

Unlocking the next wave of digital growth: beyond metropolitan Indonesia

A study by Alpha JWC Ventures and
Kearney in collaboration with Credit Suisse,
AWS, and Xiaomi
March 2021

KEARNEY



Foreword from Coordinating Minister for Maritime and Investment Affairs



Luhut Binsar Pandjaitan Coordinating Minister for Maritime and Investment Affairs

In 2014, when this cabinet was formed, the president had a vision to make Indonesia one of the world's strongest nation. With unparalleled natural resources, huge population of productive age, and the 16th largest economy in the world, Indonesia is on its way to become 4th biggest economy in the world by 2040. But being 'big' is not enough, a country should serve its people and make their lives better in every way. Hence, the president set out his national priority programs, including economic transformation and economic equity.

In this modern world, Indonesia can no longer rely on natural resources to strive. We need to increase our competitiveness in various industries and in human quality. We also believe that welfare should be distributed evenly throughout the country. Prosperity will not be achieved if wealth and progress are concentrated in some areas while the others are struggling to survive. For the past six years, we have worked to achieve those goals. We have accomplished many things, but there are still a lot to work on.

Technology is one sector that can answer these challenges. We have seen how Indonesia raise six unicorns and thousands of rising technology startups in less than a decade. We have seen digital solutions change Indonesians' ways of life, from the use of e-commerce for easier daily trades to the rising number of SMEs due to better access to lending brought by fintech companies. The potential is limitless. This report shows that industry players have focused only on the metropolitan areas, but now, the other parts of Indonesia are ready to join the digital revolution as well.

The government is ready to continue its part in providing a fertile landscape for growth and supporting startups, investors, users, and other industry players. We are continuously building the needed physical, digital, and regulatory infrastructure. Long gone is the old-fashioned bureaucratic pace of working with the government — we are transforming our activities and institutions to become proactive partners of this dynamic, ambitious ecosystem. We are also pushing for more digital talent development through public-private partnership programs and education reform, while also opening Indonesia's doors to more capital with 2020 Job Creation Laws and streamlined business licensing process.

With this progress, I am very sure that we are not done yet. We hope that we can continually strive to be better as a government bodies. We are welcome if there is any input regarding how can we support entrepreneurs, investors, corporates, individuals and all stakeholders to enhance Indonesia's digital economy. We must work together to create this environment. This is a collaboration between generations, and I am encouraging everyone to participate in this digital transformation so our generation and the next generation can reap the benefits.

Foreword from Alpha JWC Ventures



Chandra Tjan
Co-Founder & General Partner, Alpha JWC Ventures

When I first started investing in Indonesian start-ups more than a decade ago, I knew that we were on to something great. I was sure that Indonesia would be able to become one of the world's biggest digital powerhouse – it just needed a little boost to start. Fast forward to 2021, Indonesia has found its sweet spot for growth: its vast consumer base coupled with the digitalization of daily business-as-usual activities, and a good mix of caution and openness to new services such as online lending & social commerce.

Over the past decade, Indonesia has also experienced a significant increase in the quantity and quality of tech start-ups, giving rise to a generation of young Indonesians who aspire to be entrepreneurs and build the country's digital ecosystem.

Our position as investors is unique, we are presenting Indonesia's digital economy to the world and also empowering them from within. We have seen the numbers and the way technology has changed our lives; we also know that we are not even close to the peak yet. We have only tapped on the tip of the iceberg: the metropolitan area of Greater Jakarta and a few other cities. What lies beyond is still vast and possesses even greater potential.

While not all, we have also seen how some start-ups not only survive but thrive amidst the pandemic. Instead of inducing setbacks, COVID-19 has become a testament to how strong and adaptable our digital ecosystem is. We hope this research report can better explain our conviction to you as well as introduce a different side of Indonesia that has yet to be fully explored to the world.

We created this report through extensive data gathering and analysis and served it in a way that is easy to understand in hopes of providing accessible knowledge about Indonesia's Tier 2 and Tier 3 cities' digital potential to various readers from students, entrepreneurs, to policy makers, at home and abroad. Eventually, we hope this will be an invitation for more investors to come to Indonesia, for regional & global industry players to enter & develop the local scene, and for our local entrepreneurs to continue innovating and creating social impact.

We are proud of this report and we hope you find it interesting and valuable. With this, we would also thank our partners for supporting this effort: Credit Suisse, AWS, and Xiaomi Indonesia. This report is just a beginning. We hope it will spark further conversations and actions to build these Tier 2 and Tier 3 cities faster, better, together.

Foreword from Alpha JWC Ventures



Jeffrey Joe
Co-Founder & General Partner, Alpha JWC Ventures

Over the past decade, we have seen Indonesia's digital economy grow from nascency into one of Asia's hotspots, and we have witnessed a transformation in the quantity and quality of local companies, products, founders, and investment opportunities. We have also had the pleasure of finding and supporting brilliant entrepreneurs and their innovative solutions to address societal challenges and introduce significant social impacts on many fronts from agriculture, social commerce, and education .

Despite outstanding growth, Indonesia has been mostly untouched. Most start-ups are based in the Greater Jakarta area, with most digital solutions focusing on this region, leaving areas beyond the capital and Java behind. As local investors, we know that these regions have a wealth of potential, as we have seen in our portfolio companies' massive growth. We believe the next Indonesian unicorns will be the ones that can tap into tier 2 and tier 3 cities.

COVID-19 has created a strong tailwind for the tech industry. The pandemic has accelerated digital adoption and brought about innovations faster than ever before. Combined with better infrastructure and a growing middle-class, technology has become an integral part of life to millions of people. This strengthened our conviction about the potential of Indonesia's digital economy, especially in non-metropolitan areas.

This research is our instrument to validate our beliefs and learnings. As an Indonesia-focused venture capital firm, we focus on backing local champions and building a winning ecosystem. However, we also believe that to maximize the country's potential, we cannot do it alone—we need involvement from industry players, investors, and government to continue our endeavors in the metropolitan cities and beyond.

We have put enormous effort and partnered with the best in the industry to understand tier 2 and tier 3 cities' characteristics, state, and potential. We hope this report motivates aspiring local entrepreneurs to create something from and for their hometowns, convince more global investors to join us in assisting these innovators, and spark conversations about how we can work together to make Indonesia's digital economy one of the world's biggest and best.

We are very excited about what's coming, and we believe the future of this industry is very promising. We hope you do too. We welcome feedback and discussions with potential partners and stakeholders to participate in the next wave of growth in Indonesia's digital economy.

Foreword from Kearney



Shirley Santoso
Partner and President Director, Kearney

Over the past 10 years, we have witnessed the tremendous growth of Indonesia's digital economy. So much of our daily conveniences now center on same-day delivery, on-demand ride hailing, and one-click purchases. With the lives of millions of Indonesians so intertwined with digital, it's no wonder that Indonesia is home to some of the world's most valuable unicorns.

The progress of our digital economy has been remarkable. However, so far, it has focused on metropolitan Indonesia. Greater Jakarta and Surabaya account for 50 to 80 percent of the country's digital economy while accounting for only 15 percent of the population. This means that the digital potential of the remaining 85 percent of the population in non-metropolitan Indonesia remains largely untapped. This prompts two questions: What is the digital potential of tier 2 and tier 3 cities? And what must be done to unlock this potential?

We often encounter the first question relating to the digital potential of tier 2 and tier 3 cities in our work advising leading corporations and budding start-ups in the region. While little was previously known about digital adoption in tier 2 and tier 3 cities, this report aims to provide clarity about the digital behavior of consumers in tier 2 and tier 3 cities, identify key barriers to digital adoption, and paint a clearer picture of the massive digital potential—which in turn should give confidence for corporations, investors, and start-ups to adjust, expand, and seize the opportunities in non-Metropolitan Indonesia.

For far too long, we have heard of Indonesia's digital potential, and as we emerge from a once-in-a-generation pandemic, now is the right time to realize such potential. This leads to the second question about what must be done to unlock the potential. In this report, we uncover six imperatives to unlock Indonesia's digital potential. We are confident that with the right approach, we can expect non-Metropolitan Indonesia to account for half of the country's digital economy by 2025 and urge all stakeholders, public and private, to collaborate to unlock this potential.

The prospect of digital growth in non-Metropolitan Indonesia is an exciting one. It should not come as a surprise that Indonesia stands a chance to be one of the world's most vibrant digital economies by unlocking digital potential of tier 2 and tier 3 cities. We are excited to have a glimpse of the future, and it goes without saying that we are all-in for this journey. We hope you do too!

Foreword from institutional partners.



Rizal Gozali

Vice Chairman of IBCM (SEA) and
Country Head (Indonesia)

“At Credit Suisse, we believe in the significant positive impact of digitalization, which has been accelerated by the pandemic. Our ‘technology at the service of humans’ super-trend theme highlights technology as a compelling sector for investors and corporates alike. The insights from the report will be invaluable, and we are delighted to be a part of this study focused on uncovering the vast opportunities arising from digital disruption across various sectors in Indonesia. Indonesian entrepreneurs are at the forefront of this innovation, and we are proud to help them achieve their ambitions by bringing them access to international markets, local market knowledge, and comprehensive solutions that deliver the best of our integrated wealth management and investment banking capabilities.”



Gunawan Susanto

Country General Manager

“Indonesia is a thriving center for companies to build their businesses, and AWS is dedicated to helping grow the next generation of business from all industries across Indonesia. We hope that this report will inspire entrepreneurs, business owners, and investors to tap into the potential offered by Indonesian tier 2 and tier 3 cities and create new opportunities for all. AWS supports Indonesia’s innovation agenda, inspiring businesses of all sizes to embrace the power of cloud computing technologies to increase agility, enhance cost effectiveness, and ultimately accelerate innovation.”



Alvin Tse

Country Director

“As an Internet company with smartphones and smart hardware connected by an Internet of Things (IoT) platform at its core, Xiaomi is confident that this report will foster optimism about the opportunities for digital economic strong growth in Indonesia in the years to come to be the Southeast Asia’s crown jewel.”

Endorsement from industry leaders.



Gita Wirjawan

**Chairman, Ancora Group &
Former Minister of Trade,
Republic of Indonesia**

“Rolling out the digital economy beyond the metropolitans is essential, especially understanding those cities’ untapped opportunities. This is also necessary for ensuring digital inclusivity, especially in Indonesia, where its Gini ratio remains high in the past year. Although digital growth and adoption are the potent means to increase access to financial, education, health, or other goods and services, focusing only on the metropolitan areas risks the future by expanding the disparity between the urban and the rural. Thus, prioritizing empowerment in the non-metropolitans, mentioned in this report as tier 2 and tier 3 cities, is highly desirable for Indonesia’s best-possible endgame.”

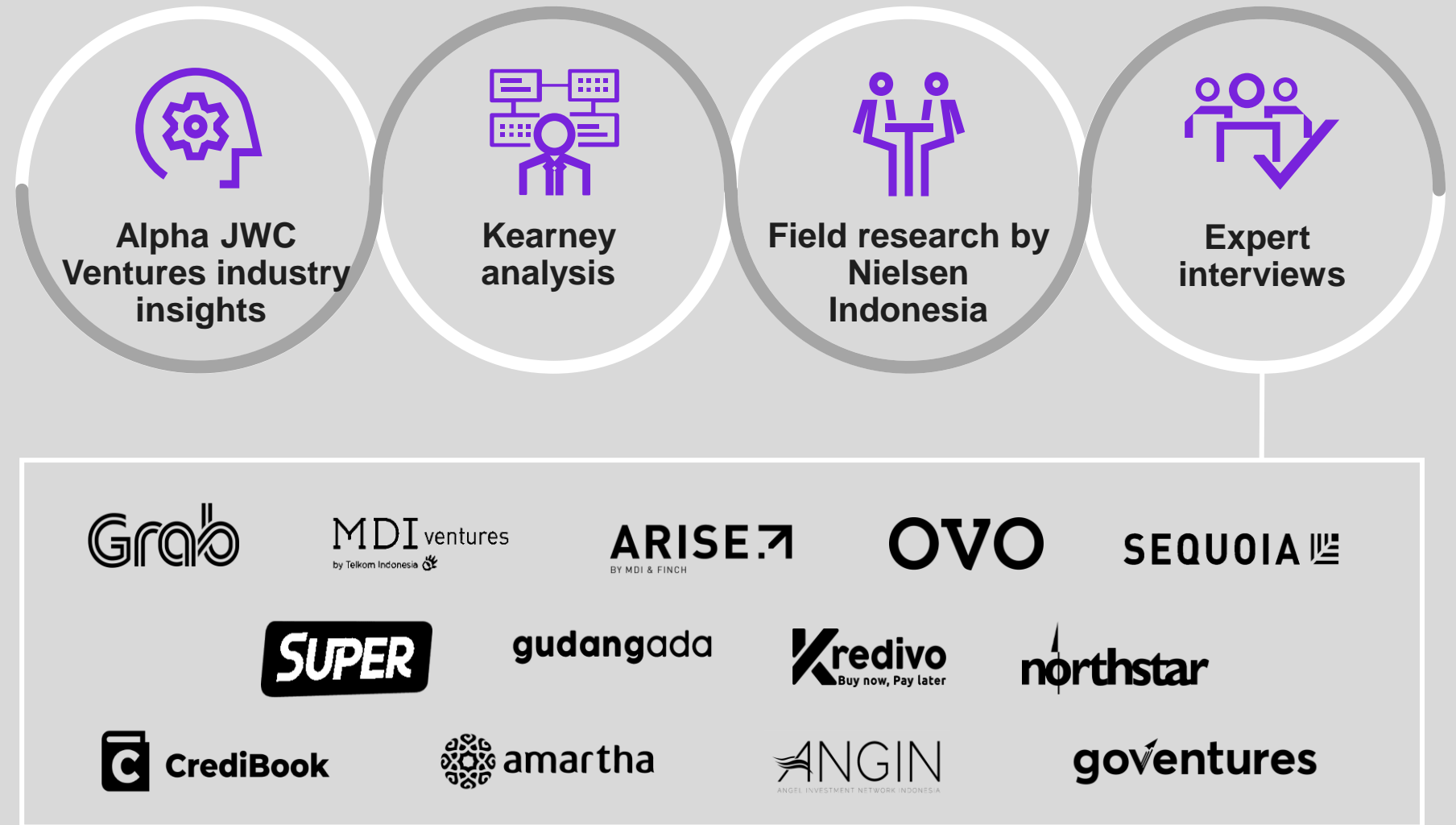
M. Chatib Basri

**Senior economist & Former
Minister of Finance, Republic of
Indonesia**

“Unlocking the next wave of digital growth: beyond metropolitan Indonesia is a timely, comprehensive analysis of the digital sector in Indonesia. This report takes us through the country’s digital transformation. It’s a commendable report that researchers and policymakers should read, especially when the role of the digital economy is getting more important. It is a stupendous work.”



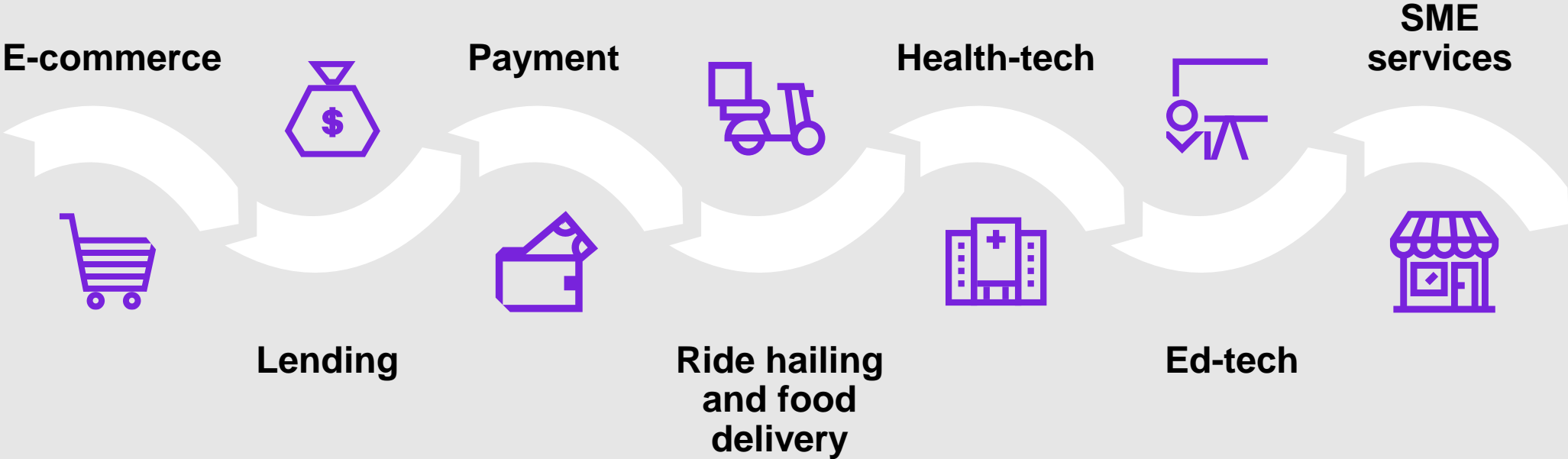
Research methodology.



We collected quantitative and qualitative data with stratified sampling through FGD and in-depth interviews with consumers and multiple industry stakeholders in 13 Tier 2 and Tier 3 cities; and through phone surveys in 23 cities (n=2100+ for end consumers and n=1100 for retailers). Data gathering was commissioned to and conducted by Nielsen Indonesia, while analysis stage was led by Alpha JWC and Kearney

Sector coverage.

Seven prominent sectors in the digital economy



Notes: Ride hailing includes both transport and food delivery. Business-to-business (B2B) services consist of end-to-end services for B2B (marketing and sales), logistics and shipping, supplier and vendor sourcing, inventory management, bookkeeping, payment and lending services. SME is small and medium-size enterprises.

- 1. Southeast Asia's crown jewel: Indonesia's digital opportunities**
- 2. The next wave of growth: digital beyond metropolitan Indonesia**
- 3. Up and coming: insights on key digital sectors**
- 4. Looking forward: much has been done, but much remains to be done**

Southeast Asia's crown jewel: Indonesia's digital opportunities

- 2020 was a rocky year for Indonesia with COVID-19 impacting key economic sectors. However, despite the pandemic, 2020 saw large digital investments as funding doubled to about \$4.4 billion.
- We also reaffirmed the bright prospect of the country with our interviews revealing that 80 percent of investors and start-ups have a bullish outlook for Indonesia regarding the economy bouncing back and the information and communications technology (ICT) sector continuing to grow post-pandemic.
- In short, we believe that even in light of the pandemic, the underlying economy is strong, and Indonesia remains the crown jewel of Southeast Asia's digital opportunities.
- Going into 2021, we expect the emergence of one key investment theme: the next wave of growth will be driven by non-metropolitan Indonesia.

The next wave of growth: digital beyond metropolitan Indonesia

- Our research classified Indonesia's 514 cities and regencies into four tiers: metropolitan (tier 1), rising urbanites (tier 2), slow adopters (tier 3), and rigid watchers (tier 4).
- Although the national economy is dominated by tier 1 cities, we expect tier 2 and tier 3 cities to become more important as they outpace the growth of tier 1 cities and expand their share of the national GDP by 3 to 5 percent (\$46 billion to \$77 billion) by 2030.
- Despite their strengthening economic might, tier 2 and tier 3 cities are three to five years behind tier 1 cities when it comes to digital adoption. Our correlation is based on survey output: more than 80 percent of the population in tier 2 and 3 cities are digital laggards and the barriers that they reported from doing online activities. Much remains to be done before these cities catch up.
- However, we believe there will be a large prize as the tier 2 and tier 3 digital economy is expected to grow by about 5x by 2025. Investors and start-ups could also expect help from macro tailwinds.

Up and coming: insights on key digital sectors

Our analysis reveals several growth patterns in the B2C sectors going into 2025:

- **Poised for mass adoption.** Sectors such as e-commerce, payments, and lending will be close to mass adoption – growing 30 to 50 percent CAGR as higher proportion of population in tier 2 and tier 3 cities start participating in the activities.
- **Nascent.** Some sectors such as ed-tech and health-tech are expected to grow about 4x of the 2020 baseline and even outpace the growth of mass adoption sectors. Going into 2025, nascent sectors will have laid a strong foundation for continued growth beyond five years.
- **Constrained.** However, we see ride hailing and food delivery experiencing more modest growth of about 27 to 30 percent CAGR as people continue to prefer their own transportation methods.

We also note the exciting opportunities in SME services. With at least 50 to 90 percent of micro, small, and medium enterprises (MSMEs) not adopting digital solutions, there is a wealth of untapped potential in digitalizing MSMEs. Given the market's large potential, it is no surprise that competition is heating up with social media and SME services and B2C start-ups competing for dominance.

Based on these observation, we expect that about three unicorns will emerge from e-commerce and lending on the back of the growth of the tier 2 and tier 3 cities.

Looking forward: much has been done, much remains to be done

- The past five years saw great progress on the regulatory and ecosystem front. However, our interviews reveal that much remains to be done.
- In the coming five years, key imperatives in infrastructure, talent, consumer education, and access to capital will have to be fulfilled to enable the Indonesian digital ecosystem to flourish and become one of the world's most vibrant ecosystems.

1. Southeast Asia's crown jewel: Indonesia's digital opportunities

- A. **Solid foundation:** the current state of the economy and digital in Indonesia
- B. **Bright outlook:** investors and start-ups on Indonesia beyond the pandemic
- C. **Growing stronger:** key growth themes for 2021 and beyond



Indonesia is well-positioned to be the next digital hub in Southeast Asia.

Indonesia's economic profile

GDP per capita

\$4,100

- Indonesia is the largest Southeast Asian economy and the 16th largest economy in the world.

Annual GDP growth

5.0%

- Nominal GDP is rising and forecasted to continue on an upward trajectory at 5% CAGR.

Population under 30 years old

51%

- The population is growing and is predominately young, with more than half of the population younger than 30 years old.

Internet users

197
million

- The number of Internet users is expected to grow about 5% year over year to reach 250 million users by 2025.

Investment size

\$4.4
billion

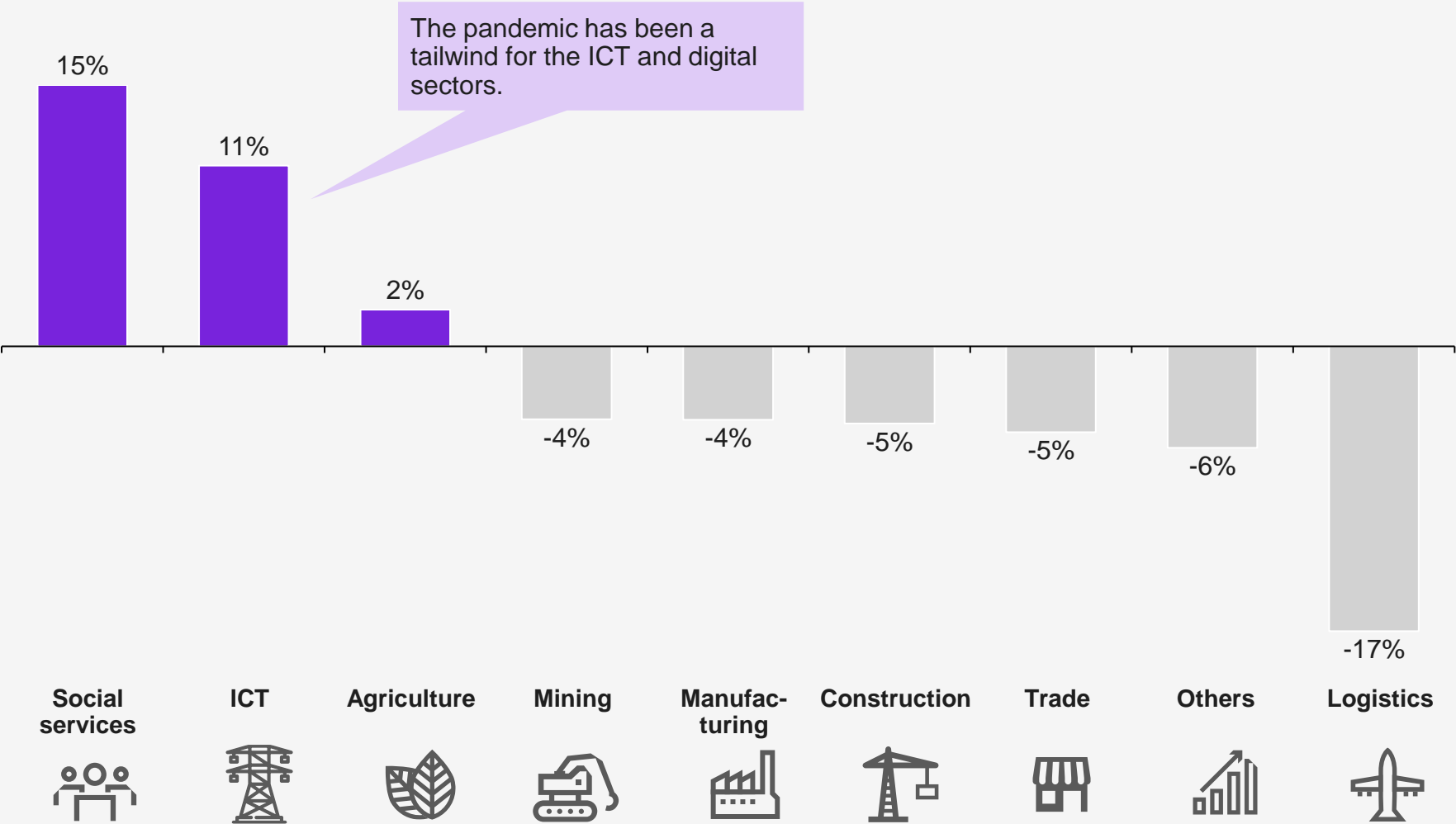
- Indonesia has seen increasing investment values, reaching 2.1 billion in 2019 and growing by more than 2x to \$4.4 billion in 2020.

Accelerated digitalization has been driven by increased Internet penetration, rising purchasing power, and infrastructure development – making Indonesia an emerging digital hub.

A. Solid foundation

Even as many sectors were adversely impacted by COVID, ICT has seen a boost .

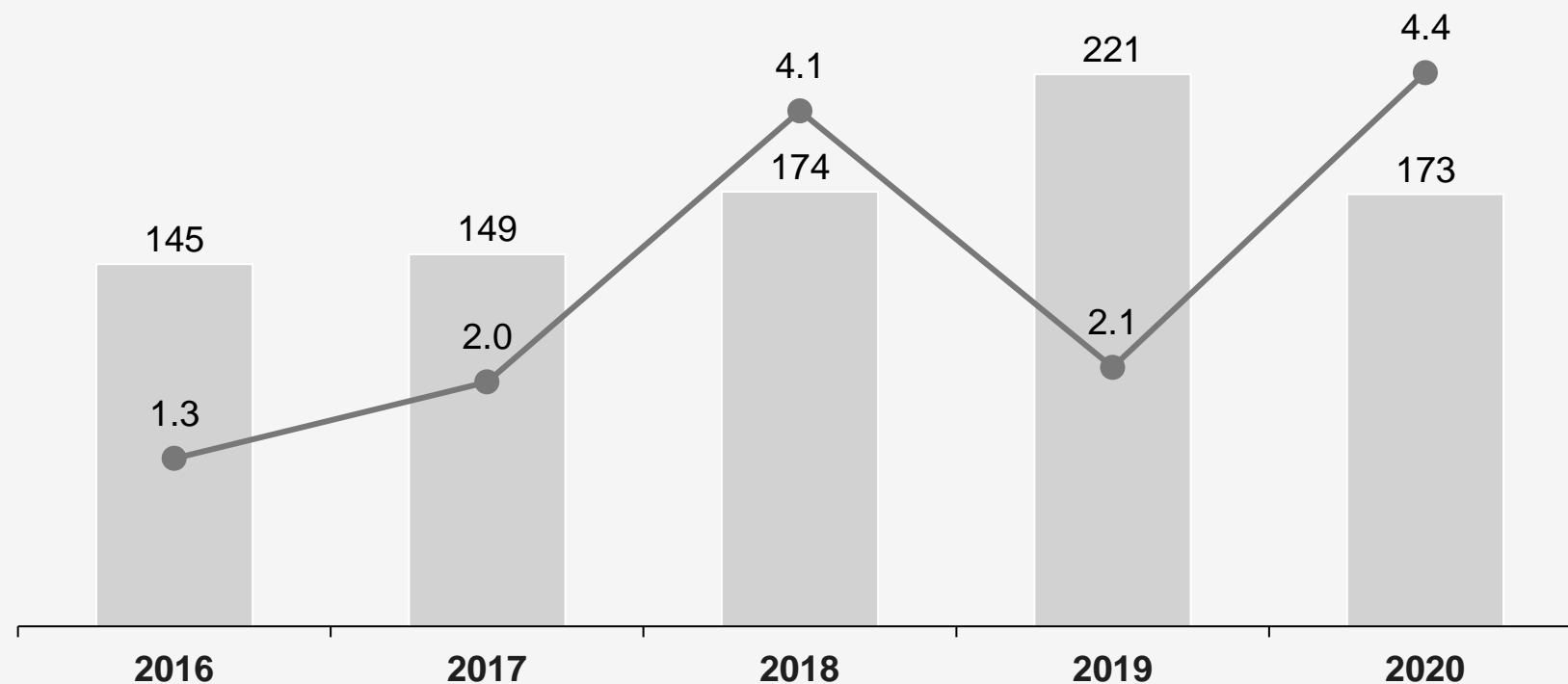
Indonesia’s economic growth by sector
(Year-on-year, Q3, % change)



A. Solid foundation

Note: ICT is information and communication technology.
Source: BPS; Kearney analysis

Digital investments in Indonesia more than doubled in 2020.



● Total investment value (\$ billion)
 ■ Total number of deals

Average deal value (\$ million)

18.9

31.7

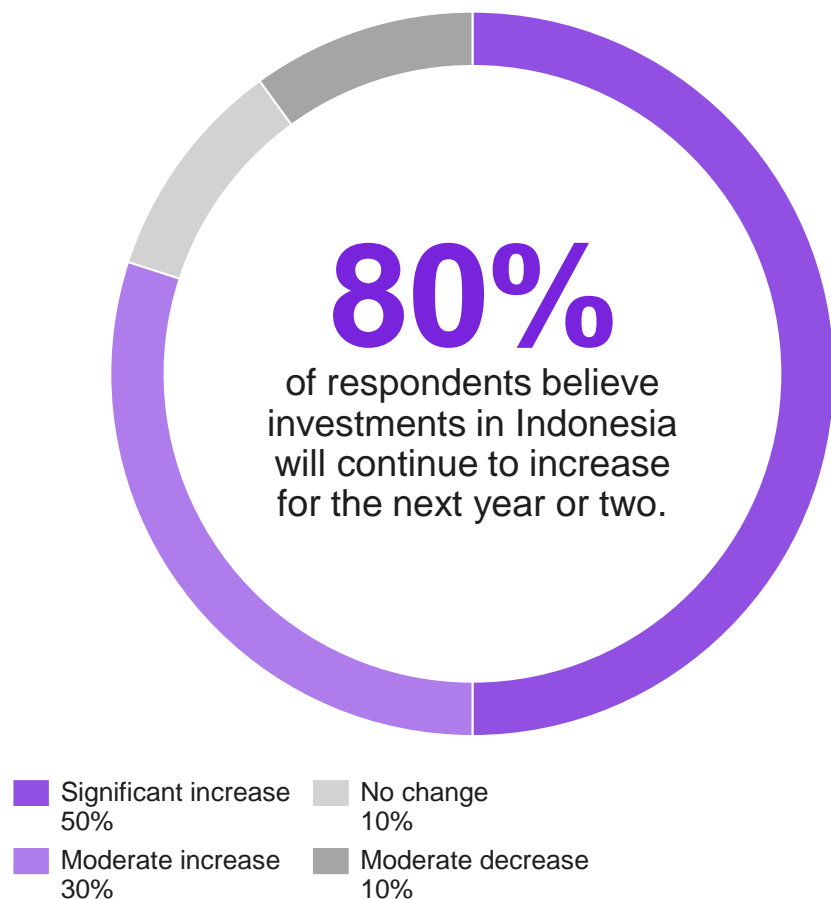
55.0

18.0

58.3

A. Solid foundation

Unfazed by the pandemic, about 80% of respondents are largely bullish about the Indonesian market.



B. Bright outlook

Key insights from interviews



Macroeconomic development, the level of innovation, and availability of quality founders are top priorities in determining investments.



The government has been putting a significant effort into boosting the tier 2 and tier 3 start-up ecosystem.



COVID has spurred innovations and accelerated digital adoptions.



Some investors are still cautious because of COVID-induced challenges, such as restricted travel, which is impacting due diligence activities.



Investor outlook indicates higher growth from regions outside of Java post-pandemic.



Dry powder has not been used to its full potential in 2020 and will likely be utilized once the market is reshaped.

Investors and start-ups can expect a new wave of growth beyond non-metropolitan areas.

*“There is **high untapped potential in tier 2/3 cities**. Even though the effort is large, the result can also be rewarding.”*

Chief executive officer,
SME SaaS

*“The growth expectation in the next one to two years will be outside of Java: **50% of growth will be outside of Java**.”*

Chief commercial officer,
lending fintech

*“We focus outside of Jakarta. Jakarta is a red ocean, and the **rest of Indonesia is still a blue-ocean market**.”*

Chief executive officer,
social commerce

Investors and start-ups on growth beyond metropolitan areas

*“We are looking to serve the underserved, looking more at **tier 2 and 3 cities as they have higher potential and a larger market**.”*

VP investments,
corporate venture capital

*“Consumers in **tier 2/3 cities are rapidly digitalizing**. The digital infra has facilitated in people becoming digital very fast.”*

VP investments,
corporate venture capital

*“There is a clear trend that **demand is going to increase in tier 2/3 cities**, especially as digital penetration increases.”*

Chief executive officer,
lending fintech

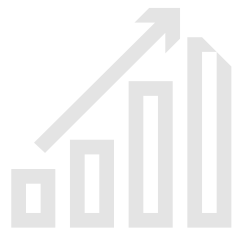
C. Growing stronger

Our assertions on digital beyond metropolitan Indonesia.

Digital economies in tier 2 and tier 3 cities will grow **by 5x** on back of efforts by start-ups and several macro tailwinds.



E-commerce, lending, and payments will be the **biggest categories**, while nascent sectors such as ed-tech and health-tech will see **significant growth from low baseline**.



Two to three **potential unicorns from of e-commerce, lending and SME services** will emerge in the next five years on back of the growth of tier 2 and tier 3 cities.



Six imperatives in infrastructure, talent development, access to capital, and consumer education will be crucial to winning the global digital race.




2. Next wave of growth digital beyond metropolitan Indonesia


- A. **No second fiddle:** growth prospect beyond Metropolitan Indonesia
- B. **Know your customers:** habits and way of life in Non-Metropolitan Indonesia
- C. **Untapped markets:** opportunities and challenges in Non-Metropolitan Indonesia
- D. **Forces at work:** macro tailwinds for start-ups and investors





We classified Indonesia’s cities and regencies into four tiers based on socioeconomic criteria.


Scoring parameters and weight

 Expenditure per capita
35%

 Population size
25%

 Internet penetration
20%

 Province GDP growth
10%

 Population density
10%

A. No second fiddle

Four archetypes of Indonesian cities and regencies



15
cities

Greater Jakarta Area,
Surabaya, and Bandung

**Metropolitans
(tier 1)**

– **Densely populated cities** that have significant economic, cultural, and political influence



76
cities

Semarang,
Makassar, and
Denpasar

**Rising urbanites
(tier 2)**

– Cities with a growing number of middle-class consumers, developing digital and logistical infrastructure, which show **promising growth opportunities for digital development**



101
cities

Magelang,
Prabumulih, and
Bangli

**Slow adopters
(tier 3)**



322
cities

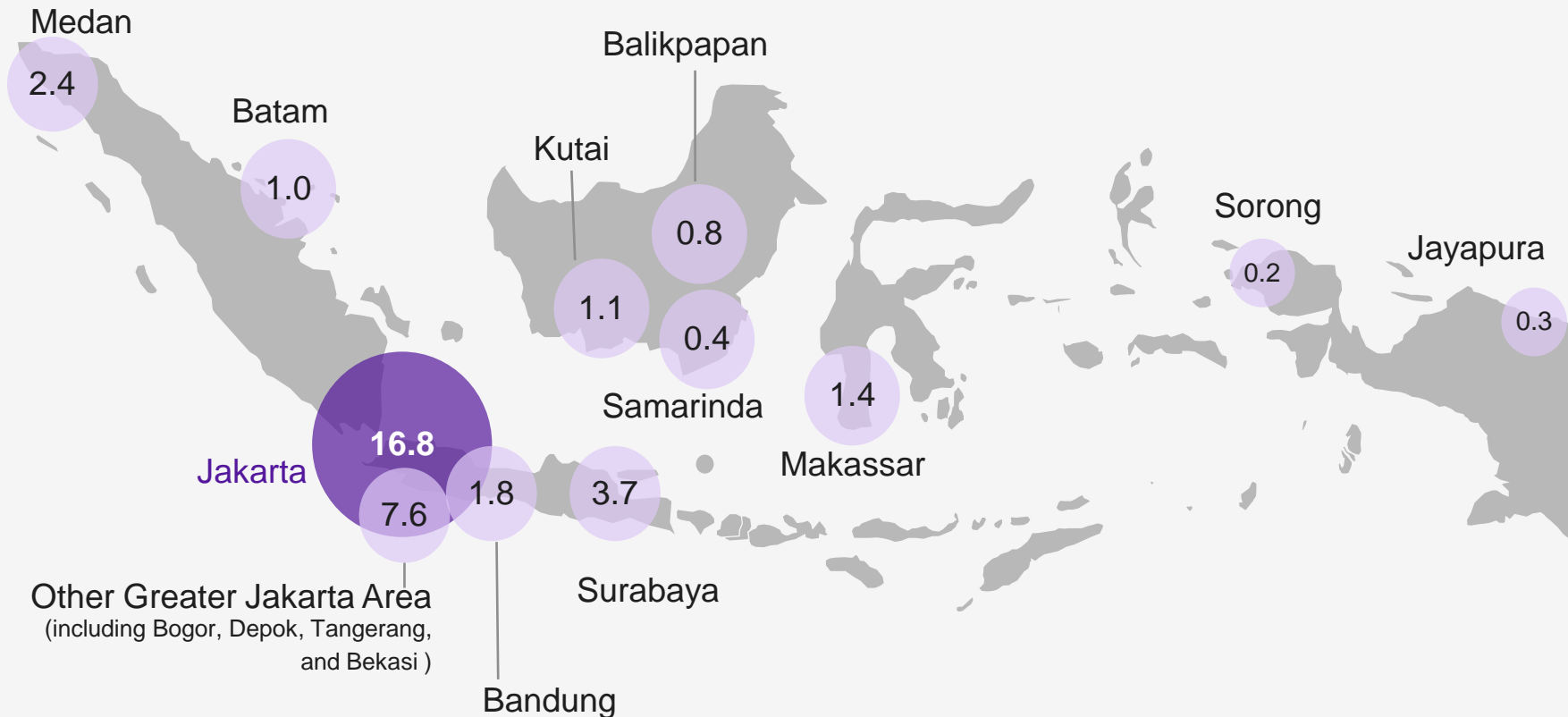
Kabupaten Jepara,
Kabupaten
Jayapura, and
Kabupaten Poso

**Rigid watchers
(tier 4)**

– **Smaller cities and regencies** with less-developed digital and logistical infrastructure

The metropolitan area of Greater Jakarta plays an outsized role in Indonesia's economy, accounting for about 24% of national GDP.

Economic contribution, selected cities (% to GDP)



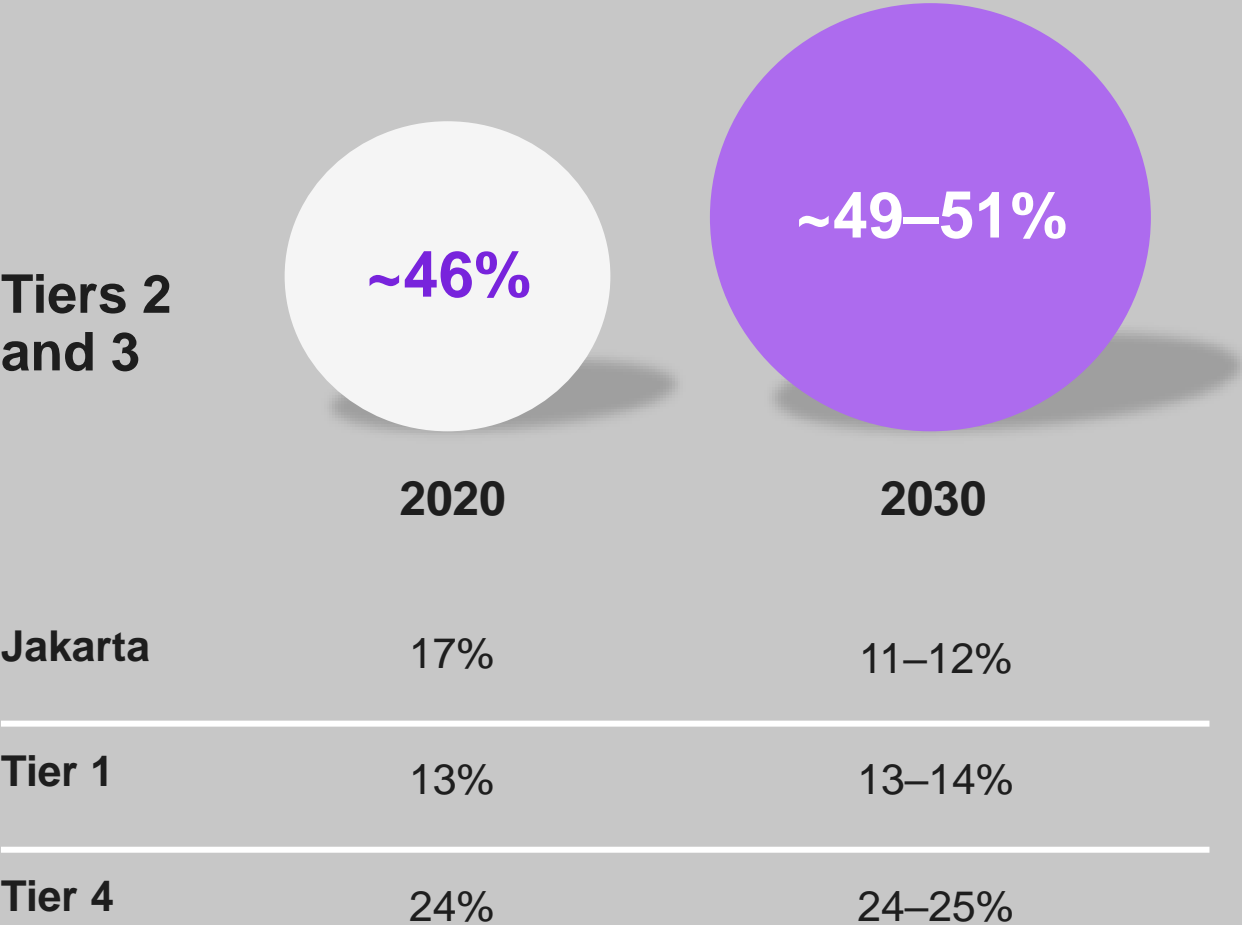
Indonesia only has one economic center for the country in Greater Jakarta. No other area comes close in economic prominence.

Given the level of economic prominence, **start-up activities and funding often start and remain centered in the Greater Jakarta area up until today.**

A. No second fiddle

However, non-metropolitan areas are growing faster and increasing in economic importance.

GDP contribution, by city tiers
(% of total GDP)



As the country grows and the government intensifies the economic diversification efforts, expect the following:

- The distribution of economic activities will be more equitable between Jakarta and other areas.
- As a result, Jakarta’s portion of GDP will decrease by 5–6% by 2030.
- Tier 2 and 3 cities will be more prominent economically, increasing the share of GDP by 3–5%.

A. No second fiddle

Notes: GDP is expected to reach about IDR 21.670 trillion by 2030 (constant 2010 method). Conversion exchange rate: \$1 = IDR 14,000
Source: Oxford Economics; Kearney analysis

We observe three types of consumers across Indonesia based on their online habits.

Types of Indonesian consumers

Early adopters



- Active in **keeping up with the latest trends**
- **More open-minded** toward technology and engaging in online activities
- Tend to become the **advocate for digital usage** among their peers and society

Average majority



- Up to date with **trends in their circle**
- Open for activities that are **popular or recommended by friends and family**
- Average majority considered as the **“real consumer” of the digital world**

Laggards



- More **cautious in following the latest trends**
- More cautious in adopting current technology, **often skeptical, and tend to distrust** technology
- **Late adopter and slow learner of the digital world**, need significant education prior to adoption



B. Know your customers













Each type of customer also has different preferences that influence their digital habits.

Habits of various types of customers

Usage intensity level:

Highest Lowest

B. Know your customers

		Early adopter 	Average majority 	Laggard 
Shopping		Has high confidence in e-commerce for shopping	Has more confidence in using online shopping	Prefers to purchase items in physical shops
Work		Uses digital to optimize work activities	Frequently uses digital to chat with and call colleagues	Rarely uses digital to chat with colleagues
Information		Relies heavily on the Internet as a main source of information	Uses TV as the main source of information	Uses TV as the main source of information
Communication		Regularly uses digital for chat and video call	Regularly uses digital for chat and video calls	Uses digital for chats but rarely uses video calls
Transport		Regularly uses online options for transportation	Uses online transportation only when urgent	Prefers to use their own transportation
Finance		Regularly uses fintech for transactions	Has yet to fully adopt fintech; frequently uses banks	Prefers to use cash for all transactions
Health		Uses online consultation for minor symptoms	Prefers physical consultation for credibility	Prefers physical medical consultations
Meal		Gets food delivered to replace eating out	Prefers to cook meals at home to reduce expenses	Prefers to cook meals at home to reduce expenses
Education		Uses ed-tech to complement schools	Not yet using online for non-formal education	Not yet using online for non-formal education

A day in the life of early adopters: digital habits ingrained in all daily activities.

B. Know your customers

What early adopters think of digital



Digital life helps make their lives easier by removing the boundaries of what can't be done.

Profile of the average majority

- Average age: 33 years
- Average monthly expenditure: about IDR 3 million
- Location: Mostly in tier 2 cities in Java

Shopping

- Are confident using **e-commerce** (similar comfort level as with physical shopping)

Work

- Regularly use **digital tools** to work remotely, especially during the pandemic
- Optimize social media for work (such as marketing)

Information

- Rely heavily on the **Internet** as the main source of information and entertainment
- Active YouTube users, such as for subscribing to channels

Communication

- Regularly have **video calls** with friends and family

Transport

- Regularly use **online transportation** and delivery, especially motorcycles

Finance

- Regularly use **m-banking** for transactions, such as to purchase electricity
- Started to use online lending for small transactions, such as phone credits

Apps used¹:



1. Apps used from most frequent to less frequent
2. Indicative profile due to low sample number for early adopters
Source: Nielsen; Kearney analysis

A day in the life of the average majority: adopting digital habits, but only for select activities.

B. Know your customers

What the average majority think of digital



“Old habits die hard. I can use online, but I still prefer the traditional methods.”



Profile of the average majority

- Average age: 29 years
- Average monthly expenditure: about IDR 3 million
- Location: Spread across tier 2 cities in Java and outside Java

Shopping

- Confident in online shopping
- Prefer shopping online only **for items that are not available in physical stores**

Work

- **Do not work remotely as much** as early adopters
- Frequently **use digital tools to chat and call** with colleagues and client

Information

- **Use TV as the main source** of information and entertainment
- Limit digital use to **hobby-related information**

Communication

- **Regularly use video calls** with friends and family

Transport

- **Rarely use** online transportation except when there is no alternative
- Still prefer to **use their own transportation** rather than ride-hailing

Finance

- **Yet to adopt** m-banking and e-money
- Still prefer to **conduct financial transactions via banks or ATMs**

Apps used¹:





¹ Apps used from most frequent to less frequent
Sources: Nielsen; Kearney analysis


A day in the life of laggards: still not adopting digital, except for communication.

B. Know your customers

What laggards think of digital



“Digital life is expensive and full of uncertainty and requires a steep learning curve.”



Profile of laggards

- Average age: 35 years
- Average monthly expenditure: IDR 2.8 million
- Location: Spread across tier 3 cities

Shopping

- Have low confidence in online shopping and still prefer to **purchase items in physical shops**

Work

- Limit digital use to chatting with clients and co-workers

Information

- Use TV as the main **source** of information and entertainment; **rarely use the Internet** for information and entertainment

Communication

- Use digital for **chatting**, but rarely use video calls

Transport

- **Avoid using online transportation** and prefer to use their own transportation

Finance

- Distrust digital financial services and still **prefer cash transactions**

Apps used¹:



← (Not active) →



← (Not active) →

¹ Apps used from most frequent to less frequent
Sources: Nielsen; Kearney analysis

Life is different for Indonesian customers based on where they live.

Different income, infrastructure, transportation, and financial habits **lead to different digital behaviors.**

Life in metropolitan cities (tier 1) is much **more conducive to digital activities**: better connections and higher income to support digital spending.

B. Know your customers

Life in metropolitan cities (tier 1)

- Greater variety of job profiles (blue collar, white collar, creative, and administrative)
- Higher income and expenditure



Income

- Better Internet connections
- More accurate geolocations



Infrastructure

- Live in satellite cities
- Bad traffic and longer travel time
- Inadequate public transportation



Transport

- High use of bank account as a “wallet”
- More familiar with financial services
- Common use of lending and credit from a bank



Financial habits

Life in other cities (tier 2 and tier 3)

- Limited variety of job profiles (such as farmers and owners of small shops)
- Lower income and expenditure

- Some “blank spots” without good connections
- Less accurate geolocations

- Live where they work
- Less traffic and shorter travel time
- Adequate public transportation

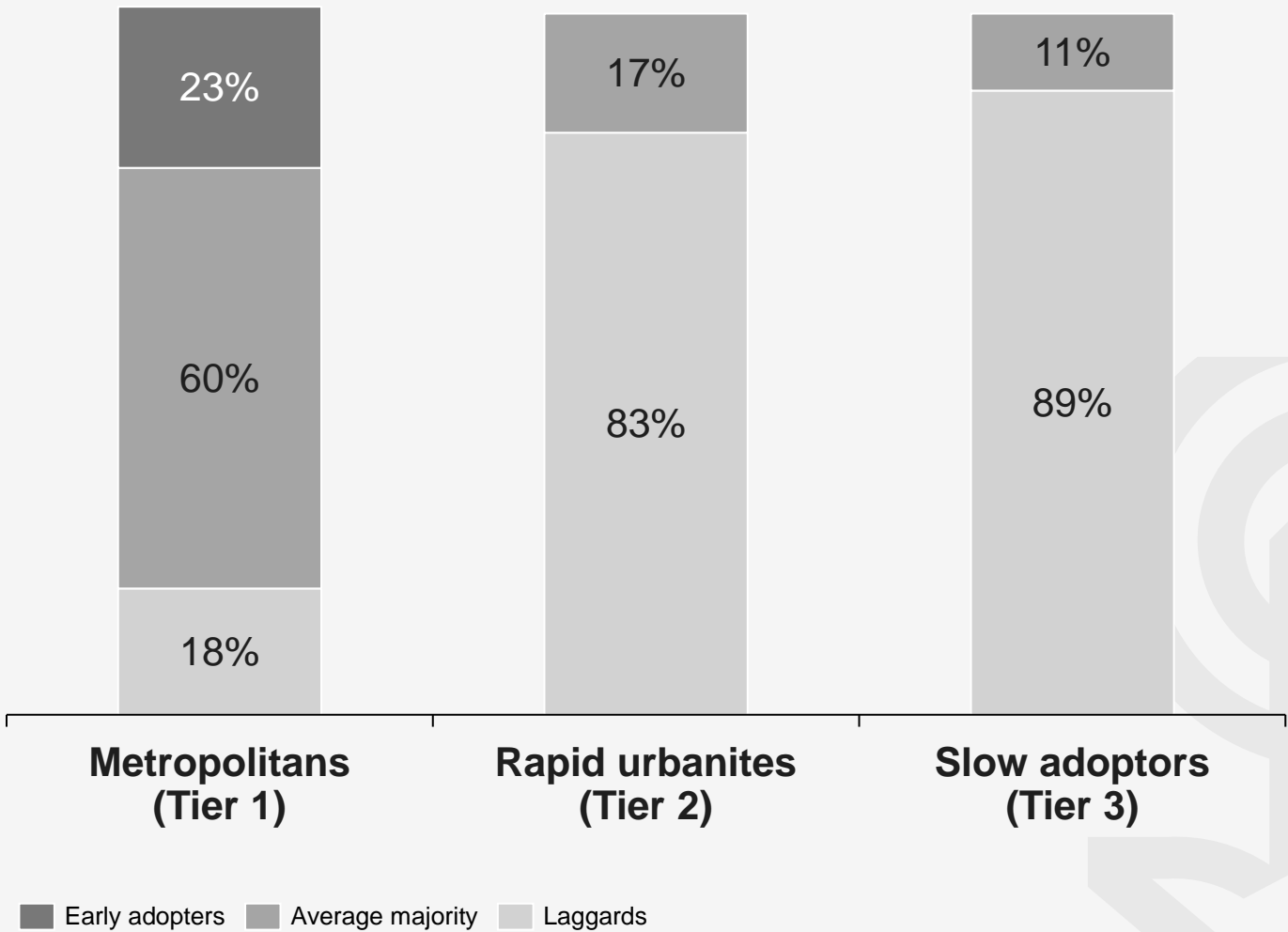
- Use of bank account as “savings”
- Less familiar with financial services
- Generally avoid lending and credit

More than 80% of the population in non-metropolitan areas are laggards when it comes to adopting technology.

Several factors are affecting digital behaviors, including occupation, income, and education – all of which are more conducive to digital adoption in bigger and higher-tier cities.

B. Know your customers

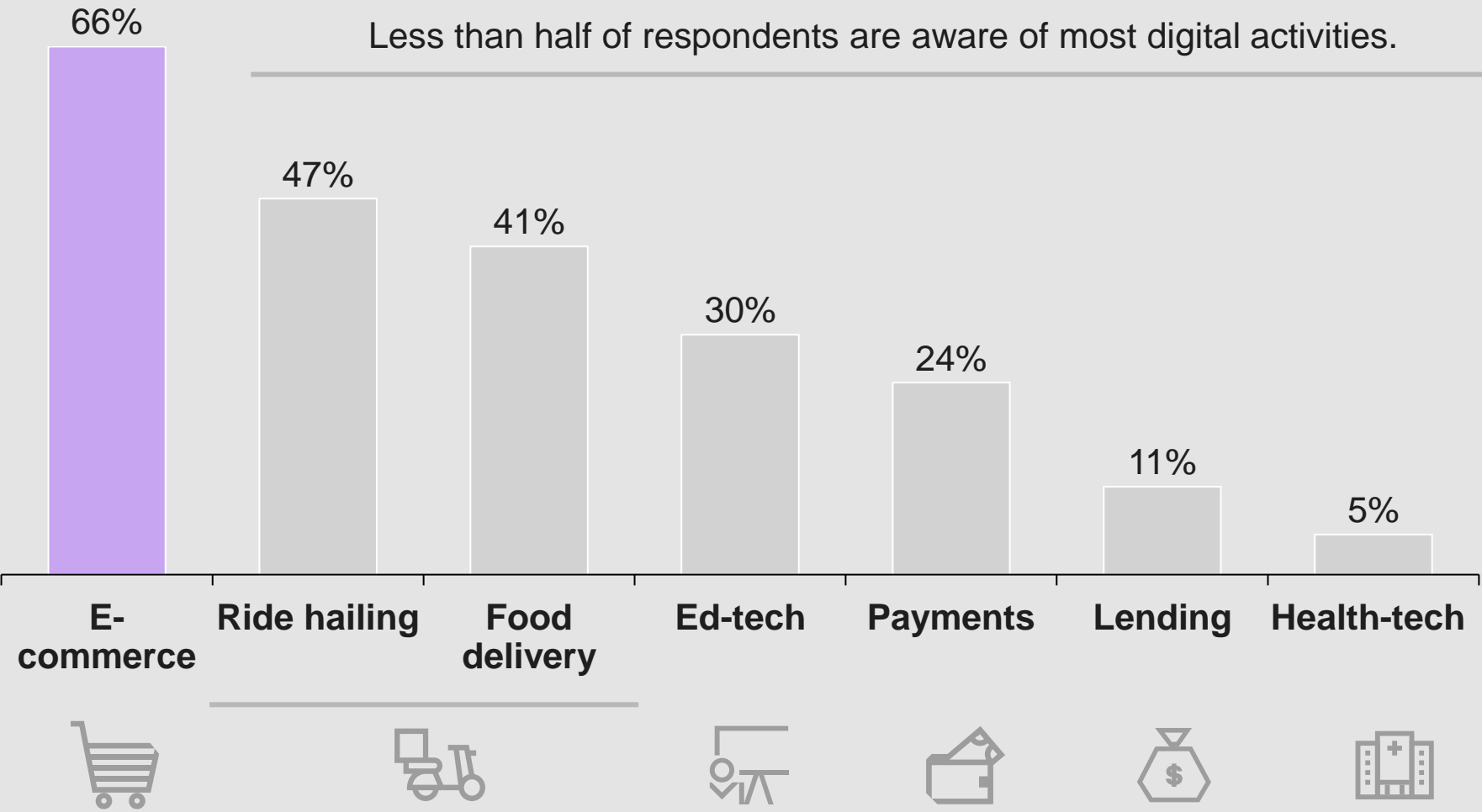
Consumer proportion, by city category
(% to total)



Source: Nielsen; Kearney analysis

The dominance of laggards in tier 2 and tier 3 cities explains why less than 50% of respondents are aware of most digital activities.

Awareness incidence of online activities by sectors
(% of consumers in tier 2 and tier 3 cities)

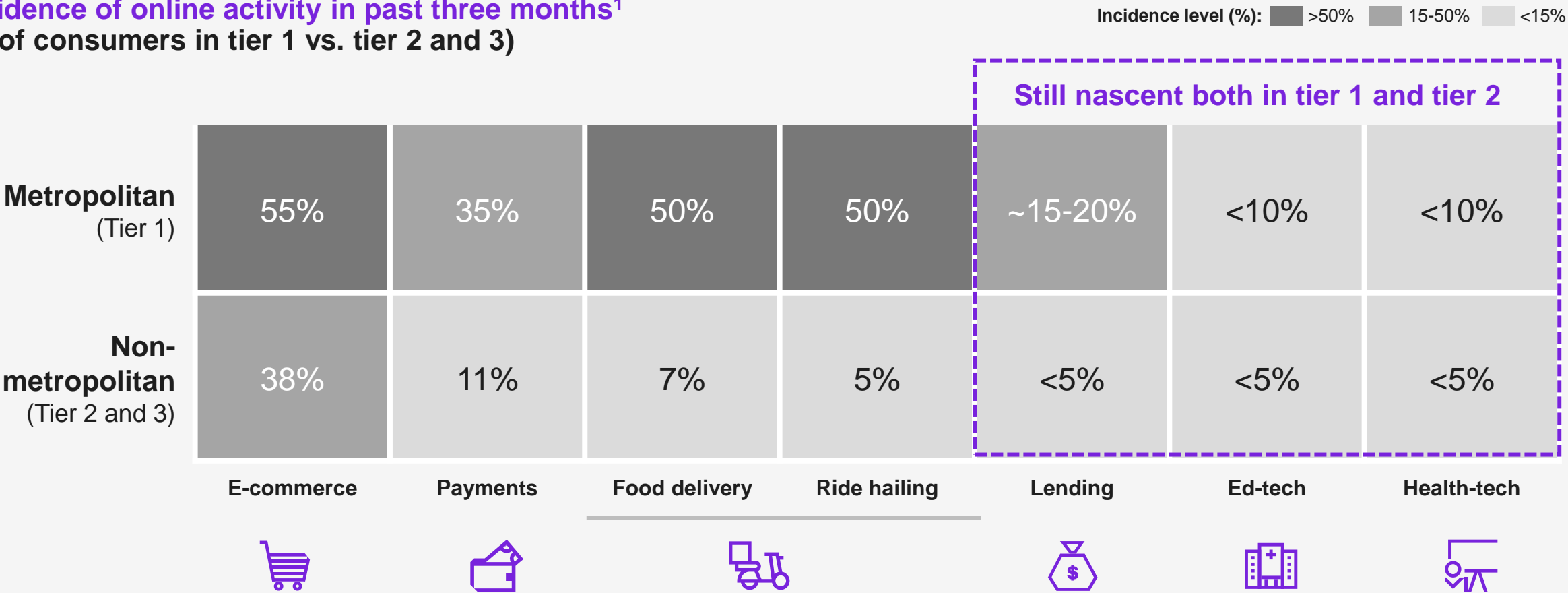


C. Untapped markets

Source: Nielsen; Kearney analysis

... as well as a low level of digital activities in all sectors.

Incidence of online activity in past three months¹
(% of consumers in tier 1 vs. tier 2 and 3)



C. Untapped markets

Note: Tier 1 is based off Jakarta; definition for e-commerce and payment slightly differ between Jakarta and tier 2 and tier 3.
Source: Nielsen; Kearney analysis

Digital in tier 2 and tier 3 cities is just starting out and is four to five years behind the adoption in tier 1 cities.

Current state

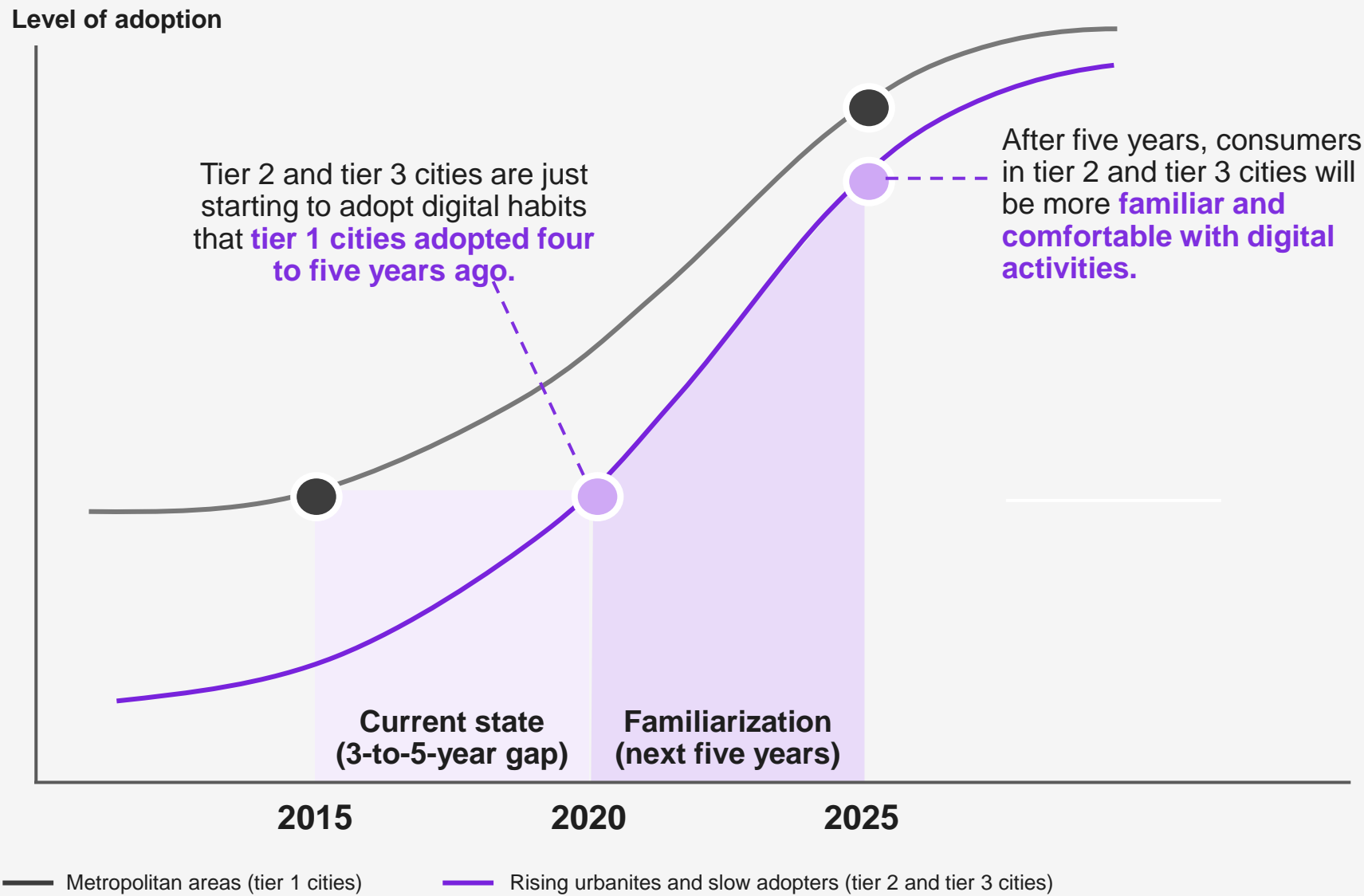
Most consumers in tier 2 and tier 3 cities are **still unfamiliar with digital behaviors**, which results in low adoption of digital behaviors.

Next five years

The coming five years will be a **familiarization period** where significant education and marketing activities need to happen to develop digital behaviors.

C. Untapped markets

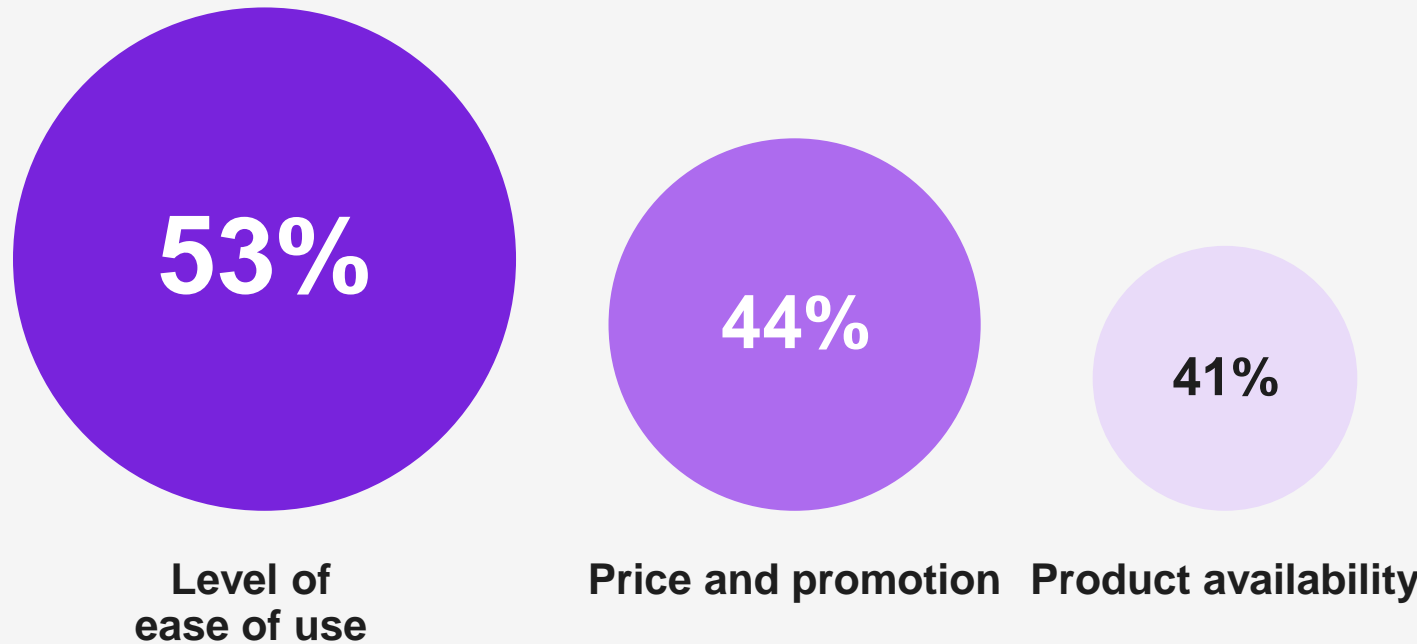
Digital adoption curve



Lowering the barriers to adoption will be key to unlocking Indonesia's large potential.

Overall barriers to adoption

(% of respondents who did not do online activities in tier 2 and tier 3 cities)



C. Untapped markets

Level of ease of use

- Most of those not participating in online transactions lack familiarity and understanding about using apps or using the Internet in general.

Price and promotion

- There is a perception of online activities being more expensive than offline because of administrative and shipping fees and availability of cheaper offline substitutes.

Product availability

- There are concerns about product quality because of the inability to touch and feel as well as difficulty in the availability of items.

Start-up and investors also need to consider region-specific barriers.

Ranking barriers of adoptions by geography

	Java		Non-Java
A	1 Ease of use	1	Security
	2 Price and promotion	2	Ease of Use
	3 Item availability	3	Shipment
	4 Payments	4	Payments
	5 Shipment	5	Price and promotion
	6 Security	6	Item availability
	7 Others	7	Others
		B	

C. Untapped markets

Regional nuances on barriers

- A Convenience is key in Java**
- Consumers in Java are more concerned with ease of use, price and promotion, and item availability.
 - The above barriers suggest that convenience is more important in Java, where digital habits are more widespread.
- B Getting basic right is crucial outside of Java**
- Non-Java consumers have very different concerns, especially security, ease of use, and shipment.
 - As digital habits are still being formed, addressing the fundamentals of digital is important outside of Java.

Investors and start-ups need a customized approach to nurture their tier 2 and tier 3 markets.

Tier 2 and tier 3 markets behave differently, with behaviors that are three to five years behind those of tier 1 markets.

Within tier 2 and tier 3 markets, Java and non-Java markets behave differently. Convenience is more important in Java, while getting the basics right is more important outside of Java.

C. Untapped markets

Key implications for investors and start-ups



Focus on getting the basics right

- Basic business building blocks such as having user-friendly apps and websites, reliable delivery and logistics networks, and active marketing operations go a long way in establishing credibility.



A nuanced and localized approach is key to awareness

- Different regions have different barriers to adoption. Non-Java regions are more concerned about infra-based issues, while Java is more price-sensitive. A different but focused approach is essential for tier 2 and tier 3 cities.



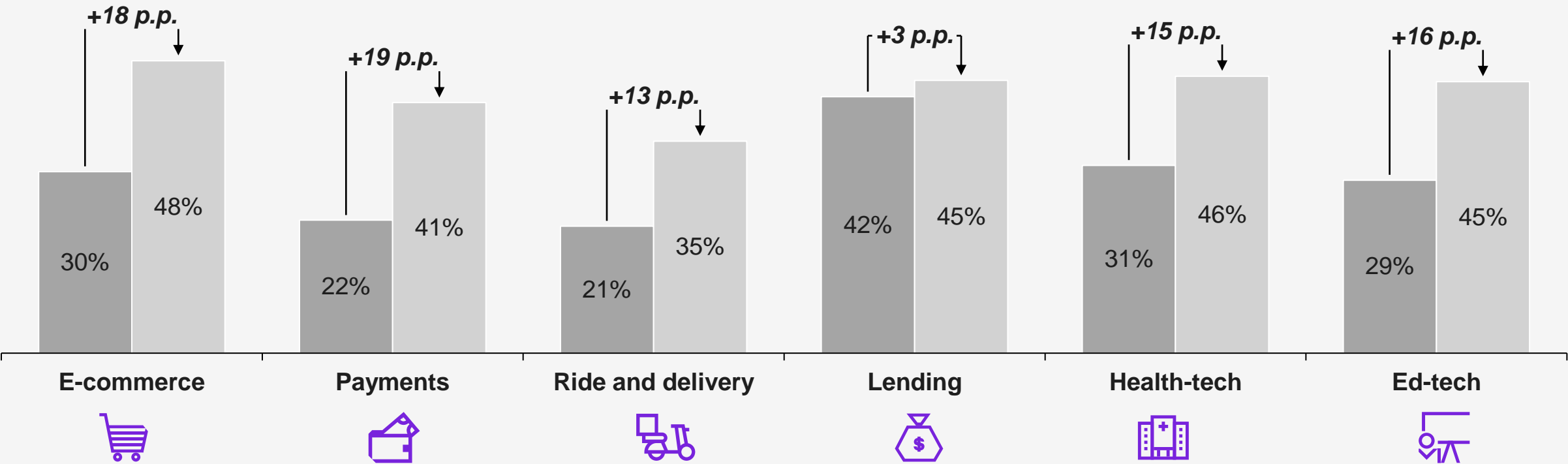
Invest for the long term

- Rolling out new infrastructure and raising awareness in tier 2 and tier 3 cities requires a long-term view of the market. Investors and start-ups need to play the long game in order to succeed.

By 2025, tier 2 and tier 3 cities will exert their economic power and be key contributors with a larger share of Indonesia's digital economy.

Tier 2 and tier 3 cities proportion to the digital economy (% of total)

2020 2025f

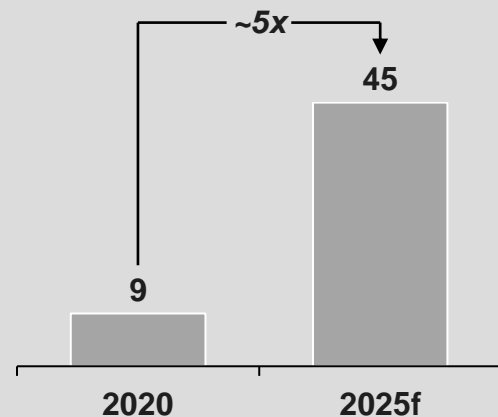


C. Untapped markets

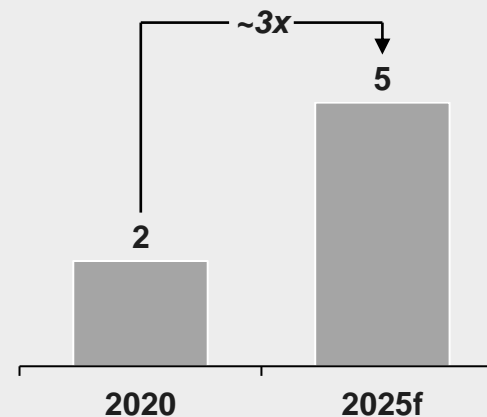
Note: Market size for health-tech and ed-tech are only for the B2C (direct-to-consumer) segment.
Source: Alpha JWC; Kearney analysis

Investors and start-ups that keep eyes on the prize stand to dominate an Internet economy that will grow 3–4x by 2025.

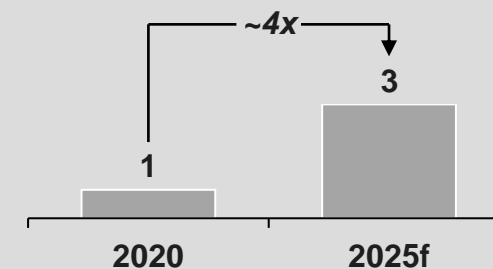
E-commerce (GMV)



Ride hailing and delivery (GMV)

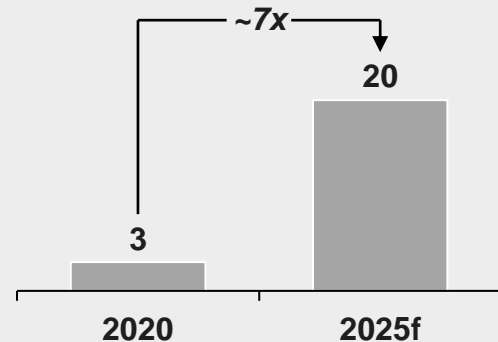


Health-tech (GMV)

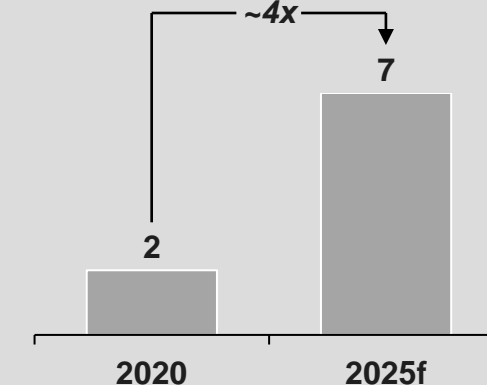


Indonesia tier 2 and tier 3 Internet economy (\$ billion)

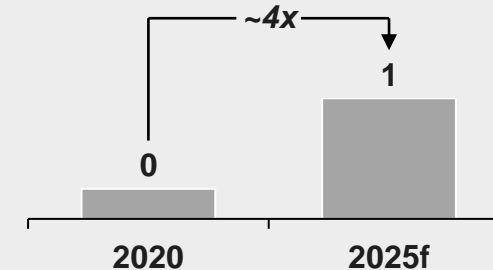
Payments (GTV)



Lending (loan disbursed)



Ed-tech (GMV)



C. Untapped markets

Note: Market size for health-tech and ed-tech are only for the B2C (direct-to-consumer) segment.
Source: Alpha JWC; Kearney analysis

Several macro factors will act as tailwinds for investors and start-ups.

Tailwinds for start-ups and investors



COVID has accelerated digital adoption

- The pandemic greatly accelerated digital adoption.
- Digital habits formed during the pandemic are here to stay: 16% of respondents say they are more likely to use tech because of the pandemic.
- COVID turbocharged awareness: about 20% of respondents became aware of digital activities in several sectors during the lockdown.



Tier 1 cities are reaching maturity

- Tier 1 cities such as Jakarta are fast becoming a red ocean as competition intensifies and consumers reach maturity.
- Incumbent and new start-ups are expanding to tier 2 and tier 3 cities.
- Although their expansion might act as competition, it also validates the digital potential of tier 2 and tier 3 cities.

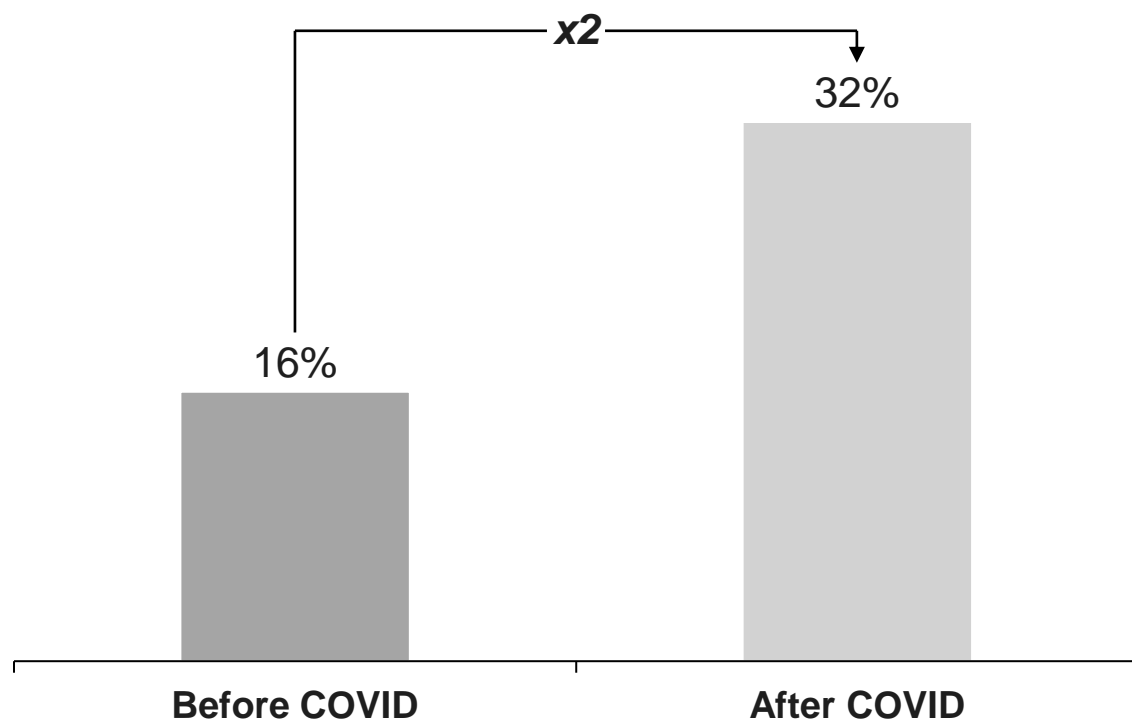


The government is pushing to digitalize tier 2 and tier 3 cities

- After the first wave of growth in tier 1 cities, the Indonesian government is no longer a stranger to start-up potential.
- There has been a major government push to encourage digitalization of tier 2 and tier 3 cities, including expanding Internet infrastructure and investing in physical infrastructure.

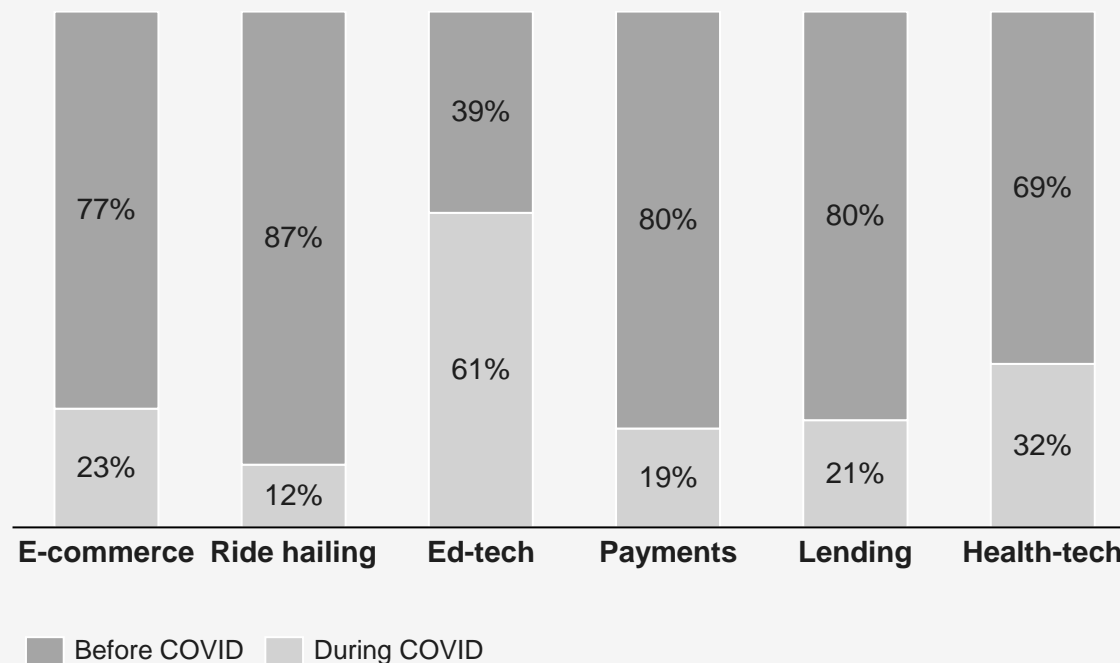
COVID has accelerated the adoption and awareness of online activities.

Likely to engage in online activities (% of respondents)

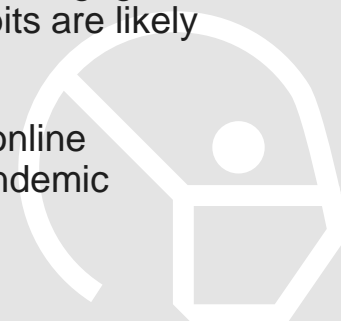


D. Forces at work

Awareness of online activities (% of respondents who are aware of activities)



- After COVID, 2x more people are more likely to engage in online activities, and the new-found digital habits are likely to stay even after the pandemic.
- About 20% of respondents who are aware of online activities became aware after COVID. The pandemic turbocharged awareness of online activities.



Start-ups are expanding to tier 2 and tier 3 cities as tier 1 cities reach maturity in certain segments.

Not exhaustive

D. Forces at work



Tier 1 start-ups are expanding aggressively to tier 2 and tier 3 cities

- As of July, Mitra Bukalapak claimed to have **5 million warungs** in its ecosystem, focused on tier 2 and tier 3 cities.
- Tokopedia is **expanding to rural villages** and signed a memorandum of understanding with the West Java government.
- GrabKios started to **establish a presence in about 500 cities** and regencies to digitalize warungs.



Tier 2 and tier 3 focused start-ups mushroomed over the past few years

- **Credibook:** Credibook is a digital debt management start-up for SMEs on second and third-tier cities in Indonesia.
- **Super:** Super is a social commerce platform that enables community leaders in tier 2 and tier 3 cities to be retailers in the community.
- **Evermos:** Evermos is a social commerce platform that addresses the everyday needs for Indonesian Muslims largely in tier 2 and tier 3 cities.



Funding for tier 2 and tier 3 focused start-ups increased over the past two years

- **Payfazz** received \$53 million in Series B round.
- **GudangAda** received \$36 million for Seed & Series A round.
- **Warung Pintar** received \$27.5 million in Series B round.
- **Amartha** received \$18 million in Series B round.
- **Tanihub** received \$17 million in Series A round.

The government has also been proactive in pushing digital in tier 2 and tier 3 cities.

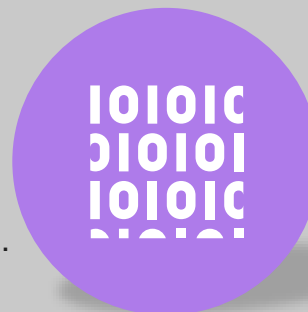
The government has been much more proactive in pushing digital development, and support is more readily available than it was five years ago.

D. Forces at work

Government support for digital development

Digital infrastructure

Expansion of digital infrastructure—such as fiber optic expansion, 4G expansion, and increased R&D support—help to accelerate adoption.



Physical infrastructure

Construction of physical infrastructure—such as the Trans-Sumatra Highway, industrial parks, and ports—will help in increasing operational efficiency.



Regulatory infrastructure

A proactive regulatory framework—such as the deliberation of personal data protection bill and OJK fintech regulations—improve consumer confidence in online activities.



Talent and capability

There is a renewed push on human capital development pinpointed by the current government administration, such as teacher competency development and applying ed-tech in a formal setting.



Access to capital

Ministry of Finance Regulation No. 53/2020 provided clarity on the start-ups grant from the government, and discussion on tax incentives for local venture capitalists will increase access to capital.



Consumer education

A government program for user education—such as the OJK–BI financial inclusion program, the MICT UMKM Go Digital, and the MOT Bangsa Buatan Indonesia—push for greater awareness about digital.



Notes: MICT is the Ministry of Information and Communication Technology; MOT is the Ministry of Trade.
Source: press research; Kearney analysis

3. Up and coming insights on key digital sectors

- A. **B2C growing fast and big:** state of B2C digital markets
- B. **SME services heating up:** state of SME services market in tier 2 and tier 3 cities
- C. **Up and coming:** our view on the up-and-coming unicorns



Fast forward to 2025: all six B2C sectors will grow under different characteristics.

Growth characteristics of B2C sectors toward 2025

Mass adoption

Largest markets by 2025



E-Commerce



Lending



Payment

Nascent

Significant growth toward 2025



Health-tech



Ed-tech

Constrained

Limited growth toward 2025



Ride hailing and food delivery

Overall, B2C markets and all sectors will **continue to grow until 2025**. However, the sectors will grow differently:

Mass adoption
Moderate growth but large market size

Nascent
Rapid growth up to 2025 from an existing low baseline

Constrained
Limited growth from the existing baseline up to 2025

A. B2C growing fast and big

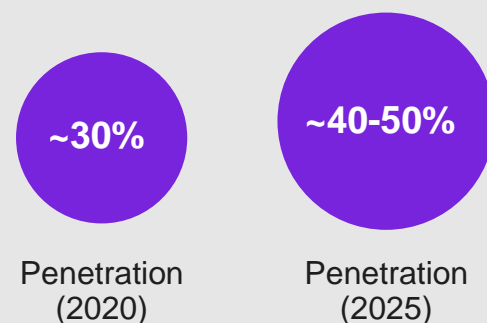
E-commerce will remain the biggest digital sector in tier 2 and tier 3 cities as adoption becomes mainstream.

E-Commerce

 Total Indonesia market (\$ billion)

A. B2C growing fast and big

E-commerce tier 2 and tier 3 cities market size (GMV in \$ billion)

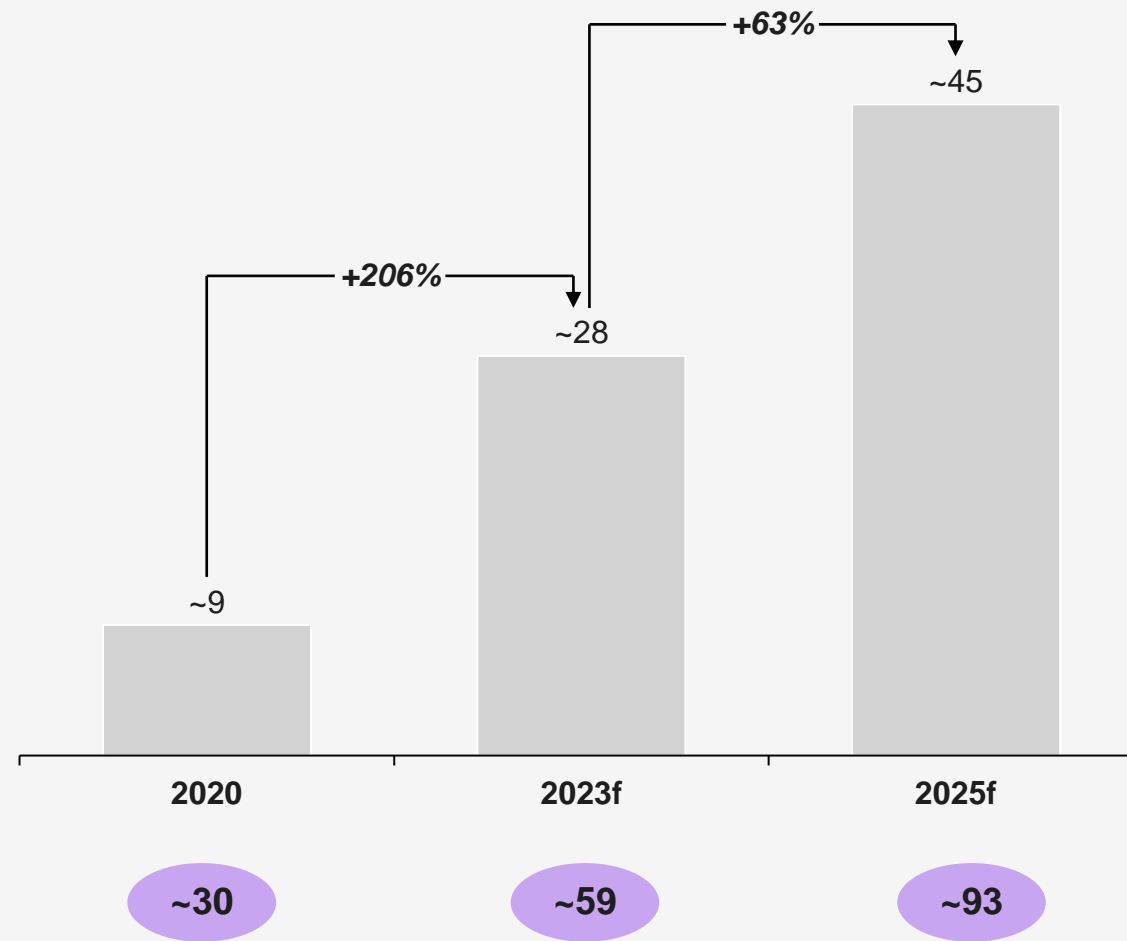


Growth on the back of mainstream adoption

- From 2020 to 2025, the population in tier 2 and tier 3 cities will be more familiar with online purchases.
- As a result, e-commerce penetration will increase in tier 2 and tier 3, and by the end of 2025, the GMV proportion will reflect the population proportion.

2020-2025 CAGR
(tier 2 and tier 3 market)

~38%



As e-commerce grows, more sub-sectors will also grow, and related sectors are also poised to benefit.

E-commerce

A. B2C growing fast and big

Implication of e-commerce growth

Emergence of e-commerce sub-sectors

Growth in traditional e-commerce will **make online purchasing behaviors mainstream.**

As more people in tier 2 and tier 3 cities adopt e-commerce, **the demand for specialized e-commerce** will grow.

This will accelerate the emergence of sub-sectors, such as the following:

- Social commerce (Evermos)
- B2B commerce (GudangAda)
- Specific commerce (Carro and TaniHub)

Growth in other sectors supporting e-commerce

E-commerce is **enabled by many other supporting sectors.**


As e-commerce grows, other **enabling sectors will also see benefits**, such as the following:

- Lending will benefit as “pay now, buy later” becomes mainstream.
- Logistics will benefit as the volume of e-commerce purchases grows.
- Payments will increase as result of higher transactions.



Consumer lending will grow, riding the wave of increasing online purchase habits.

Lending

 Total Indonesia market

A. B2C growing fast and big

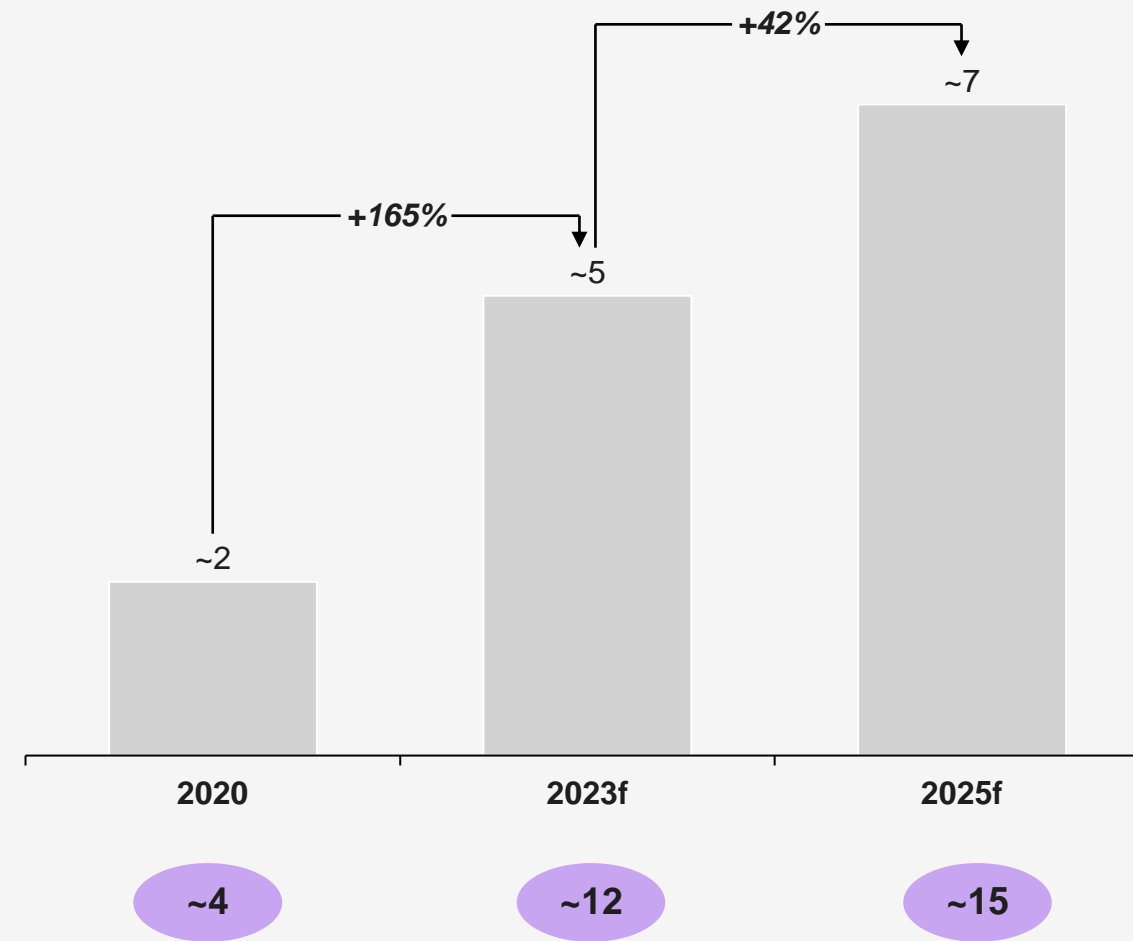
Fintech lending tier 2 and tier 3 market size (total loan in \$ billion)

2020-2025 CAGR
(tier 2 and tier 3 market)

~30%

Familiarization period within tier 2 and tier 3

- Increased acceptance through regulation and cybersecurity measures (OJK stamp) will drive adoption.
- Lending platforms can also expect an increase in adoption through synergies with other digital platforms (e-commerce).



Note: OJK is Otoritas Jasa Keuangan (Financial Services Authority of Indonesia).
Source: Alpha JWC; Kearney analysis

However, fintech lending still faces constraints that need to be solved to accelerate growth.

Lending

A. B2C growing fast and big

Low ease of use for borrowers



- Tier 2 and 3 borrowers reported a **difficult and cumbersome process while applying for credit**, resulting in instances of loan rejections.
- Tier 2 and 3 borrowers reported **having difficulties in identifying loans that are appropriate** for their purposes.

“The mobile applications are hard to use, and my loan requests keep getting rejected.”

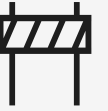
Negative consumer perception



- Customers perceive fintech lending to be **more expensive in interest and less favorable in repayment tenor** than conventional loans.
- Customers also perceive lending to be bad because of their **religious and cultural beliefs**.

“I am worried because I have heard some bad news, such as scams and high rates that are related to digital lending.”

Lack of sector accessibility




- **Suboptimal digital infrastructure** in Indonesia results in cited transaction errors and a small participant base.
- **The limited lender population** has only 0.02 lender accounts for every borrower account.

“I am worried that there will be a transaction failure because we don’t have good-quality Internet in this region.”

Digital payments are expected to grow as the ecosystem and use cases for cashless payments expand.

Payment

 Total Indonesia market (\$ billion)

A. B2C growing fast and big

Digital payment tier 2 and tier 3 market size (GTV in \$ billion)

Merchant QRIS adoption (million)



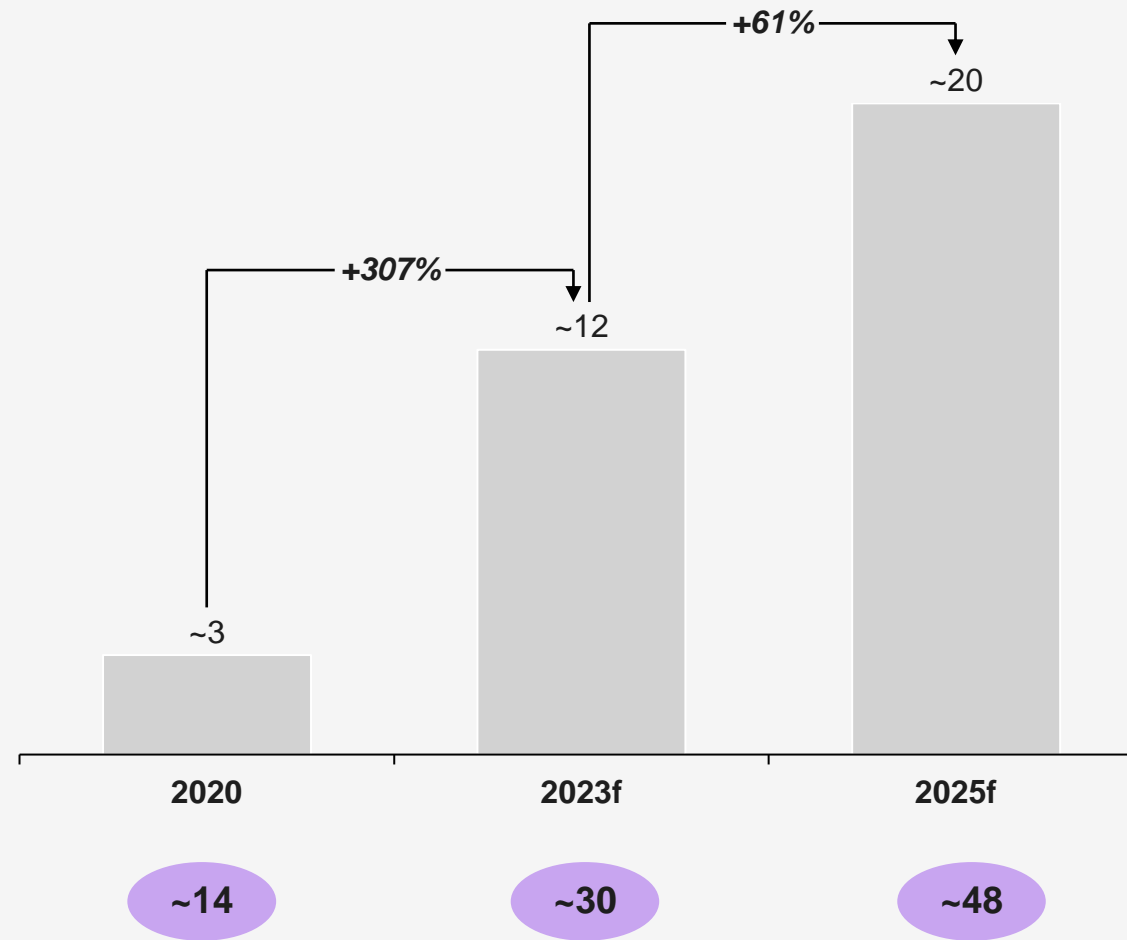
- Beyond e-commerce, digital payments' rise to mainstream is **fueled by rapid expansion in acceptance points**.
- **Regulations had also been favorable**, with BI standardizing QRIS, which led to more than 4x growth in points of acceptance since January 2020.

"I just have to access the app on my phone, so I don't have to go to ATM. The app is also easy to use."

Note: QRIS is the Quality Rating and Improvement System.
Source: press searches, Alpha JWC; Kearney analysis

2020-2025 CAGR (tier 2 and tier 3 market)

~46%



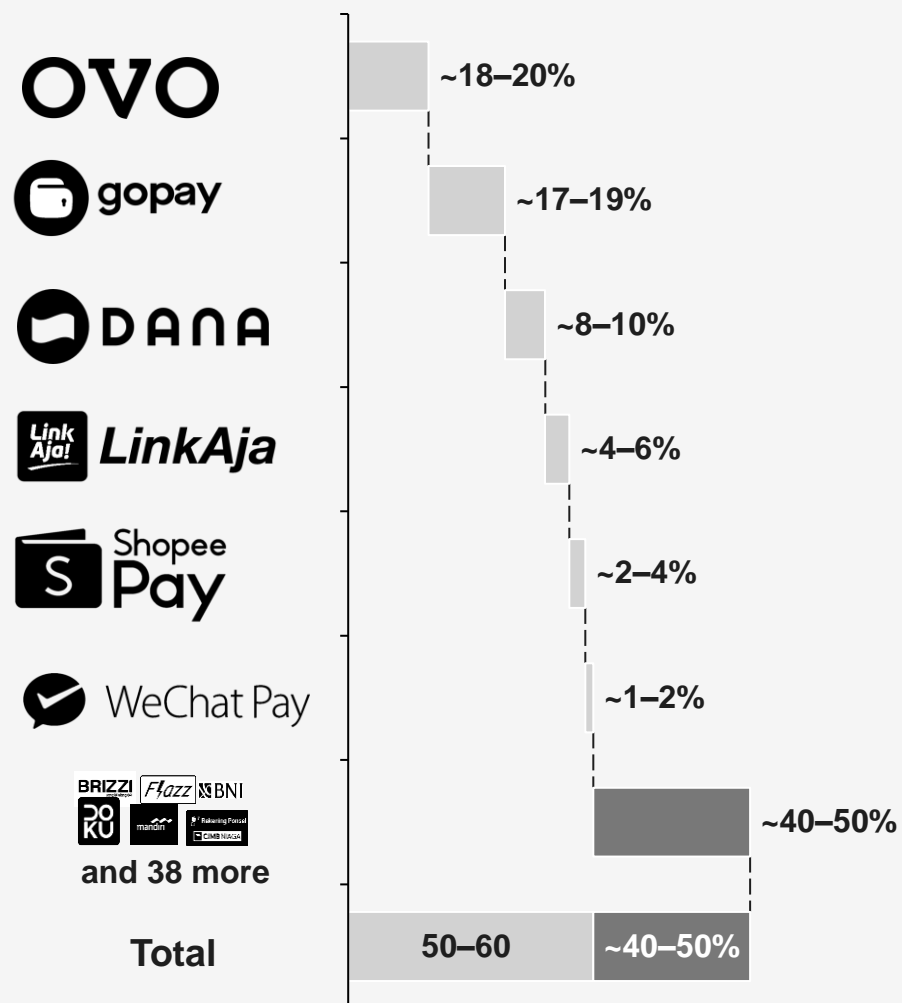
The digital payment market is dominated by large players with strong connections to the wider ecosystem – leaving little room for newer players.

Payment

A. B2C growing fast and big

Digital payment market share (% of GTV, 2019)

Digital payment market share (% of GTV, 2019)



Penetration strategy

Link with ride-hailing (Grab) and e-commerce (Tokopedia) companies

Link with Gojek ecosystem and partnering with other start-ups (such as Halodoc)

Partnership with other e-commerce players (Bukalapak and Lazada) and transport (Blue Bird)

Leverages state-owned enterprises connection for points of acceptance

New entrant but links with Shopee creating meaningful traction

Partnership with conventional financial institutions

Backed and managed by conventional financial institutions

- Six players in the market **account for 50–60% of the country's** digital payment gross transaction value.
- The largest payment players are **linked with other players in the ecosystem** (such as e-commerce, ride-hailing, and transport companies).

The growth of ride-hailing and food delivery will be limited in tier 2 and tier 3 cities as the importance of convenience is lower.

Ride and food


 Total Indonesia market (\$ billion)

A. B2C growing fast and big

Ride hailing and food delivery tier 2 and tier 3 market size (GTV in \$ billion)

Penetration (% to population, 2025f)

Tier 1 cities
 ~54%

Tier 2 and tier 3 cities
 ~10-20%

Less penetration in tier 2 and tier 3 cities

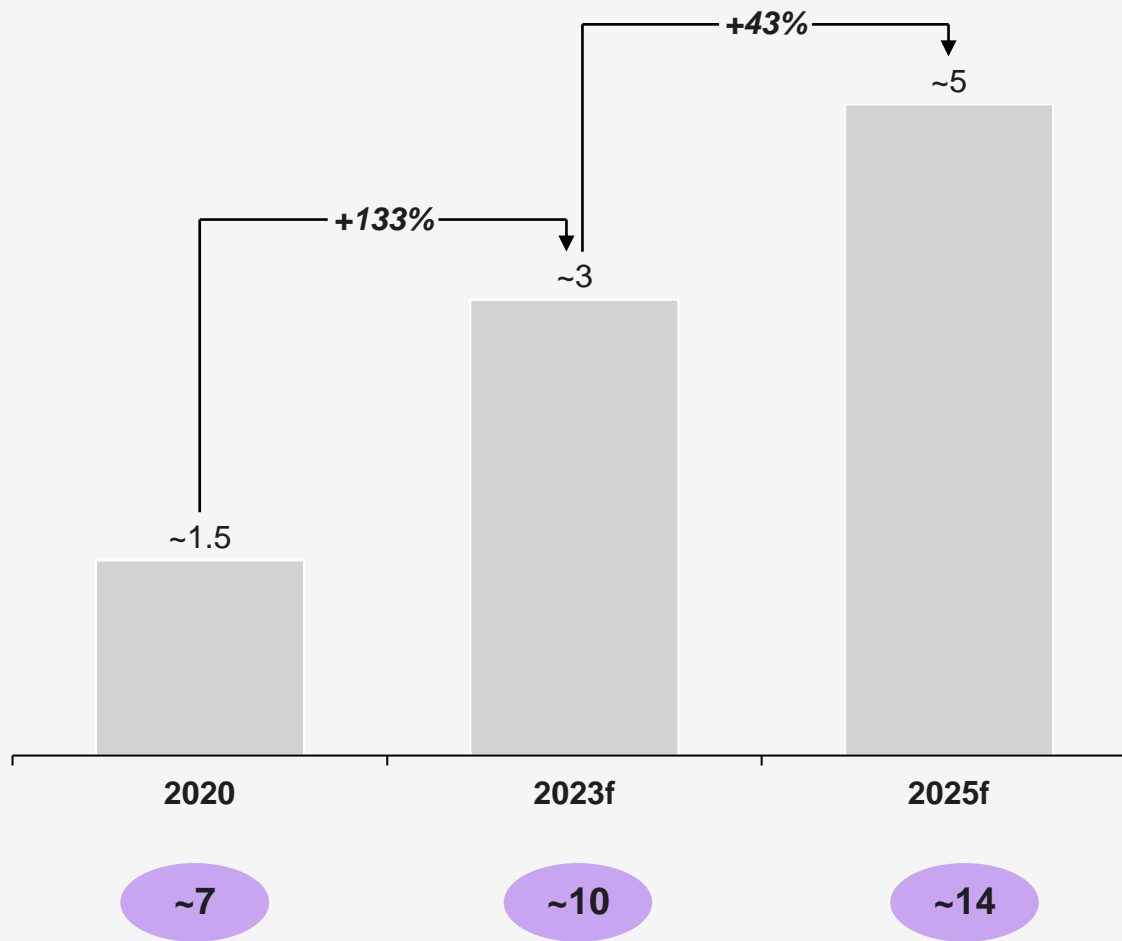
- Penetration in tier 2 and tier 3 cities will be lower than in tier 1 cities as the **level of importance for convenience from the services will be lower**. (For example, traffic is not a big issue in tiers 2 and 3, so convenience is not a priority.)

“I don’t use ride-hailing because most places are quite close to where I am. I prefer to use my own transportation.”

Note: Penetration is defined by the average monthly active users per capita across food delivery, motorcycle ride-hailing, and car ride-hailing.
 Source: Nielsen, Alpha JWC; Kearney analysis

2020-2025 CAGR (tier 2 and tier 3 market)

~27%



By 2025, health-tech will still be nascent despite growing penetration among the tier 2 and tier 3 population.

Health-tech

 Total Indonesia market (\$ billion)

A. B2C growing fast and big

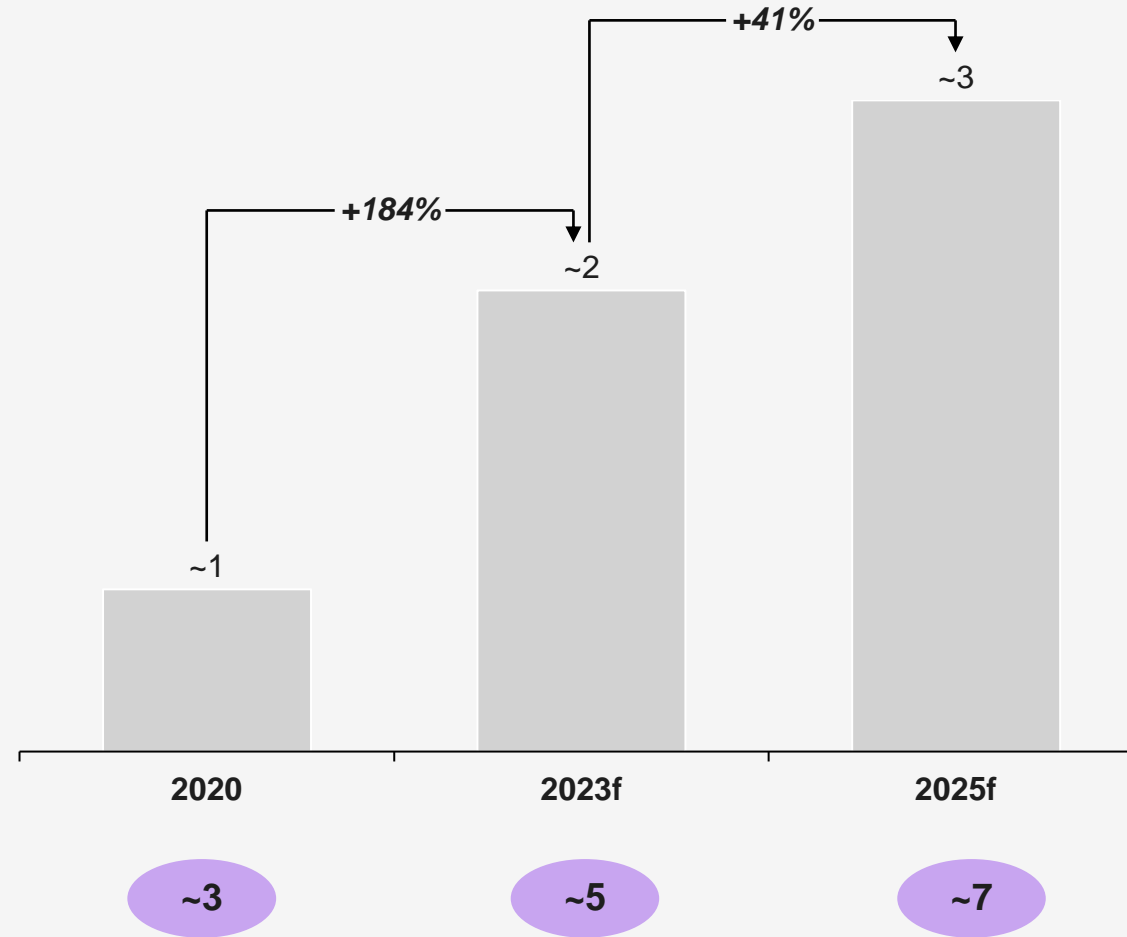
Health-tech tier 2 and tier 3 market size (GMV in \$ billion)

Growing fast but still nascent even in 2025

- As of 2020, 97% of health-tech users in tier 2 and tier 3 cities are early adopters.
- In 2025, health-tech penetration will increase from about 3% of the population to 16%.
- However, the industry will still be nascent and not as widely adopted in comparison to e-commerce, lending, and payment because of the large number of barriers, including quality doctors and clear regulations.

2020-2025 CAGR
(tier 2 and tier 3 market)

~32%



Note: The market size for health-tech is only for the B2C (direct-to-consumer) segment.
Source: Alpha JWC; Kearney analysis

Key to unlocking HealthTech growth is to expand presence and build credibility among tier 2/3 population.

Health-tech

A. B2C growing fast and big

Issues and comments from the ground

Fear of misdiagnosis by a doctor

"We don't meet the doctor in person. I'm afraid it's a fraud or hoax. The doctor also can't check our body directly, so how does the doctor know what sickness I am suffering from?"

Not trusting doctors in an app

"I already have a doctor I usually go to. Why would I use the app if I can go to my own doctor, whom I trust more than those doctors in the app?"

Still preferring physical consultations

"There is a nearby clinic that I can go to. It is much easier for me to go to the clinic directly than to use app for a consultation."

Implications for start-ups and investors

Crucial to build credibility to penetrate tier 2 and tier 3 cities' population, which could be done via the methods:

- Onboarding local medical personnel or health facilities with significant ties to the community
- Getting local influencers and leaders to endorse the use of health applications for non-urgent medical conditions
- Working with the Ministry of Health and the regulatory bodies to expedite clear regulation and potential escalation in case symptoms do not ease after the virtual consultations



Ed-tech will see a significant increase in the market size, driven by higher penetration in tier 2 and tier 3 cities.

Ed-tech

 Total Indonesia market (\$ billion)

A. B2C growing fast and big

Ed-tech tier 2 and tier 3 market size (GMV in \$ billion)

COVID accelerated the adoption of ed-tech

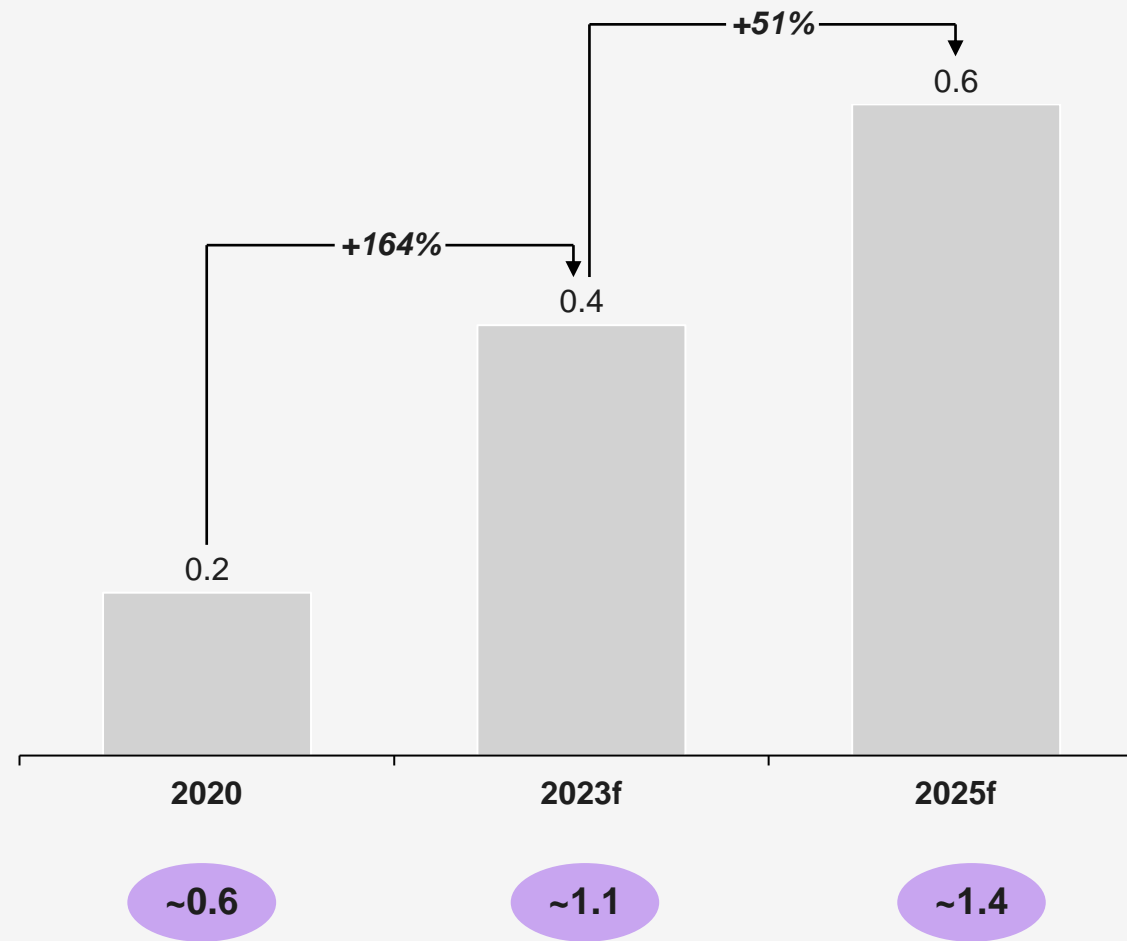
- School closures have had a major impact on the adoption of ed-tech, especially for online content and virtual learning tools.

Unlock ed-tech's potential requires a systematic push in the system

- Ed-tech goes beyond online content and virtual learning tools. However, unlocking the potential requires systematic change in education systems and digital infrastructure.

2020-2025 CAGR (tier 2 and tier 3 market)

~32%



Note: The market size for ed-tech is only for the B2C (direct-to-consumer) segment.
Source: Alpha JWC; Kearney analysis

However, unlocking full potential will require more systematic push in the education system

Ed-tech

A. B2C growing fast and big

Factors constraining the growth of ed-tech growth

Why people use the app:

It helps my kids to learn. I am using it because the school asked us to.

Why people don't use the app:

The signal depends on the weather here. So, if rain comes when my kids are studying, we have a poor Internet connection, and the signal drops.



Lack of dedicated devices to support virtual learning

To be effective, online learning and ed-tech in general require decent Internet connections and a dedicated device for every student. Solving connectivity and affordability challenges will be key to unlocking ed-tech's potential.

Lack of integration with formal education: ed-tech is “good to have” but not a “must have”

Parents are not yet committing to ed-tech as they view it as a “good-to-have” rather than a “must-have” for formal education. Systematic integration with formal education will go a long way to unlocking the full potential.

Digital challenges for Indonesian educators

Indonesian educators find it challenging to conduct lessons virtually because of a lack of training and low digital literacy. Onboarding younger educators and upskilling current educators will be vital to bridging gap in digital learning.

MSMEs are major contributors to Indonesia's economy.

Contribution of MSMEs to the national economy (2019)

61%

of GDP contributed by MSMEs

97%

of national workforce employed

99%

of all registered businesses are MSMEs

58%

of investments in country are by MSMEs

14%

of total exports are made by MSMEs



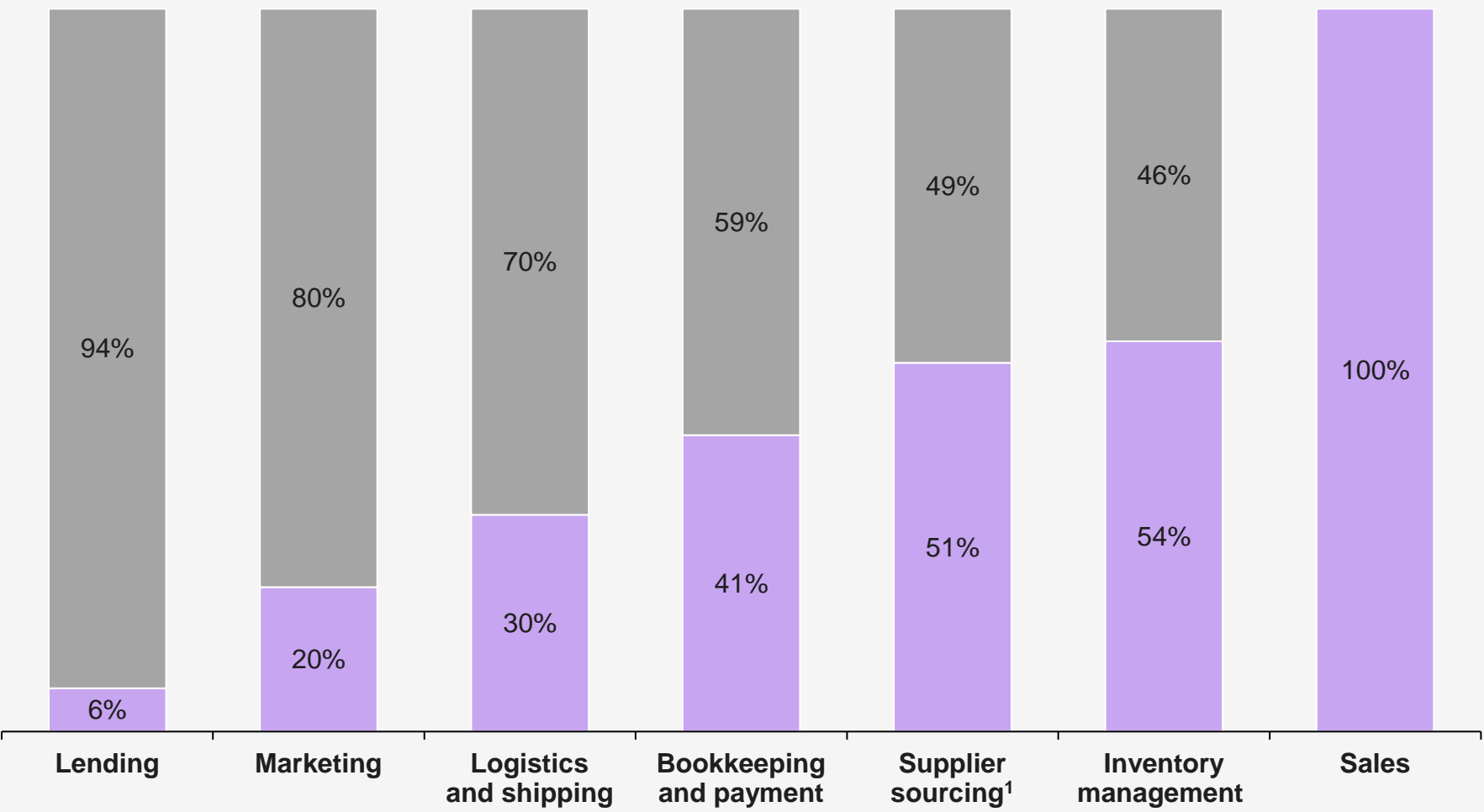
Aspirations for 2025

- Realizing the significance of MSMEs to the national economy, the government has set a target of MSMEs contributing 65% to GDP and 22% of total exports.
- Going forward, MSMEs will play a larger role in the national economy.

Note: MSMEs are micro, small, and medium enterprises.
Source: press searches, Ministry of Cooperatives and SMEs; Kearney analysis

However, Indonesian MSMEs are not realizing their full potential since most take a passive approach—not actively performing business activities at all.

Prevalence of business activities among MSMEs
(% of total MSMEs respondents in tier 2 and tier 3 cities)

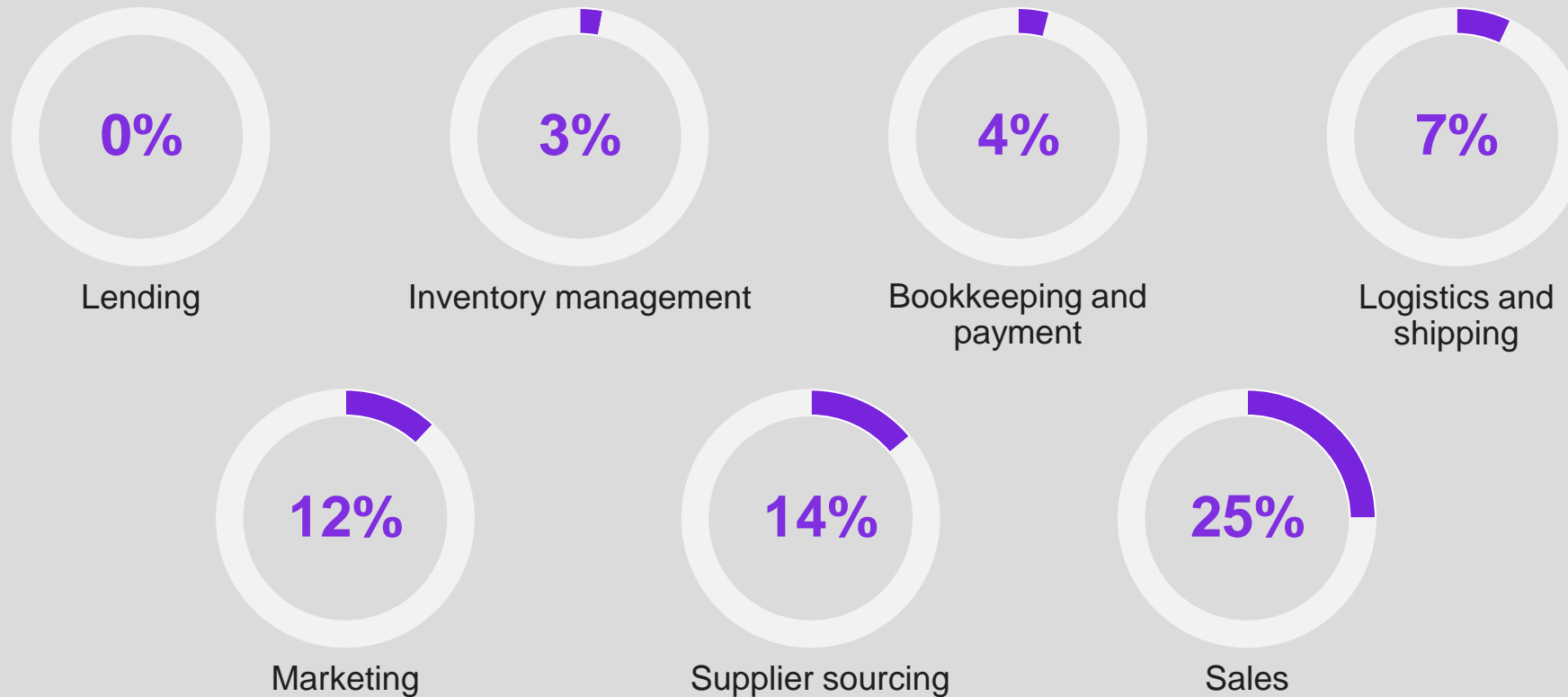


B. SME services heating up

Note: MSMEs are micro, small, and medium enterprises. Supplier sourcing refers to actively searching for new suppliers and new products, comparing prices. Not actively performing this means doing business as usual.
Source: Nielsen; Kearney analysis

Adoption of online methods is still minimal, even among MSMEs that are actively managing businesses.

Incidence of online activities (% of MSMEs that performed activities)

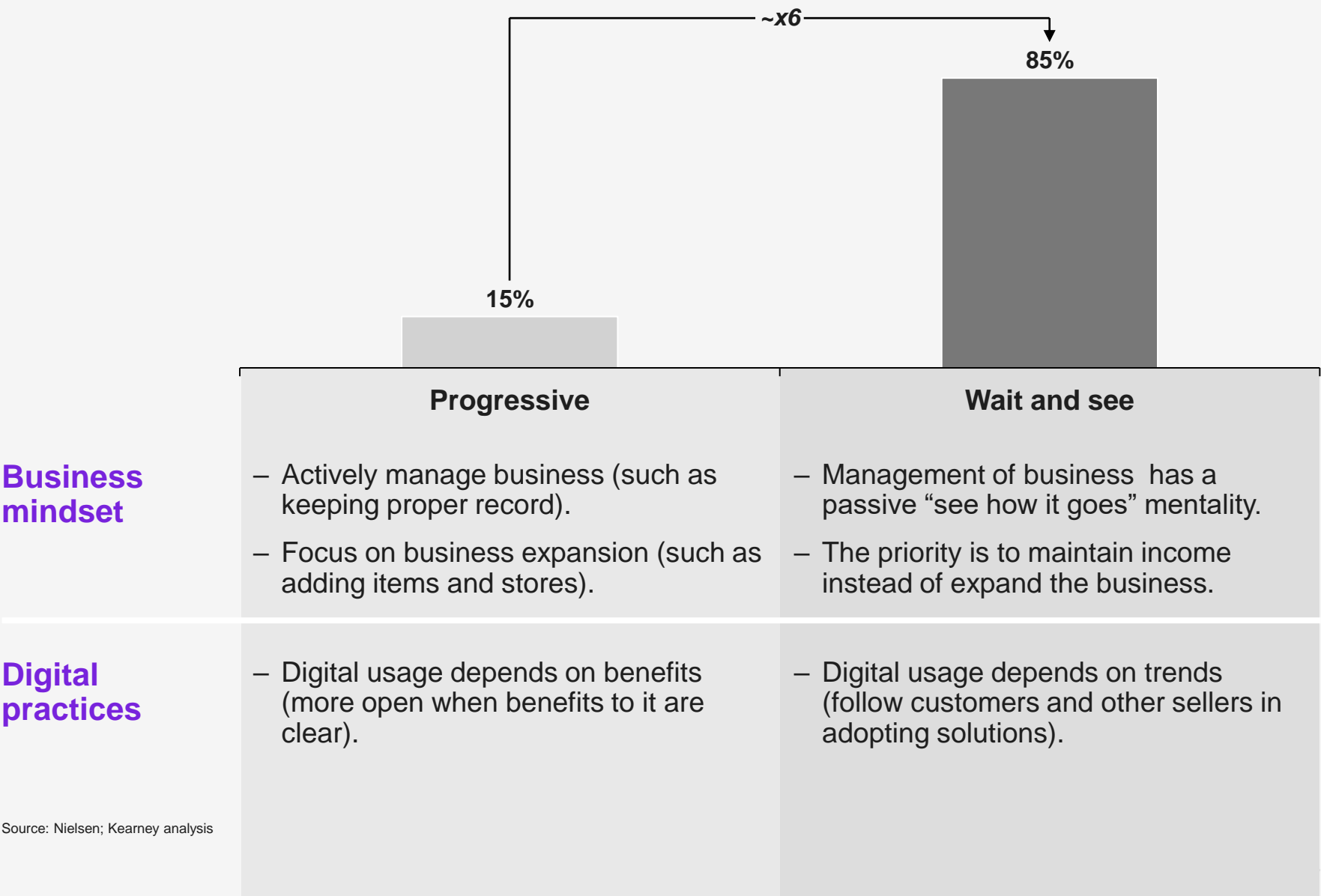


B. SME services heating up

- MSMEs that are active are still more comfortable **performing activities offline.**
- The low prevalence of online activities despite some categories—marketing, sales, and logistics—**have less than 30% awareness among MSMEs.**
- Relatively high awareness, but low incidence **suggests the need for more intense onboarding efforts to familiarize and encourage digital adoption in MSMEs.**

Overall, more than 80% of MSMEs in tier 2 and tier 3 cities adopt a wait-and-see mentality when it comes to digital practices.

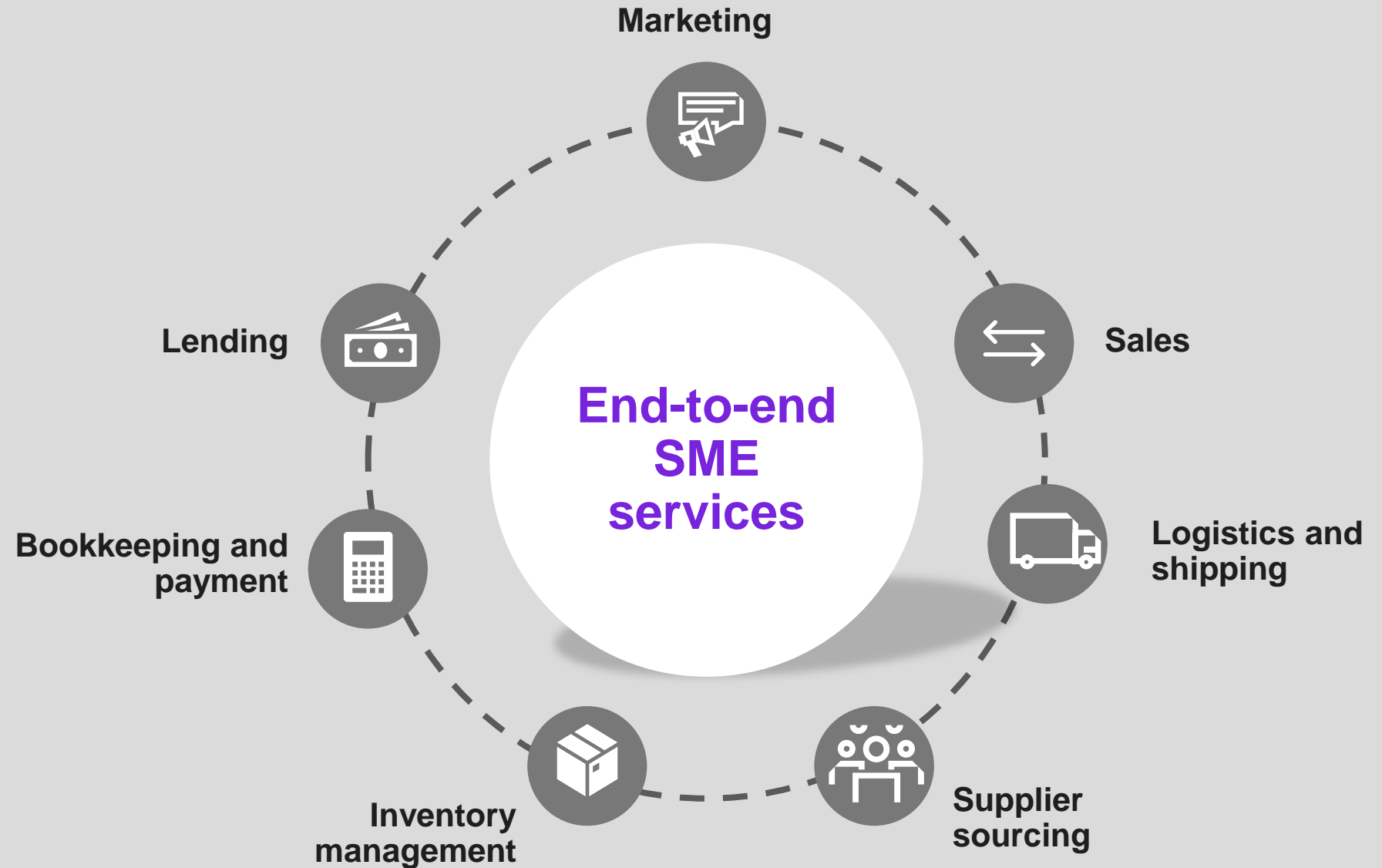
Types of MSMEs
(% total MSMEs respondents in tier 2 and tier 3 cities)



B. SME services heating up

Given the strong potential for MSMEs, digital solutions for end-to-end SME services are springing up

Digital solutions in SME services



B. SME services heating up

Social media giants are ramping up their shop offerings and positioning themselves as total SME solutions.

Social media as a total SME solution



Social media (Facebook, WhatsApp, Instagram) are by far the most used apps for marketing, sales, and sourcing platforms among active SMEs.

B. SME services heating up

Social media as an MSME super app

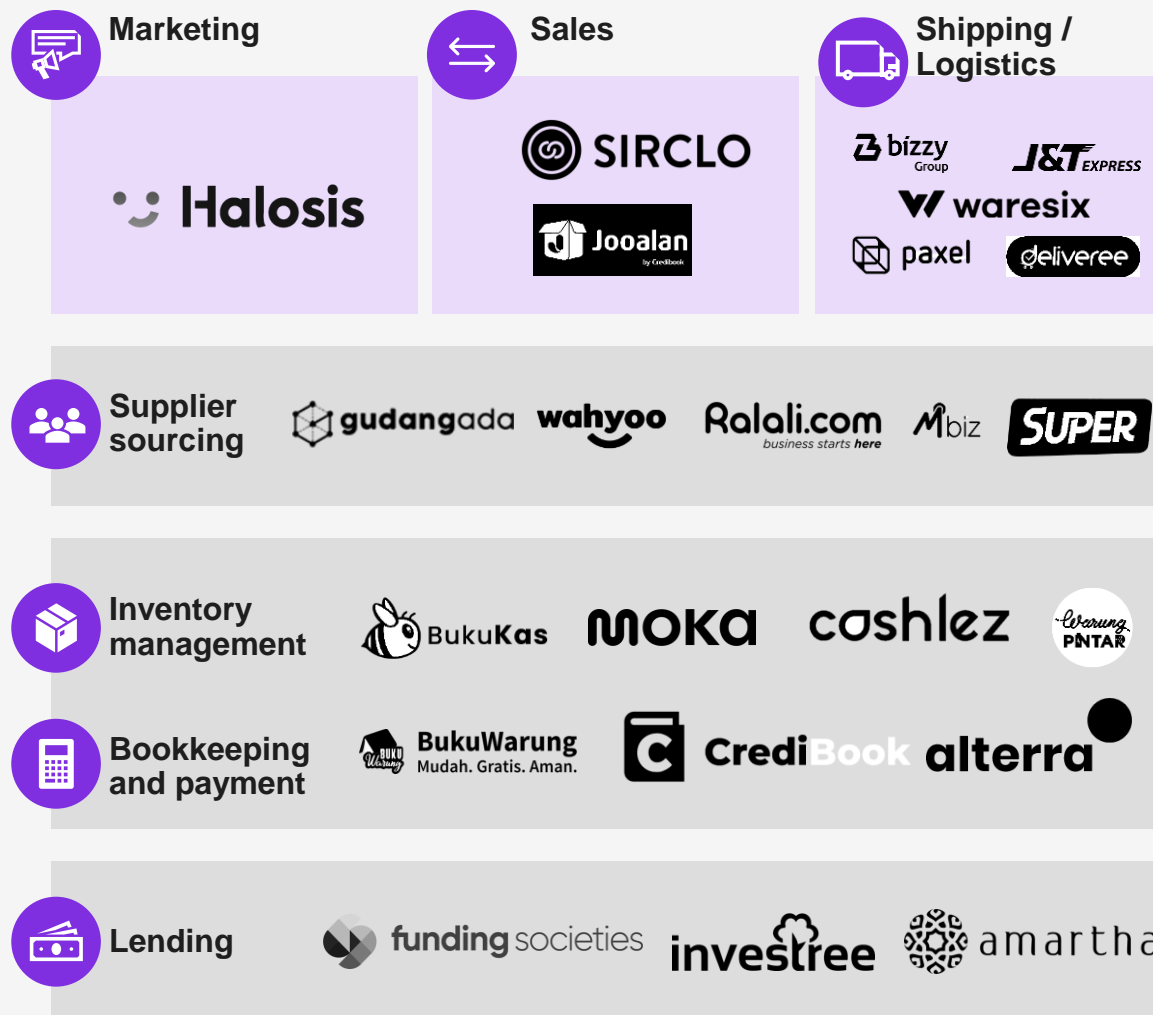
- Social media companies have been ramping up their **store functions**.
- They are **widely adopted as MSMEs** are already familiar from using them in personal life.
- Social media giants might aim to **follow WeChat's evolution in China** to be an **MSME super-app**.

WeChat as MSMEs super-app in China

- WeChat offers a **marketing platform** to users beyond retail reach.
- WeChat plays the role of **storefront and sales platform**.
- WeChat offers **other services** (such as geo-location and customer services) as part of its SME solutions.

At the same time, dedicated SME services start-ups are also pursuing the market.

Start-ups in SME services market



Not Exhaustive

Front-facing Enablers

B. SME services heating up

J&T EXPRESS

Indonesia-based, **Southeast Asia leading last-mile delivery services** with more than 2 million daily delivery in 2020

gudangada

Largest B2B e-commerce player in Indonesia with a presence in more than 500 cities and \$700 million of monthly GMV processed

funding societies

Pioneer in MSME funding in Southeast Asia with more than IDR 20 trillion (\$2 billion) processed from about 3.6 million in total loans as of January 2021

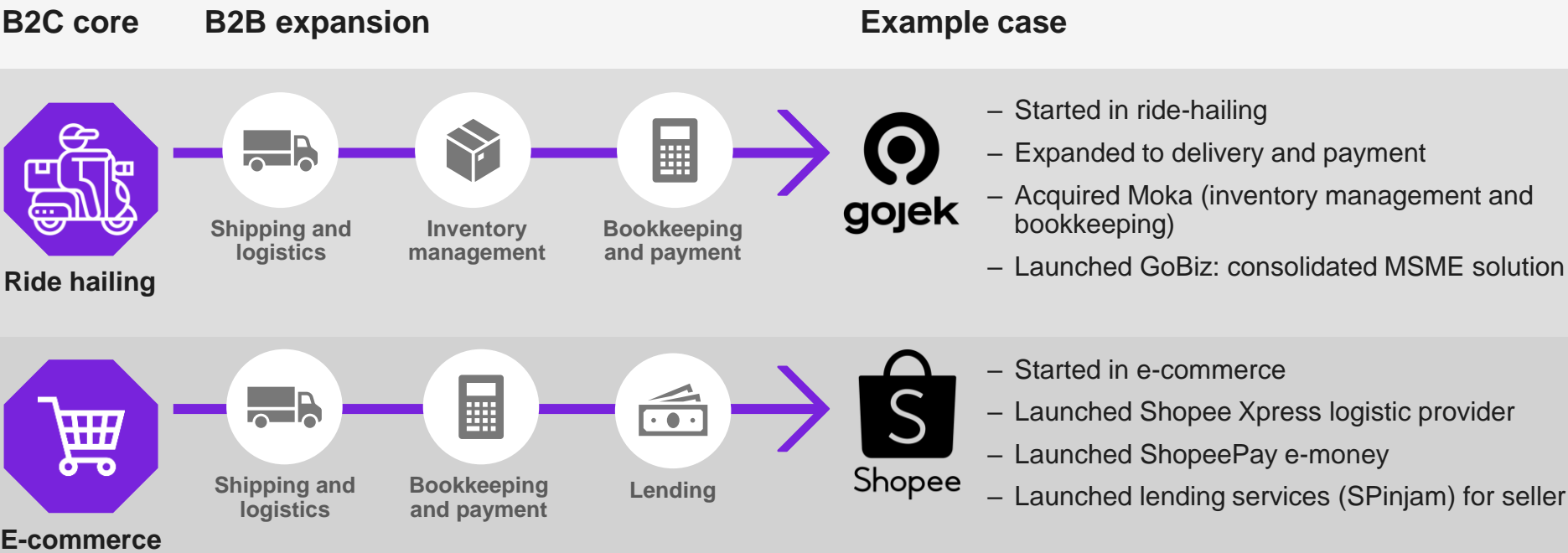
alterra

Indonesia's leading bill payment platform processing millions of payments daily and is official partner of more than 200 online partners

While traditional B2C start-ups are also expanding to adjacent SME services.

Not exhaustive

Observed B2C to B2B Expansion



Traditionally, B2C start-ups are expanding to adjacent SME services:

- SME services (B2B) unit economics are more favorable than B2C.
- B2C start-ups could leverage core B2C offerings to capture value by offering SME services.

B. SME services heating up

Digital could be a game-changer for Indonesian MSMEs, but significant efforts from start-ups and investors will be required.

Current state of Indonesian SME services market

Most MSMEs do not actively manage their businesses.

- Most MSMEs are not actively managing businesses even offline.
- Most are comfortable with the status quo, more concerned about maintaining income than about having a thriving business.

Implications for start-ups and investors

Start from the basics and build a clear value proposition from MSMEs.

- Educating MSMEs with “handholding” to adopt digital for more active management is key.
- Many MSMEs have no idea about the upside they are missing. The value proposition needs to be clearly laid out to encourage adoption.

Competition is intensifying from social media and B2C start-ups.

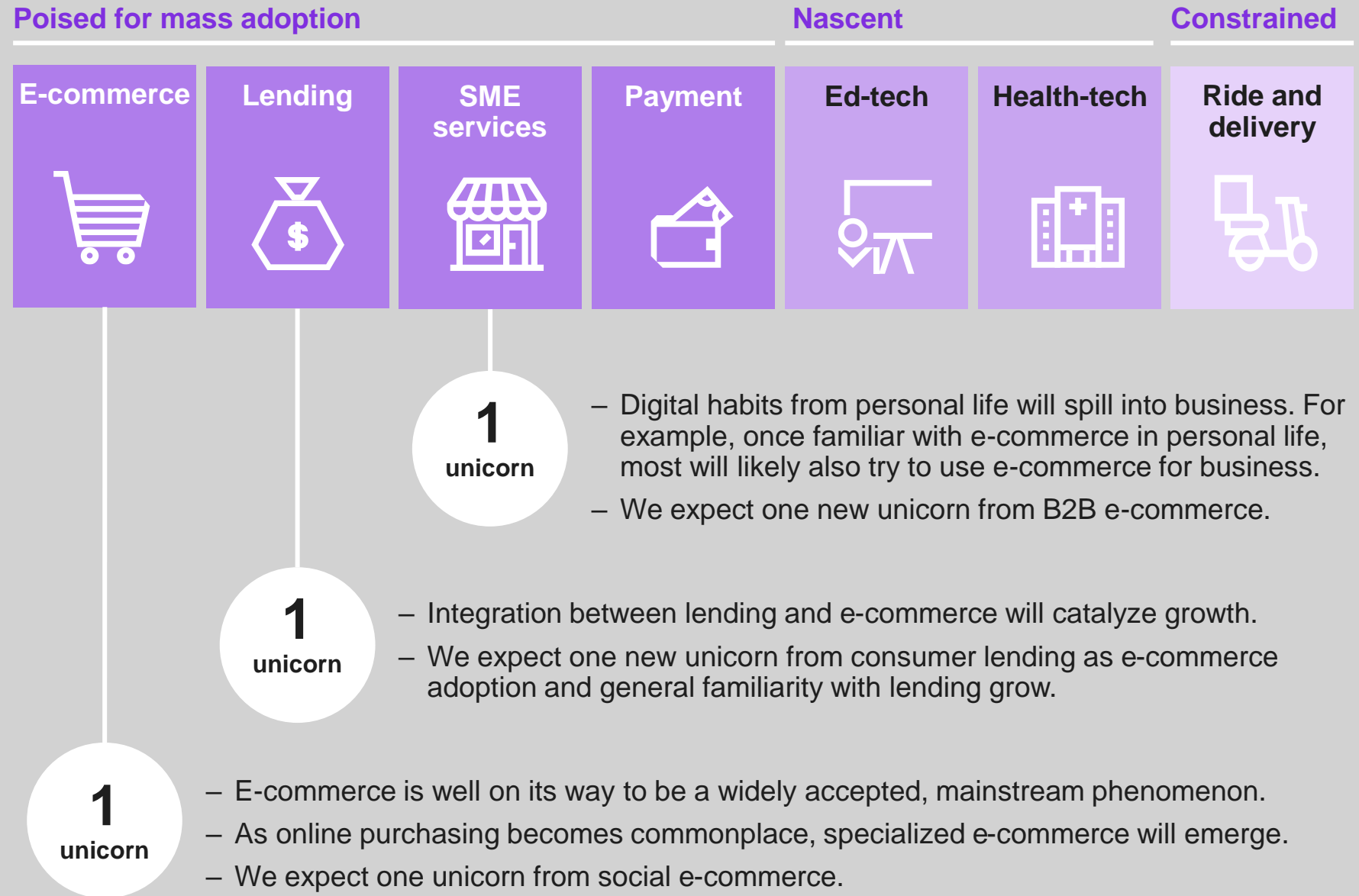
- Large social media apps (such as Facebook, WhatsApp, and Instagram) are ramping up MSME offerings.
- At the same time, traditional B2C players (such as ride-hailing and e-commerce) are also making a big push to SME services and leveraging core B2C offering to capture value of SME services.

Carving out a niche in an increasingly crowded market is crucial to success.

- Investors and start-ups will have to adapt and think about how to compete against social media and B2C giants.
- This could be achieved by carving out a niche in the enablers where they are not active in or by leveraging functionalities already offered by social media and B2C giants to enrich own offerings.

B. SME services heating up

Based on our observations, we expect three unicorns from three large categories in the next five years.



C. Up and Coming

In e-commerce, Evermos becomes Indonesia's largest social commerce platform by adopting reseller-based model for Indonesia's tier 2 and tier 3 cities.

Data provided by: EVERMOS

Large contribution of non-tier 1 cities across key metrics, 2020

Tapping into the potential of non-tier 1 cities ...

50,000

active resellers in 34 provinces

82%

active resellers in non-tier 1 cities

60%

of GMV from non-tier 1 cities

Overcoming e-commerce trust barrier among tier 2 and tier3 consumers

- Instead of being just another e-commerce player, Evermos brings a curated “three-sided marketplace” connecting brand owners to resellers to end customers.
- This model allows Evermos to grow beyond tier 1 cities as most consumers outside of tier 1 are still not comfortable with online purchases.

Evermos' user based and social profile, 2020

... by building an inclusive economy for everyone via social commerce

63%

of active resellers are female

58%

active resellers earn less than minimum wage

>50%

of resellers –w/o tertiary education

Creating an inclusive economy and improving SME competitiveness

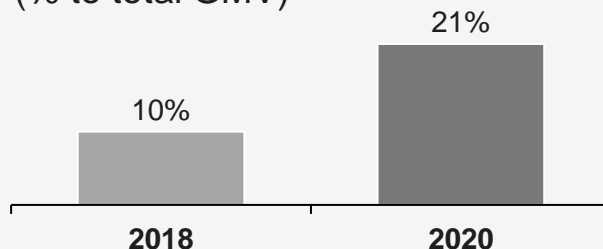
- By adopting a social commerce model, Evermos aspires to be the largest economic empowerment platform and ecosystem in the country by creating an inclusive economy and improving SME competitiveness.

C. Up and coming

In lending, Kredivo sees non-tier 1 cities as up and coming markets that are driving growth across key metrics.

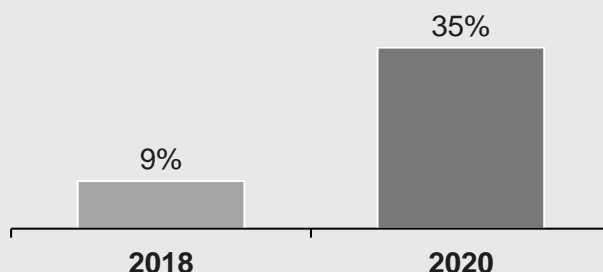
Significant growth of non-tier 1 cities across key metrics in 2020

Loan disbursed
(% to total GMV)



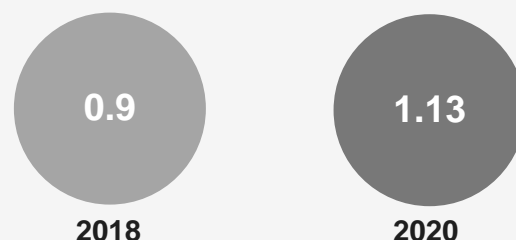
The proportion of loans disbursed to non-Tier 1 cities **doubled** from about 10% in 2018 to about 21% in 2020.

New users activated
(% to total new users)



The proportion of new users activated from non-tier 1 cities had grown about **4x** from 9% in 2018 to about 35% in 2020.

Non-tier-1 transaction frequency
(Tier 1 cities = 1.0)



Non-tier 1 users are already transacting **1.13x** more frequently than users from tier 1 cities.

Note: GMV is gross merchandise value; P2P is peer-to-peer.
Source: FinAccel; Kearney analysis

Data
provided by:



- Founded in 2016, Kredivo is a major digital credit company in Indonesia and has served about **3 million users** and partnered with about **1,000 companies**.
- Since then, it has been **expanding coverage to T2 and T3 cities**. Now everyone with a smartphone and access to the Internet can apply for a basic account.
- As Kredivo refines its credit assessment model, **more users from T2 and T3 cities will qualify for loans while keeping risks comparable** to mid-top tier banks in Indonesia.
- Further, FinAccel (ParentCo) now **eyes expansion to serve under-banked and underserved segments in Indonesia** with its new KrediFazz, which provides P2P personal loans and productive lending.

In SME services, GudangAda establishes itself as leading B2B e-commerce player by serving more than 300,000 merchants beyond tier 1 cities in Indonesia.

Data provided by:



- GudangAda is Indonesia's **fastest-growing, and currently largest**, FMCG B2B marketplace platform.
- It aims to **empower the whole FMCG ecosystem by using technology** to provide one-stop solutions from marketplace, logistics, financing, data, and other services.
- The company facilitates **bulk transactions between FMCG traders (buyers and sellers) and principals**, enabling faster inventory turnover, better buying price, and a larger pool of customers and product selection.

C. Up and coming

Non-tier-1 cities are important growth drivers for GudangAda (2020)

More than 300,000
active users
(merchants)

500
cities with GA
network

More than 600 million
monthly GMV
processed

50%
of GMV from
non-tier-1 cities

60%
of users from
non-tier-1 cities



4. Looking forward: much has been done, much remains to be done

- A. **Much has been done:** ecosystem wish list and progress
- B. **Much remains to be done:** key imperative to successes



We interviewed prominent investors and start-ups on key considerations to boost digital adoptions.

Select quotes on keys to boost digital adoption

*“When **digital infra improves along with government’s increased push for user education**, there will be a lot more focus outside of Java.”*

*“Social economics and physical infrastructure **are the main driving factors** of the difference in tier 1 versus tier 2 and tier 3 cities.”*

*“Requirements for foreign investors should be lighter. **It is still very complicated for foreign VCs to invest.**”*

*“**Talent development in tier 2 and 3 cities is key.** It’s difficult to recruit outside talent as many are not willing to move out from big cities.”*

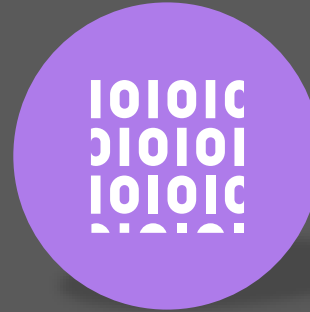
*“**Local capital development** is important to fund entrepreneurs in tier 2 and tier 3 cities.”*

*“The social behaviors in tier 2 and 3 needs to change; **you have to educate the users** – and social presence here is important.”*

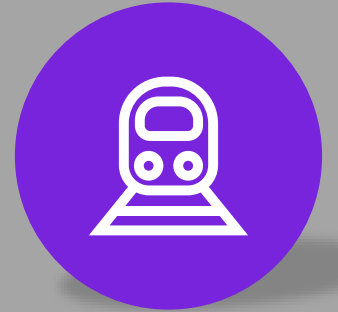
A. Much has been done

From our interviews, we identified six enablers for digital adoption.

Digital infrastructure



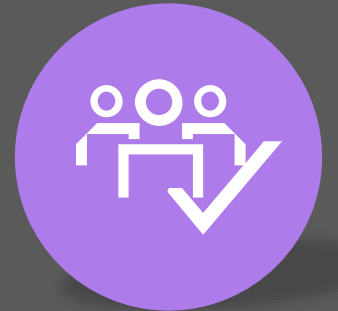
Physical infrastructure



Regulatory infrastructure



Talent and capability



Access to capital



Consumer education



A. Much has been done

The government has deployed initiatives to improve Indonesia's digital ecosystem.

Key developments across six areas

Digital infrastructure

- **Accelerated digital infrastructure development.** Allocated \$30 billion, largely dedicated to improving digital connectivity in 2021



Physical infrastructure

- **Accelerated focus on physical infrastructure spending.** Planned investment of \$430 billion from 2020–2024 (20% increase from 2015–2019)



Regulatory infrastructure

- **Proactive regulatory framework.** For example, the passing of the Job Creation Law, OJK digital banking, and fintech lending licenses



Talent and capability

- **Renewed focus on digital talent development.** For example, public–private partnership between the MICT, Google, and LinkedIn and an educator competency push



Access to capital

- **Laid out foundation for access to capital.** For example, the passing of Ministry of Finance Regulation No. 53/2020 on government investment and the Job Creation Law that allows foreign investments in MSMEs



Consumer education

- **Implemented digital inclusion programs.** For example, OJK–BI financial inclusion program, MICT UMKM Go Digital, and MOT Bangga Buatan Indonesia



A. Much has been done

However, several imperatives need to be accelerated.

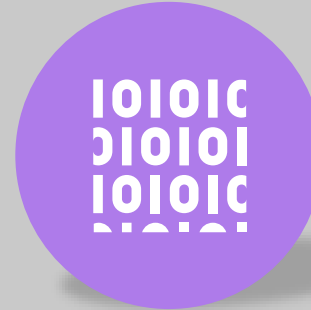
Going forward, the government should look to these imperatives as a guide in policy development and execution so that the Indonesian Internet economy can flourish, especially in tier 2 and tier 3 cities.

B. Much remains to be done

Key imperatives to accelerate digital adoption

Digital infrastructure

Widen **connectivity penetration**, and improve **connectivity speed**.



Physical infrastructure

Strengthen connectivity, and facilitate commerce across the nation.



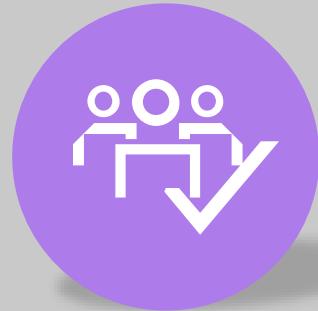
Regulatory infrastructure

Enact **timely, transparent regulations** that facilitate ease of doing digital business.



Talent and capability

Prioritize **competency development in digital**, such as vocational training in collaboration with industry.



Access to capital

Facilitate access to capital to start-ups via fair investments regulations and transparent risk sharing and explore partnerships with private institutions.



Consumer education

Promote the use of digital solutions, and increase **digital literacy** across all segments of population.



Prominent countries with flourishing digital ecosystem are pushing to achieve key imperatives.

Race to fulfill key imperatives



China

The **14th Five-Year-Plan** pushed for progress across key imperatives to be a global digital powerhouse.



India

A series of initiatives (including **Digital India and Start-Up India**) was launched and accelerated key imperatives.



S. Korea

The **Digital New Deal** was launched for key imperatives (such as investing in 5G and R&D funding) for a digital future.

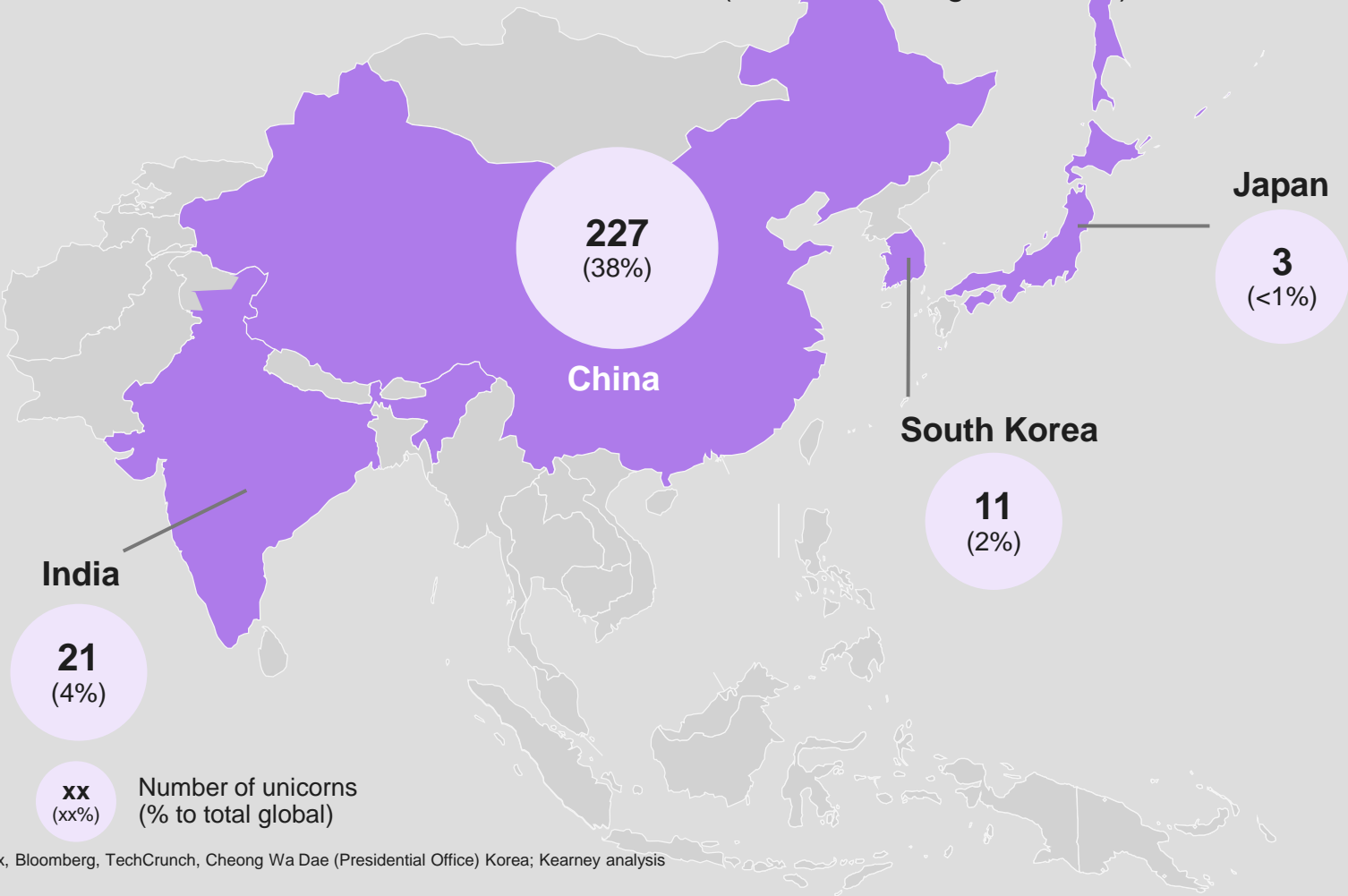


Japan

The **Society 5.0** policy transforms society by blurring cyberspace and physical and includes a commitment to develop key imperatives.

B. Much remains to be done

Top Asia Pacific countries with the most unicorns (2020, excluding Indonesia)



xx
(xx%)

Number of unicorns
(% to total global)

China's 14th Five-Year Plan signaled a central government focus on key imperatives to be a global technology powerhouse in the next five years.

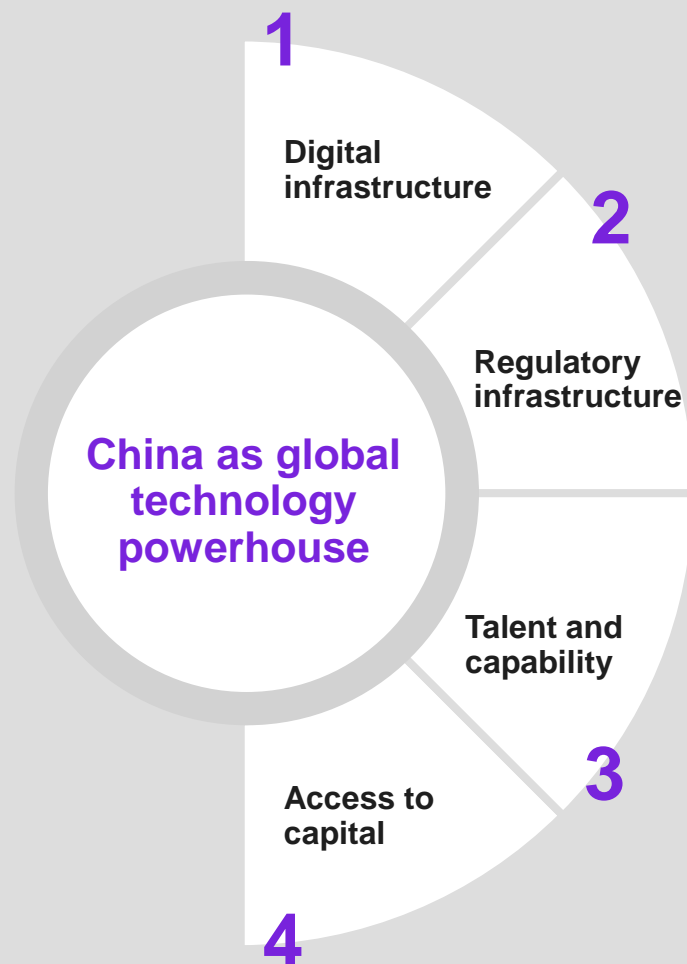
Not exhaustive

China's 14th Five-Year Plan lays out a vision where China achieves quality economy growth via innovation and technology. If successful, China is expected to make huge progress across all key imperatives required to accelerate digital economy .

B. Much remains to be done



China's Five-Year Plan to be a digital powerhouse



\$1.4 trillion of investment in new infrastructure (such as big data, 5G, artificial intelligence, and cloud computing) in the next five years



Maintaining an “opening-up” policy (such as reducing the negative list and attracting an FDI inflow) and **enhancing property rights protection**



Shifting focus to education quality – build world class colleges, accelerate development of modern vocational education, industry-linked education system



Encouraging international collaboration in key technologies by commercializing research and revitalization of national R&D

Note: As of the release of this report, details of the plan had not been released. However, central theme of becoming technology powerhouse remains
Source: BBVA Bank, China Global Television Network, USA Congressional Research Services; Kearney analysis

While India has launched a comprehensive approach for developing key imperatives to accelerate its digital economy.

Not Exhaustive



India government digital approach



Digital infrastructure



Physical infrastructure



Regulatory infrastructure



Talent and capability



Access to capital



Consumer education

Digital programs

BharatNet Project

Special-purpose vehicle by India's government to create a National Optical Fiber Network

Bharatmala Pariyojana

Government-sponsored 34,500-kilometer road and highways project that will connect 80% of all districts, including rural areas

Make in India

Initiative in improving the ease of doing business with tax exemptions and protecting minority investors

FutureSkills Prime

Public-private collaboration with NASSCOM, offering lessons on digital skills, such as big data

Startup India

Program to build a strong digital ecosystem via start-up funding, handholding, and incubation

Digital India

National digital program that aims for digital empowerment for citizens among others

Progress and outcome

100,000

more villages connected (December 2017)

2,900 km

roads constructed (August 2020)

142nd→63rd

World Bank EODB rank (2014–2019)

200,000

professionals trained (December 2019)

About 193

start-ups funded (March 2019)

More than 20,000

government services digitized (January 2021)

B. Much remains to be done

Note: NASSCOM is the National Association of Software and Service Companies; EODB is ease of doing business.
Source: Digital India, Startup India, FutureSkills PRIME; Kearney analysis

Other countries around the world are also racing to achieve key imperatives.

Digital infrastructure



Thailand

Robust national strategy for network penetration through the Thailand 4.0 initiative, achieving about 66% 4G penetration by 2018 (above Southeast Asia's average), despite a large rural population

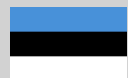
Physical infrastructure



Australia

Significant initiatives in regional development, such as the Towards 2030 program, which outlines the national plan in **increased spending for rural infrastructure development**

Regulatory infrastructure



Estonia

Established e-governance to cover large scope of digital services by partnering with public companies to enable the service (such as banks for e-payment and health institutions for e-health)

Talent and capability



Malaysia

National upskilling through the Human Resource Development Fund, which provides **vocational training in digital skills** (software development and data analytics)

Access to capital



Singapore

Various start-up grants by government agencies (such as Startup SG Founder and Startup SG Tech) and match funding from private investors

Consumer education



South Korea

ICT is integrated within all levels of national education, resulting in one of the world's most digitally literate populations

Note: ICT is information and communications technology.
Source: World Bank, OECD

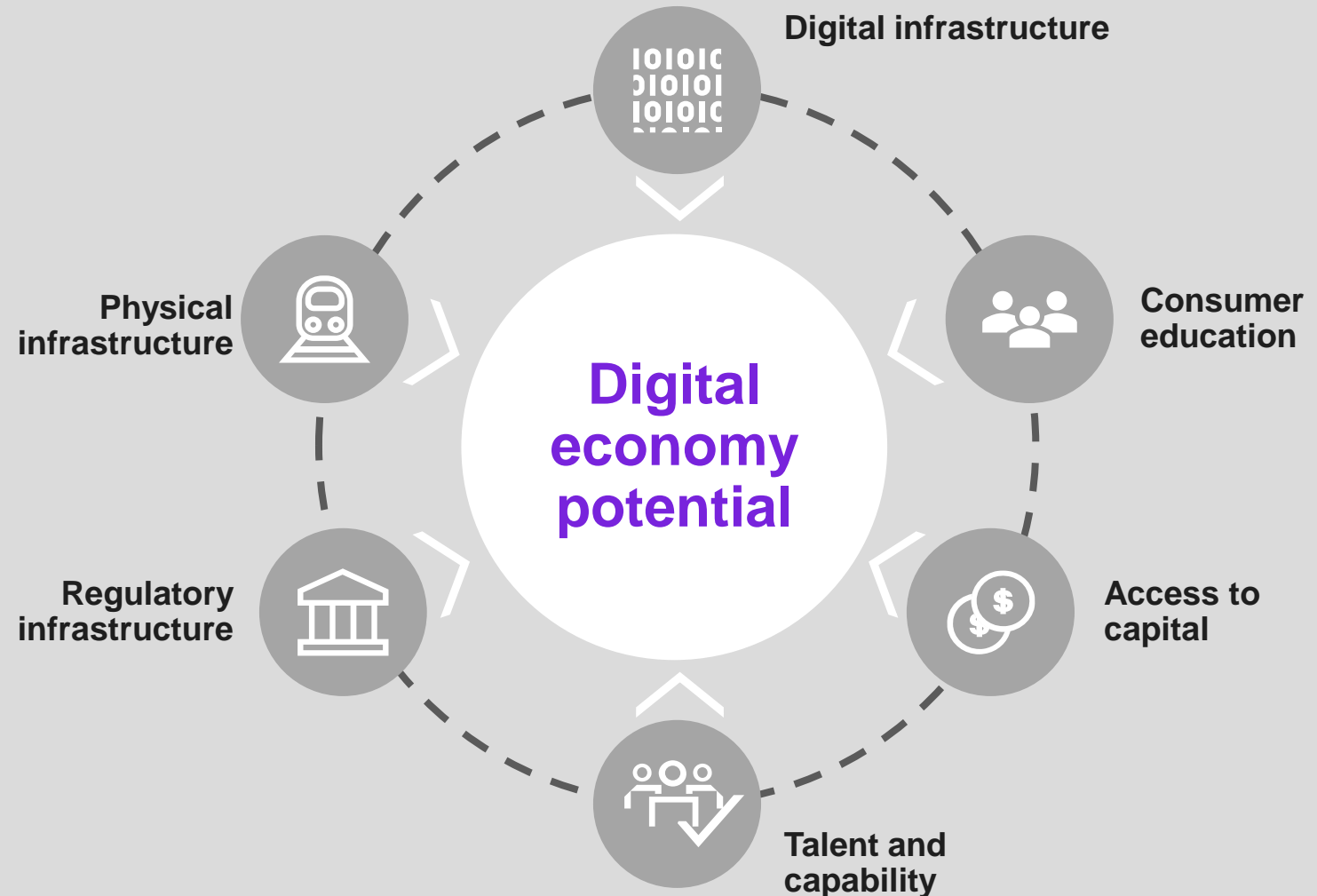
B. Much remains to be done

Unlocking the potential of the digital economy requires solving interlinked issues.

Interlinked key imperatives for digital economy

- Unlocking digital economy potential requires **solving all interlinked key imperatives**.
- **Solving one or the other key issue will not be enough** to unlock digital the economy.
- Given the interlinkage of issues, the approach to unlocking potential requires a **more comprehensive approach**.

B. Much remains to be done



Therefore, a comprehensive “whole of government” collaboration with the private sector is crucial.

Not exhaustive

B. Much remains to be done

Government and private-sector collaboration



Widen **connectivity penetration**, improve **connectivity speed**, and ensure **cyber and data security**.



Strengthen connectivity, and facilitate commerce across the nation.

All ministries

Create **timely, transparent regulations** that facilitate the ease of business.



“Future-proof” the workforce by prioritizing **digital skills and competency** across the workforce.



Facilitate access to capital via favorable regulations, and **promote** Indonesia’s digital ecosystem.



Promote use of digital solutions for people and MSMEs (such as use e-commerce for domestic products.)

SuPrivate sector



Digital infrastructure

– Proactively engage and communicate key issues.



Physical infrastructure

– Provide key inputs on government digital policies.



Regulatory infrastructure

– Actively participate in national digitalization program:



Talent and capability

– Develop a digitally enabled workforce.



Access to capital

– Invest in digital solutions.



Consumer education

– Participate in a public–private partnership on digital.

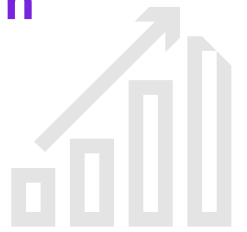
Notes: MICT is the Ministry of Information and Communication Technology; MPW is the Ministry of Public Works and Public Housing; MOT is the Ministry of Transport; MOE is the Ministry of Education; MOM is the Ministry of Manpower; MOF is the Ministry of Finance; BKPM is the Badan Koordinasi Penanaman Modal; MSME is the Ministry of Micro, Small and Medium Enterprises; MTrade is the Ministry of Trade.

Reiterating our assertions: digital potential beyond metropolitan Indonesia.

For the next five years, the tier 2 and tier 3 digital economy **will clock 5x growth into 2025 as mass adoption begins** in several sectors on the back of efforts by start-ups and macro tailwinds.



E-commerce, lending, and payments will emerge as the biggest sectors as mass adoption starts, while nascent sectors such as **health-tech and ed-tech will experience significant growth from low baseline**



As a result of mass adoption, **two to three potential unicorns from e-commerce, lending and SME services** will emerge in the next five years.



Six imperatives in infrastructure, talent, consumer education, and access to capital will be crucial for the digital ecosystem to flourish as one of the world's best.



Authors.



Chandra Tjan
Co-founder and
General Partner,
Alpha JWC
Ventures



Shirley Santoso
Partner,
Kearney



Jeffrey Joe
Co-founder and
General Partner,
Alpha JWC
Ventures



Shekhar Chauhan
Partner,
Kearney



Eko Kurniadi
Partner,
Alpha JWC
Ventures



Sanath K.B
Partner,
Kearney



**Erika Dianasari
Go**
Partner,
Alpha JWC
Ventures



**Rinaldo
Augusta**
Principal,
Kearney



Arief Wibisono
Consultant,
Kearney



Nabila Abeng
Consultant,
Kearney



Nadia Putri
Senior
Associate,
Alpha JWC
Ventures



**Adelia Anjani
Putri**
Manager, Alpha
JWC Ventures



About Alpha JWC Ventures

Alpha JWC Ventures is an early to growth-stage Southeast Asian venture capital firm with an Indonesia+ angle. Over the years, Alpha JWC has established a strong reputation and clear positioning in the market as the leading venture capital firm that has one of the largest on-the-ground teams in Indonesia with a global network. Its debut fund of US\$50 million was launched in 2016 as Indonesia's first independent and institutional early-stage venture capital fund. Since then, the first fund has been invested in 23 companies in Southeast Asia, mostly in Indonesia, which more than 90 percent of them have received follow-on funding and 3 have been acquired by global companies. The firm's second fund was closed in 2019 and has been invested in 20 fast-growing companies by Q4 2020. www.alphajwc.com

About Kearney

As a global consulting partnership in more than 40 countries, our people make us who we are. We're individuals who take as much joy from those we work with as the work itself. Driven to be the difference between a big idea and making it happen, we help our clients break through. www.kearney.com

About Credit Suisse

Credit Suisse is one of the world's leading financial services providers. Our strategy builds on Credit Suisse's core strengths: its position as a leading wealth manager, its specialist investment banking capabilities and its strong presence in our home market of Switzerland. We seek to follow a balanced approach to wealth management, aiming to capitalize on both the large pool of wealth within mature markets as well as the significant growth in wealth in Asia Pacific and other emerging markets, while also serving key developed markets with an emphasis on Switzerland. Credit Suisse employs approximately 48,770 people. The registered shares (CSGN) of Credit Suisse Group AG, are listed in Switzerland and, in the form of American Depositary Shares (CS), in New York. Further information about Credit Suisse can be found at www.credit-suisse.com.

About Amazon Web Services

For almost 15 years, Amazon Web Services has been the world's most comprehensive and broadly adopted cloud platform. AWS has been continually expanding its services to support virtually any cloud workload, and it now has more than 200 fully featured services for compute, storage, databases, networking, analytics, machine learning and artificial intelligence (AI), Internet of Things (IoT), mobile, security, hybrid, virtual and augmented reality (VR and AR), media, and application development, deployment, and management from 77 Availability Zones (AZs) within 24 geographic regions, with announced plans for 18 more Availability Zones and six more AWS Regions in Australia, India, Indonesia, Japan, Spain, and Switzerland. Millions of customers—including the fastest-growing startups, largest enterprises, and leading government agencies—trust AWS to power their infrastructure, become more agile, and lower costs. To learn more about AWS, visit www.aws.amazon.com.

About Xiaomi Corporation

Xiaomi Corporation was founded in April 2010 and listed on the Main Board of the Hong Kong Stock Exchange on July 9, 2018 (1810.HK). Xiaomi is an internet company with smartphones and smart hardware connected by an Internet of Things (IoT) platform at its core. With an equal emphasis on innovation and quality, Xiaomi continuously pursues high-quality user experience and operational efficiency. The company relentlessly builds amazing products with honest prices to let everyone in the world enjoy a better life through innovative technology. Xiaomi is currently the world's third-largest smartphone brand and has established the world's leading consumer AIoT (AI+IoT) platform with 289.5 million smart devices connected to its platform, excluding smartphones and laptops. Xiaomi products are present in more than 90 markets around the world. In August 2020, the company made the Fortune Global 500 list for the second time, ranking 422nd, up 46 places compared to the previous year. Xiaomi also ranked 7th among internet companies on the list. Xiaomi is a constituent of the Hang Seng Index, Hang Seng China Enterprises Index and Hang Seng TECH Index. For more information about Xiaomi as a company, please visit <https://blog.mi.com/en/>

Unlocking the next wave of digital growth: beyond metropolitan Indonesia



Thank you

Stay connected with Kearney



This document is exclusively intended for selected client employees. Distribution, quotations and duplications – even in the form of extracts – for third parties is only permitted upon prior written consent of Kearney.

Kearney used the text and charts compiled in this report in a presentation; they do not represent a complete documentation of the presentation.

KEARNEY

