Indonesia's Economic Optimism

By J. B. Sumarlin

I would like to take this opportunity to describe for you briefly the current directions of economic development in my country of Indonesia. In particular, I would like to make you aware of some of the recent economic measures we have adopted to modernize and streamline our economy in order to make Indonesia more attractive and competitive as a regional economic power.

Perhaps I could begin by emphasizing that Indonesia is by no means a "typical" developing country. We are a nation of enormous size and diversity. Let me cite a few examples of the ways in which Indonesia is unique:

1) Indonesia has both abundant natural resources and a large population. Most other countries of Asia or the developing world have one or the other, but not both. In development terms, this means Indonesia cannot simply follow a labor-intensive manufacturing strategy, like Korea or Taiwan, or a resource-intensive strategy, like Malaysia or Thailand. Instead, we must pursue policies that attempt to strike a balance, building on both our human and our natural resources. We need to develop industries that are both labor intensive and competitive in the international marketplace.

2) Indonesia has maintained fiscal discipline through balanced budgets for more than twenty years. This contrasts sharply with many other countries – both industrialized and developing – experiencing fiscal deficits and the attendant problems of debt and inflation.

3) A third striking difference about Indonesia is that we have operated an open foreign exchange system for nearly twenty years based on the maintenance of a realistic exchange rate, which makes us almost unique within the developing world. We have learned in Indonesia that control of exchange is not only impossible to enforce but also creates unhealthy and undesirable distortions in the market. Instead, we have adjusted our economic policies to fit an open exchange system, as we believe this to be far more conducive to overall long-term economic growth.

Three-Pronged Crisis. Indonesia has just come through a very difficult period of economic stress, beginning in early 1983 and continuing for the next four years. Three negative external forces hit our economy simultaneously: the collapse of oil prices, weak overall prices for our other traditional commodity exports, and the sharp realignment of the yen vis-à-vis the dollar. These factors caused us great difficulties. Our export earnings were cut in half, while our overseas debt repayment burden soared because our exports are denominated in dollars while our debt is denominated largely in yen.

How we handled this crisis is a story in itself. In the space of two years, from 1986 to 1988, many bold and decisive steps were taken. We succeeded: there was no balance of payments crisis, no default on our debt, no major loss of confidence in our currency, no runaway inflation, and no requests for a rescheduling of our debt. Throughout this period, our economy continued to grow.

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Absorbing the Shock. Much of the credit for Indonesia's economic resiliency during this period of great stress can be attributed to policies already in place. These policies ensured that Indonesia's windfall oil revenues were put to productive use in other sectors of the economy throughout the oil-boom years. Hence when the crunch came, Indonesia was able to absorb the shock without seeing its economy collapse.

Nonetheless, the Indonesian economy clearly had become excessively reliant on oil. Inefficiency, waste, and a wide range of nonmarket forces had been allowed to creep into the fabric of the economy during the boom years. In many ways, we look upon the oil crisis of the mid-1980s as a "blessing in disguise." It forced us to focus our attention on the inefficiencies in our economic system and to undertake a thorough housecleaning.

Therefore, in broad terms, the priorities we have identified for Indonesia's economic growth in the 1990s are as follows:

◆◆ Broadening the country's industrial base and increasing the relative proportion of manufactured goods within the total GDP.

◆◆ Utilizing and adding value to our country's base of raw materials, while at the same time preserving our natural resources and ensuring economic growth based on sustainable development.

◆◆ Stepping up job creation to absorb each year's 2.3 million new entrants into the job market, improving our human resources capabilities, and upgrading the skill of our workforce.

◆◆ Ensuring export-led economic growth, especially through exports of non-oil products and services.

◆◆ Helping our private sector to grow by improving the range and capabilities of our financial system through a wider portfolio choice for our savers and investors, better banking and other services, and money and capital markets that are functioning well.

To achieve these objectives, we have set a target for overall economic growth at 5 percent annually for the next five years. We are completely confident of achieving, even exceeding, this growth target. Indonesia's economy today is in infinitely better shape than it was three years ago.

Manufacturing competitiveness, the breadth of production capabilities, increasing awareness of the tough imperatives of international marketing – in all these areas, Indonesian businessmen are considerably more experienced, more capable, and more competitive than they have ever been before.

For some of this, we have the realities of the global marketplace to thank. Tough times breed keener competition. Keener competition, in turn, leads to greater efficiency. Much of the credit for the new environment in Indonesia, however, can be attributed to direct policy initiatives by the government. The key policy direction in Indonesia throughout the 1980s has not been in the form of intervention, but rather, in the form of deregulation.

Reforms in the 1980s. During the past seven years – starting with the first weakening in oil prices in 1982 – there has been hardly a single sector of the Indonesian economy that has not been touched by government reform policies. We have eliminated excessive regulations, or to be blunt, "red tape." We have overhauled our ports and customs procedures, import and export facilities, shipping and transportation sectors, manufacturing licensing system, and foreign investment regulations. To illustrate what I mean, let me describe the foreign direct investment regulations.

Much of Indonesia's sustained economic growth depends on its continued ability to attract investment from overseas to supply the necessary capital for plant, equipment, and technology. Actually, we have had remarkable success in developing a class of Indonesian entrepreneurs and technical experts. Nevertheless, we continue to need infusions of new capital and technical expertise from overseas investors.

Attracting Foreign Dollars. It should be noted that Indonesia has long had a good record of foreign investment. More than twenty years ago we introduced legislation to attract foreign investment. Under this system, foreign investment has flourished. Between 1967 and 1988, direct foreign investment in our industrial and manufacturing sectors had reached a total of $21.3 billion. This figure does not include participation in mining, energy, and finance, for which the investment procedures are different. When these are added in — particularly the vast foreign commitment to our energy industry — today's cumulative total of overseas involvement in Indonesia's private sector economy is closer to $40 billion. Indonesia thus ranks among the top two or three developing countries in the world in terms of foreign direct investment.

It must be acknowledged, however, that during the 1970s and early 1980s, our investment environment developed what we might call "bureaucratic hardening of the arteries." Inadvertently we permitted the proliferation of secondary rules, regulations, and permits. We recognized that this situation was not attractive to the world's investment community. Indeed, we came to recognize that many of these regulations served little constructive purpose and were counterproductive to growth. As a result, we set about cleaning house in the investment sector, just as we had in other areas.

Overall, we identified two broad areas in which we felt modifications or simplifications were called for either by fine-tuning regulations or by eliminating them altogether.

♦ ♦ Greater Ease in Investing in Indonesia

Today's procedures are simple. They eliminate former complicated and time-consuming processes for obtaining permits from a battery of government agencies. Whereas we used to permit investment only in specifically identified areas, today investment is permitted in all areas except those specifically closed, and those areas are kept to a bare minimum.

♦ ♦ Improvements to the Operating Environment for Foreign Investors in Indonesia

The improvements in this regard include: The maximum level of start-up equity that can be held by the foreign investor has been increased to 85 percent. In new ventures involving high risk, high technology, or extensive capital or located in remote areas, the initial foreign ownership can go as high as 95 percent. Such changes are designed to give foreign investors more control over the direction and strategy of their Indonesian operations as well as greater return on investment.

In conclusion, I would like to refer briefly to Indonesia's financial system, as this is currently an area of tremendous growth and change. Indonesia's financial management is one of the country's greatest strengths. Our record of monetary management, our control of inflation, our maintenance of foreign reserves, and our support of the nation's currency are all indicative of a financial system that is rigorously and carefully managed. The fact that we have maintained stability while operating with full and unlimited currency convertibility for nearly two decades, a condition almost unique in the developing world, is proof in itself of the soundness of our policies.

Our country's financial requirements, however, are rapidly expanding. To meet these growing needs, we have implemented a wide range of improvements to our financial sector. For example, Indonesia has opened its doors to new joint venture banks, and our fledgling stock market, the Jakarta Stock Exchange, has suddenly taken hold.

Foreign Cooperation. I hope I have succeeded in communicating some of the optimism we are feeling in Indonesia today. These are times of tremendous change and growth for us. While we are especially pleased and optimistic about the progress we are making, we cannot do it all alone. We have always needed – and we will continue to need – the support and cooperation of the world's industrialized nations, including our friend the United States, especially in keeping markets open to our products. We want to pay our way in the world. For this, we need your support in helping to fight protectionism. We can do our part in two ways. We can keep our own markets open for your export products, and we can ensure that the products we bring to market are up to the standards of quality that you require.

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