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THE POLITICAL ECONOMY BEHIND ENERGY SUBSIDY POLICY: IMPLICATIONS FOR INFLATION IN INDONESIA

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Abstract: Energy subsidy policy remains a central component of Indonesia's economic governance due to its significant implications for inflation, fiscal sustainability, and social welfare. While previous studies have predominantly examined either the economic consequences of energy subsidies or the political challenges associated with subsidy reform, limited attention has been given to the interaction between these dimensions within a comprehensive political economy framework. This study aims to analyze how energy subsidy policies influence inflation in Indonesia and to examine the political, fiscal, and social factors that shape subsidy-related decision-making. Employing a qualitative research design, the study utilizes document analysis of government reports, budget documents, publications from Statistics Indonesia (BPS), reports from international organizations, and relevant academic literature. The data were analyzed using thematic content analysis to identify patterns linking energy subsidies, inflation dynamics, fiscal conditions, and political incentives. The findings indicate that energy subsidies contribute to short-term price stability by reducing energy-related production and transportation costs, thereby moderating inflationary pressures. However, prolonged reliance on subsidies generates fiscal burdens, distorts market incentives, and increases vulnerability to external energy price shocks. The analysis further reveals that subsidy policies are strongly influenced by political considerations, including electoral incentives, public expectations, and concerns regarding social stability, which often constrain reform efforts. Although subsidy reforms tend to trigger short-term inflationary effects, they can enhance fiscal sustainability, improve resource allocation efficiency, and support long-term economic resilience when accompanied by appropriate social protection measures. This study contributes to the literature by offering an integrated political economy perspective that connects economic, political, social, and environmental dimensions of energy subsidy policy. The findings suggest that sustainable inflation management requires a balanced policy framework that combines fiscal discipline, targeted social assistance, and long-term energy transition strategies to promote both macroeconomic stability and inclusive development.
Keywords: energy subsidy policy; political economy; inflation; fiscal sustainability; energy transition; Indonesia

Abstrak: Kebijakan subsidi energi tetap menjadi salah satu instrumen utama dalam tata kelola ekonomi Indonesia karena implikasinya yang signifikan terhadap inflasi, keberlanjutan fiskal, dan kesejahteraan masyarakat. Meskipun berbagai penelitian sebelumnya telah banyak membahas konsekuensi ekonomi dari subsidi energi atau tantangan politik yang terkait dengan reformasi subsidi, perhatian terhadap interaksi antara kedua dimensi tersebut dalam suatu kerangka ekonomi politik yang komprehensif masih relatif terbatas. Penelitian ini bertujuan untuk menganalisis bagaimana kebijakan subsidi energi memengaruhi inflasi di Indonesia serta mengkaji faktor-faktor politik, fiskal, dan sosial yang membentuk proses pengambilan keputusan terkait subsidi. Penelitian ini menggunakan pendekatan kualitatif dengan metode analisis dokumen terhadap laporan pemerintah, dokumen anggaran, publikasi Badan Pusat Statistik (BPS), laporan organisasi internasional, dan literatur akademik yang relevan. Data dianalisis menggunakan analisis tematik untuk mengidentifikasi pola hubungan antara subsidi energi, dinamika inflasi, kondisi fiskal, dan insentif politik. Hasil penelitian menunjukkan bahwa subsidi energi berkontribusi terhadap stabilitas harga dalam jangka pendek melalui penurunan biaya produksi dan transportasi yang berkaitan dengan energi, sehingga membantu menekan tekanan inflasi. Namun, ketergantungan yang berkepanjangan terhadap subsidi juga menimbulkan beban fiskal, mendistorsi insentif pasar, dan meningkatkan kerentanan terhadap guncangan harga energi global. Analisis lebih lanjut mengungkapkan bahwa kebijakan subsidi sangat dipengaruhi oleh pertimbangan politik, termasuk insentif elektoral, ekspektasi publik, dan kebutuhan menjaga stabilitas sosial, yang sering kali membatasi upaya reformasi. Meskipun reformasi subsidi cenderung menimbulkan dampak inflasi dalam jangka pendek, reformasi tersebut berpotensi meningkatkan keberlanjutan fiskal, memperbaiki efisiensi alokasi sumber daya, dan memperkuat ketahanan ekonomi jangka panjang apabila didukung oleh mekanisme perlindungan sosial yang memadai. Penelitian ini berkontribusi pada literatur dengan menawarkan perspektif ekonomi politik yang terintegrasi yang menghubungkan dimensi ekonomi, politik, sosial, dan lingkungan dalam kebijakan subsidi energi. Temuan penelitian menunjukkan bahwa pengendalian inflasi yang berkelanjutan memerlukan kerangka kebijakan yang seimbang antara disiplin fiskal, bantuan sosial yang tepat sasaran, dan strategi transisi energi jangka panjang guna mewujudkan stabilitas makroekonomi sekaligus pembangunan yang inklusif.

Kata Kunci: subsidi energi; ekonomi politik; inflasi; keberlanjutan fiskal; transisi energi; Indonesia.

Introduction

Energy subsidy policy has long been one of the most influential instruments in Indonesia's economic and social policy framework. As a developing country with a large population and significant income disparities, Indonesia has historically relied on energy subsidies—particularly for fossil fuels such as gasoline and diesel—to maintain affordable energy prices and support household welfare. According to the Ministry of Energy and Mineral Resources (ESDM, 2022), total energy subsidies reached approximately IDR 170 trillion in 2022, highlighting the substantial fiscal commitment allocated to this policy. Beyond its economic function, energy subsidies also serve as a political instrument that governments use to maintain social stability and public support, particularly during periods of economic uncertainty.

From a political economy perspective, energy subsidies represent more than a fiscal mechanism; they reflect the interaction between economic objectives and political incentives. Governments often face competing pressures to ensure affordable energy access while simultaneously preserving fiscal sustainability and macroeconomic stability. Consequently, energy subsidy policies frequently become the subject of intense political debate, particularly when rising global energy prices increase the fiscal burden of maintaining subsidies.

Despite their intended benefits, energy subsidies have generated significant concerns regarding their long-term economic consequences, particularly their impact on inflation. In recent years, Indonesia has experienced notable inflationary pressures driven by fluctuations in global energy prices, exchange rate volatility, and adjustments to domestic energy pricing policies. Data from Statistics Indonesia indicate that annual inflation reached 6.5% in 2023, representing one of the highest inflation rates recorded during the previous decade (BPS, 2023). This trend suggests that the relationship between energy subsidy policies and inflation is neither straightforward nor linear but instead involves complex interactions among fiscal policy, market expectations, and global economic conditions.

The inflationary implications of energy subsidy reforms are particularly significant because energy prices directly affect production costs, transportation expenses, and household consumption expenditures. When governments reduce subsidies or adjust fuel prices, the resulting increase in energy costs often triggers broader price increases across multiple sectors of the economy. Conversely, maintaining extensive subsidies may suppress inflationary pressures in the short term but can create fiscal vulnerabilities that threaten long-term economic stability.

In addition to economic considerations, energy subsidy policies are deeply embedded within Indonesia's political landscape. Policy decisions regarding fuel subsidies are often influenced by electoral incentives, public opinion, interest-group pressures, and concerns regarding social unrest. As a result, governments frequently encounter challenges when attempting to implement subsidy reforms, even when such reforms are economically justified. Understanding these political dynamics is therefore essential for explaining why energy subsidy policies persist and how they influence inflation and broader economic outcomes.

Although previous studies have examined either the economic effects of energy subsidies or the political challenges associated with subsidy reform, relatively few studies have integrated both dimensions within a comprehensive political economy framework. This study seeks to address this gap by analyzing how political considerations shape energy subsidy policies and how these policies subsequently influence inflation and social welfare in Indonesia.

This study aims to examine the relationship between energy subsidy policies and inflation in Indonesia while simultaneously identifying the broader economic and social consequences of these policies. Specifically, the research seeks to provide a deeper understanding of how energy subsidies, as a policy instrument, influence price stability, purchasing power, and overall economic performance.

To achieve this objective, the study analyzes historical patterns of inflation and energy subsidy policies over time in order to identify recurring trends and policy outcomes. Existing evidence suggests that changes in subsidy regimes can significantly affect inflation dynamics. For example, (Anas et al., 2022) found that the removal or reduction of energy subsidies often leads to short-term inflationary pressures due to increased energy prices. However, the same study also argues that subsidy reforms may generate long-term economic benefits by improving resource allocation efficiency, reducing fiscal burdens, and enhancing economic competitiveness.

Furthermore, this study aims to assess the social implications of energy subsidy policies, particularly their effects on different socioeconomic groups. Energy subsidies are frequently justified as a mechanism for protecting low-income households from rising living costs. However, previous research has demonstrated that subsidy benefits are not always distributed equitably, with higher-income households often capturing a disproportionate share of subsidy advantages due to their greater energy consumption. Therefore, evaluating the social distributional effects of energy subsidies is crucial for determining whether these policies effectively achieve their intended welfare objectives.

By integrating economic and political perspectives, this study seeks to provide a comprehensive assessment of the role of energy subsidies in shaping inflation and social welfare outcomes in Indonesia. The findings are expected to contribute to the broader literature on political economy and public policy while offering practical insights for policymakers seeking to balance economic efficiency, social protection, and political feasibility.

Based on the foregoing discussion, this study addresses two primary research questions.

First, how do energy subsidy policies influence inflation in Indonesia? To answer this question, the study investigates the relationship between changes in energy subsidy policies and fluctuations in inflation rates while considering external factors such as global oil prices, exchange rate movements, and monetary policy interventions. Previous evidence suggests that Indonesia's inflation dynamics are highly sensitive to developments in global energy markets. (Resosudarmo et al., 2023) demonstrate that increases in international energy prices contribute directly to domestic inflation through higher transportation costs, production expenses, and consumer prices. This finding highlights the vulnerability of Indonesia's economy to external energy shocks and underscores the importance of subsidy policies as a mechanism for mitigating these effects.

Second, what political factors influence the formulation and implementation of energy subsidy policies in Indonesia? Energy subsidy decisions are often shaped by political considerations that extend beyond purely economic calculations. In many cases, governments face pressure from voters, business groups, labor organizations, and other stakeholders who benefit from maintaining low energy prices. These political incentives become particularly pronounced during election periods, when policymakers may be reluctant to implement unpopular subsidy reforms despite their potential economic benefits.

Research by (Akimaya & Dahl, 2022) indicates that energy subsidy reforms are frequently constrained by political interests and short-term electoral considerations. Policymakers often prioritize immediate political stability and public approval over long-term fiscal sustainability and economic efficiency. Consequently, subsidy reforms may be delayed, modified, or reversed in response to political pressures, creating challenges for effective economic management.

By addressing these research questions, this study seeks to provide a more comprehensive understanding of the complex interaction between energy subsidy policies, inflation dynamics, and political decision-making processes in Indonesia. Such an understanding is essential for developing policy recommendations that promote both economic stability and social welfare while recognizing the political realities that shape public policy outcomes.

Literature Review

Political economy examines the interaction between economic systems and political institutions, emphasizing how public policies are shaped by the distribution of power, interests, and resources within society. From this perspective, economic policies are not solely determined by efficiency considerations but are also influenced by political incentives and electoral calculations. Energy subsidy policy represents one of the most prominent examples of this interaction, particularly in developing countries where governments often utilize subsidies as instruments to maintain social stability and political legitimacy.

In the Indonesian context, energy subsidies have long constituted a central component of economic policy. Although originally designed to protect household purchasing power and support economic development, energy subsidies have increasingly become intertwined with political considerations. Governments frequently face significant public resistance when attempting to reduce fuel subsidies, especially among lower-income groups that are highly dependent on subsidized energy. Consequently, policymakers often encounter a trade-off between maintaining fiscal sustainability and preserving political support.

According to Lockwood, (2015), energy subsidies can create structural dependency, discourage energy efficiency, and delay the transition toward more sustainable energy systems. The persistence of subsidies often reflects political incentives rather than economic rationality, as governments seek to avoid social unrest and electoral costs associated with higher energy prices. Similarly, (Resosudarmo et al., 2023) argue that while energy subsidies may provide short-term welfare benefits, their long-term consequences—including fiscal pressure, market distortions, and inflationary risks—are frequently underestimated in public policy debates.

The political economy perspective further suggests that inefficient subsidy schemes may divert public resources away from more productive sectors such as infrastructure, education, and technological innovation. Such resource misallocation can weaken economic productivity and contribute to macroeconomic instability. Moreover, subsidized energy prices often encourage excessive consumption, increasing fiscal burdens and reducing incentives for investment in renewable energy development.

The Indonesian government's recurring dilemma regarding fuel subsidy reform illustrates these dynamics. Rising global oil prices and widening fiscal deficits have repeatedly prompted efforts to reduce subsidy expenditures. However, such reforms often face strong political opposition because fuel price increases directly affect household expenditures and transportation costs. Consequently, governments may postpone or moderate reform initiatives despite mounting fiscal pressures.

Evidence from other developing economies reinforces these observations. For example, Abdul et al., (2025) demonstrate that energy subsidy removal in Nigeria contributed to greater economic resilience and lower inflationary pressures in the long run, despite generating short-term political and social challenges. This finding highlights the importance of balancing immediate political considerations with long-term economic sustainability when designing energy subsidy policies.

Empirical Evidence on Energy Subsidies and Inflation

A growing body of literature has investigated the relationship between energy subsidies and inflation, particularly in developing economies where energy prices play a significant role in production and consumption activities. Existing studies generally indicate that energy subsidies can influence inflation through both direct and indirect channels.

(Anas et al., 2022) found that extensive energy subsidies create price distortions by keeping domestic energy prices below market equilibrium levels. While such policies may temporarily suppress inflationary pressures, they encourage excessive energy consumption and reduce incentives for investments in alternative and renewable energy sources. Over time, these distortions can contribute to economic inefficiencies and increase vulnerability to external energy price shocks.

Comparative evidence from Latin America provides additional insights into the consequences of subsidy reforms. (Ordonez et al., 2021) reported that energy subsidy reductions in countries such as Brazil and Mexico initially generated inflationary pressures due to rising energy and transportation costs. However, the reforms ultimately improved fiscal balances, encouraged private investment, and supported the development of more sustainable energy sectors. These findings suggest that while subsidy reform may impose short-term adjustment costs, it can produce significant long-term economic benefits.

In Indonesia, the relationship between energy subsidies and inflation is particularly complex due to the central role of fuel prices in the economy. (Wulansari, 2021) observed that energy subsidy policies are often implemented independently of broader fiscal and monetary strategies, resulting in policy uncertainty and inflation volatility. This lack of coordination may amplify the inflationary effects of subsidy reforms and undermine their effectiveness.

The inflationary transmission mechanism is especially evident during periods of fuel price adjustments. When the government reduces fuel subsidies, transportation and logistics costs typically increase, leading to higher production expenses across various sectors. These higher costs are subsequently passed on to consumers through increased prices for food, manufactured goods, and services. As a result, inflationary pressures can emerge throughout the economy, reducing household purchasing power and potentially affecting social welfare.

Taken together, prior studies reveal that the relationship between energy subsidies and inflation is multidimensional and context-dependent. While subsidies may temporarily stabilize prices and protect consumers, they can also create long-term economic distortions that ultimately contribute to inflationary instability. Therefore, a comprehensive analytical framework is necessary to understand how political considerations, fiscal constraints, and market mechanisms jointly shape inflation outcomes in Indonesia.

Building upon political economy theory and empirical findings, this study adopts a theoretical framework that integrates political economy analysis with the supply-and-demand model to explain the relationship between energy subsidy policy and inflation in Indonesia.

From a political economy perspective, government decisions regarding energy subsidies are influenced by both economic objectives and political incentives. Policymakers seek to maintain social stability and electoral support while simultaneously addressing fiscal sustainability concerns. These competing objectives shape the timing, magnitude, and implementation of subsidy reforms.

From a market perspective, energy subsidies directly affect energy prices by lowering the cost of fuel and electricity below market levels. According to the supply-and-demand framework, changes in subsidy levels alter relative prices and influence consumption and production decisions throughout the economy. When subsidies are reduced, energy prices increase, leading to higher transportation and production costs. Producers subsequently transfer these additional costs to consumers through higher prices for goods and services, generating cost-push inflation.

The framework identifies several key variables. The independent variable is government energy subsidy policy, while inflation serves as the primary dependent variable. Energy prices function as an important transmission mechanism linking subsidy policy to inflation outcomes. In addition, macroeconomic factors such as economic growth, unemployment, fiscal conditions, and monetary policy may influence the magnitude of this relationship.

Furthermore, external factors must also be considered. Global oil price fluctuations, exchange rate movements, and changes in international trade policies can significantly affect domestic energy costs and inflation dynamics. Since Indonesia remains connected to global energy markets, these external variables may either amplify or moderate the impact of subsidy reforms on inflation.

Based on this framework, the study proposes that reductions in energy subsidies are likely to increase inflation in the short term through rising production and transportation costs. However, over the long term, subsidy reforms may improve fiscal sustainability, encourage more efficient resource allocation, stimulate investment in productive sectors, and support more sustainable economic growth. Consequently, the overall impact of energy subsidy policy should be understood as a dynamic process shaped by both political incentives and economic mechanisms.

The conceptual framework therefore positions energy subsidy policy as a politically driven economic instrument whose effects on inflation operate through market price adjustments, fiscal conditions, and broader macroeconomic interactions. This integrated approach provides a comprehensive foundation for analyzing the political economy of energy subsidies and their implications for inflation in Indonesia.

Methods

Research Design

This study employs a qualitative research design using document analysis to investigate the political economy underlying energy subsidy policies and their implications for inflation in Indonesia. A qualitative approach is considered appropriate because the relationship between energy subsidies, political decision-making, and inflation is embedded within complex institutional, economic, and socio-political contexts that cannot be fully understood through numerical analysis alone.

Document analysis enables researchers to systematically examine policy narratives, institutional decisions, and economic arguments reflected in official publications and scholarly works. According to Denzin and Lincoln (2011), qualitative research is particularly useful for exploring complex social and political phenomena because it facilitates a contextual understanding of policy processes and institutional behavior. Similarly, Creswell (2014) argues that qualitative inquiry allows researchers to interpret meanings, identify patterns, and develop comprehensive explanations regarding social and policy issues.

In the context of Indonesia's energy subsidy policy, document analysis provides an effective means of examining how political and economic considerations influence policy formulation and implementation. Furthermore, this approach allows for the exploration of the relationship between subsidy policies and inflation through the interpretation of policy documents, economic reports, and previous academic findings. By focusing on documentary evidence, the study seeks to generate a comprehensive understanding of the political economy factors that shape energy subsidy decisions and their broader macroeconomic consequences.

Data Collection

The study relies exclusively on secondary data obtained from a variety of authoritative documentary sources. These sources include government regulations, state budget documents (APBN), reports issued by the Ministry of Finance, the Ministry of Energy and Mineral Resources, Bank Indonesia publications, Statistics Indonesia (BPS) reports, parliamentary documents, policy briefs, and official statements related to energy subsidy programs. In addition, reports from international organizations such as the World Bank, the International Monetary Fund (IMF), and the Organisation for Economic Co-operation and Development (OECD) were reviewed to provide comparative perspectives and broader contextual understanding.

Academic literature was also utilized as an important source of evidence. Peer-reviewed journal articles, books, and conference papers addressing energy subsidies, political economy, public policy, fiscal sustainability, and inflation were systematically examined. These sources provided theoretical foundations and empirical findings that informed the analysis.

The selection of documents was guided by three primary criteria. First, documents had to be directly relevant to energy subsidy policies or inflation in Indonesia. Second, they had to originate from credible institutions or reputable academic publications. Third, the documents needed to provide sufficient information regarding policy objectives, implementation mechanisms, fiscal impacts, or inflationary outcomes. Through these criteria, the study ensured that the collected data were relevant, reliable, and suitable for addressing the research objectives.

Data Analysis

The collected documents were analyzed using thematic content analysis. This analytical approach allows researchers to identify, classify, and interpret recurring themes and patterns within textual materials. Thematic analysis is particularly suitable for political economy research because it facilitates the examination of relationships between political interests, economic objectives, and policy outcomes.

The analysis was conducted in several stages. First, all documents were carefully reviewed to gain familiarity with their content and context. Second, relevant information related to energy subsidies, inflation, fiscal policy, political considerations, and socioeconomic impacts was coded and categorized. Third, recurring themes were identified and organized into broader analytical categories.

Several major themes emerged during the analysis, including the role of energy subsidies in maintaining price stability, political motivations behind subsidy retention or reform, fiscal pressures associated with subsidy expenditures, public responses to subsidy adjustments, and the inflationary consequences of changes in energy prices. These themes were subsequently examined to identify patterns and relationships that explain how political and economic considerations influence energy subsidy policies and their effects on inflation.

By applying thematic content analysis, the study not only describes policy developments but also interprets the underlying political economy mechanisms that shape government decisions regarding energy subsidies in Indonesia.

Validity and Trustworthiness

To enhance the credibility and trustworthiness of the findings, this study employs source triangulation. Source triangulation involves comparing information obtained from different types of documents and institutions to verify consistency and reduce potential bias. For example, government reports regarding subsidy expenditures and inflation control were compared with findings from academic studies and reports published by international organizations.

Cross-document verification was also conducted to ensure the reliability of interpretations. Policy narratives presented in official government documents were examined alongside independent analyses from scholars and international institutions. This process allowed the researcher to identify converging and diverging perspectives regarding the effectiveness and consequences of energy subsidy policies.

Furthermore, the study maintained analytical rigor by systematically documenting the coding process and thematic development. This transparency enhances the dependability of the research and allows future researchers to understand how conclusions were derived from the available evidence.

Through the application of source triangulation, cross-document verification, and systematic thematic analysis, the study seeks to produce robust and credible findings regarding the political economy of energy subsidy policies and their implications for inflation in Indonesia.

Results And Discussions

The findings demonstrate that energy subsidy policy in Indonesia plays a central role in shaping inflation dynamics, fiscal sustainability, and political decision-making Coady, D., et. al. (2019). Rather than functioning solely as an economic instrument, energy subsidies have evolved into a politically sensitive policy mechanism that directly influences public welfare, government legitimacy, and macroeconomic stability (Kim, 2021). This interaction reflects the broader political economy framework in which economic policies are frequently influenced by electoral incentives, social pressures, and fiscal constraints (Baker et al., 2023).

Indonesia has historically maintained substantial subsidies for fuel and electricity to protect household purchasing power and stabilize domestic prices (*Indonesia's Energy Support Measures | International Institute for Sustainable Development*, n.d.). In the short term, these subsidies help reduce production and transportation costs, thereby limiting inflationary pressures across multiple sectors of the economy. However, the findings indicate that such policies simultaneously create structural distortions by suppressing market-based price signals and increasing the fiscal burden on the state budget . According to BPS-Statistics Indonesia (2023) shows that Indonesia's annual inflation rate reached 5.51% in 2022, reflecting significant price pressures across transportation, household energy, and consumer expenditure categories. Energy-related expenditures were among the major contributors to inflation during this period.

From a political economy perspective, the persistence of energy subsidies cannot be understood solely through economic considerations. Subsidy policies are strongly influenced by political calculations because energy prices directly affect the daily lives of citizens and are highly visible indicators of government performance (Hahn & Metcalfe, 2021). Consequently, governments often face political pressure to maintain low fuel prices even when global energy prices increase. This condition is particularly evident during electoral periods, when policymakers tend to prioritize social and political stability over fiscal efficiency. Previous studies on Indonesia's subsidy policy have shown that fuel price adjustments frequently become politically contentious because they generate immediate public reactions and may reduce government popularity. As a result, subsidy policies often reflect a compromise between economic rationality and political interests.

The empirical evidence further indicates that inflationary pressures intensify when subsidy reductions are implemented. Historical data reveal that fuel price adjustments have consistently produced substantial increases in consumer prices. One of the most significant examples occurred in 2014 when the government implemented fuel price increases as part of subsidy reform measures. Following the policy adjustment, Indonesia's inflation rate rose sharply to approximately 8.36%, illustrating the strong transmission mechanism between energy prices and overall inflation. Energy functions as a fundamental production input throughout the economy; therefore, increases in fuel costs affect transportation, logistics, manufacturing, and food distribution simultaneously. These cascading effects eventually translate into higher consumer prices and broader inflationary pressures.

The Indonesian experience is consistent with patterns observed in many developing economies (Hill, 2018). International Monetary Fund (IMF) analyses suggest that countries maintaining extensive energy subsidy programs often experience heightened inflationary vulnerability during periods of global energy market volatility. Although subsidies may temporarily shield consumers from external price shocks, they frequently postpone necessary market adjustments rather than eliminate underlying inflationary pressures. Consequently, governments eventually confront difficult policy choices between maintaining expensive subsidy programs and implementing reforms that may trigger short-term inflation. Global energy market disruptions during the post-pandemic recovery period further reinforced these challenges by increasing international oil and commodity prices, thereby intensifying fiscal pressures on energy-importing countries.

The findings also reveal important distributional consequences associated with energy subsidy reform. Inflation generated by fuel price adjustments does not affect all socioeconomic groups equally. Lower-income households are considerably more vulnerable because a larger proportion of their income is allocated to essential expenditures such as food, transportation, and household energy consumption. When energy prices rise, these households experience a more significant decline in purchasing power compared with higher-income groups. This condition increases the risk of poverty and socioeconomic inequality, particularly when inflation is not accompanied by adequate compensation mechanisms. Therefore, the social consequences of subsidy reform constitute a critical consideration in the formulation of public policy.

At the fiscal level, large-scale energy subsidies generate substantial opportunity costs. Government expenditures allocated to subsidizing fuel and electricity reduce the availability of public resources for investments in education, healthcare, infrastructure, and technological development. From a developmental perspective, this allocation pattern may limit long-term economic growth because productive sectors receive fewer resources than consumption-based subsidy programs. Consequently, although subsidies may contribute to short-term price stability, they can simultaneously weaken the state's capacity to invest in sectors that generate sustainable economic returns. This finding supports the argument that subsidy policies should be evaluated not only in terms of inflation control but also in relation to broader development objectives and fiscal sustainability.

Regional comparisons further strengthen this argument. Compared with several ASEAN countries, Indonesia has historically allocated a relatively larger share of public expenditure to energy subsidies. In recent years, countries such as Malaysia and Thailand have gradually introduced alternative approaches aimed at reducing fiscal dependence on universal energy subsidies. These measures include targeted social assistance, renewable energy incentives, and market-based pricing mechanisms. Such policy shifts reflect increasing recognition that broad subsidy programs are difficult to sustain under conditions of volatile global energy prices and growing fiscal demands.

The analysis also highlights the importance of energy transition policies in reducing long-term inflationary risks. Dependence on fossil-fuel subsidies exposes Indonesia to fluctuations in international oil prices and increases vulnerability to external economic shocks. In contrast, investments in renewable energy can strengthen energy security while reducing the fiscal burden associated with subsidy programs. The World Bank has emphasized that renewable energy development can contribute to greater fiscal sustainability and long-term economic resilience by reducing dependence on imported energy resources and volatile global commodity markets. A transition toward sustainable energy systems may therefore provide a strategic pathway for addressing both inflationary pressures and fiscal challenges simultaneously.

These findings suggest that Indonesia faces a fundamental policy dilemma. On one hand, energy subsidies remain politically attractive because they help maintain affordability, protect purchasing power, and reduce immediate inflationary pressures. On the other hand, prolonged dependence on subsidies creates fiscal vulnerabilities, distorts market incentives, and constrains long-term economic development. As a result, the challenge is not whether subsidy reform should occur, but rather how such reforms can be implemented without generating excessive inflation or social instability.

A gradual and carefully designed reform strategy appears to be the most feasible policy option. Phased subsidy reductions accompanied by targeted social protection programs can help mitigate inflationary shocks while preserving public welfare. Direct cash transfers, transportation support, and targeted energy assistance for vulnerable households may reduce the adverse distributional effects of rising energy prices. Furthermore, transparent policy communication is essential to strengthen public trust and reduce political resistance to reform. Without effective communication and compensation mechanisms, subsidy reforms may generate significant social and political opposition regardless of their economic rationale.

Overall, the results indicate that inflation in Indonesia cannot be explained solely through conventional market mechanisms. Instead, inflation outcomes are closely linked to the political economy of energy subsidy policy, where economic objectives interact with electoral incentives, fiscal constraints, and social welfare considerations. The evidence suggests that sustainable inflation management requires a comprehensive policy framework that integrates fiscal responsibility, social protection, and long-term energy transition strategies. Such an approach would allow Indonesia to move beyond a subsidy-dependent model toward a more resilient and sustainable economic structure capable of maintaining both macroeconomic stability and public welfare.

Conclusion

This study examined Indonesia's energy subsidy policy through a political economy perspective, focusing on its implications for inflation and broader economic outcomes. The findings indicate that energy subsidies play a significant role in maintaining short-term price stability and protecting household purchasing power. However, subsidy reductions or reforms often generate temporary inflationary pressures as energy prices adjust to market conditions. Consistent with previous studies, the analysis suggests that while subsidy reforms may increase inflation in the short run, they can contribute to improved fiscal efficiency and more sustainable economic management in the long term Fathurrahman et al., 2015. The study further demonstrates that energy subsidy policies are not determined solely by economic considerations but are also shaped by political interests, electoral incentives, and public expectations, making reform efforts particularly challenging in a democratic context (Basri & Hill, 2020).

Beyond its economic implications, this study highlights the multidimensional nature of energy subsidy policy. The findings suggest that effective reform requires balancing fiscal sustainability with social protection and environmental objectives. While reducing fossil fuel subsidies may create opportunities to promote renewable energy development and support long-term sustainability goals Bazilian & Onyeji, (2012), such reforms must be accompanied by targeted measures that protect vulnerable groups from adverse welfare effects. In this regard, the study contributes to the existing literature by providing a more comprehensive understanding of energy subsidy policy that integrates economic, political, social, and environmental considerations. This broader perspective extends previous research that has primarily focused on the fiscal and inflationary consequences of subsidies, offering a more holistic framework for evaluating policy outcomes.

The findings also carry important implications for policymakers. Energy subsidy reform should be implemented gradually and supported by transparent communication strategies, effective social protection programs, and coordinated fiscal and monetary policies to mitigate inflationary pressures and maintain public support. Furthermore, savings generated from subsidy reforms should be strategically allocated to productive sectors, particularly renewable energy infrastructure and sustainable development initiatives, in order to enhance long-term economic resilience and energy security.

Despite these contributions, this study has several limitations. The analysis is based on evidence from a specific period and does not fully incorporate external factors such as global oil price volatility, geopolitical developments, exchange rate fluctuations, and changes in international energy markets. Future research should therefore employ broader datasets and more comprehensive analytical frameworks to capture these dynamics. In addition, further studies are needed to examine the social distributional effects of subsidy reforms and to conduct comparative analyses with other countries that have successfully implemented energy subsidy reforms. Such efforts would provide valuable insights for developing more effective, equitable, and sustainable energy policies in Indonesia.

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