Crawford School Dialogue

Indonesia
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Tuesday, 12 March, 2011
Weston Theatre, J G Crawford Building 132, Lennox Crossing, ANU
One of very few countries not to suffer a severe decline in growth as a result of the GFC

- GDP growth rate remained above 4% p.a. (mid-2009)
-Recovered to 6.9% by the end of 2010
  - Driven mainly by private investment: business confidence high
  - On supply side, growth is most rapid in services, especially wholesale/retail trade, hotels and restaurants
- Inflation around 7%, c.f. target range 4-6%
  - Reflects central bank unwillingness to allow Rp to appreciate
- Recent surges in food prices
  - Temporary removal of tariffs (rice, wheat, soybeans)
  - Increased imports of rice
- Financial markets
  - Exchange rate against $US very stable
  - Stock market has been booming (but recent signs of nervousness)
There is a severe fiscal problem

- Not an unsustainable deficit
- Rather, enormous subsidies to energy consumption (fuel/electricity)
- No threat to macro stability
- But huge waste of Indonesia’s hydrocarbon wealth (oil, gas, coal)
- Main benefits to middle & upper classes, who consume much more energy
  - 2011 budget subsidies to energy: $15 billion
- Funds misallocated away from infrastructure, education, health...
- Government repeatedly promises to cut subsidies, then backs down
Composition of exports has altered dramatically and unexpectedly over the last two decades

- Earlier high hopes for labour-intensive exports (especially textiles, clothing and footwear) have not come to fruition
- Instead, the big growth has been in coal and palm oil
- Country shares of exports have been changing significantly
  - Traditional export markets becoming less important
  - Rapid expansion into ‘new’ Asian markets
Guarding against collapse of financial sector

- Banking sector collapsed in AFC at huge cost to government (perhaps $50 billion)
- By contrast, GFC had little impact:
  - Only 1 (small) bank failed (Bank Century)
  - Cost to government ‘only’ about $700 million
  - But was used as a political lever to get rid of the reformist finance minister
- Reminded policymakers of earlier decision to unify financial institution supervision in single body (FSA)
- New law drafted and discussed, but not yet enacted
- Draft is poor: would lead to wasteful/confusing duplication of supervision in BI and new FSA
- Unclear why it should be expected to achieve anything
Economic dynamism comes mainly from the private sector rather than the public sector

• Government fails to create sufficient public infrastructure
• Less noticed: it fails to manage such infrastructure well
• Both problems clearly evident in dysfunctional large cities
  – Traffic congestion
  – Frequent flooding
  – Inadequate, poor quality water supply
  – Depletion of aquifers and consequent land subsidence
  – Absence of sewerage
  – Poor environmental quality
• Key to improvement is a shift from government financial support to charging costs to users
Corruption remains a major concern

• Plenty of evidence that the anti-corruption campaign is making little headway
• Gayus Tambunan case highlighted high level corruption in
  – Tax office
  – Police
  – Judiciary
  – Prisons
  – Immigration office...
• SBY’s popularity remains high, but his approval rating has fallen a great deal
Indonesia and Australia

• Not major trading partners
  – Australia not a large market for Indonesian exports
  – Australia supplies less than 5% of Indonesian imports
• Competing exporters of coal, natural gas, and certain minerals
• Not much Indonesian investment in Australia
• Australia invests in mining industry and in certain services
• Indonesian legislation has not created an environment that is truly welcoming to foreign investment
• Significant trend to protectionism in relation to foreign investment likely to constrain Australia’s role
GDP Growth (Demand side)
(% p.a.)
Composite Stock Price Index (CSPI) and Exchange Rate

- **CSPI**: Composite Stock Price Index
- **Exchange rate**: The exchange rate

The chart shows the trend of CSPI and exchange rate from 9-Apr-10 to 9-Apr-11.
Trends in Key Manufactured Exports (% of total exports)

- Wood Manufactures
- Paper & Cardboard
- Footwear
- Electrical & telecomm's
- Textiles & clothing
Trends in Energy Exports
(% of total exports)

- Oil
- Gas
- Coal
Trends in Other Natural Resource Exports
(% of total exports)

- Vegetable Oil & Fats
- Crude Rubber
- Metalliferous Ores & Metal Scrap
- Seafood
- Coffee, Tea, Cocoa & Spices