizing central and regional fiscal policies. The government states that such harmonization should improve basic services, narrow regional disparities, and align regional planning and budgeting with the national agenda. This direction matters, but harmonization must not become a form of centralization. Regional governments need sufficient fiscal space to finance environmental protection, basic services, and the ecological needs of their territories. Regions that provide ecosystem services, upstream regions, Indigenous territories, and disaster-prone regions must not be treated merely as recipients of central government programs.

The 2027 KEM-PPKF should also recognize inequality as an ecological issue. The Gini ratio measures the distribution of income or consumption; it does not capture how the risks of floods, droughts, forest fires, air pollution, loss of access to land, and lost livelihoods are distributed. Martinez-Alier (2002) shows that environmental conflicts often arise because vulnerable groups bear the ecological costs of economic projects whose benefits accrue to others. Fiscal policy in 2027 should therefore make geographical and ecological justice part of the inequality-reduction agenda.

Budget governance also requires serious attention. The Open Budget Survey 2025 shows improvements in Indonesia's scores for transparency, public participation, and oversight. According to the International Budget Partnership, Indonesia scored 71/100 for transparency, 33/100 for public participation, and 74/100 for oversight. These gains matter, but the participation score remains far from adequate. Budget transparency without public participation produces accessible documents, not social accountability. Citizens, civil

society, academics, women's groups, Indigenous Peoples, farmers, fishers, informal workers, persons with disabilities, and communities affected by projects need meaningful opportunities to engage throughout the budget cycle, from the preparation of the KEM-PPKF, Financial Note, Draft State Budget (RAPBN), and State Budget Bill through budget implementation, audits, and the evaluation of outcomes.

The 2027 KEM-PPKF also requires an ecological constitutional test. Article 23(1) of the 1945 Constitution states that the APBN must be implemented openly and responsibly for the greatest prosperity of the people. Article 33 likewise obliges the state to use the earth, water, and natural resources for the people's prosperity. Such prosperity cannot be separated from ecological carrying capacity. A state budget that finances extractive growth may appear procedurally lawful yet remain substantively problematic if its expenditure and financing decisions worsen environmental damage, deepen land conflicts, and shift risks onto future generations.

3. Proposing a Green Economic and Fiscal Policy Framework

Green economic and fiscal policy begins with fundamental questions: growth for whom, through which sectors, using which resources, at what ecological cost, and with benefits shared among whom? These questions challenge a conventional fiscal approach that often stops at deficit, revenue, expenditure, financing, and GDP growth figures. Green fiscal policy treats the APBN as an instrument of structural transformation toward a low-carbon, equitable, and crisis-resilient economy.

Pearce, Markandya, and Barbier (1989) introduced the concept of the green economy by integrating economic and environmental considerations. Barbier (2011) emphasizes that a green economy requires public investment capable of transforming production and consumption. Raworth (2017) offers a doughnut economics framework that places economic activity between social foundations and ecological limits. This framework is relevant to the 2027 APBN because Indonesia must ensure that people have access to food, health care, education, work, energy, and social protection without exceeding ecological carrying capacity.

A green framework should change how the government interprets its 2027 macroeconomic targets. Growth may remain an objective, but its sources should be disaggregated. The government should distinguish extractive growth, carbon-intensive growth, growth based on ecosystem services, circular economic growth, clean-energy growth, and local economic growth. It should also publish indicators of green value added, green jobs, low-carbon investment, emissions intensity per unit of GDP, and the contribution of restorative sectors to the economy.

The 2027 APBN should apply comprehensive green budget tagging. The government already has experience with climate budget tagging, but this practice should be expanded to cover ecological expenditure more broadly. The tags should cover climate mitigation and adaptation, biodiversity, forest protection, land rehabilitation, peatland restoration, mangrove rehabilitation, waste management, water quality, disaster risk reduction, the circular economy, and the protection of Indigenous Peoples. Every rupiah of expenditure should be classified as green, neutral, or brown spending that increases emissions and environmental damage.

The government should also review brown expenditure. Simply increasing green spending is insufficient; the APBN must also reduce expenditure that reinforces a carbon-intensive and extractive economy. Energy subsidies should shift from subsidizing fossil-fuel consumption toward targeted social protection and faster clean-energy adoption. Infrastructure spending should undergo climate-impact and ecological-damage assessments. Strategic investment financing should incorporate shadow carbon pricing, climate-risk analysis, ecosystem restoration plans, and social protection mechanisms for affected communities.

A green fiscal framework must also reform state revenue policy. The government should reduce fiscal dependence on income from natural resource extraction. Natural-resource non-tax state revenue can remain a source of revenue, but it should be treated as transitional income that declines over time. The government should strengthen a credible carbon tax, excise duties on environmentally harmful products, waste charges, taxes on resource rents, and tax incentives for renewable energy, energy efficiency, regenerative agriculture, and low-carbon industry.

Revenue policy must also uphold social

justice. Environmental taxes can be regressive if the government places transition costs on low-income households. Part of green revenue should be returned to these households through direct assistance, public transport subsidies, improved basic services, and support for household clean energy. A just transition requires the state to distribute its costs and benefits fairly. Newell and Mulvaney (2013) emphasize that the energy transition requires procedural, distributive, and restorative justice.

Transfers to regional governments should become a primary vehicle for ecological financing. The central government could strengthen the Fiscal Incentive Fund by incorporating ecological performance criteria. The 2027 KEM-PPKF already refers to using the Fiscal Incentive Fund to encourage healthy competition among regions, sharpen performance indicators, improve regional governments' understanding, and strengthen monitoring and evaluation. The government should make ecological measures core indicators, including reduced deforestation, increased forest cover, mangrove rehabilitation, waste reduction, lower regional emissions, protection of Indigenous territories, and disaster preparedness.

Ecological financing must go beyond incentives. Upstream regions, forest stewards, small-island regions, and disaster-prone regions need affirmative allocations because they provide ecological benefits to other areas. The government can strengthen Provincial Ecological Fiscal Transfers (TAPE) and District Ecological Fiscal Transfers (TAKE). It could also develop an Ecological Special Allocation Fund (DAK Ekologi) to finance forest and land rehabilitation, peatland recovery, mangrove rehabilitation, waste management, protection of water sources, and social forestry.

A green economic framework must strengthen the rights of Indigenous Peoples and local communities. Many forests, coastal areas, peatlands, and small islands remain intact because local communities act as stewards of natural resources. The 2027 APBN should finance faster recognition of Indigenous territories, social forestry, ecological agrarian reform, local economic capacity, and community access to climate finance. The government must not treat Indigenous Peoples merely as parties to be consulted about carbon or conservation projects. It must recognize them as rights holders, economic actors, and ecosystem stewards.

Green downstream processing requires more demanding standards. The government should distinguish extractive downstream processing from green industrialization. Processing battery minerals can support the global energy transition, but it can also damage local environments if factories run on coal, generate hazardous waste, clear forests, and disregard community rights. The government should require renewable energy, critical-mineral recycling, waste-management standards, supply-chain audits, meaningful consultation, and strong domestic industrial linkages. Green downstream processing must generate technology, decent jobs, and lower emissions, rather than merely increase exports of processed goods.

Food policy should also move toward regenerative agriculture. The government should avoid large-scale food projects that clear forests, drain peatlands, or marginalize local farmers. The 2027 APBN can support local seeds, small-scale irrigation, agroforestry, organic fertilizer, agricultural extension services, farmer cooperatives, short supply chains, local food reserves, and farmland protection. Green food policy treats farmers as active agents rather than program recipients. It also reduces deforestation risks and strengthens regional resilience.

The Free Nutritious Meals program should be incorporated into green fiscal design. The government can link it to local food systems, agroecological farming, farmer cooperatives, community kitchens, reduced food waste, and green public procurement. The APBN should require low-carbon supply chains, nutrition and food-safety standards, procurement transparency, and assessments of impacts on children, low-income families, farmers, and local economies. This major program should help transform the food system rather than simply finance recurrent consumption.

A green fiscal framework calls for stronger accountability. The government should publish a green APBN annex showing green spending, brown spending, climate risks, Danantara's contingent liabilities, high-risk strategic projects, and the fiscal impact of disasters. The DPR should establish a dedicated process for examining climate and ecological fiscal risks. The BPK should audit the performance of green spending and environmental liabilities. Civil society needs open data to scrutinize projects and expenditure, while the media needs space to investigate the links

among budgets, projects, land, and public benefits.

This approach is consistent with the Open Budget Survey's findings. Indonesia has improved transparency and oversight, but public participation continues to lag. A green APBN will succeed only if the government enables meaningful public participation. Such participation should begin while the KEM-PPKF is being drafted, not only after the RAPBN has been completed. Public consultations should include affected groups, not only businesses and technocratic institutions.

A green scenario for 2027 should rest on five anchors. First, the government should set a green growth target that measures the contribution of low-carbon and restorative sectors to GDP. Second, it should set an annual target for reducing brown expenditure. Third, it should strengthen regional ecological financing through transfers based on performance and ecological need. Fourth, it should govern Danantara through full transparency, independent audits, and climate-risk assessments. Fifth, it should link national priority programs to ecological, social, and gender indicators.

The green paradigm does not reject growth; it rejects growth that conceals ecological costs. It does not reject investment; it rejects investment that concentrates benefits while distributing losses across the public. It does not reject downstream processing; it rejects downstream processing that reproduces extraction in a new form. The 2027 APBN must demonstrate that the state can build a strong economy without undermining the ecological foundations of life.

4. Policy Recommendations

The President and the Minister of Finance should make the 2027 KEM-PPKF a turning point toward a green APBN. The government must incorporate ecological indicators into macro-fiscal targets, including lower emissions and deforestation, restoration of degraded land, mangrove rehabilitation, improved water and air quality, and reduced disaster risk. It should also present the sources of growth in 2027 according to the contributions of green and extractive sectors.

The Minister of Finance should publish a green APBN annex to the Financial Note accompanying the 2027 RAPBN. It should include

green and brown expenditure tags, climate risks, allocations for forest and land rehabilitation and waste management, energy-transition spending, energy subsidies, Danantara financing, contingent liabilities, and the social and gender impacts of priority spending.

The government should strengthen regional ecological financing. The Fiscal Incentive Fund should include ecological indicators as core performance measures. An Ecological Special Allocation Fund should finance forest protection, peatland recovery, mangrove rehabilitation, waste reduction, water-source protection, and disaster resilience. The government should also make affirmative allocations to regions that steward ecosystems and regions that are particularly vulnerable to disasters.

The President should place Danantara under a strict fiscal accountability regime. The government must disclose its project list, funding sources, risks, guarantees, contingent liabilities, beneficiaries, environmental impacts, and audit results. Danantara must not become a channel for development financing beyond public oversight.

The DPR RI should strengthen its consideration of the KEM-PPKF, Financial Note, RAPBN, and State Budget Bill through a green

fiscal assessment. It should require the government to explain the ecological implications of 5.8–6.5 percent growth, the sources of state revenue, priority expenditure, innovative financing risks, and central–regional impacts. It should also hold public hearings with civil society, academics, Indigenous Peoples, farmers, fishers, workers, women, and vulnerable groups.

The BPK should develop performance audits of green expenditure. These audits should assess whether the APBN actually lowers emissions, restores ecosystems, improves basic services, and protects vulnerable groups. The government should publicly follow up on audit findings so that the public can assess the tangible changes delivered by every rupiah of state expenditure.

The 2027 APBN must redirect development from extractive to restorative growth. The state can pursue high growth, but it must ensure that such growth broadens prosperity, restores the environment, strengthens fiscal democracy, and fulfills constitutional obligations. The green paradigm offers Indonesia a path to faster growth without undermining the resources on which people's lives depend.

References

Barbier, E. B. (2011). The policy challenges for green economy and sustainable economic development. *Natural Resources Forum*, 35(3), 233–245.

Buchanan, J. M. (1967). *Public finance in democratic process: Fiscal institutions and individual choice*. University of North Carolina Press.

Evans, P. (1995). *Embedded autonomy: States and industrial transformation*. Princeton University Press.

Hirschman, A. O. (1958). *The strategy of economic development*. Yale University Press.

International Budget Partnership. (2025). *Open Budget Survey 2025: Indonesia*. International Budget Partnership.

International Labour Organization. (2018). *World employment and social outlook 2018: Greening with jobs*. ILO.

Ministry of Finance of the Republic of Indonesia. (2026). *Macroeconomic Framework*

and Fiscal Policy Principles for 2027: Grow Higher, Prosper Faster [Original title: Kerangka Ekonomi Makro dan Pokok-Pokok Kebijakan Fiskal Tahun 2027: Tumbuh Lebih Tinggi, Sejahtera Lebih Cepat]. Government of the Republic of Indonesia.

Kuznets, S. (1955). Economic growth and income inequality. *The American Economic Review*, 45(1), 1–28.

Martinez-Alier, J. (2002). *The environmentalism of the poor: A study of ecological conflicts and valuation*. Edward Elgar.

Mazzucato, M. (2013). *The entrepreneurial state: Debunking public vs. private sector myths*. Anthem Press.

Musgrave, R. A. (1959). *The theory of public finance: A study in public economy*. McGraw-Hill.

Newell, P., & Mulvaney, D. (2013). The political economy of the “just transition.” *The Geographical Journal*, 179(2), 132–140.

Pearce, D., Markandya, A., & Barbier, E. B.

(1989). Blueprint for a green economy. Earthscan.

Prayitno, H. (2026). Testing 2027 fiscal policy: Growth, fiscal discipline, and the constitutional mandate [Original title: Menguji Kebijakan Fiskal 2027: Pertumbuhan, Disiplin Fiskal, dan Amanat Konstitusi]. The Reform Initiatives.

Raworth, K. (2017). Doughnut economics: Seven ways to think like a 21st-century economist. Chelsea Green Publishing.

Stiglitz, J. E., Sen, A., & Fitoussi, J.-P. (2009). Report by the Commission on the Measurement of Economic Performance and Social Progress. Commission on the Measurement of Economic Performance and Social Progress.

The Reform Initiatives

Jl. Tebet Dalam II A No. 17, RT. 9/RW. 1, Tebet Barat, Tebet District, South Jakarta, DKI Jakarta 12810

Website: www.tri.or.id | Email: reform@tri.or.id | Phone: (+62) 811-1182-9939