THE INDONESIAN ECONOMY DURING THE SOEHARTO ERA: A REVIEW

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ABSTRACT

At the beginning of the 1970s it was easy to believe that the road ahead for Indonesia was difficult. But as the decade unfolded, the changes across the Indonesian economy, and the sustained growth, surpassed all expectations. Numerous dramatic events seized Indonesian and international attention during the 1970s including corruption issues, the 1972 rice crisis, the *Malari* riots of early 1974, and the impact of the first oil boom including the Pertamina crisis. Anne Booth and I reviewed these developments in our edited collection of articles on *The Indonesian economy during the Soeharto era*. Looking back, our edited volume captured the excitement of the 1970s and, perhaps, was rather too cautious in looking towards the further gains that changes in the next few decades would bring to Indonesia**.**

Keywords: Indonesian economy, Soeharto era, Crisis

INTRODUCTION

Over three decades ago Anne Booth and I cooperated to edit *The Indonesian Economy during the Soeharto Era*. The collection (Booth and McCawley 1981) was one of the first major surveys of economic developments in Indonesia during the early part of the *Orde Baru* period. We prepared our edited collection at the end of the 1970s, a decade during which Indonesia experienced both turbulent economic times and much economic progress. As a contribution to recognizing the remarkable contribution that colleague Anne Booth has made towards the study of both the Indonesian economy and global development issues, it seems appropriate to revisit the view of the Indonesian economy that we presented together at the end of president Soeharto's first decade in office. Looking back, our edited volume captured the excitement of the 1970s and, perhaps, was rather too cautious in looking towards the further gains that changes in the next few decades would bring to Indonesia.

THE 1970S IN INDONESIA

At the beginning of the 1970s it was easy to believe that the road ahead for Indonesia was difficult. There had been a recovery of sorts in the late 1960s, and in 1969 a new five-year plan, *Repelita I* (*Rencana Pembangunan Lima Tahun I)* had been launched. Nevertheless the challenges ahead looked very daunting, partly because the resources available to support any sustained development program seemed so meagre. But as the 1970s unfolded the changes across the Indonesian economy, and the sustained growth, surpassed all expectations. To be sure, there were many difficulties, and there were some bad policy mistakes. Yet throughout the decade, the Indonesian economy steadily grew in strength.

The Commission of Four. Looking back over the 1970s, the contrasts between the progress and the problems in Indonesia is striking. One of the first surprising events of the decade related to an issue which had plagued Indonesia for many years and which has continued to be a headline issue ever since – corruption. In January 1970, in response to student protests and press criticism, president Soeharto announced that a 'Commission of Four' would be appointed to report on corruption within the Indonesian civil service. Jamie Mackie summarized the mood of the day as follows:

> Corruption is not a new phenomenon in Indonesia. It was becoming almost endemic under the Sukarno regime … where financial accountability virtually collapsed because of administrative deterioration. … The change in the political temper of the country between 1965 and 1970 is also relevant. Corruption was a source of frequent complaints in the Sukarno era, but it was a relatively minor political issue since so many more contentious conflicts loomed much larger … Today, there are few other burning issues of comparable horse-power for opponents or critics of the regime. (Mackie 1970: 87-88)

The full contents of the report became available, perhaps in an unintended way, when the well-known Jakarta daily *Sinar Harapan* obtained a copy of the document and proceeded to publish it in full in July 1970. The following month president Soeharto, in his Independence Day speech to parliament, spoke of his determination to lead the fight against corruption personally. In retrospect, it can be seen that president Soeharto was doing what every president of Indonesia (and dozens, probably thousands of other political figures in Indonesia) has done since – boldly announce measures to investigate and curb corruption but, in the end, leave the nation deeply disappointed with the results.

1972 rice crisis. Another major problem arose for Indonesian economy policy-makers in 1972 when a serious drought occurred across Southeast Asia leading to low rice production in the region and pressure on rice prices. The dry season in 1972 was especially dry. However effective crop monitoring procedures did not exist so neither officials in the field nor policy-makers in Jakarta realized that there was a problem until prices started rising. By August and September it had become obvious that a shortfall in production was looming. To make matters worse, world rice stocks were at a very low level, world rice prices were rising quickly, and emergency imports of rice were hard to obtain. Within several months, market prices of rice doubled in some parts of Indonesia putting upward pressure on other prices as well and causing widespread hardship amongst poorer sections of the population.

The rice crisis of late 1972, and the sudden end to economic stability sent shock waves through senior echelons of the Indonesian government. The events of late 1972 underlined the fact that economic stability in Indonesia (and perhaps political stability as well) was still very fragile. The repercussions of the crisis had a number of implications for policy-making over the following few years.

For one thing, the Indonesian government increased the focus on the issue of food security (especially rice security). President Soeharto showed every sign of being aware of the maxim that ‘an army marches on its stomach’ (although, in this case, it was the nation). During October and November in

1973 president Soeharto regularly met with officials from the national rice agency BULOG (*Badan Urusan Logistik*, or the Logistics Board) and held sessions with the Economic Stabilisation subcommittee of cabinet to discuss the rice situation (Dwipayana & Sjamsuddin 1991: 490).

For another thing, new programs to strengthen food security were implemented which influenced the approach to rice policy in Indonesia for the rest of the decade and into the 1980s. For example, the nation-wide rice marketing and procurement systems were strengthened working through rural semi-cooperatives, BUUDs (*Badan Usaha Unit Desa*) and full cooperatives, KUDs (*Koperasi Unit Desa*). In addition, ambitious plans were announced to strengthen BULOG, including the goal of establishing a national buffer stock of one million tons of rice. And, indeed, considerable progress was made throughout the decade. Although the operations of BULOG were often the subject of much comment, including many suggestions of mismanagement and personal aggrandisement on the part of BULOG officials, by the end of the 1970s many of the goals had been substantially achieved. By 1979, an impressive network of modern warehouses with a total capacity of one million tons had been built across Indonesia.

Malari. The 1972-73 rice crisis also contributed to the rising tide of discontent across Indonesia in 1973 which erupted in the dramatic *Malari* (*Malapetaka Lima belas Januari*, or '15th of January disaster') riots in Jakarta and other major Indonesian cities in January 1974. During the several days of sustained rioting, thousands of students took to the streets in anti-government demonstrations, much damage was done, including looting of shops and burning of cars in large cities, and the armed forces along with tanks were mobilised to restore order. The nominal trigger for the riots was a visit by Japanese Prime Minister Tanaka to Jakarta in mid-January. However other causes included resentment over various aspects of economic policy, especially rising prices and resentment at Japanese commercial influence in Indonesia, and divisions within the Indonesian military (Wanandi 2012: 112).

The *Malari* episode quickly led to a change of mood in Indonesia, not least within the upper echelons of government. President Soeharto moved decisively to bolster his power. Key military personnel were reassigned and a number of daily newspapers and weekly magazines were banned. In discussing the implications of the *Malari* riots, Wanandi (2012: 119) notes that 'Never again did Soeharto allow his ministers, generals and advisors as much leeway.' There were swift adjustments in economic policy as well. There was a tightening of the rules on foreign investment to close down some sectors to foreign investment and a closer examination of the role of Japanese investment in Indonesia. These moves were intended to demonstrate that policies during the earlier part of the *Orde Baru* in the direction of liberalization of foreign investment policies had been sharply revised.

The first oil boom. But at the same time that the *Malari* riots were taking place a tectonic change in global economic conditions was occurring: the first great oil boom of the 1970s was underway. This change would transform the environment for growth and development in Indonesia for the rest of the decade. The price of oil had started climbing almost two years earlier. However the price of other commodities was rising as well and so for a time policy-makers both in Indonesia and around the world did not realise what was happening. In April 1972 the oil price received by Indonesia was around

$2.90 per barrel. One year later it was $3.70. By November 1973 it had risen to $6.00. And then it rose again, climbing to over $10.00 in January 1974. By mid- 1974 it was clear that the international economic environment was changing in a dramatic way. Writing in the *Bulletin of Indonesian Economic Studies* in July 1974, Heinz Arndt observed that

> The increase in the price of Indonesian crude oil … has transformed the country's economic prospects … It has added to the external resources for development on a scale undreamed of a year ago, resources which can and should be used over the next few years to promote the social objectives of *Repelita II.* (Arndt 1974: 1)

And to add to the amazing windfall, the pro-foreign investment policies introduced in the late 1960s had encouraged new investment in the oil sector in Indonesia, so the output of oil in Indonesia was rising rapidly as well. In

1966, oil production in Indonesia had been running at the modest level of around 470,000 bpd (barrels per day). By early 1974 production had expanded to nearly 1.4 million bpd. Thus in less than a decade, the price of oil had risen fourfold and production had risen threefold.

The impact of influx of 'petro-dollars' on this Indonesian economy during this period was dramatic. Oil revenues recorded in the budget rose more than tenfold between 1970 and 1977, from around Rp 100 billion (around $

260 million) in the 1970/71 budget to nearly Rp 1,700 billion (over $ 4,000 million) in 1976/77. Many of the students who were demonstrating against foreign investment in the *Malari* riots would, during the next few years,

soon themselves begin to benefit substantially from the boost to Indonesia's development prospects that the oil boom would bring.

But the receipts from the boom needed to be used well. And, broadly speaking, for much of the rest of the decade the oil revenues in Indonesia were indeed used relatively effectively. A number of other oil-exporting developing countries which benefitted from the oil boom did not spend the windfall of oil revenues so efficiently. However, in Indonesia much of the new revenue was used for development purposes in infrastructure and in rural development programs. These expenditures supported economic growth during subsequent decades.

The Pertamina crisis. The most dramatic exception to good public sector management during this period was the Pertamina crisis. The state-owned oil company Pertamina had been founded in 1968 from the merger of Pertamina and Pertamin, two state-owned enterprises which had carried on operations in the oil sector during the Sukarno era. By 1974 Pertamina had become perhaps the most well-known state-owned enterprise in Indonesia. Pertamina was led by a dynamic president director, Dr Ibnu Sutowo, who was known for his 'can-do' philosophy and record of delivering the goods. It was often said in Indonesia at the time that Pertamina was a 'state within a state' with a large budget that lacked transparency and which was often used for transactions outside of the national budget that president Soeharto saw as important.

It seems that the windfall of petrodollars during 1973 and 1974 tempted Ibnu Sutowo into high risk financial dealings (McCawley 1978). Programs were announced to expand Pertamina's activities into new and diverse activities such as programs with the state-owned steel firm P.T. Krakatau and rice estates in South Sumatra. And, of much higher risk again, Pertamina took on short-term borrowings in international credit markets, apparently judging that the loans could be easily refinanced whenever they fell due. It seems that these financing arrangements worked well during 1973 and 1974 until international capital markets began to tighten with the onset of a recession of a major recession in rich nations in late 1974. Ironically, a major factor contributing to the recession in rich nations was the very increase in oil prices that had benefited Pertamina so handsomely in the preceding months. Pertamina was able to manage the cash-flow problems for some time, including by drawing on government financing. However in March 1975 the company found itself unable to meet its financial obligations and the Indonesian government was called on to step in.

In the next few months it became clear that the debts that Pertamina had entered into were much larger than had first been realized. Early reports suggested that Pertamina's short-term debts were not less than $1.5 billion. Later in the year, *Bappenas* (National Planning Board) Minister Professor Widjojo Nitisastro made a comprehensive statement to parliament in which he reported that Pertamina's total debts appeared to exceed $2.3 billion (Widjojo 2010: 301). But towards the end of 1975 rumours began circulating in Jakarta that the true debts were much higher, and perhaps as high as $6 billion or more. In early March 1976 Ibnu Sutowo was removed from his post as president director of Pertamina. These developments attracted much attention in the international press and did much damage to Indonesia's economic and financial reputation during this period.

The speculation was finally ended in May 1976 when the Minister for Mining, Professor Mohamad Sadli, provided a frank and detailed statement to parliament. Professor Sadli reported that Pertamina had run up debts of over $10 billion and that the debts were in the process of being pruned. Professor Sadli discussed how the situation had got out of hand in the following terms. He said:

> It is true that the Government knew of, and moreover agreed to, various non- oil ventures being carried on by Pertamina … However, without the knowledge or agreement of the Government, Pertamina took on large and heavy financial commitments to finance business ventures … the majority of which were not economically justifiable nor directly connected with Pertamina's main activities; examples of these ventures include the hire-purchase of ocean tankers and other development projects which gave rise to large debts … (McCawley 1978: 12)

Professor Sadli went on to provide extensive details, and to outline measures that the government would take to overcome the problems. He later described the Pertamina problems as 'the greatest crisis I faced as Minister of Mining' (Sadli 2003: 134).

At the time, the Pertamina crisis was widely regarded as delivering a serious blow to the Indonesian economy. And, of course, the crisis reflected very serious errors of judgement and internal accountability within the Indonesian government. But seen within a longer-term context, the Pertamina crisis was a passing problem. In important ways, the Indonesian economy and Indonesian governance systems are surprisingly resilient. Within a few years the main damage caused by the Pertamina crisis had been largely overcome. And many institutions are resilient. During the next few decades, Pertamina re-established itself as one of the leading corporate firms within Indonesia.

These events, then, were some of the main developments in the Indonesian economy in the period up to 1978 discussed in *The Indonesian Economy during the Soeharto Era.* During the next few years, into the early 1980s, the Indonesian economy grew strongly at rates of around 6-7 per cent per annum in real terms (Hill 1994). In taking stock of developments in the Indonesian economy during the Soeharto era to that stage, Anne Booth and I found it helpful to consider both the changes and continuities that seemed evident. And since these changes and continuities (we singled out five of each for discussion) are perhaps as marked today as they were three decades ago, it is useful to revisit the issues and to consider what might be said about them.

CHANGES

New technologies. In our edited collection Anne and I observed that

> … one of the most important changes in Indonesia in the last decade has been the rapid introduction and adoption of new technologies in a broad range of economic activities and the impact they have had, particularly in rural areas... Intrusions of modern technology have also occurred in less expected areas. (Booth & McCawley 1981: 7)

The same comment about the importance of new technologies could surely be said today although, during the last decade or so, the impact of new technologies has been more pronounced in the services sector than in agriculture.

It is something of a paradox that although economic nationalists in Indonesia often emphasize the need as much economic self-reliance as possible, Indonesia has benefitted enormously from the influx of global technology in key areas. Two of the most striking areas where this is evident are in the electronic and telecommunications sector, and in the domestic air travel industry. In the electronic and telecommunications sector Indonesians across the nation have eagerly adopted all of the wonders of modern technology – computers, hundreds (probably thousands) of internationally-designed software programs, modern visual (TV) and sound systems, and especially mobile telephones. The adoption and widespread of mobile telephones, especially, has been quite remarkable. Even in far-flung parts of the archipelago, away from the towns and out in rural areas, local people use mobile phones for social and business purposes. Traders in rural markets use mobile telephones numerous times each day to check on commercial transactions -- and even travellers far out in the middle of the Java sea will use mobile phones to maintain contact with their families.

The transformation in the airlines sector, especially on domestic routes, has been just as astonishing. Indonesians are now on the move across Indonesia as never before. Between 2002 and 2012, domestic passenger movements carried by LCC (low-cost carrier) airlines in Indonesia increased at the extraordinary rate of 20 per cent per year. Airline terminals are bursting at the seams at major airports. The largest terminal in the country – the Soekarno-Hatta airport which serves Jakarta – was estimated to be operating at over 200 per cent of capacity in 2012. But somehow, most of the time, the systems continue to work. Flights are often delayed. Maintenance and standards are believed to often be below acceptable standards. But such is the priority that middle-class Indonesians now give to mobility that most travellers grumble a bit when things go wrong but, generally, put up with the inconvenience and risks and line up for flights anyway.

The rapid adoption of new technologies shows up in the national income figures. The share of the services sector – particularly the telecommunications and airline transport sectors – has grown rapidly during the past decade. The services sector, overall, now makes up over 50 per cent of GDP. This is a far cry from the situation in Indonesia in 1965 when output from agriculture contributed over 50 per cent of national income.

Institutional changes. Current development thinking places much emphasis on the importance of institutional change during the development process. In *The Indonesian Economy during the Soeharto Era,* Anne and I noted important institutional changes that had occurred during the 1970s. We pointed to the *Bimas* rice intensification program, other changes in the agricultural sector, and the changes in the political and governance systems during the Soeharto era. Commenting on changes in national management, we observed that

> …the political atmosphere of the day has affected the conduct of economic policies: trade union and labour activities have been suppressed; political activities have generally been closely controlled and the government-sponsored political organisation *Golkar* has been the dominant political party; and conditions for government bureaucrats have been substantially improved. … But the cost has been that healthy discussion of development strategies has been greatly limited, and social groups who feel aggrieved have found it more difficult than even to make their voices heard in policy-making circles.
>
> (Booth & McCawley 1981: 10)

Institutional arrangements in such things as the political atmosphere of the day and many of the procedures for the management of government have, today, been transformed since Anne Booth and I set down this description of the situation during the *Orde Baru*.

Two of the most sweeping changes during the Era Reformasi since 1998 have been widely commented on – these are the dramatic liberalization of the political system during the Era Reformasi and the 'big bang' decentralization of processes of government in Indonesia. There have been many other institutional changes as well in recent years at both the macro (nation-wide) level and at the micro level of individual institutions. But the two changes of a dramatic expansion of the democratic space combined with remarkable decentralization have done much to transform the entire process of governance of the nation during the past decade.

Attitudes towards development priorities. National attitudes towards development priorities changed sharply in the late 1960s between the Sukarno and Soeharto eras. During the Sukarno era there was much emphasis on the need to combat colonialist influences in Indonesia and to curb the negative influences of foreign capitalism. During the first decade of the Soeharto era priorities altered dramatically. Much more emphasis was given to economic goals of stability and growth and almost all of the talk of opposing neo-colonialism disappeared from the national dialogue.

Perhaps the distinguishing characteristic of *Era Reformasi* in attitudes towards development is that there has been a search for a middle ground between the priorities that the first two presidents of Indonesia set out for the nation. On the one hand, the need for sustained growth and for effective economic management is now widely accepted in Indonesia. On the other hand, the traditional nationalist concerns about the need to build up the strength of the domestic economy and the allegedly excessive influence of foreign investors in Indonesia are still evident. In recent years, senior ministers in Indonesia have tried to balance these concerns. A realistic evaluation of the alternative approaches would seem to be that both strands of thinking – a cautious and conservative approach toward economic management, and a radical view looking towards anti-capitalist reform – continue to vie for support within the senior echelons of government institutions in Indonesia today.

External economic constraints. Throughout the first two decades of the Indonesia's existence as a new nation there were recurrent balance of payments problems. But in the first decade of the Soeharto *Orde Baru* government the situation changed dramatically. First, the inflows of foreign aid and investment in the early period of new regime strengthened the capital account and permitted increased levels of much-needed imports. And then the inflows of petro-dollars from the first oil boom transformed the balance of payments. In the late 1970s, Anne Booth and I took the view that

> … it seems likely that the present reasonably healthy reserve situation will continue into the future – certainly balance of payments problems are unlikely to impose the same kind of restraint on policy-making as was the case in the fifties.
>
> (Booth & McCawley 1981: 12)

For a time after the mid 1970s – indeed for the next two decades – it seemed that the balance of payments was no longer a constraint on development programs in Indonesia. Because of the surplus on the capital account during this period, Indonesia was able to maintain a high level of imports to support development and to sustain a deficit on the current account.

A sea-change occurred when the Asian financial crisis hit in 1997-98. Suddenly, volatility in capital flows crippled the external account forcing a sharp devaluation of the rupiah and a sharp recession. The contraction in output in Indonesia 1998 was over 10 per cent of GDP.

For most of the period since the Asian financial crisis – in marked contrast to the two decades before the crisis – Indonesia has moved into surplus on the current account. Indeed, during the past decade it has become the accepted conventional wisdom amongst many policy-makers in Jakarta that a surplus on the current account is desirable and, amongst other things, reflects the strength of the Indonesian economy.

In fact it seems that there is little correlation -- either in Indonesia or in many other developing countries – between the surplus on the current account of the balance of payments and the overall growth rate. Some developing countries (such as China) grow rapidly while maintaining a surplus on the current account while others (such as India and Papua New Guinea) grow rapidly while maintaining a deficit. What is worrying, however, is that just in the last year or so – during 2012 and 2013 – some policy-makers in Jakarta appear to have become over-confident and have begun to take the view that Indonesia's external balance is so sound that the strength on the external account can be taken for granted. However this approach carries substantial risks. The risks became evident during the first half of 2013 when unexpected strains on the balance of payments led to a fall in foreign exchange reserves and a marked depreciation of the rupiah.

Perhaps the main lesson from Indonesia's experience with fluctuations in both the current account and the capital account since independence is that the Indonesian economy is vulnerable to external shocks. It would seem wise for policy-makers to aim to maintain foreign exchange reserves at comfortable levels and, in addition, to allow the foreign exchange rate to fluctuate reasonably freely when appropriate to help maintain equilibrium in the foreign current market. The alternative approach of trying to intervene heavily in the foreign exchange market when strains appear – which has been tried by authorities in Indonesia at various times – tends to fail. When Indonesian officials try to fight international markets, then international markets tend to win.

Internal economic management. The early and mid-1970s saw striking improvements in internal economic management. For one thing, the five-year planning process was strengthened with the preparation of *Repelita* I (*Rencana Pembangunan Lima Tahun* II, or the First Five Year Development Plan) covering the period 1969-1974. Perhaps more important from the point of view of regular economic management, the national budgeting process was significantly strengthened. National budgets became increasingly credible documents and the flow of economic statistics released by both the Ministry of Finance and the central bank, Bank Indonesia, became more reliable. And perhaps most important of all, president Soeharto appointed a team of respected 'economic technocrats' to the top economic positions within government.

This broad approach to economic management in Indonesia – of working to strengthen the bureaucratic processes, and of appointing policy-makers with strong economic skills – has endured since the late 1960s. It is true that there have been exceptions to the practice of appointing strong economists to the top ministerial positions. Nevertheless, the exceptions have been unusual. As a general rule the top team of economic ministers and advisers in Indonesia has, since the late 1960s, been consistently strong. Similarly, the quality of documentation about economic issues, including national budget transparency, has consistently improved. In this area of public governance, the reforms introduced during the early years of the *Orde Baru* administration have endured, and have strengthened over time.

CONTINUITIES

The edited collection which Anne Booth and I prepared identified five continuities in development policy in Indonesia. Looking back over these issues thirty years later, what is striking is how these subjects continue to resonate in public policy today. *Plus ca change, plus c'est la meme chose.*

Dualism. The phenomenon of dualism – that is, various types of divisions which mark sharp divisions across society – has long been a topic of discussion in the economic analysis of the Indonesian economy. In *The Indonesian Economy during the Soeharto Era,* Anne Booth and I suggested that

> … few contemporary observers would deny that the dualistic features of the Indonesian economy … are still obvious today, and have in many ways been aggravated by … technological change … The large inflow of capital since 1968 has served to accentuate the differences between the modern and traditional sector of the urban economy, while the increased use of new technologies in rural areas has probably increased the dualistic nature of the indigenous rural economy …

In recent years, if anything these divisions have become more marked. Today, it is appropriate to talk not so much of *dualism*, but rather *multiple* levels of economic, social and technical strata in Indonesia. These things are difficult to define and measure precisely but there are, perhaps, at least four distinct levels of economic society in Indonesia. These four levels are the following:

- The *EE sector.* The 'Elite and Expatriate' sector which can be seen in the malls, the expensive cars, and the gated accommodation that this sector lives in.
- The *upper middle class sector.* Citizens in this group live in comfortable and relatively safe accommodation in urban areas, often with air-conditioning, and usually own cars (often with drivers) and have regular staff to help maintain the household.
- The *urban rakyat*. This group includes the vast majority of *rakyat* (ordinary people) who live in the main urban areas of Indonesia. Standards of living across this group vary widely from families who are managing quite well to lower-income groups who live a precarious existence.
- The *rakyat*. Around 50 per cent of Indonesians live below the World-Bank nominated figure of $2.00 per day. The main part of the *rakyat* who fall into this group live outside of the largest urban areas and earn incomes wherever they can on a daily basis. Nearly all of the people in this group live and work in the 'informal sector'.

The phenomenon of dualism, and indeed the emergence of further structures within dualism, is perhaps even more evident today than was the case during the 1970s in Indonesia.

Indigenous entrepreneurship. The issue of *pribumi* entrepreneurs relates to the question of who owns and controls the Indonesian economy. There is a widespread feeling in Indonesia that although political independence from foreign domination was achieved in 1945, there is still too much foreign control over the Indonesian economy. On one hand, it is easy to sympathize with the idea that Indonesian entrepreneurs rather than foreign companies should be dominant in Indonesia. On the other hand, it is puzzling that so few large private firms controlled by Indonesian managers and owners have emerged and flourished since independence was achieved 1945.

In commenting on this issue Anne and I noted that one of the structural characteristics of the Indonesian economy was that it was dominated by thousands of 'micro-enterprises'. In the decades since then, some *pribumi* entrepreneurs have managed to establish expanding corporate firms, but the number of well-known successful *pribumi* entrepreneurs is not large (Booth 1998: 320). Further, it is widely-believed that many of them have done well through their links with government and political parties rather than through their commercial success in genuinely competitive market-oriented ventures.

This apparent shortage of large, successful *pribumi* entrepreneurs, therefore, gives rise to a policy dilemma – what should government do to foster the growth of an Indonesian business class? There does not seem to be any easy answer to this question. It is hard to imagine how a pro-*pribumi* policy along the lines of that adopted in Malaysia could work successfully in Indonesia because economic and social conditions in Indonesia are so different. Yet other, less ambitious approaches designed to assist small-scale entrepreneurs in Indonesia have seldom been particularly successful. In the meantime, virtually every political leader in Indonesia continues to pay lip service, as a routine matter, to the goal of promoting small-scale entrepreneurship across the nation.

Inward-looking and outward-looking attitudes. Ever since independence there has been tension within Indonesian economic policies between inward-looking protectionist attitudes and more outward-looking internationalized approaches. The pendulum swung markedly away from inward-looking approaches in the early years of the *Orde Baru* government, and then swung back again somewhat after the *Malari* riots. There was a movement back towards more liberalised policies, especially in the manufacturing sector, during the 1980s, and then a more inward-looking mood developed towards the end of the Soeharto period.

These tensions in economic policy have continued to the present day. Recently, during 2011 and 2012, several years of strong economic growth, there were signs of a drift towards more protectionist policies in several areas of economic policy. Interventionist measures were announced in the agricultural sector to assist domestic producers, and foreign companies operating in the resources sector were directed to increase the level of domestic processing of resources before export regardless of whether the value added to resource exports in this was profitable or not. But marked pressures emerged on the balance of payments in mid-2013 and there was a sudden market-determined depreciation of the rupiah. A policy package was announced in late August 2013 which emphasized the need for more internationally-competitive measures and which amounted to a move away from protectionist policies.

Fortunately, within limits, there are significant market-determined constraints in Indonesia which ensure that excessive levels of protection for tradable goods are difficult to maintain. The well-known quip that 'Indonesia was made for free trade' reflects the nature of Indonesia's geography where there are long borders open to neighbouring countries. In the past, when prices in regulated markets inside Indonesia have diverged too far from regional prices, smuggling of goods (in both directions, depending on the nature of the regulation in Indonesia) has ensured that Indonesian prices have not diverged too far from international prices.

However it is true that disagreements between inward-looking and outward-looking policy-makers occur in many countries. The tug of war between nationalist 'engineers' and internationally-minded 'technocrats' in Indonesia (as the groups are sometimes called) seems likely to be a feature of Indonesian policy-making for many years to come.

The economic role of government. Writing in our edited collection about patterns of government policy in Indonesia, Anne and I noted 'the absence of benign government intervention and the presence of malign intervention'. What we did not discuss in any detail are the practical restrictions imposed upon governments in Indonesia by the straitjacket of resource constraints that most branches of government must operate within.

A key problem that most parts of government in Indonesia must deal with is that their resources are very limited. At the national level, government spending in Indonesia in 2011 was less than $700 per capita. This compares with national expenditure in OECD countries such as the United States and Germany of around $20,000 per capita. Thus, for every $1.00 per person that the president of Indonesia can allocate to programs to support national priorities, the leaders of the United States and Germany can allocate around

$30. The shortage of resources is stark at the provincial level in Indonesia as well. In 2011 the average level of per capita expenditure by provincial governments in Java (excluding the special case of Jakarta) was a remarkably low level of $24 per capita. Similar levels of government in rich OECD countries (in provinces, or province-like jurisdictions) often maintain levels of annual spending around $6,000- 8,000 per capita or more.

These figures are very sobering and prompt the question of what should be the role of governments in Indonesia given that their resources are so limited? It would seem that in order for governments in Indonesia to become more effective, governments need to define (and limit) their roles far more carefully than is currently the case. In particular, in planning for service delivery, key decisions are needed about which services will be provided *directly* by the government itself, or *indirectly* through reliance on service providers. More broadly, the extreme resource constraint facing most government agencies in Indonesia suggests that, often, agencies should move towards an improved regulatory role and reduce attempts to deliver services themselves.

Unemployment and poverty. The final area of continuity relates to problems of unemployment, poverty, and insecurity. Anne and I noted that these issues were 'related through a chain of circular causation' and that 'it is … difficult to point to any sizeable government program that is likely to have an impact on these problems'.

It is true that in some directions, significant progress has been made in addressing these issues since the late 1970s. Levels of absolute poverty have dropped markedly in Indonesia, and most measures of human welfare point to notable progress. Further, in contrast to the situation in Indonesia in the 1970s, governments at all levels now recognize that poverty-reduction must be a focus of policy and encourage public discussion about appropriate measures. Yet mass poverty remains a very serious problem in Indonesia. World Bank estimates are that close to 50 per cent of Indonesians live on less than $2 per day. And perhaps the most important lesson of the Indonesian development experience since independence is that the single most effective measure that can be taken to alleviate mass poverty in Indonesia is to promote sustained economic growth.

CONCLUSION

Looking back at the overall view presented in the edited collection of articles in *The Indonesian Economy during the Soeharto Era,* it is hard to avoid the impression that our view of the prospects of the Indonesian economy was too cautious. We perhaps underestimated the resilience and flexibility both of the economy overall, and of the institutions of government in Indonesia. And we were, arguably, too concerned about possible storm clouds ahead. For example, we recorded scepticism about the potential growth rate for Indonesia when we noted that

> … the official growth target for *Repelita III* (1979-1984) is 6.5 per cent and some observers feel this may be difficult to achieve.
>
> (Booth & McCawley 1981: 20)

In fact, the average growth rate of the Indonesian economy for the period from 1980 until the onset of the 1997-98 financial crisis was only slightly below 6.5 per cent (Van der Eng 2010). And at the conclusion of our collection, in surveying some of the potential problems ahead, we glumly observed that

> … to the extent that the problems are avoided rather than faced up to, the prospects for stable development in Indonesia over the longer term seem bleak.

But as things have turned out, and despite the continuing existence of quite a few of the problems that we identified, Indonesia has continued to grow and to develop. One of Indonesia's most well-known economists, Professor Mohamad Sadli, used to remind his friends that Indonesian policy-makers often have the useful ability of being able to 'muddle through'. And indeed, Sadli was surely right (cited in Thee 2003). The myriad of actors involved in the Indonesian economy have indeed muddled through remarkably well since Anne Booth and I prepared *The Indonesian Economy during the Soeharto Era* at the end of the 1970s. With luck, this pragmatic approach to economic management will provide similar success for many decades to come.

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